WHO IS YOUR SPOUSE?
THE DEMISE OF DOMA AND ITS IMPACT ON ESTATE PLANNING IN TEXAS

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- Author/Speaker: *Warning! Your Annual Exclusion May Be an Illusion*, ACTEC 2013 Annual Meeting
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- Co-Author/Speaker: *Fixing Broken Trusts: How to Tell if Your Ox is in the Ditch, and How to Get it Out*, Texas Society of CPAs Advanced Estate Planning Conference, 2012
- Co-Author/Speaker: *Recent Developments and Predictions in Tax Law–Pending Legislation, Portability and Decanting*, South Texas College of Law Wills & Probate Institute, 2012
- Author/Speaker: *Tax, Procedural And Administration Rules: Contrasting Revocable Trusts with Estates*, 46th Annual Southern Federal Tax Institute, 2011
- Author/Speaker: *Update on Administering 2010 Estates–What Have We Learned So Far?*, State Bar of Texas 35th Annual Advanced Estate Planning and Probate Course, 2011; Houston Business and Estate Planning Council, 2011; Texas Society of CPAs Advanced Estate Planning Conference, 2010
- Panelist: *Keeping Your Plan from Getting Waylaid in Administration*, State Bar of Texas 17th Annual Advanced Estate Planning Strategies Course, 2011
- Author/Speaker: *Practical Issues and Esoterica of Form 1041 Preparation and Presentation*, 45th Annual Southern Federal Tax Institute, 2010
- Author/Panelist: *2010 and Beyond: Estate Planning and Administration Issues*, South Texas College of Law Wills & Probate Institute, 2010

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I. Introduction

On June 26, 2013, the United States Supreme Court ruled that Section 3 of the Defense of Marriage Act ("DOMA") is unconstitutional as a deprivation of the equal liberty of persons that is protected by the Fifth Amendment. *United States v. Windsor*, 570 U.S. 12, 133 S. Ct. 2675 (2013). As a result, it is now apparent that same-sex couples who reside in a state that recognizes same-sex marriage will be considered as married for federal tax purposes. But what of same-sex couples who lawfully marry in such a jurisdiction but reside in a state that does not recognize same-sex marriages? Under what circumstances and for what purposes will these individuals be treated as married? How, as estate planning professionals, should we treat Texas same-sex couples who have been lawfully married in a jurisdiction other than Texas? Although perhaps there are still more questions than answers in this area, this outline seeks to raise issues that estate planners should consider as a result of the sea-change brought about by the Court's decision in *Windsor*.

II. Marriage in Texas

Article I, Section 32 of the Texas Constitution provides:

> (a) Marriage in this state shall consist only of the union of one man and one woman.
>
> (b) This state or a political subdivision of this state may not create or recognize any legal status identical or similar to marriage.

These constitutional provisions, adopted by popular vote in 2005, are codified in the Texas Family Code. In particular, Sec. 6.204 of the Texas Family Code provides:

> 6.204. RECOGNITION OF SAME-SEX MARRIAGE OR CIVIL UNION.
>
> (a) In this section, "civil union" means any relationship status other than marriage that:
>
> (1) is intended as an alternative to marriage or applies primarily to cohabitating persons; and
>
> (2) grants to the parties of the relationship legal protections, benefits, or responsibilities granted to the spouses of a marriage.
>
> (b) A marriage between persons of the same sex or a civil union is contrary to the public policy of this state and is void in this state.
>
> (c) The state or an agency or political subdivision of the state may not give effect to a:
>
> (1) public act, record, or judicial proceeding that creates, recognizes, or validates a marriage between persons of the same sex or a civil union in this state or in any other jurisdiction; or
>
> (2) right or claim to any legal protection, benefit, or responsibility asserted as a result of a marriage between persons of the same sex or a civil union in this state or in any other jurisdiction.

But what about persons residing in Texas who have been lawfully married in another jurisdiction? (The Appendix lists U.S. jurisdictions that currently recognize same-sex marriage,

and their dates of application). As discussed in more detail below, Texas law applies to persons married elsewhere who are domiciled in this state. TEX. FAM. CODE §1.103. In most cases, courts apply a "place of celebration" rule to determine the validity of a marriage. *See* TEX. FAM. CODE §1.101. However, with respect to marriages determined to be "void" under Texas law, a "place of domicile" rule apparently prevails. Section 6.204(c) of the Texas Family Code thus generally precludes Texas courts from recognizing as married same-sex couples who are lawfully married in other jurisdictions.

Federal law currently reinforces this Texas policy. In particular, Section 2 of DOMA (which was not addressed by the Court in *Windsor*) provides:

> No State . . . shall be required to give effect to any public act, record, or judicial proceeding of any other State . . . respecting a relationship between persons of the same sex that is treated as a marriage under the laws of such other State . . . or a right or claim arising from such relationship.

Although Section 2 of DOMA seems to support Texas's ability to take a place-of-domicile versus a place-of-celebration approach to same-sex marriage, one must keep in mind Article IV Section 1 of the U.S. Constitution (the "Full Faith and Credit" clause). That section provides:

> Full faith and credit shall be given in each state to the public acts, records, and judicial proceedings of every other state.

The language of the Constitution seems to be absolute, but the U.S. Supreme Court has recognized a "public policy exception" to the Full Faith and Credit Clause. In 1939, the Court in *Pacific Employers Insurance v. Industrial Accident* wrote:

> [T]here are some limitations upon the extent to which a state may be required by the full faith and credit clause to enforce even the judgment of another state in contravention of its own statutes or policy. *See Wisconsin v. Pelican Insurance Co*., 127 U.S. 265; *Huntington v. Attrill*, 146 U.S. 657; *Finney v. Guy*, 189 U.S. 335; *see also Clarke v. Clarke*, 178 U.S. 186; *Olmsted v. Olmsted*, 216 U.S. 386; *Hood v. McGehee*, 237 U.S. 611; *cf. Gasquet v. Fenner*, 247 U.S. 16. And in the case of statutes...the full faith and credit clause does not require one state to substitute for its own statute, applicable to persons and events within it, the conflicting statute of another state, even though that statute is of controlling force in the courts of the state of its enactment with respect to the same persons and events.

306 U.S. 493, 502 (1939).

While the Supreme Court applies this public policy exception, it does so differently for state judgments as compared to state laws. In the 2003 case of *Franchise Tax Board v. Hyatt*, the Court reiterated that, "[o]ur precedent differentiates the credit owed to laws (legislative measures and common law) and to judgments." *Franchise Tax Board v. Hyatt*, 538 U.S. 488, 494 (2003), quoting *Baker v. General Motors*, 522 U.S. 222, 232 (1998). In summary, if the *legal pronouncements* of one state conflict with the public policy of another state, federal courts have been reluctant to force a state to enforce the pronouncements of another state in contravention of its own public policy. (Note that Section 6.204 of the Texas Family Code not only declares same-sex marriages to be void, but also declares them to be "contrary to the public policy of this state . . . ."). For out-of-state *judgments*, the Court has stated that there may be exceptions to enforcement and jurisdiction, but maintains that there is no "public policy" exception to the Full Faith and Credit Clause for judgments. *See Baker v. General Motors*, 522 U.S. 222 (1998).

III. Marriage Under Federal Law

Historically, the federal government has deferred to each state for purposes of defining marriage for that state. *See Williams v. North Carolina*, 317 U.S. 287, 298 (1942) ("Each state as a sovereign has a rightful and legitimate concern in the marital status of persons domiciled within its borders"). In the words of another case, "[T]he states, at the time of the adoption of the Constitution, possessed full power over the subject of marriage and divorce . . . [and] the Constitution delegated no authority to the Government of the United States on the subject of marriage and divorce." *Haddock v. Haddock*, 201 U.S. 562, 575 (1906); *see also In re Burrus*, 136 U.S. 586, 593-594 (1890) ("The whole subject of the domestic relations of husband and wife, parent and child, belongs to the laws of the States and not to the laws of the United States."). Against this backdrop, and prior to same-sex marriage being recognized as lawful in any state, Congress adopted DOMA.

For purposes of federal law, Section 3 of the Defense of Marriage Act ("DOMA") provides:

> In determining the meaning of any Act of Congress, or of any ruling, regulation, or interpretation of the various administrative bureaus and agencies of the United States, the word 'marriage' means only a legal union between one man and one woman as husband and wife, and the word 'spouse' refers only to a person of the opposite sex who is a husband or a wife.

1 USC § 7.

As noted above, however, on June 26, 2013, the United States Supreme Court ruled that Section 3 of DOMA is unconstitutional as a deprivation of the equal liberty of persons that is protected by the Fifth Amendment. *United States v. Windsor*, 570 U.S. 12, 133 S. Ct. 2675 (2013). *Windsor* was a tax case, and more specifically, an estate tax case. Briefly, Edith Windsor and Thea Spyer, a same-sex couple residing in New York, were lawfully married in Ontario, Canada in 2007. Ms. Spyer died in 2009, at a time when the State of New York did not permit same-sex marriages, but did recognize same-sex marriages performed elsewhere. Ms. Spyer left her entire estate to Ms. Windsor, who sought to claim the federal estate tax marital deduction for property passing to a surviving spouse pursuant to Code Section 2056. The IRS asserted that she was barred from doing so by Section 3 of DOMA. As a result, the IRS, finding that the unlimited marital deduction was not available to the estate of a deceased spouse in a same-sex marriage, denied Ms. Windsor's estate tax marital deduction and compelled her to pay $363,053 in estate taxes. Ms. Windsor paid the tax and sued for a refund, ultimately prevailing in the U.S. Supreme Court. As a result, it is now clear that same-sex couples who reside in a state that recognizes same-sex marriage will be considered as married for federal tax purposes.

IV. Implications of *Windsor* for Texans

What are the implications of *Windsor* for same-sex couples who lawfully marry in a jurisdiction that permits same-sex marriage, but who reside in a state that does not recognize same-sex marriage? The question must be addressed from both a federal and a state perspective.

A. Federal Law Issues

By declaring Section 3 of DOMA unconstitutional, the Court appears to have paved the way for applying state law rules for determination of the marital status of individuals when interpreting federal laws. Nevertheless, it remains to be seen whether these rules regarding marriage will be applied based upon the place that the marriage ceremony was celebrated, or based upon the place of the domicile of the parties.

1. Marriage for Federal Tax Purposes–Revenue Ruling 2013-17

Windsor makes clear that lawfully married same-sex couples who reside in a jurisdiction that recognizes such a marriage are to be considered married for federal tax purposes. On August 29, 2013 the IRS issued Revenue Ruling 2013-17 (IR 2013-72, Aug. 29, 2013), holding that all same-sex married couples will be treated as married for all federal tax purposes, including income, estate, gift, and generation-skipping transfer tax purposes, regardless of the state of the couple's residence. The Revenue Ruling expressly adopts a place-of-celebration rule for determining marital status, stating, "[I]ndividuals of the same sex will be considered to be lawfully married under the Code as long as they were married in a state whose laws authorize the marriage of two individuals of the same sex, even if they are domiciled in a state that does not recognize the validity of same-sex marriages." *See* Rev. Rul. 58-66, 1958-1 CB 60 (couple married under common law and filing income tax returns as married-filing-jointly will continue to be treated as married, even after moving to a jurisdiction that doesn't recognize common-law marriages). Revenue Ruling 2013-17 includes foreign jurisdictions in its use of the term "state," so out-of-country same-sex marriages will also be recognized. The Ruling also makes it clear that the term "spouse" as well as any gender-specific terms such as "husband" and "wife" include same-sex married persons. The Ruling provides that the term "marriage" does not include registered domestic partnerships, civil unions, or other similar formal relationships recognized under state law that are not denominated as a marriage under that state's law. The ruling applies prospectively from September 16, 2013, but affected taxpayers may also generally rely on the ruling for the purpose of filing original returns, amended returns, adjusted returns, or claims for credit or refund for any overpayment of tax resulting from these holdings, provided the applicable limitations period for filing such a claim under Section 6511 of the Code has not expired. This prospective application with a permissive look-back gives same-sex married persons the option to apply the ruling to prior years if it is to their advantage to do so.

2. Marriage under Other Federal Rules

Windsor has given rise to a number of other administrative announcements regarding same-sex marriages. For example:

- On August 2, 2013, Secretary of State John Kerry announced that the United States will immediately begin applying a place-of celebration rule for processing visa applications for same-sex couples, stating, "as long as a marriage has been performed in a jurisdiction that recognizes it so that it is legal, then that marriage is valid under U.S. immigration laws." Updated FAQs regarding same-sex marriage state that "the law of the place where the marriage was celebrated determines whether the marriage is legally valid for immigration purposes."
- Likewise, the Department of Defense has announced that it will follow a place-of-celebration rule. The announcement states that "[t]he Department will construe the words 'spouse' and 'marriage' to include same-sex spouses and marriages, and the Department will work to make the same benefits available to all military spouses, regardless of whether they are in same-sex or opposite-sex marriages. The Department will continue to recognize all marriages that are valid in the place of celebration."
- On August 9, 2013, Labor Secretary Tom Perez announced in an email to Department of Labor employees that the spousal leave provisions of the Family and Medical Leave Act will be interpreted to apply to same-sex married persons. The Wage and Hour Division of the DOL has updated its FMLA Fact Sheet (#28F) to provide that "[s]pouse means a husband or wife as defined or recognized under state law for purposes of marriage in the state *where the employee resides*, including 'common law' marriage and same-sex

marriage." At least for now, this announcement thus limits it application to a place-of-residence rule.

- The Social Security Administration recently issued a "Program Operations Manual System" update that appears to apply a place-of-residence standard. It provides that all claims filed on or after June 26, 2013 (the date of the *Windsor* decision), or that were pending final determination at the time of the decision, are now subject to so-called "*Windsor* instructions," which allow for payment of claims when the applicant (i) was married in a state that permits same-sex marriage, and (ii) is domiciled, at the time of application or while the claim is pending a final determination, in a state that recognizes same-sex marriage.

3. Estate Planning Implications of Being Married under Federal Law

For estate planners, there are a number of issues to consider for same-sex clients who are treated as married solely for purposes of federal law. These couples reside in a bifurcated world where their property rights are fixed by state law, but the implications of those state-law property rights when interpreting federal law might be quite different. It is well established that, when applying federal tax rules, the property rights of the parties are a matter of state law. For example, although federal law determines which of the decedent's property interests are subject to estate tax, state law determines the nature and extent of those interests. *Morgan v. Comm'r*, 309 U.S. 78, 80, 23 AFTR 1046 (1940). In a federal tax controversy, however, the IRS (or a federal court) is not bound by a state court determination of property interests where the United States was not a party to the proceeding. *Estate of Bosch*, 387 U.S. 456 (1967). In applying state law to the facts of a particular case, the Court in *Bosch* held that (i) when a state law property right has been decided by the highest court of the state, the decision should be followed and respected as the best authority for that state's law; but (ii) when a state law property right has not been decided by the highest court of the state, federal authorities "must apply what they find to be the state law after giving 'proper regard' to relevant rulings of other courts of the State." *Id.* at 465. *See also*, *Lake Shore National Bank v. Coyle*, 296 F.Supp. 412 (N.D. Ill. 1968).

In interpreting the federal law, its application to state property issues presents unique estate planning considerations. For example, consider:

a. Unlimited gift tax marital deduction

An outright transfer to a surviving spouse who is a United States citizen qualifies for the unlimited gift tax marital deduction, so long as the interest is not a life estate or other terminable interest. IRC § 2523. The availability of this deduction may be critical in a situation where one same-sex spouse has substantial assets, and wants to provide for his or her spouse by making significant lifetime transfers. Absent recognition of the marital status for federal gift tax purposes, those transfers would constitute taxable gifts to the extent that they exceed the gift tax annual exclusion, or are made to providers of educational or medical services. IRC § 2503.

b. Unlimited estate tax marital deduction

An outright testamentary transfer to a surviving spouse who is a United States citizen qualifies for the unlimited estate tax marital deduction, so long as the interest is not a life estate or other terminable interest. IRC § 2056. In addition, transfers to various forms of testamentary trusts are eligible for the deduction. Thus, for example, an interest passing to a trust for the benefit of the surviving spouse that provides the spouse with the exclusive right to all income for life, and grants to the spouse a general power of appointment over the trust property at death (a so-called "life estate-power of appointment" or "LEPA" trust) qualifies for the estate tax marital deduction. IRC §2056(b)(5). More commonly, a marital deduction is available for an interest passing to a

trust for the benefit of the surviving spouse that provides the spouse with the exclusive right to all income for life, and for which an election is made causing the property remaining in the trust to be taxed in the spouse's estate at the time of the spouse's later death (a so-called "qualified terminable interest property" or "QTIP" trust). IRC § 2056(b)(7).

c. Portability

The Tax Reform Act of 2010 added, and the American Tax Reform Act of 2012 made permanent, the notion of "portability" of a deceased spouse's unused exemption amount. In essence, portability provides that upon the death of one spouse, the surviving spouse may inherit any unused federal estate tax exemption of the deceased spouse. IRC § 2010(c)(2)(B). The unused exclusion amount is referred to in the statute as the "deceased spousal unused exclusion amount," otherwise known as the "DSUE amount." Once a spouse inherits the DSUE amount, the surviving spouse can use the DSUE amount either for gifts by the spouse or for estate tax purposes at the surviving spouse's subsequent death. An individual can only use the DSUE amount from his or her "last deceased spouse." IRC § 2010(c)(4)(B)(i). To understand how portability works, assume, for example, that X dies in 2013 with an estate of $3 million. He leaves $2 million to his surviving spouse Y, and the balance to his parents. As a result, his taxable estate is $1 million (his $3 estate, less the $2 million passing to his spouse). X's executor may elect to file an estate tax return using $1 million of X's $5.25 million estate tax exemption to shelter the gift to the parents, and "pass" the other $4.25 million of X's estate tax exemption to Y. Y would then have an estate and gift tax exemption of $9.5 million (Y's own $5.25 million exemption plus X's unused $4.25 million exemption).

d. Right to elect gift-splitting (Remember still no community property in Texas)

Until same-sex marriages are recognized in Texas, same-sex married couples will not generate any community property while residing here (although they may own community property arising while domiciled in a community property state such as California that does recognize same-sex marriage). Nevertheless, they will be eligible to elect to treat gifts made by one spouse as though they were made one-half by each spouse. IRC § 2513. This election would allow those gifts to utilize both spouses' annual exclusion, or for larger gifts, take advantage of both spouses' $5.25 million gift tax exemption.

e. Spousal Benefits under 401(k)s and Other ERISA Plans

Qualified plans must provide for the distribution of benefits in the form of annuities payable to the surviving spouse, either at retirement or when the employee dies prior to retirement, if there is not a valid participant election that incorporates spousal consent. IRC §§ 401(a)(11), 417. Therefore, a married retiree does not have the exclusive right to designate the beneficiaries of a retirement plan account governed by ERISA. The Retirement Equity Act of 1984 (REA) significantly affects benefit distributions under qualified and other employee benefit plans, particularly the requirements for providing qualified annuity benefits to the surviving spouse. Therefore, in planning for the treatment of potential plan distributions, consideration must be given to these requirements. In general, REA expanded the scope of the "Qualified Joint and Survivor Annuity" provisions and the preretirement survivor provisions as follows: (i) Surviving spouse annuity requirements are applicable to all qualified plans (with a limited exception for certain non-pension defined contribution plans), whether or not the plan has traditionally offered annuities. IRC § 401(a)(11)(B). (ii) Surviving spouse annuity requirements apply to the payment of benefits with respect to any participant who has vested accrued benefits under the plan. IRC § 401(a)(11)(A). (iii) A participant can elect out of the surviving spouse annuity coverage, but only with the written consent of the participant's spouse. Treas. Reg. § 1.401(a)-11(c)(1). In addition, the consent must be acknowledged before a plan representative or a notary public. IRC

§ 417(a)(2)(A)(iii). *See Cozen O'Connor, P.C. v. Tobits*, 2013 WL 3878688 (ED Penn., July 29, 2013) (slip opinion available at www.boomerisablog.com/files/2013/08/COZEN-OCONNOR-P-C-v-TOBITS-et-al.pdf) (Notwithstanding Pennsylvania's ban on recognition of valid Illinois same-sex marriage, "*Windsor* makes it clear that where a state has recognized a marriage as valid, the United States Constitution requires that the federal laws and regulations of this country acknowledge that marriage." As a result, a purported beneficiary change not signed by the participant's same-sex spouse held not valid under ERISA) (slip opinion p. 11-12).

f. Spousal Rollovers under IRAs/401(k)s

When a person passes away owning an interest in an IRA or 401(k) that passes to a surviving spouse, the surviving spouse may roll over the account to a spousal IRA. IRC § 402(c)(9); Treas. Reg. § 1.402(c)-2, A-12. The election to roll the account into a spousal IRA rollover may be made at any time after the participant's death. Treas. Reg. § 1.408-8, Q&A 5(a). Non-spousal beneficiaries may roll funds into an inherited IRA under current law, but must begin distributions from the inherited IRA beginning the year following the plan participant's death. IRC § 409(c)(11). In contrast, with a spousal IRA, the spouse may treat the account as his or her own IRA, and may defer distributions until his or her required beginning date. IRC § 409(c)(9). Note that a spousal rollover can be a two-edged sword. If the surviving spouse is younger than age 59½, distributions made to the surviving spouse from the IRA prior to attaining age 59½ would be subject to the ten percent penalty for early withdrawals. For inherited retirement assets, if the surviving spouse may need access to the funds prior to attaining age 59½, a better strategy would be to leave those assets in the deceased spouse's IRA or in the qualified plan with the deceased spouse's employer, so that no ten percent penalty would apply to any distributions. After the surviving spouse attains the age of 59½, the remaining balance of the retirement funds could be rolled over to an IRA without subjecting future distributions to the ten percent penalty.

g. Deduction for/Taxability of Alimony Paid to Former Spouse

Payments to a former spouse which are characterized as alimony are deductible to the ex-spouse who is making the payment. IRC § 215. Likewise, amounts received as alimony are taxable as income to the ex-spouse receiving the alimony. IRC § 71. Of course, the issue of alimony brings up a host of other issues regarding the ability of same-sex married couples to obtain a divorce. It is unclear whether Texas courts have jurisdiction to grant a divorce to same-sex married couples. At least one trial court has granted such a divorce, despite the filing of a post-judgment motion to intervene by the Texas Attorney General, who alleged that the trial court had no jurisdiction to grant a divorce to a same-sex couple married in Massachusetts but residing in Texas. The Texas Court of Appeals ruled that the State lacked standing to appeal the judgment, but the Texas Supreme Court has agreed to hear the petition for review. *See State v. Naylor*, 330 S.W.3d 434 (Tex. App. –Austin, pet. granted). Most states with little or no residency requirements for marriage do have such requirements for divorce. For example, California requires that at least one of the spouses be a resident of California for at least six months prior to filing a petition for dissolution. Cal. Fam. Code § 2320(a). Minnesota requires one spouse to have resided in, served in the armed forces in, or been a domiciliary of the state for 180 days prior to filing for divorce. Minn. Stat. § 518.07. Delaware generally requires that one spouse/partner be a resident of the state for at least six months prior to petitioning for dissolution of a marriage or civil union. Del. Code Ann. Tit. 13, § 1504. However, the Delaware Family Court may dissolve a marriage or civil union entered into in Delaware if both partners live in a state where the courts will not dissolve their marriage or civil union. Del. Code Ann. tit. 13, § 216. Similarly, effective August 16, 2013, non-resident spouses may obtain a divorce in the Canadian province where their marriage was performed if a) the spouses have lived separate and apart for at least one year, b) neither spouse resides in Canada when applying for divorce, and c)

both spouses reside, and have resided for at least one year immediately preceding the application, in a state that will not grant them a divorce because that state does not recognize their marriage. Civil Marriage Act, SC 2005, ch 33, § 7 (Canada). *See* NCLR, Divorce for Same-Sex Couples Who Live in Non-Recognition States: A Guide For Attorneys. (www.nclrights.org/site/DocServer/Divorce_in_DOMA_states_Attorney_Guide.pdf?docID=9761).

h. Other Unexpected Tax Issues for Spouses

A number of other issues may arise by virtue of a person being treated as one's spouse. It is not uncommon for one partner in a same-sex relationship to name his or her partner as the trustee of a trust. But remember, if the *spouse* of a grantor is the *trustee* of a trust, the powers of the trustee are attributed to the grantor. IRC § 672(e). This rule may cause a trust that was formerly taxed as a simple or complex trust to now be treated as a grantor trust for federal income tax purposes. For purposes of the generation-skipping transfer ("GST") tax, transfers made to an unrelated individual who is more than 37½ years younger than the transferor are treated as generation-skipping transfers. IRC § 2651(d). If, however, the transferee is the lawful spouse of the transferor, the persons are treated as being in the same generation for purposes of the GST tax. IRC § 2651(c). The generational assignment of any transferee who is a descendant of the spouse's grandparents is similarly realigned. IRC § 2651(b)(2). Another common planning technique for same-sex couples is for one partner to make gifts as part of a split-interest transfer or of an interest in an entity, such as a limited partnership or limited liability company. Certain planning with split interest trusts or entities with multiple classes of ownership can achieve valuation discounts if the transferee is not a member of the transferor's family. Those discounts are largely ignored under Chapter 14 of the Code, however, if the transfer is to a family member, including a spouse. *See* IRC § 2701(e)(2)(A).

4. Planning Implications for Same-Sex Spouses

A number of estate planning issues arise because of the foregoing issues, and recognition of marriage may cause a fundamental shift in some of the effects of existing estate planning. In addition, estate planners should evaluate other matters in light of the fact that their same-sex married clients will be treated as married for federal tax purposes.

a. Consider Updating Estate Plans to Provide for Possible Marital Deduction Planning

In testamentary planning, one spouse often chooses to create a trust for the surviving spouse to protect inherited assets from creditors or new spouses, to control the ultimate disposition of the property when the spouse dies, to provide management assistance for the surviving spouse, etc. For wealthy spouses, the availability of the estate tax marital deduction may give rise to a desire to defer estate tax until both spouses are deceased. As a result, same-sex married couples may wish to include QTIP, QDOT, or similar trust provisions in their estate plans.

b. Consider Amending Income Tax Returns for Open Years

Same-sex married couples should evaluate whether to amend income tax returns for all years for which the statute of limitations is open. Due to the progressive nature of income tax rates, and the thresholds for various deductions and exclusions, it may or may not be advantageous for persons to file jointly. Especially in the case of couples both of whom have substantial income, the so-called "marriage penalty" may cause overall taxes to increase. For returns filed before September 16, 2013, it appears that same-sex married couples may simply choose whichever reporting position works to their advantage and amend tax returns accordingly if not closed by the applicable statute of limitations. Rev. Rul. 2013-17 (IR 2013-72, Aug. 29, 2013). On or after that date, however, if a couple is married for tax purposes, they may not file as two single

taxpayers, nor may either spouse file as "head of household." Unanswered questions remain for same-sex married couples who owe state income tax in a state that (i) bases taxable income and filing status on one's federal return, but (ii) does not recognize same-sex marriage.

c. Consider Amending Gift Tax Returns for Open Years

Same-sex married couples should evaluate whether to file amended gift tax returns for all years for which the statute of limitations is open. Taxpayers who reported transfers as taxable gifts to a spouse on gift tax returns filed before September 16, 2013 may now modify those returns to take advantage of the gift tax marital deduction for any gift tax return not closed by the applicable statute of limitations. Rev. Rul. 2013-17 (IR 2013-72, Aug. 29, 2013). For gift tax returns filed after that date, the unlimited gift tax marital deduction should be applied. IRC §2523.

d. Consider Filing "Supplemental" Estate Tax Returns if Statute Hasn't Run

For those couples with a same-sex spouse who is now deceased, consider whether an estate tax return should be file or supplemented to claim an estate tax marital deduction or to elect portability. If the surviving spouse is not a U.S. citizen, a post-death "Qualified Domestic Trust" may be needed. *See* IRC § 2056A.

e. Consider Impact on State Death Taxes for "Decoupled" States that Base Tax on U.S. Return Principles

For those couples with a deceased same-sex spouse who owned assets in a state with a stand-alone estate or inheritance tax, consider whether an estate or inheritance tax should be filed or supplemented to claim a state-law marital deduction.

B. State Law Issues

1. Section 2 of DOMA

As noted above, Section 2 of DOMA was not addressed by the Court in *Windsor*. Again, that section provides:

> No State . . . shall be required to give effect to any public act, record, or judicial proceeding of any other State . . . respecting a relationship between persons of the same sex that is treated as a marriage under the laws of such other State . . . or a right or claim arising from such relationship.

28 USC § 1738C.

Justice Scalia, in his dissenting opinion in *Windsor* notes:

> [N]o one questions the power of the States to define marriage (with the concomitant conferral of dignity and status), so what is the point of devoting seven pages to describing how long and well established that power is? Even after the opinion has formally disclaimed reliance upon principles of federalism, mentions of "the usual tradition of recognizing and accepting state definitions of marriage" continue. What to make of this? The opinion never explains. My guess is that the majority, while reluctant to suggest that defining the meaning of "marriage" in federal statutes is unsupported by any of the Federal Government's enumerated powers, nonetheless needs some rhetorical basis to support its pretense that today's prohibition of laws excluding same-sex marriage is confined to the Federal Government (leaving the second, state-law shoe to be dropped later, maybe next Term). But I am only guessing.

United States v. Windsor, 570 U.S. 12 , ___ , 133 S. Ct. 2675 , ____ (2013) (slip opinion, Scalia, J. dissenting at 15-16) (citations omitted).

Is there any merit to this prophesy? In *Obergefell v. Kasich*, 2013 WL 3814262 (SD Ohio, July 22, 2013) (slip opinion available at www.scribd.com/doc/155439035/Obergefell-v-Kasich), the U.S. District Court for the Southern District of Ohio held that, despite provisions of the Ohio Constitution, the State of Ohio could not refuse to recognize the validity of a same-sex marriage lawfully entered into in another state. In *Obergefell*, an Ohio same-sex couple, one of whom was terminally ill, flew in a medically equipped jet to Maryland where they were married on the tarmac. After returning to Ohio, the healthy spouse brought suit in federal court to require the local Ohio registrar of death certificates to accept for recording a death certificate that reflected the decedent's marital status at death as "married" with the plaintiff named as his "surviving spouse." The Court noted that the courts of Ohio have consistently treated a marriage solemnized outside of Ohio as valid in Ohio if it is valid where solemnized. Thus, for example, under Ohio law, out-of-state marriages between first cousins are recognized by Ohio, even though Ohio law does not authorize marriages between first cousins. Likewise, under Ohio law, out-of-state marriages of minors are recognized by Ohio, even though Ohio law does not authorize marriages of minors. The Court held that by treating lawful same-sex marriages differently than it treats lawful opposite-sex marriages (e.g., marriages of first cousins and marriages of minors), Ohio law violates the Equal Protection Clause of the 14th Amendment to the United States Constitution, which guarantees that "No State shall make or enforce any law which shall ... deny to any person within its jurisdiction equal protection of the laws." Lest there be any doubt as to the import of this holding, the Court noted:

> While the holding in *Windsor* is ostensibly limited to a finding that the federal government cannot refuse to recognize state laws authorizing same sex marriage, the issue whether States can refuse to recognize out-of-state same sex marriages is now surely headed to the fore. Indeed, just as Justice Scalia predicted in his animated dissent, by virtue of the present lawsuit, "the state-law shoe" has now dropped in Ohio. *Windsor*, 133 S.Ct. at 77-78.

Slip opinion at p. 2.

2. Application of Texas Law

a. Recognition of Out-of-State Marriages

As noted above, both the Texas Constitution and the Texas Family Code define marriage as being between one man and one woman. With regard to out-of-state marriages, Texas law applies to persons married elsewhere who are domiciled in this state. TEX. FAM. CODE § 1.103. The Texas Family Code goes on the provide that:

> [I]n order to provide stability for those entering into the marriage relationship in good faith and to provide for an orderly determination of parentage and security for the children of the relationship, *it is the policy of this state to preserve and uphold each marriage against claims of invalidity unless a strong reason exists for holding the marriage void or voidable*. Therefore, every marriage entered into in this state is presumed to be valid unless expressly made void by Chapter 6 or unless expressly made voidable by Chapter 6 and annulled as provided by that chapter.

TEX. FAM. CODE § 1.101 (emphasis added).

b. Void Marriages

In Texas, Chapter 6 of the Texas Family Code declares that certain marriages are simply void. In particular, a marriage is void if one party to the marriage is related to the other as: (1) an ancestor or descendant, by blood or adoption; (2) a brother or sister, of the whole or half blood or by adoption; (3) a parent's brother or sister, of the whole or half blood or by adoption; or (4) a son or daughter of a brother or sister, of the whole or half blood or by adoption. TEX. FAM. CODE § 6.201. A marriage is void if entered into when either party has an existing marriage to another person that has not been dissolved by legal action or terminated by the death of the other spouse. TEX. FAM. CODE § 6.202. A marriage is void if either party to the marriage is younger than 16 years of age, unless a court order has been obtained under Section 2.103 of the Family Code. TEX. FAM. CODE § 6.205. A marriage is void if a party is a current or former stepchild or stepparent of the other party. TEX. FAM. CODE § 6.206. And of course, as noted above, a marriage between persons of the same sex or a civil union is "contrary to the public policy of this state" and is void in this state. TEX. FAM. CODE § 6.204(b).

c. Common-Law Marriage

Texas is among twelve states that still recognize common-law or informal marriages. An issue as to whether a common-law or informal marriage exists between the decedent and another often arises during the estate settlement process. *See Crowson v. Wakeham*, 897 S.W.2d 779 (Tex. 1995); *Hinojosa v. Hinojosa*, 866 S.W.2d 67 (Tex. App.–El Paso 1993, no writ); *Estate of Giessel*, 734 S.W.2d 27 (Tex. App.–Houston [1st Dist.] 1987, writ ref'd n.r.e.); *Jordan v. Jordan*, 938 S.W.2d 177 (Tex. App.–Houston [1st Dist.] 1997, no writ). Once the existence of a common-law or informal marriage is established, the rights and duties of a common-law spouse are equal to those afforded a spouse of a ceremonial marriage. *See Weaver v. State*, 855 S.W.2d 116 (Tex. App.–Houston [14th Dist.] 1993, no writ). The legal status of a common-law spouse is equal to that of any other married person. *See Baker v. Mays & Mays*, 199 S.W.2d 279 (Tex. Civ. App.–Fort Worth 1946, writ dism'd). These rights include community property and other statutory rights and claims. *See, e.g., Garduno v. Garduno*, 760 S.W.2d 735 (Tex. App.–Corpus Christi 1988, no writ) (informally married spouses may acquire and own community property); *Barker v. Lee*, 337 S.W.2d 637 (Tex. Civ. App.–.Eastland 1960, no writ) (informally married spouses acquire homestead rights). As noted above, a couple that is treated as married under local law by virtue of a common-law marriage continues to be treated as married for federal income tax purposes, even if they move to a jurisdiction that doesn't recognize common-law marriages. Rev. Rul. 58-66, 1958-1 CB 60. In issuing its recent guidance, the IRS cited this ruling and its rationale in adopting the "place-of-celebration" rule for same-sex marriages. Rev. Rul. 2013-17 (IR 2013-72, Aug. 29, 2013).

d. Determination of Gender

Which couples are "same-sex" couples for determining the validity of a marriage? In Texas, gender for purposes of determining the validity of a marriage is determined by genetic means, and not by anatomy. *Littleton v. Prange*, 9 S.W.3d 223 (Tex. App.–San Antonio 1999, pet. denied).

C. Spousal Rights in Texas

There are many state-law rights that arise by virtue of one's marital status in Texas[1]. If the state of Texas ultimately recognizes same-sex marriages, the examples below outline some of those rights:

[1] This material is adapted from Davis and Pacheco, "Peace Treaties: Considerations when Negotiating, Drafting & Enforcing Settlement Agreements" presented to the Probate, Trusts and Estate Section of the Houston Bar Association, September, 2012.

1. Community Property

One of the most fundamental spousal rights in Texas relates to the character of property owned by a married couple. Separate property consists of (i) property owned or claimed by the spouse before marriage; (ii) property acquired by the spouse during marriage by gift, devise, or descent; and (iii) recovery for personal injuries sustained by the spouse during marriage, except any recovery for loss of earning capacity during marriage. TEX. FAM. CODE § 3.001. Community property is all property, other than separate property, acquired by either spouse during marriage. TEX. FAM. CODE § 3.002. A presumption exists that all property acquired by either of the spouses during marriage is community property. *See* TEX. FAM. CODE § 3.003.

If an asset is community property, then upon the death of one spouse, death works a partition, so that the asset will be owned in equal undivided interests between the estate and the surviving spouse. The personal representative is authorized to administer not only the separate property of the deceased spouse, but also the former community property which was the sole management community property of the deceased spouse during the marriage, and all of the joint management community property. TEX PROB. CODE § 177. The surviving spouse is entitled to retain possession and control of all of the former sole management community property which he or she managed during the marriage. *Id.* The surviving spouse may by written instrument filed with the clerk waive any right to exercise powers as the community survivor, in which case, the personal representative of the deceased spouse is authorized to administer the entire community estate. *Id.* The personal representative also has a duty to account to the surviving spouse for post-death income from any community property assets that are in the hands of the personal representative. TEX. PROB. CODE § 378B.

2. Claims for Contribution and Reimbursement

When one spouse's marital estate has benefited from expenditures made during the marriage to the exclusion of a marital estate in which the other spouse has an interest, claims for economic contribution and reimbursement arise. While originally based in equity, the Texas Legislature enacted a statutory reimbursement right governing certain claims in 1999. When first enacted, this statutory reimbursement right granted a spouse an "equitable interest" in property. It was amended in 2001 to establish claims for "economic contribution" based upon an algebraic formula. *See* former TEX. FAM CODE § 3.402-.403. Dissatisfied with both of these approaches, the 2009 Legislature again amended the statute to essentially codify the common law for reimbursement claims. The codification of these rules is intended to provide some measure of certainty regarding equitable claims for spousal reimbursement. An overview of these potential claims follows.

a. Claim for Economic Contribution

For deaths between 1999 and 2009, a surviving spouse may have a statutory claim for economic contribution. *See* former TEX. FAM. CODE § 3.403. A claim for economic contribution is generally based on a reduction in the principal amount of debt on the other spouse's separate property or capital improvements to the other spouse's separate property. *See* former TEX. FAM. CODE § 3.402-.403.

b. Claim for Reimbursement

Beginning September 1, 2009, a surviving spouse may have a claim for reimbursement. TEX. FAM. CODE § 3.402. A claim for reimbursement may be based on (i) payment during the marriage by "one marital estate of the unsecured liabilities of another marital estate" (i.e., a community debt by one spouse's separate estate or vice versa); (ii) inadequate compensation for the time, toil, talent, and effort of one spouse by a business under the control and direction of that

spouse; and (iii) certain debt reductions and capital improvement from one marital estate to another. TEX. FAM. CODE § 3.402. As compared to the statutory formula that applied to claims for economic contribution, a claim for reimbursement is decided by the court by "using equitable principles, including the principle that claims for reimbursement may be offset against each other if the court determines it to be appropriate." TEX. FAM. CODE § 3.402(b). Thus, the court may offset the monetary value of the spouse's use and enjoyment of property against a claim for reimbursement. TEX. FAM. CODE § 3.402(c). The court is authorized to impose a lien for payment of the claim upon death or dissolution of the marriage. TEX. FAM. CODE § 3.406. Certain payments, such as for necessaries, are not reimbursable. TEX. FAM. CODE § 3.409.

3. Homestead

A homestead right, regardless of whether the property is separate or community, may be claimed when the decedent is survived by a spouse. *See* TEX. PROB. CODE §§ 271, 282; *Givens v. Hudson*, 64 Tex. 471 (1885); *Zwerneznann v. Von Rosenburg*, 76 Tex. 522, 13 S.W. 485 (1890); *Childers v. Henderson*, 76 Tex. 664, 13 S.W. 481 (1890); *Jenkins v. Hutchens*, 287 S.W.2d 295 (Tex. Civ. App.–Eastland 1956, writ ref'd n.r.e.). A rural homestead consists of 200 acres of land for a married decedent or 100 acres for a single decedent, while an urban homestead consists of a lot or lots not exceeding ten acres. *See* TEX. CONST. ART. 16, § 51; TEX. PROP. CODE § 41.002.

Title to a homestead vests in the heirs of the decedent as other real property under the laws of descent and distribution if one dies with a surviving spouse. *See* TEX. PROB. CODE §§ 37, 283. Thus, the homestead cannot be construed as an estate asset subject to the control of the representative or court, nor is any income derived therefrom subject to such control. *See Childers v. Henderson*, 76 Tex. 664, 13 S.W. 481 (1890); *Franklin v. Woods*, 598 S.W.2d 946 (Tex. Civ. App.–Corpus Christi 1980, no writ); *Thompson v. Thompson*, 149 Tex. 632, 236 S.W.2d 779 (1951). The homestead may not be partitioned until all superior rights of occupancy have been terminated. *See* TEX. CONST. ART. 16, § 52; TEX. PROB. CODE §§ 284, 285; *Hudgins v. Sansom*, 72 Tex. 229, 10 S.W. 104 (1888).

4. Family Allowance

Immediately upon the approval of a filed probate inventory or upon the filing of an affidavit in lieu thereof, the court must fix a family allowance for support of the surviving spouse (as well as any minor or adult incapacitated children). The spouse and children may apply for the allowance even prior to the approval of the inventory and the court may fix it at that time. The allowance is to be in an amount sufficient for their maintenance for one year from the date of death. *See* TEX. PROB. CODE §§ 286-293. No allowance can be made for surviving spouses who possess sufficient separate property of their own from which they are able to provide for their own maintenance. *See* TEX. PROB. CODE § 288; *Pace v. Eoff*, 48 S.W.2d 956 (Tex. Comm'n App. 1932, holding approved); *Kennedy v. Draper*, 575 S.W.2d 627 (Tex. Civ. App.–Waco 1978, no writ); *Noble v. Noble*, 636 S.W.2d 551 (Tex. Civ. App.–San Antonio 1982, writ ref'd n.r.e.). This allowance, when proper, is a matter of right and is not construed as an advancement. Thus, repayment at the end of the estate administration is not required. *See* TEX. PROB. CODE § 290; *Chefflet v. Willis*, 74 Tex. 245, 11 S.W. 1105 (1889); *Stutts v. Stovall*, 544 S.W.2d 938 (Tex. Civ. App.–San Antonio 1976, writ ref'd n.r.e.). A family allowance can consist of money, property, or both, and the court may order a sale of assets to raise the allowance, including the sale of property specifically bequeathed when no other assets exist. *See* TEX. PROB. CODE §§ 292, 293.

5. Exempt Personal Property

In addition to the homestead, surviving spouses are entitled to have certain exempt personal property set aside for their use during administration. *See* TEX. PROB. CODE §§ 271, 272; TEX. CONST. ART. 16, § 49; TEX. PROP. CODE §§ 42.001 and 42.002.

a. Solvent Estates

In a solvent estate, exempt property may be used by persons entitled thereto during the administration. But, the right to use these assets (other than the homestead or allowance) terminates when the estate is closed. The personal property is then distributed to the heirs or devisees of the decedent. *See* TEX. PROB. CODE § 278; *Kelley v. Shields*, 448 S.W.2d 135 (Tex. Civ. App.–San Antonio 1969, writ ref'd n.r.e.).

b. Insolvent Estates

In an insolvent estate, title to the exempt personal property passes to the spouse and children free of all debts, except those debts secured by existing liens, or claims for funeral and last illness expenses. *See* TEX. PROB. CODE §§ 277, 279, 281, 320(a)(1); *American Bonding Co. of Baltimore v. Logan*, 106 Tex. 306, 166 S.W. 1132 (1914) (Certified Questions Answered).

c. Allowance in Lieu

When a decedent's estate does not contain a homestead or exempt personal property, the surviving spouse and children may apply to the court for an allowance in lieu thereof. An allowance is permitted of up to $45,000 for the homestead (increased from $15,000 on January 1, 2014) and $30,000 for other exempt property (increased from $5,000 on January 1, 2014). *See* TEX. PROB. CODE §§ 273, 275; *In re: Mays' Estate*, 43 S.W.2d 306 (Tex. Civ. App.–Beaumont 1931, writ ref'd). The allowance may be satisfied in money, property, or both, and regardless of whether it was bequeathed to another. *See* TEX. PROB. CODE § 274. Property of the estate may be sold by court order to obtain funds necessary for the payment of the allowance. *See* TEX. PROB. CODE § 276.

V. Conclusion

United States v. Windsor makes it clear that same-sex couples who reside in a state that recognizes same-sex marriage will be considered as married for federal tax purposes. Revenue Ruling 2013-17 amplifies *Windsor*, holding that all same-sex married couples will be treated as married for all federal tax purposes, including income, estate, gift, and generation-skipping transfer tax purposes, regardless of the state of the couple's residence. As a result, in Texas (at least for now), we find ourselves in a setting where same-sex couples are treated as married for purposes of federal law, but not for purposes of state law. This bifurcation of marital status will require estate planners to evaluate their clients' goals while applying "married" federal tax principles to "single" state-law property rights. Estate planners representing same-sex married couples will be challenged to develop and implement estate plans that adapt to this complex and rapidly changing area of the law.

List of States Recognizing Same-Sex Marriage and their Effective Dates

California—recognized same-sex marriages from other states and permitted same-sex marriage June 17, 2008 through Nov. 4, 2008, and June 26, 2013 through the present.

Connecticut—recognized same-sex marriages from other states and permitted same-sex marriage Nov. 12, 2008.

Delaware—recognized same-sex marriages from other states and permitted same-sex marriage July 1, 2013.

Iowa—recognized same-sex marriages from other states Apr. 30, 2009; permitted same-sex marriage Apr. 20, 2009.

Maine—recognized same-sex marriages from other states and permitted same-sex marriage Dec. 29, 2012.

Maryland—recognized same-sex marriages from other states Feb. 3, 2010; permitted same-sex marriage Jan. 1, 2013.

Massachusetts—recognized same-sex marriages from other states and permitted same-sex marriage May 17, 2004.

Minnesota—recognized same-sex marriages from other states and permitted same-sex marriage Aug. 1, 2013.

New Hampshire—recognized same-sex marriages from other states and permitted same-sex marriage Jan. 1, 2010.

New York—recognized same-sex marriages from other states Feb. 1, 2008; permitted same-sex marriage July 24, 2011.

Rhode Island—recognized same-sex marriages from other states Feb. 1, 2008; permitted same-sex marriage Aug. 1, 2013.

Vermont—recognized same-sex marriages from other states and permitted same-sex marriage Sept. 1, 2009.

Washington—recognized same-sex marriages from other states and permitted same-sex marriage Dec. 6, 2012.

Washington, DC—recognized same-sex marriages from other states July 7, 2009; permitted same-sex marriage Mar. 9, 2010.