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## Filing Joint Tax Returns Is the Usual Choice, but Separate Returns Can Sometimes Be Better

*Thomson Reuters analyst explains advantages and disadvantages for U.S. individuals filing under either status*

**NEW YORK, March 13, 2013**— Every tax season, married couples must choose between filing a joint return or filing two separate returns. “For most people, joint filing is the usual and preferred choice,” says Scott Weiner, a senior tax analyst at Thomson Reuters. “But there are some cases in which the option to file separate returns should be taken.”

**Who can file jointly.** To qualify to file a joint return, a couple must be married as of the close of the tax year. So, a couple that marries on December 31 can file a joint return, but a couple that divorces on December 31 cannot. If a taxpayer’s spouse died during the year, a joint return can be filed with the deceased spouse unless the taxpayer remarries before year’s end.

If married and not filing jointly, a taxpayer must file with the status of “married filing separately.” The taxpayer cannot file as a single individual or a head of household. There is an exception for the abandoned spouse—an individual who lived apart from his or her spouse for the last six months of the year, maintained a household for a dependent child, and furnished more than half the costs of that household. Those individuals can file as head of household, taking advantage of lower rates and a higher standard deduction.

When spouses file separately, each spouse reports only his or her own income, exemptions, credits, and deductions. In the nine community property states—Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin—income and deductions are generally split 50-50 on separate returns. As a result, filing separately is less likely to produce a tax advantage in those states.

**Why file jointly.** By filing jointly, taxpayers save on paper work and preparer fees. More importantly, they may also save on taxes.

For one thing, a couple’s income may be taxed at a lower marginal tax rate on a joint return. The dollar amounts at which each rate bracket begins on a joint return are exactly double the corresponding figures for a separate return. For example, in 2012, the 28 percent rate bracket begins above $142,700 on a joint return and above $71,350 on separate returns.

So, if one spouse has earned most of the couple’s income during the year, filing jointly may allow that income to be taxed at a lower rate. For example, one spouse had $100,000 of taxable income for 2012 and the other spouse had $20,000. On a joint return, none of their combined income of $120,000 would be taxed at a 28 percent rate. On separate returns, $28,650 of the high-earning spouse’s income would be taxed at 28 percent.

In addition, many tax breaks are unavailable on a separate return. A taxpayer cannot claim the earned income credit (EIC), the adoption credit, the education credits, or the credit for the elderly or the disabled. Deductions for student loan interest or tuition and fees for higher education are also not available. There are still more disadvantages to separate returns. If a spouse files a separate return and itemizes deductions, the other spouse cannot claim the standard deduction on his or her separate return, even if it would be advantageous to do so. If an individual receives social security benefits, filing separately may mean that a larger portion of the benefits are taxed. If either spouse is covered by an employer’s qualified retirement plan, the deduction for IRA contributions may be less if filing a separate return.

**When to file separately.** With all of these disadvantages, why would anyone file a separate return? One reason is to lessen the impact of limitations that are based on an individual's adjusted gross income (AGI). For example, medical expenses are deductible only to the extent they exceed 7.5 percent of the individual's AGI (10 percent of AGI after 2012 for individuals under age 65). In the case of miscellaneous itemized deductions, the amount that must be exceeded is 2 percent of AGI.

*Scenario.* For 2012, husband had $140,000 of AGI and $2,000 of medical expenses. Wife had $60,000 of AGI and $12,000 of medical expenses, which she paid herself.

- On a joint return, the couple would have $200,000 of AGI and $14,000 of medical expenses. The medical expense deduction would be completely barred by the 7.5 percent limit.
- On separate returns, husband still cannot deduct any of his medical expenses, but wife can deduct $7,500 of hers. That is the amount by which her $12,000 of expenses exceeds $4,500, which is 7.5 percent of her AGI.

"Even in cases like this one, it is important to make sure that the extra deductions are not outweighed by the other advantages of filing a joint return," advises Weiner. "The only way to do this is by figuring the tax both ways."

**File separately to avoid joint liability.** A husband and wife who file a joint return have joint and several liability for the tax. This means that both spouses are liable for the entire tax on the return, even if all the income belonged to one spouse. This is true even if the spouses later divorce and the divorce decree says that one spouse is liable for the tax. Both spouses are also liable for tax and penalties on income that one spouse should have reported but did not.

"Where there is a suspicion that the other spouse may have underreported income or overstated deductions, filing separately may be advisable to avoid potential liability," says Weiner. "While the law does grant some relief after the fact to 'innocent spouses', this is far from automatic." Among other requirements, the innocent spouse must prove that he or she had no reason to know about the tax understatement. "It's better to prevent trouble in the first place by filing a separate return than to rely on escaping it later by claiming to be an innocent spouse."

**Same-sex couples.** Whether two people are married is usually a matter of state law. But an important exception to this rule applies in the case of same-sex couples. Same-sex marriages are legal in nine states—Connecticut, Iowa, Maine, Maryland, Massachusetts, New Hampshire, New York, Vermont, and Washington—and the District of Columbia. But the IRS does not recognize these marriages because a federal statute, the Defense of Marriage Act (DOMA), defines "marriage" as a legal union between one man and one woman as husband and wife.

The result is that same-sex couples cannot file a joint return or married filing separately returns for federal tax purposes. They must use another filing status, such as single or head of household. Sometimes, this inability to file jointly can work to the advantage of same-sex couples. Filing two single returns can produce a better tax result than filing a joint return. This is a consequence of the "marriage penalty," which may cause a married couple to pay more tax than they would as two singles.
On the other hand, DOMA denies same-sex couples important tax breaks, such as the opportunity to get tax-free employer health coverage for the same-sex spouse.

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Taxpayers have met with some success in lawsuits challenging DOMA's unequal treatment of same- and different-sex couples. In one case, *Windsor v. U.S.*, the Second Circuit held that DOMA is unconstitutional as it relates to the federal estate tax marital deduction. The Supreme Court has agreed to hear an appeal from the Second Circuit's decision, with oral arguments scheduled for March 27.

It is impossible to know what the Supreme Court will decide or how far-reaching its decision will be. In the meanwhile, one option for same-sex couples would be to file returns applying the DOMA rules that deny their marital status. Later, they can file an amended return claiming tax breaks that are currently allowable only to spouses of the opposite sex.

"The couple should disclose that they are a legally married same-sex couple and are making the claim on the basis that DOMA is unconstitutional," advises Weiner. "This filing may preserve their right to a refund if DOMA is struck down or repealed."

Taxpayers should consult with a personal tax adviser before applying these or other tax strategies.

Up-to-date analyses of legislation and regulations affecting individual taxpayers are available for tax and accounting professionals on the industry-leading, award-winning Thomson Reuters Checkpoint research platform.

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