



## NEW DRAFT INCOME TAX FILING GUIDELINES FOR CALIFORNIA REGISTERED DOMESTIC PARTNERS: IMPLEMENTING SB 1827 AND SB 105

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### **NEW LAW**

Since 2003, the California legislature has passed a series of bills intended to rectify the issues of inequality that have come to light since the implementation of [AB 205: the California Domestic Partner Rights and Responsibilities Act of 2003](#). One of these bills, [SB 1827: the State Income Tax Equity Act of 2006](#), was signed into law in September 2006. SB 1827, along with a subsequent associated bill, SB 105, amends the California Tax Code and the California Family Code so that RDPs are now required, absent a valid agreement to the contrary, to characterize their earned income as community property for income tax purposes, and are required to file their state income tax returns jointly or separately "by applying the standards applicable to spouses." The new filing status is applicable for the fiscal year 2007 and affects only California state income tax returns.

### **BACKGROUND**

AB 205 was adopted by the California legislature and signed by Governor Davis in September 2003. The primary intent of AB 205 was to help move California "closer to fulfilling the promises of inalienable rights, liberty, and equality contained in ... the California Constitution by providing all caring and committed couples, regardless of their gender or sexual orientation, the opportunity to obtain essential rights, protections, and benefits and to assume corresponding responsibilities, obligations, and duties."<sup>1</sup> However, primarily as a result of the political realities at the time AB 205 was adopted, the final version of AB 205 included a number of important exceptions to the goal of absolute equality. Two of these exceptions were that California registered domestic partners (RDPs) were precluded from characterizing their earned income as community property for income tax purposes, and that RDPs were required to file their state tax returns using the same filing status as they used on their federal income tax returns. This meant that RDPs could only file as "individual" taxpayers or, in some instances, as "head of household," since the federal government does not recognize same-sex couples as anything more than legal strangers.

### **IMPLEMENTATION**

Since the adoption of SB 1827, the [California Franchise Tax Board \(FTB\)](#) has been working diligently to develop instructions that will help RDP taxpayers and their tax practitioners understand how to file state income tax returns with the least amount of difficulty and the greatest degree of equality. This has been an especially challenging but critical step because SB 1827, in recognizing the rights of RDPs, effectively makes California law more inclusive than federal tax laws, which continue to deny equal treatment to same-sex couples.

The FTB has recently published detailed directions for RDPs and their tax practitioners for filing California income tax returns beginning in 2008. These guidelines are reflected in Publication 737: Tax Information for Registered Domestic Partners.

### **WHAT TO EXPECT FROM THE NEW FILING REQUIREMENTS**

The following provides an explanation of some of the key topics addressed by the FTB in Publication 737.

#### *Who Is Affected?*

Every taxpayer who is required to file a California personal income tax return for fiscal year 2007 and who is registered with the State of California as a domestic partner is subject to the new tax filing regulations. However, only those taxpayers with *RDP adjustments* will find it necessary to utilize the guidelines and worksheet provided in Publication 737.

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<sup>1</sup> California Domestic Partners Rights and Responsibilities Act of 2003 § 1(a), ch. 421, 2003 Cal. Stat. 2586. This bill states, "This act is intended to help California move closer to fulfilling the promises of inalienable rights, liberty, and equality contained in Sections 1 and 7 of Article 1 of the California Constitution by providing all caring and committed couples, regardless of their gender or sexual orientation, the opportunity to obtain essential rights, protections, and benefits and to assume corresponding responsibilities, obligations, and duties and to further the state's interests in promoting stable and lasting family relationships, and protecting Californians from the economic and social consequences of abandonment, separation, the death of loved ones, and other life crises."

RDP adjustments include such items as:

- ◆ Division of Community Property
- ◆ Capital losses
- ◆ Transactions between RDPs
- ◆ Sale of a residence
- ◆ Dependent care assistance
- ◆ Investment interest
- ◆ Qualified residence acquisition loan and equity loan interest
- ◆ Expense depreciation property limitations
- ◆ Individual Retirement Accounts
- ◆ Education loan interest
- ◆ Rental real estate passive loss
- ◆ Rollover of publicly traded securities gains into specialized small business investment companies<sup>2</sup>

### *Filing Requirements*

The first step for all RDP taxpayers is to complete a Federal personal income tax return as usual, using the “individual” or, where appropriate, the “head of household” filing status. **This is the return that should actually be filed with the IRS.**

Then, depending on whether the RDP taxpayers have filing status adjustments, there are three ways to properly complete their California personal income tax returns.

1. If the RDP taxpayers have no RDP adjustments, they simply combine the Adjusted Gross Income (AGI) from each individual federal return and enter this sum as the AGI on their California return.
1. If the RDP taxpayers do have RDP adjustments, they can **choose one** of the following methods to properly recalculate their federal AGI for reporting on their California return:
  - A. Create a *pro forma* Federal personal income tax return. This return should reflect all community property<sup>3</sup>, as well as deductions, credits, and exemptions that would be available to the taxpayer if she or he was filing the Federal return using the “married filing jointly” or “married filing separately” status. **This return is for calculation purposes *only* and should *not* be submitted to the IRS.**
  - B. Complete the California RDP Filing Status Adjustments Worksheet provided in Publication 737. This will allow the taxpayers to make adjustments for such items as employer-provided accident and health insurance, certain medical expenses and qualified long-term health care insurance, and self-employed health insurance, all of which are allowed as deductions for California income tax purposes even if they are not permitted for federal income tax purposes.<sup>4</sup>

The recalculated adjusted gross income from either of these calculations will then be entered on Schedule CA, as directed, so that the resulting state tax liability for RDP taxpayers will be substantially equivalent to similarly situated married spouses.

### *Filing Status*

Until this year, RDPs have been required to file their state income tax returns using the same filing status as they used on their federal income tax returns – either “individual” or, in the appropriate circumstances, “head of household.” Going forward, RDPs will be required to file their state income tax returns using (almost) the same filing statuses as are used by married spouses.

These filing status options include<sup>5</sup>:

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<sup>2</sup> Cal. Franchise Tax Bd., FTB Publication 737: Tax Information for Registered Domestic Partners (Dec. 2007), available at [http://www.ftb.ca.gov/forms/07\\_forms/07\\_737.pdf](http://www.ftb.ca.gov/forms/07_forms/07_737.pdf).

<sup>3</sup> IRS, Dep’t of the Treasury, Publication 555: Community Property (May 2007).

<sup>4</sup> Cal. Franchise Tax Bd., Publication 737, *supra* note 2, at 14.

<sup>5</sup> *Id.* at 4.

### Married/RDP Filing Jointly

RDP taxpayers may file with this status if *any* of the following is true:

- ◆ The taxpayer is registered with the State of California as a domestic partner as of 12/31/07,
- ◆ The taxpayer's RDP died during the 2007 calendar year and the surviving RDP did not re-register prior to 12/31/07, or
- ◆ The taxpayer's RDP died in the 2008 calendar year but before the surviving taxpayer filed her or his state income tax return.

### Married/RDP Filing Separately<sup>6</sup>

Although filing with this status will usually result in greater tax liability than filing jointly, depending on their individual circumstances certain taxpayers may determine that it will be necessary or beneficial to file using this status.

Taxpayers who choose to file using this status should be aware that the community property rules apply to the division of income for filing purposes.<sup>7</sup>

### Head of Household (HOH)

Most RDPs will no longer be able to file as "head of household" at the state level unless the taxpayer complies with *all* of the following criteria:

- ◆ The taxpayer is not an RDP as of 12/31/07,
- ◆ The taxpayer paid more than 50% of the cost of keeping her or his home during the year,
- ◆ The taxpayer's home was the primary home for the taxpayer and her or his child for more than 50% of the year, and
- ◆ The taxpayer was not a resident alien at any time during the year.

Taxpayers can continue to file as HOH for federal purposes if they meet the qualification requirements, which include contributing more than 50% of a dependent's expenses.

A taxpayer's claimed filing status can have significant ramifications for her or his tax liability. Therefore, we strongly encourage affected parties to continue visiting this site or the [FTB site](#) for updated materials, and to consult a qualified tax practitioner who is current with the new requirements if you have additional questions and/or a particularly complex asset mix.

Because RDPs are subject to an ever-changing legal and tax landscape that confers greater rights and recognition of relationships, it is necessary to work with professionals who are committed to understanding the complexities and options that are emerging. As an active participant in the development of this and other legislation beneficial to same-sex couples, such as the recently adopted [law affecting real property tax reassessments](#), [DLKLawGroup, PC](#) is uniquely situated to work with RDPs and other same-sex, unmarried, or blended families to create estate plans that will provide the greatest benefits to those parties.

Additional information can be found at the following sites:

[California Secretary of State: Domestic Partners Registry](#)  
[Equality California](#)  
[National Center for Lesbian Rights](#)

*DLKLawGroup<sup>PC</sup> provides comprehensive and competent estate planning, probate and trust administration services, and beneficiary representation for Registered Domestic Partners and other members of the LGBT community. We provide realistic solutions that reflect the goals and desires of each client from our offices in San Francisco, Santa Rosa, and Palm Springs. If you would like to find out more about how to protect yourself and your loved ones, please visit [www.dlklawgroup.com](http://www.dlklawgroup.com), or call 415.693.0550.*

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<sup>6</sup> Additional information regarding this status is provided in FTB Publication 1051A: Guidelines for Married/RDP Filing Separate Returns, *available at* [http://www.ftb.ca.gov/forms/04\\_forms/04\\_1051A.pdf](http://www.ftb.ca.gov/forms/04_forms/04_1051A.pdf).

<sup>7</sup> Community property and separate property are defined briefly in Publication 737 at page 5. Additional information regarding community property is provided in Publication 555, *supra* note 3.