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In 1990 the Louisiana Legislature repealed the provisions of the Louisiana Civil Code authorizing a judgment of separation from bed and board.¹ Under the current Civil Code, married couples can no longer file for legal separation. If a husband and wife in Louisiana do not wish to remain together, they may either separate informally or file a petition for divorce which will be granted after 180 days.²

The repeal of the provisions authorizing separation from bed and board was part of a major revision of Louisiana’s marriage and divorce law which simplified the procedures for obtaining a divorce, making no-fault divorce available without requiring spouses to live apart for a period of time.³ Before the revision, spouses could obtain a no-fault divorce in Louisiana by living separate and apart for one year.⁴ A Louisiana spouse who desired to obtain a divorce sooner was required to prove that the other spouse either had committed adultery or had been convicted of a felony; an expedited divorce also could be achieved by claiming a lesser degree of fault on the part of the other spouse in order to obtain a judgment of separation from bed and board first.⁵

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⁵. La. Civ. Code art. 139 (1870); La. R.S. 9:302 (repealed 1990). Under the former provisions of the Louisiana Civil Code, a spouse who wished to obtain a divorce without asserting any fault on the part of the other spouse had to wait the same amount of time to obtain the divorce, whether the spouse filed a petition for a judgment of separation from bed and board or merely filed a petition for a judgment of divorce. A spouse could obtain a judgment of divorce on a no-fault basis after living separate and apart from the other spouse for one year. La. R.S. 9:301 (repealed 1990). A spouse could obtain a judgment
The living separate and apart statutes were considered an unnecessary requirement which, by obliging spouses to live apart for a substantial period of time prior to the entry of a judgment of divorce, tended "to defeat the main purpose of the statutory waiting periods—to promote reconciliation." Legal separation was seen as a step on the way to divorce that served little purpose other than creating a backlog of cases for family courts. Under the current provisions of the Civil Code, spouses may obtain a divorce without first obtaining a judgment of separation from bed and board, thereby avoiding the cumbersome process, the long delays, and the added expenses that were required under former law.

Easing the burden on divorcing spouses by simplifying the divorce procedures should have no federal income tax consequences. Unfortunately, however, by eliminating the possibility of obtaining a legal separation, the Louisiana Legislature has limited the federal tax savings options of many separating spouses in Louisiana. The Internal Revenue Code is laced with provisions whose application depends upon the marital status of the taxpayer. For some taxpayers, the tax savings are greater if they are considered "married" for federal income tax purposes. In such cases, the Internal Revenue Code produces a marriage bonus. In more cases, however, greater tax savings can be achieved if a couple is "not married." Provisions that result in a higher tax to married taxpayers are referred to as the marriage penalty provisions of the Internal Revenue Code.

of separation from bed and board after living separate and apart from the other spouse for six months. La. Civ. Code art. 138(a) (1987). Upon obtaining the judgment of separation from bed and board, the spouse was required to wait another six months before being eligible to obtain a judgment of divorce. La. R.S. 9:302 (repealed 1990).

Obtaining a separation from bed and board, however, could expedite the procedure in many cases. Under the former provisions, a spouse who filed a petition for divorce could obtain a divorce within a year only by proving either adultery on the part of the other spouse or conviction of the other spouse of a felony and his or her sentence to death or imprisonment at hard labor. La. Civ. Code art. 139 (1870). In many cases a spouse could expedite the procedure by obtaining a separation from bed and board upon proof of one of the fault grounds listed in former La. Civ. Code art. 138(1)-(8), which included, in addition to adultery or conviction of a felony, the habitual intemperance of the other spouse, public defamation by the other spouse, abandonment, attempted murder, status as a fugitive from justice, or intentional non-support. These rules obviously required a showing of lesser fault than the fault required to obtain an expedited judgment of divorce. In many cases a spouse could obtain a judgment of divorce within one year by first obtaining a judgment of separation from bed and board on one of the lesser fault grounds listed in former La. Civ. Code art. 138 and then waiting six months.


7. Statement of Cynthia Samuel, Divorce Revision: Meeting of the Joint Leg. Study Committee 2 (Feb. 1, 1989); Laborde, supra note 3, at 1004.

The so-called "marriage bonus" provisions of the Internal Revenue Code generally produce tax savings for one-earner married couples. The traditional justification for the marriage bonus provisions is that the earning spouse incurs greater financial responsibilities than a person who has no spouse or child to support.\textsuperscript{9} Some commentators have justified the tax relief provided to the earning spouse on a "benefits" theory, arguing that to the extent the nonworking spouse benefits from the income earned by the spouse who works, the nonworker should be taxed on the worker's income.\textsuperscript{10}

The "marriage penalty" provisions, which generally add to the tax burden of a married couple when both spouses earn income,\textsuperscript{11} have been justified on the grounds that a married couple has a greater capacity to pay a higher tax than an unmarried individual earning the same amount.\textsuperscript{12} A married couple enjoys economies of scale by sharing household expenses, and a married couple benefits from the free household services provided by each spouse. The assumptions upon which the marriage bonus and penalty provisions are based lose their validity when a couple separates.\textsuperscript{13} Congress implicitly has recognized this fact by

\textsuperscript{9} Boris I. Bittker, \textit{Federal Income Taxation and the Family}, 27 Stan. L. Rev. 1389, 1417 (1975). The marriage bonus provisions originally were enacted to equalize the tax burden of married couples. Before 1948 the individual was the taxable unit for purposes of the federal income tax. A married couple could not split the family's income between the two spouses unless the couple was domiciled in a community property state. Because each spouse in a community property state is the owner of one-half of the community income, each spouse is responsible for the tax on one-half of the community income. Poe v. Seaborn, 282 U.S. 101, 51 S. Ct. 58 (1930). The rule allowing spouses to share community income reduced the tax burden of spouses in community property states because each half of the community income was taxed at the lower rates that apply under the progressive rate structure of the federal income tax. Married taxpayers in noncommunity property states could not achieve the same tax savings, even if they contracted to share all of their earnings. Lucas v. Earl, 281 U.S. 111, 50 S. Ct. 241 (1930). In 1948 Congress equalized the tax treatment of married couples by authorizing every married couple, whether the spouses reside in a community property state or noncommunity property state, to file a joint return, aggregating the spouses' income and deductions, and paying a tax equal to twice what a single person would pay on one-half of their consolidated taxable income. Revenue Act of 1948, Pub. L. No. 471, 80th Cong., 2d Sess. (April 2, 1948). For a discussion of the Revenue Act of 1948, see Stanley S. Surrey, \textit{Federal Taxation of the Family—The Revenue Act of 1948}, 61 Harv. L. Rev. 1097 (1948). For a history of the income-splitting provisions of the Internal Revenue Code, see Bittker, \textit{supra}, at 1399-1418.

\textsuperscript{10} See, \textit{e.g.}, Michael J. McIntyre & Oliver Oldman, \textit{Taxation of the Family in a Comprehensive and Simplified Income Tax}, 90 Harv. L. Rev. 1573 (1977).

\textsuperscript{11} The income tax rate schedules and the limitations on deductions generally produce a marriage penalty whenever one spouse earns eighty percent or less of the couple's combined income and the other spouse earns twenty percent or more of the combined income. For an explanation of the effect of the income tax rates on a two earner couple, see Michael J. McIntyre, \textit{Fairness to Family Members Under Current Tax Reform Proposals}, 4 Am. J. Tax Pol'y 155, 161-74 (1985).

\textsuperscript{12} Bittker, \textit{supra} note 9, at 1419-20.

\textsuperscript{13} Many commentators have argued that the assumptions upon which the marriage
providing that, under certain circumstances, separated spouses are considered unmarried for federal income tax purposes.\textsuperscript{14}

In general, a taxpayer's marital status is determined on the last day of the taxable year.\textsuperscript{15} If a couple is not divorced by December 31, both spouses are considered married for most tax purposes no matter how long they have been living apart unless they are "legally separated under a decree of divorce or of separate maintenance"\textsuperscript{16} or unless an exception known as the "abandoned spouse" rule applies.\textsuperscript{17}

The phrase "legally separated under a decree of divorce or of separate maintenance" is a term of art. Spouses must be legally separated


See \textit{I.R.C. § 7703(a)(2), (b)} (1988) (a person who is legally separated and certain married persons who live separately and apart from their spouses are considered unmarried for federal income tax purposes).


16. Each provision of the Internal Revenue Code whose operation varies depending on the taxpayer's marital status has its own definition of marital status. Under most of these provisions, however, a spouse is considered unmarried if the spouse is legally separated under a decree of divorce or separate maintenance. See, e.g., \textit{I.R.C. §§ 1(a), (c), (d); 2(c); 21(e)(3); 22(e)(2); 32(d); 55(d); 68(b)(1); 86(c)(3)(A); 135(d)(2); 151; 318(a)(1)(A)(i); 7703(a)(2)} (1988 & Supp. 1991).

17. When the abandoned spouse rule applies a spouse often, but not always, will be considered unmarried for federal income tax purposes. For the abandoned spouse rule, see \textit{I.R.C. § 7703(b)} (1988). A number of provisions of the Internal Revenue Code incorporate the abandoned spouse rule by referring to \textit{I.R.C. § 7703(b)}. See, e.g., \textit{I.R.C. §§ 1(a), (c), (d); 2(c); 22(e)(2); 32(d); 55(d); 68(b)(1); 86(c)(3)(A); 135(d)(2); 151} (1988 & Supp. 1991).
to establish that they are no longer married under this standard. A court decree that merely requires one spouse to make support payments to another spouse does not effect a legal separation for purposes of determining that a couple is not married. 18

Even if a couple is not legally separated under a decree of divorce or of separate maintenance, one or both of the spouses may be considered not married for purposes of federal income taxation under the abandoned spouse rule. 19 Under this rule, an individual is considered not married if, *inter alia*, the individual maintains as his or her home a household which constitutes for more than one-half of the taxable year the principal place of abode of a dependent child. 20 Thus it is possible, where one spouse has custody of the children, for the custodial spouse to be considered not married while the noncustodial spouse is considered married. Of course, if a Louisiana couple has no children and the divorce is not final, the couple will be considered married. Thus, many Louisiana couples who are living apart but do not wish to divorce for either religious or personal reasons and spouses whose divorces are not final are considered married for federal tax purposes.

This article discusses some of the federal tax provisions that most often affect Louisiana couples who are living separate and apart. Because the federal tax burden can be reduced significantly for many couples who qualify as being not married, this article suggests that the Louisiana Legislature restore some provision for legal separation to the Louisiana

18. See, e.g., Boyer v. Commissioner, 732 F.2d 191 (D.C. Cir. 1984), rev’g 79 T.C. 143 (1982) (court order for temporary support coupled with a temporary restraining order did not effect a legal separation); Capodanno v. Commissioner, 602 F.2d 64, 68 (3d Cir. 1979) (issuance of a court decree that merely enforces a right to a support payment does not result in a legal separation for purposes of establishing that the spouses are unmarried for purposes of federal income taxation); Dunn v. Commissioner, 70 T.C. 361 (1978) (a court order for temporary maintenance does not render the spouses unmarried); Boettiger v. Commissioner, 31 T.C. 477 (1958), *acq.* 1959-1 C.B. 3 (a court decree that only provides for payment of support does not effect a legal separation); Palmquist v. United States, 284 F. Supp. 577 (N.D. Cal. 1967) (an interlocutory decree does not effect a legal separation); Muracca v. Commissioner, 40 T.C.M. (CCH) 3 (1980) (decree for alimony pendente lite does not effect a legal separation). *But see* Legget v. Commissioner, 329 F.2d 509 (2d Cir. 1964) (Florida decree for alimony without divorce was in effect a limited divorce, rendering the taxpayer unmarried for federal income tax purposes).

19. I.R.C. § 7703(b) (1988). A spouse need not actually be abandoned to be considered not married under this rule. To satisfy the "abandonment" requirement, a taxpayer must live apart from his or her spouse during the last six months of the taxable year. I.R.C. § 7703(b)(3) (1988).

20. The child must be a dependent for whom the taxpayer is entitled to deduct a dependency exemption under I.R.C. § 151, or would be entitled to deduct the exemption but for the fact that the taxpayer has waived the right to the deduction under I.R.C. § 152(e) so that the noncustodial parent can claim the deduction. I.R.C. § 7703(b)(1) (1988). For a discussion of the abandoned spouse rule, see *infra* notes 188-91 and accompanying text.
Civil Code. This article does not advocate reenactment of any requirement that a spouse obtain a judgment of separation from bed and board as a prerequisite to obtaining an expedited, no-fault divorce. Indeed, because some couples can achieve greater tax savings if they are considered married, this article suggests that the provisions for legal separation be optional rather than mandatory for a couple who files for divorce.

Each spouse in a community property state like Louisiana is liable for the tax on one-half of the community income, no matter which spouse actually earns the income or has the beneficial enjoyment of it. The tax liability for one-half of the community income often imposes a heavy burden on the spouse who has access to less of the community income, because the spouse earns less or because the spouse has no access to property producing community income. For convenience, this article will refer to the spouse with reduced access to community income as the "low income spouse" and the spouse who has greater access to community income as the "high income spouse."

The low income spouse most easily can escape the liability for tax on one-half of the community income by terminating the community. Several different events can trigger a termination of the community in Louisiana, including a judgment of divorce, a matrimonial agreement that terminates the community, and a judgment of separation of property. A judgment of separation from bed and board under former provisions of the Louisiana Civil Code also terminated the community. While a separated spouse can terminate the community under the current provisions of the Louisiana Civil Code, it may be difficult to do so before the divorce is final. Spouses who separate without contemplating a divorce could face serious obstacles to terminating the community. Enactment of provisions authorizing a judgment of separation from bed and board which would terminate the community would make it easier for separated spouses in Louisiana to terminate the community.

Part I explains the rules for taxation of community income and provides the background for understanding how various provisions of community income are treated. It also discusses the rules for taxation of community income for both the high income spouse and the low income spouse.

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22. Admittedly, it is inaccurate to refer to either spouse living under a community property regime as a low income or a high income spouse. Each spouse in Louisiana has an undivided one-half ownership interest in all of the community income. La. Civ. Code art. 2336.


24. Id.
the Internal Revenue Code affect the tax liability of separated spouses in Louisiana. Part II of this article discusses the effect of marital status on the amount of federal income tax that an individual must pay, explaining first the federal rules for determining marital status and then the effect of a taxpayer's marital status on (1) the rate of tax that the taxpayer must pay, (2) the amount of taxable income to which the tax rates apply, (3) the amount of tax credits a taxpayer may use to offset any tax liability for the year, and (4) the alternative minimum tax.

I. TAXATION OF COMMUNITY INCOME

A. Allocation of Liability for Paying the Federal Income Tax on Community Income

Louisiana is one of nine community property states.25 Spouses domiciled in Louisiana are subject to the community regime unless they contract otherwise.26 Under community property law, spouses share equally in the acquets and gains of either spouse during the marriage.27

The community property shared by the spouses in general consists of all property acquired by the spouses after the marriage except property acquired by an individual spouse by gift, devise, or descent, or by use of the proceeds of separate property.28 In Louisiana, community property


26. La. Civ. Code art. 2334-provides: "The legal regime of community of acquets and gains applies to spouses domiciled in this state, regardless of their domicile at the time of marriage or the place of celebration of the marriage.”

Spouses domiciled in Louisiana, however, may “opt out” of the community property regime by entering into a matrimonial agreement. La. Civ. Code art. 2329. If the spouses enter into an agreement that modifies or terminates the community property regime that existed during their marriage, they must obtain court approval. Id. Court approval is not necessary, however, if the spouses enter into an antenuptial agreement to live under a separate property regime. Id. Nor is court approval necessary if a couple enters into a matrimonial agreement within the first year of moving into and acquiring a domicile in Louisiana. Id.


28. In other words, community property consists of all property acquired during the existence of the community that is not separate property La. Civ. Code art. 2338. Separate
also includes the fruits and revenues derived from separate property unless the owner executes and records in the public records a declaration to reserve them as separate property. Thus, the community income of a couple domiciled in Louisiana includes the earnings of the husband, the earnings of the wife, income derived from community property, and income derived from separate property unless the owner has made an effective declaration.

Because each spouse is the owner of a "present undivided one-half interest" in the community income, each is liable for payment of the federal income tax on one-half of the community income, regardless of which spouse actually earned the income or controlled the property to which the income was attributable. This rule, established in Poe v. Seaborn, creates no problem if the spouses file a joint return. How-

property is defined as:

- property acquired by a spouse prior to the establishment of a community property regime;
- property acquired by a spouse with separate things or with separate and community things when the value of the community things is inconsequential in comparison with the value of the separate things used;
- property acquired by a spouse by inheritance or donation to him individually;
- damages awarded to a spouse in an action for breach of contract against the other spouse or for the loss sustained as a result of fraud or bad faith in the management of community property by the other spouse;
- damages or other indemnity awarded to a spouse in connection with the management of his separate property;
- things acquired by a spouse as a result of a voluntary partition of the community during the existence of a community property regime.


29. La. Civ. Code art. 2339. If property became separate because one spouse donated his or her interest in a community asset to the other spouse, however, the fruits and revenues are the separate property of the owner even without a declaration. La. Civ. Code art. 2343.


33. I.R.C. § 6013(a) (1988) permits most spouses, whether living under a community property regime or under a separate property regime, to file a joint return reporting their aggregate income, even if one of the spouses has neither gross income nor deductions. If the spouses file a joint return, each spouse is jointly and severally liable for any deficiency in tax for the year that the return is filed, I.R.C. § 6013(d)(3) (1988), unless one of the spouses qualifies as an "innocent spouse" under I.R.C. § 6013(e) (1988).
ever, if no return is filed, or if the spouses file separately, the Seaborn rule can impose significant burdens on the low income spouse, especially when the couple has separated.

As long as the community remains in existence, the low income spouse must report and pay federal income tax on one-half of the entire community income which, of course, includes the income earned by the other, high income spouse. The Seaborn rule imposes this liability upon the low income spouse even though the low income spouse may have been living separate and apart from the other spouse, has no control or enjoyment of the other spouse's income, and has no knowledge of the amount required to be reported on the income tax return.

Courts have been relentless in applying the Seaborn rule. The disparity in the amount of community income available to each of the spouses is irrelevant. For example, in Brent v. Commissioner, the United States Court of Appeals for the Fifth Circuit held that Mrs. Brent, a Louisiana domiciliary, was liable for the tax on one-half of her husband's $76,500 of income even though she had been living separately and apart from him for the entire year and had received a total of only $4,800 in alimony pendente lite from him. In Bagur v. Commissioner, it was irrelevant that Mrs. Bagur had no access to her husband's financial records.

In United States v. Mitchell, Mrs. Mitchell had renounced the community upon her divorce from her husband. Under former provisions


35. The rule can create a windfall for the high income spouse who has the beneficial enjoyment of income only one-half of which is taxable.


37. 630 F.2d 356 (5th Cir. 1980).

38. 603 F.2d at 495.

of the Louisiana Civil Code, a renunciation of the community caused a wife to lose entitlement to a distribution of community property or a property settlement upon divorce and at the same time exonerated the wife of any liability to pay community debts.\textsuperscript{40} The United States Supreme Court held that Mrs. Mitchell was liable for the tax on one-half of the community income earned during the existence of her marriage notwithstanding the fact that the tax liability for community income is a community debt, from which Mrs. Mitchell should have been absolved upon her renunciation of the community.\textsuperscript{41} The Supreme Court explained:

[The renunciation might be effective] in connection with a tax or other obligation the collection of which is controlled by state law. But an exempt status under state law does not bind the federal collector. Federal law governs what is exempt from federal levy.\textsuperscript{42}

\textbf{B. Judicial Remedy: The Theft Loss Deduction}

In \textit{Bagur v. Commissioner},\textsuperscript{43} the Fifth Circuit attempted to provide a remedy to mitigate the harsh results of the \textit{Seaborn} rule by permitting the low income spouse to claim a theft loss deduction under section 165(c)(3) of the Internal Revenue Code\textsuperscript{44} with respect to the portion of community income on which the spouse paid tax, without receiving any benefit. The availability of a theft loss deduction to the low income spouse, however, is speculative. To claim a theft loss deduction, the

\textsuperscript{40} La. Civ. Code art. 2410 (1870).
\textsuperscript{41} \textit{Mitchell}, 403 U.S., at 204, 91 S. Ct. at 1771.
\textsuperscript{42} Id.
\textsuperscript{43} 603 F.2d 491 (5th Cir. 1979), \textit{rem'g}, 66 T.C. 817 (1976). \textit{See also}, Brent \textit{v. Commissioner}, 630 F.2d 356 (5th Cir. 1980), \textit{rev'g and rem'g} 70 T.C. 775 (1978) (remanding the case of a Louisiana taxpayer who was liable for the tax on one-half of her husband's community income for development of facts to determine whether the taxpayer was entitled to a theft loss deduction).
\textsuperscript{44} I.R.C. § 165 (1988) provides in part:

\begin{quote}
Sec. 165 Losses.
(a) General rule.—
There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(c) Limitation on losses of individuals.—
In the case of an individual, the deduction under subsection (a) shall be limited to—

(3) ... losses of property not connected with a trade or business or a transaction entered into for profit, if such losses arise from ... theft.
\end{quote}
spouse must prove that there was a theft. The question of whether a theft has occurred is determined by reference to the criminal law of the jurisdiction where the loss occurred.

Louisiana law defines theft as:

The misappropriation or taking of anything of value which belongs to another, either without the consent of the other to the misappropriation or taking, or by means of fraudulent conduct, practices, or representations. An intent to deprive the other permanently of whatever may be the subject of the misappropriation or taking is essential.

It may be difficult for the low income spouse to prove that any disposition of community income by the spouse who earned it constitutes a theft. Under Louisiana community property law, either spouse "acting alone may manage, control, or dispose of community property unless otherwise provided by law." Concurrence of the other spouse is required only with respect to the "alienation, encumbrance, or lease of community immovables, furniture or furnishings while located in the family home, all or substantially all of the assets of a community enterprise and movables issued or registered as provided by law in the names of the spouses jointly," and with respect to a donation of community property unless a spouse makes "a usual or customary gift of a value commensurate with the economic position of the spouses at the time of the donation." Thus, a Louisiana spouse has broad powers of discretion in disposing of community income. It would be difficult to prove that a spouse, acting within the discretion authorized by law, either misappropriated any community income or intended to deprive the other of it permanently.

In Bagur the Fifth Circuit held that an intent to deprive a spouse of his or her share of the community income may be inferred from a spouse's "wanton appropriation of community assets in pursuit of his

45. The Internal Revenue Service has defined "theft" to include any "felonious taking of money or property by which a taxpayer sustains a loss, whether defined and punishable under the penal codes of the states as larceny, robbery, burglary, embezzlement, extortion, kidnapping for ransom, threats, or blackmail." Rev. Rul. 72-112, 1972-1 C.B. 60.


48. La. Civ. Code art. 2346. Professors Spaht and Hargrave explain that the law provides no mechanism to settle disputes between the spouses over particular transactions or uses of community; court intervention is available primarily to protect the interests of third parties. Spaht & Hargrave, supra note 25, at § 5.3.


own pleasure or needs." A question remains as to what facts are necessary to establish such a "wanton appropriation." In Bagur the Fifth Circuit remanded two consolidated cases to the Tax Court for development of facts to determine whether the husband in each case had appropriated his earnings to his own purposes in such a way as to be the equivalent of a theft of the wife's ownership of one-half of the earnings. There is no report of either of the consolidated cases on remand. In subsequent reported cases, however, no taxpayer has been able to prove the requisite intent to establish a theft loss for appropriation of community income.

In Connor v. Commissioner, the taxpayer's husband was a musician and songwriter who performed with the Kingston Trio. Mr. Connor's employment required him to travel away from home sometimes for months at a time. He left Mrs. Connor at home, intermittently sending her small amounts of money with which Mrs. Connor and her son "eked out a meager existence." When he was on the road, Mr. Connor lived lavishly, entertaining frequently and expensively, and occasionally sending money to some of his female friends. While Mrs. Connor was unable to qualify for a theft loss deduction for other reasons, the Tax Court opined that Mr. Connor's failure to divide the community income would not constitute the "wanton appropriation" of community income that constitutes the equivalent of theft under state law.

In all of the cases, including Connor, in which a theft loss deduction was disallowed, the taxpayer was living with her spouse during the taxable year or years in issue. Proving a theft loss when the spouses

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51. Bagur v. Commissioner, 603 F.2d 491, 502 (5th Cir. 1979).
52. Id., at 503. See also Brent v. Commissioner, 630 F.2d 356, 361 (5th Cir. 1980), rev'g and rem'g 70 T.C. 775 (1978) (remanding a similar case to the Tax Court for the development of facts to determine whether the wife was entitled to a theft loss deduction for her husband's appropriation of community income).
53. Nor is there a report of Brent, 630 F.2d 356, on remand.
55. 44 T.C.M. (CCH) 6 (1982).
56. Id., at 7.
57. A theft loss is deductible only in the year in which it is discovered. I.R.C. § 165(e) (1988). Because Mrs. Connor was unaware that her husband was earning more than twice the amount that he sent to her, she did not discover her loss until after her divorce. Mrs. Connor's post-divorce taxable years were not before the Tax Court. Therefore, the Tax Court did not have jurisdiction to allow Mrs. Connor an offsetting theft loss deduction. Connor, 44 T.C.M. (CCH), at 8 n.4.
58. Id.
reside together can be especially difficult because the low income spouse cannot establish that he or she did not share in the fruits of the high income spouse's earnings. In none of the reported cases did a spouse who was living separately and apart and who received no payments from the high income spouse claim a theft loss deduction.

One can only speculate as to the reason for the failure of such cases to appear in the reporters. Perhaps the Internal Revenue Service (the "Service") settles these cases by allowing the deduction. On the other hand, low income spouses may settle their cases by agreeing not to claim the deduction because the cost of litigating is too high. Low income spouses may not claim the deduction because they are unfamiliar with tax law and do not know that the deduction is available. Perhaps low income spouses do not claim a theft loss deduction because its benefits in reducing taxable income are limited.

A theft loss is deductible only in the taxable year in which the taxpayer discovers the loss. To claim a theft loss deduction, the low income spouse must prove the year in which the loss occurred and the amount of the loss. It is likely that a low income spouse who is living separately and apart from the high income spouse will not know the amount of community income of which he or she was deprived until there is a partition of the community. The year of partition then, will be the year of discovery. Even if the low income spouse discovers the loss in an earlier year, no theft loss deduction is allowed if the spouse has a claim for reimbursement with respect to which there is a reasonable prospect of recovery.

Thus, if the high income spouse has saved any of the community income, the low income spouse cannot claim a theft loss deduction for amounts that later may be received upon partition of the community. The deduction will be allowed only later if in fact

60. Lucia, 61 T.C.M. (CCH) at 1989; Schmidt, 41 T.C.M. (CCH) at 797; Hall, 40 T.C.M. (CCH) at 1351.
64. The community property regime is terminated "by the death or judgment of declaration of death of a spouse, declaration of the nullity of the marriage, judgment of divorce or separation of property, or matrimonial agreement that terminates the community." La. Civ. Code art. 2356. While a partition generally will occur after termination of the community property regime, La. Civ. Code art. 2336 permits spouses to partition community property "in whole or in part" during the existence of the community. On partition each spouse is entitled to a one-half share of the community assets net of community obligations. La. R.S. 9:2801 (1991). To the extent, however, that the high income spouse has spent community income on living and travel expenses or incurred community debts, there will be less community property to share on partition of the community. For a discussion of the types of expenses that are considered community obligations, see Spaht & Hargrave, supra note 25, at § 7.12.
the low income spouse does not recover his or her share of the community income upon which the low income spouse paid tax.

The amount that the low income spouse can deduct as a theft loss is also reduced by statutory limitations. The theft loss suffered by the spouse who is deprived of his or her share of community income is not incurred in a trade or business. Section 165(h)\(^65\) of the Internal Revenue Code reduces the deductible amount of such nonbusiness theft

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65. I.R.C. § 165(h) (1988) provides:

(h) Treatment of Casualty Gains and Losses.—

(1) $100 limitation per casualty.—Any loss of an individual described in subsection (c)(3) shall be allowed only to the extent that the amount of the loss to such individual arising from each casualty, or from each theft, exceeds $100.

(2) Net casualty loss allowed only to the extent it exceeds 10 percent of adjusted gross income.—

(A) In general.—If the personal casualty losses for any taxable year exceed the personal casualty gains for such taxable year, such losses shall be allowed for the taxable year only to the extent of the sum of—

(i) the amount of the personal casualty gains for the taxable year, plus

(ii) so much of such excess as exceeds 10 percent of the adjusted gross income of the individual.

(B) Special rule where personal casualty gains exceed personal casualty losses.—If the personal casualty gains for any taxable year exceed the personal casualty losses for such taxable year—

(i) all such gains shall be treated as gains from sales or exchanges of capital assets, and

(ii) all such losses shall be treated as losses from sales or exchanges of capital assets.

(3) Definitions of personal casualty gain and personal casualty loss.—For purposes of this subsection—

(A) Personal casualty gain.—The term "personal casualty gain" means the recognized gain from any involuntary conversion of property, which is described in subsection (c)(3) arising from fire, storm, shipwreck, or other casualty, or from theft.

(B) Personal casualty loss.—The term "personal casualty loss" means any loss described in subsection (c)(3). For purposes of paragraph (2), the amount of any personal casualty loss shall be determined after the application of paragraph (1).

(4) Special rules.—

(A) Personal casualty losses allowable in computing adjusted gross income to the extent of personal casualty gains.—In any case to which paragraph (2)(A) applies, the deduction for personal casualty losses for any taxable year shall be treated as a deduction allowable in computing adjusted gross income to the extent such losses do not exceed the personal casualty gains for the taxable year.

(B) Joint returns.—For purposes of this subsection, a husband and wife making a joint return for the taxable year shall be treated as 1 individual.

(C) Determination of adjusted gross income in case of estates and trusts.—
losses by requiring the spouse to subtract $100 from the amount claimed as a loss.\textsuperscript{66} After subtracting $100 from this amount, the spouse must then subtract ten percent of the spouse's adjusted gross income.\textsuperscript{67} A spouse's ability to take advantage of a theft loss deduction is further limited because a nonbusiness theft loss deduction is an itemized deduction.\textsuperscript{68} Spouses who might qualify for a theft loss deduction because they have been living separately and apart probably do not claim the deduction because a more certain remedy is available under Section 66 of the Internal Revenue Code.

C. Statutory Remedy: I.R.C. § 66

Recognizing the inequity of taxing a spouse on community income from which the spouse has received no benefit,\textsuperscript{69} Congress added section 66 to the Internal Revenue Code.\textsuperscript{70} While section 66 provides a better solution to the problems created by the Seaborn rule than an allowance of a theft loss deduction, it offers only limited relief to low income

For purposes of paragraph (2), the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that the deductions for costs paid or incurred in connection with the administration of the estate or trust shall be treated as allowable in arriving at adjusted gross income.

(D) Coordination with estate tax.—No loss described in subsection (c)(3) shall be allowed if, at the time of filing the return, such loss has been claimed for estate tax purposes in the estate tax return.

(E) Claim required to be filed in certain cases.—Any loss of an individual described in subsection (c)(3) to the extent covered by insurance shall be taken into account under this section only if the individual files a timely insurance claim with respect to such loss.


\textsuperscript{67} I.R.C. § 165(h)(2)(A)(ii) (1988). The spouse may deduct the theft loss in full if the spouse has sufficient casualty gains for the year. I.R.C. § 165(h)(4)(A) (1988) permits a taxpayer to deduct casualty and theft losses from gross income to the extent of the taxpayer's casualty gains. I.R.C. § 165(h)(2)(A)(ii) limits the deductibility of "net" casualty and theft losses, i.e. the amount of casualty and theft losses in excess of casualty gains. The discussion in the text assumes that the spouse has no casualty gains for the year.

\textsuperscript{68} See I.R.C. § 62(a) (1988) (omitting a nonbusiness theft loss deduction from the list of deductions that reduce gross income); I.R.C. § 67(b)(3) (1988) (listing the nonbusiness theft loss deduction allowed by I.R.C. § 165(c)(3) as an itemized deduction that is not considered a miscellaneous itemized deduction).

\textsuperscript{69} I.R.C. § 66 was "intended to provide relief for abandoned spouses who are presently taxed on a portion of the income earned by the other spouse but have received no benefit from that income." 126 Cong. Rec. 24810 (1980) (statement of Rep. Rostenkowski). See also S. Rep. No. 1036, 96th Cong., 2d Sess. 8 (1980), reprinted in 6 U.S.C.C.A.N. 7293, 7299 [hereinafter S. Rep. No. 1036].

spouses in community property states. A spouse who meets the stringent requirements of section 66 will be exempt from liability for the income tax on some, but not necessarily all, of the community income from which the spouse receives no benefit.

71. For a discussion of the shortcomings of I.R.C. § 66, see Filler, supra note 34, at 145-48; Kalinka, supra note 34, at 658-69; Miller, supra note 34, at 1115-21; Minick, supra note 34, at 59; Parks, supra note 34; Quick & DuCanto, supra note 34, at 82-87; Salchow, supra note 34; Vaughn, supra note 34.


SEC. 66. TREATMENT OF COMMUNITY INCOME.
(a) Treatment of community income where spouses live apart.—If-
(1) 2 individuals are married to each other at any time during a calendar year;
(2) such individuals-
   (A) live apart at all times during the calendar year, and
   (B) do not file a joint return under section 6013 with each other for a taxable year beginning or ending in the calendar year;
(3) one or both of such individuals have earned income for the calendar year which is community income; and
(4) no portion of such earned income is transferred (directly or indirectly) between such individuals before the close of the calendar year,
then for purposes of this title, any community income of such individuals for the calendar year shall be treated in accordance with the rules provided by section 879(a).
(b) Secretary may disregard community property laws where spouse not notified of community income.—The Secretary may disallow the benefits of any community property law to any taxpayer with respect to any income if such taxpayer acted as if solely entitled to such income and failed to notify the taxpayer's spouse before the due date (including extensions) for filing the return for the taxable year in which the income was derived of the nature and amount of such income.
(c) Spouse relieved of liability in certain other cases.— Under regulations prescribed by the Secretary, if-
(1) an individual does not file a joint return for any taxable year,
(2) such individual does not include in gross income for such taxable year an item of community income property includable therein which, in accordance with the rules contained in section 879(a), would be treated as the income of the other spouse,
(3) the individual establishes that he or she did not know of, and had no reason to know of, such item of community income, and
(4) taking into account all facts and circumstances, it is inequitable to include such item of community income in such individual's gross income,
then, for purposes of this title, such item of community income shall be included in the gross income of the other spouse (and not in the gross income of the individual).
(d) Definitions.—For purposes of this section—
(1) Earned income.—The term "earned income" has the meaning given to such term by section 911(d)(2).
(2) Community income.—The term "community income" means income which, under applicable community property laws, is treated as community income.
(3) Community property laws.—The term "community property laws" means the community property laws of a State, a foreign country, or a possession of the United States.
Subsections (a) and (c) of section 66 provide relief from the *Seaborn* rule under different circumstances.

A spouse will qualify for relief under Section 66(a) if: (1) the spouses live apart from each other for an entire calendar year;73 (2) the spouses do not file a joint return;74 (3) one or both of the spouses have earned income for the calendar year which is community income;75 and (4) no portion of the earned income is transferred (directly or indirectly) between the spouses before the close of the calendar year.76 If the requirements of section 66 are met, the community income is taxed in accordance with the rules set forth under section 879(a) of the Internal Revenue Code.77 Section 879(a) allocates the liability for tax as follows:

1. Earned income . . . , other than trade or business income and a partner's distributive share of partnership income, is treated as income of the spouse who rendered the personal services;78
2. Trade or business income and deductions are treated as the income and deductions of the spouse who exercises substantially all of the management and control of the business;79
3. A partner's distributive share of ordinary income or loss from a partnership is treated as the income or loss of the spouse who is the partner;80
4. Income from separate property is treated as the income of the spouse who owns the property;81 and
5. All other community income is treated as provided in the applicable community property law.82

Under these rules, the benefits of section 66(a) are not available to spouses who have lived together at any time during the taxable year. Even if the spouses live apart, the low income spouse will not qualify for relief under section 66(a) if there is any transfer between the spouses of earned community income, such as a spousal support payment or

75. I.R.C. § 66(a)(3) (1988). "Earned income" is defined as "wages, salaries, or professional fees, and other amounts received as compensation for personal services actually rendered and certain income derived from a trade or business in which both personal services and capital are material income-producing factors." I.R.C. §§ 66(d)(1), 911(d)(2) (1988 & Supp. 1991).
80. *Id*.
alimony pendente lite. Furthermore, section 66(a) does not exempt the low income spouse from liability for the tax on one-half of the community income derived from community property regardless of whether such income inures to the sole benefit of the other spouse.

Spouses who fail to meet the requirements of section 66(a) may qualify for relief under section 66(c). Section 66(c) applies, under regulations yet to be promulgated, if:

1. the spouse does not file a joint return;
2. the spouse does not include in gross income an item of community income that would be includable in the gross income of the other spouse under the rules of section 879(a) of the Internal Revenue Code;
3. the spouse establishes that he or she did not know of, and had no reason to know of, such item of community income;
4. taking into account all facts and circumstances, it is inequitable to include the item of community income in the spouse's gross income.

The utility of section 66(c) is circumscribed by the requirement that the spouse did not know of and had no reason to know of the omitted item of community income. In most of the reported cases, the taxpayer seeking relief under section 66(c) has been unable to prove lack of actual or constructive knowledge of significant amounts of community income. Lack of knowledge of the amount of community income earned by the other spouse is irrelevant. Only in cases where the taxpayer had no

83. It should be noted that de minimis transfers and payments for child support will not disqualify the spouse from relief under I.R.C. § 66(a). See supra note 76.

84. Louisiana community property law confers sole management over titled moveable property to the spouse whose name appears on the title. La. Civ. Code art. 2351. Thus, the spouse whose name appears on the community paycheck, stock, bonds, bank account, or patent may collect the earnings, capital gains, dividends, interest and royalties, deposit the income in a sole bank account, and enjoy the income to the exclusion of the other spouse.


89. See, e.g., Roberts v. Commissioner, 860 F.2d 1235 (5th Cir. 1988), aff'd 54 T.C.M. (CCH) 94 (1987) (I.R.C. § 66 did not relieve Texas wife of the tax on illegal kickback by husband because she knew that the husband was engaging in an income-producing activity; however, wife had no reason to know that the kickback was invested in certificates of deposit; therefore, I.R.C. § 66(c) applied to the wife's one-half share of the interest earned on the certificates of deposit); Dooley v. Commissioner, 63 T.C.M. (CCH) 1858 (1992) (Louisiana wife was aware that husband was earning commissions, therefore she was liable for the tax on one-half of the commissions); Lytle v. Commissioner, T.C.M. (P-H) 1992-
reason to know that his or her spouse was engaged in an income-producing activity has a taxpayer qualified for relief under section 66(c). 90

For example, in Roberts v. Commissioner, 91 Mrs. Roberts’ husband, a real estate broker, received an illegal kickback that was community income. While Mrs. Roberts had no actual knowledge of the existence

185 (1992) (Texas wife was aware that her husband’s business was producing income; therefore she did not meet requirement under I.R.C. § 66(c) that she have no actual or constructive knowledge of the income); McGee v. Commissioner, 62 T.C.M. (CCH) 976 (1991) (Texas wife was aware that her husband earned income from his dental practice, therefore no relief was available under I.R.C. § 66(c)); McPherson v. Commissioner, 62 T.C.M. (CCH) 1039 (1991) (although Idaho wife had no control over her husband’s business books nor access to its funds, she knew that her husband was receiving income from the business; therefore I.R.C. § 66(c) did not apply); Lucia v. Commissioner, 61 T.C.M. (CCH) 1982 (1991) (California wife held taxable on one-half of the community income from a business that she knew existed; however I.R.C. § 66(c) shielded her from liability for the tax on one-half of the community income from a business of whose existence she was not aware); Butler v. Commissioner, 61 T.C.M. (CCH) 1767 (1991) (California wife knew that estranged husband sold community property; therefore I.R.C. § 66(c) did not shield her from liability for the tax on one-half of the gain recognized on the sale); Thatcher v. Commissioner, 56 T.C.M. (CCH) 707 (1988) (California wife was aware that husband owned a dental technical business; therefore I.R.C. § 66(c) did not shield her from liability for tax on one-half of the community income from the business); Warner v. Commissioner, 53 T.C.M. (CCH) 703 (1987) (Texas husband knew that his wife was employed; therefore, I.R.C. § 66(c) did not apply with respect to the tax on one-half of her salary); Nelson v. Commissioner, 53 T.C.M. (CCH) 1448 (1987) (California wife participated in the operation of husband’s adult theater business and had too much knowledge of the business to qualify for relief under I.R.C. § 66(c)); Baldwin v. Commissioner, 52 T.C.M. (CCH) 22 (1986) (Texas wife held to have actual or constructive knowledge that her husband earned a salary; therefore, no relief was available to her under I.R.C. § 66(c)); Bozek v. Commissioner, 51 T.C.M. (CCH) 350 (1986) (California wife knew that her husband was earning real estate commissions; I.R.C. § 66(c) did not apply); Sanders v. Commissioner, 51 T.C.M. (CCH) 317 (1986) (Arizona wife was unable to obtain information from her husband with regard to the amount of his wages; nevertheless, because she knew that he was employed I.R.C. § 66(c) relief was not available to her); Rimple v. Commissioner, 49 T.C.M. (CCH) 1533 (1985) (Texas wife participated in husband’s businesses that generated community income; she had too much knowledge of the income to qualify for relief under I.R.C. § 66(c)).

90. See, e.g., Roberts, 860 F.2d 1235 (Texas wife held to have constructive knowledge of illegal kickback received by her husband; however, she had no reason to know that her husband would invest the illegal kickback in certificates of deposit; therefore, wife was not liable for the tax on one-half of the interest earned on the certificates of deposit); Lucia, 61 T.C.M. (CCH) 1982 (California wife not liable for the tax on one-half of the community income derived from her husband’s business where she had no reason to know that the business even existed); Costa v. Commissioner, 60 T.C.M. (CCH) 1178 (1990) (California wife did not know of and had no reason to know of her husband’s illegal drug trafficking business; therefore I.R.C. § 66(c) shielded her from liability for the tax on one-half of the income from that business); Hilton v. Commissioner, 60 T.C.M. (CCH) 217 (1990) (I.R.C. § 66(c) shielded Louisiana wife from liability for one-half of the tax on funds that husband embezzled from his employer and placed in an interest-bearing checking account because the wife did not know of and had no reason to know of the illegal activity or of the existence of the checking account).

91. 54 T.C.M. (CCH) 94 (1987), aff'd, 860 F.2d 1235 (5th Cir. 1988).
or the amount of the kickback, the Tax Court denied her relief from
liability for tax on one-half of the kickback under section 66(c), holding
that she had reason to know of the kickback.92 The Tax Court imputed
constructive knowledge of the kickback to Mrs. Roberts because she
knew that her husband was involved in real estate transactions during
the year and that such activities generated income.93

Mrs. Roberts' husband invested income from his real estate trans-
actions in four certificates of deposit. Because Mrs. Roberts had no
reason to know that the income had been invested or that the certificates
of deposit existed, section 66(c) shielded her from liability for the tax
on one-half of the interest income from the certificates of deposit.94

Even if a spouse could qualify for relief under section 66(c), the
spouse would still be liable for the tax on half the income derived from
community property. Section 66(c) applies only to items of income that
would be includable in the income of the other spouse under the rules
of section 879(a).95 Section 879(a) provides that income from community
property is treated as the income of the spouse who owns it under
applicable community property law.96 Under Louisiana community prop-
erty law, each spouse owns a one-half share of income derived from
community property, regardless of which spouse controls the property

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92. Roberts, 54 T.C.M. (CCH) at 97.
93. Id. The United States Court of Appeals for the Fifth Circuit affirmed the Tax
Court's opinion on this issue, explaining in addition that (1) Mrs. Roberts had noticed her
husband carrying large sums of cash, (2) her husband had deposited a portion of the
kickback in a joint checking account, (3) she enjoyed a comfortable and expensive life style,
and (4) one of her husband's business associates had warned her that he suspected her
husband of defrauding the investment group involved in the real estate transaction. Roberts,
860 F.2d, at 1239-40. Under the Fifth Circuit's analysis, a suspicions wife must report one-
half of her husband's suspected income even if she is not certain of the amount or the
existence of the income.
94. Roberts, 54 T.C.M. (CCH) at 97. Actually the Tax Court should not have permitted
Mrs. Roberts to exclude her one-half share of the income derived from the certificates of
deposit under I.R.C. § 66(c). Section 66(c) shields a spouse from liability for the tax on
one-half of an item of community income that would be includable in the income of the
other spouse under I.R.C. § 879(a). The interest earned on the certificates of deposit was
income derived from community property. See Tex. Fam. Code Ann. §§ 5.01(b) (defining
community property as property, other than separate property, acquired by either spouse
during the marriage), 501(a) (defining separate property as property owned or claimed by
a spouse before the marriage, property acquired by a spouse during the marriage by gift,
device, or descent, and the recovery by a spouse for certain personal injuries sustained
during the marriage). Under I.R.C. § 879(a)(4), income derived from community property
is treated as provided in the applicable community property law. In Texas, such income is
owned equally by the spouses. Hopkins v. Bacon, 282 U.S. 122, 51 S. Ct. 62 (1930);
Johnson v. Commissioner, 88 F.2d 952, 954-55 (8th Cir. 1937). Thus, Mrs. Roberts should
have been liable for the tax on one-half of the interest.
or has the beneficial enjoyment of the income from that property.97

Section 66(b) authorizes the Service to disallow the benefits of any community property law to any taxpayer who acted as if solely entitled to such income and failed to notify the taxpayer’s spouse of the nature and amount of such income before the due date for filing the return.98 This provision seems to offer greater relief than sections 66(a) or 66(c) because there is no requirement that the spouses live apart, there is no express requirement that the nonpossessory spouse prove lack of constructive knowledge of the item, and section 66(b) applies to all items of community income. Section 66(b) fails to provide adequate relief for the low income spouse, however, because it merely authorizes, but does not require, the Service to collect the tax from the high income spouse.99 Moreover, the high income spouse need only notify the low income spouse of the amount and nature of the item of income to avoid liability for the tax on it. If such notice is given, there is no requirement that the income be shared.

One commentator has suggested that section 66(b) imposes a heavy burden of proof on the low income spouse.100 If the spouses lived together, it is difficult to prove that the high income spouse acted as if solely entitled to the income.101 Even if the spouses are separated, the low income spouse could be held to have constructive notice of the other’s income in cases where the high income spouse has retained the same employment after the separation.102

The limited availability of relief under sections 66(b) and 66(c) assures that most spouses who do not qualify for relief under section 66(a) will be liable for the tax on one-half of the community income under the Seaborn rule.103 If the spouses live together104 at any time during the calendar year, if there is a transfer of earned community income between the spouses,105 or if the community income is derived from community

99. See, e.g., Rutledge v. Commissioner, T.C.M. (P-H) 1992-52 (1992) (explaining that I.R.C. § 66(b) is not a relief provision but rather permits the Service to disallow the benefits of community property law under the prescribed conditions).
100. Miller, supra note 34, at 1117.
101. Id.
102. Id.
103. If one of the spouses is a nonresident alien who does not elect to be taxed on worldwide income, however, the spouse who is a citizen or resident of the United States will be taxed on community income under the rules of I.R.C. § 879(a) (1988).
property,106 each spouse will be liable for the tax on one-half of the community income.

D. Avoiding the Harsh Effects of the Seaborn Rule Through Termination of the Community

The failure of the judicial and statutory remedies to provide adequate protection to the low income spouse from the harsh effects of the Seaborn rule requires the low income spouse to plan ahead. The ability to avoid the Seaborn rule through planning, however, is limited. A low income spouse cannot avoid liability for the tax on one-half of the other spouse's income by moving to a noncommunity property state if the income of the spouse domiciled in the community property state is community property under state law.107 Under Louisiana law, the income of a spouse domiciled in Louisiana is community property regardless of the domicile of the other spouse.108 This rule determines the character of the income for purposes of federal taxation as well.

In rare instances a low income spouse might be able to convince the high income spouse to agree to pay the tax on the higher income. Such an agreement, even if it is in writing and enforceable under local law, is not binding on the federal tax collector.109 If the high income spouse becomes insolvent or unavailable for service of process and fails to reimburse the low income spouse for payment of the tax, the low

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107. Commissioner v. Cavanagh, 125 F.2d 366 (9th Cir. 1942); Owens v. Commissioner, 26 T.C. 77 (1956); Hunt v. Commissioner, 22 T.C. 228 (1954); Dippel v. Commissioner, 14 T.C.M. (CCH) 232 (1955).
108. La. Civ. Code art. 3523. See also Fuori v. Fuori, 334 So. 2d 488 (La. App. 1st Cir. 1976) (where husband and wife had not contracted otherwise, all property acquired in Louisiana by husband became community property even though only the husband resided in Louisiana); Succession of Dill, 155 La. 47, 98 So. 752 (1923) (same); Succession of McKenna, 23 La. Ann. 369 (1871) (same).
109. Cf. Rude v. Commissioner, 48 T.C. 165, 175 (1967) (not-withstanding husband's agreement to pay his share of deficiencies in tax with respect to a joint return, the Service had an absolute right to collect the full amount entirely from the wife because she was jointly and severally liable for the full amount). See also United States v. Mitchell, 403 U.S. 190, 205, 91 S. Ct. 1763, 1771 (1971) (wife's renunciation of the community which under state law exonerated her of debts contracted during the marriage not binding on the federal tax collector with respect to her obligation to pay federal income tax on her one-half share of community income); Lawrence M. Phillips & Robert P. Stellick, Tax Reporting in the Year a Divorce Decree Is Granted, 6 Wis. J. Fam. L. 8, 9 (No. 1, 1986) (the Service takes the position that an agreement by divorcing spouses for each to declare and pay tax only on the community income earned by the spouse filing the return is not valid for federal income tax purposes, even if sanctioned by a state court with jurisdiction over the divorce action).
income spouse is not even entitled to claim a bad debt deduction.\textsuperscript{110}

The most certain method of avoiding the Seaborn rule is to terminate the community. In deciding whether to terminate the community, the low income spouse must, of course, weigh the current tax savings against the economic advantage of keeping the community alive and sharing a larger interest in community property on a later termination. Given the time value of money,\textsuperscript{111} a current tax savings often will be of greater benefit than waiting to receive a larger portion on a later termination. If the low income spouse loses income-producing assets or is forced to borrow money, incurring an interest liability in order to pay the tax, the economic burden is obvious. Even if the low income spouse is able to pay the tax on one-half of the community income, an investment of the tax savings that would be achieved by termination of the community could yield a higher return than the spouse would achieve by waiting for community assets to accumulate for receipt on a later termination.

Termination of the community also can shield a spouse from tax liabilities other than those arising under the Seaborn rule. As long as the community exists, the Service is authorized to garnish the wages of one spouse to pay any tax liability incurred by the other spouse either before or during the marriage.\textsuperscript{112} A lien for unpaid federal taxes, including interest, additions to tax, and any applicable penalties, attaches to "all property and rights to property . . . belonging to" the person liable for the taxes.\textsuperscript{113} State law determines the extent to which a taxpayer has an interest in property.\textsuperscript{114} Where state law makes all of the community property available to satisfy the debts of either spouse, courts have held that the federal government may look to the delinquent taxpayer’s entire property to satisfy his or her tax obligations.\textsuperscript{115}


\textsuperscript{111} The time value of money is an accounting concept that recognizes that a dollar of savings today is worth more than a dollar tomorrow. A spouse who pays less tax by preventing application of the Seaborn rule could invest the tax savings and possibly receive more on the investment than would be available on a later termination of the community. For a discussion of the time value of money concept, see Gary E. Clayton & Christopher Spivey, The Time Value of Money: Worked and Solved Problems (1978); John A. Biek, Note, Salvaging Accrual Method Deductions: Adding a "Time Value of Money" Component to the "All Events" Test, 40 Tax Law. 185, 188-90 (1986).

\textsuperscript{112} See, e.g., Medaris v. United States, 884 F.2d 832 (5th Cir. 1989).

\textsuperscript{113} I.R.C. § 6321 (Supp. 1991).


\textsuperscript{115} See, e.g., Medaris, 884 F.2d at 835; United States v. Stonehill, 702 F.2d 1288, 1298-99 (9th Cir. 1983); Babb v. Schmidt, 496 F.2d 957, 960 (9th Cir. 1974).
Under Louisiana law, "[a] separate or community obligation may be satisfied during the community property regime from community property. . . ." This rule permits the Service to seek satisfaction for both premarital tax liabilities and community tax liabilities incurred by one spouse from any community property, including community income earned by the other spouse. The spouse from whom property or wages were seized has a limited right under state law to sue for reimbursement from the other spouse after such a seizure.

Premarital tax liabilities are separate obligations under Louisiana law. If community property is used to satisfy a separate obligation of a spouse, the other spouse is entitled to reimbursement for one-half of the amount or value that the property had at the time it was used to satisfy the obligation. The right to reimbursement, however, can only be exercised upon termination of the community. If the spouse who incurred a premarital tax obligation is insolvent when the community is terminated, the spouse who paid the tax may not be able to collect even half of the amount that he or she paid.

A spouse who pays the tax liability on the other spouse's one-half share of the community income has no right to reimbursement for any amount that he or she paid unless the spouse satisfied the tax liability with separate property. The obligation to pay income tax on community income is a community obligation. When community income is used to pay a community obligation, there is no right to reimbursement,

116. La. Civ. Code art. 2345. A creditor also may seek satisfaction of the debt from the separate property of the spouse who incurred the obligation. Id. The creditor, however, is not required first to seek satisfaction from the incurring spouse's separate property. The only recourse of the nonincurring spouse is a right of reimbursement upon termination of the community for one-half of the amount or of the value of community property used to satisfy the separate obligation. La. Civ. Code art. 2364.

117. Under La. Civ. Code art. 2363, the term "separate obligation" is defined to include an obligation incurred by a spouse prior to the establishment of a community property regime.


119. Id.

120. The right to reimbursement is permitted against the spouse who incurred the separate obligation, not merely against the incurring spouse's share of community property. La. Civ. Code art. 2358. For a discussion of a spouse's right to reimbursement upon termination of the community, see Spah & Hargrave, supra note 25, at § 7.14.

121. See, e.g., Maginnis v. Maginnis, 580 So. 2d 709, 711 (La. App. 1st Cir. 1991) (husband's payment of community obligation for federal income tax with separate property entitled husband to reimbursement from his spouse for one-half of the tax liability). See also La. Civ. Code art. 2365 (if separate property of a spouse has been used to satisfy a community obligation, the spouse is entitled, on termination of the community, to reimbursement for one-half of the amount or value of the property).

regardless of which spouse earned the community income used to satisfy the obligation.

Termination of the community does not protect a spouse against seizure by the Service of former community assets to satisfy the other spouse's tax liabilities. Under Louisiana law, "[a]n obligation incurred by a spouse before or during the community property regime may be satisfied after termination of the regime from the property of the former community. . . ."123 Louisiana law also authorizes the Service, like any other creditor, to seize separate property of one spouse to satisfy a tax liability incurred by the other spouse to the extent of the value of any former community property that the nonincurring spouse has disposed of for purposes other than satisfaction of community obligations.124 A spouse whose former community property or separate property is seized to satisfy the other spouse's tax liability, however, may recover from the other spouse one-half of the value of the property seized if the tax liability was a community obligation and the entire value of the property seized if the tax liability was a separate obligation.125

If a tax liability is incurred because of an underpayment of tax with respect to a joint return, termination of the community does not protect either spouse from seizure of any assets, whether they are former community or separate assets. A spouse who signs a joint return is jointly and severally liable for the tax on the aggregate income of both spouses.126 A spouse whose property is seized in satisfaction of the community tax liability with respect to a joint return, however, is entitled on termination of the community to reimbursement from the other spouse for one-half of the value of the property that was seized.127

Thus, it could be advantageous for both spouses to terminate the community as soon as possible upon separation. Not only does termination of the community relieve a spouse of the liability for tax on one-half of the other spouse's post-termination earnings, but termination also reduces a spouse's exposure to tax liabilities incurred by the other spouse and entitles a spouse whose property is seized to reimbursement from the spouse who incurred the tax liability.

In Louisiana, the community property regime is terminated by the death of a spouse, the nullification of the marriage, a judgment of

123. La. Civ. Code art. 2357. A pre-termination creditor also may seek satisfaction of the debt from the separate property of the spouse who incurred the obligation. Id. There is no requirement, however, that the creditor first seek satisfaction from the incurring spouse's separate property.
124. Id.
125. Spaht & Hargrave, supra note 25, at § 7.10.
126. I.R.C. § 6013(d)(3) (1988). A limited exception to the joint and several liability incurred with respect to a joint return applies to a spouse who can satisfy the innocent spouse requirements of I.R.C. § 6013(e).
127. Spaht & Hargrave, supra note 25, at § 7.10.
divorce or separation of property, a matrimonial agreement that terminates the community, or the absence of a spouse.\textsuperscript{128} As long as both spouses are alive and can be located, the low income spouse for whom divorce or nullification is not an option must either enter into a court-approved marital agreement with the high income spouse to partition the community\textsuperscript{129} or obtain a judgment of separation of property\textsuperscript{130} in order to terminate the community.

In cases where application of the \textit{Seaborn} rule inflicts a hardship, the low income spouse should enter into a marital agreement to terminate and partition the community.\textsuperscript{131} Such an agreement, however, requires the concurrence of both spouses and a finding by the court that the agreement serves the spouses' best interests and that the spouses understand the governing principles and rules.\textsuperscript{132}

If the high income spouse is unwilling to sign a marital agreement, the low income spouse might sue for a judgment of separation of property. To obtain such a judgment, the low income spouse must show that the spouse's interest in community property is threatened to be diminished by the fraud, fault, neglect, or incompetence of the other spouse, or by the disordered affairs of the other spouse.\textsuperscript{133} There are no reported cases in which a spouse sought a judgment of separation

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\item \textsuperscript{128} La. Civ. Code art. 2356.
\item \textsuperscript{129} In Louisiana a couple can sign a prenuptial agreement to live under a separate property regime. La. Civ. Code art. 2329. If the couple wishes to opt out of a community property regime during the marriage, however, the spouses must obtain court approval of the agreement. \textit{Id.} Court approval is not required if the spouses have recently moved to Louisiana from another state and enter into a matrimonial agreement within one year of moving into and acquiring a domicile in Louisiana. \textit{Id.} When a community is partitioned under a marital agreement, the courts and the Internal Revenue Service generally will respect the agreement for federal income tax purposes. \textit{See, e.g.,} Clay v. United States, 161 F.2d 607 (5th Cir. 1947); I.R.S. Pub. No. 555, supra note 31. Community income that has been earned but not collected before the date of the agreement, however, is considered community income for purposes of federal taxation. \textit{See, e.g.,} Johnson v. United States, 135 F.2d 125 (9th Cir. 1943); Hubner v. Commissioner, 28 T.C. 1150 (1957).
\item \textsuperscript{130} La. Civ. Code art. 2374 authorizes a judgment of separation of property when the interest of a spouse in a community property regime is threatened by the fraud, fault, neglect, incompetence, disorder of the affairs of, or absence of the other spouse.
\item \textsuperscript{131} Professors Spaht and Hargrave warn that the marital agreement should state expressly that it terminates the community property regime; otherwise it could be interpreted as a modification of the legal regime. Spaht & Hargrave, \textit{supra} note 25, at § 7.8.
\item \textsuperscript{132} La. Civ. Code art. 2329. If the spouses have moved into Louisiana within one year of signing their agreement, court approval is not necessary. \textit{Id.}
\item \textsuperscript{133} La. Civ. Code art. 2374. The low income spouse also can obtain a judgment of separation of property if the other spouse is an absent person. \textit{Id.} An "absent person" is "one who has no representative in this state and whose whereabouts are not known and cannot be ascertained by diligent effort." La. Civ. Code art. 74. Unless the absent spouse has moved to a community property state, the low income spouse will not suffer under the \textit{Seaborn} rule.
\end{itemize}
of property to avoid the application of the Seaborn rule. A spouse seeking a judgment of separation of property should have no difficulty in establishing that the other spouse's refusal to partition the community threatens to diminish the petitioning spouse's interest in community property. Not only does the low income spouse incur a greater tax liability under the Seaborn rule on income that the high income spouse is likely to consume, but the time value of money often makes the value of a current tax savings to the low income spouse worth more than any increase in assets that may be available on a later termination of the community.\textsuperscript{134}

It is not certain, however, whether a spouse seeking to avoid application of the Seaborn rule by obtaining a judgment of separation of property can prove the requisite fraud, fault, neglect, incompetence, or disorder of the affairs of the other spouse merely by showing an increased current tax burden. A court could require a showing of the other spouse's extreme mismanagement of community assets to obtain a judgment of separation of property.\textsuperscript{135} A low income spouse seeking a judgment of separation of property, however, may be able to establish that the other spouse's refusal to partition the community imposes such a burden on the low income spouse that the refusal constitutes fault or neglect. Under Louisiana law, the term "fault" includes "very slight fault," a term that is defined as fault "which is excusable, and for which no responsibility is incurred."\textsuperscript{136}

A spouse need not prove one of the specified acts of fault or mismanagement to obtain a judgment of separation of property if a petition for divorce is filed. When such a petition is filed, either spouse may obtain a judgment of separation of property upon a showing that the spouses have lived separately and apart for thirty days from the date of the filing of the petition for divorce.\textsuperscript{137} This provision makes it easier for separated spouses to terminate the community. Separated spouses who do not seek a divorce, however, cannot obtain a judgment

\textsuperscript{134} For a discussion of the time value of money concept, see supra note 111 and accompanying text.

\textsuperscript{135} The reported cases in which a judgment of separation of property was issued have involved extreme mismanagement. For example, in Cooper v. Cooper, 509 So. 2d 616 (La. App. 3d Cir. 1987), the court held that a separation of property was appropriate where the wife's mismanagement involved her signing her husband's name on checks drawn from his personal checking account and on various notes and loans totaling $24,500 without his authorization or knowledge, writing 101 overdraft checks, and failing to file federal income tax returns for the community business, resulting in a tax deficiency of approximately $30,000.

In Mitchell v. Mitchell, 231 So. 2d 414 (La. App. 2d Cir. 1970), the court held that a wife was entitled to a judgment of separation of property where the numerous debts of her husband who was unable to obtain or hold a steady job threatened to deprive her of her meager earnings.

\textsuperscript{136} La. Civ. Code art. 3506(13).

\textsuperscript{137} La. Civ. Code art. 2374(C).
of separation of property without proving one of the statutory acts of fault or mismanagement.

Under former provisions of the Louisiana Civil Code, a judgment of separation from bed and board terminated the community. A spouse did not have to prove any wrongdoing, incompetence, or disorder in the affairs of the other spouse to obtain a judgment of separation from bed and board. While specified acts of wrongdoing could constitute grounds for a judgment of separation from bed and board, a spouse also could obtain such a judgment by showing that the spouses voluntarily had lived separately and apart for six months without reconciliation. A revival of these provisions could make it easier for separated spouses in Louisiana to terminate the community without having to file for divorce.

In many cases it is advantageous for the low income spouse to terminate the community as quickly as possible to avoid taxation under the Seaborn rule and to avoid liability for payment of the other spouse's income tax. Thus, the date of termination is crucial. Federal law often relies on state law for a determination of when the community is terminated.

For purposes of federal income taxation, the community terminates on the date prescribed by state law when termination results from a

139. A spouse could obtain a judgment of separation from bed and board upon a showing (1) of adultery by the other spouse, (2) of a conviction "of a felony and sentence to death or imprisonment at hard labor in a state or federal penitentiary," (3) of the "habitual intemperance . . . , excesses, cruel treatment, or outrages" of the other spouse that rendered the couple's living together insupportable, (4) of public defamation of the petitioning spouse by the other spouse, (5) of abandonment, (6) of an attempt of one of the spouses against the life of the other, (7) that the other spouse was a fugitive from justice, or (8) intentional non-support. La. Civ. Code art. 138(1)-(8) (1987). For a discussion of the former provisions of the Civil Code concerning grounds for a judgment of separation from bed and board, see Robert Anthony Pascal & Katherine Shaw Spaht, Louisiana Family Law Course 133-69 (3d ed. 1982).
140. La. Civ. Code art. 138(9) (1987). Spouses who lived separately and apart for only six months could obtain a judgment of separation from bed and board only if both spouses executed an affidavit attesting to the fact that they voluntarily had lived separately and apart for six months and that there existed irreconcilable differences between them such that their living together was insupportable and impossible. La. Civ. Code art. 138(10) (1987).
141. Of course, the Louisiana legislature could make it easier for separating spouses to terminate the community by permitting unilateral termination of the community upon a showing that the spouses had lived separately and apart for a period of time even if neither of the spouses files a petition for divorce. Perhaps the legislature has not enacted such a provision because it would prefer to see proof that the spouses intend to dissolve the marital bond before permitting a spouse unilaterally to terminate the community possibly to the detriment of the other spouse.
matrimonial agreement\textsuperscript{142} or a null marriage.\textsuperscript{143} The date of termination of the community under state law, however, will not always be respected for federal income tax purposes. In \textit{Brent v. Commissioner},\textsuperscript{144} the United States Court of Appeals for the Fifth Circuit held that a Louisiana wife was liable under the \textit{Seaborn} rule for the tax on one-half of her husband’s income earned during the entire 1970 calendar year despite the fact that under state law termination of the community was retroactive to March 26, 1970, the date the petition for divorce was filed. Louisiana law provides that a judgment of divorce terminates a community property regime retroactively to the date that the petition was filed.\textsuperscript{145} Thus, if a divorce is granted, the income of each spouse earned during the pendency of the suit is the separate property of each spouse. However, if the divorce action fails for any reason, the income earned by each

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\textsuperscript{142} See, e.g., Clay v. United States, 161 F.2d 607 (5th Cir. 1947) (prenuptial agreement of Louisiana couple effective to characterize all future earnings of each spouse as separate property for federal income tax purposes); Van Dyke v. Commissioner, 120 F.2d 945 (9th Cir. 1941) (earnings of each spouse after entering into separation of property agreement were separate property for federal income tax purposes); Helvering v. Hickman, 70 F.2d 985 (9th Cir. 1934) (same); Shoehair v. Commissioner, 45 B.T.A. 576 (1941) (same); I.R.S. Pub. No. 555, \textit{supra} note 34, at 2-3 (state law determines when a matrimonial agreement terminates the community for federal income tax purposes). In Louisiana termination of the community by matrimonial agreement is effective “as to immovable property, when filed for registry in the conveyance records of the parish in which the property is situated and as to movables when filed for registry in the parish or parishes in which the spouses are domiciled.” La. Civ. Code art. 2332.

\textsuperscript{143} I.R.S. Pub. No. 555, \textit{supra} note 31, at 2 (state law determines whether a community exists and/or when it terminates with respect to a null marriage). The effective date of termination of a community upon declaration of a nullity in Louisiana generally, but not always, is the date that the marriage is declared null. Louisiana recognizes two types of nullity: absolute nullity and relative nullity. A marriage is absolutely null if it is contracted without a marriage ceremony, with a party absent and represented by another person, or in violation of an impediment. La. Civ. Code arts. 94, 92. Such a marriage generally produces civil effects in favor of the party who is in good faith and only as long as the good faith lasts. La. Civ. Code art. 96; Evans v. Eureka Grand Lodge, 149 So. 2d 305 (La. App. 2d Cir. 1983). When the cause of an absolute nullity is one party’s prior undissolved marriage, however, the civil effects of the absolutely null marriage “continue in favor of the other party regardless of whether the latter remains in good faith, until the marriage is pronounced null or the latter party contracts a valid marriage.” La. Civ. Code art. 96. A marriage is relatively null in Louisiana if the consent of one of the parties was not freely given. La. Civ. Code art. 95. Such a marriage may be declared null upon application of the party whose consent was not free unless “that party confirmed the marriage after recovering his liberty or regaining his discernment.” Id. The civil effects of a relatively null marriage continue until a declaration of the nullity. See, e.g., State v. Loyacano, 135 La. 945, 66 So. 307 (1914); Delpit v. Young, 51 La. Ann. 923, 25 So. 547 (1899).

\textsuperscript{144} 630 F.2d 356 (5th Cir. 1980).

\textsuperscript{145} La. Civ. Code art. 159. During the year in issue in \textit{Brent}, former La. Civ. Code art. 155 (1870) also provided for retroactive termination of the community upon the rendering of a divorce decree.
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correspondingly, Mrs. Brent had a right to one-half of her husband's income until her right to that income was extinguished retroactively when the divorce became final on December 9, 1971.

The retroactivity of the termination of the community cannot be recognized for federal income tax purposes because the federal income tax system operates on an annual accounting basis. The annual accounting principle requires that an amount received under a claim of right must be reported as income in the year received even though it is determined in a later year that the taxpayer had no right to the amount and is required to repay it. The annual accounting principle is an integral part of our taxing system so that the amount of a taxpayer's income is "ascertainable and payable to the government, at regular intervals." The Fifth Circuit explained that Mrs. Brent had to report one-half of her husband's income even though she was not entitled to it because

[t]here is no practical way for the tax collector to know that a married person who files a tax return is party to a separation or divorce proceeding. Even if that fact were known, the levy of an assessment against the husband would be improper if the suit were dismissed or terminated without a decree favorable to the plaintiff. The Fifth Circuit suggested in dicta, however, that a remedy might be available to Mrs. Brent under section 1341 of the Internal Revenue Code. If a taxpayer, like Mrs. Brent, is required to repay an amount that was previously included in income under a claim of right, the taxpayer is entitled to deduct the amount in the year it is repaid. The allowance of a deduction in a later year, however, will not offset the tax liability incurred in the earlier year if the taxpayer, as is likely, was

146. If an action for divorce fails, the community remains in effect because termination is only retroactive once a judgment of divorce is rendered. La. Civ. Code art. 159. If one of the spouses has obtained a judgment of separation of property upon proof that the spouses have lived separately and apart for thirty days from the filing of the petition for divorce, termination of the community will remain in effect even if the divorce action fails unless the spouses reconcile and do not execute a matrimonial agreement terminating the community. La. Civ. Code art. 2375(B).
147. Brent, 630 F.2d at 359.
149. Burnet, 282 U.S. at 365, 51 S. Ct. at 152.
150. Brent, 630 F.2d at 360.
151. Brent, 630 F.2d at 360-61 & n. 8.
in a higher income bracket in the year of inclusion than in the year of
the deduction. To alleviate this problem, Congress enacted section
1341 of the Internal Revenue Code.

153. The federal income tax is a progressive tax, imposed at higher rates as taxable
income increases. Under the current rules, increments of an individual's income are taxed
at rates of fifteen percent, twenty-eight percent and thirty-one percent. I.R.C. § 1 (1988).
The additional amounts included in a taxpayer's income are likely to cause the income to
be placed in a higher tax bracket in the year of the inclusion. The deduction in the later
year will reduce taxable income, causing the taxpayer's income to fall into a lower bracket
in the year of the deduction.


155. I.R.C. § 1341 (1988) provides:

SEC. 1341. COMPUTATION OF TAX WHERE TAXPAYER RESTORES SUBSTANTIAL AMOUNT HELD UNDER CLAIM OF RIGHTS.

(a) General rule.—If:

(1) an item was included in gross income for a prior taxable year (or years)
because it appeared that the taxpayer had an unrestricted right to such item;
(2) a deduction is allowable for the taxable year because it was established
after the close of such prior taxable year (or years) that the taxpayer did not
have an unrestricted right to such item or to a portion of such item; and
(3) the amount of such deduction exceeds $3,000,

then the tax imposed by this chapter for the taxable year shall be the lesser of
the following:

(4) the tax for the taxable year computed with such deduction; or
(5) an amount equal to—;

(A) the tax for the taxable year computed without such deduction, minus;
(B) the decrease in tax under this chapter (or the corresponding provisions
of prior revenue laws) for the prior taxable year (or years) which would
result solely from the exclusion of such item (or portion thereof) from
gross income for such prior taxable year (or years).

For purposes of paragraph (5)(B), the corresponding provisions of the Internal Revenue
code of 1939 shall be chapter 1 of such code (other than subchapter E, relating to self-
employment income) and subchapter E of chapter 2 of such code.

(b) Special rules.—

(1) If the decrease in tax ascertained under subsection (a)(5)(B) exceeds the
tax imposed by this chapter for the taxable year (computed without the
deduction) such excess shall be considered to be a payment of tax on the last
day prescribed by law for the payment of tax for the taxable year, and shall
be refunded or credited in the same manner as if it were an overpayment for
such taxable year.

(2) Subsection (a) does not apply to any deduction allowable with respect to
an item which was included in gross income by reason of the sale or other
disposition of stock in trade of the taxpayer (or other property of a kind
which would properly have been included in the inventory of the taxpayer if
on hand at the close of the prior taxable year) or property held by the taxpayer
primarily for sale to customers in the ordinary course of his trade or business.
This paragraph shall not apply if the deduction arises out of refunds or
repayments with respect to rates made by a regulated public utility (as defined
in section 7701(a)(33) without regard to the limitation contained in the last
In cases where the amount repaid in the later year exceeds $3,000, a taxpayer who satisfies the requirements of section 1341 is permitted to deduct the amount of the repayment or claim a tax credit for tax paid on the amount included in the earlier year. The taxpayer must use the method of computing tax (deduction or credit) that results in the lesser tax liability. If the credit claimed in the year of repayment exceeds the tax liability for that year, the taxpayer is entitled to a refund.

While section 1341 does much to alleviate the burden of the claim of right doctrine, it does not compensate the taxpayer who is required to liquidate important assets in order to pay the tax liability for the year of inclusion. Nor does the provision take into account the time two sentences thereof if such refunds or repayments are required to be made by the Government, political subdivision, agency, or instrumentality referred to in such section, or by an order of a court, or are made in settlement of litigation or under threat or imminence of litigation.

(3) If the tax imposed by this chapter for the taxable year is the amount determined under subsection (a)(5), then the deduction referred to in subsection (a)(2) shall not be taken into account for any purpose of this subtitle other than this section.

(4) For purposes of determining whether paragraph (4) or paragraph (5) of subsection (a) applies—
(A) in any case where the deduction referred to in paragraph (4) of subsection (a) results in a net operating loss, such loss shall, for purposes of computing the tax for the taxable year under such paragraph (4), be carried back to the same extent and in the same manner as is provided under section 172; and
(B) in any case where the exclusion referred to in paragraph (5)(B) of subsection (a) results in a net operating loss or capital loss for the prior taxable year (or years), such loss shall, for purposes of computing the decrease in tax for the prior taxable year (or years) under such paragraph (5)(B), be carried back and carried over to the same extent and in the same manner as is provided under section 172 or section 1212, except that no carryover beyond the taxable year shall be taken into account.

(5) For purposes of this chapter, the net operating loss described in paragraph (4)(A) of this subsection, or the net operating loss or capital loss described in paragraph (4)(B) of this subsection, as the case may be, shall (after the application of paragraph (4) or (5)(B) of subsection (a) for the taxable year) be taken into account under section 172 or 1212 for taxable years after the taxable years to the same extent and in the same manner as—
(A) a net operating loss sustained for the taxable year, if paragraph (4) of subsection (a) applied, or
(B) a net operating loss or capital loss sustained for the prior taxable year (or years), if paragraph (5)(B) of subsection (a) applied.

value of money: section 1341 does not permit the taxpayer to collect interest with respect to the credit for taxes paid in the earlier year. Moreover, section 1341 relief will not be available to the unsophisticated taxpayer who does not know that the provision exists and does not claim its benefits for the year of repayment. Furthermore, it is not certain that a taxpayer who is required to pay tax on one-half of the community income during the pendency of a divorce can actually claim relief under section 1341 for the year in which the divorce is final.

The Service seems to take the position that section 1341 relief is not available to divorcing spouses in Louisiana. In Revenue Ruling 74-393, the Service ruled that the community does not terminate in Louisiana until the decree of divorce is rendered, notwithstanding retroactivity under state law. Louisiana law provides that "[t]he retroactive termination of the community shall be without prejudice to the rights of third parties. . . ." In Revenue Ruling 74-393, the Service interpreted this provision to mean that the community does not retroactively terminate with respect to the federal tax liability incurred during the pendency of the divorce. If each spouse is considered the actual owner of one-half of the community income earned during the pendency of the divorce, in accordance with the Service's position, the inclusion of income in the earlier year was proper, and there is no reason for the allowance of a deduction or a credit in a later year.

Disallowing a spouse any relief under section 1341 would establish a rule of administrative convenience. If one spouse is entitled to claim a deduction or credit for putative community income improperly included in the spouse's income, the other spouse should be required to include the same amount in income in the later year, either under a tax benefit theory or because the spouse's right to more than one-half of the

163. The tax benefit rule requires a taxpayer to include in income an item recovered during that taxable year that would not be includable in income except for the fact that the item produced a tax benefit in an earlier year. For example, taxpayers often deduct bad debts when they become worthless. I.R.C. § 166 (1988). If a debtor becomes solvent and repays a debt that the creditor deducted as worthless in a prior year, the creditor must include the amount of the repayment in income in the year that the debt is recovered. See, e.g., National Bank of Commerce of Seattle v. Commissioner, 115 F.2d 875 (9th Cir. 1940). The statutory provision concerning the tax benefit rule does not literally apply to items, like community income, that were omitted from income in earlier years. I.R.C. § 111 (1988) requires a taxpayer to include in income recovered amounts that were previously deducted
income vested in the later year. Adjustment would also be necessary for any alimony pendente lite payments. Alimony pendente lite generally is deductible by the payor and income to the payee. If alimony pendente lite is paid during the existence of the community, however, the payor may deduct and the payee must include in income only the amount by which the alimony pendente lite payments exceed one-half of the community income for the year. A later determination that the community retroactively terminated for tax purposes should allow the payor to deduct in the year that the divorce becomes final alimony pendente lite payments previously disallowed and require the payee to include in income such payments that previously were excluded. A rule establishing that the community terminates for tax purposes only when the divorce is final eliminates all of the adjustments that must be made under section 1341 and the tax benefit rule.

The different positions taken by the Fifth Circuit and the Service raise questions as to the reporting of community income and alimony pendente lite not only when a divorce becomes final in a later year but also when a divorce becomes final in the same year that the petition for the divorce was filed. In Louisiana, a spouse may obtain a decree of divorce after 180 days of filing the petition. Thus, in Louisiana, many divorces will be final within the same year in which the petition is filed. The Fifth Circuit's rationale in Brent seems to require that for federal tax purposes, the termination date of the community relates back to the date the petition was filed when the year of the filing and the year of the entry of the final decree of divorce coincide. While the claim of right doctrine requires a spouse to report putative community income earned during the time the suit for divorce is pending, a determination in the same year that neither spouse had a right to one- or credited to the extent that deduction or credit reduced the amount of tax that the taxpayer was required to pay in the earlier year. Courts, however, have applied tax benefit principles to require the inclusion in income of recovered amounts that were previously excluded from income. See, e.g., Keystone Nat'l Bank in Pittsburgh v. United States, 52 AFTR 1511 (W.D. Pa. 1957) (embezzled funds that had been omitted from income in the year of the embezzlement must be included in income in the year of the recovery under the tax benefit rule).

164. See, e.g., Alsop v. Commissioner, 290 F.2d 726 (2d Cir. 1961) (cash method rules required cash basis taxpayer to include in income embezzled amounts that were excluded from income in the year of the embezzlement).
167. Rev. Rul. 62-115, 1962-2 C.B. 23. Professor Miller raises a question with respect to the application of this rule when a spouse with both community income and separate income claims to make alimony pendente lite payments with separate funds. In such a case, the payor could argue that the payments are deductible by the payor and income to the payee, Miller, supra note 34, at 1102 n.96. Of course, tracing the funds used for the payments could be problematic.
half of the other's income should be effective for the year of the divorce. Excluding each spouse's share of the other's income when the year of the filing of the petition and the entry of the decree of divorce coincide does no violence to the annual accounting principle.

The Service's position, however, that the community does not terminate until the decree of divorce is entered,\textsuperscript{169} contradicts this interpretation. While the Fifth Circuit's opinion in \textit{Brent} is binding with respect to Louisiana taxpayers,\textsuperscript{170} the suggestion of a remedy under section 1341 is only dictum.\textsuperscript{171} It is not certain whether the Fifth Circuit actually would allow relief under section 1341. Because the Service's position would disallow application of section 1341, a taxpayer who cannot afford litigation probably will not be able to claim such relief.\textsuperscript{172} Because of the uncertainty, it would be better for a low income spouse to terminate the community by entering into a matrimonial agreement or obtaining a judgment of separation of property before the divorce is final, rather than to rely on any possible relief under section 1341. While Louisiana law permits the low income spouse to claim reimbursement from the other spouse for the tax paid on the income that belonged to the other spouse, terminating the community in a way that is effective for federal income tax purposes, could save the low income spouse the effort and expense required in seeking reimbursement after the divorce is final.

The retroactivity problem is not limited to termination of the community by divorce. In Louisiana, a judgment of separation of property


\textsuperscript{171} The litigation in \textit{Brent} concerned only Mrs. Brent's income for 1970, the year in which the petition for divorce was final. Thus, the Fifth Circuit did not have jurisdiction over the issue of whether Mrs. Brent was entitled to a deduction or a credit in 1971, the year in which the divorce became final.

\textsuperscript{172} No reported cases could be found in which a Louisiana divorcee claimed relief under I.R.C. § 1341. The Service's official position is that the community terminates when a final decree of divorce is issued, notwithstanding retroactivity under state law. Rev. Rul. 74-393, 1974-2 C.B. 28. In \textit{Brent}, however, the final decree of divorce was not entered until December 9, 1971. There was no issue in \textit{Brent} concerning any community income earned from January 1 until December 9, 1971. Under Rev. Rul. 74-393, half of that income should have been taxable to Mrs. Brent. One can only speculate as to the lack of an issue concerning Mrs. Brent's 1971 tax liability. Perhaps the Service overlooked the 1971 tax year until the statute of limitations had run. Perhaps the Brents had partitioned the community by January 1, 1971. It is possible, however, that the Service simply did not pursue the issue because the divorce decree entered before the end of the taxable year retroactively rendered all income earned by the spouses during 1971 as separate income. The lack of an issue concerning Mrs. Brent's 1971 income tax liability might be an indication that the Service in fact has accepted the Fifth Circuit's suggestion that relief is available under I.R.C. § 1341.
also terminates the community retroactively to the date that the petition for separation of property was filed.\(^{173}\) In cases where a petition is filed in one year and the judgment of separation of property is rendered in a later year, each spouse must report and pay tax on one-half of the community income until the judgment is final. Whether a spouse is entitled to claim relief under section 1341 of the Internal Revenue Code remains uncertain. Even when a judgment of separation of property is rendered in the same year that the petition is filed, the status of the community between the date of filing the petition and the date the judgment is entered also is uncertain.

A recently enacted provision of the Louisiana Civil Code permits either spouse to obtain a judgment of separation of property when a petition for divorce has been filed, upon a showing that the spouses have lived separate and apart for 30 days from the date of the filing of the petition for divorce.\(^{174}\) If such a judgment effectively terminates the community for federal income tax purposes, the expedited procedure for unilateral termination of the community could reduce the adverse impact of the retroactivity problem.

It is not certain, however, whether a 30-day judgment of separation of property will be effective in terminating the community for federal income tax purposes. Under Louisiana law a reconciliation of the spouses retroactively reestablishes the community if it has been terminated by a 30-day judgment of separation of property.\(^{175}\) On the date that such a judgment is final, it cannot be certain that the community is in fact terminated. Only when the divorce is final is the termination established. The Service may adopt a rule of administrative convenience, providing that a judgment of separation of property rendered upon a showing of a 30-day separation is ineffective in terminating the community for federal income tax purposes.

On the other hand, reestablishment of the community upon reconciliation after a 30-day judgment of separation of property is not effective as to third parties unless a notice of the reestablishment is filed in the public records.\(^{176}\) The Service and the federal courts may follow state law and find that the date that a 30-day judgment of separation of property is rendered is the date upon which the community terminates for federal tax purposes. Until the Service or a court rules on the issue, the answer remains uncertain.

\(^{175}\) La. Civ. Code art. 2375(B).
\(^{176}\) Id.
E. Amending State Law to Mitigate the Harsh Effects of the Seaborn Rule

The Seaborn rule imposes an onerous burden on low income spouses in community property states. Commentators have called upon Congress to override the rule. Unless and until Congress acts, however, the Louisiana Legislature should try to help protect its domiciliaries against the adverse impact of the Seaborn rule.

Low income spouses in Louisiana can protect themselves by entering into a matrimonial agreement to partition the community or by petitioning for a judgment of separation of property. Either remedy, however, may be difficult to obtain. A matrimonial agreement requires the concurrence of both spouses and judicial approval. Separating spouses may not be able to cooperate well enough to concur in a matrimonial agreement. Furthermore, it is uncertain whether a spouse could obtain a judgment of separation of property if the only grounds for the petition were the obligation to pay federal income tax on one-half of the community income. Moreover, spouses who either do not understand their rights under the community property system or are unaware of the federal rules for taxation of community income often do not appreciate the need to terminate the community to avoid application of the Seaborn rule.

Spouses who divorce escape the burdens of the Seaborn rule because the community necessarily terminates for tax purposes, at least by the time the divorce decree is entered. No such automatic termination is available, of course, for spouses who wish to live separate and apart without obtaining a divorce. Such spouses will continue to be liable for one-half of the community income unless they enter into a matrimonial agreement, obtain a judgment of separation of property, or qualify for relief under the stringent requirements of section 66 of the Internal Revenue Code.

Louisiana could help some of these taxpayers by enacting a provision authorizing a suit for separation from bed and board which would terminate the community. Such a provision would make it easier for separated spouses to terminate the community. Spouses who do not

177. See, e.g., Richard C.E. Beck, Joint Return Liability and Poe v. Seaborn Should Both Be Repealed, Tax Notes 457, 464-67 (Oct. 22, 1990); Gann, supra note 13; Kalinka, supra note 34; Miller, supra note 34.
178. La. Civ. Code art. 2329. If the spouses have moved into Louisiana within one year before signing their agreement, court approval is not necessary. Id.
179. For a discussion of the problem in seeking a judgment of separation of property to avoid application of the Seaborn rule, see supra notes 133-137 and accompanying text.
desire to divorce and do not understand that it would be beneficial for them to partition the community to avoid application of the *Seaborn* rule might nevertheless seek a legal separation, thereby terminating the community.

Under former law, a judgment of separation from bed and board, like a divorce or suit for separation of property, terminated the community retroactively to the date of filing the petition. The retroactive termination of the community in the context of a separation from bed and board creates the same problem for the low income spouse as it does in the context of a divorce or a suit for separation of property.

To eliminate the retroactivity problem, the Louisiana Legislature could enact legislation providing that the community terminates upon the filing of a petition for separation from bed and board, divorce, or separation of property. Such a rule would protect the low income spouse from the adverse effects of the *Seaborn* rule. Such a rule, however, would create inequities because a spouse could terminate the community unilaterally, merely by filing a petition, thereby depriving the other spouse of the benefits of community property law.

Another solution to the federal tax problem would be to enact a provision that the community terminates upon the entry of a decree of separation from bed and board, a decree of divorce, or a judgment of separation of property. This rule would coincide with the rule for federal taxation, thereby at least giving the low income spouse an interest in and possible chance of recovering the income on which the spouse paid tax. This rule, however, creates too much potential for abuse. As long as the community remains in existence, each spouse can contract debts, diminishing the amount of community property that will be available to the other spouse upon later termination.


182. La. Civ. Code art. 2345 provides: "A separate or community obligation may be satisfied during the community property regime from community property and from the separate property of the spouse who incurred the obligation."

After termination of the community, pre-termination creditors can seize former community assets from either spouse in satisfaction of such debts. La. Civ. Code art. 2357. The creditor, of course, must be able to identify the property as former community property or risk an action for wrongful seizure. Spaht & Hargrave, supra note 25, at § 7.10. In cases where the creditor seizes former community property from the non-debtor spouse, the non-debtor may be able to recover reimbursement from the debtor spouse. For a discussion of the rights of the non-debtor spouse against the debtor spouse in such a case, see id.

Nevertheless, a community obligation could consume the entire community. A non-contracting spouse has no right to reimbursement when community obligations are satisfied with community property. For a discussion of the rights of the spouses to reimbursement upon termination of the community, see id., at §§ 7.13-7.18.

A community obligation is one "incurred by a spouse during the existence of a community property regime for the common interest of the spouses or for the interest of
While there may be no solution to the retroactivity problem, permitting a spouse to obtain a separation from bed and board could protect some Louisiana taxpayers who are unable to enter into a matrimonial agreement terminating the community, who are unable to obtain a judgment of separation of property, or who are unaware that they are liable for the tax on one-half of the community income earned during the existence of the community. The case for enacting a provision authorizing legal separation, however, is much stronger upon consideration of the effect of a legal separation on the operation of the marriage penalty provisions of the Internal Revenue Code.

II. MARITAL STATUS AND THE INTERNAL REVENUE CODE: THE CASE FOR LEGAL SEPARATION

A taxpayer’s marital status has a major impact on the amount of federal income tax that is due. Not only do the tax rates on the same amount of taxable income differ depending on a taxpayer's marital status, but marital status also affects a taxpayer's ability to take advantage of many deductions and credits. Attribution rules that apply to married taxpayers can affect tax liability as well. While it is sometimes advantageous for a taxpayer to be married for purposes of federal income taxation, in many cases a married taxpayer incurs a substantially higher tax burden than one who is not married. In repealing the provisions authorizing a judgment of separation from bed and board, Louisiana has made it more difficult for separated spouses to qualify as unmarried for federal income tax purposes. Thus, a significant class of Louisiana domiciliaries incurs a higher federal income tax burden than would be necessary if the state authorized legal separation. The burden often falls upon spouses at a time when they are straining under the economic hardship of establishing separate households. In some cases, the absence of a provision authorizing legal separation in Louisiana adds uncertainty as to the federal tax status of Louisiana taxpayers.

A. Determination of a Taxpayer's Marital Status for Purposes of Federal Income Taxation

Because the application of so many provisions of the Internal Revenue Code depends on a taxpayer’s marital status, it is essential to know

the other spouse . . . ." La. Civ. Code art. 2360. Upon careful analysis of the jurisprudence, Professors Spaht and Hargrave have compiled a list of community obligations that includes, inter alia, obligations relating to a business conducted by one or both of the spouses and obligations incurred for family goods and household or living expenses. Spaht & Hargrave, supra note 25, at § 7.12. Under these rules a spouse could easily incur debts that would diminish the other spouse's share of community property upon termination.
whether a taxpayer is married or not.\(^\text{183}\) Section 7703 of the Internal Revenue Code provides the general rules for determining marital status.\(^\text{184}\) For federal income tax purposes, the determination of whether an individual is married generally is made as of the close of the taxable year.\(^\text{185}\) Tax law generally looks to state law for a determination as to marital status.\(^\text{186}\) There are two statutory exceptions to this rule. First,


\[^{184}\text{Each provision of the Internal Revenue Code whose operation varies depending on the taxpayer's marital status has its own definition of marital status. Many such provisions, however, define marital status by referring to I.R.C. § 7703. See, e.g., I.R.C. §§ 1(a), (c), (d); 2(c); 22(e)(2); 32(d); 55(d); 63(g); 68(b)(1); 86(c)(3)(A); 135(d)(3); 151(d) (1988 & Supp. 1991). In general, then, the rules of I.R.C. § 7703 apply in determining a taxpayer's marital status.}\]

\[^{185}\text{I.R.C. § 7703(a)(1) (1988). If a taxpayer's spouse dies before the end of the taxable year, however, the taxpayer's marital status will be determined at the time of the death. Id. In other words, a surviving spouse is considered married for federal income tax purposes.}\]

\[^{186}\text{See, e.g., Gersten v. Commissioner, 267 F.2d 195 (9th Cir. 1959); Commissioner v. Eccles, 208 F.2d 796 (4th Cir. 1953), aff'd 19 T.C. 1049 (1953); Dunn v. Commissioner, 70 T.C. 361 (1978); Capodanno v. Commissioner, 69 T.C. 638 (1978), aff'd, 602 F.2d 64 (3d Cir. 1979); Lee v. Commissioner, 64 T.C. 552 (1975), aff'd, 550 F.2d 1201 (9th Cir. 1977); Untermann v. Commissioner, 38 T.C. 93 (1962). See also Morgan v. Commissioner, 309 U.S. 78, 60 S. Ct. 424 (1940) ("State law creates legal interests and rights. The federal revenue acts designate what interests or rights, so created, shall be taxed"). But see Estate of Steffke v. Commissioner, 538 F.2d 730, 732 (7th Cir. 1976) ("[t]he meaning of the words or the legal status of circumstances for federal tax purposes need not be identical to their meaning or their legal effect under state law").}\]

A person who was never married generally is not married for federal income tax purposes. The federal tax rules, however, recognize common law marriages if such a marriage is invalid under the law of the state of the domiciliary. Von Tersch v. Commissioner, 47 T.C. 415 (1967); Rev. Rul. 58-66, 1958-1 C.B. 60. An individual who receives a decree of annulment was never married for state law purposes. The Service takes the position that such a person must file amended returns claiming unmarried status for all taxable years affected by the annulment that are not closed by the statute of limitations. Rev. Rul. 76-255, 1976-2 C.B. 40; I.R.S. Pub. No. 504, Tax Information for Divorced or Separated Individuals 1 (1991). If, however, there is no decree of annulment, the putative marriage, whether absolutely null or relatively null, will be recognized for federal income tax purposes. See, e.g., Newburger v. Commissioner, 61 T.C. 457 (1974); Reisman v. Commissioner, 49 T.C. 570 (1968).

An individual who obtains a decree of divorce is considered not married as of the date of the decree. I.R.C. § 7703(a)(2) (1988). If, however, a couple obtains a divorce for tax avoidance purposes and contemplates remarriage, the Service treats the divorce as a sham. Rev. Rul. 76-255, 1976-2 C.B. 40; I.R.S. Pub. No. 504, supra, at 1. Courts have also disregarded such divorces. See, e.g., Boyter v. Commissioner, 74 T.C. 989 (1980), aff'd, 668 F.2d 1382 (4th Cir. 1981). If taxpayers divorce and continue to live together without
an individual who is "legally separated from his spouse under a decree of divorce or of separate maintenance" is considered not married for federal income tax purposes.\textsuperscript{187} The second exception is the so-called "abandoned spouse" rule. Under the abandoned spouse rule, a taxpayer is not considered married if: (1) the taxpayer maintains as his or her home a household that constitutes for more than one-half of the taxable year the principal place of abode of the taxpayer's dependent

remarrying, however, the Service and the courts generally treat the divorce as valid. See, \textit{e.g.}, \textit{Boykin v. Commissioner}, 48 T.C.M. (CCH) 267 (1984); \textit{Priv. Ltr. Rul. 78-350-76} (June 1, 1978).

The courts are split with respect to the effect of a foreign divorce that is later declared invalid by the domiciliary state. The Tax Court and the Ninth Circuit have held that such a divorce decree is also invalid for purposes of determining a taxpayer's filing status. See, \textit{e.g.}, \textit{Lee, 64 T.C. 552}; \textit{Estate of Buckley v. Commissioner}, 37 T.C. 664 (1962), \textit{acq.}, 1964-2 C.B. 4. The Second Circuit, however, applies a "rule of validation" which validates a current marriage for income tax purposes by giving conclusive effect to a foreign divorce decree even after it is adjudicated a nullity by a state court with jurisdiction over the parties. See, \textit{e.g.}, \textit{Estate of Borax v. Commissioner}, 349 F.2d 666 (2d Cir. 1965); \textit{Wondsel v. United States}, 350 F.2d 339 (2d Cir. 1965), \textit{cert. denied}, 383 U.S. 935, 86 S. Ct. 1064 (1966), \textit{rev. in part} 23 T.C.M. (CCH) 1278 (1964). The Second Circuit has also applied the rule of validation in cases involving the determination of whether an individual is a surviving spouse for purposes of the federal estate tax unless a court of the state where the decedent's estate was administered has ruled the prior divorce invalid. \textit{Compare} \textit{Estate of Spalding v. Commissioner}, 537 F.2d 666 (2d Cir. 1976) (New York Supreme Court declared \textit{ex parte} Nevada divorce invalid, but decedent's estate was administered in California; held, second marriage was valid for purposes of the federal estate tax) \textit{with} \textit{Estate of Coldwater v. Commissioner}, 539 F.2d 878 (2d Cir. 1976) (New York court administering the decedent's estate declared \textit{ex parte} Mexican divorce invalid; held, decedent's first wife, rather than his second wife, was the surviving spouse for purposes of the federal estate tax). See also \textit{Estate of Steffke}, 538 F.2d at 735 (the decision of the state court that has primary jurisdiction over the administration of the decedent's estate determines whether an individual is a surviving spouse for federal estate tax purposes). For purposes of determining whether a spouse is entitled to claim an alimony deduction, the Third Circuit and Tax Court have validated marriages despite an adjudication that they were null. See, \textit{e.g.}, \textit{Feinberg v. Commissioner}, 198 F.2d 260 (3d Cir. 1952); \textit{Newburger v. Commissioner}, 61 T.C. 457 (1974). For a discussion of the application of state law to determine marital status for purposes of federal taxation, see Daniel J. Lathrope, \textit{State-Defined Marital Status: Its Future as an Operative Tax Factor}, 17 U.C. Davis L. Rev. 257 (1983); Case Comment, \textit{State Domestic Relations Law and Federal Tax Policy}, 66 Colum. L. Rev. 150, 151 (1966); \textit{Note, The Haitian Vacation: The Applicability of Sham Doctrine to Year-End Divorces}, 77 Mich. L. Rev. 1332, 1339-44 (1979). For a defense of the rule of validation, see Noreen A. Shugrue, \textit{Note, Divorce, Conflict of Laws, and the IRS—The "Rule of Validation" As a Solution to Matrimonial Tax Difficulties}: \textit{Estate of Spalding v. Commissioner}, 537 F.2d 666 (2d Cir. 1976), 9 Conn. L. Rev. 282 (1977).


\textsuperscript{188} A spouse need not actually be deserted to qualify; I.R.C. § 7703(b)(3) requires only that the taxpayer live apart from his or her spouse during the last six months of the taxable year to qualify as an abandoned spouse.
child;\textsuperscript{189} (2) the taxpayer furnishes over one-half of the cost of maintaining the household during the taxable year;\textsuperscript{190} and (3) during the last six months of the taxable year, the taxpayer's spouse is not a member of the taxpayer's household.\textsuperscript{191}

In repealing the provisions for legal separation, the Louisiana Legislature has made it more difficult for its domiciliaries to be considered not married for federal income tax purposes. In cases where there is no decree requiring spousal support, Louisiana taxpayers who separate from their spouses but do not wish to obtain a divorce and individuals whose divorce decrees are still pending as of December 31 are considered married unless they qualify under the abandoned spouse rule. Childless couples and noncustodial parents who fail to meet the requirement that a taxpayer have a dependent child under the abandoned spouse rule, are considered married. If the community has not terminated, it is impossible even for a custodial parent to qualify as not married because the abandoned spouse rule requires the parent to furnish over one-half the cost of maintaining the household. To the extent that the parent uses community funds to pay the household expenses, the parent furnishes only one-half of the cost.\textsuperscript{192}

Before the repeal of the provisions for separation from bed and board, Louisiana taxpayers could easily qualify as not married for federal income tax purposes. Spouses who were separated under the former provisions authorizing judgments of separation from bed and board\textsuperscript{193} were considered legally separated under a decree of divorce, and therefore not married for federal income tax purposes.\textsuperscript{194}

The status of separated spouses in Louisiana is less certain when a court decree requires one of the spouses to make support payments to

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\textsuperscript{189} I.R.C. § 7703(b)(1) (1988). The child will qualify if the taxpayer would have been entitled to claim the dependency exemption but for the fact that the taxpayer permitted the other spouse to claim the deduction pursuant to the rules of I.R.C. § 152(e)(2) or (4). \textsuperscript{id}
\end{flushright}

\begin{flushright}
\textsuperscript{190} I.R.C. § 7703(b)(2) (1988).
\end{flushright}

\begin{flushright}
\textsuperscript{191} I.R.C. § 7703(b)(3) (1988).
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\textsuperscript{192} Cf. Abrams v. Commissioner, 57 T.C.M. (CCH) 1433, 1436 (1989) (during the existence of the community the total support of the household and the children is allocable evenly to both parents for purposes of determining whether one of the parents has satisfied the requirement for qualifying as a head of household that the taxpayer furnish over one-half of cost of maintaining a household); Tech. Adv. Mem. 77-40-006 (June 26, 1977) (married taxpayer living under a community property regime did not qualify for head-of-household status; absent proof that the taxpayer used separate funds, taxpayer could establish only that he furnished one-half, rather than over one-half of the cost of maintaining his household).
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\textsuperscript{193} La. Civ. Code arts. 140, 143, 152-153 (1825); 141-142, 144-151, 154-158 (1870).
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\textsuperscript{194} Garsaud v. Commissioner, 28 T.C. 1086 (1957).
\end{flushright}
the other spouse. A taxpayer is considered not married for federal tax purposes if the taxpayer is legally separated from his or her spouse under a decree of separate maintenance.\textsuperscript{195} If a decree orders spousal support, the parties must be legally separated to be considered unmarried for federal tax purposes.\textsuperscript{196} Spouses who are separated under a written separation agreement, even one requiring support payments, are considered married because there has been no court decree,\textsuperscript{197} unless one or both qualifies as unmarried under the abandoned spouse rule. A judgment of separation of property will not satisfy the legal separation requirement.\textsuperscript{198} Nor will a decree requiring a spouse to pay alimony pendente lite satisfy the requirement.\textsuperscript{199} To constitute a legal separation, the court order must alter the marital status of the parties.\textsuperscript{200} Neither a judgment for separation of property nor an interlocutory decree ordering payment of alimony pendente lite will accomplish this result. Thus, in Louisiana where a spouse cannot obtain a judgment of separation from bed and board, a spouse who is separated, but not divorced, in most cases is married for federal tax purposes, regardless of whether one of the spouses is making support payments, unless the abandoned spouse rule applies.

In cases where one of the spouses is making support payments under a decree entered pursuant to section 9:291 of the Louisiana Revised Statutes, however, the marital status of Louisiana spouses is uncertain.\textsuperscript{201} Courts do not seem to agree as to whether a decree ordering a spouse

\begin{footnotes}
\item[196] See, e.g., Frazier v. Commissioner, 638 F.2d 63 (8th Cir. 1981), aff’d T.C.M. (P-H) 1979-515 (1979); Capodanno v. Commissioner, 602 F.2d 64 (3rd Cir. 1979); Hulick v. Commissioner, 357 F.2d 329 (2d Cir. 1966); Dunn v. Commissioner, 70 T.C. 361 (1978); Palmquist v. Commissioner, 284 F. Supp. 577 (N.D. Cal. 1967); Rafal v. United States, 267 F. Supp. 61 (D. Del. 1967).
\item[197] See, e.g., Smith v. Commissioner, 168 F.2d 446 (2d Cir. 1948); Donigan v. Commissioner, 68 T.C. 632 (1977).
\item[198] Cash v. Commissioner, 580 F.2d 152, 154 (5th Cir. 1978).
\item[200] Boyer v. Commissioner, 732 F.2d 191, 194 (D.C. Cir. 1984); Capodanno v. Commissioner, 602 F.2d 64, 67 (3d Cir. 1979); Seaman v. Commissioner, 479 F.2d 336, 338 (9th Cir. 1973); Legget v. Commissioner, 329 F.2d 509 (2d Cir. 1964), rev’g 39 T.C. 1022 (1963); Boettiger v. Commissioner, 31 T.C. 477, 483 (1958), acq. 1959-1 C.B. 3.
\item[201] La. R.S. 9:291 (1991) provides:

Spouses may not sue each other except for causes of action pertaining to contracts or arising out of the provisions of Book III, Title VI of the Civil Code; for restitution of separate property; for divorce or declaration of nullity of the marriage; and for causes of action pertaining to spousal support or the support or custody of a child while the spouses are living separate and apart.
\end{footnotes}
to make support payments and to live separately and apart causes the couple to be "legally separated" within the meaning of section 7703 of the Internal Revenue Code.

In *Legget v. Commissioner*, the taxpayer's wife had obtained a decree under former section 65.09 of the Florida Statutes ordering him to pay alimony unconnected with divorce. The couple had been living separately and apart. Florida, like Louisiana, has no statute authorizing a legal separation or separation from bed and board. Section 65.09 of the Florida Statutes authorized a wife to obtain alimony without seeking divorce if she had grounds for divorcing her husband and lived separate and apart from him. Such a decree had the effect of releasing the wife from the control of her husband.

The issue in *Legget* concerned the deductibility of the alimony payments. At the time of the decision, alimony was not deductible by the husband unless the couple was "legally separated." The Second Circuit distinguished a line of cases denying the deduction to taxpayers making separate maintenance payments in jurisdictions whose laws also make specific provision for legal separation and held that the payments at issue were deductible because former section 65.09 of the Florida Statutes...
was in substance "a legal separation although not baptized as such." In reaching its decision, the Second Circuit relied on opinions of the Florida Supreme Court explaining that the right to relief authorized by former section 65.09 was "in the nature of a limited divorce," like a divorce a mensa et thoro.

It is not certain whether a federal tax court would hold that section 9:291 of the Louisiana Revised Statutes constitutes "a legal separation, although not baptized as such." Section 9:291 enforces the obligation of married persons to support each other under article 98 of the Louisiana Civil Code. The obligation of spousal support arises from the marital relation and ceases upon divorce. Thus, it appears that a decree pursuant to section 9:241 requiring spousal support does not alter the marital status of the parties in order to effect a legal separation for federal income tax purposes. Under prior Louisiana law a judgment of separation from bed and board did not extinguish a spouse's duty of support authorized by the predecessor of article 98. The Tax Court has held, however, that a judgment of separation from bed and board under prior Louisiana law altered the marital status of the parties to such an extent that they were considered unmarried for federal income tax purposes. To qualify for spousal support under section 9:291, the spouses must be living separately and apart. The duty to make support payments ceases upon reconciliation of the parties. Because a spouse must be living separate and apart in order to obtain support payments, a court could follow Legget and hold that a decree under section 9:291 constitutes a separation from bed and board.

The precedential value of Legget is uncertain, however. In subsequent cases, courts have held that a decree for spousal support entered in jurisdictions other than Florida did not constitute legal separation for federal tax purposes. Indeed, it is not even certain that the Fifth Circuit...
Circuit would agree with Legget that a decree under former section 65.09 of the Florida Statutes constituted a legal separation. Both the Ninth Circuit and the Tax Court have held that a decree under the same Florida statute did not effect a legal separation.\textsuperscript{216}

The determination of whether an order for spousal support issued pursuant to section 9:291 constitutes a legal separation depends on state court interpretation of the statute. In Boyer v. Commissioner,\textsuperscript{217} the issue was whether a decree issued by a Massachusetts Probate Court, holding that the taxpayer's wife was living apart for justifiable cause, ordering the taxpayer to pay spousal support, and restraining him from approaching his wife or the marital residence, constituted a legal separation for federal income tax purposes. The Tax Court reviewed decisions of the Massachusetts Supreme Court and determined that the decree in question modified the parties' marital status in such a way that the taxpayer was legally separated from his wife.\textsuperscript{218}

The Court of Appeals for the District of Columbia Circuit reversed the Tax Court's decision, explaining,

In determining whether a party is legally separated for purposes of [federal income taxation] the proper inquiry is not whether a state order of separate maintenance affects marriage status under applicable state law; rather the proper inquiry is whether an order of separate maintenance affects marriage status in such a way that it is deemed a legal separation under applicable state law.\textsuperscript{219}

The order in Boyer was expressly denominated "'Temporary Order.'" The Supreme Court of Massachusetts had held that such an order did not "create a judicial separation, nor establish a permanent status for

\textsuperscript{216} See, e.g., Tressler v. Commissioner, 228 F.2d 356, 360 (9th cir. 1955), aff'g 12 T.C.M. (CCH) 358 (1953); Legget v. Commissioner, 39 T.C. 1022 (1963), rev'd, 329 F.2d 509 (2d Cir. 1964).


\textsuperscript{218} Boyer v. Commissioner, 79 T.C. 143, 147-52 (1982).

Accordingly, the Court of Appeals for District of Columbia Circuit held that the order did not constitute a legal separation for purposes of federal income taxation. If the Louisiana Supreme Court were to hold that a decree pursuant to section 9:291 effects a legal separation under state law, separated spouses in Louisiana paying or receiving spousal support would be considered unmarried for federal income tax purposes. Unless and until the Louisiana Supreme Court decides the issue, however, it is uncertain whether Louisiana taxpayers who are making support payments pursuant to such a decree are considered married for federal income tax purposes. Nevertheless, the weight of authority seems to indicate that such taxpayers are considered married.

Thus, in repealing the provisions for separation from bed and board, the Louisiana legislature practically has assured that spouses who are separated but not divorced will be considered married for federal tax purposes unless the abandoned spouse rule applies. "Married" status may be inconsequential for some taxpayers and in fact, may offer tax savings to others. In the majority of cases, however, that status will increase the tax burden of separated spouses in Louisiana as compared with separated spouses in jurisdictions that authorize judgments of legal separation. The following sections of this article illustrate the problem.

221. Boyer, 732 F.2d at 195.
222. One commentator finds evidence in two cases that spouses may be considered unmarried without obtaining a legal separation. Ulven, supra note 183, at 908. Neither of these cases, however, is helpful in establishing a rule of law giving separated spouses unmarried status unless the spouses have obtained a legal separation. In Hilliard v. Commissioner, 49 T.C.M. (CCH) 505 (1985), the Tax Court held that a Louisiana taxpayer was unmarried for federal tax purposes even though he could not provide court records to show that he had obtained a judgment of separation from bed and board under former provisions of the Louisiana Civil Code. While no court records were introduced into evidence, the Tax Court concluded, based on the testimony of the witnesses, that the taxpayer was legally separated. Id. at 506. At best, Hilliard only relaxed the taxpayer's burden of proving legal separation by permitting a taxpayer to submit oral proof rather than court records.

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In Abrams v. Commissioner, 57 T.C.M. (CCH) 1433 (1989), nonacq., action on decision, 1990-017 (July 2, 1990), the Tax Court assumed in dicta and without any analysis that two Texas spouses were legally separated. While legal separation is not available under Texas law, there was no issue in Abrams as to whether the taxpayer was considered unmarried under the "legally separated" requirement of I.R.C. § 7703(a)(2). The issue in Abrams concerned the taxpayer's eligibility to claim head-of-household filing status. The Tax Court held that the taxpayer was not eligible for such status because she did not furnish over one-half of the cost of maintaining her household. Not only do Hilliard and Abrams fail to provide substantive law regarding the definition of legal separation for purposes of determining filing status, but they have no precedential value. Hilliard and Abrams are both memorandum opinions. Tax Court memorandum opinions do not constitute binding precedent. Nico v. Commissioner, 67 T.C. 647, 654, aff'd in part and rev'd in part on unrelated issues, 565 F.2d 1234 (2d Cir. 1977).
B. Filing Status and the Income Tax Rates: The Marriage Penalty and the Marriage Bonus

The federal income tax is a progressive tax; an individual’s taxable income is taxed on a graduated schedule as income increases. The first dollars of taxable income are taxed at fifteen percent; the next bracket of taxable income is taxed at twenty-eight percent; and a third bracket is taxed at thirty-one percent. The amount of tax that an individual must pay with regard to taxable income depends on the individual’s filing status. Sections 1(a) through (d) of the Internal Revenue Code prescribe different tax rates for four classes of individual filers: (1) married individuals filing joint returns and surviving spouses, (2) heads of households, (3) unmarried individuals (other than surviving spouses and heads of households), and (4) married individuals filing separate returns.223

223. I.R.C. § 1(a)-1(d) (Supp. 1991) set forth the 1991 income tax rates for natural persons as follows:

§ 1. Tax imposed
(a) Married individuals filing joint returns and surviving spouses.—There is hereby imposed on the taxable income of—
(1) every married individual (as defined in section 7703) who makes a single return jointly with his spouse under section 6013, and
(2) every surviving spouse (as defined in section 2(a)), a tax determined in accordance with the following table:

<table>
<thead>
<tr>
<th>If taxable income is:</th>
<th>The tax is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not over $32,450</td>
<td>15% of taxable income.</td>
</tr>
<tr>
<td>Over $32,450 but not over $78,400</td>
<td>$4,867.50, plus 28% of the excess over $32,450.</td>
</tr>
<tr>
<td>Over $78,400</td>
<td>$17,733.50, plus 31% of the excess over $78,400.</td>
</tr>
</tbody>
</table>

(b) Heads of households.—There is hereby imposed on the taxable income of every head of a household (as defined in section 2(b)) a tax determined in accordance with the following table:

<table>
<thead>
<tr>
<th>If taxable income is:</th>
<th>The tax is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not over $26,050</td>
<td>15% of taxable income.</td>
</tr>
<tr>
<td>Over $26,050 but not over $67,200</td>
<td>$3,907.50, plus 28% of the excess over $26,500.</td>
</tr>
<tr>
<td>Over $67,200</td>
<td>$15,429.50, plus 31% of the excess over $67,200.</td>
</tr>
</tbody>
</table>

(c) Unmarried individuals (other than surviving spouses and heads of households).—There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 7703) a tax determined in accordance with the following table:

<table>
<thead>
<tr>
<th>If taxable income is:</th>
<th>The tax is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not over $19,450</td>
<td>15% of taxable income.</td>
</tr>
</tbody>
</table>
The amount of taxable income that is taxed at the lower rates varies depending on the taxpayer's filing status. These variations create for some a marriage penalty and for others a marriage bonus.\(^2\) A marriage penalty results when two married persons with the same income would pay a lower tax in the aggregate if they were not married. A marriage bonus results when the fact of marriage reduces the aggregate amount of tax that the two must pay.

This article will use the 1992 rate schedules to illustrate the marriage penalty and the marriage bonus. The 1991 schedules are found in sections 1(a) through (d) of the Internal Revenue Code. For taxable years after 1991, these schedules are adjusted annually for inflation.\(^2\)

The 1992 rate schedules that apply to individuals in each of the four classes are as follows:

**Section 1(a)—Married Individuals Filing Joint Returns and Surviving Spouses**

<table>
<thead>
<tr>
<th>If Taxable Income Is:</th>
<th>The Tax Is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Over $35,800</td>
<td>15% of the taxable income</td>
</tr>
<tr>
<td>Over $35,800, but not over $86,500</td>
<td>$5,370 plus 28% of the excess over $35,800</td>
</tr>
<tr>
<td>Over $86,500</td>
<td>$19,566 plus 31% of the excess over $86,500</td>
</tr>
<tr>
<td>Over $19,450 but not over $47,050</td>
<td>$2,917.50, plus 28% of the excess over $19,450</td>
</tr>
<tr>
<td>Over $47,050</td>
<td>$10,645.50, plus 31% of the excess over $47,050</td>
</tr>
</tbody>
</table>

(d) Married individuals filing separate returns.—There is hereby imposed on the taxable income of every married individual (as defined in section 7703) who does not make a single return jointly with his spouse under section 6013, a tax determined in accordance with the following table:

<table>
<thead>
<tr>
<th>If taxable income is:</th>
<th>The tax is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not over $16,225</td>
<td>15% of taxable income</td>
</tr>
<tr>
<td>Over $16,225 but not over $39,200</td>
<td>$2,433.75, plus 28% of the excess over $16,225</td>
</tr>
<tr>
<td>Over $39,200</td>
<td>$8,866.75, plus 31% of the excess over $39,200</td>
</tr>
</tbody>
</table>

These rate schedules are adjusted annually for inflation. I.R.C. § 1(f) (1988).


\(^{225}\) I.R.C. § 1(f) (1988).
Section 1(b)—Heads of Households

<table>
<thead>
<tr>
<th>Taxable Income Is:</th>
<th>The Tax Is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Over $28,750</td>
<td>15% of the taxable income</td>
</tr>
<tr>
<td>Over $28,750 but not over $74,150</td>
<td>$4,312.50 plus 28% of the excess over $28,750</td>
</tr>
<tr>
<td>Over $74,150</td>
<td>$17,024.50 plus 31% of the excess over $74,150</td>
</tr>
</tbody>
</table>

Section 1(c)—Unmarried Individuals (Other Than Surviving Spouses and Heads of Households)

<table>
<thead>
<tr>
<th>Taxable Income Is:</th>
<th>The Tax Is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Over $21,450</td>
<td>15% of the taxable income</td>
</tr>
<tr>
<td>Over $21,450 but not over $51,900</td>
<td>$3,217.50 plus 28% of the excess over $21,450</td>
</tr>
<tr>
<td>Over $51,900</td>
<td>$11,743.50 plus 31% of the excess over $51,900</td>
</tr>
</tbody>
</table>

Section 1(d)—Married Individuals Filing Separate Returns

<table>
<thead>
<tr>
<th>Taxable Income Is:</th>
<th>The Tax Is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Over $17,900</td>
<td>15% of the taxable income</td>
</tr>
<tr>
<td>Over $17,900 but not over $43,250</td>
<td>$2,685 plus 28% of the excess over $17,900</td>
</tr>
<tr>
<td>Over $43,250</td>
<td>$9,783 plus 31% of the excess over $43,250</td>
</tr>
</tbody>
</table>

A glance at the rate schedule shows that separated spouses, each with taxable income of $21,450 in 1992, pay a higher tax if they are considered married than if they are considered unmarried. Unmarried taxpayers with income of $21,450 or less pay income tax at a rate of fifteen percent. Thus, the total combined tax liability on the $42,900 of combined income is $6,435. If the two are considered married, however, the fifteen percent rate applies only to the first $35,800 of taxable income. The remaining $7,100 of their combined income is taxed at twenty-eight percent. The tax liability for a married couple with $42,900 of taxable income is $7,358, resulting in a marriage penalty of $923.227

A marriage bonus would result, however, if only one of the spouses has taxable income. A separated spouse with taxable income of $42,900 who is considered unmarried incurs a tax liability of $9,223.50. If the taxpayer is considered married and his or her spouse has no taxable

227. If each spouse had taxable income of $21,450 in 1992, the couple's aggregate tax liability would be $7,358, whether the spouses filed a joint return or separate returns. The rate schedule for a married taxpayer filing a separate return is exactly one-half of the schedule that applies to a joint return. I.R.C. § 1(a), (d); Rev. Proc. 91-65 § 2, 1991-2 C.B. 867, 868.
income, the tax liability on the joint return is $7,358,228 resulting in a marriage bonus of $1,865.50.

The amount of the marriage penalty and marriage bonus increases as taxable income increases. For example, two unmarried taxpayers with taxable income of $60,000 each in 1992 incur a tax liability of $28,509 in the aggregate. If they were considered married, the tax liability on their $120,000 of combined taxable income would be $29,951, resulting in a marriage penalty of $1,442. The marriage bonus for a taxpayer with $120,000 of taxable income who is considered married to a spouse with no taxable income in 1992 is $2,903.50.229

In both examples the marriage bonus is greater than the marriage penalty. The computations seem to indicate that taxpayers would prefer to be considered married for federal income tax purposes. The marriage penalty, however, falls most heavily upon two-earner couples. Separated spouses often will feel the bite of the marriage penalty because the economic burden of establishing separate households generally requires that separated spouses both work.230 Such taxpayers, of course, would prefer to be considered unmarried to avoid the marriage penalty.

Separated spouses may prefer to be considered unmarried even if a marriage bonus might be available because the marriage bonus generally results only if the couple files a joint return.231 If a couple is living under a separate property regime and one spouse has $120,000 of taxable income and the spouse with no income refuses to sign a joint return, the spouse with the income must use the rate schedule that applies to married individuals filing separate returns. Such an individual would

228. For the sake of simplicity, the example in the text does not take into account the fact that married taxpayers filing a joint return are entitled to two personal exemptions and to a higher standard deduction than the standard deduction for unmarried taxpayers. The additional personal exemption and the higher standard deduction could reduce the taxpayer's taxable income, increasing the amount of the marriage bonus. For a discussion of the standard deduction and the personal exemption, see infra notes 249-59, 294-303 and accompanying text.


230. A study of divorcing couples in California in 1977 revealed that in most cases the spouses had few community assets to divide, that only seventeen percent of divorcing spouses received spousal support upon divorce, that in the few cases where spousal support was awarded, the spouse received a median of $210 per month, and that the mean child support order was $126 per child even though it cost more than $4,000 per year to raise a child at a moderate standard of living in 1980. Lenore J. Wiltzman, The Economics of Divorce: Social and Economic Consequences of Property, Alimony and Child Support Awards, 28 U.C.L.A. L. Rev. 1181 (1981). No doubt these meager awards provide strong incentive for the supported spouse to find a job.

incur a 1992 tax liability of $33,575 or $721 more than the spouse would pay if the spouse could qualify as unmarried for federal tax purposes. The spouse earning the income might be able to convince the other spouse to sign a joint return, especially if there is an offer to increase support payments in exchange for such an agreement. The agreement to sign a joint return, however, requires not only the cooperation but also the trust of the nonearning spouse. A spouse who signs a joint return incurs joint and several liability for any deficiency in tax, as well as penalties and interest with respect to the return. Such cooperation and trust may not be present when the spouses are separating.

Of course, a high income spouse’s tax burden is reduced significantly, to the detriment of the other spouse, if the community is not terminated and section 66 of the Internal Revenue Code does not apply. In that case, the Seaborn rule requires each spouse to pay tax on $60,000 of taxable income, resulting in a tax liability of $14,475.50 to each if they file separate returns. If, however, the low income spouse is aware of the Seaborn rule and has obtained a partition or judgment of separation of property, the high income spouse will not be able to take advantage of the Seaborn rule. Moreover, if the spouses live apart for the entire calendar year and no earned community income is transferred between

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232. For simplicity, the example in the text disregards the fact that I.R.C. § 151(b) (1988) permits a married taxpayer filing a separate return to reduce taxable income by claiming an additional exemption deduction for the taxpayer’s spouse if the spouse has no gross income and is not the dependent of another taxpayer. In many cases the separate filer will not be entitled to claim the additional exemption deduction either because the spouse who has no gross income is supported by another individual who claims the spouse as a dependent or because the taxpayer is paying spousal support, includable in the spouse’s gross income under I.R.C. § 71(a) (1988).

233. I.R.C. § 6013(d)(3) (1988). A spouse who signs a joint return may be relieved of liability for the tax if the spouse qualifies as an “innocent spouse” under I.R.C. § 6013(e) (1988). The stringent requirements of § 6013(e), however, limit the availability of such relief. The technical requirements and the requirement of I.R.C. § 6013(e)(1)(C), that the spouse “did not know, and had no reason to know” that there was a substantial understatement of tax on the return, precludes many taxpayers from qualifying for innocent spouse relief. For a criticism of the innocent spouse rules, see Richard C.E. Beck, The Innocent Spouse Problem: Joint and Several Liability for Income Taxes Should Be Repealed, 43 Vand. L. Rev. 317 (1990); Beck, supra note 177; Borison, Innocent Spouse Relief: A Call for Legislative and Judicial Liberalization, 40 Tax Law. 819 (1987); Filler, supra note 34; Minick, supra note 34; J. Timothy Phillips & L. Bradford Bradford, Even a Tax Collector Should Have Some Heart: Equitable Relief for the Innocent spouse Under I.R.C. § 6013(e), 8 N. Ill. U. L. Rev. 33 (1987); Note, The Innocent spouse Rule: Recent Developments and Proposed Changes, 14 Sw. U. L. Rev. 129 (1983).

them, section 66 will prevent application of the rule with respect to all community income except income derived from community property.\textsuperscript{235} Thus, in many cases the high income spouse is able to take advantage of the Seaborn rule only during the first year of separation.\textsuperscript{236}

The marriage penalty is more pronounced if one or both of the spouses qualifies for the rate schedule that applies to heads of households.\textsuperscript{237} An individual is considered a head of a household\textsuperscript{238} if the individual is not married at the close of the taxable year and either (1) furnishes over half of the cost of maintaining a household that is the home of the taxpayer and that constitutes for more than one-half of the taxable year the principal place of abode of the taxpayer's unmarried child\textsuperscript{239} or grandchild\textsuperscript{240} or any other person, including a married child or stepchild, if the taxpayer is entitled to claim the person as a dependent,\textsuperscript{241} or (2) furnishes over half of the cost of maintaining a household which is the principal place of abode of the taxpayer's de-

\textsuperscript{235.} See I.R.C. § 66(a) (requiring community income to be taxed in accordance with the rules of I.R.C. § 879(a) if (1) the spouses live apart at all times during the calendar year, (2) the spouses do not file a joint return, (3) one of both of the spouses has earned income which is community income, and (4) no portion of such earned income is transferred between the spouses during the calendar year). The Seaborn rule is also inapplicable if the low income spouse satisfies the requirements of I.R.C. § 66(c) (which permits a taxpayer to exclude from income items of community income attributable to the other spouse under I.R.C. § 879(a) if (1) the taxpayer files a separate return, (2) the taxpayer establishes lack of actual or constructive knowledge of the item of community income, and (3) taking into account all facts and circumstances, it is inequitable to include the item in the taxpayer's income).

\textsuperscript{236.} Even during the first year of separation, the high income spouse may not be able to take advantage of the Seaborn rule if the high income spouse acted as if solely entitled to the community income and failed to notify the other spouse of the nature and amount of the income. I.R.C. § 66(b) (1988).

\textsuperscript{237.} I.R.C. § 1(b) (1988).

\textsuperscript{238.} For definition of the term "head of a household," see I.R.C. § 2(b) (1988).

\textsuperscript{239.} For this purpose the term "child" includes the taxpayer's son, stepson, daughter, or stepdaughter. I.R.C. § 2(b)(1)(A)(i) (1988).

\textsuperscript{240.} For this purpose, the term "grandchild" includes only descendents of the taxpayer's son or daughter I.R.C. § 2(b)(1)(A)(ii) (1988). If the member of the household is a descendant of the taxpayer's stepson or stepdaughter, the taxpayer apparently must be entitled to claim a dependency exemption for the ward to qualify as a head of a household. I.R.C. § 2(b)(1)(A)(ii) (1988).

\textsuperscript{241.} I.R.C. § 2(b)(1)(A)(ii) (1988). If the taxpayer would be entitled to claim a child as a dependent but cannot because the taxpayer entered into an agreement permitting the taxpayer's spouse or ex-spouse to claim the child as a dependent, the taxpayer may still be eligible to claim head-of-household status. I.R.C. § 2(b)(1)(A)(i) (1988). A member of the taxpayer's household whom the taxpayer is entitled to claim as a dependent will not cause the taxpayer to be eligible to file as a head of household, however, if the dependent is not related to the taxpayer within the rules of I.R.C. § 152(a)(1)-(B) or if the only reason the taxpayer may claim the dependent is because of a multiple support agreement. I.R.C. § 2(b)(3)(B) (1988).
dependent father or mother. Where each spouse with $60,000 of taxable income in 1992 qualifies for the head-of-household rate schedule, the aggregate tax liability is $26,125, a tax savings of $3,826 when compared with the amount of tax they would have to pay if they filed a joint return or separate returns as married individuals.

A threshold requirement for qualifying as a head of a household, however, is that the taxpayer be unmarried. A taxpayer is considered unmarried for purposes of head-of-household status if (1) the taxpayer is legally separated from his or her spouse under a decree of divorce or of separate maintenance, (2) the taxpayer's spouse is a nonresident alien, or (3) the taxpayer is considered unmarried under the abandoned spouse rule. Under these rules, a separated spouse in Louisiana will not qualify as a head of a household even though the spouse furnishes over one-half of the cost of maintaining a household for a dependent unless the other spouse was not a member of the household during the last six months of the taxable year. As long as the community is in existence, a separated spouse in Louisiana will not qualify as a head of a household for failure to provide over one-half of the cost of maintaining a household. In this respect, the Seaborn rule imposes a double burden on a low income spouse who files a separate return. Not only must the low income spouse pay tax on one-half of the community income, but the low income spouse must pay tax at the high rates that apply to a married taxpayer filing separately rather than at the lower rate that applies to a head of a household. If a decree of legal separation were available in Louisiana, it would be easier for separated spouses to qualify for the more favorable tax rates that apply to heads of households.

The enactment of provisions authorizing legal separation, of course, would not offer tax savings to separated spouses in Louisiana who qualify for a marriage bonus under the income tax rate structure. Enactment of such provisions, however, would not necessarily increase the federal tax burden of separated spouses. Spouses could continue to take advantage of the marriage bonus provisions of the Internal Revenue Code by failing to file a petition for a judgment of separation from bed and board.

246. I.R.C. §§ 2(c), 7703(b) (1988).
If the Louisiana Legislature were to enact a provision authorizing legal separation, separating spouses would have to compare the cost of filing for a legal separation, including attorney fees, against the tax savings that could be achieved by qualifying as unmarried for federal income tax purposes. For taxpayers who plan to live separately and apart from their spouses for a long period of time because they do not plan to be divorced, a savings of approximately $1,000 to $3,000 per year because of reduced tax rates could quickly offset the cost of obtaining a legal separation.

Even taxpayers who plan to divorce their spouses shortly after the end of the taxable year in which the separation occurs and taxpayers who will qualify as unmarried under the abandoned spouse rule in the year after the separation, could achieve substantial tax savings by qualifying as unmarried during the first year of separation. The foregoing comparison of tax burdens considered only the results of the application of the tax rates. The marriage penalty actually is greater for a two-earner couple because the higher rates that apply to such married taxpayers generally are imposed on a broader tax base than the lower rates that apply to unmarried individuals or heads of households. In computing taxable income, married taxpayers generally are allowed more limited deductions and must include greater amounts in income than their unmarried counterparts.

C. Further Consideration of the Marriage Penalty: Broadening the Income Tax Base of Two Earner Married Couples

A two-earner married couple generally must report a larger amount of taxable income than two unmarried taxpayers with the same aggregate amount of gross income and expenditures. The Internal Revenue Code achieves this result by reducing the amount of deductions available to married taxpayers, as compared to unmarried taxpayers, requiring married taxpayers to include more in income than their unmarried counterparts, and by attributing the interests in an entity from one spouse to another. Thus, when separated spouses both have income, tax savings can be achieved if the spouses are considered unmarried for federal tax purposes.

1. The Standard Deduction

Individual taxpayers must choose between itemizing their personal deductions or deducting a flat allowance, known as the standard deduction, in lieu of their itemized deductions. Taxpayers who have

attained the age of sixty-five or are blind may claim an additional standard deduction for each qualifying attribute.\textsuperscript{250} The amount of the basic standard deduction\textsuperscript{251} and/or the additional standard deduction\textsuperscript{252} an individual may claim depends on the taxpayer's marital status. The rules for computing the standard deduction create a marriage penalty and a marriage bonus similar to the penalty and bonus that result from application of the rate schedules. In 1992, the basic standard deduction is $6,000 for a joint return, $5,250 for a head of household, $3,600 for an unmarried individual, and $3,000 for a married individual filing a separate return.\textsuperscript{253} The structure of the deductible amounts shows that a one-earner married couple achieves a $2,400 deduction bonus under the 1992 amounts that would not be available if the earning spouse were considered not married.\textsuperscript{254} A two-earner couple, however, loses $1,200 of the standard deduction the taxpayers could have claimed if they were considered not married.\textsuperscript{255} A spouse who, but for the fact of marriage, would be eligible to claim head-of-household status loses $2,250 of the standard deduction.

The allowances for the additional standard deduction have a similar effect. In 1992, the additional standard deduction is $700 for a married individual and $900 for an unmarried individual.\textsuperscript{256} A taxpayer who is married to an elderly or blind individual with no taxable income in 1992 could claim an additional $700 standard deduction that would not be allowable if the taxpayer were considered unmarried. If the taxpayer's spouse is both elderly and blind, a bonus deduction of $1400 results. When the earner is the elderly or blind person, however, there is a marriage penalty of $200 for each qualifying attribute.\textsuperscript{257}

\textsuperscript{250} I.R.C. § 63(c)(3), (f) (1988).
\textsuperscript{251} I.R.C. § 63(c)(2) (1988). If an individual is claimed as a dependent of another taxpayer, however, the individual's standard deduction may not exceed the greater of $600 or the individual's earned income plus any additional standard deduction that is allowed if the dependent taxpayer has attained the age of 65 or is blind. I.R.C. § 63(c)(5), (f) (1988); Rev. Proc. 91-65 § 3.02, 1991-2 C.B. 867, 869.


\textsuperscript{253} Rev. Proc. 91-65 § 3.01, 1991-2 C.B. 867, 868.

\textsuperscript{254} An unmarried taxpayer's standard deduction in 1992 is $3,600. By marrying an individual with no taxable income and filing a joint return, the individual could claim a $6,000 standard deduction.

\textsuperscript{255} Each unmarried taxpayer may claim a $3,600 standard deduction or a total of $7,200. By marrying and filing a joint return the couple could claim only a $6,000 deduction. If the spouses file separate returns, each could claim a standard deduction of $3,000 or a total of $6,000.


\textsuperscript{257} The $900 additional standard deduction that applies to unmarried individuals is reduced to $700 when an individual marries. Rev. Proc. 91-65 § 3.03, 1991-2 C.B. 867, 869.
The burden of the marriage penalty can fall heavily upon a married taxpayer filing a separate return. If the taxpayer’s spouse itemizes deductions on a separate return, the taxpayer may claim neither the $3,000 standard deduction that generally applies for separate returns nor any additional standard deduction regardless of whether the taxpayer is elderly or blind.258

A taxpayer is considered unmarried for purposes of claiming the standard deduction if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the taxpayer qualifies as an abandoned spouse.259 Thus, when a two-earner couple in Louisiana separates, the spouses often suffer a marriage penalty with respect to the standard deduction unless one or both of them qualifies as an abandoned spouse.

2. Itemized Deductions

a. The Overall Limitation on Itemized Deductions

If the spouses choose to itemize their deductions, rather than to use the standard deduction, they may suffer a marriage penalty with respect to the amount of itemized deductions they may claim. Section 68 of the Internal Revenue Code generally reduces the amount of a taxpayer’s otherwise allowable itemized deductions by three percent of the amount by which the taxpayer’s adjusted gross income exceeds $105,250 ($52,625 in the case of a married taxpayer filing a separate return).260 The reduction under section 68, however, may not exceed eighty percent of the taxpayer’s otherwise allowable deductions.261 Section 68 applies to all itemized deductions except four deductions that are subject to limitations under other provisions of the Internal Revenue Code. The itemized deductions excepted from reduction under section 68 are the deduction for medical expenses, the deduction for investment interest, the deduction for personal casualty and theft losses, and the deduction for wagering losses.262

An example illustrates the application of section 68. An unmarried taxpayer with adjusted gross income of $505,250 in 1992 loses the ability to deduct $12,000 of the taxpayer’s otherwise allowable itemized de-

259. I.R.C. §§ 63(g), 7703 (1988).
ductions to which section 68 applies.\textsuperscript{263} If the taxpayer only had $14,000 of such itemized deductions, however, the reduction under section 68 would be limited to eighty percent of the itemized deductions, or $11,200.\textsuperscript{264}

Under section 68, there is no marriage bonus. A taxpayer's itemized deductions are reduced if the taxpayer has adjusted gross income in excess of $105,250 whether the taxpayer is unmarried or is married and files a joint return with a spouse who has no taxable income. Section 68 imposes a significant marriage penalty. Separated spouses who are considered unmarried may deduct their itemized deductions in full if each spouse had adjusted gross income of $105,000 or less. If they are considered married and each has $105,250 of adjusted gross income, they must reduce their itemized deductions by three percent of $105,250, or $3,157.50. Filing separate returns will not alleviate the tax burden. A married taxpayer who files a separate return will suffer a reduction in itemized deductions by three percent of the amount by which the taxpayer's adjusted gross income exceeds $52,625.\textsuperscript{265}

The ability to itemize deductions, however, can result in a marriage bonus. A married taxpayer may deduct the itemized deductions of the taxpayer's spouse by filing a joint return, even if the spouse has no taxable income. When both spouses have adjusted gross income, however, the benefits of combining the spouses' itemized deductions on a joint return may be reduced or eliminated if the combined adjusted gross income on the joint return exceeds $105,250.

For purposes of section 68, marital status is determined under the rules of section 7703 of the Internal Revenue Code.\textsuperscript{266} Thus, separated spouses in Louisiana are considered married unless the abandoned spouse rule applies.\textsuperscript{267} By enacting a provision authorizing legal separation, the Louisiana Legislature could enable more separated spouses to avoid any marriage penalty resulting under section 68.\textsuperscript{268}

\textbf{b. The Deduction For Home Mortgage Interest}

The reductions required by section 68 apply after the application of any other limitation on the allowance of the itemized deduction in question. The fact of marriage may limit the amount of the taxpayer's itemized deductions under provisions of the Internal Revenue Code other

\begin{footnotes}
\item \textsuperscript{263} The taxpayer's $505,250 of adjusted gross income exceeds the $105,250 threshold amount by $400,000. Three percent of $400,000 is $12,000.
\item \textsuperscript{264} Such a taxpayer, of course, should claim the standard deduction of $3,600 in lieu of itemizing.
\item \textsuperscript{265} I.R.C. § 68(a)(1) (Supp. 1991).
\item \textsuperscript{266} I.R.C. § 68(b)(1) (Supp. 1991).
\item \textsuperscript{267} I.R.C. § 7703(b) (Supp. 1991).
\item \textsuperscript{268} A taxpayer who is legally separated under a decree of divorce or of separate maintenance is considered unmarried for purposes of I.R.C. § 68. I.R.C. §§ 68(d), 7703(a)(2) (1988 & Supp. 1991).
\end{footnotes}
than section 68. For example, section 163(h)(3) authorizes a deduction for home mortgage interest. In general, the maximum amount of

269. I.R.C. § 163(h) (1988) provides in part:

(h) Disallowance of deduction for personal interest.—
(1) In general.—In the case of a taxpayer other than a corporation, no deduction shall be allowed under this chapter for personal interest paid or accrued during the taxable year.
(2) Personal interest.—For purposes of this subsection, the term "personal interest" means any interest allowable as a deduction under this chapter other than—

(D) any qualified residence interest (within the meaning of paragraph (3))

(3) Qualified residence interest.—For purposes of this subsection—
(A) In general.—The term "qualified residence interest" means any interest which is paid or accrued during the taxable year on—
(i) acquisition indebtedness with respect to any qualified residence of the taxpayer, or
(ii) home equity indebtedness with respect to any qualified residence of the taxpayer.

For purposes of the preceding sentence, the determination of whether any property is a qualified residence of the taxpayer shall be made as of the time the interest is accrued.
(B) Acquisition indebtedness.—
(i) In general.—The term "acquisition indebtedness" means any indebtedness which—
(I) is incurred in acquiring, constructing, or substantially improving any qualified residence of the taxpayer, and
(II) is secured by such residence. Such term also includes any indebtedness secured by such residence resulting from the refinancing of indebtedness meeting the requirements of the preceding sentence (or this sentence); but only to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.
(ii) $1,000,000 Limitation.—The aggregate amount treated as acquisition indebtedness for any period shall not exceed $1,000,000 ($500,000 in the case of a married individual filing a separate return).
(C) Home equity indebtedness.—
(i) In general.—The term "home equity indebtedness" means any indebtedness to the extent the aggregate amount of such indebtedness does not exceed—
(I) the fair market value of such qualified residence, reduced by
(II) the amount of acquisition indebtedness with respect to such residence.
(ii) Limitation.—The aggregate amount treated as home equity indebtedness for any period shall not exceed $100,000 ($50,000 in the case of a separate return by a married individual).
(D) Treatment of indebtedness incurred on or before October 13, 1987.—
(i) In general.—In the case of any pre-October 13, 1987, indebtedness—
(I) such indebtedness shall be treated as acquisition indebtedness, and
(II) the limitation of subparagraph (B)(ii) shall not apply.
(ii) Reduction in $1,000,000 Limitation.—The limitation of subparagraph
principal debt that will qualify for the interest deduction is $1,100,000\textsuperscript{270} ($550,000 in the case of a separate return by a married individual).\textsuperscript{271}

(B)(ii) shall be reduced (but not below zero) by the aggregate amount of outstanding pre-October 13, 1987, indebtedness.

(iii) Pre-October 13, 1987, indebtedness.—The term “pre-October 13, 1987, indebtedness” means—

(I) any indebtedness which was incurred on or before October 13, 1987, and which was secured by a qualified residence on October 13, 1987, and at all times thereafter before the interest is paid or accrued, or

(II) any indebtedness which is secured by the qualified residence and was incurred after October 13, 1987, to refinance indebtedness described in subclause (I) (or refinanced indebtedness meeting the requirements of this subclause) to the extent (immediately after the refinancing) the principal amount of the indebtedness resulting from the refinancing does not exceed the principal amount of the refinanced indebtedness (immediately before the refinancing).

(iv) Limitation on period of refinancing.—Subclause (II) of clause (iii) shall not apply to any indebtedness after—

(I) the expiration of the term of the indebtedness described in clause (iii)(I), or

(II) if the principal of the indebtedness described in clause (iii)(I) is not amortized over its term, the expiration of the term of the 1st refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such 1st refinancing).

(4) Other definitions and special rules.—For purposes of this subsection—

(A) Qualified residence.—

(I) In general.—The term “qualified residence” means—

(1) the principal residence (within the meaning of section 1034) of the taxpayer, and

(II) 1 other residence of the taxpayer which is selected by the taxpayer for purposes of this subsection for the taxable year and which is used by the taxpayer as a residence (within the meaning of section 280A(d)(1)).

(ii) Married individuals filing separate returns.—If a married couple does not file a joint return for the taxable year—

(I) such couple shall be treated as 1 taxpayer for purposes of clause (i), and

(II) each individual shall be entitled to take into account 1 residence unless both individuals consent in writing to 1 individual taking into account the principal residence and 1 other residence.

(iii) Residence not rented.—For purposes of clause (i)(II), notwithstanding section 280A(d)(1), if the taxpayer does not rent a dwelling unit at any time during a taxable year, such unit may be treated as a residence for such taxable year.

\textsuperscript{270} A taxpayer may deduct the interest on $1,000,000 or less of “acquisition indebtedness,” defined as indebtedness incurred in acquiring, constructing, or substantially improving any qualified residence of the taxpayer which is secured by the residence. I.R.C. § 163(h)(3)(B) (1988). A taxpayer may also deduct the interest on $100,000 or less of “home equity indebtedness,” defined as indebtedness (other than acquisition indebtedness) secured by a qualified residence to the extent that it does not exceed the fair market value of the residence reduced by the amount of acquisition indebtedness with respect to the residence. I.R.C. § 163(h)(3)(C) (1988). Indebtedness that was incurred on or before October 13, 1987, however may exceed the $1,100,000 and $550,000 limitations. I.R.C. § 163(h)(3)(D) (1988).

\textsuperscript{271} I.R.C. § 163(h)(3)(B), (C) (1988).
A taxpayer may claim the deduction with respect to a maximum of two "qualified residences," defined as the taxpayer's principal residence and one other residence that the taxpayer selects.\textsuperscript{272} If the taxpayer is married and files a separate return, however, the taxpayer may deduct home mortgage interest with respect to only one residence unless the taxpayer's spouse consents in writing to forego the home mortgage interest deduction.\textsuperscript{273}

These rules impose a marriage penalty on very wealthy taxpayers. Separated spouses who are considered unmarried may deduct the interest on an aggregate of $2,200,000 of home mortgage principal with respect to four residences. If they are considered married, the deduction is limited to the interest on $1,100,000 of debt with respect to two residences. A spouse who is considered married and files a separate return, however, feels the greatest impact of the marriage penalty because the separate filer may only deduct the interest on a maximum of $550,000 of indebtedness even if the taxpayer's spouse agrees to permit the taxpayer to claim the deduction with respect to two residences. The ability to obtain a judgment of separation from bed and board in Louisiana could help some separated spouses to avoid a marriage penalty under section 163(h)(3).\textsuperscript{274}

c. Estimated Losses on Deposits in Insolvent and Bankrupt Financial Institutions

A similar marriage penalty can result under section 165(l) of the Internal Revenue Code which allows a taxpayer to elect to deduct as an itemized deduction reasonably estimated losses with respect to deposits in certain bankrupt or insolvent financial institutions.\textsuperscript{275} The election

\textsuperscript{272} I.R.C. \S 163(h)(4)(A) (1988). The second residence will qualify if the taxpayer does not rent it out. I.R.C. \S 163(h)(4)(A)(iii) (1988). If the taxpayer rents the second residence to third parties, the residence will qualify only if the taxpayer uses it for personal purposes for the greater of 14 days or ten percent of the number of days during the year for which the residence is rented at fair rental. I.R.C. §§ 163(h)(4)(A)(ii), 280A(d)(1) (1988).


\textsuperscript{274} I.R.C. § 163(h) provides no definition of marital status. This article assumes that the references in I.R.C. § 163(h)(3)(B)(ii) and (h)(3)(C)(ii) to a married individual filing a separate return and the reference in I.R.C. § 163 (h)(4)(A)(ii) to a married couple that does not file a joint return incorporate the rules for filing status. For purposes of determining an individual's filing status, the individual is considered unmarried if the individual is legally separated from his or her spouse under a decree of divorce or of separate maintenance or if the abandoned spouse rule applies. I.R.C. §§ 1(a), (c), (d); 2(b)(2)(B), (c); 7703 (1988).

\textsuperscript{275} I.R.C. § 165(l) (1988 & Supp. 1991) provides:

(l) Treatment of certain losses in insolvent financial institutions.—

(1) In general.—If—

(A) as of the close of the taxable year, it can reasonably be estimated that there is a loss on a qualified individual's deposit in a qualified financial
under section 165(i) is authorized only with respect to losses on deposits

institutions, and;
(B) such loss is on account of the bankruptcy or insolvency of such institution,
then the taxpayer may elect to treat the amount so estimated as a loss described in subsection (c)(3) incurred during the taxable year.

(2) Qualified individual defined.—For purposes of this subsection, the term "qualified individual" means any individual, except an individual—
(A) who owns at least 1 percent in value of the outstanding stock of the qualified financial institution,
(B) who is an officer of the qualified financial institution,
(C) who is a sibling (whether by the whole or half blood), spouse, aunt, uncle, nephew, niece, ancestor, or lineal descendant of an individual described in subparagraph (A) or (B), or
(D) who otherwise is a related person (as defined in section 267(b)) with respect to an individual described in subparagraph (A) or (B).

(3) Qualified financial institution.—For purposes of this subsection, the term "qualified financial institution" means—
(A) any bank (as defined in section 581),
(B) any institution described in section 591,
(C) any credit union the deposits or accounts in which are insured under Federal or State law or are protected or guaranteed under State law, or
(D) any similar institution chartered and supervised under Federal or State law.

(4) Deposit.—For purposes of this subsection, the term "deposit" means any deposit, withdrawable account, or withdrawable or repurchasable share.

(5) Election to treat as ordinary loss.—
(A) In general.—In lieu of any election under paragraph (1), the taxpayer may elect to treat the amount referred to in paragraph (1) for the taxable year as an ordinary loss described in subsection (c)(2) incurred during the taxable year.
(B) Limitations.—
(i) Deposit may not be federally insured.—No election may be made under subparagraph (A) with respect to any loss on a deposit in a qualified financial institution if part or all of such deposit is insured under Federal law.
(ii) Dollar limitation.—With respect to each financial institution, the aggregate amount of losses attributable to deposits in such financial institution to which an election under subparagraph (A) may be made by the taxpayer for any taxable year shall not exceed $20,000 ($10,000 in the case of a separate return by a married individual). The limitation of the preceding sentence shall be reduced by the amount of any insurance proceeds under any State law which can reasonably be expected to be received with respect to losses on deposits in such institution.

(6) Election.—Any election by the taxpayer under this subsection for any taxable year—
(A) shall apply to all losses for such taxable year of the taxpayer on deposits in the institution with respect to which such election was made, and
(B) may be revoked only with the consent of the Secretary.

(7) Coordination with section 166.—Section 166 shall not apply to any loss to
in financial institutions such as banks, mutual savings banks, savings and loan associations, and credit unions whose deposits are insured, protected, or guaranteed under state or federal law.\footnote{276} If any part of the deposit is federally insured, the taxpayer may elect to treat the loss as a personal casualty loss, deductible only to the extent that it exceeds $100 and to the extent that when combined with the taxpayer’s other casualty losses for the year, it exceeds ten percent of the taxpayer’s adjusted gross income.\footnote{277} If no part of the deposit is federally insured, the taxpayer may deduct the full amount of the loss.\footnote{278} The maximum of non-federally insured losses that a taxpayer may deduct in full, however, is $20,000.\footnote{279} A married taxpayer who files a separate return, however, may deduct only a maximum of $10,000 of such losses.\footnote{280} Thus, separated spouses who are considered unmarried taxpayers may deduct an aggregate of $40,000 of non-federally insured losses under section 165(l). If they are considered married, they may only deduct an aggregate of $20,000 of such losses.

The fact of marriage can eliminate the deduction under section 165(l) entirely. The deduction is available only to a taxpayer who is a “qualified individual.”\footnote{281} For this purpose, a taxpayer is not a qualified individual if the taxpayer owns one percent or more of the outstanding stock of

which an election under this subsection applies.

A taxpayer who does not elect to deduct the losses under I.R.C. § 165(l) may be able to deduct the losses as a nonbusiness bad debt under I.R.C. § 166(d) (1988). While a nonbusiness bad debt deduction can be more advantageous because a taxpayer may deduct the nonbusiness bad debt from gross income and also claim the standard deduction, I.R.C. §§ 166(d)(1)(B), 62(a)(3) (1988), the itemized deduction authorized by I.R.C. § 165(l) may be more advantageous. To deduct a nonbusiness bad debt under I.R.C. § 166(d), the taxpayer must prove that the debt has become worthless. An election under I.R.C. § 165(l), on the other hand, permits the taxpayer to deduct the reasonably estimated loss before it becomes worthless. A nonbusiness bad debt is also deductible only as a short term capital loss. I.R.C. § 166(d)(1)(B) (1988). Capital losses are deductible by an individual taxpayer only to the extent of the taxpayer’s capital gains for the year plus $3,000. I.R.C. § 1211(b) (1988). Amounts that are disallowed are carried forward indefinitely, subject to the same limitations in future years. I.R.C. § 1212(b) (1988). A taxpayer may obtain a larger current deduction of losses by electing under I.R.C. § 165(l) because the losses authorized by I.R.C. § 165(l) are considered ordinary losses. The time value of money may cause the current deduction of losses under I.R.C. § 165(l) to be worth more than a suspended deduction under I.R.C. § 166(d). For a discussion of the advantages of making an election under I.R.C. § 165(l), see 2 Bittker & Lokken, supra note 46, at ¶ 33.3.2.

\footnote{277} I.R.C. § 165(l)(1), (h) (1988). The example in the text assumes that the taxpayer has no personal casualty gains for the year. A taxpayer may deduct personal casualty losses in excess of $100 to the extent of the taxpayer’s personal casualty gains for the year. I.R.C. § 165(h)(2) (1988).
\footnote{280} Id.
the financial institution or is an officer of the financial institution.\textsuperscript{282} If the taxpayer's spouse owns a prohibited interest in or is an officer of the financial institution, the taxpayer also fails to be a qualified individual.\textsuperscript{283} Thus, ability to obtain a legal separation could allow some separated spouses in Louisiana larger deductions under section 165(l) of the Internal Revenue Code. A taxpayer may be able to avoid disqualification resulting from a spouse's interest in the institution by obtaining a legal separation.\textsuperscript{284}

d. 

Floors Limiting the Deductibility of Certain Itemized Expenses

The Internal Revenue Code limits the deductibility of some itemized expenses by imposing a floor on the deductions, measured with respect to a percentage of the taxpayer's adjusted gross income. For example, in computing the amount of allowable miscellaneous itemized deductions, such as unreimbursed employee business expenses and certain investment expenses, a taxpayer must subtract two percent of the taxpayer's adjusted gross income.\textsuperscript{285} A taxpayer must subtract ten percent of his or her adjusted gross income from net personal casualty and theft losses before any amount of the losses is deductible.\textsuperscript{286} Medical expenses are deductible only to the extent that they exceed seven and one-half percent of the taxpayer's adjusted gross income.\textsuperscript{287}

When a married taxpayer's adjusted gross income exceeds the adjusted gross income of an unmarried taxpayer with the same amount of gross income and deductions, these floors create a marriage penalty.

\textsuperscript{282} I.R.C. § 165(l)(2)(A), (B) (1988).
\textsuperscript{283} I.R.C. § 165(l)(2)(C) (1988). A taxpayer's sibling, aunt, uncle, nephew, niece, ancestor, or lineal descendant who owns a prohibited interest or is an officer of the financial institution also disqualifies the taxpayer from claiming the deduction. \textit{Id.} Nor can the taxpayer claim the deduction if a related entity owns a prohibited interest in or is an officer of the financial institution. I.R.C. § 165(l)(2)(D) (1988). Spousal attribution can cause an entity to be related if the taxpayer's spouse owns a sufficient interest in the entity. For a discussion of marriage penalties resulting from spousal attribution, see infra notes 455-498 and accompanying text.

\textsuperscript{284} I.R.C. § 165(l) provides no definition of marital status. This article assumes that the reference in I.R.C. § 165(l) (5)(B)(ii) to "a separate return by a married individual" incorporates the rules concerning marital status with respect to filing status. Under those rules, a taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse under a decree of divorce or of separate maintenance or if the abandoned spouse rule applies. I.R.C. §§ 1(a), (c), (d); 2(b)(2)(B), (c); 7703 (1988).


\textsuperscript{286} I.R.C. § 213(a) (1988).
A married taxpayer will have more adjusted gross income than his or her unmarried counterpart if certain provisions of the Internal Revenue Code apply that either increase the gross income of married taxpayers or reduce the deductions allowable in computing adjusted gross income of married taxpayers in comparison to unmarried taxpayers. A marriage bonus can result, of course, when only one spouse has adjusted gross income and the other spouse has itemized expenses. Certain provisions of the Internal Revenue Code reduce the adjusted gross income of a married couple as compared to the adjusted gross income of two similarly situated unmarried taxpayers. When both spouses have income, however, the benefits of pooling deductions and the benefit of any reductions in adjusted gross income can lose their value because spouses who file a joint return must also combine their income, thereby increasing adjusted gross income and the amount of the floor limiting the deductions.

e. The Charitable Deduction

With respect to some itemized deductions, the pooling of income on a joint return can result in a marriage bonus. For example, section 170 of the Internal Revenue Code places a ceiling on the amount of charitable contributions a taxpayer can deduct for the taxable year. The maximum amount that an individual taxpayer can deduct in any year under section 170 is generally fifty percent of the taxpayer’s adjusted gross income. Thus, the increase in adjusted gross income achieved by filing a joint return could increase the amount of currently deductible charitable contributions. The beneficial effects of pooling income on a joint return, however, could be illusory. Once the adjusted gross income on the joint return exceeds $105,250, section 68 reduces the amount of the charitable contribution that can be deducted. A married taxpayer may not be able to escape the section 68 limitation on the charitable

288. For a discussion of the different rules for computing the adjusted gross income of married and unmarried taxpayers, see infra notes 304-454, and accompanying text.
289. For a discussion of the marriage bonus provisions that affect the computation of adjusted gross income, see infra notes 304-454 and accompanying text.
291. I.R.C. § 170(b)(1)(A) (1988) provides that the maximum amount of charitable contributions that a taxpayer can deduct for the year is 50 percent of the taxpayer’s “contribution base.” The term “contribution base” is defined as “adjusted gross income (computed without regard to any net operating loss carryback to the taxable year under section 172).” I.R.C. § 170(b)(1)(F) (1988). A taxpayer may carry forward for five years charitable contributions that are not deductible because of the limitations that apply in the current year. I.R.C. § 170(d) (1988). Amounts carried forward are subject to the same limitations in future years. Id.
292. For a discussion of the limitations on itemized deductions under I.R.C. § 68 see supra notes 260-268, and accompanying text.
deduction by filing a separate return because the amount of the deduction is reduced once adjusted gross income reported on the separate return exceeds $52,625.293

Whether a spouse elects to use the standard deduction or to itemize personal expenses, a marriage penalty usually results when both spouses have income. When both separated spouses have income, they can reduce their taxable income and the consequential tax burden by qualifying as unmarried for federal income tax purposes. The Louisiana Legislature could help such taxpayers by authorizing suits for legal separation, thereby making it easier for them to claim unmarried status on their income tax returns.

3. The Deduction for Personal Exemptions

In addition to any other allowable deductions, a taxpayer generally may deduct an amount for a personal exemption. Section 151 of the Internal Revenue Code allows an individual taxpayer to deduct an exemption for the taxpayer, the taxpayer’s spouse, and the taxpayer’s dependents unless some other taxpayer is entitled to the deduction.294 The amount of the exemption deduction in 1992 is $2,300 per person claimed.295

Taxpayers with a large amount of adjusted gross income may not be able to deduct exemptions to which they would otherwise be entitled. A taxpayer must reduce the otherwise allowable deduction for exemptions by two percentage points for each $2,500 (or fraction thereof) by which the taxpayer’s adjusted gross income exceeds a threshold amount.296 A married taxpayer filing a separate return must reduce the otherwise allowable deduction by two percentage points for each $1,250 of adjusted gross income in excess of the threshold amount.297 The applicable threshold amount depends on a taxpayer’s filing status: $157,900 in the case of a joint return; $131,550 for a head of a household; $105,250 for an unmarried taxpayer; and $78,950 for a married taxpayer filing a separate return.298

The rules for reducing the deduction for exemptions have a similar marriage penalty/bonus effect as previously discussed provisions of the

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294. I.R.C. § 151(a), (b), (c), (d)(2) (1988).
297. Id.
298. I.R.C. § 151(d)(3)(C) (Supp. 1991) provides that the threshold amounts are:
   (1) $150,000 in the case of a joint return,
   (2) $125,000 for a head of a household,
   (3) $100,000 for an unmarried taxpayer, and
   (4) $75,000 for a married taxpayer who files a separate return.
Internal Revenue Code. For example, separated spouses who are considered unmarried may take advantage of an aggregate of $4,600 in exemption deductions, assuming that neither taxpayer has a dependent when each has adjusted gross income of $105,250 or less. If they are considered unmarried, the total exemption deduction allowable is $2,576, resulting in a marriage penalty of $2,024 in reduced deductions. If the taxpayers have dependents, the $2,300 exemption deduction for each of the dependents also is reduced proportionately.

A marriage bonus may result in the case of a one-earner couple. A separated spouse with adjusted gross income of $157,900 who is considered unmarried may deduct an exemption amount of $1,288. If the same taxpayer is considered married and his or her spouse has no adjusted gross income, there will be two fully deductible exemptions, totaling $4,600 on a joint return. If a "married" taxpayer files a separate return, however, whether or not the taxpayer is entitled to claim an exemption deduction for the spouse or for any dependents, the limitations on the exemption deduction prevent the taxpayer from claiming any deduction for an exemption unless spouses are living under a community property regime. If a community is in existence, each spouse must report $78,950 of adjusted gross income on his or her separate return, and each spouse is entitled to a $2,300 exemption deduction.

When one or both of the separated spouses has adjusted gross income in excess of $78,950 and the spouses file separate returns, tax

299. Following the rules of I.R.C. § 151(d)(3), the result in the text was reached first by determining that the taxpayers' $210,500 of adjusted gross income exceeded the threshold amount of $157,900 that applies to a joint return, by $52,600. The excess $52,600 is then divided by $2,500 to determine the number of $2,500 "(or fraction thereof)" amounts of adjusted gross income that exceed the threshold amount. The result is twenty-two, which then must be multiplied by two percent to determine the reduction in the exemption deduction. Under these facts, the exemption deduction must be reduced by forty-four percent. Because there are two taxpayers, the exemption deduction allowable before reduction is $4,600. This otherwise allowable amount must be reduced by forty-four percent, or $2,024, leaving an allowable deduction of $2,576. The aggregate deduction is the same if the taxpayers file separate returns.

300. The reduction under I.R.C. § 151(d)(3) applies to the total amount of exemptions that the taxpayer is otherwise entitled to deduct.

301. A married taxpayer who files a separate return may claim an additional exemption amount for the spouse if the spouse has no gross income and is not the dependent of another taxpayer. I.R.C. § 151(b) (1988).

302. This results because of the additional reductions that apply to separate filers under I.R.C. § 151(d)(3). In the example in the text, the taxpayer's $157,900 exceeds the $78,950 threshold amount by $78,950. The $1,250 increment that applies to a married taxpayer filing a separate return occurs 63.16 times. The rounded number sixty-four is then multiplied by two percent, resulting in a reduction of 128 percent of the otherwise allowable exemption amount. Section 151 gives the taxpayer a reprieve in such a situation by reciting that, "In no event shall the applicable percentage [of reduction] exceed one hundred percent." I.R.C. § 151(d)(3)(B) (Supp. 1991).
savings can be achieved if the spouses qualify as unmarried. The rules for determining marital status for purposes of the reduction in the exemption deduction are the same as the rules that apply with respect to filing status. Thus, for some taxpayers, the availability of a decree of legal separation in Louisiana would increase the amount of the deduction for personal exemptions.

4. Adjusted Gross Income and Marriage Penalty/Bonus Issues

To the extent that the fact of marriage increases or decreases a taxpayer’s adjusted gross income, a corresponding marriage penalty or bonus results. Any increase in adjusted gross income has a direct impact on taxable income. As explained earlier, an increase in adjusted gross income also can cause an indirect increase in taxable income because adjusted gross income serves as a measuring rod that reduces the overall amount of itemized deductions, miscellaneous itemized deductions, personal casualty and theft losses, medical expenses, and the exemption amount that a taxpayer may claim. Adjusted gross income also serves as a measuring device for other purposes of the Internal Revenue Code, generally limiting tax savings otherwise available as adjusted gross income increases.


304. “Taxable income” is defined as gross income minus the taxpayer’s deductions including either itemized deductions or the standard deduction. I.R.C. § 63(a) (1988). In other words, taxable income is adjusted gross income minus: (1) either the taxpayer’s itemized deductions or the standard deduction, and (2) the deduction for exemptions. Thus, as adjusted gross income increases, so does taxable income.


310. An increase in adjusted gross income sometimes can be advantageous because adjusted gross income determines the maximum amount of charitable contributions that a taxpayer may deduct for the taxable year. I.R.C. § 170(b) (1988). The benefits of the larger deduction for charitable contributions, however, can be reduced if adjusted gross income exceeds the applicable amounts in I.R.C. § 68. For a discussion of the impact of adjusted gross income on the charitable deduction, see supra notes 290-93 and accompanying text.

311. See, e.g., I.R.C. §§ 21(a) (limiting the amount a taxpayer can claim as a credit for dependent care services); 22(d) (reducing the amount of credit for elderly and permanently and totally disabled taxpayers); 32(b) (limiting the amount of the earned income credit); 86(b) (increasing the amount of social security and tier one railroad retirement benefits that a taxpayer must include in gross income); 135(b)(2) (limiting the excludable amount of interest derived from government savings bonds used to fund qualified higher education expenses); 219(g)(2) (reducing the deductible amount of contributions to an individual retirement account where an individual or the individual’s spouse is an active participant in certain pension plans); 469(i)(3) (limiting the deductible amount under the active rental real estate exception to the passive activity loss rules).
The term “adjusted gross income” is defined as gross income minus the deductions listed in section 62 of the Internal Revenue Code. The fact of marriage often increases a married taxpayer’s adjusted gross income as compared with the adjusted gross income of an unmarried taxpayer because the Internal Revenue Code generally requires a married taxpayer to include more in gross income and allows a married taxpayer to take smaller deductions than his or her unmarried counterpart.

a. Gross Income

i. Social Security Benefits

Several provisions of the Internal Revenue Code require a married taxpayer to include more in gross income than an unmarried taxpayer. For example, a taxpayer who receives social security benefits may be required to include a portion of the benefits in income.\(^{312}\) Under section 86 of the Internal Revenue Code, a recipient of social security benefits\(^{313}\) usually must include one-half of the benefits in income. The taxpayer may exclude the entire amount of the benefits from income, however, if the taxpayer’s adjusted gross income is sufficiently low.\(^{314}\)

Section 86 permits a taxpayer to exclude social security benefits from income if the sum of one-half of the social security benefits and the taxpayer’s “modified adjusted gross income” does not exceed a “base amount.” The term “modified adjusted gross income” is defined as adjusted gross income, excluding social security benefits, increased by tax-exempt interest and certain amounts that otherwise would be excludable because the taxpayer resides outside the United States.\(^{315}\) The “base amount” generally is $25,000 except that in the case of a joint return, the base amount is $32,000.\(^{316}\) In the case of a married taxpayer


\(^{313}\) For this purpose, the term “social security benefit” also includes certain amounts received under the Railroad Retirement Act of 1974. I.R.C. § 86(d) (1988).

\(^{314}\) I.R.C. § 86 requires a taxpayer to include in income the lesser of one-half of the social security benefits received during the year or one-half of the excess of the amount by which the sum of one-half of the social security benefits plus the taxpayer’s modified adjusted gross income exceeds a base amount. The term “modified adjusted gross income” means adjusted gross income (excluding social security benefits) increased by tax-exempt interest, earned income from foreign sources that is excluded under I.R.C. § 911, and income of a resident of Puerto Rico, Guam, American Samoa, or the Northern Mariana Islands that is excluded under I.R.C. § 931 or § 933. I.R.C. § 86(b)(2) (1988). The base amount is $25,000 unless the taxpayers file a joint return, in which case the base amount is $32,000. I.R.C. § 86(c)(1), (2) (1988). In the case of a spouse who does not live apart from the other spouse for the entire taxable year and who files a separate return, the base amount is zero. I.R.C. § 86(c)(3) (1988).


\(^{316}\) I.R.C. § 86(c)(1), (2) (1988).
who files a separate return, however, the base amount is zero unless the taxpayer has lived apart from his or her spouse for the entire taxable year.317

The disparity in the base amounts effects a marriage bonus for some and a marriage penalty for others. When only one spouse receives benefits and has modified adjusted gross income, the fact of marriage permits the taxpayer to use a higher base amount in determining the excludable amount of the social security benefits. If both spouses have income, however, not only is the income combined in determining whether modified adjusted gross income plus one-half of the benefits exceed the base amount, but the base amount is $32,000 instead of the two $25,000 amounts that each taxpayer could use if the two were unmarried.

The greatest impact of the section 86 computation falls upon a married spouse who files a separate return during the first year of separation. Such a person must pay tax on one-half of the social security payments even if the spouse has no income from other sources. The spouse might escape taxation on the benefits by filing a joint return, but the income of the other spouse that must be reported on the joint return could, when added to one-half of the social security benefits, exceed the $32,000 base amount that applies to joint returns. A joint return might not even be a possibility if the other spouse refuses to sign it. For purposes of section 86, marital status is determined under the rules that apply with respect to filing status.318 Thus, in Louisiana a separated spouse may suffer a marriage penalty under section 86 unless the abandoned spouse rule applies. If the recipient of the benefits could obtain a legal separation before the end of the taxable year, the taxpayer could enjoy the benefit of a $25,000 base amount.

ii. Employer-Provided Day Care

Section 129 of the Internal Revenue Code can make employer-provided day care more expensive for married taxpayers than for their unmarried counterparts. Section 129 permits a taxpayer to exclude up to $5,000 of employer-provided day care assistance.319 A married taxpayer who files a separate return, however, may not exclude more than $2,500 of such assistance.320 A marriage penalty results in cases where two

taxpayers, each with employer-provided day care, marry, reducing the $10,000 aggregate exclusion for two unmarried taxpayers to $5,000. The separate filer loses one-half of the $5,000 maximum exclusion, regardless of whether the separate filer’s spouse is also entitled to claim an exclusion under section 129. If the taxpayer qualifies as unmarried because the taxpayer is legally separated or divorced or is considered unmarried under the abandoned spouse rule, the taxpayer may exclude up to $5,000 of such assistance on a separate return. Under these rules, a Louisiana spouse who is separated from his or her spouse generally must include additional amounts in income during the first year of separation unless the spouse files a joint return.

Section 129 further reduces the excludable amount for a married taxpayer whose spouse has little or no earned income. Section 129(b) limits the amount of the exclusion for married taxpayers to the lesser of the earned income of either spouse. Thus, in cases where one spouse has only investment income and the other receives employer-provided dependent care assistance, the entire amount of the assistance must be included in income, whether a joint or separate return is filed. A taxpayer who separates from his or her unemployed spouse also must include in income the full amount of employer-provided dependent care assistance unless the taxpayer is considered unmarried. If the community

323. Under the abandoned spouse rule for purposes of I.R.C. § 129, an otherwise "married" taxpayer is considered unmarried if: (1) the taxpayer files a separate return, (2) the taxpayer furnishes over one-half of the cost of maintaining as his home a household which constitutes for more than one-half of the year the principal place of abode of a dependent of the taxpayer, and (3) during the last six months of the taxable year, the taxpayer's spouse is not a member of the household. I.R.C. §§ 129(a)(2)(C), 21(e)(4) (1988). Under these rules, a taxpayer who separates from his or her spouse after June 30, will be considered married unless there is a decree of divorce or legal separation by December 31. If the community is still in existence and I.R.C. § 66 does not apply, a taxpayer will fail to qualify as unmarried even if the taxpayer's spouse was not a member of the taxpayer's household for the entire taxable year because of the requirement that the taxpayer furnish over one-half of the cost of maintaining the household. While the community is in existence, the spouse only furnishes exactly one-half of the cost. Cf. Abrams v. Commissioner, 57 T.C.M. (CCH) 1433, 1436 (1989) (for purposes of determining whether a taxpayer has furnished over one-half of the cost of maintaining a household for purposes of filing as head of a household, the total support of the household is allocable evenly to parents during the period the marital community exists); Tech. Adv. Mem. 77-40-006 (June 20, 1977) (same).

324. I.R.C. § 129(b)(1) (1988). If the nonearning spouse is a student or incapable of caring for himself, the nonearning spouse will be deemed to earn $200 a month if the family includes only one dependent under the age of thirteen or one dependent or spouse who is physically or mentally incapable of caring for himself. I.R.C. §§ 129(b)(2), 21(b)(1), (d)(2) (1988). If the family includes two or more such individuals, the nonearning spouse is deemed to earn $400 per month. I.R.C. §§ 129(b)(2), 21(d)(2) (1988).
is in existence, the taxpayer will fail to qualify as unmarried and therefore, will be required to include all of such assistance in income during the subsequent years as well. Of course, the existence of the community in such a case places an additional burden on the unemployed spouse. Under the Seaborn rule, the unemployed spouse is liable for the tax on one-half of the community income which includes the full amount of the employer-provided dependent care assistance. If legal separation were available, separated spouses in Louisiana could achieve greater tax savings under section 129.

iii. Interest From Government Bonds Used to Pay Higher Education Expenses

Section 135 of the Internal Revenue Code has a marriage bonus penalty effect on the computation of adjusted gross income. Under section 135 a taxpayer may exclude from income interest earned on Series EE bonds redeemed to pay the taxpayer's "qualified higher education expenses." Qualified higher education expenses generally are tuition and fees incurred by the taxpayer for enrollment or attendance of the taxpayer, the taxpayer's spouse, or the taxpayer's dependent at a college, university, or vocational school. The amount of the exclusion is phased out for taxpayers who have high income. The income lim-

325. If the community is in existence, the taxpayer will not be able to meet the requirement of furnishing over one-half the cost of maintaining a household to qualify as an abandoned, and therefore, unmarried spouse. See supra note 192. Any support payments made to the unemployed spouse in post-separation years could preclude application of I.R.C. § 66(a), thereby assuring the continuance of the community unless the spouses cause it to terminate by partitioning, obtaining a judgement of separation of property, or obtaining a divorce. See supra note 83 and accompanying text.

326. I.R.C. § 135(a), (b)(1) (Supp. 1991). To qualify, the bonds must be issued after December 31, 1989, and the taxpayer must have attained the age of twenty-four before the date of issuance. I.R.C. § 135(c)(1) (1988). This rule assures that the benefits of I.R.C. § 135 are not available to wealthy taxpayers. The income limitations under I.R.C. § 135(b)(2) prevent taxpayers with high incomes from excluding the interest. The twenty-four-year age limit prevents a wealthy taxpayer from purchasing bonds in his child's name and permitting the child to redeem them later when the child is in a low income bracket.


328. The phase-out begins when the taxpayer's 1992 "modified adjusted gross income" exceeds $44,150 ($66,200 in the case of a joint return). I.R.C. § 135(b)(2)(A) (Supp. 1991); Rev. Proc. 91-65 § 7, 1991-2 C.B. 867, 869. For purposes of I.R.C. § 135, modified adjusted gross income is the taxpayer's adjusted gross income for the year increased by certain amounts that would otherwise be excludable because the taxpayer resided outside the United States after taking into account includable social security benefits, deductible passive losses, and the deduction for contributions to an investment retirement account. I.R.C. § 135(c)(4) (Supp. 1991). A taxpayer who has modified adjusted gross income in excess of the applicable amount must reduce the otherwise excludable amount under a formula that requires the taxpayer to multiply the otherwise excludable amount by a fraction, using the excess of
TAX, SEPARATION, AND DIVORCE

Limitations vary depending on whether the taxpayer is unmarried or files a joint return, generally creating a marriage bonus for a one-earner couple and a marriage penalty for a two-earner couple. No exclusion is allowed if a married individual files a separate return. For purposes of section 135, a taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies. Under these rules, a separated spouse in Louisiana who does not meet the requirements of the abandoned spouse rule must include in income the full amount of interest earned on bonds used to finance the cost of advanced education for the spouse or for a child unless a joint return is filed. Even if a joint return is filed, the combined income on the return may prevent an exclusion. If the spouses could obtain a legal separation, the interest on the bonds could be tax-free.

iv. Exclusion of Gain From the Sale of a Personal Residence for Taxpayers Who Have Attained the Age of Fifty-Five

Section 121 of the Internal Revenue Code produces a marriage penalty that can affect a separated spouse for a lifetime. Section 121 allows a taxpayer who has reached the age of fifty-five to elect to exclude up to $125,000 of the gain on the sale or exchange of property that the taxpayer has owned and used as a principal personal residence for three of the five years preceding the sale or exchange. A taxpayer may make an election under section 121 only once in a lifetime. A married taxpayer is not permitted to make the election unless the tax-

modified adjusted gross income over the applicable amount as the numerator, and $15,000 ($30,000 in the case of a joint return) as the denominator. I.R.C. § 135(b)(2)(A) (Supp. 1991). In no event will the excludable amount be less than zero. Id. The $44,150 and $66,200 amounts are adjusted annually for inflation. I.R.C. § 135(b)(2)(B) (1988); Rev. Proc. 91-65 § 7, 1991-2 C.B. 867, 869.

332. I.R.C. § 121(a) (1988). To qualify as a principal personal residence, the property must have been owned and used by the taxpayer as a principal personal residence for periods aggregating at least three out of the five years preceding the sale or at least one year during the five-year period if the taxpayer becomes physically or mentally incapable of self care. I.R.C. § 121(a)(2), (d)(9) (1988 & Supp. 1991). The holding period and use of a prior personal residence that was involuntarily converted is treated as the holding period and use of the taxpayer's current residence if I.R.C. § 1033 applied to exclude the gain on the involuntary conversion of the former residence because the taxpayer used the proceeds of the involuntary conversion to purchase the residence for which the I.R.C. § 121 election is made. I.R.C. § 121(d)(8) (1988).
payer's spouse joins in the election. The spouse who joins in the election then will be precluded from ever making another election under section 121, even if the couple later divorces and the spouse remarries. In fact, if a spouse who has joined in a section 121 election divorces and later marries a taxpayer who has never made such an election, the new spouse will not be entitled to claim an exclusion under section 121.

The marriage penalty that results from the limitations of section 121 is obvious. If two unmarried taxpayers each over age fifty-five sell a qualifying residence they can each exclude up to $125,000 of gain on the sale, or an aggregate of $250,000. If they marry and then sell both residences, the maximum exclusion is $125,000, and only one residence will qualify. The maximum exclusion for a married taxpayer filing a separate return is $62,500.

Unmarried taxpayers over age fifty-five who own a qualifying residence as joint tenants or tenants in common each can take advantage of a $125,000 exclusion with respect to the respective share of the gain. Thus, the aggregate exclusion with respect to the jointly owned residence is $250,000. If they marry, any gain in excess of $125,000 cannot be excluded under section 121.

A marriage bonus may result in cases where one of the spouses does not satisfy the age, holding, and use requirements. If a husband and wife own property as joint tenants, tenants by the entirety, or community property, and one spouse satisfies the age, holding, and use requirements, the couple can exclude $125,000 of the gain by filing a joint return. The holding and use requirements satisfied by a deceased spouse will be deemed satisfied by the deceased spouse.

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334. I.R.C. § 121(c) (1988). If the residence is held by the husband and wife as joint tenants, tenants by the entirety, or community property, and they file a joint return, they will qualify for the election even though only one of the spouses meets the age, holding, and use requirements of I.R.C. § 121(a) (1988).


339. See, e.g., Rev. Rul. 67-235, 1967-2 C.B. 79 (brother and sister who were joint owners of their principal residence may each exclude their own gain under I.R.C. § 121 if each meets the age, holding-period, and use requirements); Rev. Rul. 67-234, 1967-2 C.B. 78 (unmarried taxpayer owning a residence as joint tenant or tenant in common may elect to exclude his share of the gain under I.R.C. § 121).

340. If the couple purchases a new residence, the gain may be shielded from recognition if I.R.C. § 1034 applies. Each spouse can take advantage of I.R.C. § 1034 to avoid recognition of his or her individual share of the gain if each purchases a new residence. Rev. Rul. 74-250, 1974-1 C.B. 202. If a spouse does not wish to purchase a new residence or cannot afford one, however, relief will not be available under I.R.C. § 1034.

spouse who has never made a section 121 election can be attributed to
the spouse who survives.\textsuperscript{342}

For purposes of section 121, an individual who is legally separated
from his or her spouse under a decree of divorce or separate maintenance
at the time of the sale or exchange of the residence is considered not
married.\textsuperscript{343} In most cases, Louisiana taxpayers over age fifty-five who
have filed for divorce should wait until the divorce is final before selling
the marital home and making a section 121 election unless one of the
spouses does not qualify for the election and a joint return is contemplated.
Because there is no abandoned spouse rule for purposes of section
121, spouses who separate in Louisiana and do not plan to divorce
cannot avoid the marriage penalties that result under section 121. If
legal separation were authorized in Louisiana, many of these taxpayers
could use the section 121 election more advantageously.

\textit{v. Fringe Benefits}

A marriage bonus results under several provisions of the Internal
Revenue Code that exclude from income fringe benefits received by an
employee or the employee’s spouse. A taxpayer whose employer furnishes
to the taxpayer’s spouse medical care,\textsuperscript{346} a qualified tuition reduction,\textsuperscript{345}
group legal services,\textsuperscript{346} excess capacity services such as stand-by airline
tickets,\textsuperscript{347} employee discounts,\textsuperscript{348} or athletic facilities\textsuperscript{349} could lose the
ability to exclude these items from income if the taxpayer’s marital
status is altered. Separated spouses to whom such benefits are offered
might not wish to obtain a legal separation.\textsuperscript{350} The enactment of pro-
visions authorizing a judgment of separation from bed and board in
Louisiana would not affect separated spouses who wish to take advantage
of the exclusions. Spouses could continue to exclude fringe benefits by
failing to file a petition for a judgment of separation from bed and
board.

\begin{itemize}
  \item[342.] I.R.C. § 121(d)(2) (1988)
  \item[343.] I.R.C. § 121(d)(6) (1988)
  \item[344.] I.R.C. § 105(b) (1988).
  \item[345.] I.R.C. § 117(d) (1988).
  \item[346.] I.R.C. § 120(a) (1988).
  \item[350.] There is no provision in the Internal Revenue Code or in the Regulations defining
  the term “spouse” for purposes of the exclusion from income of the fringe benefits discussed
  in the text. Both the Tax Court and the Second Circuit have held that a person who was
  legally separated from her spouse was a “surviving spouse” for purposes of the federal
  estate tax provisions. See, \textit{e.g.}, Estate of Goldwater v. Commissioner, 64 T.C. 540 (1975),
  \textit{aff’d}, 539 F.2d 878 (2d Cir. 1976). The application of this precedent to an income tax
  case, however, is uncertain. For a discussion of the uncertainty, see \textit{infra} note 454.
\end{itemize}
b. Above-the-Line Deductions

The foregoing discussion of the effect of a taxpayer's marital status on the amount of items that a taxpayer must include in gross income concerned only a portion of the impact of marital status on a taxpayer's adjusted gross income. Marital status also affects the amount and availability of some of the deductions that a taxpayer may deduct from gross income in computing adjusted gross income.

A taxpayer computes his or her adjusted gross income by subtracting from gross income the so-called "above-the-line" deductions listed in section 62 of the Internal Revenue Code. Section 62 does not authorize the deduction of any particular expense; it merely lists the deductions authorized by other provisions of the Internal Revenue Code that can be taken from gross income. The deductions that do not appear in the section 62 list, the so-called "below-the-line" deductions, are itemized deductions which a taxpayer may deduct only if the taxpayer elects to forego the standard deduction. The availability and the amount of some of the above-the-line deductions vary depending on marital status, causing for some a marriage penalty and for others a marriage bonus.

i. Trade or Business Expenses

(a) Bonus Depreciation Under Section 179

An important category of above-the-line deductions includes expenses incurred in a trade or business. Among the trade or business expenses that a taxpayer may deduct above the line, is an allowance for depreciation with respect to certain assets used in the taxpayer's trade or business. A taxpayer who purchases tangible personal property for use in a trade or business that satisfies the requirements of section 179 of the Internal Revenue Code ("section 179 property") may be able to deduct the entire cost of the property in the year of the purchase rather than taking smaller depreciation deductions over the years that constitute the property's recovery period. The time value of money makes the...

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351. I.R.C. § 63(b) (1988). The "line" is adjusted gross income. The deductions listed in I.R.C. § 62 are subtracted from gross income, so that the taxpayer can determine his or her adjusted gross income. Itemized deductions are subtracted from adjusted gross income.

352. I.R.C. § 62(a)(1) (1988). If the trade or business consists of the performance of services by the taxpayer as an employee, however, most unreimbursed expenses are not deductible above the line. Id.; § 62(a)(2) (1988).


354. Section 179 property generally consists of tangible, depreciable personal property that the taxpayer has purchased for use in the active conduct of a trade or business. I.R.C. § 179(d)(1) (1988).
accelerated deduction under section 179 advantageous to taxpayers.\textsuperscript{355} The rules for the application of section 179 can effect a marriage penalty or a marriage bonus, depending on the circumstances.

Under section 179, a taxpayer may elect to deduct, rather than capitalize and depreciate, up to $10,000 of the cost of a section 179 property.\textsuperscript{356} The deduction is allowed for the taxable year in which the property is placed in service.\textsuperscript{357} A taxpayer may make an election with respect to all or a portion of the cost of one asset or several assets,\textsuperscript{358} but the total deduction for all section 179 property placed in service during the taxable year cannot exceed $10,000.\textsuperscript{359}

A taxpayer who places more than $210,000 of section 179 property in service during the year cannot expense any of it under section 179. The $10,000 limit is reduced by the amount by which the cost of section 179 property placed in service during the year exceeds $200,000.\textsuperscript{360} Thus, for example, a taxpayer who places $203,000 of section 179 property in service during the year may only expense $7,000 of it under section 179.

After the reduction, if any, attributable to the amount of section 179 property placed in service during the year, the $10,000 limitation is further limited to the aggregate amount of taxable income derived from the active conduct by the taxpayer of any trade or business during the taxable year.\textsuperscript{361} In determining the amount of active trade or business income, the taxpayer may aggregate all such income, including income derived from the trade or business of being an employee.\textsuperscript{362}

For purposes of applying the $10,000 limitation and for determining the cost of section 179 property placed in service during the year, a

\textsuperscript{355} A taxpayer who elects to expense an asset under I.R.C. §179 must reduce the depreciable basis of the asset by the amount of the §179 deduction. Prop. Treas. Reg. §1.179-1(f), 56 Fed. Reg. 12868 (1991). The reduced basis will in turn result in smaller depreciation deductions with respect to the expensed asset in later years. Because of the time value of money, the taxpayer benefits from the larger deductions in the first year that the asset is placed in service. The taxpayer could invest the tax savings achieved in the first year, earning income that would not be produced if the taxpayer waited to take the deduction in later years. For a discussion of the time value of money, see supra note 111 and accompanying text.  
\textsuperscript{357} I.R.C. §179(a) (1988)  
\textsuperscript{358} I.R.C. §179(c)(1) (1988).  
\textsuperscript{360} I.R.C. §179(b)(2) (1988).  
\textsuperscript{361} I.R.C. §179(b)(3) (1988). For this purpose, taxable income is computed without regard to the deduction allowable under I.R.C. §179. I.R.C. §179(b)(3)(C) (1988). Amounts that are disallowed because of the taxable income limitation are carried forward, to be used as a deduction in future years, subject to the dollar limitations and active trade or business income limitations discussed in the text. I.R.C. §179(b)(3)(B) (1988).  
husband and a wife are treated as one taxpayer, whether they file a joint return\textsuperscript{363} or each files a separate return.\textsuperscript{364} Thus, the maximum amount of the so-called "bonus depreciation" that both spouses may deduct under section 179 is $10,000, and the cost of section 179 property that each spouse has purchased is aggregated to determine whether the cost of such property purchased during the taxable year exceeds $200,000. The marriage penalty is obvious: if the taxpayers were not married, each could claim up to $10,000 of bonus depreciation, resulting in an aggregate deduction of $20,000, and neither taxpayer would have to take into account the other's purchases of section 179 property during the year. Separated spouses who qualify as unmarried can avoid the marriage penalty resulting from the $10,000 limitation on the amount of bonus depreciation allowable under section 179.

An additional limitation applies to married taxpayers who file separate returns. Once the spouses aggregate the cost of section 179 property that each has placed in service during the year, the maximum amount of bonus depreciation that either spouse can deduct is one-half of the otherwise allowable amount, unless both spouses make an election to share the allowable bonus depreciation unequally.\textsuperscript{365} Thus, in a case where a husband places $195,000 of section 179 property in service during the year, and his wife places $9,000 of such property in service during the same taxable year, the total amount of bonus depreciation that the spouses may deduct is $6,000.\textsuperscript{366} If they file separate returns, each may claim up to $3,000 of bonus depreciation unless they agree to share the $6,000 amount differently and each makes an election on his or her separate return.\textsuperscript{367} If one spouse claims $3,000 of bonus depreciation, the other cannot claim more than 3,000.\textsuperscript{368} These rules often require separated spouses to cooperate in order to obtain the greatest aggregate tax savings under section 179. Such cooperation may be unattainable.

For purposes of applying these rules, a taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies.\textsuperscript{369} A provision authorizing a decree of legal separation in Louisiana could help some separated spouses to use section 179 to achieve greater tax savings.

\begin{footnotes}
\item[367] Id.
\item[369] Id.
\end{footnotes}
Section 179 has one marriage bonus feature. Spouses who file a joint return may aggregate their income for purposes of determining the amount of the taxpayer's active trade or business income.\(^{370}\) Thus, the active trade or business income of one spouse may increase the amount of bonus depreciation allowable with respect to property placed in service by the other spouse. Of course, spouses who file separate returns are not permitted to aggregate their income for purposes of the taxable income limitation.\(^{371}\) The ability to obtain a judgment of separation from bed and board would not prevent separated spouses from taking advantage of the marriage bonus feature of section 179. Separated spouses who cooperate well enough to file a joint return could take advantage of any bonus that would result by foregoing a separation from bed and board.

**(b) Reforestation Expenses**

When both spouses are in the timber business, a marriage penalty can result with respect to their reforestation expenses.\(^{372}\) Reforestation costs are the direct costs incurred in connection with forestation or reforestation by planting or artificial or natural seeding, including costs (1) for the preparation of the site, (2) of seeds or seedlings, and (3) for labor and tools, including depreciation of equipment used in planting or seeding.\(^{373}\) Such expenses are capital expenditures, which generally must be added to the adjusted basis of the timber and recovered later through a depletion allowance as the timber is cut or as adjusted basis of the timber when it is sold.\(^{374}\) Section 194 of the Internal Revenue Code allows a taxpayer to amortize, over an eighty-four-month period, up to $10,000 of qualifying reforestation expenses.\(^{375}\) The maximum amount of such expenses that can be amortized by a married taxpayer who files a separate return is $5,000.\(^{376}\) Reforestation expenses that qualify for amortization under section 194 also qualify for an investment tax credit under section 46 of the Internal Revenue Code.\(^{377}\) A taxpayer may claim the credit whether or not the taxpayer elects to amortize the reforestation costs.\(^{378}\) The maximum amount of reforestation expenses


\(^{373}\) I.R.C. § 194(c)(3) (1988).


\(^{376}\) Id.


that a taxpayer can claim as a credit is $10,000 ($5,000 in the case of a taxpayer who is married and files a separate return).

Under these rules separated spouses who are considered unmarried can amortize a maximum of $20,000 of reforestation expenses and can claim a maximum credit of $20,000 in the aggregate. If they are considered married, the maximum amount that qualifies for amortization and/or credit is $10,000. For purposes of applying these rules, a taxpayer is not considered married if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies. A provision in the Louisiana Civil Code authorizing legal separation could result in federal income tax savings to some separated spouses with respect to reforestation expenses.

(c) Passive Activity Losses

While a taxpayer may deduct most business expenses above the line, there may be a limit on the amount of expenses that the taxpayer may deduct if the business is a passive activity. The passive activity loss rules contain both marriage bonus and marriage penalty provisions.

In general, an individual taxpayer may deduct expenses attributable to a passive activity only to the extent that the taxpayer has income from passive activities. The term "passive activity" is defined generally as: (1) any activity involving the conduct of a trade or business in which the taxpayer does not materially participate, or (2) any rental activity. Congress enacted the passive activity loss rule to curtail the use of tax shelters. In general, the passive activity loss rules prevent a taxpayer from using net losses from passive activities such as limited partnerships and real estate rental activities to "shelter," or reduce, either income...

382. For the rules limiting the deductibility of expenses attributable to passive activities, see I.R.C. § 469 (1988). The rules apply to individuals, estates, trusts, certain closely held C corporations, and personal service corporations. I.R.C. § 469(a)(2) (1988). I.R.C. § 469(a)(1) disallows a taxpayer's "passive activity loss" and "passive activity credit" for the year. A taxpayer's "passive activity loss" is a net loss, defined as the amount by which the aggregate losses from all passive activities exceed the aggregate income from all passive activities for the taxable year. I.R.C. § 469(d)(1) (1988). The term "passive activity credit" means the amount by which credits other than the foreign tax credit that are attributable to passive activities exceed the regular tax liability of the taxpayer attributable to passive activities for the year. I.R.C. § 469(d)(2) (1988).
383. I.R.C. § 469(c)(1), (2) (1988). A working interest in any oil and gas property which the taxpayer holds directly or through an entity that does not limit the taxpayer's liability, however, is not a passive activity, regardless of any lack of material participation by the taxpayer. I.R.C. § 469(c)(3)(A), (4) (1988).
from active businesses, such as salaries and fees, or portfolio income, such as interest and dividends.385

Net losses from a trade or business, other than a rental business, in which a taxpayer materially participates, on the other hand, generally can be used to offset income from any other activity, whether the activity is active or passive or generates portfolio income, unless some other provision of the Internal Revenue Code restricts the deduction.386

Thus, it often is advantageous for a taxpayer to establish that the taxpayer materially participated in a business that generates net losses.387

A taxpayer is treated as materially participating in an activity if the taxpayer is involved in the operations of the activity on a regular, continuous, and substantial basis.388 The Regulations interpreting the passive activity loss rules provide safe harbor tests for establishing material participation, generally based on the number of hours that the taxpayer has devoted to the activity during the taxable year.389 In determining whether a taxpayer has materially participated in an activity, any participation by the taxpayer's spouse is attributed to the taxpayer.390

It is not necessary for the spouse to own an interest in the activity, nor is it necessary for the spouses to file a joint return for the spouse's participation to be considered for purposes of establishing material participation.391 A spouse's participation is not attributed to a taxpayer, however, if the taxpayer is legally separated from the spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies.392 Thus, separated spouses who wish to aggregate their participation in a business activity in order to avoid application of the passive activity loss rules will not want to obtain a legal separation. The authorization of legal separation in Louisiana will not prevent spouses from aggregating their participation for purposes of the passive

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385. For a discussion of the passive activity loss rules, see 1 Bittker & Lokken, supra note 46, at ¶ 28.
386. For other limitations on the deduction of net losses see, e.g., I.R.C. § 704(d) (limiting the amount of partnership losses a partner may deduct to the partner's basis in his or her partnership interest); 465 (1988) (permitting a taxpayer to use net losses incurred in one activity to offset income derived from another activity only to the extent that the taxpayer has placed capital or personal credit at risk in the activity generating the losses); 1366(d) (limiting the amount of S corporation losses than a shareholder may deduct to the shareholder's basis in stock or debt of the corporation).
387. If a business generates a net profit, it could be advantageous for the taxpayer to establish a lack of material participation in order to characterize the income from the business as passive income. The taxpayer then could use net loses from passive activities to offset the income from the business.
392. Id.
activity loss rules. Separated spouses who wish to take advantage of the spousal attribution provisions may continue to do so if neither spouse files a petition for a judgment of separation from bed and board.

Congress carved out an exception to the passive activity loss rules for a taxpayer who actively participates in a rental real estate activity. A natural person may offset active or portfolio income with up to $25,000 of net losses attributable to all rental real estate activities in which the taxpayer actively participated during the year. A taxpayer is considered to be an active participant if the taxpayer owns at least a ten percent interest in the rental real estate activity and participates in a significant and bona fide sense in the activity. To be an active participant, a taxpayer need not satisfy the rules of the material participation test. Active participation can be established if the taxpayer makes management decisions, such as approving capital or repair expenditures, or arranges "for others to provide services (such as repairs)."

For purposes of determining whether a taxpayer has actively participated in a rental real estate activity, both the interest owned and any participation by the taxpayer's spouse are attributed to the taxpayer. In this respect, the so-called "active rental real estate exception" to the passive activity loss rules provides a marriage bonus. Separated spouses wishing to aggregate their ownership interests and participation in a rental real estate activity may not wish to obtain a judgment of separation from bed and board. The availability of a judgment of separation from bed and board in Louisiana will not prevent separated spouses who do not file for the judgment from taking advantage of spousal attribution under the active rental real estate exception to the passive activity loss rules.

The marriage penalty provisions of the active rental real estate exception, however, may make a legal separation an important option.

393. I.R.C. § 469(i)(1) (1988). The allowance also applies to up to $25,000 of the deduction equivalent of the passive activity credit for any taxable year which is attributable to all rental real estate activities in which the taxpayer actively participated. Id.
394. I.R.C. § 469(i)(6)(A) (1988). If the interest is a limited partnership interest in the real estate activity, however, the taxpayer will not be considered an active participant no matter how great an interest the taxpayer owns in the activity. I.R.C. § 469(i)(6)(C) (1988).
396. Id.
398. Marital status is not defined for all purposes of the passive activity loss rules. In determining whether a spouse's participation is attributable to the taxpayer, however, the taxpayer is considered unmarried if there is a legal separation or if the abandoned spouse rule applies. Temp Treas. Reg. § 1.469-5T(f)(3) (as amended in 1989). This article assumes that the same rules apply in determining whether the interests of the spouses should be aggregated.
The amount of active rental real estate losses that a taxpayer may deduct is phased out for taxpayers who have adjusted gross income in excess of $100,000.\(^{399}\) The $25,000 ceiling for active rental real estate losses is reduced by fifty percent of the amount by which the taxpayer’s adjusted gross income exceeds $100,000.\(^{400}\) Thus, a taxpayer with adjusted gross income in excess of $150,000 cannot take advantage of the active rental real estate exception to the passive activity loss rules.\(^{401}\)

The active rental real estate exception is even more limited for a married individual who files a separate return. Such a separate filer is denied the $25,000 allowance unless the taxpayer lives apart from his or her spouse for the entire taxable year, regardless of the taxpayer’s adjusted gross income.\(^{402}\) A separate filer who lives apart from his or her spouse for the entire taxable year loses at least one-half of the allowance. The maximum amount of active rental real estate losses that a married separate filer can use to offset active or portfolio income is $12,500.\(^{403}\) The $12,500 ceiling is reduced by fifty percent of the amount by which the separate filer’s adjusted gross income exceeds $50,000.\(^{404}\)

Under these rules separated spouses in Louisiana who do not meet the requirements of the abandoned spouse rule must file a joint return for the first year of their separation to take advantage of the active rental real estate exception to the passive activity loss rules. Even after the first year of separation, a joint return may be necessary to take the fullest advantage of the exception. As has been explained, filing a joint return requires a degree of trust and cooperation that may not be present in the context of a separation.\(^{405}\) If the spouses could obtain a judgment of separation from bed and board, each spouse could use up to $25,000 of active rental real estate losses to offset active or portfolio income.

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399. I.R.C. § 469(i)(3) (1988). For this purpose adjusted gross income is determined without regard to: (1) social security benefits that are includable in gross income under I.R.C. § 86, (2) interest earned from government bonds used to pay qualified higher education expenses, excluded under I.R.C. § 135, (3) contributions to an individual retirement account that are deductible under I.R.C. § 219, and (4) any passive activity loss. I.R.C. § 469(i)(3)(E) (1988 & Supp. 1991).

400. I.R.C. § 469(i)(3)(A) (1988). With respect to a passive activity loss credit attributable to a rehabilitation credit, there will be no phase out until the taxpayer’s adjusted gross income exceeds $200,000. I.R.C. § 469(i)(3)(B) (1988). There is no phase out under this rule for a passive activity credit attributable to a low-income housing credit. I.R.C. § 469(i)(3)(C) (1988).

401. The $25,000 allowance is reduced by $25,000, or fifty percent of the $50,000, the amount of the taxpayer’s adjusted gross income in excess of $100,000.


405. See supra notes 231-233 and accompanying text.
and the $25,000 ceiling would not be reduced until adjusted gross income of the spouse claiming the deduction or credit exceeded $100,000.

ii. Expenses of a Qualified Performing Artist

The rules concerning the deduction of business expenses incurred by performing artists can result in a marriage penalty. Unreimbursed employee business expenses of a qualified performing artist are deductible above the line.\textsuperscript{406} The unreimbursed employee business expenses of other taxpayers are miscellaneous itemized deductions, not only deductible below the line, but also deductible only to the extent that they exceed two percent of the taxpayer's adjusted gross income.\textsuperscript{407} The limitation on miscellaneous itemized deductions often prevents the deduction of unreimbursed employee business expenses incurred by a taxpayer other than a qualified performing artist.

To be able to deduct the unreimbursed expenses above the line, a performing artist must satisfy several requirements, including a requirement that the artist's adjusted gross income for the taxable year not exceed $16,000.\textsuperscript{408} A married performing artist who has not lived apart from his or her spouse for the entire taxable year may not deduct the unreimbursed expenses above the line unless the performing artist files a joint return.\textsuperscript{409} If the combined adjusted gross income on the joint return exceeds $16,000, the unreimbursed employee business expenses


\textsuperscript{408} I.R.C. § 62(b)(1)(C) (1988). For this purpose, adjusted gross income is determined without taking into account any deduction for the unreimbursed expenses. \textit{Id.} The performing artist will not qualify for the above-the-line deduction of unreimbursed employee business expenses unless the following requirements are also met: (1) the individual performed services in the performing arts as an employee during the taxable year for at least two employers, and (2) the aggregate amount of the individual's unreimbursed employee business expenses exceeds ten percent of the individual's gross income attributable to the performance of such services. I.R.C. § 62(b)(1)(A), (B) (1988). An individual is not treated as performing services in the performing arts as an employee for any employer unless the amount received for the performing arts services exceeds $200. I.R.C. § 62(b)(2) (1988).

are not deductible above the line. For this purpose, the performing artist is considered not married if the performing artist is legally separated from his or her spouse under a decree of divorce or separate maintenance as of the close of the taxable year.

Under these rules a Louisiana performing artist whose adjusted gross income is less than $16,000 and who is separated from his or her spouse must file a joint return to qualify for an above-the-line deduction of unreimbursed employee business expenses during the first year of separation. Even if the artist and the spouse cooperate well enough to file a joint return, the combined adjusted gross income on the return could easily exceed $16,000, eliminating the ability to deduct the expenses above the line. If the community remains in existence, the community income earned by the performing artist's spouse could cause the performing artist's adjusted gross income to exceed the $16,000 threshold on a separate return. A legal separation would not only eliminate the joint return requirement but would also terminate the community, making it easier for the performing artist to deduct unreimbursed employee business expenses above the line.

iii. Losses From the Sale or Exchange of Property

(a) Capital Losses

A taxpayer also may deduct above the line allowable losses from the sale or exchange of property. There is a limitation, however, on the amount that can be deducted if a loss is attributable to the sale or exchange of a capital asset. The maximum amount of such capital losses that an individual taxpayer may deduct in any year is the amount

412. In years after the first year of separation the performing artist could be relieved of income attribution under the Seaborn rule if I.R.C. § 66 applies. Under I.R.C. § 66(a) (1988), performing artist who lives apart from his or her spouse for the entire calendar year will qualify for relief from the Seaborn rule with respect to all community income except income derived from community property unless earned community income is transferred between the spouses. I.R.C. § 66(a) (1988). A performing artist receiving spousal support, (which could be necessary for a person earning less than $16,000 a year) must satisfy the stringent requirements of I.R.C. § 66(c) to avoid application of the Seaborn rule. For a discussion of the difficulty of qualifying for relief under I.R.C. § 66(c), see supra notes 89-97 and accompanying text. If there is significant income earned from community property, the performing artist could have adjusted gross income in excess of $16,000, regardless of whether the performing artist has any access to the income from the property.
414. I.R.C. §§ 165(f), 1211, 1212 (1988). In general, a capital asset is an asset held for investment. See I.R.C. § 1221 (1988) (defining the term "capital asset" to include all property except the property listed in subsections (1) through (5) of I.R.C. § 1221). Congress causes
of gains recognized from the sale or exchange of capital assets plus $3,000.\textsuperscript{415} A taxpayer who is married and files a separate return may deduct capital losses to the extent of capital gains plus a maximum of $1,500.\textsuperscript{416}

The limitation on the deductibility of capital losses results in a marriage bonus when a spouse who has capital losses in excess of $3,000 can use the other spouse’s capital gains to offset the losses by filing a joint return. When each of the spouses has net capital losses in excess of $1,500, however, a marriage penalty results. A separated spouse who files a separate return can neither use the other spouse’s capital gains to offset capital losses\textsuperscript{417} nor deduct more than $1,500 of net capital losses for the year. While an individual taxpayer carries forward disallowed capital losses indefinitely,\textsuperscript{418} the time value of money makes a current deduction worth more than a deferred deduction. The Louisiana Legislature could help some separated spouses obtain larger current capital loss deduction by permitting them to obtain a legal separation, thereby qualifying as unmarried for federal income tax purposes.\textsuperscript{419} Those spouses who would like to pool their capital gains and losses on a joint

\textsuperscript{415} I.R.C. § 1211(b) (1988).

\textsuperscript{416} I.R.C. § 1212(b) (1988).

\textsuperscript{417} Of course, if the community is still in existence, the separated spouse will include in income one-half of the community capital gains and will be entitled to deduct one-half of the community capital losses, subject to the $1,500 limit that applies to net capital losses. Johnson v. Commissioner, 72 T.C. 340, 347 (1979); Stewart v. Commissioner, 35 B.T.A. 406, 411 (1937), aff’d 95 F.2d 821, 822 (5th Cir. 1938); I.R.S. Pub. no. 555, supra note 31, at 2.

\textsuperscript{418} I.R.C. § 1212(b) (1988).

\textsuperscript{419} I.R.C. § 1211(b), limiting the amount of capital losses that an individual taxpayer may deduct in a taxable year, provides no definition of marital status. Nor do the Regulations promulgated under I.R.C. § 1211 define marital status. This article assumes that Congress’s reference in I.R.C. § 1211(b)(1) to “a married individual filing a separate return” incorporates the definition of marital status that applies for purposes of determining a taxpayer’s filing status. For such purposes, an individual taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse or if the abandoned spouse rule applies. I.R.C. §§ 1(a), (c), (d); 2(c); 7703 (1988).
return could do so by failing to file a petition for separation from bed and board.

(b) Section 1244 Stock

Section 1244 of the Internal Revenue Code offers a marriage bonus to taxpayers. Section 1244 permits a taxpayer to deduct, as ordinary losses, losses on the sale, exchange, or worthlessness of the stock of certain small business corporations that would otherwise be treated as capital losses.\textsuperscript{420} The maximum amount that can be deducted as an ordinary loss under section 1244 is $50,000, or $100,000 in the case of a joint return.\textsuperscript{421} Thus, in a case where one spouse has qualified losses in excess of $50,000, the couple may achieve aggregate tax savings by filing a joint return. If the spouses are legally separated under a decree of divorce or separation, however, they will not be able to take advantage of the more generous deduction because joint filing will be unavailable to them.\textsuperscript{422} The availability of legal separation in Louisiana would not prevent separated spouses who cooperate well enough to file a joint return from taking advantage of the marriage bonus under section 1244. To be eligible to file a joint return, the spouses merely should not seek a judgment of separation from bed and board.

iv. Contributions to an IRA

Contributions to an individual retirement account ("IRA") are deductible above the line.\textsuperscript{423} The maximum amount that can be contributed to an IRA in any taxable year is $2,000.\textsuperscript{424} Section 219 of the Internal Revenue Code limits the amount of such contributions that an individual may deduct to the lesser of $2,000 or the amount of compensation

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\textsuperscript{420} I.R.C. § 1244(a) (1988). The loss will qualify as ordinary if: (1) at the time the stock was issued, the aggregate amount of money and adjusted basis of property received by the corporation as a contribution to capital and paid-in surplus did not exceed $1,000,000, (2) the stock was issued for money or property other than stock or securities, and (3) during the five most recent years before the loss was sustained (or the period the corporation was in existence if less than five years), more than one-half of the corporation's gross receipts were from sources other than royalties, rents, dividends, interest, annuities, and sales or exchanges of stock. I.R.C. § 1244(c) (1988).

\textsuperscript{421} I.R.C. § 1244(b) (1988).

\textsuperscript{422} I.R.C. § 603(d)(2) (1988).

\textsuperscript{423} I.R.C. §§ 62(a)(7), 219(a) (1988).

includable in the taxpayer’s gross income for the year. The maximum deduction is computed separately for each individual. Thus, if a husband and wife both have sufficient compensation, each can establish a separate IRA, and together they can deduct a maximum of $4,000 on a joint return. Community income, however, will not qualify a non-earning spouse for the deduction.

Section 219 provides a small marriage bonus to couples who file a joint return if one of the spouses has no compensation for the year. In that case, the spouse with compensation may establish a separate IRA for the nonworking spouse, known as a spousal IRA. The maximum deduction a couple can claim for IRA contributions under the spousal IRA provisions is $2,250.

A marriage penalty may result under the IRA provisions if one of the spouses is an active participant in a pension plan. In that case,
the $2,250 limit for aggregate contributions to an individual’s IRA and a spousal IRA or the $2,000 limit for each spouse is reduced. The otherwise deductible amounts under the spousal IRA provisions are reduced by twenty-two and one-half cents on the dollar for each dollar of the couple’s adjusted gross income in excess of $40,000.\textsuperscript{433} The reduction is twenty cents on the dollar for each dollar of adjusted gross income in excess of $40,000 in cases where one or both of the spouses otherwise qualify for a $2,000 IRA deduction.\textsuperscript{434}

Thus, when one of the spouses is an active participant in a retirement plan, and the couple’s combined adjusted gross income is $45,000, each spouse is entitled to deduct only $1,000, or a total of $2,000 on the joint return, for IRA contributions. If the couple has $50,000 or more of adjusted gross income, no deduction is allowable to either spouse for contributions made to an IRA.

In the case of an unmarried individual who is an active participant in a pension plan, the $2,000 maximum allowable deduction is reduced by twenty cents per dollar for each dollar of adjusted gross income in excess of $25,000.\textsuperscript{435} Thus, an unmarried individual with adjusted gross income of $35,000 or more who actively participates in a pension plan will not be entitled to deduct any amount contributed to an IRA. The different dollar limitations of adjusted gross income that apply depending on a taxpayer’s marital status and the availability of a spousal IRA deduction cause a marriage bonus for one-worker couples. The different dollar limitations and the attribution of one spouse’s participation in a pension plan to the other spouse result in a marriage penalty to two-worker couples.

In the case of a married individual filing a separate return, no matter which spouse is an active participant in a pension plan, the twenty-cent-per-dollar reduction applies to adjusted gross income in excess of zero.\textsuperscript{436} Under these rules, the maximum $2,000 deduction for IRA contributions is eliminated when adjusted gross income on the separate return exceeds $10,000.

\textsuperscript{433} I.R.C. § 219(g)(2)(A), (g)(3)(B)(i) (1988). In no event is the deduction reduced below zero. I.R.C. § 219(g)(1) (1988). The dollar limitation will not be reduced below $200 as long as the couple’s adjusted gross income is less than the amount at which the maximum dollar limit is reduced to zero. I.R.C. § 219(g)(2)(b) (1988). For purposes of determining the amount of the reduction, adjusted gross income is determined by including social security benefits as required under I.R.C. § 86, allowing a deduction for passive activity losses as permitted under I.R.C. § 469, adding interest excludable under I.R.C. § 135 when Series EE bonds are redeemed to pay qualified higher education expenses, and including income earned abroad that is excludable under I.R.C. § 911. I.R.C. § 219(g)(3)(A) (1988 & Supp. 1991).


If the spouses live apart at all times during the taxable year, they will be considered unmarried for purposes of applying the rules reducing the deduction for active participants in pension plans. Thus, a spouse's participation in a pension plan and the stricter rules for separate returns apply to separated spouses only during the first year of separation. If the spouses could obtain a legal separation, thereby qualifying as unmarried during the first year of separation, they might be entitled to deduct larger amounts of their IRA contributions.

### c. Section 1041: Nonrecognition of Gain or Loss With Respect to Interspousal Transfers

Under section 1041 of the Internal Revenue Code, a spouse recognizes neither gain nor loss on the transfer of property to another spouse, regardless of whether or not the transferor spouse receives any consideration. As a consequence of the nonrecognition of gain or loss by the transferor, the transferee spouse takes the property with the same basis as it had in the hands of the transferor, regardless of whether the transferee paid for the property. These rules also apply to former spouses who are legally separated or divorced, however, are generally considered unmarried for federal income tax purposes. Considering legally separated spouses as unmarried does no violence to the policy behind the separate return provision. Congress's purpose in enacting the limitation was to eliminate the incentive for married spouses living together to file separate returns, thereby avoiding the limitations that applied to joint returns under prior law. S. Rep. No. 100-445, 100th Cong., 2d Sess. 132-33 (1988), reprinted in 6 U.S.C.C.A.N. 46 49-50 (1988). If a couple is legally separated under a decree of divorce or separate maintenance, the couple is not entitled to file a joint return. I.R.C. § 6013(d)(2) (1988). Thus, the potential abuse under prior law was not available to legally separated spouses.

Spouses who are legally separated or divorced, however, are generally considered unmarried for federal income tax purposes. Considering legally separated spouses as unmarried does no violence to the policy behind the separate return provision. Congress's purpose in enacting the limitation was to eliminate the incentive for married spouses living together to file separate returns, thereby avoiding the limitations that applied to joint returns under prior law. S. Rep. No. 100-445, 100th Cong., 2d Sess. 132-33 (1988), reprinted in 6 U.S.C.C.A.N. 46 49-50 (1988). If a couple is legally separated under a decree of divorce or separate maintenance, the couple is not entitled to file a joint return. I.R.C. § 6013(d)(2) (1988). Thus, the potential abuse under prior law was not available to legally separated spouses.

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438. For purposes of determining whether a taxpayer is considered an active participant in a pension plan merely because a spouse is an active participant, marital status is determined as of the end of the year. Notice 87-16, 1987-1 C.B. 446, 447 (A4). Thus, if an individual is not married at the end of the year, the fact that the individual's former spouse is an active participant will not be considered in determining whether the individual is an active participant. Id. There is no provision in I.R.C. § 219(g) or the regulations, however, indicating whether individuals who are legally separated under a decree of divorce or separate maintenance are considered unmarried for purposes of the limitations that apply to active participants in pension plans and to their spouses. The only statement concerning marital status with respect to the limitations is that a husband and wife who file separate returns and live apart at all times during the taxable year are considered unmarried. I.R.C. § 219(g)(4) (1988). Arguably, unless the spouses live apart at all times during the taxable year, legally separated spouses are considered married under these rules.


440. I.R.C. § 1041(b) (1988). “Basis” is a term of art used in the Internal Revenue Code. The basis of property generally is its cost. I.R.C. § 1012 (1988). A taxpayer's cost basis in property is adjusted, however, to take into account certain expenditures made by
spouses if the transfer of property is incident to the divorce. A transfer is incident to the divorce if it occurs within one year of the cessation of the marriage or if the transfer is "related to the cessation of the marriage." Regulations promulgated under section 1041 provide that a transfer of property is related to the cessation of the marriage if it is pursuant to a divorce or separation instrument and occurs not more than six years after the date on which the marriage ceases.

Section 1041 is a double-edged sword, often benefitting one spouse or former spouse to the detriment of the other. For example, a taxpayer who purchases stock that is separate property for $1,000 has a $1,000 "cost" basis in the stock. If the stock appreciates in value and the taxpayer sells the stock to his or her spouse for $2,000, section 1041 relieves the taxpayer of any tax liability for the gain. The spouse who paid $2,000 for the stock, however, must take the stock with a basis of $1,000. On a later sale of the stock for $2,000, the transferee spouse must pay tax on the $1,000 gain. Similarly, a spouse who purchases stock with separate funds for $2,000 that declines in value may not deduct the loss on its sale to a spouse for $1,000. The transferee spouse takes a $2,000 basis in the stock, and may recognize a $1,000 loss on its later sale.

Whether the application of section 1041 will result in a tax savings or an increased tax liability to the spouses depends on the circumstances surrounding the transfer. For example, if the property has appreciated

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the taxpayer and certain deductions taken by the taxpayer with respect to the property. For example, the cost basis of property is increased by capital expenditures and decreased by allowable depreciation deductions. For a list of the adjustments made to basis, see I.R.C. § 1016 (1988).

443. Temp. Treas. Reg. § 1.1041-1T(b)(A-7), 49 Fed. Reg. 34453 (1984). For this purpose a "divorce or separation instrument" means: (1) a decree of divorce or separate maintenance or a written instrument incident to such a decree, (2) a separation agreement, (3) a decree requiring a spouse to make support payments to the other spouse, or (4) any modification thereof. Id. I.R.C. § 71(b)(2) (1988). The Regulations provide a rebuttable presumption that any transfer not pursuant to a divorce or separation instrument or that occurs more than six years after the cessation of the marriage is not related to the cessation of the marriage and therefore does not qualify for nonrecognition treatment. Temp. Treas. Reg. § 1.1041-1T(b) (A-7), 49 Fed. Reg. 34453 (1984).
in value and the transferee does not intend to sell\textsuperscript{451} the property or take depreciation deductions\textsuperscript{452} with respect to the property, application of section 1041 benefits both of the spouses. The nonrecognition of loss under section 1041 with respect to a transfer of property that has declined in value results in an aggregate increase in tax liability when the transferee spouse does not sell or depreciate the property.

Spouses can do nothing to avoid application of section 1041 to transfers of property between them.\textsuperscript{453} Former spouses, however, can use section 1041 as a planning device with respect to transfers of property that occur more than one year after the cessation of the marriage. By providing for the transfer of the property in a divorce or separation instrument, former spouses can assure that section 1041 will apply to a transfer that occurs within six years of the cessation of the marriage. Similarly, the former spouses can avoid application of section 1041 by omitting a provision for the transfer in the divorce or separation instrument. The availability of a judgment of separation from bed and board might help separated spouses in Louisiana take better advantage of the rules in section 1041.\textsuperscript{454}

\textsuperscript{451} If the transferee holds the property until he or she dies, the basis of the property in the hands of the transferee's heirs will be the fair market value of the property at the time of the transferee's death. I.R.C. § 1014(a) (1988). In that case, the appreciation in the property will escape federal income taxation forever.

\textsuperscript{452} The transferee will desire to have a higher basis in depreciable property because depreciation deductions are computed by reference to the taxpayer's basis in the property. I.R.C. § 167(c) (1988).

\textsuperscript{453} I.R.C. § 1041 offers limited planning opportunities to married taxpayers. Spouses who live under a separate property regime can use I.R.C. § 1041 to assign the gain or loss on the sale of an asset to the spouse who would receive an advantage from the assignment. For example, a spouse who incurs medical expenses can only deduct the expenses to the extent that they exceed seven and one-half percent of the spouse's adjusted gross income. I.R.C. § 213(a) (1988). To increase the amount of deductible medical expenses, a spouse living under a separate property regime could reduce his or her adjusted gross income by selling at a loss stock received from his or her spouse and reporting both the medical expenses and the loss on a separate return. Of course, the amount of deductible loss on the sale of the stock would be limited to that amount of the spouse's capital gains for the year plus $1,500. I.R.C. § 1211(b) (1988).

\textsuperscript{454} Application of I.R.C. § 1041 to separated spouses, however, is not certain. There is no provision in the Internal Revenue Code or in the Regulations defining the term "spouse", "former spouse", or "cessation of the marriage" for purposes of section 1041. In cases where there is no statutory or regulatory definition of marital status, courts have relied on state law definitions. See, e.g., Deyoe v. Commissioner, 66 T.C. 904, 913-14 (1976) (interpreting California law to determine whether the parties were "husband and wife" for purposes of former I.R.C. § 1239); Estate of Goldwater v. Commissioner, 64 T.C. 540 (1975), aff'd, 539 F.2d 878 (2d Cir. 1976) (defining the term "surviving spouse" for purposes of I.R.C. § 2056). But see Estate of Steffke v. Commissioner, 538 F.2d 730, 732 (7th Cir. 1976) (defining the term "surviving spouse" for purposes of I.R.C. § 2056 and explaining that "[t]he meaning of the words or the legal status of circumstances for federal tax purposes
d. Spousal Attribution

The Internal Revenue Code contains a number of provisions that attribute one spouse's ownership interest in an entity to the other spouse. need not be identical to their meaning or their legal effect under state law"). While it seems that spouses who are legally separated are still married under state law, the Tax Court has interpreted the former provisions of the Louisiana Civil Code authorizing a judgment of separation from bed and board to effect a limited divorce that qualified as a "divorce" for tax purposes. Garsaud v. Commissioner, 28 T.C. 1086 (1957). The application of this interpretation, however, is uncertain with respect to transfers under I.R.C. § 1041. The decision in Garsaud concerned the meaning of the statutory phrase, "legally separated under a decree of divorce or of separate maintenance" that causes taxpayers to be considered unmarried. I.R.C. § 1041 does not designate whether an individual who is legally separated under a decree of divorce or of separate maintenance is considered unmarried.

The operative terms under I.R.C. § 1041 are "spouse," "former spouse," and "cessation of the marriage". In Estate of Goldwater, 64 T.C. 540 (1975), aff'd, 539 F.2d 878 (2d Cir. 1976), both the Tax Court and the Second Circuit held that a New York spouse who had obtained a final decree of separation was a "surviving spouse" within the meaning of I.R.C. § 2056. The decisions in Goldwater, however, do not require a similar interpretation with respect to the meaning of the term "spouse" for purposes of I.R.C. § 1041. Neither court in Goldwater addressed the issue of whether a legally separated spouse is considered a "spouse" under federal income tax law.

The issue in Goldwater concerned the effect of an ex parte Mexican decree of divorce later declared null by a state court with jurisdiction over all of the parties. In Goldwater, Gertrude Goldwater obtained a final decree of separation from Leo Goldwater. Leo then obtained an ex parte decree of divorce in Mexico and married Lee Jablow. When Leo died, he bequeathed to Lee an interest in property equal to or greater than 50 percent of his gross estate. Gertrude sued as a widow for her elective share of Leo's estate and was awarded approximately $206,000. The question in Goldwater was whether the estate could deduct the $395,000 bequeathed to Lee or the $206,000 inherited by Gertrude as an amount left to a "surviving spouse" under I.R.C. § 2056. Both the Tax Court and the Second Circuit deferred to a judgment issued by the New York Supreme Court declaring that Gertrude was the lawful wife of the decedent for purposes of the New York estate tax law. Estate of Goldwater, 64 T.C. at 550; 539 F.2d at 880.

Goldwater involved the construction of a federal estate tax provision. Section 1041 concerns matters of federal income taxation. Income tax provisions are not always construed as though they are in pari materia with the estate tax law. See, e.g., Farid-Es-Sultaneh v. Commissioner, 160 F.2d 812, 814 (2d Cir. 1947). In Goldwater, both the Tax Court and the Second Circuit distinguished their holding from caselaw defining marital status for purposes of the income tax provisions. Goldwater, 64 T.C. at 548-51; 539 F.2d at 881-82. Thus, the determination in Goldwater that a legally separated spouse qualified as a surviving spouse under the estate tax provisions should not constitute binding precedent with respect to the definition of the term "spouse" for purposes of I.R.C. § 1041.

Regulations promulgated under I.R.C. § 1041 seem to equate legal separation with divorce and the cessation of the marriage. Question 2 in the Regulations asks, "Does section 1041 apply only to transfers of property incident to divorce?" Temp. Treas. Reg. § 1.1041-1T(a)(Q-2) (1984). The response is: "No. Section 1041 is not limited to transfers of property incident to divorce . . . . A divorce or legal separation need not be contemplated between the spouses at the time of the transfer nor must a divorce or legal separation ever occur."
The spousal attribution rules sometimes reduce taxable income. More often, however, spousal attribution increases the couple's taxable income. Section 318 treats a taxpayer as the constructive owner of any shares of stock owned by the taxpayer's spouse, whether the stock is community property or separate property. If a taxpayer's spouse is the constructive owner of stock because of the spouse's interest in a partnership, trust, or corporation that owns the stock, or because the spouse


\[456. \text{Stock owned directly or indirectly by a partnership is considered as owned proportionately by its partners. I.R.C. § 318(a)(2)(A) (1988). A partnership is considered the constructive owner of all of the stock owned by its partners. I.R.C. § 318(a)(3)(A) (1988). Stock constructively owned by a partnership by virtue of its ownership by a partner, however, is not reattributed to the other partners. I.R.C. § 318(a)(5)(C) (1988).} \]

\[457. \text{Stock owned directly or indirectly by a trust (other than certain employees' trusts) generally is considered as owned by its beneficiaries in proportion to the actuarial interest of the beneficiaries in the trust. I.R.C. § 318(a)(2)(B)(i) (1988). If the trust is a grantor trust, stock owned by the trust is considered owned by the grantor. I.R.C. § 318(a)(2)(B)(ii) (1988). A trust generally is considered the owner of stock owned, directly or indirectly, by its beneficiaries except for a beneficiary whose interest in the trust is a remote contingent interest. I.R.C. § 318(a)(3)(B)(i) (1988). Stock owned by the grantor of a grantor trust is considered as owned by the trust. I.R.C. § 318(a)(3)(B)(ii) (1988). Stock that is constructively owned by a trust because of its ownership by a beneficiary or a grantor is not reattributed to the other beneficiaries or to the grantor of the trust. I.R.C. § 318(a)(5)(C) (1988).} \]

\[458. \text{Stock owned directly or indirectly by an estate is attributed proportionately to its beneficiaries. I.R.C. § 318(a)(2)(A) (1988). Stock constructively owned by an estate because the stock is owned by a beneficiary is not reattributed to other beneficiaries. I.R.C. § 318(a)(3)(A), (a)(5)(C) (1988).} \]

\[459. \text{If fifty percent or more of the stock of a corporation is owned directly or indirectly by or for any person, the person is considered the owner of stock owned by the corporation in proportion to the person's interest in the value of the stock of a corporation. I.R.C.} \]
has an option to purchase the stock, the taxpayer is also considered to be an owner of the stock. Spousal attribution does not apply under section 318, however, if the spouses are legally separated under a decree of divorce or of separate maintenance. Thus, the availability of legal separation in Louisiana could help separated spouses avoid attribution under section 318.

The attribution rules of section 318 apply to determine the tax consequences of transactions governed by other sections of the Internal Revenue Code. For example, spousal attribution can cause a redemption of a shareholder’s stock to be taxed as a dividend. A distribution by a corporation to a shareholder with respect to its stock generally is taxed as a dividend resulting in ordinary income to the shareholder to the extent of the corporation’s earnings and profits. A distribution in redemption of a shareholder’s stock, however, is treated as a sale or exchange of the stock, resulting in capital gain or loss to the shareholder, computed by subtracting the shareholder’s basis in the redeemed stock from the amount of the distribution. A distribution to a shareholder that qualifies as a redemption generally results in a smaller tax.
liability than if the distribution is considered a dividend. Any capital gain that results from the redemption could be used to offset the shareholder's capital losses from other transactions, thereby reducing the amount of capital losses subject to the $3,000 or $1,500 limitation. If the shareholder held the redeemed stock for more than one year, any capital gain in excess of the taxpayer's capital losses could qualify for the lower tax rate that applies to net capital gain. The most significant tax savings achieved by characterization of the distribution as a redemption, however, generally result because the shareholder is able to use the basis of the redeemed stock to offset the amount of the redemption, reducing the gain to be included in income or increasing the taxpayer's recognizable loss.

A redemption does not always qualify for taxation as a sale or exchange of the stock. A redemption that is not made in partial liquidation of the corporation is taxed as a dividend to the extent of the corporation's earnings and profits unless the redemption (1) is not essentially equivalent to a dividend, (2) is substantially disproportionate, or (3) results in a complete termination of the shareholder's entire stock interest in the corporation. The redemption generally satisfies these tests if the shareholder's proportionate ownership interest in the corporation after the redemption is sufficiently reduced as compared to the shareholder's proportionate interest in the corporation before the redemption.

The redemption rules draw a distinction between a redemption that should be taxed as a dividend because it enables a shareholder to withdraw cash or property from the corporation while leaving the shareholder's proportionate interest intact, and a redemption that resembles a sale of the shareholder's stock because it results in a meaningful reduction in the shareholder's interest in the corporation. The attribution rules of section 318 apply to determine whether the redemption in fact has meaningfully reduced the shareholder's interest in the corporation.

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468. A corporate shareholder, however, can achieve greater tax savings on the receipt of a dividend if the corporate shareholder qualifies for a dividend received deduction under I.R.C. §§ 243-245 (1988).

469. For a discussion of the rules limiting the deductibility of an individual taxpayer's capital losses, see supra notes 413-419 and accompanying text.


473. For a discussion of the various tests and the amount of reduction in proportionate ownership required under each of the tests, see Bittker & Eustice, supra note 455, at ¶ 9.04-9.06.

A shareholder can avoid spousal attribution only if (1) the redemption is a complete redemption of all of the shareholder’s stock in the corporation, (2) immediately after the redemption, the former shareholder has no interest in the corporation (including an interest as officer, director or employee), other than an interest as a creditor, and (3) the former shareholder does not acquire any interest in the corporation (other than stock acquired by bequest or inheritance) for ten years after the redemption.

When a redemption does not completely terminate a shareholder’s interest in the corporation or the shareholder retains a tainted interest in the corporation, spousal attribution can increase the shareholder’s tax burden. For example, to qualify for sale or exchange treatment under the substantially disproportionate rule, (1) the shareholder must own, immediately after the redemption, less than 50 percent of the voting stock of the corporation, and (2) the shareholder’s proportionate share of the voting stock of the corporation after the redemption must be less than 80 percent of the shareholder’s proportionate share of voting stock before the redemption. If the shareholder owns 50 shares of a corporation’s voting stock, the shareholder’s spouse owns 25 shares, and an unrelated party owns the remaining 25 shares, a redemption of 20 shares of the shareholder’s stock will fail the substantially disproportionate test and therefore be taxed as a dividend. Because of spousal attribution, the shareholder is considered as owning 75 of the outstanding 100 shares, or 75 percent of the voting stock, before the redemption and 55 of the outstanding 80 shares, or 68.75 percent of the voting stock, after the redemption, thereby failing the requirement that the shareholder own less than 50 percent of the voting stock after the redemption.

476. I.R.C. § 302(b)(3), (c)(2) (1988). The redeemed shareholder must also file an agreement with the Service to notify the Service of any prohibited acquisition and to retain proper records. I.R.C. § 302(c)(2)(A)(iii) (1988). If the redeemed shareholder acquires a prohibited interest in the corporation, the statute of limitations for assessment and collection of any deficiency in tax resulting from the prohibited acquisition is extended to include one year following the date that the redeemed shareholder notifies the Service. I.R.C. § 302(c)(2)(A) (1988). The redeemed shareholder may not disregard spousal attribution if any of the redeemed stock was acquired (directly or indirectly) from the spouse within the ten-year period preceding the distribution or if the spouse of the former shareholder acquired any stock in the redeeming corporation from the former shareholder within the same prior ten-year period. I.R.C. § 302(c)(2)(B) (1988). The same rules apply for purposes of disregarding attribution of stock from any family member. I.R.C. §§ 302(c), 318(a) (1988).
478. The retention of more than fifty percent of the voting stock will cause the shareholder to fail the essentially-equivalent-to-a-dividend and the complete-termination-of-interest tests as well. For a discussion of these tests, see Bittker & Eustice, supra note 455, at ¶¶ 9.05-9.06.
Spousal attribution applies to separated spouses, no matter how long they have been separated, unless the spouses are legally separated under a decree of divorce or separate maintenance. If the shareholder in the example were able to obtain a judgment of separation from bed and board, the redemption would qualify for sale or exchange treatment. Without spousal attribution, the shareholder owns 50 of the 100 outstanding shares, or 50 percent of the voting stock before the redemption. After the redemption, the shareholder owns 30 of the 80 outstanding shares, or 37.5 percent of the voting stock. The reduction in proportionate stock ownership satisfies both prongs of the substantially disproportionate test. After the redemption the shareholder’s ownership interest is less than 50 percent of the voting stock of the corporation, and the shareholder’s interest, 37.5 percent, is less than 80 percent of the shareholder’s prior 50 percent interest.

Spousal attribution under section 318 can also trigger rules requiring a sale of stock to a related corporation to be taxed as a dividend and causing a sale of section 306 stock to be taxed as a dividend even if the sale terminates the shareholder’s entire interest in the corporation.

480. I.R.C. § 304 (1988). The rules of I.R.C. § 304 prevent a shareholder from circumventing the tests in I.R.C. § 302 which determine whether a redemption is taxed as a sale or exchange or as a dividend. Absent some provision, a shareholder could sell stock in one corporation that the shareholder controls to another controlled corporation, thereby bailing out corporate earnings at capital gains rates while effectively retaining control of both corporations. After the sale the shareholder would continue to control the corporation whose stock was sold by virtue of the shareholder’s control of the purchasing corporation. I.R.C. § 304 provides that the tests for dividend equivalency under the redemption rules apply to determine whether the sale of stock in one controlled corporation to another controlled corporation qualifies for taxation as a sale or exchange. I.R.C. § 304(a) (1988). The attribution rules of I.R.C. § 318 apply to determine whether a shareholder has “control”, i.e., owns fifty percent or more of the stock by vote or by value, of each corporation before the sale, and if so, whether the sale results in a significant reduction in the shareholder’s proportional interest in the corporation whose stock was sold. I.R.C. § 304(b), (c) (1988).
481. I.R.C. § 306(b) (1988). “Section 306 stock” generally is preferred stock that was received by a shareholder tax-free. I.R.C. § 306(c) (1988). The proceeds of a sale or redemption of section 306 stock are not taxed as a dividend. I.R.C. § 306(a) (1988). In enacting I.R.C. § 306, Congress intended to prevent shareholders from avoiding dividend treatment on distributions of corporate earnings by selling or redeeming preferred stock that was received in a tax-free stock dividend or in a tax-free reorganization. Before Congress enacted I.R.C. § 306, a shareholder could bail out corporate earnings at capital gains rates and reduce the amount includible in income by causing the corporation to make a tax-free stock dividend of preferred stock. The shareholder then could sell the preferred stock, subtract the basis of the stock from the amount realized, and receive the preferential tax treatment for capital gains realized on the sale. In selling the preferred stock, the shareholder retained control of the corporation by continuing to hold the common stock. Later the corporation could redeem the preferred stock from the purchaser. The purchaser would recognize little or no gain on the redemption because the purchaser’s basis in the stock is its cost. The result of such a transaction is economically equivalent to a dividend. The
Stock attributed to a spouse under section 318 can cause the spouse to be a United States shareholder and therefore unable to defer taxation on certain income earned by a controlled foreign corporation. A taxpayer who is separated from his or her spouse may avoid the adverse effects caused by spousal attribution only by obtaining a legal separation from the spouse. The enactment of provisions authorizing a judgment of separation from bed and board could help separated spouses in Louisiana avoid the burdens resulting from spousal attribution under section 318.

Section 267 of the Internal Revenue Code provides attribution rules similar to the attribution rules of section 318. Among the related parties

shareholder indirectly received corporate earnings while retaining the same proportional control of the corporation. In Chamberlin v. Commissioner, 207 F.2d 462 (6th Cir. 1953), cert. denied, 347 U.S. 918, 74 S. Ct. 516 (1954), the Sixth Circuit held that the sale of such preferred stock was to be treated as a sale for tax purposes, entitling the shareholder to capital gains treatment. Congress overruled Chamberlin by enacting I.R.C. § 306. Under I.R.C. § 306, the proceeds of a sale of section 306 stock are ordinary income to the extent that they would have been taxed as a dividend at the time the stock was issued. I.R.C. § 306(a)(1) (1988). A redemption of section 306 stock results in ordinary income to the extent of the corporation's earnings and profits at the time of the redemption. I.R.C. § 306(a)(2) (1988). The potential for abuse does not exist, however, if a sale of the preferred stock terminates the shareholder's entire interest in the corporation; in such a case the shareholder loses control of the corporation. Therefore, when a shareholder's sale of section 306 stock terminates the shareholder's entire interest in the corporation, the transaction generally is respected as a sale. I.R.C. § 306(b)(1)(A) (1988). If the sale is to a related person, however, the shareholder effectively could retain control of the corporation through the related party while bailing out corporate earnings at capital gains rates. Therefore, a sale of section 306 stock to a related entity generally is taxed as a dividend. I.R.C. § 306(b)(1)(A)(ii) (1988). Spousal attribution under I.R.C. § 318 applies in determining whether a shareholder owns an interest in the purchasing entity. I.R.C. § 318(a) (1988). For a discussion of I.R.C. § 306, see Bittker & Eustice, supra note 455, at ¶¶ 10.01-10.07.

482. I.R.C. §§ 951, 958(b) (1988). A "United States shareholder" is a United States person who owns directly or indirectly ten percent or more of the voting stock of a foreign corporation. I.R.C. § 951(b) (1988). The attribution rules of I.R.C. § 318 apply in determining how much stock is owned. I.R.C. § 958(b) (1988). A controlled foreign corporation is any foreign corporation if more than fifty percent of its stock by vote or by value is owned by United States shareholders on any day of its taxable year. I.R.C. § 957(a) (1988). A United States shareholder must include in income the shareholder's pro rata share of the controlled foreign corporation's subpart F income as it is earned, rather than deferring taxation until the income is distributed. I.R.C. § 951 (1988). A United States shareholder also must include in income a pro rata share of the controlled foreign corporation's previously untaxed earnings that are invested in United States property. Id. Subpart F income generally consists of the type of income on which United States taxpayers could, absent some provision, defer taxation by using tax haven operations. A discussion of subpart F income is beyond the scope of this article. For such a discussion, see 1 Joel D. Kuntz & Robert J. Peroni, U.S. International Taxation ¶ B3.04 (1992). Spousal attribution under I.R.C. § 318 also can subject a taxpayer to the information reporting requirements of I.R.C. § 6038 that apply to a United States person who owns more than fifty percent of the voting stock or more than fifty percent of the value of the stock of a foreign corporation. I.R.C. § 6038(e)(1) (1988).

listed in section 267(b) whose interests in an entity are attributed to a taxpayer are family members,\textsuperscript{484} which, of course, include the taxpayer's spouse.\textsuperscript{485} Spousal attribution under section 267 may cause the disallowance of loss on a sale of property to a corporation\textsuperscript{486} or to a partnership\textsuperscript{487} if the taxpayer is considered as owning more than fifty percent of the equity interest in the corporation\textsuperscript{488} or the partnership.\textsuperscript{489} When a spouse's ownership interest is attributed to a taxpayer under section 267, the taxpayer may have to recognize ordinary income, rather than capital gain, on the sale of property to a related corporation, partnership, or trust if the property is depreciable in the hands of the transferee.\textsuperscript{490} In the case of a sale to a partnership, spousal attribution may cause the gain to be ordinary if the asset is not a capital asset in the hands of the partnership.\textsuperscript{491} Attribution under section 267 also may require a seller of all the substantial rights to a patent to recognize ordinary income rather than capital gain\textsuperscript{492} and may prevent a taxpayer from claiming a current deduction of reasonably estimated losses on deposits in bankrupt or insolvent financial institutions.\textsuperscript{493} Section 267 attribution may impose an indirect tax burden on a taxpayer by disallowing losses on the sale of property from a related entity to the taxpayer,\textsuperscript{494} deferring deductions for expenses otherwise accrued by a related entity,\textsuperscript{495} and requiring a related entity to recognize ordinary income, rather than capital gain, on

\textsuperscript{485} I.R.C. § 267(c)(4) (1988).
\textsuperscript{487} I.R.C. § 707 (1988).
\textsuperscript{488} The loss is disallowed if the taxpayer owns, directly or through attribution, more than fifty percent of the value of the stock of the corporation. I.R.C. § 267(b)(2) (1988).
\textsuperscript{489} The loss is disallowed if the seller owns, directly or through attribution, more than fifty percent of the capital interest or profits interest in the partnership. I.R.C. § 707(b)(1)(A) (1988).
\textsuperscript{490} I.R.C. § 1239 (1988). The gain on the sale is ordinary income if the sale is to a trust in which the taxpayer or his spouse is a beneficiary or if the sale is to a corporation or partnership in which the taxpayer owns, directly or through attribution, a greater than fifty percent interest. I.R.C. § 1239(b)(2), (c)(1)(A), (B) (1988).
\textsuperscript{491} I.R.C. § 707(b)(2) (1988).
\textsuperscript{492} I.R.C. § 1235 (1988).
\textsuperscript{493} I.R.C. § 165(l)(2)(D) (1988). A taxpayer is not entitled to a current deduction of such estimated losses unless the taxpayer is a "qualified individual". I.R.C. § 165(l)(1)(A) (1988). The term "qualified individual" is defined to include any individual except one who owns at least one percent of the value of the outstanding stock of the bankrupt or insolvent financial institution, who is an officer of the institution, or who is related to a person who owns at least one percent of the stock or is an officer of the financial institution. I.R.C. § 165(l)(2) (1988). The rules of I.R.C. § 267 apply for purposes of determining whether a person owning a prohibited interest in or participating as an officer of the financial institution is related to the taxpayer. I.R.C. § 165(l)(2)(D) (1988). For a discussion of I.R.C. § 165(l), see supra, notes 275-284 and accompanying text.
\textsuperscript{495} I.R.C. § 267(a)(2) (1988).
the sale of an asset to the taxpayer.\footnote{496} Several other provisions of the Internal Revenue Code provide spousal attribution rules that can increase the tax burden of the attributee.\footnote{497} In such cases, a provision authorizing legal separation in Louisiana could help separated spouses avoid adverse tax consequences that result from spousal attribution.\footnote{498}

\footnote{496. I.R.C. §§ 707(b)(2), 1239(a) (1988).}
\footnote{497. See, e.g., I.R.C. § 341 (taxing as ordinary income gain recognized on the sale or exchange of stock or the liquidation or partial liquidation of a collapsible corporation); §§ 542-544 (imposing an additional twenty-eight percent tax on undistributed income of a personal holding company); §§ 671-679 (attributing income of a trust to the grantor rather than to the beneficiaries of the trust); § 1014(e) (denying a step-up in basis of property acquired from a decedent by an individual or the individual's spouse if the individual gave the property to the decedent within one year of the decedent's death); § 1092 (disallowing losses in certain straddle transactions); § 1233 (providing for short-term rather than long-term capital gain on short sales of property); § 1272 (imputing original issue discount income with respect to certain loans); §§ 1561-1563 (limiting a taxpayer's ability to avoid taxation by incorporating multiple corporations); § 7872 (imputing interest on certain loans).

498. It is not certain whether a legal separation will cause a taxpayer to be considered unmarried for purposes of attribution under I.R.C. § 267. Nothing in the Internal Revenue Code or the Regulations defines the term "spouse" or determines marital status for purposes of I.R.C. § 267. For a discussion of the uncertainty that results when there is no statutory or administrative definition of marital status for purposes of a federal income tax provision, see supra note 454. Unless and until a court determines whether an individual who is legally separated retains his or her status as a "spouse" for purposes of I.R.C. § 267, the individual's status for that purpose remains in doubt. Some of the other sections of the Internal Revenue Code provide that spousal attribution will not apply to legally separated spouses. See, e.g., I.R.C. §§ 318(a)(1)(A)(i) (no spousal attribution if the taxpayer is legally separated from his or her spouse under a decree of divorce or of separate maintenance); 672(e)(2) (individual who is legally separated under a decree of divorce or separate maintenance is not married for purposes of the grantor trust rules); 1233(e)(2)(C) (individual who is legally separated under a decree of divorce or separate maintenance is not considered a spouse for purposes of the short sale rules). Regulations promulgated under I.R.C. § 1239 contain a rule providing for the retroactive nonapplication of I.R.C. § 1239 when property is transferred between a husband and wife pursuant to an interlocutory decree of divorce which subsequently becomes final. Treas. Reg. § 1.1239-1(l)(1) (as amended in 1986). The rule in the regulation is curious because I.R.C. § 1041, which governs transfers between spouses provides that a taxpayer will not recognize gain at all when property is transferred to a spouse or a former spouse if the transfer is incident to the divorce. I.R.C. § 1041(a) (1988). The rule could be a vestige from regulations promulgated under former I.R.C. § 1239 which did apply to transfers between spouses. I.R.C. § 1239(b)(1) (repealed 1984). The regulations also provide that in general the attribution rules of I.R.C. § 318(a) apply in determining whether a transferor or transferee is a related party for purposes of I.R.C. § 1239. Treas. Reg. § 1.1239-1(c)(5) (as amended in 1986). Under I.R.C. § 318 stock owned by one spouse is not attributed to the other spouse if the spouses are legally separated under a decree of divorce or separate maintenance. I.R.C. § 318(a)(1)(A)(i) (1988). I.R.C. § 1239, however, states that constructive ownership for purposes of section 1239 "shall be determined in accordance with rules similar to the rules under section 267(c) (other than paragraph (3) thereof)." I.R.C. § 1239(c)(2) (1988). I.R.C. § 267 is silent with respect to any definition of marital status. The application of I.R.C. § 318 attribution could be a reference to former I.R.C. § 1239 which did apply such rules to determine constructive ownership. I.R.C. § 1239(c)(2) (repealed 1986).}
Occasionally, spousal attribution can result in tax savings. For example, section 1361 of the Internal Revenue Code treats a husband and a wife as one person for purposes of counting the number of shareholders who own stock in an S corporation.\(^499\) A corporation cannot elect to be an S corporation if it has more than thirty-five shareholders.\(^500\) If the number of an S corporation’s shareholders increases to more than thirty-five, the corporation’s subchapter S election terminates.\(^501\) Thus, a divorce could trigger the termination of a subchapter S election where a husband and wife each own stock in a corporation with thirty-four other shareholders.

Ineligibility to make a subchapter S election or termination of an existing subchapter S election can be expensive to the shareholders. The income of most nonelecting corporations is taxed twice: once as it is earned by the corporation,\(^502\) and a second time when it is distributed to the shareholders.\(^503\) Even if corporate earnings are not distributed, the tax burden on the earnings can be heavier if the corporation does not have a subchapter S election in effect because a nonelecting corporation generally pays tax at a higher rate than the tax rates that apply to the income of individuals.\(^504\) When the corporation has a subchapter S election in effect, the corporation’s income generally is taxed once at the rate that applies to the individual shareholders.\(^505\)

Regulations promulgated under subchapter S provide that a husband and wife will not be treated as one person upon the dissolution of the marriage for any reason other than death.\(^506\) Neither the Internal Revenue Code nor the Regulations define the terms “husband,” “wife,” or “dissolution of the marriage” for purposes of counting the number of shareholders in an S corporation. If a legal separation constitutes a dissolution of the marriage under subchapter S, separated spouses may wish to avoid a legal separation to prevent a termination of a subchapter S election.\(^507\) The availability of a legal separation in Louisiana will not

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507. Spousal attribution under I.R.C. § 1034 also may result in tax savings to spouses. I.R.C. § 1034 generally provides for nonrecognition of gain on the sale of a taxpayer’s principal residence if the taxpayer invests the proceeds of the sale in a new principal residence within a period beginning two years before the date of the sale and ending two years after the sale date. I.R.C. § 1034(a) (1988). As a consequence of the nonrecognition of gain, the
necessarily terminate a subchapter S election. Separated spouses can prevent termination by not filing a petition for a judgment of separation from bed and board.

**D. Marital Status as a Determining Factor With Respect to Tax Credits**

A number of provisions of the Internal Revenue Code authorize credits against tax. To the extent that a taxpayer can take advantage of a tax credit, the amount of tax that must be paid will be less than the computed tax liability. A tax credit generally is more advantageous to a taxpayer than a deduction because a credit reduces the tax liability dollar-for-dollar, whereas a deduction reduces taxable income, resulting in a smaller reduction in tax liability. The fact of marriage can reduce the amount of, or even eliminate the availability of, a tax credit that the taxpayer otherwise would be entitled to claim.

**1. The Child Care Credit**

The limitations on the child care credit impose significant marriage penalties. Section 21 of the Internal Revenue Code permits an individual taxpayer to claim a tax credit for household and dependent care services incurred to enable the taxpayer to be gainfully employed. To be eligible to claim the credit, the taxpayer must have a dependent who is under the age of thirteen or who is physically or mentally incapable of caring for himself or herself.

The maximum amount that a taxpayer may claim as a child care credit for the taxable year is thirty percent of $2,400, (i.e., a maximum credit of $720) of dependent care expenses if the taxpayer has one qualifying dependent. A taxpayer with two or more qualifying dependents may credit up to thirty percent of $4,800, or $1,440, of

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dependent care expenses incurred during the taxable year.\textsuperscript{512} The percentage of expenses that a taxpayer may claim as a child care credit is reduced (but not below twenty percent) by one percentage point for each $2,000 (or fraction thereof) by which the taxpayer's adjusted gross income for the year exceeds $10,000.\textsuperscript{513} Thus, a taxpayer with adjusted gross income in excess of $30,000 is entitled to claim a maximum credit of $480 if the taxpayer has one qualifying dependent and $960 if the taxpayer has two or more such dependents.\textsuperscript{514}

The maximum amount of dependent care expenses that can be taken into account also cannot exceed the individual's earned income for the year.\textsuperscript{515} For a married individual, the limitation is the lesser of the individual's earned income or the earned income of the individual's spouse.\textsuperscript{516} A married taxpayer is not eligible to claim the credit unless the taxpayer and his or her spouse file a joint return.\textsuperscript{517} For purposes of section 21, an individual is considered not married if the individual is legally separated from his or her spouse under a decree of divorce or separate maintenance\textsuperscript{518} or if the abandoned spouse rule applies.\textsuperscript{519}

Under these rules a separated spouse in Louisiana must file a joint return to be eligible to claim the child care credit unless the abandoned

\textsuperscript{512} I.R.C. § 21(a)(2), (c)(2) (1988).

\textsuperscript{513} I.R.C. § 21(a)(2) (1988).

\textsuperscript{514} The $2,400 and $4,800 limitations are reduced, no matter how much adjusted gross income the taxpayer has, by amounts that are excludable from income under I.R.C. § 129 because they are employer-provided dependent care expenses. I.R.C. § 21(c) (1988). For a discussion of the exclusion under I.R.C. § 129, see supra notes 319-25 and accompanying text.


\textsuperscript{516} I.R.C. § 21(d)(1)(B) (1988). There is an exception to this rule if the individual's spouse is a full-time student or is incapable of taking care of himself or herself. In that case, the spouse will be deemed to have income each month that the spouse is a full-time student or unable to care for himself or herself of $200 per month if the taxpayer has one qualifying dependent and $400 per month if the taxpayer has two or more qualifying dependents. I.R.C. § 21(d)(2) (1988).

\textsuperscript{517} I.R.C. § 21(e)(2) (1988).

\textsuperscript{518} I.R.C. § 21(e)(3) (1988).

\textsuperscript{519} I.R.C. § 21(e)(4) (1988). The abandoned spouse rule under I.R.C. § 21 differs in one respect from the abandoned spouse rule under I.R.C. § 7703(b). To be considered unmarried under the I.R.C. § 7703(b) abandoned spouse rule, the taxpayer, \textit{inter alia}, must maintain as his home a household which constitutes the principal place of abode of a dependent child (or a child who would be a dependent except for an agreement to permit the noncustodial parent to claim the exemption deduction for the child). Under I.R.C. § 21(e)(4)(A)(i), the child for whom the taxpayer provides an abode must be a "qualifying individual," \textit{i.e.}, a dependent child who is under the age of thirteen or physically or mentally incapable of taking care of himself or herself. The noncustodial parent is not entitled to claim the child care credit. I.R.C. § 21(e)(5) (1988 & Supp. 1991). The custodial parent, however, may claim the credit even if the custodial parent has signed an agreement permitting the noncustodial parent to claim the exemption deduction with respect to the qualifying child. \textit{Id.}
spouse rule applies. If the community is still in existence, the abandoned spouse rule will not apply because the taxpayer will not be able to meet the requirement that the taxpayer furnish over one-half of the household expenses for the year.\textsuperscript{520} Even spouses who have partitioned the community must file a joint return to claim the credit for the first year of their separation unless they were separated during the last six months of the taxable year.\textsuperscript{521} If the spouses could obtain a judgment of separation from bed and board, they could avoid the joint return requirement.\textsuperscript{522}

The joint return requirement is problematic. Separated spouses may not be able to cooperate well enough to file a joint return. Spouses who file a joint return could lose part of the credit if combined adjusted gross income on the return exceeds $10,000. If the noncustodial spouse does not work, the child care credit will not be available to the joint filers because of the earned income limitation.\textsuperscript{523} The enactment of provisions authorizing legal separation in Louisiana could help separated spouses obtain greater tax savings with respect to the child care credit.

2. The Credit for the Elderly and Totally Disabled

Section 22 of the Internal Revenue Code allows a tax credit to a low-income individual taxpayer who is over the age of sixty-five or who is retired because of a permanent and total disability\textsuperscript{524} (the "credit for the elderly and totally disabled"). The amount of the credit often is reduced for a married taxpayer. The maximum amount of the credit is fifteen percent of the taxpayer's "section 22 amount," which consists of an initial amount, reduced by certain factors.\textsuperscript{525}

The initial amount is $5,000 in the case of a single individual or a joint return where only one spouse qualifies for the credit.\textsuperscript{526} In the case of a joint return, the initial amount is $7,500 if both spouses qualify for the credit.\textsuperscript{527} A qualifying spouse who files a separate return has an initial amount of $3,750.\textsuperscript{528} Thus, the maximum credit for an

\textsuperscript{520} I.R.C. § 21(e)(4)(A)(ii) (1988). For a discussion of the impossibility of meeting the requirement that the taxpayer furnish over one-half of household costs during the existence of the community, see supra notes 192, 248 and accompanying text.


\textsuperscript{522} Under I.R.C. § 21(e)(3) (1988), the spouses who are legally separated under a decree of divorce or of separate maintenance are considered unmarried for purposes of claiming the child care credit.

\textsuperscript{523} I.R.C. § 21(d) (1988).

\textsuperscript{524} For a discussion of the credit for the elderly and the permanently and totally disabled, see 2 Bittker & Lokken, supra note 46, at ¶ 37.2.

\textsuperscript{525} I.R.C. § 22(a), (c) (1988).


unmarried taxpayer or a joint return where only one spouse qualifies is $750. On a joint return, spouses may claim a maximum credit of $1,125 if they both qualify. A married taxpayer who files a separate return may claim a maximum credit of $562.50. The marriage penalty resulting from the statutory limitations is obvious. Separated spouses who are considered unmarried and qualify for the credit may claim a maximum of $1,500 in the aggregate; if they are considered married, the maximum credit is $1,125.

The maximum credit often is unavailable to taxpayers because of factors that reduce the initial amount. The initial amount for a disabled taxpayer who is under the age of sixty-five may not exceed the taxpayer's disability income. For both elderly and disabled taxpayers, the initial amount is further reduced by certain retirement or disability income that is exempt from tax. On a joint return, the exempt income of both spouses is combined to reduce the initial amount. Thus, in the case of a joint return, even if the spouses are living under a separate property regime, the exempt income of one of the spouses could eliminate a credit that otherwise would be available to the other spouse. A married taxpayer cannot avoid this problem by filing a separate return unless the taxpayer lives apart from his or her spouse for the entire taxable year.

The initial amount is finally reduced by one-half of the taxpayer's adjusted gross income in excess of $7,500 in the case of an unmarried taxpayer, $10,000 in the case of a joint return, and $5,000 in the case of a married taxpayer filing a separate return. The reduction for

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529. I.R.C. § 22(c)(2)(B) (1988). Disability income is the aggregate amount includable in the individual's gross income for the taxable year under I.R.C. § 72 or 105(a) to the extent that the amount constitutes wages (or payment in lieu of wages) for the period during which the individual is absent from work on account of permanent and total disability. I.R.C. § 22(c)(2)(B)(iii) (1988). If both spouses qualify for the credit and only one of the spouses is over the age of sixty-five, the initial amount on their joint return is the sum of $5,000 plus the disability income of the spouse who is under age sixty-five. I.R.C. § 22(c)(2)(B)(ii)(II) (1988). Because I.R.C. § 22 does not contain a special provision for community income, it seems that the existence of the community could reduce the amount of the credit significantly by cutting the under sixty-five-year-old spouse's disability income in half.

530. There are four categories of exempt income that reduce the initial amount: (1) benefits under title II of the Social Security Act; (2) retirement benefits under the Railroad Retirement Act of 1974; (3) disability benefits payable on account of personal injuries or sickness resulting from active service in the armed forces; and (4) pensions, annuities, and disability benefits excluded from income by any provision of law not contained in the Internal Revenue Code. I.R.C. § 22(c)(3)(A) (1988).


532. Except in the case of a taxpayer who lives apart from his or her spouse for the entire taxable year, the taxpayer may not claim the credit unless a joint return is filed. I.R.C. § 22(e)(1) (1988).

adjusted gross income may result in a marriage penalty when two spouses have adjusted gross income, and a marriage bonus when only one spouse has adjusted gross income.

For purposes of section 22, a taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies. Under these rules, a separated spouse in Louisiana who does not satisfy the requirements of the abandoned spouse rule cannot avoid the joint return requirement unless the spouse has been separated for the entire taxable year. Not only will the other spouse’s exempt income reduce or eliminate the otherwise available credit, but the other spouse’s adjusted gross income that must be reported on the joint return could also reduce or eliminate the taxpayer’s ability to claim a credit under section 22. If the community remains in existence in post-separation years, the one-half of the other spouse’s exempt income and adjusted gross income that must be reported on the taxpayer’s separate return could reduce or eliminate an otherwise available credit. The availability of a judgment of separation from bed and board in Louisiana would help such spouses both to avoid the joint return requirement during the first year of separation and to terminate the community.

Even Louisiana spouses who have been separated for the entire taxable year and who are living under a separate property regime could benefit from the availability of a judgment of separation from bed and board. A separated spouse who does not meet the requirements of the abandoned spouse rule and who is not legally separated must compute the section 22 credit for the elderly or totally disabled by using the smallest initial amount and the smallest adjusted gross income threshold that applies if the spouse files a separate return. A judgment of separation from bed and board would entitle the spouse to the larger credit that is available to unmarried taxpayers.

3. The Earned Income Credit

The earned income credit is one of the most important credits available to low income taxpayers. Section 32 of the Internal Revenue Code allows a taxpayer to claim the earned income credit which consists of a basic earned income credit and a health insurance credit. The fact of marriage may reduce the amount of the credits if both spouses have income. The maximum amount that a taxpayer can claim under the earned income credit provisions in 1992 is $2,211. The earned income credit often serves as a subsidy to low income taxpayers because

it is refundable, to the extent that it exceeds the taxpayer's pre-credit tax liability.537

The credit is available only if the taxpayer has at least one "qualifying child" during the taxable year.538 A qualifying child is a son, daughter, grandchild, stepson, stepdaughter, or foster child of the taxpayer539 who has the same principal place of abode as the taxpayer, 540 and (1) is under the age of nineteen, (2) is a student under the age of twenty-four, or (3) is permanently and totally disabled.541

The basic earned income credit for 1992 is computed as a percentage of the first $7,520 of the taxpayer's earned income.542 "Earned income" includes wages, salaries, tips, other employee compensation, and net earnings from self-employment.543 Earned income is computed without

537. A taxpayer who qualifies for the earned income credit may receive the refund as income is earned, thereby increasing his or her wages. I.R.C. § 3507 (1988). For a discussion of the mechanics for receiving advance payments of the refundable portion of the earned income credit, see 2 Bittker & Lokken, supra note 46, at ¶ 37.3 (Supp. 1992). Any refund available under the earned income credit provisions is subject to I.R.C. § 6402(c) which requires the Service to apply tax refunds for overpayments to past-due child support obligations. Sorenson v. Secretary of the Treasury, 475 U.S. 851, 106 S. Ct. 1600 (1986). A refund created by the earned income credit, however, is not an asset that passes to the taxpayer's trustee in bankruptcy. In re Searles, 445 F. Supp. 749, 753 (D. Conn. 1978).


541. I.R.C. § 32(c)(3)(A)(iii), (c) (1988 & Supp. 1991). A child who meets all of the tests in the text will not be a "qualifying child", however, unless the taxpayer includes on his or her income tax return the child's name, age, and for a child over the age of one, the child's taxpayer identification number. I.R.C. § 32(c)(3)(A)(iv), (D)(i) (1988 & Supp. 1991). If the taxpayer also claims a health insurance credit under I.R.C. § 32(a)(2), the Service can also require the taxpayer to include the insurance policy number or other evidence of insurance on the return. I.R.C. § 32(c)(3)(D)(ii) (1988 & Supp. 1991).


543. I.R.C. § 32(c)(2)(A) (1988). Earned income also includes compensation that is excluded from gross income, such as fringe benefits. Treas. Reg. 1.43-1(c)(3) (1980). Earned income is reduced by any net loss from self-employment. Id. Earned income does not include pensions, annuities, unemployment compensation, workmen's compensation or a nonresident alien's income not connected with a United States business. Id.
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regard to community property laws. Thus, the earned income of a Louisiana couple living under a community property regime is attributed to the spouse who performs the services.

The maximum amount of the credit in 1992 is 17.6 percent of $7,520, or $1,323.52, if the taxpayer has one qualifying child and 18.4 percent of $7,520, or $1,383.68, for a taxpayer with two or more qualifying children. In the case of a taxpayer with a qualifying child who has not attained the age of one by the end of the taxable year, a supplemental young child credit is allowed, increasing the credit percentage by five percentage points, to 22.6 percent for a taxpayer with one child and 23.4 percent for a taxpayer with two or more qualifying children.

The credit is phased out for a taxpayer whose adjusted gross income (or, if greater, earned income) for 1992 exceeds $11,840. For 1992 the credit for a taxpayer with one qualifying child is reduced by 12.57 percent of the amount by which adjusted gross income or earned income (whichever is greater) exceeds $11,840. The phaseout percentage for a taxpayer with two qualifying children in 1992 is 13.14. The phaseout percentage for a taxpayer who claims the supplemental young child credit is 3.57. Thus, a taxpayer whose adjusted gross income or earned income is greater than $22,370 in 1992 is not entitled to claim the basic earned income credit.

The health insurance credit is allowed for premiums paid by the taxpayer for medical insurance which covers at least one qualifying child. The maximum amount of insurance premiums that the taxpayer

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546. I.R.C. § 32(b)(1)(D)(i) (1988 & Supp. 1991). If the taxpayer elects to claim this supplemental young child credit, the taxpayer may not claim a child care credit with respect to the child. Id.
551. I.R.C. § 32(a)(2), (b)(2)(B) (1988 & Supp. 1991). If the taxpayer or the taxpayer's spouse is also covered by the insurance policy, the credit is not limited to the portions of the premium allocable to the qualifying child. A taxpayer may not take into account, however, any amount that is paid, reimbursed, or subsidized by the federal government, a
can claim as a health insurance credit in 1992 is limited to six percent of the taxpayer’s first $7,520 of earned income, or $451.51. This amount is phased out by 4.285 percent of the amount by which the taxpayer’s adjusted gross income or earned income (whichever is greater) exceeds $11,840. The health insurance credit, like the basic earned income credit, is completely phased out for a taxpayer whose 1992 adjusted gross income or earned income exceeds $22,370.

A taxpayer who is married is ineligible to claim either the basic earned income credit or the health insurance credit unless the taxpayer files a joint return. For purposes of the joint return requirement, a taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies. Thus, in Louisiana a separated spouse who does not meet the requirements of the abandoned spouse rule, either because the spouse has not been separated during the last six months of the taxable year or because the community is still in existence, cannot claim the earned income credit unless the spouse files a joint return. The combined adjusted gross income on a joint return could reduce the amount of the credit or eliminate it completely. There would be no need to file a joint return if the spouse could obtain a judgment of separation from bed and board before the end of the taxable year.

4. The General Business Credit

The limitations on the allowance of the general business credit can result in a marriage penalty, especially for spouses who file separate returns. The general business credit includes seven business-related credits: (1) the investment credit, (2) the targeted jobs credit, (3) the alcohol fuels credit, (4) the research credit, (5) the low-income housing credit, (6) the enhanced oil recovery credit, and (7) in the case of an eligible small business, the disabled access credit. Section 38 of the Internal Revenue Code places a ceiling on the aggregate amount of the seven credits that a taxpayer can use as a credit against tax in any taxable state or local government, or any government agency or instrumentality and not includible in the recipient’s gross income. I.R.C. § 32(b)(2)(C) (1988 & Supp. 1991).


557. If the community is still in existence, the spouse will fail the requirement of I.R.C. § 7703(b)(2) (1988) that the spouse furnish over one-half of the costs of maintaining the household. See supra notes 192, 248 and accompanying text.

year.\textsuperscript{559} Amounts that are disallowed under section 38 are carried back three years and forward fifteen years, subject to the section 38 limitations in the carry-back and carry-forward years.\textsuperscript{560} The limitations can be detrimental to the taxpayer because the time value of money makes a current tax credit worth more than a credit that is applied in a future year. Because the limitations of section 38 apply to amounts carried back or forward, a taxpayer could lose the advantage of a suspended credit altogether.

The limitation under section 38 is based on the taxpayer’s “net income tax,” defined as the sum of the regular tax liability and the alternative minimum tax liability, reduced by the foreign tax credit and the nonrefundable personal credits (including the child care credit and the credit for the elderly and disabled).\textsuperscript{561} The maximum amount of the otherwise allowable general business credit that the taxpayer may claim for the year is the lesser of two amounts. The first is the excess of the taxpayer’s net income tax over the tentative minimum tax for the taxable year.\textsuperscript{562} The second is the excess of the taxpayer’s net income tax over twenty-five percent of so much of the taxpayer’s net regular tax liability as exceeds $25,000.\textsuperscript{563} The term “net regular tax liability” means regular tax liability reduced by the foreign tax credit and the nonrefundable personal credits.\textsuperscript{564}

The first of these measures, based on tentative minimum tax, can result in a marriage penalty, especially for separate filers. The tentative minimum tax is an element of the alternative minimum tax, discussed later in this article.\textsuperscript{565} To the extent that the fact of marriage increases the tentative minimum tax, it also reduces the taxpayer’s ability to use the general business credit unless the second measure results in a smaller allowable credit.\textsuperscript{566}

The second measure reduces the otherwise creditable amount for taxpayers with a high income tax liability. The combined income on a joint return often increases the amount of net tax liability as compared with the tax liability incurred with respect to a separate return. Of course, any increase in the taxpayer’s net tax liability will also result

\textsuperscript{559} I.R.C. § 38(c) (1988). For an explanation of the limitation on the general business credit, see 1 Bittker & Lokken, supra note 46, at ¶ 27.1 (Supp. 1992).


\textsuperscript{561} I.R.C. § 38 (c)(1) (1988).


\textsuperscript{565} See infra notes 569-586 and accompanying text.

\textsuperscript{566} Of course, to the extent that the fact of marriage reduces the tentative minimum tax, it also increases the taxpayer’s ability to use the general business credit unless the second measure results in a smaller allowable credit.
in an increase in the taxpayer's net income tax, which is the amount from which twenty-five percent of the excess of the taxpayer's net tax liability over $25,000 must be subtracted. The amount to be subtracted from net income tax, however, can be greater for separated spouses who are considered married for federal tax purposes than their counterparts who are considered unmarried. The formula for computing that amount requires a married couple to reduce the couple's joint net tax liability by $25,000, whereas an unmarried taxpayer reduces the taxpayer's single net tax liability by $25,000.

Separated spouses who are considered married cannot avoid this problem by filing separate returns unless one of the spouses has no current business credit or business credit carryforward or carryback to the taxable year. In cases where both spouses have general business credits, the second measure of the limit on the creditable amount is computed by subtracting from the net income tax on the separate return, twenty-five percent of so much of the taxpayer's net regular tax liability as exceeds $12,500.\footnote{567} Separated spouses in Louisiana who do not satisfy the requirements of the abandoned spouse rule cannot avoid any marriage penalty resulting from the section 38 limitations on the general business credit. The availability of a judgment of separation from bed and board could increase the amount a separated spouse in Louisiana can claim as a general business credit.\footnote{568}

\section*{E. The Alternative Minimum Tax}

The provisions of the Internal Revenue Code concerning the computation of the alternative minimum tax\footnote{569} ("AMT") create a marriage bonus for some taxpayers and a marriage penalty for others. In general, the AMT for an individual is a tax computed at a rate of twenty-four percent that applies to an expanded income tax base called alternative minimum taxable income ("AMTI").\footnote{570} AMTI is taxable income increased to eliminate the benefits of many tax preferences allowed in computing a taxpayer's regular tax liability.\footnote{571} The amount of tax that a taxpayer must pay for any year is essentially the greater of the regular income tax or the AMT. Section 55 of the Internal Revenue Code refers

\footnote{568} I.R.C. § 38 provides no definition of marital status. The reference in I.R.C. § 38(c)(2)(A) to "a husband or wife who files a separate return," however, seems to be a reference to the taxpayer's filing status. For purposes of determining a taxpayer's filing status, the taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse or if the abandoned spouse rule applies. I.R.C. §§ 1(a)-(d); 2(b), (c); 7703 (1988).
\footnote{569} I.R.C. §§ 55-59 (1988).
\footnote{570} For a discussion of the AMT, see 4 Bittker & Lokken, supra note 46, at ¶ 111.4.
to the AMT as the "tentative minimum tax" because a taxpayer must pay the AMT only if the AMT exceeds the taxpayer's regular tax liability for the taxable year.

The purpose of the AMT is to ensure that a taxpayer with substantial economic income cannot avoid significant tax liability by using tax incentives and other special allowances authorized by the Internal Revenue Code. To that end, Congress has assured that a taxpayer's AMTI is greater than the taxpayer's taxable income to which the regular income tax rates apply. For purposes of determining AMTI, (1) depreciation is computed on a slower basis than is allowed for regular tax purposes, (2) certain expenses that are deductible for regular tax purposes, such as mining development and exploration costs, must be capitalized and amortized, (3) gain on certain installment sales must be reported in full in the year of the sale, (4) certain itemized deductions are reduced or disallowed, (5) the standard deduction and deduction for personal exemptions are disallowed, (6) certain excess depletion deductions and intangible drilling costs are disallowed, (7) certain interest that is exempt from the regular income tax is included, and (8) numerous other tax preferences and incentives that reduced the regular income tax are added or adjusted to increase the tax base. Credits generally are disallowed for AMT purposes except for a limited foreign income tax credit.

The twenty-four percent individual AMT rate applies to the amount of the taxpayer's AMTI that exceeds an exemption amount. The exemption amount is: (1) $40,000 in the case of a joint return, (2) $30,000 for an unmarried individual, and (3) $20,000 for a married taxpayer who files a separate return. The marriage bonus and penalty that result from the variations in the exemption amount are obvious. A separated spouse who is considered unmarried may reduce AMTI by

581. For an explanation of all of the items that are adjusted or included in computing an individual's AMT base, see Gaved A. Khokhar, 288-4th Tax Mgmt., Alternative Minimum Tax A-8 to A-44 (1991).
$30,000. If the taxpayer is considered married and his or her spouse has no AMTI, the taxpayer's AMTI is reduced by $40,000, resulting in a marriage bonus of an additional $10,000 exemption amount. Separated spouses with AMTI who are considered unmarried can each reduce their AMTI by $30,000, resulting in an aggregate exemption of $60,000. If they are considered married, the total exemption from the combined AMTI is only $40,000 on a joint return. Each spouse may reduce AMTI reported on a separate return by only $20,000.

The exemption amount is phased out for high income taxpayers. A taxpayer must reduce the applicable exemption amount by twenty-five percent of the taxpayer’s AMTI in excess of (1) $150,000 in the case of a joint return, (2) $112,500 in the case of an unmarried taxpayer, and (3) $75,000 in the case of a married taxpayer who files a separate return. The threshold amounts of AMTI used in computing the reduction in the exemption amount produce a marriage bonus or penalty similar to the bonus and penalty resulting from the exemption amounts.

For purposes of computing an individual's AMT, a taxpayer is considered unmarried if the taxpayer is legally separated from his or her spouse under a decree of divorce or separate maintenance or if the abandoned spouse rule applies. Thus, in Louisiana, a separated spouse cannot avoid any marriage penalty resulting from the computation of the AMT unless the spouse meets the requirements of the abandoned spouse rule. The ability to obtain a decree of separation from bed and board in Louisiana could help some separated spouses avoid some of the adverse impact of the AMT provisions.

III. CONCLUSION

The federal rules concerning the taxation of community income and the computation of an individual’s income tax liability often impose a burden on separated spouses. While application of the rules sometimes results in a marriage bonus, a marriage penalty usually results in cases where both spouses work. When spouses separate, it is not unusual for both spouses to work to pay the costs of maintaining two households. Thus, separated spouses who are considered married often are subject to the marriage penalties that result from many different provisions of the Internal Revenue Code.

Commentators have criticized the Seaborn rule which requires each spouse to report and pay tax on one-half of the community income, the rules whose effect depends on marital status, and the rules requiring

587. See authorities cited supra note 177.
588. See authorities cited supra note 13.
a legal separation to establish that a taxpayer is unmarried for federal tax purposes. While there is great need for reform at the federal level, none seems to be forthcoming in the near future. In the meantime, Louisiana could help some of its taxpayers to avoid the adverse impact of the Seaborn rule and the marriage penalties by enacting provisions authorizing legal separation. A judgment of separation from bed and board would not only make it easier for separated spouses to terminate the community, releasing such spouses from the burden of the Seaborn rule, but it would also permit more separated spouses in Louisiana to be considered unmarried for federal income tax purposes, removing the burdens of the marriage penalty. The availability of a judgment of separation from bed and board would not prevent Louisiana taxpayers from taking advantage of the marriage bonus provisions of the Internal Revenue Code. Separated spouses could take advantage of the marriage bonus provisions by not filing a petition for a separation from bed and board. Authorizing legal separations in Louisiana, therefore, would give separated spouses a choice in selecting the federal income tax consequences that would result in the greatest tax savings.

589. Hesch, supra note 183; Ulven, supra note 183.