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TAXING LESBIANS†

PATRICIA A. CAIN*

I. INTRODUCTION

In his scholarship, and especially in his recent book Taxing Women,¹ Professor Edward McCaffery argues that the United States tax law unfairly burdens women. The women at the center of his critique are working women who are married. McCaffery has identified the disincentives such women face when deciding whether to enter the workplace. He has done so in more detail than any other scholar who has addressed this issue.² His work presents a valuable critique of current tax policy as it affects married working women, especially those who are also mothers. His careful delineation between the "marriage penalty" which increases the tax burden for all two-earner married couples and the bias against the "secondary earner," which is almost always the wife, refocuses the debate over taxation and the family so that the concerns of women are made central.³ I am honored to be part of a symposium celebrating his work and I commend the editors of this journal for their decision to make the taxation of women a more visible concern for feminist scholarship.

In this Essay, I am concerned with women who have remained invisible in most of the feminist scholarship dealing with tax law. The women at the center of my analysis are lesbian couples who share a life of commitment and love. They are not threatened by the marriage

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1. EDWARD McCAFFERY, TAXING WOMEN (1997).
tax penalty because they cannot marry. At the same time, single-earner lesbian couples cannot take advantage of the income splitting effects of joint returns. The law generally refuses to recognize their relationships and the tax law is no different. Every year when they file income tax returns, they are required to fill out forms that force them into separate spheres from each other as though their lives were lived separately. When one partner dies, federal and state transfer taxes impose heavy burdens that, absent careful planning, can prevent the survivor from continuing her established standard of living. These tax burdens are increased when there are dependent children in the lesbian household.

The tax law has never been well designed to account for personal relationships. Spouses and lovers do not bargain for exchanges in the same way that buyers and sellers in an established marketplace do. Yet our tax law often treats spouses and lovers no differently from buyers and sellers.

Our tax law also has a difficult time distinguishing between gifts, income, and support when transfers are made between family members or persons in similar close relationships. Statutory solutions have diminished the problem for spouses. But for unmarried couples, and in particular for lesbian and gay couples who cannot

4. There is a case pending in Hawaii that might change this state of the law, at least for Hawaiian lesbians. See Baehr v. Lewin, 852 P.2d 44 (Haw. 1993) (holding that the state may only limit marriage to opposite-sex couples if it can demonstrate a compelling reason for doing so). On remand, the trial court held that the state had failed to present a compelling justification. Baehr v. Muike, 1996 WL 694235 (Cir. Ct. Haw. Dec. 3, 1996). The case is currently on appeal. However, in 1996, Congress enacted the Defense of Marriage Act (DOMA), which amended the United States Code to provide that in any Act of Congress or any administrative agency's interpretation of such Acts, the word "marriage" means "only a legal union between one man and one woman as husband and wife." Pub. L. 104-199, § 3(a), 110 Stat. 2419 (1996). Assuming that DOMA withstands constitutional attack, this means that same-sex marriages will be recognized only for state tax purposes and not for federal tax purposes.

5. For an article on what is at stake in the failure to recognize lesbian and gay families, see Paula L. Ettelbrick, Wedlock Alert: A Comment on Lesbian and Gay Family Recognition, 5 J.L. & POL'Y 107 (1996).


7. Compare Pascarelli v. Commissioner, 55 T.C. 1082 (1971) (payments in exchange for "wifely services" are not taxable income) with Green v. Commissioner, 846 F.2d 870 (2d Cir. 1988) (payments for "wifely services" are taxable when collected against decedent's estate).

marry, the law remains unclear in many cases. In other cases, the law is clear and generally disadvantageous.

In this Essay, I do not intend to develop a lesbian tax jurisprudence that would solve the problems of lesbian couples. Rather, my intentions are much more modest. I wish to give context to some of the tax problems faced by lesbian couples by describing some concrete issues for which the tax treatment under current law is both unclear and unfair. In doing so, I hope to bring the reality of lesbian lives into the broader tax policy conversation regarding taxation of the family.

II. LESBIAN COUPLES IN GENERAL

It is difficult to count lesbian couples. Recent census data show that there are over 3.5 million unmarried opposite-sex couples in the United States. Although there is no accurate count of same-sex couples, the Census Bureau, based on recent changes in its survey questions, has estimated the number at 145,000 for 1990. There is no indication how many of these are lesbian couples.

The 145,000 estimate seems low, especially since it purports to estimate the incidence of both male-male and female-female couples. Lesbian couples tend to break up more frequently than gay male couples, but lesbians tend to be more relationship-centered than gay men. There is no reason to presume that in any given year there would be a greater or lesser number of female same-sex couples than male couples. And if half the 145,000 estimated same-sex couples were lesbian couples, then the number of lesbian couples would be around 72,500.

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9. For example, if one partner pays for the support of the other are the payments received taxed as income, as a gift, or as legally enforceable support payments? When partners split up, how are their rearrangements of jointly owned property taxed?

10. There is clearly no marital deduction for gifts made between lesbian partners. If the partners agree to hold property as joint tenants with right of survivorship, they must contend with I.R.C. § 2040 (1989) and similar state laws that presume the property was in reality owned by the first to die.


If one uses the statistics from the recent Chicago study rather than the more traditionally cited 10%, then at least 1.4% of the women in this country are likely to report some level of homosexual (or bisexual) identity. The current adult female population of the United States is around 100 million. If 1.4% identify as lesbian, then there are 1.4 million lesbians. If all of these lesbians lived in couples, the number of couples would be 700,000. If only half lived in couples, the number would be 350,000. The Census Bureau estimate seems low by comparison.

Of these couples, however many there are, a substantial number are likely to have children. Estimates range from thirty to forty percent. There is no question that the occurrence of lesbian couples raising children is on the increase. In many cases, these children are planned by the two women who form the couple. Artificial insemination is the means used to impregnate one of the women. Sometimes the sperm is obtained from a sperm bank and sometimes it is obtained from a male friend. In both cases, the intent of the lesbian couple is that the child will be their joint child, raised by the two of them.

14. The Kinsey study, famous for its estimate that 10% of the male population is “more or less exclusively homosexual,” has been under attack in more recent studies. See Edward O. Laumann et al., The Social Organization of Sexuality: Sexual Practices in the United States 288-90 (1994) (citing to the Kinsey study and discussing the fact that its 10% estimate is higher than the estimate in other studies). Kinsey did not study lesbians.

15. Id. at 293.

16. The 1990 Census counted 101,324,687 women over the age of 15, broken down into the following marital categories:

<table>
<thead>
<tr>
<th>Marital Status</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Never married</td>
<td>23,755,235</td>
</tr>
<tr>
<td>Now married</td>
<td>53,144,096</td>
</tr>
<tr>
<td>Separated</td>
<td>2,676,840</td>
</tr>
<tr>
<td>Widowed</td>
<td>12,121,939</td>
</tr>
<tr>
<td>Divorced</td>
<td>9,626,577</td>
</tr>
</tbody>
</table>


17. Not all lesbians live in couples. But given the tendency of lesbians to form couples, it is likely that most women who identify as lesbian will at some time be part of a couple. Blumstein & Schwartz, supra note 13, at 178.


together, with the two of them equally responsible for the child’s welfare.

Lesbian couples form households as various as those formed by married couples. Some may pool income and resources while others keep assets and income separate. Some plan to live together forever while some are clear about the short-term nature of their relationship. Often, as with married couples, the terms of the relationship are not spelled out and thus expectations of the partners may differ. Nonetheless, everyday transactions in lesbian households, such as the lending of property or money, or the payment by one partner for consumables that are shared by both partners, mirror in intent and consequence similar transactions in married couple households. The Internal Revenue Code, however, does not recognize the household as a legal entity, but only the legally married couple. Thus, the reality of lesbian households is ignored under current tax law.

III. TAXATION OF LESBIAN COUPLES

A. The Case of Uncertainty in the Tax Law

There are no special rules for taxing lesbian couples. Just like any unmarried couple, the lesbian couple can rely by analogy on cases that have been decided for husbands and wives. They cannot rely on special statutes designed for spouses. Thus, the partners in a lesbian couple who agree to pool income cannot shift the tax burden from the earner of the income to the non-earner. This is as true for husbands and wives as it is for unrelated taxpayers who live together in a committed relationship.

What is not clear for lesbian couples is the tax treatment of intra-couple transfers of property. While Lucas v. Earl decided that Mr. Earl could not shift income tax liability to Mrs. Earl, it did not decide the income tax consequences to Mrs. Earl of receipt of the pooled income benefit. Some scholars have argued that income pooling might create a double tax burden: a tax on the earner and a second tax

21. See Lucas v. Earl, 281 U.S. 111 (1930) (holding that an income splitting agreement between husband and wife would be ignored for tax purposes). The effect of Lucas v. Earl has been significantly minimized for spouses by the availability of joint return rates which allow husbands and wives, in effect, to split income between the earner and non-earner.
22. Id.
on the recipient. Why? Because receipts are presumed to be income unless there is a specific statutory exclusion. The most likely exclusion is Section 102, which excludes gifts. But unfortunately, we have a Supreme Court opinion, Commissioner v. Duberstein, which defines gifts so narrowly that the definition might not include transfers made pursuant to a binding agreement to share income. I have argued elsewhere that since such income pooling agreements come into existence because of love and affection, then any transfers made pursuant to the agreement are also based on love and affection. Such transfers are thus gifts, excluded from income.

Although I think such transfers are clearly gifts, it is disturbing that others continue to suggest in print and at tax workshops that such payments might constitute taxable income to the recipient. And yet, these suggestions are not so far-fetched given the Internal Revenue Service's traditional treatment of couples, married or not. The IRS has tended to view couples, including husbands and wives, as individuals who are capable of bargaining with each other in much the same way unrelated individuals negotiate commercial transactions. In other words, the IRS often determines the tax consequences of a two-party transaction by ignoring personal relationships and focusing solely on individuals as independent actors. The husband and wife relationship was finally recognized as a special unit with the passage of I.R.C. § 1041. But prior case law is available to IRS agents to argue that lesbian couples should be taxed on their most intimate agreements as though they were two businesswomen negotiating a business deal.

Because the tax law is completely silent regarding the tax treatment of lesbian couples, the tax consequences of intra-couple transactions is unknown. Absent a statute such as I.R.C. § 1041, which

26. See Cain, supra note 6, at 97.
27. See United States v. Davis, 370 U.S. 65 (1962) (holding that property transfers incident to divorce could be taxed as bargained-for exchanges).
28. "No gain or loss shall be recognized on a transfer of property from an individual to . . . (1) a spouse, or (2) a former spouse, but only if the transfer is incident to the divorce." I.R.C. § 1041(a) (West Supp. 1996).
covers only spouses, transfers of property between unmarried cohabitants may raise unexpected tax consequences. Let me give a specific example of how this silence in the tax law operates with respect to a problem that arises quite often in the lesbian community.

**Example:** Ann and Beth have agreed to live together for life. Ann currently owns her home, having purchased it ten years ago, shortly after her divorce from Al. Beth and Ann intend to share all living expenses equally. Ann promises Beth she can live with her in the home forever and Beth agrees to pay as much of the mortgage and utilities as she is able. However, since she makes less income than Ann, she is not likely to be able to pay a full half. None of this is in writing and of course neither Beth nor Ann has consulted a tax attorney. What are the tax consequences of this arrangement?

There are several approaches the IRS might take. The most likely approach would be for the IRS to argue that the payment from Beth to Ann is rent which must be reported on Schedule E. Ann would be allowed to claim certain deductions in full, e.g., allocable interest and property taxes, and other deductions subject to the limitations contained in I.R.C. § 280A. All of this seems unnecessarily complex since it is likely to result in no taxable income. But it will reduce the amount of interest and taxes available for Ann to claim as an itemized deduction on Schedule A. And if the payments from Beth to Ann occur in the later years of the mortgage, then there may be insufficient interest to offset the rental income generated. Ann would then have to claim depreciation deductions to offset the rental income and reduce basis by the amount of such depreciation. Furthermore, if and when she sold the home, the IRS could take the position that only part of the gain can be rolled over under I.R.C. § 1034 since she was selling both principal residence and rental real estate.

The IRS might also take the position that there is a taxable benefit to Beth to the extent that the fair rental value of the home exceeds what she is paying for the privilege of living there. If Beth has agreed to do the grocery shopping or other household chores, a creative IRS

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29. Section 1041 also covers transfers between ex-spouses so long as made incident to a divorce. *Id.*

30. Taxpayers who rent out a "dwelling unit" which is also used by the taxpayer as a residence can only deduct the expenses allocated to the rental use and cannot claim deductions in excess of rental income. I.R.C. § 280A (West Supp. 1996).
agent might take the position that the value of the rental use in excess
of what she pays for it is compensation income.\textsuperscript{31}

I prefer a different approach. In my view, Ann should not report
rental income. Nor should Beth report compensation income.
There's no real gain in this fact situation. Two people have decided to
share living expenses according to their relative financial abilities.
They are each paying for the benefits that they enjoy.\textsuperscript{32} If one of them
makes a payment that does benefit the other person more than her-
sell, then the excess payment should be viewed as a gift excluded from
income under § 102.\textsuperscript{33} The entire transaction arises out of love and
affection. There is no real landlord-tenant relationship here any more
than there is an employer/employee relationship.

Which approach should prevail? Since there is no clear authority
dealing with this situation, the IRS position I have outlined does not
appear unreasonable. And although I believe my approach should
ultimately prevail, the threat of the IRS challenge may be sufficient to
affect the tax position of lesbian couples. Given the vulnerability of
many lesbian and gay couples,\textsuperscript{34} their tax advisors sometimes suggest
that the wise approach is to file returns which do not connect the two
people. Thus, for example, Ann, who is supporting Beth, might
forego claiming a dependency exemption,\textsuperscript{35} even though she may be
legally entitled to claim Beth as a dependent under § 152(a)(9).\textsuperscript{36}

\textsuperscript{31} The IRS made a similar argument in a case in which ex-spouses decided to live together
and the ex-husband paid household expenses. The commissioner argued that the relationship
was one of employer/employee, as the ex-wife was responsible for housekeeping. The court

\textsuperscript{32} For example, if Beth pays half of the grocery bill and half of the utilities, we can view
those payments as benefitting Beth, not Ann.

\textsuperscript{33} For example, if Beth is also paying half of the mortgage principal, a debt of Ann's, then
Ann must either recognize income or claim that the benefit to her is a gift under I.R.C. § 102

\textsuperscript{34} Many lesbian and gay couples are closeted and thus unwilling to fight the IRS when an
issue is raised regarding tax liability.

\textsuperscript{35} The dependency exemption has been contested by the IRS when the payments to the
dependent can be characterized as compensation for services rendered. See Kieffer, 53 T.C.M. at
681; Peacock v. Commissioner, 37 T.C.M. (CCH) 177 (1978); Limpert v. Commissioner, 37 T.C.
447 (1961); Hamilton v. Commissioner, 34 T.C. 927, 928 (1960). Although the cases usually only
involve the person claiming the deduction, the recharacterization of payments as compensation
could subject the payor to FICA and FUTA taxes. See Rev. Rul. 54-572, 1954-2 C.B. 341; Priv.

\textsuperscript{36} Ann can claim Beth as her dependent for tax purposes so long as she provides over half
of Beth's support, Beth is a member of Ann's household for the full tax year, and Beth's gross
income is less than the exemption amount. I.R.C. §§ 151(c) and 152(a)(9) (West Supp. 1996).
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The result, then, of uncertainty and silence in the tax law, is that a class of persons (e.g., lesbian couples) may well over-report their taxable income. This occurs in part because lesbian couples have greater reason to fear challenges from the IRS than do other couples.

B. THE CASE OF CERTAIN AND UNFAVORABLE TAX LAW

Consider again the case of Ann and Beth. Assume that Ann earns $50,000 a year and that they decide to have a child. Since Beth is earning less than Ann, they decide that it will be better for Beth to become pregnant. Her absence from work will cost the couple less in lost income. Thus, they plan for Beth not only to give birth, but also to stay at home and raise the child. Because they use a sperm bank, there is no identifiable father. The two women agree to raise the child together and Ann agrees to support both Beth and the child.

Compare their situation to that of Arnold and Betty, who are also cohabitating outside of marriage and who decide to have a child. Both of them are recognized as parents of the child and agree to raise the child together. Arnold, who earns $50,000 a year, agrees to support both Betty and the child.

What is the tax payable by each couple? It will depend on two things: (1) whether Arnold and Ann can claim the members of their households as dependents, and (2) whether they can claim head of household filing status rather than single filing status.

So long as Ann is providing over half the support for both Beth and their child, she should be able to claim them both as dependents. If Beth's gross income exceeds the exemption amount, the exemption for her will be lost. Also, if the child's gross income exceeds the exemption amount, that exemption will be lost. Similarly, Arnold can claim an exemption for Betty and for their child. The only difference in the two cases is that if Arnold's child has gross income in excess of the exemption amount, he will not forfeit the dependency exemption.

37. See id.

38. The exemption amount in the Code is $2,000, but it is adjusted annually for inflation. All computations in this Essay will be based on the amounts as stated in the Code, unadjusted for inflation. I.R.C. § 151(d) (West Supp. 1996).

39. See I.R.C. § 151(c)(1)(B) (West Supp. 1996) (dependency exemptions for children under age 19 and for children who are students under age 24 are not contingent upon child's gross income). This provision only applies to children of the taxpayer. Although a child can include a "stepchild," I do not believe the IRS or the courts will read the definition of
If we assume that Ann and Arnold have no deductions other than the personal and dependency exemptions, then we can compare their ultimate tax liability. They will both claim the standard deduction rather than itemized personal deductions.

At this point it becomes crucial to determine whether Ann can claim head of household status. To claim head of household, she must maintain as her home a household which serves as the principal place of abode for more than half the year of a person whom she can claim as a dependent. Under my assumed facts, Ann does maintain a household because she provides over half the cost of the home.\(^4\) It is also her home because she lives there. And it is also the home of two people whom she can claim as dependents, Beth and their child. However, if the only reason she can claim Beth and the child as dependents is because they fit the definition of § 152(a)(9), then Ann will not be allowed to claim head of household status.\(^4\) Since neither Beth nor the child are related to her, she cannot claim them except under § 152(a)(9). Her only argument will be that Beth's child is her stepchild,\(^4\) an argument that is not likely to prevail.

Arnold can claim head of household status. Although he claims Betty as a dependent solely on the basis of § 152(a)(9), the child is his own. Section 2(b)(1)(A)(i) grants head of household status if the maintained home is the home of the taxpayer and a child or stepchild of the taxpayer.\(^4\)

Using the higher standard deduction available for heads of household, Arnold's taxable income, after all deductions, is $39,600.\(^4\)


\(^4\) See I.R.C. § 2(b)(3)(B)(i) (West Supp. 1996) ("[f]or purposes of this subtitle a taxpayer shall not be considered to be a head of household . . . by reason of an individual who not be a dependent for the taxable year but for . . . paragraph (9) of section 152(a)").

\(^4\) In some jurisdictions Ann may be able to adopt the child. Adopted children qualify as children of the taxpayer. However, most adoption statutes are written in a way that normally prevents two parents of the same sex from adopting. But see Matter of Jacob, 660 N.E.2d 397 (N.Y. 1995); In re Adoption of Tammy, 619 N.E.2d 315 (Mass. 1993). These cases recognized the right of the nonbiological mother to adopt the child of her lesbian partner so that the child would have two parents. Interpreting the statute to permit both lesbian mothers to become legal parents was thought to be in the best interest of the child.

Alternatively, Ann might adopt Beth. But see In re Robert Paul P., 471 N.E.2d 424 (N.Y. 1984) (holding that gay male could not adopt his adult partner).

\(^4\) If a descendant of a child or stepchild lives there, the taxpayer may qualify as well. I.R.C. § 2(b)(1)(A)(i) (West Supp. 1996).

\(^4\) $50,000 minus $6,000 personal exemptions and dependency deductions minus $4,400 standard deduction.
Applying the head of household rate schedule, the amount of tax he owes is $7,240. Ann, by contrast, has taxable income of $41,000. Her tax bill is $8,607. The difference is $1,367. Ann and Beth end up paying a higher tax bill than similarly situated unmarried heterosexual couples.

It is true that much of Ann and Beth’s difficulty stems not directly from the tax law but from state family law. State law does not recognize Ann and Beth and their child as a family. Unfortunately, much of federal tax law incorporates state family law. But tax law ought to recognize the reality of Ann and Beth’s situation. Head of household rates were intended to give taxpayers who were supporting others, in particular children, some of the benefits of income splitting. The net result is to provide a tax subsidy for some parents and not for others, a result that is hard to explain. Two possible explanations occur to me: (1) the result is an oversight in that lesbian lives were never considered when the head of household rules were drafted, or (2) the result stems from intentional discrimination against lesbians.

**IV. CONCLUSION**

Lesbian couples face a number of tax difficulties. I have raised only two specific problems that arise under the income tax. My first example is illustrative of problems that arise because tax rules are not clear. My second example is illustrative of problems that arise because tax rules are clear. Both sorts of problems arise because the tax law was written with a blind eye toward the reality of lesbian lives. It is time to take a closer look at the tax inequities that result from this blindness. As Professor McCaffery has argued, sound tax policy cannot be based on patriarchal assumptions about who works and who stays home. Nor should it exclude the reality of real taxpayers who are working wives, mothers, and yes, lesbians.

45. $50,000 minus $6,000 personal exemption and dependency deductions minus $3,000 standard deduction.

A SOCIO-THEORETIC OVERVIEW