



# LESSER KNOWN FEDERAL INCOME TAX FILING TIPS AND RELATED INFO

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This is the time of year when income tax filing questions arise. The following presents selected tax filing tips and related information somewhat off the beaten path.

## Joint Income Tax Returns

It is widely known that if a couple is legally married as of December 31, the couple may file a joint tax return for the year. This is often beneficial if one spouse has substantially more income than the other – usually resulting in the higher level income taxable in a lower tax bracket. In such situations, it is not uncommon for divorces concluding late in a calendar to defer entry of judgment into the succeeding year to take advantage of joint tax return filing one last time.

Whenever a joint return may be filed for a year and it is certain the parties will be divorced in the following year, the following matters may be relevant.

### Joint and Several Liability

Parties will be jointly and severally liable for unpaid taxes and/or deficiencies later arising from an IRS tax examination. So, if it is suspected that one spouse is underreporting income and/or claiming excessive deductions, it is generally advisable that the other spouse not agree to file jointly.

While Innocent Spouse Relief protects some unwary joint filers from liability, such protection may not be available if a spouse had reason to believe that income is understated or deductions are padded.

**Take Away** – Consider potential liability before agreeing to file jointly to achieve tax savings.

### Joint Tax Refunds

Most divorce settlements provide for the division of a tax refund on the final joint return. The check will be sent to the address on the return and will be payable to both parties. Thus, delay in receipt of a refund may result if the principal residence is used on the return and the refund is sent after the house is sold and the effective “forwarding address” period has expired. If this is foreseeable, use another address on the return (e.g., in care of the CPA/tax preparer).

**Take Away** – Consider any potential logistical problems concerning receipt of a joint tax refund and make appropriate arrangements.

### Joint Tax Overpayments Applied to Estimated Tax

Many taxpayers apply for extensions rather than filing by April 15. And most with income not subject to withholding – LLC income; S Corporation income; investment income – must make estimated tax payments due April 15, June 15, September 15, and January 15 each year.

An overpayment from a prior year is deemed received by the IRS as of the April 15 initial due date even if the return is filed six months later at or near the October 15 extended due date. Thus, it is often advantageous to apply an overpayment to the succeeding year tax liability, especially if a taxpayer realizes late in the year when the return is filed that preceding estimated payments are insufficient to avoid the underpayment tax liability. This can be done with the entire overpayment or just part of it, with the balance refunded.

Parties are free to agree on the application of an overpayment on a joint return to the next year’s tax. If the amount so applied is allocated 100% to the husband, nothing needs to be done on either spouse’s succeeding year tax return. However, if such amount applied exceeds 50% of the overpayment that is to be divided equally, husband will need to make an after-tax payment to wife to square things off.

If any of the overpayment is to be applied to wife’s tax, she must enter husband’s SSN in the appropriate space on page one of her Form 1040 followed by “DIV”. If wife has remarried, she must enter ex-husband’s SSN at the bottom of Form 1040 page one, again followed by “DIV”.

**Take Away** – If either party relies on estimated tax payments and an overpayment is possible, make provisions in advance for potential advantageous use of the overpayment.

### Married Filing Separately

Parties legally married at year-end – or either of them – may choose not to file a joint return. As indicated above, this will generally result in a higher combined tax than if they filed jointly. The usual reason for “married filing separately” vs.

jointly is concern over liability for the other spouse's suspected improper reporting of income or deductions.

Not only are the tax brackets 50% of joint tax brackets – meaning, of course, reaching the next higher bracket twice as fast – but there are other negatives to “married filing separately” status, including:

- Both spouses must either itemize deductions or use the standard deduction. The route selected by the first to file locks in the other spouse.
- Neither spouse may claim (1) the earned income credit; (2) the credit for child and dependent care expenses; (3) the credit for adoption expenses (in most cases); or (4) the credit for higher education expenses.
- Threshold income limits that reduce the child tax credit, itemized deductions, and personal exemptions are half of the limits on a joint return.
- The standard deduction is also half the amount on a joint return.

**Take Away** – If there is meaningful suspicion of improper reporting by the other spouse, it is generally advisable not to file a joint return. But, absent such suspicion, refusing to do so can result in a significantly higher combined tax liability.

While a judge cannot force a party to file a joint return, such party can be charged with receipt of the increased tax if no valid reason for refusing to file – often presented in chambers – has been proffered.

## Estimated Taxes

Many recipients of spousal support have never needed to make quarterly estimated tax payments. However, since no income tax is withheld on spousal support payments, estimated tax payments are generally necessary to avoid (1) a large April 15 payment and (2) corresponding underpayment of tax penalties. This applies to both federal and state income taxes.

The underpayment penalty may be avoided if the amount paid in – via wage withholding or estimated tax payments – exceeds the party's hypothetical prior year tax based solely on his or her individual income and deductions. This often applies in the first year of receipt of spousal support, but not generally to subsequent years.

**Take Away** – Attorneys should advise clients awarded spousal support to contact his or her tax advisor regarding estimated tax payment requirements.

## About the Author

*Joe Cunningham has over 25 years of experience specializing in financial and tax aspects of divorce, including business valuation, valuing and dividing retirement benefits, and developing settlement proposals. He has lectured extensively for ICLE, the Family Law Section, and the MACPA. Joe is also the author of numerous journal articles and chapters in family law treatises. His office is in Troy though his practice is statewide.*