Election for Married Couples Unincorporated Businesses

An unincorporated business jointly owned by a married couple is generally classified as a partnership for Federal tax purposes. For tax years beginning after December 31, 2006, the Small Business and Work Opportunity Tax Act of 2007 (Public Law 110-28) provides that a "qualified joint venture," whose only members are a married couple filing a joint return, can elect not to be treated as a partnership for Federal tax purposes.

Reasons Why a Married Couple Might Want to Make the Election Not to be Treated as a Partnership

Because a business jointly owned and operated by a married couple is generally treated as a partnership for Federal tax purposes, the spouses must comply with filing and record keeping requirements imposed on partnerships and their partners. Married co-owners failing to file properly as a partnership may have been reporting on a Schedule C in the name of one spouse, so that only one spouse received credit for social security and Medicare coverage purposes. The election permits certain married co-owners to avoid filing partnership returns, provided that each spouse separately reports a share of all of the businesses' items of income, gain, loss, deduction, and credit. Under the election, both spouses will receive credit for social security and Medicare coverage purposes.

Definition of a Qualified Joint Venture

A qualified joint venture is a joint venture that conducts a trade or business where (1) the only members of the joint venture are a married couple who file a joint return, (2) both spouses materially participate in the trade or business, and (3) both spouses elect not to be treated as a partnership. A qualified joint venture, for purposes of this provision, includes only businesses that are owned and operated by spouses as co-owners, and not in the name of a state law entity (including a limited partnership or limited liability company) (See below). Note also that mere joint ownership of property that is not a trade or business does not qualify for the election. The spouses must share the items of income, gain, loss, deduction, and credit in accordance with each spouse's interest in the business. The meaning of "material participation" is the same as under the passive activity loss rules in section 469(h) and the corresponding regulations (see Publication 925, Passive Activity and At-Risk Rules). Note that, except as provided in section 469(c)(7), rental real estate income or loss generally is passive under section 469, even if the material participation rules are satisfied, and filing as a qualified joint venture will not alter the character of passive income or loss.

How to Make the Election to be Treated as a Qualified Joint Venture

Spouses make the election on a jointly filed Form 1040 by dividing all items of income, gain, loss, deduction, and credit between them in accordance with each spouse's respective interest in the joint venture, and each spouse filing with the Form 1040 a separate Schedule C (Form 1040), Profit or Loss From Business (Sole Proprietorship) or Schedule F (Form 1040), Profit of Loss From Farmingand, if otherwise required, a separate Schedule SE (Form 1040), Self-Employment Tax. For example, to make the election for 2014, jointly file your 2014 Form 1040, with the required schedules (see below). The partnership terminates at the end of the taxable year immediately preceding the year the election takes effect. For information on how to report the business for the taxable year before the election is made, see Publication 541 on Partnerships and terminations.

A Business Owned and Operated by the Spouses through a Limited Liability Company Does Not Qualify for the Election

Only businesses that are owned and operated by spouses as co-owners (and not in the name of a state law entity) qualify for the election. See Rev. Proc. 2002-69, 2002-2 C.B. 831, for special rules applicable to married couple state law entities in community property states.

How to Report Federal Income Tax as a Qualified Joint Venture (Including Self-Employment Tax)

Spouses electing qualified joint venture status are treated as sole proprietors for Federal tax purposes. The spouses must share the businesses' items of income, gain, loss, deduction, and credit. Therefore, the spouses must take into account the items in accordance with each spouse's interest in the business. The same allocation will apply for calculating self-employment tax if applicable, and may affect each spouse's social security benefits. Each spouse must file a separate Schedule C (or Schedule F) to report profits and losses and, if otherwise required, a separate Schedule SE to report self-employment tax for each spouse. Spouses with a rental real estate business not otherwise subject to self-employment tax must check the QJV box on Line 2 of Schedule E.

However, if there are other net earnings from self-employment of $400 or more, the spouse(s) with the other net earnings from self-employment should file Schedule SE without including the amount of the net profit from the rental real estate business from Schedule E on line 2. If the election is made for a farm rental business that is not included in self-employment, file two Forms 4835 instead of Schedule F.

In General, Spouses Do NOT Need an Employer Identification Number (EIN) for the Qualified Joint Venture

Spouses electing qualified joint venture status are treated as sole proprietors for Federal tax purposes. Using the rules for sole proprietors, an EIN is not required for a sole proprietorship unless the sole proprietorship is required to file excise, employment, alcohol, tobacco, or firearms returns. If an EIN is required, the filing spouse should complete a Form SS-4 and request an EIN as a sole proprietor.

What to Do if the Spouses Already Have an EIN for the Partnership

One spouse cannot continue to use that EIN for the qualified joint venture. The EIN must remain with the partnership (and be used by the partnership for any year in which the requirements of a qualified joint venture are not met). If you need EINs for the sole proprietorships, see above on EINs for sole proprietors.

How to Handle Requests from the IRS for a Partnership Return from the Spouses for Tax Years for Which the Election is in Effect

Once the election is made, if the spouses receive a notice from the IRS asking for a Form 1065 for a year in which the spouses meet the requirements of a qualified joint venture, the spouses should contact the toll-free number that is shown on the notice and advise the telephone assistor that they reported the income on their jointly-filed individual income tax return as a qualified joint venture. Alternatively, the spouses can write to the address shown on the notice and provide the same information.

If the Spouses Elect to be Treated as a Qualified Joint Venture, How Do They Report and Pay Federal Employment Taxes?

If the business has employees, either of the sole proprietor spouses may report and pay the employment taxes due on wages paid to the employees, using the EIN of that spouse's sole proprietorship. If the business already filed Forms 941 or deposited or paid taxes for part of the year under the partnership's EIN, the spouse may be considered the "successor employer" of the employee for purposes of determining whether the wages have reached the social security and Federal unemployment wage base limits. See Publication 15 for more information on the successor employer rules. See above regarding the allocation of the deductions for income tax purposes.

Duration that the Election Remains in Effect

Once the election is made, it can be revoked only with the permission of the IRS. However, the election technically remains in effect only for as long as the spouses filing as a qualified joint venture continue to meet the requirements for filing the election. If the spouses fail to meet the qualified joint venture

requirements for a year, a new election will be necessary for any future year in which the spouses meet the requirements to be treated as a qualified joint venture.

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