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The Husband-Wife Qualified Joint Venture Filing Option:

Proper Social Security and Medicare Crediting and Simplified Tax Reporting

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The Qualified Joint Venture Filing Option

Do you prepare tax returns for or know of a husband and wife who co-own and co-operate a trade or business? If so, now may be a good time to inform them of the Qualified Joint Venture (QJV) filing option. The potential benefit to the spouses: proper Social Security and Medicare crediting and simplified tax reporting.

Why the QJV Filing Option?

The Partnership Approach

An unincorporated business jointly owned by a married couple is generally treated as a partnership for federal tax purposes. As a tax partnership, the couple must file at least seven tax return forms and schedules for their business (see table below). Form 1065 and the Schedules K-1 are typically the most difficult and expensive to prepare.

The Sole Proprietorship Approach

To avoid the burden of preparing partnership tax returns, many married couples treat their jointly-owned businesses as sole proprietorships. Under this approach, a couple may only have to file three tax forms and schedules for their business (see table below), including one Schedule C or F and one Schedule SE. Because a Schedule SE is filed for only one spouse, the other spouse does not receive Social Security and Medicare credit for his or her share of self-employment earnings from the business.

The QJV Filing Option

To remedy the imbalance between the two approaches, Congress enacted Internal Revenue Code ("Code") Section 761(f), which provides for the QJV filing option. Under the QJV filing option, a married couple may elect to treat their qualifying business as a QJV and file tax forms and schedules as if they were each sole-proprietors (see table below). Each spouse files a Schedule C or F and a Schedule SE with the couple's joint Form 1040, which ensures both spouses receive proper Social Security and Medicare credit. Under the QJV filing option, no partnership tax returns are required. In this manner, the QJV election provides a "best of both worlds" approach: simplified tax reporting and full Social Security and Medicare crediting.

Filing Option	Forms / Schedules	Advantages	Disadvantages
Sole Proprietorship	1 Form 1040 1 Schedule C or F 1 Schedule SE	Taxpayer only files one form and two schedules.	Only one spouse receives Social Security and Medicare credit.
Qualified Joint Venture	1 Form 1040 2 Schedules C or F 2 Schedules SE	Taxpayer does not have to file Form 1065 or Schedules K-1. Both husband and wife receive Social Security and Medicare credit.	Increased burden to file an additional Schedule C (or F) and Schedule SE.
Partnership	1 Form 1065 2 Schedules K-1 1 Form 1040 1 Schedule E 2 Schedules SE	Both spouses receive Social Security and Medicare credits.	This option requires the highest number of forms and schedules.

What Type of Business Qualifies as a QJV?

A qualified joint venture is defined as a trade or business where: (1) the only members of the business are a husband and wife; (2) the husband and wife file a joint tax return and elect not to be treated as a partnership under Code Section 761(f); and (3) both spouses materially participate in the business, as defined under Code Section 469(h) and the corresponding Treasury Regulations, without regard to Code Section 469(h)(5).

- **Note: The QJV filing option is not allowed for a state law entity. Only a business co-owned and co-operated by a husband and wife may qualify as a QJV.**

Making the QJV Filing Option Election

- To make the election, the spouses must divide all items of income, gain, loss, deduction and credit between each other in accordance with their respective interests in the business. These items are then reported on each spouse's Schedule C (or Schedule F in the case of farming activities). The spouses must also file separate Schedules SE.

- The election is effective for as long as the business meets the QJV requirements and may only be revoked with IRS approval.
- If the QJV requirements are not met in a given year, the business will be treated as a partnership, and a new QJV election will be necessary if the spouses desire to file as a QJV in a future year in which the QJV requirements are met.
- If partnership tax returns were previously filed for the business, the partnership's EIN is not used when filing as a QJV. Rather, the EIN remains with the partnership and should be used by the partnership in any future year in which the requirements of a QJV are not met.

Additional Considerations

- *State Law Entities* – As noted above, a business owned in the name of a state law entity (e.g., a general partnership, limited partnership or a limited liability company ("LLC")), cannot qualify as a QJV.
- *Trade or Business* – The spouses must be engaged in a trade or business to qualify as a QJV. **Mere co-ownership of property is not enough**. **Consequently, the QJV option is not available to spouses who merely co-own rental or investment real estate which does not arise to a trade or business.**
- *Partnerships Electing QJV Filing Option* – If the spouses operate their business as a partnership and make the QJV filing election, the IRS has stated only the partnership filing requirement is terminated, not the partnership itself.
- *Employer Identification Number (EIN)* – Because spouses are treated as sole proprietors under the QJV filing option, they are not required to obtain an EIN unless otherwise required by the rules for sole proprietors, i.e., if the sole proprietorship is required to file excise, employment, alcohol, tobacco, or firearms returns. For obvious privacy reasons, however, obtaining an EIN may be warranted.
- *Tax Advice* – Prior to making an election, a careful analysis of both spouses' tax situation is warranted.
- *LLCs in Community Property States* – Although the QJV filing election is not available if spouses own a business through an LLC, if spouses live in a community property state and own an LLC as community property, they may elect to treat the LLC as a disregarded entity and file tax returns accordingly. See Rev. Proc. 2002-69.

Conclusion

Married couples who co-own and operate businesses should be informed of the QJV filing option. The QJV filing option can eliminate the additional time and expense of preparing partnership tax returns while ensuring both spouses receive full Social Security and Medicare credit.

If you have any questions or desire to learn more about the QJV filing option, please contact Larry Brant, Steve Nofziger or Jason Faas at (503) 228-3939.

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