

EMPLOYMENT TAX IMPLICATIONS AFTER DOMA

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PANELISTS

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OVERVIEW

- ▶ Overview of the *Windsor* Decision
- ▶ Summary of IRS and DOL Guidance
- ▶ Impact on Health and Welfare/Fringe Benefit Plans
- ▶ Impact on FMLA Policies
- ▶ Impact on Qualified Retirement Plans
- ▶ Pending IRS Guidance/Open Issues
- ▶ Update on Employee Benefits Litigation
- ▶ Action Steps

U.S. V. WINDSOR (June 26, 2013): **THE DECISION**

- ▶ **Summary:** Windsor and Spyer met in 1963; became NY domestic partners in 1993; married in Toronto in 2007; Spyer died in 2009 leaving \$363,053 estate tax bill
- ▶ Section 3 of the Defense of Marriage Act (“DOMA”) is unconstitutional:
 - ▶ Limited federal definition of marriage/spouse to opposite-sex unions
- ▶ Section 2 of DOMA remains:
 - ▶ Allows states to refuse to recognize the validity of same-sex marriages that were legally performed in other states.

SCOPE OF CHANGES

- ▶ Decision issued on June 26, 2013; USDOJ statement issued June 28, 2013 extending federal benefits to same-sex couples
- ▶ Per CRS report, 1,138 statutory provisions in the U.S. Code in which marital status was a factor in determining benefits.
 - ▶ All federal regulations affected as well
- ▶ Roughly 200 of the provisions are Internal Revenue Code sections that include the terms “spouse,” “marriage,” “husband” and/or “wife”

PATCHWORK OF STATE LAWS RE: SAME-SEX MARRIAGE

- ▶ Same-sex marriage licenses issued in: CA, CT, DC, DE, HI, IA, IL (6/1/14), IA, ME, MD, MA, MN, NH, NJ, NM, NY, RI, VT and WA
 - ▶ UT: State prohibition struck down 12/20/13; SCOTUS granted stay pending appeal 1/6/14 – USDOJ will recognize the roughly 1,300 12/20/13-1/6/14 marriages
 - ▶ IL: 2/21/14 N.D. Ill. authorized SSM in Cook County; 3/4/14 AG says county clerks should find decision “persuasive”; 3/4/14 Gov. says Ill. DPH will accept marriage licenses issued by any Ill. county
 - ▶ MI: State prohibition struck down 3/21/14; 6th Cir. granted stay 3/22/14; no guidance yet from DOJ for roughly 300 marriages
- ▶ Foreign countries: Argentina, Belgium, Brazil, Canada, Denmark, France, Iceland, Netherlands, New Zealand, Norway, Portugal, Spain, South Africa, Sweden, UK (England/Wales 3/29/14; Scotland 10/2014), Uruguay)

PATCHWORK OF STATE LAWS RE: SAME-SEX MARRIAGE (cont.)

- ▶ States that *prohibit* same-sex marriages (and recognition of such marriages that were performed in other states)
 - ▶ AL, AK, AZ, AR, FL, GA, ID, IN, KS, KY, LA, MI, MS, MO, MT, NE, NC, ND, OH, OK, PA, SC, SD, TN, TX, UT, VA, WV, WY
 - ▶ OK: State prohibition struck down by District Court 1/14/14; immediate stay;
 - ▶ KY: State recognition prohibition struck down by District Court 2/12/14 – suggested state prohibition on performing SSM wouldn't survive constitutional challenge;
 - ▶ VA: State prohibition struck down by District Court 2/13/14 immediate stay;
 - ▶ TX: State prohibition struck down by District Court 2/26/14 immediate stay;

WHAT *WINDSOR* DID NOT DO

- ▶ Extend federal recognition to same-sex couples with civil unions or domestic partnerships (“This opinion and its holding are confined to those lawful marriages.”)
- ▶ Require states to legalize same-sex marriages
- ▶ Require states to recognize same-sex marriages legally performed in other jurisdictions
- ▶ Require health plans to cover same-sex spouses
- ▶ Hold that members of the LGBT community are entitled to heightened scrutiny under the Equal Protection Clause of the 14th Amendment (***But*** heightened scrutiny for distinctions based on sexual orientation in 9th Cir.)

REVENUE RULING 2013-17

- ▶ **Definition of Spouse** for federal tax law:
 - ▶ “Spouse,” “marriage,” “husband,” and “wife” includes spouses of the same-sex, if couple is legally married under state or foreign law;
 - ▶ *Place of celebration* controls the definition of spouse; and
 - ▶ “Marriage” does not include domestic partnerships or civil unions under state law.

REVENUE RULING 2013-17 (cont.)

Effective date: September 16, 2013

- ▶ Applies to all qualified plans and health plans (to extent impacted), even if plan amendments not yet adopted
- ▶ Taxpayers *may* rely on the ruling retroactively with respect to:
 - ▶ Filing amended returns (2010 still in statute until 4/15/14), and/or
 - ▶ Filing claims for refunds of overpaid taxes

REVENUE RULING 2013-17

- ▶ No longer taxable benefits to same-sex spouse:
 - ▶ Code § 106 (health care coverage);
 - ▶ Code § 117 (qualified tuition reduction);
 - ▶ Code § 119 (meals and lodging for convenience of employer);
 - ▶ Code § 125 (cafeteria plans);
 - ▶ Code § 129 (dependent care assistance plans); and
 - ▶ Code § 132 (fringe benefits, such as employee discounts, retirement planning services).

IRS Frequently-Asked-Questions ("FAQS")

- ▶ Two sets of FAQs:
 - ▶ Same-sex marriages (major changes)
 - ▶ Domestic partners (no changes in tax treatment)
- ▶ Income Tax and Filing Status: FAQs 1-9
 - ▶ Same-sex married couples now MFJ or MFS
 - ▶ Previously, SSM couples filing state MFJ had to draft MFJ 1040 for state return, then file MFJ state and single 1040
 - ▶ State filing status still determined at state level
 - ▶ **Beware:** Marriage penalty and joint & several liability
 - ▶ MFS: If one spouse itemizes, both have to
 - ▶ Now subject to community property rules and married for passive RE loss purposes

IRS Frequently-Asked-Questions ("FAQS") (cont.)

- ▶ Tax treatment of health/welfare coverage: FAQs 10-14
 - ▶ Provide examples of amounts eligible for refund, and the refund process by the employer/employee
 - ▶ Income Tax Refunds: Form 1040-X for years in statute
 - ▶ Employment Tax Refunds: Notice 2013-61 procedures; (Q21) employee should first seek FICA refund from employer – if employer won't adjust, employee can file Form 843 with "Windsor Claim" at top margin
 - ▶ FUTA: sole prop may claim FUTA refund for compensation paid to same-sex spouse as employee in the business
- ▶ Impact on Qualified Plans: FAQs 16-19
 - ▶ Explains that effective Sept. 16, a spouse must include same-sex marriages for "qualification requirements that relate to spouses"

NOTICE 2013-61

- ▶ Streamlined employer process for correcting payroll post-DOMA
 - ▶ 2013:
 - ▶ No imputed income as of 9/16/2013 (or earlier, if elected)
 - ▶ Process to adjust taxes on 4Q 2013 Form 941 and avoid the need for a 2013 W-2c/941-X
 - ▶ If SS wages > \$113,700 without imputed income then no correction
 - ▶ Prior Years:
 - ▶ Streamlined employer FICA refund process for prior open tax years (if employer elects to issue W-2c and file 4Q Form 941-X)

DOL TECHNICAL RELEASE 2013-04

- ▶ Department of Labor (“DOL”) follows Revenue Ruling – adopts “place of celebration” rule
 - ▶ A spouse for Title I of the Employee Retirement Income Security Act (“ERISA”) includes all same-sex marriages that were validly performed in a domestic or foreign jurisdiction
- ▶ No Effective Date
- ▶ Opens up participant’s right to sue for benefits
- ▶ Does this require that health and welfare plans cover same-sex spouses?

NOTICE 2014-1

- ▶ Effective date: 12/16/13
- ▶ Amplifies Rev. Rul. 2013-17
- ▶ Addresses cafeteria plan treatment of same-sex spousal coverage
 - ▶ Mid-Year Election Changes
 - ▶ Flexible Spending Account (“FSA”) Reimbursements
 - ▶ Contribution Limits for Health Savings Accounts (“HSAs”) and Dependent Care FSAs
 - ▶ Written Plan Amendments

NOTICE 2014-1

▶ Mid-Year Election Changes

- ▶ *Windsor* decision treated as a change-in-status event (i.e., change in legal marital status) for spouses lawfully married as of the date of the decision (June 26,2013) and after.
- ▶ Change in tax treatment alone does not constitute a “significant change in the cost of coverage” under cafeteria plan regulations but transition relief provided for 2013.

NOTICE 2014-1

▶ Mid-Year Election Changes

- ▶ Cafeteria Plan election with respect to coverage for same-sex spouse made between 6/26/13 and 12/16/13 must be effective no later than the later of:
 - ▶ the date the election would be effective under the cafeteria plan, or
 - ▶ a reasonable period of time after 12/16/13.
- ▶ Cafeteria Plan election made after 12/16/13 must be effective on the date that any other change becomes effective.

NOTICE 2014-1

▶ Mid-Year Election Changes

- ▶ Employer must begin to treat health coverage for a same-sex spouse as a pre-tax election under cafeteria plan as of the later of:
 - ▶ The date that an employer is required to be reflected for income tax withholding purposes, or
 - ▶ A reasonable period after 12/16/13.
- ▶ Employee can exclude and/or apply for refund for income and employment taxes.

NOTICE 2014-1

▶ FSA Reimbursements

- ▶ May reimburse covered expenses of the same-sex spouse or the same-sex spouse's dependent beginning on the first day of the cafeteria plan year that includes the date of the *Windsor* decision (6/26/13), or, if later, the date of the marriage.
- ▶ FSA election need not specifically identify same-sex spouse in order for employee to receive reimbursement.

NOTICE 2014-1

- ▶ Contribution Limits for HSAs and Dependent Care FSAs
 - ▶ HSA: Same-sex spouses must comply with family contribution limit of \$6,450 beginning in 2013.
 - ▶ Dependent Care FSA: Same sex spouses are subject to Dependent Care Assistance Plan (“DCAP”) contribution limits of the lesser of \$5,000 (\$2,500 for married, filing separately) or the employee or spouse’s earned income.

NOTICE 2014-1

▶ Written Plan Amendments

- ▶ Cafeteria plan may not need to be amended
- ▶ If plan sponsor chooses to permit election changes that were not previously provided in plan document, those changes must be in writing
 - ▶ Transition relief for plan amendments (until 12/31/14 for calendar year plans)
 - ▶ Amendments can be retroactive to 2013

DOL GUIDANCE – FMLA

- ▶ DOL “Fact Sheet” (August 2013) -- “spouse” for **FMLA** purposes refers to:

“a husband or wife as defined or recognized under state law . . . *In the state where the employee resides*, including ‘common law’ marriage and same-sex marriage.”

IMPACT ON HEALTH AND WELFARE/FRINGE BENEFIT PLANS

- ▶ Same-sex spouse benefits tax-free (or pre-tax) as available to opposite sex spouses – so no more imputed income
- ▶ Spousal rights/restrictions under the Code (and ERISA) apply to same-sex spouses

IMPACT ON QUALIFIED RETIREMENT PLANS

- ▶ Spousal rights/restrictions under the Code (and ERISA) apply to same-sex spouses, including:
 - ▶ QJSA and death benefits (e.g., right to survivor annuities, including preretirement survivor annuities)
 - ▶ Spousal consent rights (e.g., to distributions and loans)
 - ▶ Hardship distributions rights (e.g., safe harbor hardship distributions for unreimbursed medical, post secondary, educational and funeral expenses)
 - ▶ Spousal rollover rights
 - ▶ Minimum Required Distributions (e.g., delay of RMD payments until participant would have been age 70½)
 - ▶ QDRO rights
 - ▶ Default beneficiary rules
- ▶ Special considerations for governmental and church plans
- ▶ Owner, Employee Determination and Attribution rules
- ▶ Prohibited Transactions

PENDING IRS GUIDANCE/ OPEN ISSUES

▶ Qualified Retirement Plans

- ▶ Possible Retroactive Effective Date
- ▶ Correction actions may be needed for qualified plan status
- ▶ Plan amendments
- ▶ Impact on Title I (ERISA) benefit claims
 - ▶ Potential for claims from multiple parties
 - ▶ Example 1: Participant and same-sex spouse separate but do not divorce. Participant subsequently designates children as beneficiaries without consent of estranged spouse. Participant dies. Who is beneficiary?
 - ▶ What if marriage license was issued by rouge clerk in state that prohibits same sex marriage? What if state law is silent on same-sex marriage?

UPDATE ON EMPLOYEE BENEFITS LITIGATION

- ▶ Challenges to state “mini-DOMA” laws
- ▶ Retroactive effect of *Windsor*
- ▶ Can health plans limit spouses to only those of the opposite sex?
 - ▶ *Hall v. BNSF Railway Co.*, 13-cv-02160 (W.D. WA)

LITIGATION ISSUES

- ▶ First post-*Windsor* employee benefits decision: *Cozen O'Connor P.C. v. Tobits*, 2013 WL 3878688 (E.D. Pa. July 29, 2013)
- ▶ Widow of same-sex couple who married in Canada and resided in IL is entitled to surviving spouse benefit under pension plan
- ▶ ERISA and the Code establish the “floor” for spousal rights in pension plans; *Windsor* “leveled the floor”
- ▶ Administrator of PA-based plan not bound by PA law, notwithstanding PA choice of law provision

LITIGATION ISSUES

- ▶ Constitutionality of state non-recognition laws: *Obergefell v. Kasich*, 2013 WL 8314262 (S.D. Ohio July 22, 2013)
- ▶ Granting TRO to prohibit local Ohio registrar from accepting death certificate that did not list decedent as married and same-sex spouse as surviving spouse
- ▶ Couple married in Maryland, resided in Ohio
- ▶ 2004 Ohio law prohibits recognition of same-sex marriages performed out of state
- ▶ Law denies equal protection by discriminating between opposite-sex couples married out of state and same-sex couples married out of state

LITIGATION ISSUES

- ▶ Retroactive changes to pre-*Windsor* pension benefits, e.g.
 - ▶ Payment of single-life annuity to married participant
 - ▶ Denial of survivor annuity to surviving same-sex spouse
 - ▶ Form of distribution to same-sex surviving spouse under defined contribution plan
 - ▶ Distribution from defined contribution plan to non-spouse beneficiary without spousal consent

LITIGATION ISSUES

- ▶ Treatment of civil union partners and registered domestic partners as spouses
- ▶ Participant communication issues: if plan excludes same-sex spouses, does summary plan description (SPD) disclose this?
- ▶ Title VII issues: if plan excludes same-sex spouses but includes opposite-sex spouses, does the plan discriminate on the basis of sex?

ACTION STEPS – QUALIFIED RETIREMENT PLANS

- ▶ Effective September 16, 2013 – Treat all same-sex spouses as “spouses” for plan purposes, regardless of plan terms or state law
 - ▶ Review/update open/general enrollment forms
 - ▶ Review/update plan policies and distribution forms:
 - ▶ Plan rollovers
 - ▶ Minimum Required Distributions
 - ▶ QDROs
 - ▶ Hardship withdrawals
 - ▶ HCE/Key Employee designations
 - ▶ QJSA/QOSA/QPSA survivor benefits

ACTION STEPS— QUALIFIED RETIREMENT PLANS

- ▶ Participant communications
 - ▶ Encourage updates to beneficiary designation forms (no requirement to seek out information about marital status)
 - ▶ Require indication of marital status on distribution forms
 - ▶ Notify of need for spousal consent, when required
- ▶ Discuss plan's current treatment of domestic partners and civil unions
- ▶ Third party administrators and other service agreements

ACTION STEPS – HEALTH AND WELFARE PLANS

- ▶ Check plan documents/SPDs to determine how “spouse” is defined
 - ▶ Distinguish between same-sex spouses and domestic partners/civil unions
 - ▶ Clarify that “spouse” is not restricted to opposite sex spouse (or clarify that it is, pending further changes in the law)

ACTION STEPS— HEALTH AND WELFARE PLANS

- ▶ Uniform definition of “spouse”
 - ▶ Plan document
 - ▶ Trust agreement
 - ▶ Insurance policies
 - ▶ ASO agreements
 - ▶ Beneficiary forms

ACTION STEPS – HEALTH AND WELFARE PLANS

- ▶ Stop imputing income for cafeteria plan benefits, including health coverage, provided to same-sex spouse as soon as reasonably possible following 12/16/13 (other benefits 9/16/13)
 - ▶ But check state law if in state that doesn't recognize same-sex marriages
- ▶ COBRA rights
- ▶ HIPAA special enrollment rights

ACTION STEPS – HEALTH AND WELFARE PLANS

- ▶ Cafeteria Plans
 - ▶ Add same-sex spouse to flexible spending arrangements
 - ▶ Allow mid-year change to salary reduction related to spousal coverage
 - ▶ Complete amendments by last day of plan year beginning after 12/16/13 (12/31/14 for calendar year plans)

ACTION STEPS – HEALTH AND WELFARE PLANS

- ▶ Health Savings Account/ Dependent Care Assistance Plan
 - ▶ Same-sex spouse will be considered a “spouse” for contribution limits *and* tax-free distributions
- ▶ Health Reimbursement Arrangement
 - ▶ Clarify whether a same-sex spouse will be considered a “spouse”

ACTION STEPS – FMLA

- ▶ Re-visit FMLA policy
 - ▶ FMLA rights **must** be extended to employees with same-sex spouses if employees reside in states recognizing such marriages;
 - ▶ Does employer want uniform policy?
 - ▶ Watch for changes to FMLA regulations

QUESTIONS