



IRS Post-DOMA Guidance: What Employers Should Do Now

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September 16, 2013

With the release of Revenue Ruling 2013-17 and accompanying Q&As, the Treasury and IRS have begun to answer some of the key questions facing benefit plan sponsors in the wake of the Supreme Court's decision in *U.S. v. Windsor*. Notably, the ruling makes clear that legally married same-sex couples will be treated as married for all federal tax purposes regardless of domicile or residence. This "state of celebration" approach should greatly simplify payroll and employee benefit plan administration, as employers can now provide benefits to same-sex spouses without having to consider whether they reside in a non-recognition state, or relocate over time.

The ruling also allows taxpayers - including employers - the option to file refund claims for tax overpayments made based on a same-sex couple's marital status. By opening the door to retroactive application of *Windsor*, this raises numerous questions for employee benefit plan administration - including the validity of past beneficiary designations, past benefit elections, and any other pre-*Windsor* participant elections requiring spousal consent. The ruling expressly reserves these and other benefit plan issues for future IRS guidance.

Below are answers to some of the near-term implementation questions confronting employers while we await further guidance from the IRS and other agencies.

What Benefit Plan Changes Must Be Implemented Now?

- Beginning on the September 16, 2013 effective date of the ruling, legally married same-sex spouses must be treated as spouses for all benefit plan purposes - regardless of how plan documents are worded and regardless of their place of residence.



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- See our June 21, 2013 and July 2, 2013 newsletters for details on the benefits and rights that now need to be provided to same-sex spouses.

What Immediate Payroll Tax Changes Should We Make For Same-Sex Spouse Health Plan Coverage?

- Employers that have been imputing income to employees for the value of employer-paid health plan coverage for same-sex spouses should immediately discontinue income imputation for all payroll tax withholding and reporting purposes going forward.
- In addition, employers can recoup excess FICA and income tax withholdings remitted earlier in 2013 by making the appropriate adjustments on their next quarterly Forms 941. Prospective payroll and income tax withholdings from affected employees' paychecks for the remainder of the year can also be reduced to compensate for over-withholding earlier in the year.
- Likewise, for employers that allow health plan participants to make after-tax premium contributions toward same-sex spousal coverage, the revenue ruling provides that these payroll withholdings may now be processed as pre-tax contributions made through a cafeteria plan. New cafeteria plan elections from the affected participants are not required.

How Should We Communicate with Employees About This Change?

- Employers have been taking a range of approaches in the scope and logistics of their *Windsor*-related employee communications efforts.
- Some have taken the broad-based strategy of sending a comprehensive communication to all employees - possibly in connection with a special mid-year benefits enrollment period for same-sex spouses and their dependents.
- More targeted approaches include sending special communications to employees who have enrolled in domestic partner coverage under group health and life insurance plans to inform them of the benefit rights that now apply to same-sex spouses and to solicit updated payroll status information and beneficiary designation forms.
- SPDs and open enrollment guides, which will need to be updated to reflect the new post-*Windsor* spouse definition, also present an opportunity to communicate with employees about these changes in the less immediate timeframe.

What Do Employees Need to Know?

Communications to employees should clarify the impact of spousal rights on the employee's pension and tax situation. If you are in a valid same-sex marriage recognized under state or foreign law:



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- Your spouse has a right to a survivor pension after your death. Your spouse's right may be waived only with his or her written consent.
- Retirement plan beneficiary designations - including past beneficiary designations - may be invalid without the consent of your spouse. The IRS has said this is definitively the case for designations made after September 15, 2013. It may also be true for earlier designations. If you have designated a non-spousal beneficiary - for example, your child, sibling, or parent - as the recipient of a survivor pension benefits after your death, this designation may now be void. If you want an individual other than your spouse to be the beneficiary of your pension plan benefit, you should make a new election and obtain spousal consent.
- You may be eligible for more favorable tax withholding based on your married status. You should fill out a new Form W-4
- If you are married and have been receiving taxable "domestic partner" benefits on behalf of your spouse, these benefits are now non-taxable. You should inform your employer of your married status so that taxable income is no longer reported to you for the value of these benefits.
- You may file an amended return to seek a refund of taxes paid on those benefits in open tax years.

Do Retirement Plan Election Forms Need to Be Updated Right Away?

- Probably not. Unless a retirement plan's benefit election packages and beneficiary designation forms explicitly define "spouse" in a manner inconsistent with *Windsor*, no immediate changes need to be made to these materials.

What Actions Should Employers Consider Taking Now for Retirement Plans?

- The most pressing changes that need to be implemented for these plans are operational in nature - for example, ensuring that spousal consents are obtained for non-spouse beneficiary designations (and non-QJSA benefit forms), and that benefit election packages for married participants contain information on QJSA and other spousal beneficiary distribution options.
- Consider reviewing call center scripts and procedures to ensure that plan representatives are prepared to properly counsel participants with same-sex spouses and provide them with the correct benefit forms and distribution options. It is important for call center representatives to understand that, while legally married same-sex spouses must be recognized as spouses for plan purposes, other formal relationships such as civil unions and domestic partnerships are not afforded the same recognition as marriage.



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Should State Income Tax Withholding on Same-Sex Spousal Health Plan Coverage be Handled Differently in Non-Recognition States?

- Employers that operate in states that both have an income tax and do not recognize same-sex marriage may need to await guidance from local tax authorities or possibly actions from state legislatures before they can determine whether to continue treating same-sex spousal health benefits and pre-tax cafeteria plan contributions as taxable compensation for state income tax withholding purposes. This will likely entail a state-by-state analysis for employers operating in several of these states.
- For the time being, most states that have an income tax use either federal AGI or federal taxable income as the starting point in computing state taxable income. Thus, unless future law changes require new adjustments to federal AGI or taxable income for state purposes, employers in many non-recognition states may be able to treat same-sex spousal benefits in the same manner for both state and federal payroll tax purposes.
- A possible complication arises in at least a handful of states that define taxable income by reference to the federal Internal Revenue Code in existence as of a specific date. In these states, changes in the IRC do not take effect for state income tax purposes until the legislature passes a new conforming law. It is not entirely clear whether such states would view the *Windsor* decision and Revenue Ruling 2013-17 as a retroactively effective change to the IRC for employee benefit income imputation purposes in the absence of a new conforming law.

What Is the Process for Claiming Payroll Tax Refunds for Prior Years?

- The ruling and Q&As authorize employers to claim refunds for FICA taxes paid on same-sex spousal benefits in prior open tax years by adjusted payroll tax returns on Form 941-X. Future IRS guidance will establish a special streamlined administrative procedure for these refund claims, so it makes sense to wait until the new procedure is announced before filing your Forms 941-X.
- In addition to computing the imputed income and refund amounts, employers who are preparing to make refund claims are required to make reasonable attempts to locate the employees who received the excludable benefits and give them the opportunity to participate in the claim for refund. If the employee declines to participate, a refund can only be claimed for the employer-paid portion of the FICA taxes. Employers are not permitted to claim refunds of excess income tax withholding in prior years.

What Documentation Should Employers Require to Verify Marital Status for Same-Sex Couples?



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- There is generally no reason that an employer or plan sponsor should need additional documentation - such as a marriage certificate - to verify the status of an employee's same-sex marriage where such documentation is not required for opposite-sex spouses. Some jurisdictions forbid employers from requiring documentation from same-sex couples unless the same requirement applies to all married couples.
- For payroll tax purposes, for instance, employers can continue to reasonably rely on marital status information reported by employees on Form W-4.
- Likewise, plan administrators that rely on participant-signed certifications to verify the identity of legal spouses can continue to do so with respect to same-sex spouses. It may be advisable to update the language of such certifications to ensure that participants understand the distinction between legal marriage and non-marriage relationships such as civil unions and domestic partnerships.

What Benefit Design Changes Should Employers Be Considering in Light of the Ruling?

- In the interests of promoting fairness for all employees, many employers that currently provide benefits to same-sex domestic partners are considering scaling back such benefits - at least for employees residing in states that permit same-sex marriage.
- For similar reasons, the relatively common practice of making tax gross-up payments to employees to compensate for the income imputation that was previously required for same-sex spousal benefits is being discontinued. Employers that provided these gross-ups now need to consider how to address the fairness issues raised by the fact that employees who received gross-ups in recent years are now eligible to seek refunds from the IRS for taxes they paid on the imputed income.

What Issues Are Expected To Be Addressed in Future IRS Guidance?

- In light of the revenue ruling's recognition that spousal status will be recognized retroactively for tax purposes, it remains to be seen what corrective measures qualified retirement plans will need to take with respect to benefits that have already been commenced without the requisite spousal consents.
- Guidance would also be welcome on whether cafeteria plans may treat the *Windsor* decision itself as a qualified change in status event for participants with same-sex spouses.
- The ruling indicates that any future guidance on the impact of *Windsor* on employee benefit plans will provide sufficient time for the adoption of necessary plan amendments and operational corrections.

FOR MORE INFORMATION

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