

IRS and Treasury Recognize Same-Sex Marriage for Federal Tax Purposes Using a “State of Celebration” Rule

BY GLOBAL COMPENSATION, BENEFITS, AND ERISA PRACTICE

GOVERNMENT PROVIDES NEEDED CLARITY

On August 29, 2013, the Treasury Department and the Internal Revenue Service (the “Government”) issued Revenue Ruling 2013-17, holding that as of September 16, 2013 (and for certain purposes, retroactively), same-sex couples who are married in a jurisdiction that recognizes same-sex marriages will be recognized as married couples for federal tax purposes, regardless of where they live (the “state of celebration” approach).¹ The Government also issued FAQs on August 29, 2013, providing further information.²

This guidance follows the Supreme Court’s June 26, 2013 holding in *United States v. Windsor* that Section 3 of the Defense of Marriage Act of 1996 (“DOMA”) unconstitutionally encroached on states’ rights to regulate marriage. In eliminating DOMA’s uniform definition of “spouse” and “marriage” for federal law purposes, *Windsor* introduced a number of questions for employers, such as how to address benefits for same-sex couples who lawfully marry in a jurisdiction that recognizes such marriages, but live or work in a jurisdiction that does not. The Revenue Ruling provides much needed clarity by holding that legal same-sex marriages will be recognized for all purposes under federal tax law where marriage is a factor – including employee benefits.

The Revenue Ruling significantly streamlines benefit plan administration. By permitting plans to treat all legally married couples the same, regardless of their current state of residence or work, the Revenue Ruling eliminates the need for multiple benefit administration schemes at the federal level.³ According to the Revenue Ruling and FAQs, the Government will issue further guidance regarding employee benefits. The further guidance will address the retroactive application of *Windsor* and how qualified retirement plans and other tax-favored arrangements must comply with *Windsor* (e.g., plan amendment requirements and corrections for plan operation).

The Revenue Ruling confirms that the IRS will allow taxpayers to apply the Revenue Ruling retroactively for open tax years for employee benefit plans and arrangements for the purposes of filing refund claims and certain other purposes with respect to employer-provided health or fringe benefits excludible under Internal Revenue Code Sections 106 (health benefits), 117(d) (tuition reduction), 119 (meals and lodging), 129 (dependent care assistance) or 132 (other fringe benefits, including

employee discounts and moving expenses) based on marital status.⁴ Taxpayers also may treat after-tax, same-sex health care coverage payments as having been made on a pre-tax basis.

The FAQs confirm that same-sex couples can pursue refund claims for the previous three tax years. Employers who have not already done so will want to consider whether to file a refund claim for payroll taxes paid on account of previously imputed income (depending on the level of employer subsidy and the number of same-sex spouse participants, this could be a significant refund claim). An IRS press release dated August 29, 2013 indicates that the Government will enact streamlined procedures for employers filing these claims.⁵

DIFFERENT STANDARD THAN THE FMLA

Notably, the Revenue Ruling and FAQs provide a different marriage recognition standard than the Department of Labor (“DOL’s”) guidance regarding the Family and Medical Leave Act (“FMLA”), leading to some continuing inconsistency with respect to treatment of same-sex couples. In a revised fact sheet issued earlier this month, the DOL defined “spouse” as “a husband or wife as defined or recognized under state law for purposes of marriage in the state where the employee resides, including ‘common law’ marriage and same-sex marriage.”⁶ This guidance is in accord with existing FMLA regulations, which define spouse as “a husband or wife as defined or recognized under State law for purposes of marriage in the State where the employee resides, including common law marriage in States where it is recognized.”⁷ This FMLA standard, which bases coverage of same-sex couples on state of residence rather than the state of celebration, produces inconsistent treatment and burdens employers with tracking such treatment. For example, imagine that a company employs two individuals, each of whom is in a same-sex marriage. If one couple resides in New York (which recognizes same-sex marriage) and the other couple resides in Pennsylvania (which does not), the employer must provide FMLA spousal coverage for the New York couple, but not for the Pennsylvania couple. The company also must continually reassess such coverage as employees in same-sex marriages move from state to state and as same-sex marriage legislation in the states continues to evolve.

In turn, FMLA coverage can impact benefit continuation rights; for example, from a technical standpoint, if an individual takes an FMLA-qualifying leave to care for a same-sex spouse (e.g., a New York employee who lives in a state that recognizes same-sex marriage), he or she can choose whether to continue employer-sponsored group health coverage at subsidized rates (subject to potential recapture) during the protected leave. An employee who does not return to work at the end of the leave will then have a COBRA-qualifying event (for a normal period of roughly up to 22 months of coverage). On the other hand, if the individual takes a non-FMLA leave to care for a same-sex spouse (e.g., a New York employee who does not live in a state that recognizes same-sex marriages), he or she normally would experience a COBRA-qualifying event at the commencement of the leave (for a normal period of roughly up to 18 months of coverage).

Employers who want to have the most uniform plan administration possible will extend the FMLA benefit continuation rights to all employees who take a leave to care for a same-sex employee, regardless of where they live. Those that do so should work with their primary insurers, third party administrators, and stop loss carriers to ensure that there are no gaps in coverage or administration and should make appropriate modifications to their plans, SPDs, SMMs, and leave policies.

RECOMMENDATIONS

Following the *Windsor* decision, we recommended a number of actions for employers.⁸ Now that the Government has provided some clarity regarding the treatment of same-sex marriages, employers should move ahead in implementing these steps, to the extent they have not done so already.

All Plans

- Take an inventory of all plans affected by the *Windsor* ruling and review existing plan terms to determine impacted areas and available alternatives.
- Allay employee concerns by promptly distributing a participant communication outlining the employer's same-sex marriage game plan for employee benefits. This communication should clearly spell out what changes the employer has or will make and the effective date of such changes. To address issues that require more analysis or guidance, the communication could indicate that other important legal matters are unclear, but that the employer is monitoring developments closely and will communicate future decisions to affected employees.
- Review plan documents to determine whether an amendment is required to offer same-sex spousal coverage when desired or required. For example, if a spouse is defined as a participant's lawfully married spouse, then no amendment is necessary, but it might be useful from an employee relations standpoint to clarify that lawfully married status will be determined based on the state of celebration. On the other hand, if the plan defines a spouse as an opposite-sex spouse, then an amendment is needed to offer same-sex spouse coverage.
- Decide whether to amend each plan individually, or whether an omnibus amendment is appropriate to address particular matters until future guidance fully clarifies all of *Windsor's* impacts.
- Amend summary plan descriptions and issue summaries of material modifications as required.
- Decide whether changes should be prospective or retroactive. The Revenue Ruling is prospective, but indicates that guidance regarding retroactive application of *Windsor* is forthcoming. In the meantime, employers considering retroactivity will need to carefully consider the administrative and financial consequences of their decision.

Welfare Plans

- If you have not offered special mid-2013 same-sex spouse enrollment rights, consider offering such enrollment, waiting until upcoming open enrollment periods, or waiting for further government guidance.
- Stop imputing income for federal purposes on employer-paid benefits provided to legally married same-sex spouses if you do not do so for opposite sex spousal benefits and determine the appropriate tax treatment for state-law purposes.
- Decide whether domestic partner and civil union coverage remains appropriate or if it needs refinement. If such coverage is no longer appropriate, consider whether to phase out such coverage over a period of time or to terminate after a set date.

- Stop providing unnecessary tax gross-ups for health coverage provided to same-sex spouses (consider how to handle past gross-ups and imputed pay for 2013, and prior years), and consider whether the company will continue its current gross-up policy for health coverage provided to domestic partners and partners in a civil union.
- Decide whether to file a refund claim for payroll taxes paid on account of previously imputed income.
- Decide whether to extend special FMLA coverage rights to employees with same-sex spouses if the employee lives in a state that does not recognize same-sex spouses.

Qualified Plans

- If not already completed, make necessary changes in light of *Windsor* and promptly communicate them to participants. See note 8.

CONCLUSION

The Government finally has provided some post-*Windsor* certainty for employers and employees alike, by ruling that legally married same-sex spouses will be recognized as married for federal tax purposes – and related employee benefits provisions – wherever they live or work. This is a positive outcome for employers because it streamlines benefit plan administration. We encourage employers to use this clarified guidance to move forward on needed benefit plan changes.

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If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

Los Angeles

Stephen H. Harris
1.213.683.6217
stephenharris@paulhastings.com

Ethan Lipsig
1.213.683.6304
ethanlipsig@paulhastings.com

Melinda A. Gordon
1.213.683.6173
melindagordon@paulhastings.com

M'Alyssa Mecenas
1.213.683.6130
malysamecenas@paulhastings.com

Washington, D.C.

Eric R. Keller
1.202.551.1770
erickeller@paulhastings.com

J. Mark Poerio
1.202.551.1780
markpoerio@paulhastings.com

Damian Myers
1.202.551.1863
damianmyers@paulhastings.com

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- ¹ The Revenue Ruling provides that taxpayers may rely on the Revenue Ruling in advance of its effective date for, among other things, income tax filing and refund claims (if the applicable statute of limitations has not expired).
 - ² Available at <http://www.irs.gov/uac/Answers-to-Frequently-Asked-Questions-for-Same-Sex-Couples>.
 - ³ Of course, at least initially, employers will have to grapple with state tax treatment for those employees with same-sex spouses who work in a state that does not treat same-sex marriage the same as opposite sex marriage for state tax purposes.
 - ⁴ The Code sections identified here are specifically cited in the Revenue Ruling. Whether taxpayers can apply the Revenue Ruling retroactively to other Code sections pertaining to spousal welfare and fringe benefits appears to be an open question.
 - ⁵ Available at <http://www.treasury.gov/press-center/press-releases/Pages/j12153.aspx>.
 - ⁶ U.S. Department of Labor, Wage and Hour Division, Fact Sheet #28F: Qualifying Reasons for Leave under the Family and Medical Leave Act, dated August 2013.
 - ⁷ 29 C.F.R. § 825.122(b).
 - ⁸ See Paul Hastings, *Stay Current*, "DOMA's Demise Requires Immediate Benefit Plan Action," July 2013.