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Client Alert:
Employee Benefits

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August 30, 2013

# *IRS Issues Guidance Regarding Same-Sex Marriage*

## Background

In our June 26, 2013, Client Alert, we informed you that the United States Supreme Court ruled that Section 3 of the Defense of Marriage Act ("DOMA") is unconstitutional.

Section 3 of DOMA had defined "marriage" for purposes of all federal laws as a legal union between one man and one woman as husband and wife, and it defined "spouse" as a person of the opposite sex who is a husband or wife. By ruling Section 3 of DOMA as unconstitutional, the definitions of "spouse" and "marriage" under state law became applicable. In essence, the court decision meant that federal benefits and protections provided to opposite-sex spouses apply to same-sex spouses *if* same sex marriage is recognized under applicable state law. If applicable state law defines spouse as including a member of the same sex, then provisions in employee benefit plans pertaining to a spouse includes an employee's same-sex spouse.

One major question following the U.S. Supreme Court's decision became *which* state's law applies in defining "spouse": the law of the state where the couple resides - or the law of the state where the couple married?

## Recent IRS Guidance

On August 29, 2013, the Internal Revenue Service ("IRS") issued guidance indicating that for federal tax purposes the IRS will recognize a marriage of same-sex individuals validly entered into in a state[1] whose laws authorize the marriage of two individuals of the same sex – even if the state in which they are domiciled does not recognize the validity of same-sex marriages. The IRS specifically noted that this rule applies for purposes of employee benefit plans employers offer to employees.

So, for example, a same-sex couple who resides in Michigan (which does not recognize the validity of same-sex marriage) who marry in New York (which does recognize the validity of same-sex marriage) is considered married (and husband and wife) for federal tax purposes.

However, the IRS stated that individuals (either of the same sex or opposite sex) who have entered into a registered domestic partnership, civil union, or other similar formal relationship recognized under state law that is not denominated as marriage under the laws of that state are not considered married and are not considered spouses (and are not considered husband and wife) for federal tax purposes.

## Implications for Tax-Qualified Retirement Plans

Beginning September 16, 2013 (the effective date of the IRS guidance) employers should ensure that in operation their tax-qualified retirement plans treat same-sex spouses in the same manner as opposite-sex spouses, if the same sex couple was married in a jurisdiction which authorizes same sex marriage.

A tax-qualified retirement plan maintained by an employer which operates only in a state that does not recognize same-sex marriages (such as Michigan) must treat a participant who legally married a spouse of the same sex in a different jurisdiction (such as New York) as married for purposes of applying the qualification requirements that relate to spouses.

For example, under a tax-qualified defined benefit pension plan or money purchase pension plan, a spouse is entitled to receive a qualified joint and survivor annuity if the participant dies after retirement. The participant may not elect any other benefit form at retirement, and may not designate any other beneficiary, unless the spouse consents to the election. Likewise, a spouse is entitled to receive a qualified pre-retirement survivor annuity if the participant dies before retirement. For purposes of these rules, a spouse now includes a same-sex spouse if the couple was married in a jurisdiction which authorizes same-sex marriage.

By means of further example, tax-qualified defined contribution plans provide that the participant's account must be paid to the participant's spouse upon the participant's death unless the spouse consents to a different beneficiary. The plan must now pay this death benefit to the same-sex surviving spouse of any deceased participant (if the couple was married in a jurisdiction which authorizes same-sex marriage). The plan is not required to provide this death benefit to a surviving registered domestic partner of a deceased participant. However, the plan is allowed to make a participant's registered domestic partner the default beneficiary who will receive the death benefit unless the participant chooses a different beneficiary.

Further, employers must now review their plan documents to determine if "spouse" is defined in a manner inconsistent with IRS guidance. The IRS indicates it will issue future guidance addressing plan amendment requirements for tax-qualified retirement plans.

**Implications for Welfare Plans**

If welfare plans make benefits available to same-sex spouses, for federal tax purposes, same-sex spouses are to be treated in the same manner as opposite-sex spouses effective September 16, 2013. For example, if a group health plan makes benefits available to an employee's same-sex spouse (if the couple was married in a jurisdiction authorizing the marriage) then the employer contribution to coverage for the same-sex spouse is tax-free and the employee contribution for the same-sex spouse can be paid with pre-tax dollars.

Unfortunately, the IRS guidance does not expressly address whether welfare plans which make benefits available to an employee's opposite-sex spouse, *must* also make the benefit available to an employee's same-sex spouse (if the same-sex couple married in a jurisdiction which authorizes same-sex marriage). Arguably, this remains an open question. Future guidance from other agencies – such as the U.S. Department of Labor – may provide insight. Any local or state laws (or employer policies) prohibiting discrimination based on sexual orientation may also play a role in determining whether an employer can provide welfare plan coverage to only opposite-sex spouses.

The IRS guidance does address a same-sex spouse in the welfare plan context with regard to certain tax refund claims for periods prior to September 16, 2013. More specifically, it notes that taxpayers may rely on the guidance retroactively (i.e. for periods prior to September 16, 2013) for purposes of filing original returns, amended returns, adjusted returns, or claims for credit or refund of an overpayment of tax concerning employment tax and income tax with respect to previously provided employer-provided health insurance, dependent care assistance program, certain fringe benefits, qualified tuition reduction, and meals and lodging for the same-sex spouse.

For example, if an employer sponsored a cafeteria plan under which an employee elected to pay for health coverage for the employee on a pre-tax basis, and if the employee purchased coverage on an after-tax basis for the employee's same-

sex spouse as allowed under the employer's health plan, the employee may now claim a refund of income taxes paid on the premiums for the coverage of the employee's spouse. This claim for a refund generally would be made through the filing of an amended IRS Form 1040. However, the employee can only seek a refund for the years for which the period of limitations for filing a claim for refund is open. Generally, a taxpayer may file a claim for refund for three years from the date the return was filed or two years from the date the tax was paid, whichever is later.

By means of further example, if an employer provided health coverage for an employee's same-sex spouse, the employee may claim a refund of income taxes paid on the value of coverage that would have been excluded from income had the employee's spouse been recognized as the employee's legal spouse for tax purposes. This claim for a refund generally would be made through the filing of an amended IRS Form 1040. However, the employee can only do so for the years for which the period of limitations for filing a claim for refund is open.

In these two situations, if the period of limitations for filing a claim for refund is open, the employer may claim a refund of, or make an adjustment for, any excess social security taxes and Medicare taxes paid on same-sex spouse benefits. (Future guidance will be forthcoming from the IRS regarding the administrative procedure to make this claim.)

The IRS states it will issue additional guidance in the future on the retroactive federal tax application of same-sex marriage on other employee benefits and employee benefit plans and arrangements. It says it may issue additional guidance in general on the topic of same-sex marriage and notes that other federal government agencies may provide guidance on programs they administer which are affected by the Internal Revenue Code.

If you have any questions regarding the IRS guidance, please contact the author of this Client Alert or a member of the Butzel Long Employee Benefits Group.

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[1] "State" means any U.S. state, the District of Columbia, a U.S. territory, or a foreign country having the legal authority to sanction marriages.

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