MINTZ

Treasury Department/IRS Clarify Federal Tax Treatment of Same-Sex Marriages: Assessing the Impact on Employee Benefit Plans

September 09, 2013 | Advisory | By **Ann M. Fievet**

VIEWPOINT TOPICS

- Employment

RELATED PRACTICES

RELATED INDUSTRIES

In recently issued Revenue Ruling 2013-17, the Treasury Department and the Internal Revenue Service (IRS) ruled that all legal same-sex marriages will be recognized for federal tax purposes. The revenue ruling was accompanied by two sets of Frequently Asked Questions, which together with the revenue ruling establish a "state of celebration" rule as opposed to a "state of residence" rule. Thus, a same-sex marriage legally entered into in any state or jurisdiction will be recognized for all federal income, gift and estate tax purposes, even if the couple later moves to a state that does not recognize same-sex marriages. According to a concurrently issued IRS press release, the rule applies broadly —

> **to all federal tax provisions where marriage is a factor, including filing status, claiming personal and dependency exemptions, taking the standard deduction, employee benefits, contributing to an IRA, and claiming the earned income tax credit or child tax credit.**

Background

Before Congress enacted the Defense of Marriage Act (DOMA), marital status for federal income tax purposes was based on state law.[1] Section 3 of DOMA barred same-sex married couples from being recognized as "spouses" for all purposes of federal law. Thus, since 1996, legally married same-sex couples have not been recognized as married for purposes of federal law, including the Internal Revenue Code. In June of this year the Supreme Court, in *United States v. Windsor*, ruled that Section 3 of DOMA is unconstitutional.

Windsor raised a host of important questions for employers in the administration of their employee benefit plans, programs, and arrangements, many (but not all) of which Revenue Ruling 2013-17 answers. (For a sampling of these questions, **please see our client advisory of July 3, 2013**.)

Revenue Ruling 2013-17

Revenue Ruling 2013-17 establishes that, as of September 16, 2013, for federal tax purposes:

- "Marriage" includes a marriage between individuals of the same sex;
- The IRS will recognize a marriage of same-sex individuals validly entered into in a state whose laws authorize the marriage of two individuals of the same sex even if they move to a state that does not recognize the validity of same-sex marriages; and
- "Marriage" does not include a registered domestic partnership, civil union, or other similar arrangement not denominated as "marriage," whether between individuals of the same or opposite sex.

The revenue ruling also clarifies that these rules apply retroactively for certain tax purposes, including tax treatment impacting employee benefit plans. Validly married, same-sex spouses are generally permitted to amend their filing status and receive a refund of the difference in taxes owed as a result of the filing change for all open tax years — generally three years from the date the return was filed or two years from the date the tax was paid, whichever is later.

A set of **Frequently Asked Questions (the "FAQs")** relating to treatment of same-sex couples married under state law (as opposed to domestic partners and individuals in civil unions), issued concurrently with Revenue Ruling 2013-17, provides the following rules that apply to tax returns filed (and to be filed) by same-sex spouses:

Tax Year	Filing Status/Options
2013 and later years	Same-sex spouses generally must file using a "married filing separately" or "married filing jointly" filing status.
2012	Same-sex spouses who file an original tax return on or after September 16, 2013 must file using a "married filing separately" or "married filing jointly" filing status. Same-sex spouses who filed their 2012 tax return before September 16, 2013, may choose (but are not required) to amend their federal tax return to file using "married filing separately" or "married filing jointly" filing status.
2011 and earlier years	Same-sex spouses who timely filed their tax returns may choose (but are not required) to amend their federal tax returns to file using "married filing separately" or "married filing jointly" filing status *provided* the period of limitations for amending the return has not expired.

Group Health Plans and Other Fringe Benefit Programs

The FAQs clarify the rights of a taxpayer who has previously included the value of group health plan coverage provided to his or her same-sex spouse in gross income. The taxpayer in this instance is permitted to file an amended Form 1040 (i.e., Form 1040-X) reflecting the taxpayer's status as a married individual and may recover federal income tax paid on the value of such coverage for all years for which the period of limitations for filing a claim for refund is open. The FAQs further clarify that the same rule applies when the coverage was provided through an employer-sponsored cafeteria plan that allowed employees to pay premiums for health coverage on a pre-tax basis — i.e., the employee may file an amended return (during the window available for filing a claim for a tax refund) to recover income taxes paid on premiums that the employee paid on an after-tax basis for the health coverage of the employee's same-sex spouse.

NOTE: According to long-standing Treasury regulations,[2] an employee must generally include in income the fair market value of group health plan coverage provided to his or her same-sex spouse. According to another equally long-standing Treasury regulation,[3] "fair market value" means the amount that an individual would have to pay for the particular fringe benefit in an arm's-length transaction. While many plan sponsors have read this to mean the difference between the single and family premium cost, the better view is that the proper measure is the cost of individual coverage (i.e., the COBRA cost less 2%). Nothing in the Q&As contradicts these principles, but neither are they acknowledged. In keeping with an approach later sanctioned in a 2007 proposed regulation,[4] most employers allow pre-tax treatment of the employee's contributions but impute as income the value of the coverage provided to the same-sex spouse on a quarterly or more frequent basis. This approach is no longer necessary in the case of same-sex spouses, but it is still viable for domestic partners.

The FAQs separately prescribe the following rules under which employers and employees may claim refunds of Social Security and Medicare taxes paid, and income taxes withheld, on benefits treated as taxable in prior, open tax years.

	Social Security & Medicare Taxes	Income Taxes
Employer	The employer may claim a refund of any excess Social Security taxes and Medicare taxes—employer and employee portion—paid by filing Form 941-X.[5] **NOTE:** The IRS will issue a special administrative procedure for employers to file claims for refunds or make adjustments for excess Social Security taxes and Medicare taxes paid on same-sex spouse benefits.	Claims for refunds of over-withheld income tax for prior years cannot be made by employers.
Employee	According to the Instructions for Form 941-X, refunds of, or adjustments to, any excess Social Security taxes and Medicare taxes are paid over to the employer, which has the obligation to repay or reimburse the employee for the employee portion or obtain the consent of an employee to file a claim on his or her behalf.	The employee may file for any refund of income tax due for prior open tax years on Form 1040X.

Many employers have been imputing income during 2013; some stopped doing so on or shortly after the Supreme Court handed down its decision in *Windsor* on June 26; and still others waited for official guidance. Regardless of an employer's decision regarding treatment of imputed income in the past, the FAQs permit but do not require employers to make adjustments for income tax withholding that was over-withheld from an employee in the current year provided the employer has repaid or reimbursed the employee for the over-withheld income tax before the end of the calendar year. Both the revenue procedure and the FAQs make clear that employers must continue to impute income for the fair market value of coverage provided to registered domestic partners, partners in a civil union, and individuals in other non-marital relationships, whether same-sex or opposite sex.

The changes wrought by Revenue Ruling 2013-17 will ripple through cafeteria plans, Health Reimbursement Arrangements (HRAs) and many fringe benefit plans and programs, including qualified tuition reduction programs, arrangements providing or reimbursing meals and lodging for the convenience of the employer, and dependent care assistance programs (relating to the care of a disabled spouse). Thus, for example, pre-tax premium contributions will be permitted for spousal coverage under an employer's cafeteria plan, and HRAs will be permitted to reimburse qualifying medical expenses of an employee's same-sex spouse.

Qualified Retirement Plans

Under Revenue Ruling 2013-17 and the FAQs, tax-qualified retirement plans must treat a same-sex spouse as a spouse for all purposes of applicable federal tax laws governing such plans. This is true for any same-sex marriage that was validly entered into in a jurisdiction whose laws authorized the marriage, even if the couple lives in a domestic or foreign jurisdiction that does not recognize the validity of same-sex marriages. A person who is in a registered domestic partnership or civil union is not, however, considered to be a spouse for purposes of this rule.

Tax-qualified retirement plans must be amended to extend spousal protections and benefits to same-sex spouses. For plans that are subject to the rules governing Qualified Joint and Survivor Annuities (QJSAs) and qualified preretirement survivor annuities (QPSAs), plans must provide QJSAs, qualified optional survivor annuities and QPSAs to all same-sex spouses. Also, the consent of a participant's same-sex spouse will be needed for the participant to elect an optional form of benefit, to designate a non-spouse beneficiary, or to take a loan from the plan. In addition, minimum required distributions will be determined under the rules that apply to married individuals, and same-sex spouses will be entitled to benefits under a qualified domestic relations order in the event of a divorce.

Qualified retirement plans must comply with these rules as of September 16, 2013. The rules permitting taxpayers to file amended returns that relate to prior periods under the revenue ruling do not extend to qualified retirement plans. Rather, application of the Supreme Court's *Windsor* decision as it applies to qualified retirement plans with respect to periods before September 16, 2013 will be the subject of future guidance that will address plan amendment requirements and any necessary corrections relating to plan operations.

Retroactive Application of *Windsor*

Other than to permit the filing of amended returns for income previously imputed in connection with group health plan coverage and refunds of Social Security and Medicare taxes, Revenue Procedure 2013-17 did not address the extent to which *Windsor* might apply retroactively to other employee benefits and employee benefit plans and arrangements. These and other items will be the subject of future guidance. Revenue Ruling 2013-17 assures us that this guidance "will take into account the potential consequences of retroactive application to all taxpayers involved, including the plan sponsor, the plan or arrangement, employers, affected employees and beneficiaries." Moreover, the regulators anticipate that the future guidance "will provide sufficient time for plan amendments and any necessary corrections so that the plan and benefits will retain favorable tax treatment for which they otherwise qualify."

Endnotes

1 Revenue Ruling 2013-17 cites as an example of prior law a 1958 ruling, which held that a couple would be treated as married for purposes of federal income tax filing status if the couple entered into a common-law marriage in a state that recognized that relationship as a valid marriage, even if the couple later moved to a state in which a ceremony was required to establish the marital relationship.

2 Treas. Reg.§§ 1.61-21(a)(4)(i) and 1.61-21(b)(1).

3 Treas. Reg. § 1.61-21(b)(2).

4 Prop. Treas. Reg. § 1.125-1(n) (Aug. 6, 2007).

5 Only the employer portion of Social Security and Medicare taxes may be claimed in cases where the employee is no longer employed and cannot be located or where a current employee declines in writing to participate in the claim for refund of Social Security and Medicare taxes. In order to claim the employer portion of Social Security and Medicare taxes for an employee who cannot be located, reasonable attempts at locating the employee have to be made.

Authors

Ann Fievet

More Viewpoints

The Impact of the Supreme Court's DOMA Decision on Employee Benefit Plans — Some Certainty, Many Unanswered Questions

July 3, 2013 | Advisory

Read more