Expert Q&A on Employee Benefits After the Supreme Court's Ruling that DOMA is Unconstitutional

Practical Law Employee Benefits & Executive Compensation

An Expert Q&A with Howard Bye-Torre of Stoel Rives LLP on the recent US Supreme Court ruling in United States v. Windsor that Section 3 of the Defense of Marriage Act (DOMA), which defined marriage for federal law purposes to mean opposite-sex marriage, is unconstitutional. The Q&A addresses the decision's impact for employers that sponsor health and retirement plans.

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The US Supreme Court has ruled that Section 3 of the Defense of Marriage Act (DOMA), which defined marriage for federal law purposes to mean opposite-sex marriage, is unconstitutional (*United States v. Windsor, 2013 WL 3196928 (2013)*). Practical Law asked Howard Bye-Torre of Stoel Rives LLP to discuss some of the implications of the *Windsor* decision for employers who sponsor retirement and health plans for their employees and family members.

THE WINDSOR DECISION

Ms. Windsor sued when she was forced to pay more than $360,000 in federal estate taxes after her wife's death, which she would not have had to pay if she had been married to a man. The US Supreme Court held that the federal government's failure to recognize her marriage, which was recognized by New York law, was a violation of her constitutional rights to liberty and equal protection, and the federal government must look at state law, not Section 3 of DOMA, to determine if she was married.

The Court noted in its decision that there are more than 1,000 federal laws that give rights and obligations to spouses and married couples, including federal laws relating to employee benefits. Now, marriages recognized under controlling state law will be recognized by federal law and spouses in those marriages will have the same rights and obligations under these myriad federal laws as spouses in opposite-sex marriages.

Importantly, the *Windsor* Court did not rule that there is a constitutional right for same-sex couples to marry anywhere in the United States. Therefore, states that do not allow same-sex couples to marry:

- Are not required to do so by the decision.
- Currently need not recognize the marriages of same-sex couples married in one of the 14 American jurisdictions allowing same-sex marriages. (The issue of the constitutionality of Section 2 of DOMA, which allows states the right to refuse to recognize same-sex marriages from other states, was not before the Supreme Court in *Windsor*.)

However, it seems likely that these and other LGBT rights issues will be brought before courts based on the *Windsor* decision in the years to come.

WHAT STATES ALLOW SAME-SEX COUPLES TO BE MARRIED?

Currently, New York, California, Delaware, Iowa, Maryland, Minnesota, Washington, Massachusetts, Maine, Vermont, Rhode Island, Connecticut, New Hampshire and the District of Columbia allow same-sex couples to be married ("Same-sex Marriage States"). In general, Same-sex Marriage States recognize same-sex marriages from other states and foreign countries, such as Canada.

WILL THE FEDERAL GOVERNMENT RECOGNIZE ALL SAME-SEX MARRIAGES IN ALL SITUATIONS?

Under *Windsor*, the federal government must look to state law to determine whether a same-sex couple is married. However, *Windsor* did not rule on which state law must be followed. The determination of which state law will control for federal purposes is an important issue for employees in same-sex marriages and their employers, since the majority of states do not recognize the marriages of same-sex couples. It seems clear under *Windsor* that the federal government will recognize the same-sex marriages of couples residing in Same-sex Marriage States. For same-sex married couples residing in other states, it is not so clear. In the past, sometimes the federal government has looked to the law of the state in which the marriage occurred (state of celebration) to determine if the couple is married. In other instances, the federal agencies have looked to the law of the state in which the couple currently resides (state of residence) to determine if the couple is married.

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For example, assume a same-sex couple was married in New York (where same-sex marriage is recognized) and now lives in Texas (where it is not). If the federal agency looks to:

- The state of residence (Texas) to determine whether the couple is married under federal law, the federal agency would not consider the couple to be married.
- The marriage law of the state in which the couple was married (New York), this same couple would be recognized as married under federal law.

The federal government will likely issue guidance on this choice of law issue for employee benefit and other purposes. It is possible that the federal government will choose the state of celebration for some purposes and the state of residence (or perhaps the state in which the employee works) for other purposes. In other words, for same-sex married couples living in states that do not recognize their marriages, the couples may be considered married for some federal laws and not married for other federal laws. In the remainder of the article, the term "Federally Recognized Spouses" refers to spouses in same-sex marriages that are recognized by the federal government for employee benefit purposes.

IS THERE ANY FEDERAL OR STATE LAW THAT REQUIRES AN EMPLOYER TO PROVIDE HEALTH PLAN COVERAGE TO SPOUSES, WHETHER OR NOT THE MARRIED COUPLE IS OPPOSITE-SEX OR SAME-SEX? WILL EMPLOYERS BE SUBJECT TO "PAY-OR-PLAY" PENALTIES UNDER HEALTH CARE REFORM IF THEY DO NOT PROVIDE COVERAGE TO SPOUSES?

There is no federal law that requires employers to provide health coverage to the spouses (opposite-sex or same-sex) of employees, and it is legal under federal law to have a health plan that provides coverage only to employees or only to employees and their children. No pay-or-play penalties will be imposed on employers if they do not offer or provide coverage to spouses. However, if the spouse does not have health coverage from some source, the employee's spouse could be subject to a federal tax penalty under health care reform's "individual mandate," which requires most Americans to have health coverage beginning in 2014.

If a private employer has an insured group health plan subject to ERISA:

- The health insurance policy is subject to state insurance law.
- State insurance law may address the issue of coverage for spouses.

If an employer is not subject to ERISA (for example, a governmental entity), there may be state laws that address the issue of health coverage for spouses.

I AM AN EMPLOYER IN A SAME-SEX MARRIAGE STATE, AND OUR HEALTH PLAN PROVIDES BENEFITS TO SAME-SEX SPOUSES OF EMPLOYEES RESIDING IN MY STATE. HOW DOES WINDSOR AFFECT OUR HEALTH PLANS?

Before the *Windsor* decision, the value of employer-provided health coverage to an employee's same-sex spouse in most instances was treated as wages or imputed income to the employee, and as such was subject to federal income and employment taxes. Health coverage for same-sex spouses could be provided to the employee on a tax-free basis only if the same-sex spouse qualified as a tax dependent of the employee for health plan purposes, and few same-sex spouses qualified as tax dependents under these rules. After *Windsor*, health coverage that you provide to Federally Recognized Spouses is tax-free to your employees, without any showing of tax dependency.

Certain other federal rights given to spouses in health plans, such as independent rights to COBRA continuation coverage and certain HIPAA special enrollment rights, will now also be available to Federally Recognized Spouses. Of course, many employers offering health plan coverage to same-sex spouses have already voluntarily extended these rights to same-sex spouses even though not required by pre-*Windsor* law to do so.

If you have employees who do not reside in a Same-sex Marriage State, it is possible that the employee's spouse will not be a Federally Recognized Spouse (see *Will the federal government recognize all same-sex marriages in all situations?*).

I AM AN EMPLOYER IN A STATE THAT DOES NOT RECOGNIZE SAME-SEX MARRIAGE. HOW DOES WINDSOR AFFECT OUR HEALTH PLANS?

It is unclear what effect, if any, *Windsor* will have on your health plans. The ruling in *Windsor* only requires that the federal government recognize same-sex marriages, not that your state government recognize them.

Therefore, if you do not provide health coverage to same-sex spouses and you sponsor an insured health plan, it is likely that *Windsor* will not have any effect on your health plan. This is because *Windsor* does not require your state's insurance commission to mandate coverage of same-sex spouses in health insurance policies. If your health plan is self-insured, it is likely, unless guidance from the federal government or future court cases provide to the contrary, that employers in states that do not recognize same-sex marriages will be allowed to continue to provide benefits for only opposite-sex spouses.

If you are an employer that provides coverage to same-sex spouses (even though your state does not recognize these marriages), we expect that the IRS will issue guidance on whether the rules and rights for Federally Recognized Spouses, such as tax-free coverage and COBRA continuation coverage, will apply to your employees and their same-sex spouses.

WHAT ARE SOME OF THE EFFECTS THAT WINDSOR MAY HAVE ON OUR PENSION PLANS AND RETIREMENT BENEFITS?

Spouses have various retirement plan rights under federal law, and pension plans must now grant an employee's Federally Recognized Spouse the rights of a "spouse" for all plan purposes.

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For example, it appears that a pension plan must honor the qualified domestic relations order (QDRO) of a Federally Recognized Spouse. In addition, a participant's Federally Recognized Spouse now has the right to receive survivor benefits or must consent to a waiver of these benefits.

HOW DOES THE RULING AFFECT HEALTH SPENDING ACCOUNTS AND OTHER CAFETERIA PLAN BENEFITS?

Before *Windsor*, employees could not use funds available through health flexible spending accounts or health reimbursement arrangements (HRAs) for medical expenses incurred by a same-sex spouse, unless the spouse was a tax dependent of the employee. Now, employees with Federally Recognized Spouses can use these funds for the medical expenses of their same-sex spouses. Similarly, employees with health savings accounts (HSAs) can use HSA funds to pay for the medical expenses of their Federally Recognized Spouses on a tax-free basis, regardless of the spouse's tax dependency, and will be subject to the HSA contribution limits applicable to married couples, rather than individuals.

There are also special rules that apply to married couples and spouses under the federal law governing cafeteria plans, dependent care assistance plans and adoption assistance benefits that will become applicable to employees and their Federally Recognized Spouses.

DOES THE RULING HAVE ANY EFFECT ON EMPLOYEES AND THEIR SAME-SEX PARTNERS WHO ARE NOT MARRIED, SUCH AS PARTNERS IN A DOMESTIC PARTNER RELATIONSHIP?

We are waiting for guidance from the federal government on this issue. On one hand, the *Windsor* Court explicitly stated that its "opinion and holding are confined to those lawful marriages." On the other hand, the IRS has previously ruled that an opposite-sex couple in a civil union in Illinois could file a joint income tax return as a married couple, even though they were not married under state law. The IRS's ruling was based on the fact that under Illinois law, persons entering into civil unions were granted the same rights and responsibilities as married couples, even though the couple was not "married." Several states have domestic partnership or civil union laws similar to the Illinois civil union law, granting registered domestic partners all of the rights and privileges of married couples, but withholding the right to be called "married." In addition to Illinois, Colorado, New Jersey, Oregon, Hawaii and Nevada have these types of "everything but married" laws.

IS THE RULING EFFECTIVE FOR BENEFIT ISSUES IN 2013? DOES THE RULING HAVE ANY RETROACTIVE EFFECT?

The ruling becomes effective in late July and thus will have an immediate impact on benefits. We are awaiting guidance on the issue of whether and exactly when the federal government will apply the ruling retroactively. However, it seems likely that the ruling will be applied retroactively, at least in some instances. For example, we expect guidance from the IRS regarding the ability of employees with Federally Recognized Spouses (and their employers) to amend prior-year tax returns to seek refunds of taxes paid on imputed income resulting from health plan coverage for Federally Recognized Spouses.

ARE WE EXPECTING ANY GUIDANCE ON WINDSOR FROM THE FEDERAL AGENCIES THAT REGULATE EMPLOYEE BENEFITS?

Yes. The President has directed the federal agencies to issue regulations and other guidance relating to the decision, and the IRS has already announced its plans to do so. Among the guidance that is expected are:

- Choice of law rules.
- Guidance on the retroactive application of the decision.
- Rules on how *Windsor* affects cafeteria plans, including whether employees will be able to immediately add their Federally Recognized Spouses to group health plans due to the change in the federal taxation of this benefit.

WHILE WAITING FOR THE FEDERAL AGENCIES TO GIVE GUIDANCE ON WINDSOR, ARE THERE ANY STEPS EMPLOYERS SHOULD IMMEDIATELY TAKE REGARDING THEIR BENEFITS AND BENEFIT PLANS?

In most instances, it is probably wise to wait until guidance is available from the federal government or regulatory agencies. However, employers should consider taking the following steps now:

- A thorough review of their benefits to determine which are provided to spouses, including consideration of the exact language used in benefit plans, summary plan descriptions, employee handbooks and other employee communications to describe these benefits for spouses. For example, language describing eligible spouses as "spouses recognized as married under federal law" may need to be changed.
- If an employer provides health coverage to Federally Recognized Spouses, the employer should alert its payroll department that the taxation of this coverage is changing.
- Alert employees participating in retirement plans, and who have Federally Recognized Spouses, that designating a person other than a spouse as beneficiary may be invalid, unless the spouse has consented to the beneficiary designation. Therefore, it may be necessary to update beneficiary designations or obtain the required spousal consent.

ABOUT THE EXPERT

Howard Bye-Torre is an employee benefits attorney working in the Seattle office of Stoel Rives LLP. He is a contributing author to the Thomson Reuters/EBIA publication, *Employee Benefits for Domestic Partners: Design, Taxation and Administration*. It is available on Thomson Reuters Checkpoint.

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- Requirements for Qualified Retirement Plans (http://us.practicallaw.com/3-506-6895)

Checklist

- Providing Health Benefits to Domestic Partners Checklist (http://us.practicallaw.com/9-518-0647)

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