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TO: Clients of Sitzmann Morris & Lavis Insurance Agency

RE: IRS Revenue Ruling on Same-Sex Spouses

On June 28th we reported on two U.S. Supreme Court decisions regarding laws affecting same-sex marriage: Defense of Marriage Act (DOMA) and California's Proposition 8. We hoped for guidance from the IRS on a number of issues. On the afternoon of August 29th the IRS provided us with [Revenue Ruling 2013-17](#) as well a set of [FAQs](#). The Ruling simplifies benefit plan administration by adopting the "State of Celebration" rule.

Key Provisions:

- **Recognizing the Marriage.** Plan sponsors were unsure which same-sex marriages to recognize: Is it the state of residence of the employee, the state in which the headquarters of the business is located, or the state in which the marriage occurs in determining the eligibility of the spouse for employee benefit coverage? The IRS states it recognizes the validity of a same-sex marriage that was valid in the state where it was entered into (the state of celebration), regardless of the married couple's place of domicile. This is the "state of celebration" rule.
- **Adjusting Current Payroll.** How far back must a plan sponsor go in recharacterizing amounts withheld based on imputed income collected? The IRS states that the guidance will be effective as of September 16, 2013. However, it will permit its retroactive application within the statute of limitations. This means that a plan sponsor must adjust income tax withholding, and Social Security and Medicare taxes for 2013, so that the cost of benefits provided to same-sex spouses are treated as excluded from gross income.
- **Cafeteria Plan Issues.** Can the plan sponsor permit a mid-year election under its cafeteria plan, including an FSA, for employees' whose spouses now qualify as covered persons? The plan sponsor may permit mid-year cafeteria elections on the basis of same-sex spouses becoming newly eligible. The pre-tax contributions for premiums, as well as FSAs, would take effect for the remainder of the year. Amounts available in a spending account could be used for reimbursement of expenses incurred during the plan year.
- **Adjusting Individual Tax Returns.** According to this Revenue Ruling, with certain exceptions, taxpayers may rely on the Ruling for purposes of filing original (timely) tax

returns as well as to amend or adjust old tax returns as long as the return is still in an open year (3 years from date of filing or 2 years from when the tax was paid). This will allow a taxpayer to claim his/her spouse filing jointly or separately, as well as to obtain refunds for overpayment of employment taxes and income taxes. In brief, the taxpayer who made after-tax contributions to cover his/her spouse for welfare benefits can have them recharacterized as pre-tax contributions. Please refer to [IRS Release 2013-72](#) for details. Please note that this is a federal ruling. It does not impact state income tax filings.

- **Domestic Partnerships and Civil Unions.** The IRS FAQs make it clear that the relief provided under federal law to same-sex marriages does not apply to Registered Domestic Partners or civil unions. Please refer to the IRS Release 2013-72 and the [FAQs involving Domestic Partnerships and civil unions](#).
- **Refund of Taxes Paid Due to Same-Sex Spouses.** The IRS has also published [FAQs](#) which expand on the retroactivity permitted by taxpayers as well as the ability of the employer to claim a refund for Social Security taxes and Medicare taxes paid on the same-sex spouse benefits (i.e. the imputed income collected and paid to the IRS). However, employers cannot make claims for refunds of over-withheld income tax for prior years. Please refer to FAQs A12 and Q13.
- **COBRA.** A spouse (including a same-sex spouse) who is covered by an employer-sponsored group health plan will have COBRA rights in the event of the employee's termination of employment or the spouse's loss of coverage due to divorce or legal separation. In states that don't recognize same-sex marriages a legal separation or divorce is not available. The remedy would require one of the individuals to move back to the celebration state to get the divorce in order to qualify for COBRA.
- **Dependent Care Assistance.** IRC Section 129 only allows benefits for the care of a qualifying person. A spouse is a qualifying person if he/she is not physically able or mentally capable of caring for him/herself and who has lived with the employee for more than half of the year. It appears that a plan sponsor could choose not to cover all qualifying persons (excluding the same-sex spouse) absent a state law prohibiting discrimination based on sexual orientation. It's also worth noting that spouses generally cannot be paid for providing dependent care services.
- **Family and Medical Leave Act (FMLA).** Existing Department of Labor (DOL) regulations for FMLA contain a residence test for purposes of defining a spouse. We expect that the DOL may revise its regulations to reflect the IRS rule being "celebration state." For states like California, which has its own family leave statute, the federal state of celebration rule would not apply, leaving it to the states to act or not act on the issue.

The Department of Health and Human Services also announced guidance with regard to Medicare.

What's Next:

Employers need to be aware that employees in same-sex marriages may be filing amended returns and seeking tax refunds related to these benefits, and take steps to quantify the imputed income or provide other information to employees to assist in retroactive tax relief.

The IRS will establish a “special administrative procedure” for employers to seek refunds or claim credits for Social Security and Medicare taxes related to same-sex spousal benefits, to be defined in future guidance.

We will provide you with more detail as it becomes available. As always, contact your SML Account team if you have any questions.

The information provided in this legislative update for our clients and colleagues is for general guidance only and is not intended to be, and does not constitute, tax or legal advice. We recommend that you consult with your tax and legal advisors for the interpretation or application of any laws for your particular circumstances and situation.