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# Treasury and IRS Adopt "State of Celebration" Rule for Same-Sex Marriages—Implications for Employee Benefit Plans

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*The U.S. Department of Treasury ("Treasury") and the Internal Revenue Service ("IRS") issued guidance treating a same-sex couple as "married" for all Federal tax purposes as long as the couple was legally married in a state or foreign country that recognizes same-sex marriage, even if the couple resides in a state that does not recognize the validity of same-sex marriage.*

On June 26, 2013, the U.S. Supreme Court in *United States v. Windsor* ruled that Section 3 of the Defense of Marriage Act, which had limited the definition of "marriage" to marriage between a man and a woman for purposes of all Federal law, was unconstitutional under the Equal Protection Clause of the Fifth Amendment. Despite its far-reaching effects on the Federal tax treatment of same-sex spouses, *Windsor* provided no guidance on its practical implementation regarding payroll administration and employer-provided benefits. One of the most vexing questions has been whether the IRS and employers should treat a same-sex couple as "married" as long as the marriage was validly entered into in a state or country whose laws authorize same-sex marriage (the so-called "state of celebration" approach), or whether such couples should be treated as "married" only if (and when) they reside in a state that recognizes same-sex marriage.

Treasury and the IRS provided their answer to this question on August 29, in the form of Revenue Ruling 2013-17 and two sets of "Answers to Frequently Asked Questions" at http://www.irs.gov/uac/Newsroom/Treasury-and-IRS-Announce-That-All-Legal-Same-Sex-Marriages-Will-Be-Recognized-For-Federal-Tax-Purposes;-Ruling-Provides-Certainty,-Benefits-and-Protections-Under-Federal-Tax-Law-for-Same-Sex-Married-Couples.Their guidance states that for Federal tax purposes, all rules affected by "marriage" (as well as all related terms such as "spouse," "husband" and "wife") will apply to same-sex couples who have been validly married under the laws of any state, U.S. territory, the District of Columbia or a foreign country that recognizes same-sex marriage, regardless of their state of residence or domicile. As noted by the IRS in its press release, a taxpayer's marriage status is implicated in numerous portions of Federal tax law, including tax filing status, claiming dependency status, taking standard deductions, employee benefits, IRA contributions, and claiming the earned income tax credit or child tax credit.

## Same-sex Marriages and State Law Issues

Despite its significance, *Windsor* did not determine whether a constitutional right to same-sex marriage exists. *Windsor* also did not mandate any particular definition of marriage on the states, or obligate states to recognize each other's definitions of marriage. Currently, only thirteen states and the District of Columbia recognize same-sex marriage.

Revenue Ruling 2013-17 was issued to enable a uniform, nationwide administration of Federal tax laws. IRS recognition of a same-sex marriage will not be limited to the couple's current place of domicile (which can change many times during the course of the marriage), but rather will be determined based on the marriage's validity under the laws of the jurisdiction where it was entered into. For instance, a same-sex couple legally married in Vermont would be recognized as married for Federal tax purposes even if the couple subsequently moves to Florida, Texas or any other state that does not currently recognize same-sex marriages validly entered into in another state.

## Implementation of Revenue Ruling 2013-17 Will Be Prospective, But Tax Refund Claims Are Permitted

Revenue Ruling 2013-17 will become effective prospectively as of September 16, 2013. The IRS has made clear, however, that affected taxpayers can nevertheless rely on the ruling for purposes of certain tax refund claims where the applicable statute of limitations has not expired.

As illustrated by the IRS, an employee whose same-sex spouse was covered under the employee's group health plan could file an amended tax return to recover the additional income taxes paid because the spouse's health plan premiums were paid on an after-tax basis, and because the value of the spouse's coverage was imputed to the employee as additional income. Income tax refund claims generally must be filed within three years from the date the tax return was filed or two years from the date the tax was paid, whichever is later. Similarly, the employer could seek a refund of any excess Social Security and Medicare taxes paid, as long as the applicable statute of limitations period for filing the refund claim remains open. An employer may also make adjustments for any excess income tax withheld in the current tax year, provided the employer repays or reimburses the employee for his or her excess withholdings before the end of the calendar year. The IRS has, however, specified that employers cannot assist employees by making claims for refunds or adjustments of income tax withholdings withheld from an employee for prior years; rather, only the affected employee may make such a claim within the applicable statute of limitations period.

## Individuals in Relationships Other Than Legal Marriages Are Not Affected

Revenue Ruling 2013-17 acknowledges that the *Windsor* decision did not alter the legal environment of domestic partnerships. The impact of *Windsor* on Federal tax laws is limited to legally-married same-sex spouses. Same-sex or opposite sex partners who entered into a registered domestic partnership or civil union that is not denominated as a valid "marriage" under that state's laws, for example, are not affected by *Windsor* or Revenue Ruling 2013-17.

## Further Guidance Is Still Needed and Will Be Forthcoming

The IRS has stated that it intends to issue further guidance with respect to the retroactive application of *Windsor* to employee benefits and, accordingly, it will take into consideration potential consequences of retroactive application to all taxpayers involved, including plan sponsors, plans, employers, and affected employees and beneficiaries. In its "Answers to Frequently Asked Questions for Individuals of Same Sex Who Are Married Under State Law," the IRS also specifically indicated that it will provide guidance on how qualified retirement plans and other tax-favored retirement arrangements must comply with *Windsor* and Revenue Ruling 2013-17, including plan amendment requirements and any other plan operations corrections.

Other Federal government agencies are also expected to provide guidance on the application of *Windsor* to the Federal programs that they administer. Of particular interest to employee benefit plan sponsors will be the views of the U.S. Department of Labor, which shares jurisdiction with Treasury and the IRS over plans subject to the Employee Retirement Income Security Act of 1974.

## Actions Employers Can Take Now

Pending further guidance on whether and how to apply *Windsor* retroactively to periods prior to September 16, 2013, employers should move forward to bring their payroll systems and benefit plans into compliance with *Windsor* and Revenue Ruling 2013-17 by September 16, 2013.

For example, employers with group health plans should cease imputing income to employees whose same-sex spouses participate in the health plan, and should allow such employees to pay the premiums for their spouses' coverage on a pre-tax basis if employees with opposite sex spouses are permitted to do so. Employers with qualified retirement plans should extend to same-sex spouses the same spousal consent requirements for beneficiary designations and benefit distributions as apply to opposite sex spouses, and permit same-sex spouses' medical, tuition or funeral expenses to be considered in determining eligibility for hardship withdrawals under 401(k) plans. Spouses are also entitled to more favorable rollover and required minimum distribution rules than non-spouse beneficiaries.

A key challenge to employers in meeting these requirements is identifying all of their employees who are legally married, as many employees with same-sex spouses might not have had a reason to report that information to the employer until now. Certainly, a starting point for doing so is to reach out directly to those employees who have imputed income for health coverage of same-sex spouses and domestic partners to seek clarification of those individuals' "marital" status.

## Plan Amendment Considerations

Plan amendments may be required if the current plan documentation specifically excludes same-sex spouses from certain protections required to be offered to spouses. However, while employers will be required to extend such protections in operation to same-sex spouses effective as of September 16, 2013, formal plan amendments should not be required to be adopted by that date. Treasury and the IRS are expected to issue further guidance on when such amendments will be required.

For assistance in complying with benefit plans and employment practices for legally-married same-sex spouses in accordance with recent guidance, including *Windsor* and Revenue Ruling 2013-17, please contact the Pillsbury Executive Compensation & Employee Benefits attorney with whom you normally work, or any of the attorneys noted below.

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