

## Alert

### Supreme Court's DOMA Decision Sparks Changes in Employee Benefits

July 16, 2013

On June 26, in a 5-4 decision called a "historic step forward" by President Obama, Justice Kennedy announced the Supreme Court's long-awaited decision to strike down a key part of the Defense of Marriage Act, or DOMA. Section 3 of DOMA defined "marriage" as a legal union between members of the opposite sex and defined "spouse" as an individual of the opposite sex for purposes of all federal laws. The Supreme Court ruled in *United States v. Windsor* that Section 3 of DOMA violated basic due process and equal protection as it prohibited same-sex couples who are legally married in the states in which they reside from enjoying many of the federal benefits opposite-sex married couples enjoy, including social security benefits, certain pension and welfare benefits and rights, favorable estate tax treatment and the ability to file joint tax returns.

Section 2 of DOMA, however, which was not before the Court, still does not require states to recognize the validity of same-sex marriages performed in other states that have legalized same-sex marriage. In addition, the Court simultaneously ruled in another decision that it did not have proper jurisdiction to hear a challenge to a state law that prohibits same-sex marriage in California. Because Section 2 of DOMA remains valid law, it appears that states can continue to prohibit same-sex marriages regardless of the Court's decision to strike down Section 3 of DOMA. Currently, only the following states and the District of Columbia have legalized, or have passed legislation that will legalize, same-sex marriages: Connecticut, Delaware, Iowa, Maine, Maryland, Massachusetts, Minnesota, New Hampshire, New York, Rhode Island, Vermont and Washington.

The Court's rulings have raised many questions. Though it is now clear that same-sex, legally wed spouses are eligible for the same benefits as opposite-sex spouses, it remains unclear: (1) whether the rulings are retroactive to 1996; (2) how employers and plan sponsors must implement the rulings; and (3) how plans can administer benefits for same-sex couples that were legally wed in a state that has legalized or recognizes same-sex marriages but now reside in a state that has not legalized, or does not recognize, same-sex marriages. To help ease confusion, President Obama has ordered all federal agencies to comply with the Court's rulings as quickly and smoothly as possible, so plan sponsors should expect additional guidance over the coming months clarifying how and when the Court's decision will affect the more than 1,300 laws, regulations and programs that rely on DOMA's definition of "spouse" and "marriage."

Employers and other benefit plan sponsors of tax-qualified pension and welfare benefit plans should be aware of the following potential changes they may need to make to their plan documents, participant communications, payroll systems and employment practices while waiting for the agencies to issue guidance on how to implement these changes:

*Pension Benefits.* If an employer sponsors a tax-qualified pension plan, the plan must provide same-sex spouses with certain benefits and protections:

- *Survivor Annuities.* Pension plans must provide that same-sex spouses are eligible to receive benefits under a pension plan's Qualified Joint and Survivor, Optional and Pre-Retirement Annuities. Same-sex spouses must also provide written notarized consent to an alternate form of benefit like a lump-sum payment.
- *Beneficiary Designations.* 401(k) plans must now treat same-sex spouses as the automatic beneficiary for a distribution upon a participant's death, unless the spouse consents to the participant's designation of an alternate beneficiary.
- *Minimum Required Distributions.* If a participant dies prior to commencing receipt of his or her plan benefit, that participant's same-sex spouse can now defer receipt of distributions until the participant would have attained age 70 ½ (and can receive such distributions over a longer period of time).
- *Loans.* If a plan requires spousal consent for a loan, same-sex spouses must now consent to a participant's request for a loan.
- *Hardship Distributions.* Plans must now treat same-sex spouses as the primary beneficiary of a hardship distribution, which will allow for distributions due to the medical, tuition or funeral expenses of the same-sex spouse.
- *QDROs.* A same-sex spouse who obtains a divorce will now be able to receive a portion of his or her former spouse's pension benefits under a qualified domestic relations order ("QDRO").
- *Rollovers.* A same-sex spouse who receives a distribution upon the death of his or her spouse, will now be able to roll over the distribution to his or her own IRA or plan, rather than an inherited IRA.

*Health Benefits.* If an employer sponsors a group health plan, the plan must provide same-sex spouses with certain benefits and protections:

- *Taxation of Health Benefits.* Generally, the cost of providing health coverage is tax deductible for employers, and the cost of such coverage and the amount of benefits received are excluded from an employee's income (including amounts for coverage and benefits for spouses). Even though prior to the Court's rulings employers could offer coverage to employees' same-sex spouses, such health coverage was treated as taxable income to the employee. After the Court's decision, employees will be able to pay for their same-sex spouses' health coverage on a pre-tax basis. Further, there will be no payroll taxes (FICA or FUTA) on the value of employer-provided coverage to same-sex spouses.
- *Reimbursements of Medical Expenses.* Employees can use arrangements that provide for reimbursement of qualified medical expenses, including flexible spending accounts ("FSAs"), health savings accounts ("HSAs") or health reimbursement accounts ("HRAs"), to pay for their same-sex spouse's medical expenses on a tax-free basis, regardless of the spouse's status as a federal tax dependent.
- *COBRA.* Employers must provide same-sex spouses the opportunity to elect to continue their health coverage under COBRA if employees lose coverage in a manner that would give rise to a COBRA obligation.
- *HIPAA.* Employers must permit same-sex spouses to enroll in their group health plans if an employee or the employee's same-sex spouse has a special enrollment right under HIPAA. For example, if the same-sex spouse loses coverage under his or her own plan, that spouse is immediately eligible to enroll in the employer's group health plan.
- *DCAP.* Employees can now use their dependent care assistance program ("DCAP") accounts on a pre-tax basis to cover expenses incurred for the care of the dependents of same-sex spouses.
- *FMLA.* Employers will now be required to provide employees with up to 12 weeks of unpaid leave in order to care for their same-sex spouses under the Family and Medical Leave Act ("FMLA").

## Action Items

It is important for employers and other benefit plan sponsors in states that have legalized same-sex marriage or that recognize same-sex marriages performed in other states to review existing benefit programs and policies to determine the scope of any necessary changes or clarifications that may be required as a result of the Court's decision, including:

- Reviewing and analyzing existing HR policies and procedures, including employee handbooks, to assess the current rights of same-sex spouses, and consider any changes;
- Reviewing benefit plan documents, summary plan descriptions, enrollment forms, distribution forms, beneficiary designation forms, consent forms and administrative procedures to assess the current rights of same-sex spouses and consider any changes;
- Conferring with insurance providers and third party administrators, and working with payroll departments to address taxation and withholding concerns; and
- Communicating the applicable rules and changes, once made, to employees and their family members.

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If you have any questions about the Court's ruling or its impact on your benefit plans please contact your attorney at Schulte Roth & Zabel or one of the authors.

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