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Who Is A Spouse? Changing Marriage Laws Impacts Employee Benefit Plans

The issue of same-sex marriages has been widely discussed and debated recently. On May 17, 2004, Massachusetts will permit gay and lesbian couples to marry. This will significantly affect many of the employee benefits that Massachusetts employers currently provide, including health benefits, qualified retirement plans and life and dependent life insurance. It will also affect employers outside of Massachusetts; employees may travel to Massachusetts to get married, or relocate to or from Massachusetts. This *Management Alert* will identify some of the issues that same-sex marriages will raise for employee benefit plans and outline how these issues may be addressed.

Requirements under ERISA and ERISA Preemption

Under the Employee Retirement Income Security Act of 1974 (ERISA), employers are not required to offer employee benefits. If an employer chooses to provide benefits, it is generally free to define who is entitled to benefits under an employee benefit plan — employees, their dependents, spouse and other beneficiaries. Employers may elect to provide benefits to same-sex spouses or domestic partners, but they are not required to do so under ERISA. Over the last few years, an increasing number of employers have chosen to provide benefits to same-sex (and opposite-sex) domestic partners.

On the other hand, because ERISA generally preempts state laws affecting employee benefits, employers who choose to limit spousal benefits to traditional opposite-sex spouses can do so. This will be true even in jurisdictions like Massachusetts and Vermont that recognize same-sex marriages or civil unions. Claims that a traditional opposite-sex spouse-only provision would violate state laws prohibiting discrimination based upon marital status or sexual orientation would arguably be preempted by ERISA to the extent that the employee seeks benefits under an ERISA-covered plan.

There are limits to ERISA's preemption of state law, however. In particular, employee benefit plans maintained by a

governmental or church employer normally fall outside the scope of ERISA entirely. Moreover, ERISA does not preempt state laws governing insurance. Although the law in this area is still nascent, we expect that health insurance policies issued in Massachusetts, for example, as well as state-regulated health maintenance organizations (HMOs), will not be permitted to distinguish between same-sex and opposite-sex partners in providing coverage or underwriting risk in that state.

State insurance laws may require insurance companies to offer products that cover certain classes of employees and dependents. Vermont insurance law, for example, requires that insurance contracts and policies offered to married persons and their families be made available to parties to a civil union and their families. Other states which have dealt with or are currently considering similar legislation include Hawaii, New Jersey, California and Massachusetts. This means that state insurance laws may impact who an insured medical plan (or plan option) must cover.

Employers offering self-insured benefits will need to decide how to treat same-sex spouses for benefit purposes. However, because of the interplay between ERISA and a state same-sex marriage law (as in Massachusetts), employers who have insured health plans may be required to extend health coverage to same-sex spouses, while employers who provide self-insured health benefits may limit coverage to opposite-sex partners. This would be true even within a single health plan that offers both insured and self-insured benefit options. Moreover, even where Massachusetts may require coverage of same-sex spouses in health insurance policies, Federal COBRA (for example) will not apply unless the plan design provides for it, but Massachusetts' COBRA would apply.

In addition, not all employee benefits are governed by ERISA. For example, paid time off arrangements, adoption assistance programs, educational assistance programs and uninsured short term disability plans generally are not governed by ERISA. In these situations, state and local laws will not be preempted, and employers will be subject to state and local coverage requirements. In some locales, municipi-

pal contractor laws (for those companies doing business with a local government) may impact who an employer must cover for certain benefits by requiring such coverage as a condition of doing business.

The Impact of a Plan's Definition of Spouse

ERISA requires that employers abide by the terms of their employee benefit plan documents. Thus, the plan document's definition will be critical to determining who is eligible for spousal or dependent benefits under the plan. Many plans define "spouse" by reference to state law (for example, any "spouse who is legally married" or "in a marriage recognized under state law"). With same-sex marriages recognized in at least one jurisdiction, the plan's definition of "spouse" should be reviewed, keeping in mind that some states may recognize same-sex marriages while other states may not.

For example, if a couple is married in Massachusetts but then moves to a state that does not recognize same-sex marriages, query whether the participant's marriage is "recognized under state law" for purposes of plan benefits. This question is particularly problematic because of the federal Defense of Marriage Act (DOMA) which provides that states do not have to recognize same-sex marriages under another state's laws. (Some critics have argued that DOMA is unconstitutional because it violates the "full faith and credit" clause of the federal constitution.)

In our example above — a participant marries a same-sex partner in Massachusetts and moves to a state that does not recognize the marriage — assume the participant dies and is survived by his same-sex spouse and by children from a previous marriage. In the absence of a designation of beneficiary form, will benefits under the life insurance plan or 401(k) plan go to the spouse or to the children? It is better to clarify this in advance than to litigate it later.

With federal and state laws changing, one way to assure benefits for same-sex couples under an employee benefit plan is to include "domestic partnership" provisions. ERISA contains no definition of "domestic partner" and, therefore, an employer is generally free to establish its own definition. Domestic partner benefits can be provided to unmarried opposite-sex couples, same-sex couples, or both. It is crucial for the employer to define carefully which types of couples are "domestic partners".

If an employer chooses to cover domestic partners, it must determine what documentation of the relationship will be required and should consider treatment of domestic partner benefits under federal law (including federal tax law, COBRA, FMLA, and HIPAA).

Income Tax Consequences

The cost of health insurance benefits provided by employers to their employees (and family members) is

generally exempt from Federal income taxation under Sections 105 and 106 of the Internal Revenue Code (Code). DOMA makes clear that this exemption will not apply to a same-sex spouse, unless the spouse is also a tax "dependent" of the employee. Thus, an employee who elects health insurance coverage for a same-sex spouse will have taxable income equal to the value of the coverage. The employer will face the daunting task of capturing that income for reporting and withholding purposes at the federal level, but omitting it from reporting and withholding at the state level in Massachusetts, for example.

Because of DOMA, same-sex spouses should not be included in a health flexible spending account (FSA) under Section 125 of the Code, since merely making an account balance available to provide benefits to a same-sex spouse could cause all of the employee's contributions to the account to be taxable income.

Favorable tax treatment can apply if the same-sex partner is also the employee's tax dependent under Section 152 of the Code. A dependent includes an individual who receives over half of his or her financial support for the taxable year from the taxpayer and who resides with the taxpayer as a member of his or her household for the entire taxable year. An individual cannot be treated as a dependent under Section 152 if his or her relationship with the taxpayer will violate local law, but this issue wanes in light of Vermont, Massachusetts and similar state law developments. Some employers who offer domestic partner benefits solicit an "affidavit of dependent status" to permit employees to establish that their domestic partner coverage is entitled to favorable income tax treatment under federal law.

What Should Employers Be Doing Now?

Check Insurance Policies and Positions. Employers providing insured health benefit options in Massachusetts and other jurisdictions that recognize same-sex marriages or civil unions should contact their insurance carriers to determine whether (and when) coverage will be provided to same-sex partners under applicable state laws. It is possible that insurance carriers will take the position that no policy coverage change is required, while other insurers may view the definition of "spouse" in existing insurance policies as automatically affected by the authorization of same-sex marriages. In any case, an employer should not put itself in the position of promising insurance benefits that the insurance carrier does not intend to provide. Know your carrier's position on this issue.

Monitor What Benefits the Company Must Provide. State laws related to same-sex benefits are in flux. If a plan is insured, state insurance laws apply and will likely not be preempted by ERISA. Some states may require insured health plans to cover same-sex partners while others may not. Employers should also monitor state and local law

changes in the treatment of marriage, domestic partnerships, and civil unions where they have employees.

Decide What Benefits the Company Wants to Provide to Whom. With respect to ERISA plans, at least in the absence of state insurance law mandates, coverage is a design decision for the employer. For example, an employer may offer their employees same-sex partner benefits in order to be competitive in attracting employees and generating new business opportunities. If only traditional opposite-sex spouses are intended to be covered, that should be reflected in the plans. Coverage may differ by plan. For example, access to health coverage for same-sex domestic partners may be provided, without extending the spousal consent requirements in a qualified retirement plan to such partners.

Review/Revise Plan Documents. The employer's plan documents (including summary plan descriptions) should be reviewed to make sure they accurately reflect the employer's intent. Clarify both "spouse" and "domestic partner" definitions. Take note of whether state law is referenced in the plan's definitions. For example, if a Massachusetts employer provides same-sex spousal benefits, the plan's definition of "spouse" should be broad enough to address what happens if a participant moves to a state that does not recognize such marriages.

If you have questions about same-sex partner coverage or spousal definitions under employee benefits plans, please contact the Seyfarth Shaw Employee Benefits Group attorney with whom you work or any Employee Benefits attorney listed on the website at www.seyfarth.com.

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