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In the Windsor decision issued June 26, 2013, the Supreme Court found Section 3 of the Defense of Marriage Act unconstitutional, thus recognizing same-sex marriage at the federal level. As a result, same-sex spouses lawfully married under state law are considered married for federal tax purposes, regardless of where the couple resides. This decision extends tax-favored treatment of many employer-provided benefits to same-sex spouses in a manner consistent with that for opposite-sex spouses.

IRS Notice 2014-1 provides FAQs that address the application of the various rules associated with cafeteria plans, FSAs, and HSAs under this expanded definition of a spouse. Briefly, the guidance:

- Confirms same-sex marriage is a status change under the permitted election rules and allows for mid-year election changes.
- Does not require a cafeteria plan amendment unless the plan does not contain the change in status rules set forth in the regulations.

- Provides that a cafeteria plan participant may pay the employee cost of same-sex spouse coverage on a pre-tax basis through the remaining pay periods in the current cafeteria plan or may continue to pay for the coverage on an after-tax basis. In either case, the participant will be able to make an adjustment on his or her annual tax return for the entire 2013 calendar year.
- Allows for reimbursement of a same-sex spouse's or same-sex spouse's dependents' otherwise qualified medical expenses through a health FSA.
- Imposes the family maximum HSA contribution of \$6,450 (for 2013) on a same-sex married couple where at least one spouse has family HDHP coverage.
- Indicates that, with respect to the dependent care FSA, the \$5,000 combined contribution limit applies to same-sex spouses.

The guidance does not discuss reimbursements from HRAs or HSAs. Presumably, expenses of a same-sex spouse are permitted (similar to the health FSA rules), but this is not explicitly addressed. In addition, complexities may arise for HSA-eligible individuals that become covered by a same-sex spouse's traditional health FSA (non-HDHP coverage) in a post-Windsor environment. Further guidance on these issues is needed.

Below you will find more specific information addressed in the FAQs.

Mid-Year Election Changes

Q1: If a cafeteria plan participant was lawfully married to a same-sex spouse as of the date of the Windsor decision, may the plan permit the participant to make a mid-year election change on the basis that the participant has experienced a change in legal marital status?

A1: Yes. A cafeteria plan may treat a participant who was married to a same-sex spouse as of June 26, 2013 as if the participant experienced a change in legal marital status under the permitted election change rules. Accordingly, a cafeteria plan may permit such a participant to revoke an existing election and make a new election in a manner consistent with the change in legal marital status. For example, subject to carrier approval, a participant could elect to revoke single health insurance coverage and make a prospective pre-tax election for employee-plus-spouse coverage.

For purposes of this election change, an election may be accepted by the cafeteria plan if filed at any time during the cafeteria plan year that includes June 26, 2013, or the cafeteria plan year that includes December 16, 2013.

A cafeteria plan may also permit a participant who marries a same-sex spouse after June 26, 2013 to make a mid-year election change due to a change in legal marital status.



Q2: When does an election by a participant with respect to a same-sex spouse take effect?

A2: An election made under a cafeteria plan with respect to a same-sex spouse as a result of the Windsor decision generally takes effect as of the date that any other change in coverage becomes effective for a qualifying benefit that is offered through the cafeteria plan.

With respect to a change in status election that was made by a participant in connection with the Windsor decision between June 26, 2013 and December 16, 2013, the cafeteria plan will not be treated as having failed to meet the requirements of Code § 125 and the applicable regulations to the extent that coverage under the cafeteria plan becomes effective no later than the later of:

- the date that coverage under the cafeteria plan would be added under the cafeteria plan's usual procedures for change in status elections, or
- a reasonable period of time after December 16, 2013.

Example 1

Employer sponsors a cafeteria plan with a calendar year plan year. Employee A married same-sex Spouse B in October 2012 in a state that recognized same-sex marriages. During open enrollment for the 2013 plan year, Employee A elected to pay for the employee portion of the cost of self-only health coverage through salary reduction under the cafeteria plan.

Employer permits same-sex spouses to participate in its health plan. On October 5, 2013, Employee A elected to add health coverage for Spouse B under Employer's health plan and made a new salary reduction election under the cafeteria plan to pay for the employee portion of the cost of Spouse B's health coverage. Employer was not certain whether such an election change was permissible, and declined to implement the election change until further guidance was issued.

Once guidance was issued, Employer determines that Employee A's revised election is permissible as a change in status election. Employer enrolls Spouse B in the health plan as of December 20, 2013 and begins making appropriate salary reductions from the compensation of Employee A for Spouse B's coverage beginning with the pay period starting December 20, 2013.

The cafeteria plan is administered in accordance with the guidance.

Example 2

Same facts as Example 1 except that Employee A submitted the election to add health coverage for Spouse B under Employer's cafeteria plan on September 1, 2013 and the employer implemented the election change and enrolled Spouse B in the health plan as of October 1, 2013, and began making appropriate salary reductions from the compensation of Employee A for Spouse B's coverage beginning with the pay period starting October 1, 2013.

Even though the employer allowed the pre-tax treatment prior to issuance of the guidance, the cafeteria plan was administered in accordance with this new guidance.

Q3: Is a plan amendment needed?

A3: If the cafeteria plan already contains written terms that permit a change in election upon a change in legal marital status (as is usually the case), a plan amendment to reflect same-sex marriage is not required.

To the extent that the cafeteria plan sponsor chooses to permit election changes that were not previously provided for in the written plan document, the cafeteria plan must be amended to permit such election changes on or before the last day of the first plan year beginning on or after December 16, 2013. Such an amendment may be effective retroactively to the first day of the plan year including December 16, 2013, provided that the cafeteria plan operates in accordance with the guidance under this new guidance.

Q4: How can an employee pay for the cost of coverage for a same-sex spouse?

A4: The IRS provides that a cafeteria plan participant may choose to pay for the employee cost of same-sex spouse coverage on a pre-tax basis through the remaining pay periods in the current cafeteria plan year by providing notice of the participant's marital status to the employer or the cafeteria plan, or to continue paying for these benefits on an after-tax basis.

In either case, the participant may seek a refund of federal income or federal employment taxes paid on any amounts representing the employee cost of spousal health coverage that were treated as after-tax and may exclude these amounts from gross income when filing an income tax return for the year.

Example 3

Same facts as Example 1 except that starting January 1, 2013, Employee A paid for the employee portion of health coverage for Spouse B under Employer's group health plan on an after-tax basis. The value of Spouse B's health coverage was \$500 per month, and this amount was included as taxable income and wages to Employee A for payroll purposes with respect to all pay periods starting January 1, 2013.

On October 5, 2013, Employee A made a change in status election under the cafeteria plan electing to pay for the employee cost of Spouse B's health coverage on a pre-tax basis through salary reduction. Employer implemented the change in status election on November 1, 2013, and excluded the cost of Spouse B's coverage from Employee A's gross income and wages with respect to all remaining pay periods in 2013 starting November 1, 2013.

Employee A and Spouse B file a joint federal income tax return for 2013. The value of Spouse B's health coverage for the full 2013 taxable year (including the \$5,000 of coverage (\$500 per month for 10 months) that was initially reported by Employer as includable in gross income with respect to all pay periods from January through October) may be excluded from gross income on the couple's joint return for 2013. Employee A may also request a refund of any federal employment taxes paid on account of such coverage.

Example 4

Same facts as Example 1 except that Employer's cafeteria plan included a health FSA. For the plan year beginning January 1, 2013, Employee A elected \$2,500 in coverage under the health FSA.

On October 5, 2013, Employee A elected to add health coverage for Spouse B under Employer's group health plan, and made a new salary reduction election under the cafeteria plan to pay for the employee cost of Spouse B's health coverage. On October 15, 2013, Employee A submitted a reimbursement request under the health FSA including a properly substantiated health care expense incurred by Spouse B on July 15, 2013. Employee A's FSA may reimburse the covered expense.

The result is the same even if the spouse was not added to the Employer's group health plan coverage.

FSA Reimbursements

Q5: When may the cafeteria plan permit a participant's FSA to reimburse covered expenses incurred by the participant's same-sex spouse (or a same-sex spouse's dependent)?

A5: A cafeteria plan may permit a participant's FSA, including a health, dependent care, or adoption assistance FSA, to reimburse covered expenses of the participant's same-sex spouse or the same-sex spouse's dependent that were incurred during a period beginning on a date that is no earlier than:

- the beginning of the cafeteria plan year that includes June 26, 2013, or
- the date of marriage, if later.

For this purpose, the same-sex spouse may be treated as covered by the FSA (even if the participant had initially elected coverage under a self-only FSA) during that period.

Contribution Limits for HSAs and Dependent Care Assistance Programs

Q6: Is a married same-sex couple subject to the joint deduction limit for contributions to an HSA (for 2013, \$6,450)?

A6: Yes. The maximum annual deductible contribution to one or more HSAs for a married couple, either of whom elects family coverage under an HDHP, is \$6,450 for the 2013 taxable year (as adjusted for cost of living increases).

This deduction limit applies to same-sex married couples who are treated as married for federal tax purposes with respect to a taxable year (that is, couples who remain married as of the last day of the taxable year), including the 2013 taxable year.

Q7: What happens if each spouse made contributions to his/her own HSA that, when combined, exceed the HSA contribution limit for the year?

A7: If the combined HSA contributions elected by two same-sex spouses exceed the HSA contribution limit for a married couple (for 2013, \$6,450), contributions for one or both of the spouses may be reduced for the remaining portion of the tax year in order to avoid exceeding the applicable contribution limit.

To the extent that the combined contributions to the HSAs of the married couple exceed the applicable contribution limit, any excess may be distributed from the HSAs of one or both spouses no later than the tax return due date for the spouses. Any such excess contributions that remain undistributed as of the due date for the filing of the spouse's tax return (including extensions) will be subject to the 6% excise tax.

Q8: Is a married same-sex couple subject to the exclusion limit for contributions to a dependent care FSA?

A8: Yes. The maximum annual contribution to one or more dependent care FSAs for a married couple is \$5,000. This limit applies to same-sex married couples who are treated as married for federal tax purposes with respect to a taxable year (that is, couples who remain married as of the last day of the taxable year), including the 2013 taxable year. If the combined dependent care FSA contributions elected by the same-sex spouses exceed the applicable contribution limit for a married couple, contributions for one or both of the spouses may be reduced for the remaining portion of the tax year in order to avoid exceeding the applicable contribution limit. To the extent that the combined contributions to the dependent care FSAs of the married couple exceed the applicable contribution limit, the amount of excess contributions will be includable in the spouses' gross income.

What Should Employers Do?

- Consider allowing employees with same-sex spouses to make a pre-tax election for health plan coverage consistent with the change in status rules and terms of the applicable coverage.
- Update plan documents, if necessary.
- Communicate that the qualified medical expenses of same-sex spouses are eligible for reimbursement through the health FSA and monitor for guidance regarding HSAs and HRAs.
- Communicate how contribution limits apply to married individuals (including married same-sex couples) with respect to the HSA and dependent care FSA.

