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IRS Provides FICA Reporting, Withholding, and Other Guidance Regarding Married Same-Sex

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Until the United States Supreme Court decision in *United States v. Windsor*, 570 U.S. ____ (2013), the Defense of Marriage Act (DOMA) required employers providing subsidized benefits to same-sex spouses and domestic partners/civil union partners (whether same-sex or opposite sex) to impute income on the subsidy relating to the spouse/partner benefits, and to pay Federal Insurance Contributions Act (FICA) taxes on that imputed income. If the employee paid an extra premium for the spouse/partner coverage under a cafeteria (section 125) plan, the extra premium amount attributable to the spouse/partner's coverage had to be paid on an after-tax basis.

Following *Windsor*,¹ the Internal Revenue Service (IRS) and the Department of Labor announced that, for purposes of ERISA and the Internal Revenue Code (the Code), same-sex marriages entered into lawfully in any state or foreign jurisdiction will be recognized as valid marriages – even if the couple resides in a state that does not recognize same-sex marriage.

On September 23, 2013, the IRS released Notice 2013-61, which can be found at [2013-38 IRB 201](#). Under Notice 2013-61, an employer may unwind the unfavorable taxation of a same-sex spouse's benefits retroactively to the beginning of 2013. Additionally, an employer may retroactively re-characterize the premiums paid for a same-sex spouse's coverage from after-tax to pre-tax, for all of 2013. An employer also may modify FICA tax payments and withholding either now or at the end of 2013.

Though this guidance offers long-awaited relief for employees with same-sex spouses, employers may face administrative hurdles before implementing these new rules. First and foremost, in the pre-*Windsor* world, most same-sex relationships were coded under the broad heading of "domestic partners" – regardless of whether the employee was married, in a civil union, in a registered domestic partnership, or simply met the employer's unique requirements for domestic partner coverage. Thus, some employers may not know which of the couples previously coded as "domestic partners" are actually legally married. This uncertainty will require employers to reach out to employees with "domestic partners" and determine whether they were married in states or jurisdictions that recognize same-sex marriage.

¹ In *Windsor*, the U.S. Supreme Court found Section 3 of DOMA to be unconstitutional, ruling that the Federal government must recognize lawful same-sex marriages.

The new IRS guidance also comes on the eve of most plans' annual enrollment cycle. This has driven employers to quickly retool their enrollment systems to properly administer the taxation of benefits for same-sex spouses. In many cases, this means shifting same-sex spouses out of the broad "domestic partner" coverage tier and into the narrower "spouse" coverage tier to capture the Code's favorable tax treatment.

Employers that continue to offer coverage to unmarried same-sex couples (such as civil union partners or registered domestic partners) face additional procedural steps. The process for imputing income for these couples must remain in place (unless the partner qualifies as the employee's tax dependent). Employers are also encouraged to broadcast clear guidance to their employees, explaining that *Windsor* does not provide tax-free coverage to *all* same-sex couples, but rather only those couples that are legally married. Likewise, employers should be sure that all employee communications indicate that the correction of overpaid employment taxes will apply to same-sex spouses only.

Special Rules for Correcting Overpaid Employment Taxes

The Notice provides specific guidance for employers and employees to make claims for refunds or adjustments (referred to in the Notice as corrections) of overpayments of FICA taxes and federal income tax withholding (employment taxes) with respect to imputed income resulting from the application of DOMA to benefits for same-sex spouses. The method for claim filing will vary depending on when the employer is able to modify its payroll system to change withholding and reporting. Note that many employers may have payroll systems that cannot distinguish between lawful same-sex marriages and non-marriage domestic partnerships or civil unions. Since only lawful same-sex marriages are eligible for the new treatment and for refunds, employers may need to reach out to their employees in same-sex partnerships to determine which have entered into lawful marriages. However, employers cannot demand proof of marriage (such as marriage licenses) unless similar documentation is required from opposite-sex married employees.

Correction Before Filing Third Quarter 2013 Form 941s (due October 31)

If an employer that withheld employment taxes on wages paid to an employee during 2013 on account of imputed income for same-sex spouse benefits repays or reimburses the employee for the amount of such taxes before filing the third quarter 2013 Form 941, the imputed income and reimbursed withholding do not need to be reported on the Form 941.

Correction After Filing Third Quarter 2013 Form 941s

If the repayment or reimbursement is not made before the Form 941 is filed, the IRS is offering two special alternative procedures to seek refunds.

Alternative Procedure One

Under the first alternative, an employer must repay or reimburse its employees for the amount of the overcollected FICA tax and the overcollected income tax withholding with respect to the same-sex spouse benefits for the first three quarters of 2013 on or before December 31, 2013. After repaying or reimbursing the employees, the employer, in reporting amounts on its fourth quarter 2013 Form 941, may reduce the fourth quarter wages reported and taxes remitted by amounts reimbursed. If this procedure is used, the employer will not have to file Form 941-X. However, under this special administrative procedure, the employer may only correct the employer share of FICA tax that corresponds to the employee share of FICA tax that has been repaid or reimbursed to the employees on or before December 31, 2013. Also, employers must remember that the Social Security wage base limit (\$113,700) still applies to the amount to be refunded. As such, if after the exclusion of the value of the same-sex spouse benefits from wages for 2013 the remaining social security wages of the employee are equal to or greater than \$113,700, no refund, credit, or adjustment of social security tax can be made for 2013 for that employee.²

Alternative Procedure Two

The second alternative can be used by an employer that does not repay or reimburse employees on or before December 31, 2013 for the amount of withheld FICA and income taxes with respect to same-sex spouse benefits provided in 2013. The 2013 fourth quarter Form 941

² With the exception of the Medicare tax, which is not subject to the wage base limit.

is filed without making the adjustment. The employer then may file one Form 941-X for the fourth quarter of 2013, reporting adjustments or claiming refunds or credits of overpayments of FICA taxes with respect to same-sex spouse benefits paid in all quarters of 2013. The employer must satisfy the usual requirements for filing Form 941-X, including repaying or reimbursing the overcollected employee FICA tax to employees (or, for refund claims, securing consents from employees to file a refund claim on their behalf), and obtaining the required written statements from employees stating that the employer has repaid the FICA overpayment. The employer should write "WINDSOR" in dark, bold letters across the top margin of page 1 of Form 941-X. Only corrections made under this special administrative procedure may be shown on this Form 941-X.

Years Prior to 2013

For years prior to 2013, employers may follow the "Alternative Two" procedure for filing a single 941-X. However, this special administrative procedure is subject to the usual requirements that apply in the case of corrections of overpayments for prior years, including the filing of Forms W-2c, repaying or reimbursing employees for the overwithheld taxes and obtaining the required written statements and consents from employees.

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