


Taxation of same-gender spousal benefits in wake of US Supreme Court ruling



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In the second of two landmark decisions on same-gender marriage, the US Supreme Court ruled on June 26, 2015, that the Fourteenth Amendment requires all states to license marriage between two people of the same gender and recognize same-gender marriages lawfully licensed and performed in another state. The court stipulated that religious entities have a First Amendment right to advocate against same-gender marriage, but states must issue marriage licenses. (*Obergefell v. US, No. 14-556, June 26, 2015.*)



State revenue departments across the US have needed to examine their guidance in light of this year's change to their marriage laws.

As of the date of the ruling, 37 states and the District of Columbia allowed same-gender couples to marry, leaving 13 states that continued to prohibit these marriages. In the weeks following the decision, all of these states released directives necessary for issuing marriage licenses to same-gender couples; however, such marriage licenses may be delayed in some counties where officials exercise their First Amendment right to refuse on religious grounds. (e.g., [Louisiana](#), [Mississippi](#) and [Texas](#)).

While the right of a same-gender couple to marry has no direct implication on payroll taxes, the definition of marriage is generally consistent throughout state laws, including those governing covered wages for income tax withholding, unemployment insurance, and other payroll tax and reporting purposes. Consequently, state revenue departments across the US have needed to examine their guidance in light of this year's change to their marriage laws.

Here we will identify where and how state payroll tax requirements have changed since June 26, 2015, and the steps employers should consider now and in the months leading to the 2015 year-end close.

Background

On June 26, 2013, the US Supreme Court ruled in *United States v. Windsor* that Section 3 of the Defense of Marriage Act (DOMA) (P.L. 104-199) is unconstitutional and that a lawfully married same-gender couple must be treated as married for federal purposes. For employment tax purposes, the ruling was limited to federal taxes and employee benefit rights and did not extend to the issue of a state's right to deny or recognize the marriage licensing of same-gender couples. Prior to this decision, only 13 states and the District of Columbia allowed same-gender couples to marry.

The ruling in *Windsor* triggered a change in state marriage laws in a number of states and legal challenges in others. On October 6, 2014, when the US Supreme Court [declined to hear appeals](#) from several states whose federal district courts overturned their bans on same-gender marriage, 25 states and the District of Columbia allowed same-gender couples to marry. The Supreme Court's decision not to hear the case in 2014 had the result of lifting the marriage ban in 11 additional states. (See Table 1 on page 2.)

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Table 1
States allowing same-gender marriage before June 26, 2015
US Supreme Court ruling in *Obergefell*

Alaska (10-17-2014)	Iowa (4-24-2009)	Oklahoma (10-6-2014)
Alabama (2-9-2015, halted 3-3-2015, resumed 5-21-2015)	Kansas (11-12-2014)*	Oregon (5-19-2014)
Arizona (10-17-2014)	Maine (5-17-2004)	Pennsylvania (5-20-2014)
California (6-28-2013)	Maryland (1-1-2013)	Rhode Island (8-1-2013)
Colorado (10-7-2014)	Massachusetts (5-17-2004)	South Carolina (11-20-2014)
Connecticut (11-12-2008)	Minnesota (8-1-2013)	Utah (12-20-2013 to 1-6-2014, resumed on 10-6-2014)
District of Columbia (3-9-2010)	Montana (11-19-2014)	Virginia (10-6-2014)
Delaware (7-1-2013)	Nevada (10-9-2014)	Vermont (9-1-2009)
Florida (1-1-2015)	New Hampshire (1-1-2010)	Washington (12-6-2012)
Hawaii (12-2-2013)	New Jersey (10-21-2013)	West Virginia (10-9-2014)
Idaho (10-15-2014)	New Mexico (12-19-2013)	Wisconsin (6-6-2014 to 6-13-2014, resumed on 10-7-2014)
Illinois (6-1-2014)	New York (7-24-2011)	Wyoming (10-23-2014)
Indiana (10-7-2014)	North Carolina (10-10-2014)	

*Kansas tax guidance did not allow same-gender married couples to file married joint, or married filing separately for tax year 2014. Consequently, same-gender spousal benefits were taxable during calendar year 2014.

Tax treatment of same-gender spousal benefits

For federal income tax purposes, health and other tax-exempt benefits provided to an employee's same-gender spouse are tax-free, provided the employee was lawfully married under state or country law. The IRS makes it clear that health and other benefits provided to an employee's domestic partner (including civil unions and registered domestic partners) continue to be taxable. ([Revenue Ruling 2013-17](#))

Whether the value of same-gender spouse or domestic partner benefits are included in taxable wages for state unemployment insurance or income tax withholding depends on the state's applicable tax rules (and not its marriage laws), making their tax and reporting requirements complex.

Pennsylvania, for instance, extends tax-free status to health benefits whenever there is a moral or legal obligation of the employee to provide them to a partner (marriage is not a determining factor).

Missouri banned the marriage of same-gender couples until the US Supreme Court ruling in *Obergefell*; nonetheless, for income tax purposes, the state has consistently followed the federal tax guidance in [Revenue Ruling 2013-17](#). ([Missouri Governor Executive Order 13-14](#).)

In contrast, Kansas' same-gender marriage ban was overturned in 2014; however, under guidance issued by the Kansas Department of Revenue, same-gender married couples were unable to file as married joint or married filing separately in calendar year 2014.

► **Effective date for tax treatment of spousal benefits.** Generally, in the year that a state's taxing authority allows same-gender married couples to file "married joint" or "married filing separately," spousal benefits are tax-free for that entire calendar year, or, if married later in the year, for the months lawfully married. For example, if a resident/work state's income tax regulations are amended to recognize same-gender marriage for tax year 2015, it would generally be the case that those couples lawfully married in the state of celebration as of January 1, 2015, will be treated as married in the resident/work state for the entire 2015 calendar year.

► **Effect on prior years.** Whether spousal benefits are retroactively tax-free for prior years as a result of a change in its marriage definition depends entirely on the state's taxing authority and its statute of limitations. (See Table 2 on page 5.) If employees are allowed to file amended state/local income tax returns for prior years under state tax rules, employers will need to be prepared to issue Forms W-2c upon request showing the reduction in imputed income for spousal benefits in box 16 (state wages) and box 18 (local wages), where applicable.

Under no circumstances should employers refund state income tax withholding for prior years. Instead, employees file an amended state/local income tax return to claim a refund of income tax.

Subsequent to the Supreme Court ruling in *Obergefell*, most of the 13 states forced to overturn their marriage bans have since issued revised tax guidelines allowing same-gender married couples to file as "married joint" or "married filing separately." A summary of that information as well as the ability of these taxpayers to file amended state income tax returns is summarized in Table 2 on page 5.

The tax treatment of domestic partner benefits

For tax purposes, a number of states (e.g., New Jersey) recognize couples who hold a civil union or domestic partnership license as married. Accordingly, benefits provided to an employee's partner under these circumstances are excluded from the state's taxable wages (although taxable for federal purposes).

In light of the *Obergefell* ruling, these states may amend their civil marriage laws, and if they do, civil union and domestic partnership benefits may no longer be tax-free. This is an area that will need to be closely monitored at the state level since the *Obergefell* decision has no direct impact on states' alternative partner licensing rules or the related state tax treatment of benefits provided to partners who do not hold marriage licenses federally recognized under [Revenue Ruling 2013-17](#).



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Top 7 payroll steps to consider in dealing with spousal and domestic partner benefits

- 1** Correct your 2015 income tax withholding rules as soon as possible so that you minimize excess income tax withholding on same-gender spousal benefits.
- 2** Don't worry about refunding 2015 income tax you have already withheld (though this is the best approach). If the 2015 Form W-2 shows the correct taxable wages, employees can obtain an income tax refund when they file their 2015 state and local income tax returns.
- 3** Remind employees in affected states that they may need to revise their state withholding allowance certificates to reflect their marital filing status for state income tax purposes.
- 4** Remember that in states that recognize same-gender marriage for income tax purposes, spousal benefits are also not subject to state unemployment insurance (SUI). You may need to make adjustments accordingly for 2015. Amended returns for prior years are not required and may not be cost effective. You should evaluate the impact and decide if prior-year amended SUI returns and claims for refund are cost-justified.
- 5** If you have grossed up same-gender spousal benefits in 2015, you will want to consider making adjustments since this could represent a significant refund back to the business.
- 6** Consider that some states currently continue to treat civil union and registered domestic partner benefits as tax-free. These rules could change given that same-gender marriage is now allowed in all states. Monitor these states closely and be prepared for future changes in the tax treatment of civil union/domestic partner benefits.
- 7** Some businesses have asked if they should now terminate their domestic partner benefit programs. Before terminating domestic partner benefit programs, thought should be given as to how long employees should be given to obtain marriage licenses. Consider, for instance, that in some states, county clerks (e.g., [Texas](#)) have been exercising what they believe to be their First Amendment right to refuse marriage licenses to same-gender couples. Also, some employees might like to plan for a wedding ceremony, and this too may take them time.

Table 2

Summary of current income tax provisions in the 14 states not recognizing same-gender marriage prior to *Obergefell* (as of July 30, 2015)

State	State revised guidance issued after June 26, 2015 recognizing same-gender marriage	Will accept amended state income tax returns (general rule)
Arkansas	The Assistant Revenue Commissioner of the Arkansas Department of Finance and Administration has indicated in written correspondence to Ernst & Young LLP that revised tax guidance is not necessary because it refers only to married couples without any distinction being made between same-gender or opposite-sex couples. Consequently, no change in guidance is necessary. (Email, Arkansas Department of Finance and Administration, July 23, 2015.)	Three years
Georgia	Follow federal	Three years
Kansas	A Kansas Department Revenue official has confirmed with Ernst & Young LLP that, effective for tax year 2015, a same-gender married couple must file as "married filing jointly" or "married filing separately" according to the filing status used on the federal income tax return. The Department will not issue guidance on this matter at this time. (Email, Kansas Department of Revenue, July 16, 2015.)	2014 only (per email)
Kentucky	Follow federal	Two years
Louisiana	Follow federal	Three years
Michigan	Follow federal	Four years
Mississippi	The Mississippi Department of Revenue confirmed with Ernst & Young LLP that it will accept "married filing jointly" income tax returns filed by same-gender couples. (Email, Mississippi Department of Revenue, July 31, 2015)	Three years
Missouri	Has followed federal since 2013	N/A
Nebraska	Follow federal	Three years
North Dakota	Follow federal	Three years
Ohio	Follow federal	Four years
South Dakota	No income tax	N/A
Tennessee	No income tax, but follows federal for other tax and registration purposes	N/A
Texas	No income tax	N/A



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SCORE No. YY3611
CSG No. 1507-1590468 SW
ED None

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