Employee Benefits after *Obergefell*

July 7, 2015

Prepared by Aon Hewitt
Agenda

- Obergefell v. Hodges
  - Analysis of decision

- Retirement Benefits after Obergefell

- Health & Welfare Benefits after Obergefell
  - Employers that currently cover same-sex spouses
  - Employers that offer same-sex domestic partner benefits
  - Employers that don’t cover same-sex spouses
  - Decision matrix for private employers

- Q&A
Obergefell v. Hodges
Background—Prelude to Obergefell

- **DOMA—Section 3.** In 2013, the Supreme Court struck down Section 3 of DOMA (requiring Federal law only to recognize marriages of the opposite sex) (*U.S. v. Windsor*)

- **DOMA—Section 2.** Section 2 of DOMA remained in effect (states are not required to give effect to same-sex marriages performed under the laws of other states)
  
  “No State, territory, or possession of the United States, or Indian tribe, shall be required to give effect to any public act, record, or judicial proceeding of any other State, territory, possession, or tribe respecting a relationship between persons of the same sex that is treated as a marriage under the laws of such other State, territory, possession, or tribe, or a right or claim arising from such relationship.”

- **Pre-Windsor.** Only 9 states and the District of Columbia recognized same-sex marriages

- **Post-Windsor.** 37 states (and the District of Columbia) recognize same-sex marriages
  - By state legislative or administrative action: 14 states and the District of Columbia
  - By federal or state court decision: 23 states
Same-Sex Marriage in the United States—Pre-Obergefell

- Full Same-Sex Marriage
- Partial Same-Sex Marriage
- Pro-marriage court ruling—stayed
- Constitutional ban of marriage
- State law banning marriage
- No recognition of marriage

* Source: Same-Sex Marriage USA, as of April 2015

Aon Hewitt
Proprietary & Confidential | 07/2015
Obergefell Legalizes Same-Sex Marriage

- Supreme Court ruled 5-4 that 14th Amendment requires a State to
  - License a marriage between two people of the same sex and
  - Recognize a marriage between two people of the same sex when their marriage was lawfully licensed and performed out of state

- Justice Kennedy, writing for the majority:
  “[T]he right to marry is a fundamental right inherent in the liberty of the person, and under the Due Process and Equal Protection Clauses of the Fourteenth Amendment couples of the same-sex may not be deprived of that right and that liberty. The Court now holds that same-sex couples may exercise the fundamental right to marry…. [T]he State laws challenged by Petitioners in these cases are now held invalid to the extent they exclude same-sex couples from civil marriage on the same terms and conditions as opposite-sex couples.”

- Four dissents, one filed by each dissenting justice, including Chief Justice Roberts
Retirement Benefits and Same-Sex Marriage
What Does the *Obergefell* Decision Mean for Retirement Plans?

<table>
<thead>
<tr>
<th>Obergefell Decision Key Points</th>
<th>Issues/Impact on Retirement Plans</th>
</tr>
</thead>
<tbody>
<tr>
<td>States Must Permit Same-Sex Marriages</td>
<td><strong>Marriage Recognition.</strong> Same-sex couples may now be married in any state and have the marriage recognized under the retirement plan</td>
</tr>
<tr>
<td>States Must Recognize Validly Performed Same-Sex Marriages from Other States</td>
<td><strong>Retroactive Effect.</strong> No guidance provided on implications involving plan’s failure to recognize marriages prior to DOMA being declared unconstitutional</td>
</tr>
<tr>
<td></td>
<td><strong>Marital Status.</strong> Domestic partnerships, civil unions, or other relationships that are not treated as a “marriage” under state law are not required to be recognized by a retirement plan</td>
</tr>
<tr>
<td></td>
<td><strong>Domestic Partners.</strong> Plan sponsors may decide to no longer recognize domestic partners now that they are free to marry in all states</td>
</tr>
<tr>
<td></td>
<td><strong>Confirmation of Marital Status.</strong> Plan sponsors should apply same procedures to verify opposite- and same-sex marital status</td>
</tr>
<tr>
<td></td>
<td><strong>Plan Documents.</strong> Plan documents should be reviewed to confirm ability to recognize same-sex marriages validly performed in any state</td>
</tr>
<tr>
<td></td>
<td><strong>Disclosure to Participants.</strong> Possible need to communicate the impact to participants, particularly any change to plan administration</td>
</tr>
<tr>
<td></td>
<td><strong>State Income Taxes.</strong> State income tax withholding laws will now be required to recognize marital status of same-sex spouses for plan distributions</td>
</tr>
</tbody>
</table>
What Does the Obergefell Decision Mean for Retirement Plans?

<table>
<thead>
<tr>
<th>Obergefell Decision Key Points</th>
<th>Issues/Impact on Retirement Plans</th>
</tr>
</thead>
<tbody>
<tr>
<td>States Must Permit Same-Sex Marriages</td>
<td><strong>Plan Administration.</strong> Post-Windsor administrative rules for same-sex spouses continue to apply</td>
</tr>
<tr>
<td>States Must Recognize Validly Performed Same-Sex Marriages from Other States</td>
<td></td>
</tr>
<tr>
<td></td>
<td>▪ Required Minimum Distributions—Age 70½</td>
</tr>
<tr>
<td></td>
<td>▪ Eligible Rollover Distributions</td>
</tr>
<tr>
<td></td>
<td>▪ Qualified Domestic Relations Orders (“QDROs”)</td>
</tr>
<tr>
<td></td>
<td>▪ Beneficiary Designations</td>
</tr>
<tr>
<td></td>
<td>▪ Qualified Joint and Survivor Annuities (“QJSAs”)</td>
</tr>
<tr>
<td></td>
<td>▪ Qualified Pre-Retirement Survivor Annuities (“QPSAs”)</td>
</tr>
<tr>
<td></td>
<td>▪ Hardship Withdrawals</td>
</tr>
<tr>
<td></td>
<td>▪ Plan Loans</td>
</tr>
<tr>
<td></td>
<td><strong>Pension Funding.</strong> Confirm financial impact, if any, to plan funding obligations for recognition of same-sex spouses for survivor annuities and death benefit payments</td>
</tr>
<tr>
<td></td>
<td><strong>Nonqualified Plans.</strong> Confirm intent to track qualified plan spousal provisions or individual contract terms</td>
</tr>
<tr>
<td></td>
<td><strong>Public Sector Plans.</strong> Provide same-sex spouses same spousal rights as apply to opposite-sex spouses</td>
</tr>
</tbody>
</table>
Health & Welfare Benefits after Obergefell
Impact on Health & Welfare Benefits

Impact will vary among employer that

- Currently cover same-sex spouses
- Offer same-sex domestic partner benefits
- Don’t cover same-sex spouses
Employers That Currently Cover Same-Sex Spouses

What stays the same?

- After Windsor, Federal tax law was settled: a lawful spouse is a spouse
  - An individual married to a person of same sex is married if the marriage occurred in a state that recognized same-sex marriage (the “place of celebration” rule)
- Under ACA, employers do not have to offer or subsidize health care coverage for spouses
- Nothing under ERISA or PHSA requires coverage of spouses under employer health plans or defines a spouse for purposes of employer health plans
- Obergefell does not apply to domestic partnerships or civil unions
  - State- or locally-recognized domestic partnerships and civil unions are not marriages
  - State and Federal income tax treatment remains the same as before

What changes?

- Under Obergefell, state income tax laws in remaining 13 non-recognition states will have to conform to Federal income tax law
  - Employers will not be required to impute income to employees on the value of benefits provided to spouses of the same sex
  - Will take time for state income tax departments to issue guidance
Employers That Offer Domestic Partner Benefits

Are domestic partner benefits still relevant after Obergefell?

- Employers that offer domestic partner benefits might re-evaluate need for continuing these benefits
- Employers originally offered domestic partner benefits to provide benefits and legal protections for same-sex couples equal to those for opposite-sex spouses
  - Eventually expanded to include opposite-sex domestic partners

Considerations in evaluating domestic partner benefits

- Cost of administration (e.g., imputed income)
- “Take rate” among employees
- Transition issues
  - End program?
  - Freeze enrollment?
- Compliance with state and municipal Equal Benefits Ordinances (“EBOs”)
  - E.g.: California; San Francisco; Los Angeles; Seattle; Miami Beach; Broward County (Florida)
  - Under EBOs, municipality (or state) will not do business with employer unless employer offers same-sex and opposite-sex domestic partners same benefits as opposite sex spouses
    - EBOs might be modified post-Obergefell
Employers That Don’t Cover Same-Sex Spouses

- *Obergefell* does not address coverage of same-sex spouses under health and welfare benefit plans

- Employers need to consider risks of not covering same-sex spouses under health and welfare benefit plans and consult counsel

- Federal law considerations
  - *Obergefell* holds that states violate 14th Amendment by not recognizing same-sex marriage
    - Same reasoning could apply to coverage of employee benefit plans of state and municipal employers
  - No Federal statute prohibits discrimination based on sexual orientation, but risk of civil lawsuit under Title VII of Civil Rights Act for sex discrimination still exists

- State law considerations
  - Twenty-one states and D.C. have passed laws prohibiting employment discrimination based on either sexual orientation, gender identity, or both
  - ERISA preemption does not apply to laws of “general applicability”

- Plans of religious employers
  - Unclear
Next Steps for Private Employer Plans After Obergefell

<table>
<thead>
<tr>
<th>FIRST</th>
<th>NEXT</th>
<th>THEN</th>
<th>AFTER State Income Tax Guidance**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consider Design Changes*</td>
<td>Implement Design Decisions</td>
<td>Communicate Design Decisions</td>
<td>State Income Tax Treatment</td>
</tr>
<tr>
<td>▪ Spouse coverage (all, some, none?)</td>
<td>▪ Formally amend plan documents</td>
<td>▪ Distribute SPDs/SMMs, SBCs</td>
<td>▪ Work with payroll vendor to stop imputation when guidance comes out</td>
</tr>
<tr>
<td>▪ Domestic partner coverage (all, some, none?)</td>
<td>▪ Update SPDs &amp; SBCs</td>
<td>▪ Revise administrative processes and procedures, call center scripts</td>
<td>▪ Communicate effective dates/retroactivity to employees</td>
</tr>
<tr>
<td>▪ Now, or for Open Enrollment 2016?</td>
<td>▪ Develop employee communications strategy</td>
<td>▪ Reach out to vendors regarding design decisions and timeline</td>
<td></td>
</tr>
<tr>
<td>▪ If fully-insured, discuss with insurer</td>
<td>▪ Work with vendors on systems changes</td>
<td>▪ Work with vendors on systems changes</td>
<td></td>
</tr>
<tr>
<td>▪ If considering only offering coverage to opposite sex spouses, discuss with legal counsel</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Some design decisions may depend, at least in part, on state tax and insurance law guidance.
** Some employers may choose to stop imputing tax immediately, or as of 1/1/2016, before states provide guidance.
Implications for Outsourcing—Imputed Income

- Imputed Income

- Employers will need to assess their current state for same sex spousal benefits to determine required action and timeline
  - Most employers previously made changes that will likely mean no immediate change.

- Employer covering same-sex spouses fall into one of three categories:
  - Sends imputed income for all same sex spouses to payroll
    • Payroll determines if imputed income applies for state and local purposes.
  - Monitors state-by-state status and only sends imputed income to payroll for those states that still require imputed income for state and local purposes
  - Does not calculate any imputed income for state and local purposes

- All three processes supported by Aon
  - Aon will make changes upon client request
    • Will not take any cross client action without further regulatory guidance
    • Aon expects ultimately all clients will end up using the third solution longer term
Implications for Outsourcing—Additional Administrative Considerations

- To which dependents will employer offer benefits?
  - Does offering vary by benefit?

- Will employer no longer offer benefits to other types of unmarried dependents?
  - Same sex domestic partner?
  - Opposite sex domestic partner
  - Civil union?

- If making a change, consider how to identify and convert any existing dependents and are all parties who receive information such as the health carrier ready to receive that information?
  - When will it be effective?
  - Will any retroactive changes be required?
  - How will communications to individuals occur?
  - Understand if there is an impact to other administrative services such as DB or DC
Questions & Answers