

Windsor, DOMA and Qualified Retirement Plans

By Jessica Summers

As we previously reported, on June 26, 2013, in the case of *U.S. v. Windsor*, the U.S. Supreme Court held that Section 3 of the Defense of Marriage Act (DOMA) – which defined “marriage” as “only a legal union between one man and one woman as husband and wife” and “spouse” as only “a person of the opposite sex who is a husband or a wife” – was unconstitutional under the Fifth Amendment. The Court’s decision in *Windsor* means that the marriage-dependent federal rights and privileges which, because of DOMA, were previously unavailable to same-sex couples, will now apply to qualifying same-sex married couples. This change will impact certain employment rights, as well as the nature and administration of the programs and benefits that many employers provide to their employees. For a comprehensive discussion of these areas which will be impacted and the outstanding questions that remain after *Windsor*, please see our article [here](#).

One significant area of employee benefits law which will be impacted by the *Windsor* decision is the qualified retirement plan system. As the qualified retirement plan system is already governed by nuanced and at times complex laws, it critical that employers and plan administrators be aware of which specific areas will be impacted by *Windsor* and what actions they will need to take to address these changes.

A qualified retirement plan can take a number of different forms, ranging from defined benefit and money purchase plans to 401(k)s and profit sharing plans. All qualified retirement plans are governed by the Employee Retirement Income Security Act (ERISA), which sets forth express rules for how the plan must be operated and the benefits distributed. A number of ERISA’s provisions are dependent on whether the participant in the qualified plan is married. ERISA was designed with the intent of creating a uniform system under which to administer retirement plans. While at this point it remains unclear which individuals who enter into same-sex marriages will be considered to be married for the purposes of federal law (referred to below as a “qualifying same-sex marriage” and “qualifying same-sex spouses”), maintaining such uniformity would be another motivation for the administration to recognize all legally entered same-sex marriages regardless of the residency of the parties. If this were to occur, employers in states that do not allow same-sex marriage would also be obligated to apply ERISA rules equally across same-sex and opposite-sex marriages. It is yet unclear how the IRS will handle situations in which a same-sex spouse would have been in a more favorable position today had they previously received the benefits and treatment provided to spouses under ERISA.

Hardship Distributions

The first area of qualified retirement plans that will be impacted by the *Windsor* decision is what is known as hardship distributions. Employees under the age of 59 ½ are generally prohibited from withdrawing money from their 401(k), 403(b) or 457(b) plans. However, such plans may, but are not required to, allow employees to make “hardship withdrawals” from the plan to address an “immediate and heavy financial need”. The IRS rules provide that, among other things, an employee is automatically considered to have a “immediate and heavy financial need” if the requested distribution is (1) to pay for medical care for the employee or his or her spouse, dependents or beneficiaries, (2) to pay tuition and related fees for the post-secondary education of the employee or his or her spouse, children, dependent or beneficiary or (3) to pay funeral expenses for the employee or his or her spouse, children dependents or beneficiaries. **After *Windsor*, employees in qualifying same-sex marriages will now have greater options for making hardship withdrawals than they previously did when their same-sex spouse was not recognized as a spouse under ERISA.**

Required Minimum Distributions

Another area of the qualified retirement plan rules that will be affected are required minimum distributions (RMDs). Under ERISA, qualified plans are generally required to begin making RMDs to employees in the year that the employee reaches 70 ½ years of age or retires, whichever is later. The amounts of these

distributions are generally calculated based on the employee-participant's life expectancy. However, if the spouse is the sole beneficiary of the plan and is more than 10 years younger than the employee, a longer life expectancy is used to calculate the RMDs. Special rules applying to spouse-beneficiaries also come into play if the employee dies before the RMDs begin. Under ERISA, if a surviving spouse is named as the beneficiary of the retirement plan and the employee dies before the RMDs begin, the surviving spouse can generally wait to begin receiving the benefits until the time when the spouse, had he or she lived, would have turned 70 ½.

Non-spouse beneficiaries of retirement plans, on the other hand, are generally required to either receive the entire value of the plan within five years of the employee's death or begin taking benefits, calculated based on the life expectancy of the beneficiary, from the plan within a year of the employee's death. **With the *Windsor* decision, if a qualifying same-sex spouse is more than 10 years younger than the employee, the couple will have the option of taking smaller RMDs from the employee's retirement plan. Further, if the employee dies before the RMDs begin, his or her qualifying same-sex spouse will be able to keep the money in the retirement plan longer, instead of being forced to bring it into income more quickly as non-spouses are required to do.**

Qualified Joint Survivor Annuities, Qualified Optional Survivor Annuities and Qualified Pre-Retirement Survivor Annuities

Also in the area of inherited retirement monies, the *Windsor* decision will impact same-sex qualifying spouses' rights as to defined benefit or money purchase plans. A qualified joint and survivor annuity (QJSA) is the default way in which money is distributed from a defined benefit or money purchase plan. Some older profit sharing plans may also have a QJSA feature as a result of a merger with a money purchase pension plan. Under a QJSA, retirement benefits are paid at 100 percent during the joint lives of the participant and the spouse and then as a survivor annuity for the spouse over his or her lifetime at a set rate of between 50 and 100 percent of the annuity paid during the joint lives of the participant and the spouse. In order to opt out of having the benefits distributed as a QJSA and instead use an alternate method of distribution, such as a lump sum distribution, the participant must elect the alternative method of payment and the spouse must consent in writing.

As to alternate methods of distribution, a defined benefit or money purchase plan is also required to provide the participant the option of a qualified optional survivor annuity (QOSA) which also provides for a spousal annuity at a rate of 75 percent of the annuity paid to the participant. Unless elected by the participant and consented to by the spouse, a defined benefit plan or money purchase plan is also required to provide spouses with a pre-retirement death benefit, generally known as a qualified pre-retirement survivor annuity (QPSA), in the event that the employee dies before reaching retirement. The QJSA, QOSA and QPSA rules, including the requirements that spouses waive their survivor rights, consent to plan loans and receive notices, do not apply if the participant does not have a spouse. **With the *Windsor* decision, qualifying same-sex spouses will now have greater rights and options as to their same-sex spouses' defined benefit or money purchase plans.**

Inherited Plans

With the *Windsor* decision, qualifying same-sex spouses will also have a greater flexibility as to how to handle distributions from retirement plans that they inherit from their same-sex spouses. While a spouse beneficiary may roll over an inherited distribution directly or indirectly to another retirement plan or IRA and treat it as their own, a non-spouse may only roll over such a distribution directly to an inherited IRA, which are subject to special and less flexible rules. Additionally while inherited money placed in an IRA will be distributed over the life expectancy of any beneficiary, the formula by which the life expectancy of a spouse is calculated is more favorable than that for a non-spouse and will generally result in the spouse having a longer period of time over which to withdraw the money.

Qualified Domestic Relations Orders

Finally, the *Windsor* decision will also impact the rules related to Qualified Domestic Relations Orders (or QDROs). Generally, ERISA prohibits participants in a qualified retirement plan from assigning their benefits. An exception to this rule is a QDRO which is issued by a state authority, generally a court, as part of a domestic relations order. A QDRO may assign an "alternate payee", generally a former spouse or dependent, the right to receive some or all of the participant's retirement plan benefits or recognize a former spouse's right to receive retirement plan benefits as if they were a current spouse. **With the *Windsor* decision, a same-sex spouse will now be eligible to obtain a QDRO upon the dissolution of his or her qualifying same-sex marriage and, depending on the nature of the QDRO, be treated as a current spouse for the purposes of distributions from the former spouse's retirement plan.**