



BENEFIT *Advisor*

In This Issue

In this eleventh issue of the McGrawWentworth Benefit Advisor for 2004, we will summarize a new law in California that may affect your employee benefit plans. The California Insurance Equality Act requires insurance carriers licensed to do business in California to extend the same benefits it offers employees' spouses to registered same sex domestic partners. The requirement is not limited to medical plans and extends to any coverage regulated by the California Department of Insurance.

We welcome your comments and suggestions regarding this issue of our technical bulletin. For more information on this Benefit Advisor, please contact your Account Manager or visit the McGrawWentworth web site at www.mcgrawwentworth.com.

“Special Alert: If You Have Employees in California”

A recently passed California bill could affect your employee benefit plans. On September 13, 2004, Governor Schwarzenegger signed into law The California Insurance Equality Act (Assembly Bill 2208 or AB 2208). This act requires all group insurance policies and group health care service plans issued in California to offer domestic partners the same benefits they offer spouses. This significant legislation affects not only health plans, but also life, accident, disability, and property and casualty coverage.



plan is fully insured, and your insurance carrier is licensed to do business in California, the carrier must comply with this bill.

If your organization fully insures life benefits, dental, vision, accident or other benefit that provides spouse coverage, your carrier must offer the same coverage options and rates to registered domestic partners.

rier must offer the same coverage options and rates to registered domestic partners.

Effective Date

The effective date depends on the coverage type. For medical plans, including dental and vision coverage, the act becomes effective for new business and renewals as of the first plan year or renewal date on or after January 2, 2005.

The effective date for any non-medical coverage is the first plan year or renewal date on or after January 1, 2005.

There are different interpretations of this law. It **does not apply directly** to employers; it applies to insurance carriers licensed to do business in California. Carriers need to determine if it applies to your contract. If your organization offers **any benefits** to employees in California that **are fully insured**, you need to determine whether your insurer interprets this bill to mean that your plan must cover your California employees' domestic partners.

Who Will Be Affected?

If you have employees in California, this bill will most likely affect you. If your medical plan is self-funded, ERISA preemption will keep you from having to comply with this bill. However, if your

Defining Domestic Partner

This law defines domestic partners as two adults who share each other's lives in a mutually caring, committed relationship. To establish a do-

mestic partnership in California, the partners must file a Declaration of Domestic Partnership with the Secretary of State and must meet all the following requirements:

1. They must live together.
2. They must agree to be jointly responsible for each other's basic living expenses incurred during the domestic partnership.
3. They are not married to someone else and they are not currently a member of another domestic partnership.
4. They may not be blood relatives or related in a way that prevents them from marrying each other under California law.
5. Both partners are at least 18 years old.
6. Either of the following are met:
 - The partners are the same sex.
 - The partners are opposite sexes but one or both of the partners is over age 62. Also one or both persons are eligible for old age insurance benefits under Title II of the Social Security Act as defined in 42 U.S.C. Section 402(a) or are eligible under Title XVI of the Social Security Act as defined in 42 U.S.C. Section 1381 for aged individuals.
7. They are both capable of consenting to the domestic partnership.

Registering as a Domestic Partner

California has a formal process to register domestic partners. The CA

2208 law requires companies to offer registered same sex domestic partners the same insurance coverage available to married spouses.

To register, domestic partners must file a Declaration of Domestic Partnership at any Secretary of State's office in California. After the state receives the necessary forms and proof of domestic partnership, it sends the couple a "Certificate of Registered Domestic Partnership." Insurers can request this certificate if an employee decides to cover a domestic partner.

To formally end a domestic partnership, the couple must file a "Notice of Termination of a Domestic Partnership" with the Secretary of State. Registered domestic partners have the same legal responsibilities when they end a partnership as married couples have when they divorce.



Tough Compliance Issues

Same gender couples must meet certain requirements before they can register as a domestic partnership in California, and the insurance carrier can require the couple to be registered in California before they can receive benefits under an insured plan. A plan can require proof that the domestic partnership is registered if, and only if, the plan requires similar proof for a heterosexual married couple.

The federal government does not recognize domestic partners in tax issues or legislation. Complying with this act will be difficult for employers on several levels:

- COBRA - COBRA does **not** require an employer to extend COBRA continuation rights to domestic partners. However, California has a very generous state law called CAL COBRA that requires insurance carriers to offer domestic partners COBRA-like coverage.
- Federal and State Taxes
 - Federal: Domestic partners are generally not considered eligible dependents under Section 125. The amount an employee spends to cover a domestic partner is not deductible. The federal government does not permit employers to provide same sex domestic partners tax-favored status. Employee contributions for the coverage are considered post tax, and the fair market value of the coverage must be considered part of the employee's income.
 - State: Under certain circumstances, California recognizes same sex domestic partners as eligible dependents. If the partnership meets the state requirements, domestic partners can take deductions on a tax-favored basis for California state tax only.
- Equal Coverage - If employers cover a spouse under a fully insured plan, they must offer equal coverage for a same sex domestic partner.

Continued on Page 3

While this rule may not directly affect your organization, it may affect your benefit plan if:

- You have employees residing in California.
- Your benefit plan is fully insured.
- Your benefit plan covers spouses.

The rule is written to apply to insurance carriers, but it will affect employers. The impact will primarily be felt in plan administration and federal tax implications.

Plan Administration

Contact your carriers to determine how they intend to comply with this act. You should contact the following carriers on behalf of your California employees if they extend any spousal coverage options and are fully insured:

- Medical
- Dental
- Vision
- Life, Voluntary Life, AD&D
- Disability
- Auto or homeowners
- Long term disability
- Group legal plans

In particular, ask the following:

- Are they required to comply with AB2208?
- Will they inform California employees of the requirement to offer same sex domestic partner coverage?
- Will they require certain documents in order to comply with AB2208 for any spousal benefits? (Carriers cannot

require domestic partners to officially verify their partnership if they do not require married couples to officially prove they are married. Carriers may now require proof of marriage before adding spouses in order to require official documents on same sex registered domestic partners.)

- Will the carrier amend the summary plan description to clarify the coverage available for same sex domestic partners under this act?
- Will this law affecting California plan participants have any effect on plan rates?

Many employers already offer medical coverage to same sex domestic partners. This act applies only to fully insured plans that cover spouses in California. If a plan already offers medical benefits

to same sex domestic partners, it must also offer life coverage, disability coverage, or any other insurance benefit available to spouses.

Employers must also decide the best way to explain the coverage California requires. Employers who currently do not wish to cover same sex domestic partners should make it clear that this law applies only to California residents.

Federal Tax Implications

This law attempts to end discrimination in spousal benefits. It ensures that same sex domestic partners receive the same benefits provided to married spouses under a fully insured plan. However, the federal government does not recognize

same sex domestic partnerships. Probably one of the more difficult issues employers will face in complying with this Act is the tax consequences of providing same sex domestic partner coverage. Unless a domestic partner is an IRS Section 152 dependent, the IRS considers the full value of the benefit provided to a same sex domestic partner as taxable income.

The IRS does not allow contributions for coverage of a same sex domestic partner to be taken from an employee's pre-tax pay. An employer's payroll administrator must be able to take the additional contribution for same sex domestic partner benefits out of the employee's post-tax pay.



In addition, the employee must pay taxes on the value of the same sex domestic partner's benefits. The following is an example of the

federal tax implications of extending same sex domestic partner benefits.

Your organization must treat the domestic partner just as any other legal spouse the plan covers. You should charge the same amount required to cover a spouse; however, this amount is considered post-tax AND the fair market value of the coverage (less the post-tax contribution for domestic partner coverage) must be imputed in the employee's income.

Assume your organization's monthly premium for single coverage is \$400 and two-person coverage is \$750. You determine the fair market value of a domestic partner's coverage is the \$400 single cover-

	Single	Two Person
Monthly Employer Premium Cost	\$400	\$750
Monthly Employee Contribution Rate	\$50	\$100
Fair Market Value	\$400	

Effect on employee: \$50 post-tax contribution and \$350 per month must be added to income to reflect the fair market value of coverage.	\$100 (The employee's pre-tax \$50 contribution and the domestic partner's post-tax \$50 contribution)
	PLUS
	\$350 (fair market value minus employee's post-tax contribution for the domestic partner's coverage)
	\$400 fair market value
	\$ 50 contribution for domestic partner = \$350

age amount. The employee contributes \$50 monthly for single coverage and \$100 monthly for two-person coverage. Normally, you would charge an employee and his legal spouse \$100 for the two person coverage, pre-tax.

To treat domestic partners and married spouses equally, you would have to charge the employee the \$100 two-person contribution (\$50 pre-tax for the employee's portion and \$50 post-tax for the partner's portion). You must also impute the fair market value of the domestic partner coverage to the employee's income. To calculate this imputed income, subtract the \$50 contribution for the domestic partner from the \$400 fair market value of the coverage (\$400 fair market value - \$50 post-tax contribution for domestic partner = \$350 to be imputed).

The tax consequences when benefits for same sex domestic partners are covered can be complicated. Any

employee who chooses to cover a domestic partner should ask a tax professional to explain the tax issues involved in electing this coverage.

Conclusion

Like it or not, California state law is compelling insurance carriers to offer same sex domestic partners the same medical, dental, vision, life or other benefits they offer spouses.

While California can regulate insurance only for carriers in that state, this law can have a significant impact on employers in other states as well. For the most part, insurance carriers are responsible for complying with this law. However, parts of this act affect employees' federal tax deductions on premiums if they provide these benefits for their domestic partners. You should clearly explain these issues to your California employees if they choose this coverage.

Overall, providing this coverage seems to have little effect on total plan cost. When employers have voluntarily offered this coverage to employees, only a few employees have enrolled their same sex domestic partners. If carriers insist the partnership be registered in California, even fewer employees would most likely participate. However, even if one California employee chooses to enroll a same sex domestic partner, you need to thoroughly understand the state and federal tax issues involved.

If you have any questions regarding California's Assembly Bill 2208, please contact your McGraw Wentworth Account Manager. **MW**

Our technical bulletins are written and produced by McGraw Wentworth staff and are intended to inform our clients and friends on general information relating to employee benefit plans. They are not intended to provide either legal or tax advice. Before implementing any welfare or pension benefit program, employers are urged to consult with their benefits advisor and/or legal counsel for advice that is appropriate to their specific circumstances.

McGraw Wentworth
3250 West Big Beaver Road, Suite 500
Troy, MI 48084
Telephone: 248-822-8000 Fax: 248-822-4131
www.mcgrawwentworth.com