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Date: May 10, 2000
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Supplement #2

To: CSU Presidents

From: Jackie R. McClain
Vice Chancellor
Human Resources

Subject: Domestic Partner Benefits Update

As a result of the passage of AB 26, effective January 1, 2000, domestic partners of CSU employees became eligible to obtain health benefits under the standard eligibility rules of the Public Employees’ Medical Health and Care Act (PEMHC A). The Board of Trustees, with the support of CSU unions, extended dental and vision benefits to domestic partners of eligible employees. Employees were advised that adding domestic partner benefits would result in taxable income to the employee and that the CSU was in the process of determining the taxable value of the benefit.

Imputed Tax Liability

The CSU, after extensive discussions with the State Controller’s Office (SCO), the Public Employees’ Retirement System (PERS), and the Department of Personnel Administration, concluded that the Internal Revenue Service (IRS) has ruled that the actual cost of the domestic partner benefit is taxable income to the employee. To arrive at the actual cost, the CSU examined the health, dental and vision premium structure. For health and dental, we have the following structure:

- Employee only
- Employee plus one dependent
- Employee plus two or more dependents

For these two benefits, the taxable income of the domestic partner benefit will be the cost difference between the employee only and the employee plus one dependent premium rate. This approach recognizes the value of adding one dependent, using a single employee as the base line. The SCO will use a flat tax rate of 28% federal, 6% state, 6.2% Social Security, and 1.45% Medicare to calculate the health and dental tax value of the benefit.

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Distribution: All with Attachment

Executive Vice Chancellor, CFO
Vice Presidents, Administration
Associate Vice Presidents/Deans of Faculty
Human Resources Directors
Benefits Officers (w/attach & labels)
Payroll Managers
The taxable value of the benefit will be constant as shown in the following examples:

- An employee enrolled in Kaiser for self only at the one-party rate adds his/her domestic partner. The monthly taxable value of the benefit is the two-party premium rate less the one-party premium rate ($368.12 — $184.06 = $184.06). Each month, the employee will have an additional $184.06 in taxable income.
- An employee enrolled for self and family at the three-party rate adds his/her domestic partner. The taxable value of the benefit is still the two-party premium rate less the one-party premium rate ($368.12 — $184.06 = $184.06). Again, each month, the employee will have an additional $184.06 in taxable income.

For vision, the cost is a flat rate, regardless of the number of dependents. Adding domestic partners to the program will have a negligible impact on the premium. As a result, there is no taxable income to the employee for adding a domestic partner to the vision insurance plan.

**Domestic Partner Party Codes**

The SCO has finalized system changes to accept party codes that denote the addition of a domestic partner and children of the domestic partner. The SCO will obtain the domestic partner information from the Public Employees' Retirement System (PERS) COMET system. These codes will be transparent to the CSU, as PERS will enter domestic partner party codes into its COMET system based upon Family Relationship codes listed by the campus on the employee’s HBD-12 form. PERS will input domestic partner information in the following format:

- Employee Adds Domestic Partner - COMET system changes the party rate from 1 to A for party rate 2.
- Employee + 1 Dependent Child Adds Domestic Partner - COMET system changes the party rate from 2 to B for party rate 3.
- Employee + 2 Dependent Children Adds Domestic Partner - COMET system changes the party rate from 1 to B for party rate 3.

For dental benefits, the same party rate coding structure is being used (please refer to HR 2000-01).

In the SCO system Payment History Inquiry Miscellaneous Deduction screen, the health and/or dental party code will reflect A or B for domestic partners.

**Taxation of Domestic Partner Benefit**

The CSU has approximately 100 employees who have added domestic partners to their benefit plans and have, as a result, incurred a tax liability. The SCO will implement a “look back” method for tax withholding on the domestic partner benefit beginning in May 2000. Key points are:
• The SCO will “look back” at the prior month to determine if an employee has added a domestic partner in that month. The SCO will then include the domestic partner taxable income from the prior month in the current month and take appropriate taxes. For example, the May “look back” will be to April.

• In May, the SCO will also “look back” and compute outstanding tax liability for Social Security and Medicare for the months of January through March, if applicable. For the May master payroll (paid May 31), the SCO will withhold applicable Social Security and Medicare monthly taxes for April, plus any prior pay period liability for January through March.

• The SCO will withhold federal and state taxes for April from the May master payroll warrant. Taxable income from the January-March pay periods will be reported on the employee’s year 2000 W-2; however, no taxes will be withheld.

Attachment A is a letter to employees with a domestic partner that provides information on relevant tax issues. This letter has been reviewed by the SCO and the content should not be modified. As a courtesy, the SCO has provided the address labels identifying the employees at your campus who should receive this letter. These labels are being provided to your campus Benefits Officers for campus distribution of the letter. Employees should be notified immediately as these deductions will be withheld from the May 31 warrant.

The Controller’s Office will issue a Payroll Letter in May that will provide additional information on the domestic partner program.

This Human Resources letter is available on the Human Resources Administration’s web page at: http://www.calstate.edu/tier3/HR-Adm/memos.html.

Please contact Pamela Chapin in Human Resources Administration at (562) 951-4414 if you have any questions.

Attachment
Date

Dear Employee:

You recently added a Domestic Partner (and children of your Domestic Partner) to your benefit plans. At the time of your enrollment, you were advised that adding a domestic partner to your benefits would result in taxable income to you and that the CSU was in the process of determining the value of the benefit for taxation purposes.

The Internal Revenue Service has ruled that the actual cost of the domestic partner benefit is taxable income to you. To arrive at the actual cost of this benefit, the CSU has examined the premium structure for health, vision, and dental benefits. For health and dental, CSU has the following structure:

- Employee only
- Employee plus one dependent
- Employee plus two or more dependents

For these two benefits, the taxable income of the domestic partner benefit will be the cost difference between the employee only and the employee plus one dependent premium rate. This approach recognizes the value of adding one dependent, using a single employee as the base line. The State Controller’s Office will use a flat tax rate of 28% federal, 6% state, 6.2% Social Security, and 1.45% Medicare to withhold taxes on the value of the benefits.

The taxable value of the benefit will be constant as shown in the following examples:

- An employee enrolled in Kaiser for self only at the one-party rate adds his/her domestic partner. The monthly taxable value of the benefit is the two-party premium rate less the one-party premium rate ($368.12 — $184.06 = $184.06). Each month, the employee will have an additional $184.06 in taxable income.
- An employee enrolled for self and family at the three-party rate adds his/her domestic partner. The taxable value of the benefit is still the two-party premium rate less the one-party premium rate ($368.12 — $184.06 = $184.06). Again, each month, the employee will have an additional $184.06 in taxable income.

For vision, the cost is a flat rate, regardless of the number of dependents. Adding domestic partners to the program will have a negligible impact on the premium. As a result, there is no taxable income to you for adding a domestic partner to your vision insurance plan.

**Taxation of Domestic Partner Benefit**

The Controller’s Office will implement a “look back” method for tax withholding on the domestic partner benefit beginning in May 2000. Key points are:
• The Controller’s Office will “look back” at the prior month to determine if an employee has added a domestic partner in that month. The domestic partner taxable income from the prior month will be included in the current month and appropriate taxes will be withheld. For example, the May “look back” will be to April.

• In May, the Controller’s Office will also “look back” and compute outstanding tax liability for Social Security and Medicare for the months of January through March, if applicable. For the May master payroll (paid May 31), the Controller’s Office will withhold applicable Social Security and Medicare monthly taxes for April, plus any prior pay period liability for January through March.

• Federal and state taxes for April will be withheld from the May master payroll warrant. Taxable income from the January-March pay periods will be reported on your year 2000 W-2; however, no taxes will be withheld.

We hope you find this information helpful. If you have any questions, please contact ___________________ at ________________.

Sincerely,

Name of Campus Representative