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Recent Developments Involving Same-Sex Marriage, Civil Unions and Gender Identity Disorder

Individuals who have entered into a same-sex marriage are currently treated less favorably for federal tax purposes than under the laws of many states due to the federal Defense of Marriage Act. However, this issue continues to evolve, as illustrated by recent developments in Congress and the Administration. In addition, with an increasing number of states recognizing civil unions, questions also arise concerning the federal tax treatment of individuals (both same and opposite sex) who have entered into a civil union. The IRS has recently weighed in on this topic. Finally, an issue that has gotten a lot of attention recently is whether treatment for gender identity disorder should be recognized as a medical expense for federal tax purposes. This question was answered in the affirmative by the Tax Court and the IRS has now indicated that it agrees with that decision. Below, we briefly describe these developments, each of which could have a significant impact on the administration of your employee benefit plans.

Senate Committee Acts on "Respect for Marriage Act"

On November 10, 2011, the Senate Judiciary Committee passed the Respect for Marriage Act (S. 598) ("RMA") which was introduced by Senator Dianne Feinstein, a Democrat from California. The RMA repeals the Defense of Marriage Act (DOMA), which was enacted in 1996. The RMA was passed on party lines with all 10 Democrats on the Committee voting for the bill and all 8 Republicans voting against it.

Although U.S. Attorney General Eric Holder has announced that the Department of Justice will no longer defend the constitutionality of DOMA, the law generally continues to be enforced by the Executive Branch, unless Congress repeals it or the law is declared unconstitutional by the Supreme Court.

DOMA provides that with regard to any law enacted by Congress and any guidance or other interpretation of federal law, the word 'marriage' means only a legal union between one man and one woman as husband and wife, and the word 'spouse' refers only to a person of the opposite sex who is a husband or a wife. In addition to repealing DOMA, the RMA affirmatively provides that for purposes of any Federal law in which marital status is a factor, an individual is treated as married if the marriage was valid in the state it was entered into. This means that federal law will recognize same-sex marriages if the state recognizes same-sex marriages.

The action by the Senate Judiciary Committee is only the first step in the legislative process. The RMA must next be passed by the entire Senate, but action by the entire Senate is highly unlikely in 2012, an election year. Although a bill similar to the RMA was introduced in the House, the House leadership will not take any action on the bill in 2012. However, the RMA illustrates that there is currently support within Congress to repeal DOMA and it is possible that, at some point, this effort may be successful.

Federal Tax Filing Status of Opposite-Sex Civil Union Members

In an August 2011 letter that was only recently made public, the IRS gave a surprisingly favorable response to an inquiry by H&R Block on the filing status, for Federal income tax purposes, of parties to an Illinois civil union who are of the opposite sex. The IRS responded that generally the status of individuals of the opposite sex, living in a relationship that Illinois treats as husband and wife, is that of husband and wife for Federal income tax purposes. The IRS cited to the Illinois Religious Freedom Protection and Civil Union Act, 750 Ill. Comp. Stat. 75/20 (2011), which provides that a party to a civil union in Illinois is entitled to the same legal obligations, responsibilities, protections and benefits as are afforded to spouses or recognized by Illinois law. Therefore, the IRS concluded that opposite-sex civil union couples in Illinois may file a joint Federal income tax return.

It is unclear whether the IRS is indicating an official position that opposite-sex civil union couples in any state that currently recognizes civil unions (*i.e.*, Delaware, Hawaii, Illinois, New Jersey and Rhode Island), and treats opposite-sex civil union couples as spouses, should also be allowed to file a joint Federal income tax return. Such a position would be a logical outgrowth of the letter, but the letter itself is not official guidance.

To the extent this letter portends an official IRS position, it could have a significant impact on employee benefit plans. For example, for tax-qualified retirement plans, this could entitle opposite-sex civil union members to spousal beneficiary and distribution rights. And, for health and welfare plans, it could result in employers not being required to impute the cost of employer-provided health coverage to opposite-sex civil union members who are treated as spouses under state law. It is important to note that same-sex civil union couples would not be entitled to these benefits in any case because of DOMA.

IRS Agrees Sex Reassignment Costs Deductible

In Action on Decision 2011-003 (Nov. 4, 2011), the IRS acquiesced in the *O'Donnabhain v. Comm'r* case (134 T.C. 34 (2010)), which held that expenses for hormone therapy and sex reassignment surgery qualify as deductible medical expenses under section 213(d) of the Internal Revenue Code (the "Code"). In *O'Donnabhain*, the Tax Court ruled that the plaintiff was entitled to deduct the costs of medical expenses for hormone therapy and sex reassignment surgery to treat her gender identity disorder disease because these expenses fall within the definition of "medical care" under section 213(d)(1)(A) of the Code.

Before the Tax Court's decision, the IRS had disallowed these deductions on the basis that these expenses did not treat a medically recognized disease or promote the proper function of the body. See CCA 200603025. The Tax Court disagreed with the IRS, primarily for the following four reasons:

- gender identity disorder is widely recognized in diagnostic and psychiatric reference texts,
- the texts and all three experts that testified consider gender identity disorder to be a serious medical condition,
- mental health professionals who examined the taxpayer found that her gender identity disorder was a severe impairment, and
- the Courts of Appeal generally consider gender identity disorder a serious medical condition.

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The IRS's acquiescence means that, where the facts are similar, the Service generally will not challenge medical expenses for hormone therapy and sex reassignment surgery to treat gender identity disorder as deductible under section 213(d) of the Code. Plan sponsors should consider reviewing how their plans treat these claims, to the extent this coverage is provided.

Contact Us

We will continue to monitor these issues, and provide updates as they become available. In the meantime, please contact us for assistance analyzing these or similar issues under your employee benefit plans.

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