



# PAYROLL CURRENTLY

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## Tax Court Says Costs of Sex Change Operation Are Deductible

The U.S. Tax Court, in a case of first impression, has ruled that the costs of gender reassignment surgery (GRS) and hormone therapy were deductible medical expenses under IRC §213 as treatment for gender identity disorder (GID), while the cost of breast augmentation surgery was not [*O'Donnabhain v. Commissioner*, No. 6402-06, 2010 U.S. Tax Ct. LEXIS 4 (2-2-10)]. In a 2005 legal memorandum, the IRS took the position that expenses associated with the treatment of GRS are not deductible (see [PAYROLL CURRENTLY, Issue No. 4, Vol. 14](#)). This case is of interest to payroll professionals because deductible medical expenses for individual income tax purposes under §213 are reimbursable under medical flexible spending arrangements (FSAs) and health reimbursement arrangements (HRAs) or from health savings accounts (HSAs).

### Background

In 1997, Robert Donovan was diagnosed with GID and began treatment under a regimen (the “Benjamin” standards of care) consisting of: (1) use of hormones to effect changes in physical appearance to resemble the opposite sex; (2) living full time publicly as a member of the opposite sex; and (3) GRS.

Donovan continued feminizing hormone therapy through 2001, the taxable year in question. In 2000, he legally changed his name to Rhiannon O'Donnabhain, began living full-time as a female, had the gender designation of his driver's license changed to female, and had surgery to feminize his facial features. After satisfactorily completing the first and second phases of the Benjamin standards, O'Donnabhain had GRS surgery in 2001. She also underwent breast augmentation surgery to make her breasts, which had developed in the course of hormone therapy, look more like the breasts of a genetic female.

O'Donnabhain claimed deductions for medical expenses related to the hormone therapy, GRS, and breast augmentation surgery. The IRS disallowed the deductions and issued a notice of deficiency.

### Definitions

For purposes of IRC §213(d), “medical care” means amounts paid for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body. It does not include “cosmetic surgery,” defined as a procedure intended to improve the patient's appearance that does not meaningfully promote the proper function of the body or treat illness or disease.

### GID as a disease

The Tax Court said that GID is a disease for purposes of §213. The IRS position to the contrary is at odds with nearly 50 years of case law, which treats mental disorders as diseases under §213 without regard to demonstrated organic or physiological origins. The two factors influencing a finding of “disease” in the context of mental conditions are (1) a determination by a mental health professional that the condition creates a significant impairment to normal functioning and warrants treatment, and (2) a listing of the condition in a medical reference text.



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Here, the court noted that GID is listed as a mental disease in the American Psychiatric Association's *Diagnostic and Statistical Manual of Mental Disorders*, which is the primary diagnostic tool of American psychiatry. As three expert witnesses agreed, it is a serious and psychologically debilitating condition. And although O'Donnabhain's diagnosis was made by a social worker with a master's degree in social work, state law authorized a licensed social worker to diagnose and treat psychiatric illness. Moreover, O'Donnabhain's social worker was trained in the diagnosis and treatment of gender-related disorders, and had ruled out other possible conditions in the case.

## **Deductibility of the procedures**

The Tax Court said that while there may be some lingering debate regarding acceptance of the Benjamin standards within the medical profession, "the evidence is clear that a substantial segment of the psychiatric profession has been persuaded of the advisability and efficacy of hormone therapy and [GRS] as treatment for GID, as have many courts." O'Donnabhain was therefore entitled to deduct her expenses in connection with these procedures.

However, the expenses O'Donnabhain incurred for breast augmentation surgery were not deductible under §213. Although such surgery can be a component of treatment for GID, here it did not serve this purpose. O'Donnabhain's hormone therapy had resulted in the development of breasts "within a normal range of appearance," and there was no evidence that she was uncomfortable with them "in the social gender role." The surgery did not promote the proper function of O'Donnabhain's breasts; instead, it merely improved her appearance. Therefore, it was nondeductible cosmetic surgery, the court concluded.