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Fertility and Surrogacy Benefits: What Are the Tax and Legal Implications?

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INTRODUCTION

Offering family-friendly employee benefits is a growing trend and sends an important message of inclusivity and support to an increasingly diverse workforce longing to start a family. However, employers looking to extend coverage or reimbursement for certain fertility benefits through a group health plan must consider the various tax and legal implications in providing such benefits.

More employers are now offering fertility and surrogacy benefits as part of their benefits package as more women delay having children to focus on their careers and more single people and same-sex couples opt to have children. This emerging employee benefit comes at a time when infertility rates among married women have also increased significantly in recent years. According to the Centers for Disease Control and Prevention, about 6% of married women aged 15 to 44 years in the United States are unable to get pregnant after one year of trying. About 12% of women aged 15 to 44 years in the United States have difficulty getting pregnant or carrying a pregnancy to term, regardless of marital status. Although parenting children is central to the identity of many Americans, about one in 10 intended parents experience infertility.[1] These societal trends are the driving force behind the rise in fertility benefits and pregnancy-related benefits offered by employers across industries.

Medical fertility treatment involves various types of Assisted Reproductive Technologies (ARTs), such as *in vitro* fertilization (IVF), intracytoplasmic sperm injection (ICSI), egg donation, and surrogacy. Such treatment can be costly and often is not covered by health insurance.[2] In an effort to recruit and maintain top talent, a growing number of companies in the United States have expanded their health benefits to cover some form of fertility benefit for their employees. Intel Corporation, for example, contributes up to $40,000 for employees' fertility treatments along with another $20,000 for prescription coverage. Couples adopting children are also eligible for up to $15,000 in reimbursement. Parents may take up to eight weeks of paid ''bonding leave,'' while mothers who have given birth may take an additional 13 weeks of paid leave. The Bank of America Corporation provides unlimited IVF coverage, although the company does require an infertility diagnosis. It also provides 16 weeks of paid leave for parents with newborn or adopted children, with an additional 10 weeks of unpaid leave also available.

'MEDICAL CARE' UNDER THE CODE

Section 105(a) provides that amounts received by an employee through an accident or health plan paid by or attributable to the employer are included in the employee's gross income, unless such amounts are expended for medical care under §105(b).[3] Section 213(d)(1)(A) defines the term ''medical care'' to include amounts paid ''for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the

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[1] *See, e.g.*, *How Common is Infertility?*, Eunice Kennedy Shriver Nat'l Inst. of Child Health & Human Dev. (stating 9% of men and 11% of women of ''reproductive age in the United States have experienced fertility problems'').

[2] *See, e.g.*, Valarie Blake, *It's an Art Not a Science: State-Mandated Insurance Coverage of Assisted Reproductive Technologies and Legal Implications for Gay and Unmarried Persons*, 12 Minn. J.L., Sci. & Tech, 651, 659 (2011) (estimating a $10,000 cost of one IVF cycle and a $66,667-$114,286 cost of a ''successful delivery'' via IVF). Egg donation adds an estimated $15,000-$20,000 cost, and surrogacy adds an estimated $50,000-$100,000 cost.

[3] Section 105(b) states that, except for amounts already deducted, gross income does not include amounts paid directly or indirectly to reimburse the employee for expenses incurred for medical care, as defined under §213(d), of the employee, spouse, or dependent. All section references herein are to the Internal Revenue Code of 1986, as amended (the ''Code''), or the Treasury regulations promulgated thereunder, unless otherwise indicated.

body [of the employee, the employee's spouse, or the employee's dependent].''

Expenses Incurred for IUI, IVF, and ICSI

For fertility treatments not involving a third-party, such as intrauterine insemination (IUI), IVF, and ICSI, the diagnosis, treatment, and amelioration of the infertility constitutes ''medical care'' under both the ''disease'' prong and the ''structure or function'' prong of the Code's definition. On the one hand, medical infertility constitutes a ''disease'' in light of the medical workup performed by reproductive care specialists.[4] On the other, the treatment is undertaken for the purpose of conceiving a child, which affects the structure or function of the body of the taxpayer. In general, if the treatment does not involve a third-party sperm donor, egg donor, or gestational surrogate, the expenses of the fertility treatment are indeed ''medical expenses.'' In IRS Pub. 502, the IRS clearly stated that taxpayers can deduct the costs of ''fertility treatments,'' such as IVF, to ''overcome an inability to have children.''

Expenses Incurred for Fertility Treatments Involving Third-Parties

The use of a third-party sperm donor, egg donor, or gestational surrogate adds an additional layer to the tax analysis but does not necessarily exclude the fertility treatment from the Code's definition of ''medical care.'' IUI and IVF involving donor sperm or donor eggs treat the ''disease'' of medical infertility and also affect the structure of function of the body of the taxpayer or the taxpayer's spouse. Such treatment is thus within the Code's definition of ''medical care.''

The next question is whether the payments made to the third-party donor, as opposed to the medical provider, also constitute ''medical care.'' In general, although the medical procedures performed on a donor's body are not performed on the **taxpayer's** body (or the taxpayer's spouse or dependent), the donor medical costs are incurred for the purpose of enabling the taxpayer and the taxpayer's spouse to conceive a child. Accordingly, the costs of the medical procedures performed on the donor are indeed for ''medical care'' of the taxpayer and the taxpayer's spouse. Ancillary donor costs, such as the legal fees and medical fees of the donor, which are necessary to the reproductive care of the taxpayer and the taxpayer's spouse, also likely qualify as ''medical care.'' In PLR 200318017, the IRS allowed a medically infertile different-sex married couple to deduct the direct and ancillary costs of egg donation.[5]

Surrogacy Expenses

Surrogacy costs further complicate the tax analysis. To date, there have been three court decisions addressing the tax consequences of fertility treatment costs — all of which involve unmarried men who claimed medical expense deductions for the costs of ARTs, including IVF, ICSI, egg donation, and surrogacy (there have been no cases involving medically infertile different-sex married couples or single or married women):

- *Magdalin v. Commissioner*, T.C. Memo 2008-293, *aff'd*, No. 09-1153 (1st Cir. Dec. 17, 2009)

The issue in this case was whether the taxpayer—a medically fertile unmarried man—could take a medical expense deduction for expenses incurred for IVF, ICSI, egg donation, and surrogacy. The taxpayer also made a constitutional argument ''that it was his civil right to reproduce, that he should have the freedom to choose the method of reproduction, and that it is sex discrimination to allow women but not men to choose how they will reproduce.'' The IRS denied the taxpayer's deductions on the grounds that: (1) his inability to conceive did not constitute medical infertility; and (2) the treatments did not affect the structure or function of his body, but instead ''affected the structures or functions of the bodies of the unrelated surrogate mothers.'' Siding with the IRS, the court stated that the expenses incurred were not expenses for ''medical care'' because the taxpayer had ''no medical condition or defect, such as, for example, infertility, that required treatment or mitigation through IVF procedures,'' and because the treatments ''did not affect a structure or function of **his** body.'' Notably, the court did not address the issue of whether a medically infertile man could deduct IVF expenses if the procedures were taken to overcome the man's medical infertility. The taxpayer's constitutional argument was also dismissed, as the U.S. Court of Appeals for the First Circuit summar-

[4] *See* §213(d)(1)(A); *Magdalin v. Commissioner*, T.C. Memo 2008-293, *aff'd*, No. 09-1153 (1st Cir. Dec. 17, 2009) (holding that the taxpayer could not deduct his ART costs because he did not have a medical condition, ''such as, for example, infertility, that required treatment or mitigation through IVF procedures'').

[5] The expenses included: ''the donor's fee for her time and expense in following proper procedures to ensure a successful egg retrieval[;] [t]he agency fee for procuring the donor and coordinating the transaction between the donor and recipient; [e]xpenses for medical and psychological testing of the donor prior to the procedure and insurance for any medical or psychological assistance that the donor may require after the procedure[;] [and] [l]egal fees for preparing a contract between [the taxpayers] and the egg donor.'' *See also* IRS Info. Ltr. 2005-0102 (Mar. 29, 2005) (''[f]ertility is a function of the body'' and the costs of fertility treatments aimed at ''overcom[ing] infertility'' satisfy §213. Specifically, the costs of egg or embryo donation to be implanted in the taxpayer's body qualify as ''medical care of the taxpayer.'').

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ily affirmed, and the U.S. Supreme Court denied the petition for a writ of certiorari.[6]

- *Longino v. Commissioner*, T.C. Memo 2013-80, *aff'd*, 593 Fed. Appx. 965 (11th Cir. 2014).

The Tax Court held that an unmarried, heterosexual man could not deduct the expenses he incurred for an IVF procedure to conceive a child with his fiancée. The decision was based on the taxpayer's failure to establish the claim that he suffered from medical infertility. ''As we explained in *Magdalin v. Commissioner*,. . .a taxpayer cannot deduct the IVF expenses of an unrelated person if the taxpayer does not have a defect which prevents him or her from naturally conceiving children. Longino has not proven that he has a defect preventing him from naturally conceiving children. Therefore, he is not entitled to deduct [the expenses he incurred] for his former fiance's [sic] IVF treatments.''

- *Morrissey v. United States*, 226 F. Supp.3d 1338 (M.D. Fla. 2016), *aff'd*, 871 F.3d 1260 (11th Cir. 2017).

An unmarried gay man incurred and paid medical expenses for IVF, ICSI, egg donation, and surrogacy costs in an unsuccessful attempt to have a child with his partner. Although the court acknowledged that the procedures performed on Mr. Morrissey's sperm constituted ''medical care,'' as they affected the structure or function of his body, the court then held that the other fertility treatments (IVF, egg donation, and surrogacy), performed on the bodies of the unrelated female egg donors and gestational surrogate, did not constitute ''medical care.'' Despite the court's concession that Mr. Morrissey is a gay man who is ''effectively infertile,'' and that the treatments were ''necessary'' for Mr. Morrissey to reproduce, it nonetheless held that the non-deductible treatments did not affect the structure or function of Mr. Morrissey's body.

Surrogacy expenses, including egg donation and freezing that is unrelated to infertility and not involving the structure or function of the taxpayer's body, likely are not deductible under §213(d). Similarly, coverage of a surrogate mother who is not eligible to participate under a plan would not be eligible for the medical care exclusion from gross income and therefore should be treated as taxable. This is not to say that a group health plan could not be designed to cover certain surrogacy expenses. Rather, it means the benefits themselves should be taxable and the group health plan should be administered to ensure the proper taxation and reporting of both the costs of coverage and the costs of the benefits provided under the group health plan.

[6] *Aff'd*, No. 09-1153 (1st Cir. 2009), *cert. denied*, 559 U.S. 1093 (2010).

LEGAL IMPLICATIONS OF SURROGACY BENEFITS

Commercial gestational surrogacy refers to a surrogacy arrangement in which the surrogate mother is compensated for her services **beyond** reimbursement of medical expenses. New York, Louisiana, and Michigan currently prohibit by statute such arrangements, but the remaining states either have laws that explicitly make commercial surrogacy contracts legal or have no laws at all, which implies such contracts are implicitly allowed.

Surrogacy Arrangements in New York

Under current New York state law, surrogate parenting contracts are contrary to public policy and are void and unenforceable.[7] Surrogate parenting contracts are any agreements, whether oral or written, in which: (1) a woman agrees either to be inseminated with the sperm of a man who is not her husband or to be impregnated with any embryo that is the product of an ovum fertilized with the sperm of a man that is not her husband; and (2) the woman agrees to, or intends to, surrender or consent to the adoption of the child born as a result of such insemination or impregnation.[8] New York law also prohibits the payment of a fee, compensation, or other remuneration in connection with any surrogate parenting contract except for payments in connection with adoption of a child or payments for reasonable and actual medical fees and hospital expenses for artificial insemination or IVF.[9] Violation of this restriction can result in a civil penalty of up to $500. Individuals who assist in arranging the contract are liable for a civil penalty up to $10,000 and must forfeit any fees, compensation, or remuneration received for brokering the contract. A subsequent violation of the restriction on arrangement of contracts constitutes a felony.

New York's current surrogacy law was passed as a result of the infamous *Baby M* case, where the birth mother, Mary Beth Whitehead, entered into a ''traditional'' surrogacy agreement with William and Elizabeth Stern in which William provided the sperm and Whitehead provided the egg and the womb.[10] Whitehead and the Sterns agreed that the Sterns would be the child's parents in exchange for a payment of $10,000. However, after the birth Whitehead wanted to retain parental rights to the child. Ultimately, the New Jersey Supreme Court determined that compensated surrogacy agreements were unenforceable as against public policy and granted the Sterns legal and physical custody and Whitehead visitation rights.

Due to changes in technology increasing the use of ''gestational surrogacy''[11] as opposed to ''traditional

[7] N.Y. Dom. Rel. Law §122.

[8] N.Y. Dom. Rel. Law §121.

[9] N.Y. Dom. Rel. Law §123.

[10] *In re Baby M*, 537 A.2d 1227 (N.J. 1988).

[11] ''Gestational surrogacy'' is when a woman carries a baby for

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surrogacy,''[12] there has been a push to change the current New York surrogacy law. The proposed Child-Parent Security Act (CPSA) attempts to lift the restrictions imposed under current New York law regarding gestational carrier arrangements. The law would allow for surrogacy agreements and compensation in New York and create a system in which the intended parents may obtain an ''order of parentage'' from the court prior to the child's birth.[13] The gestational agreement must be signed and compensation placed in an escrow fund before any medical procedures commence. The law goes into detail regarding termination of the agreement after execution and prior to pregnancy, reimbursements for expenses as allowed under the agreement, and the retention of payments that have been paid and/or to which the surrogate is entitled under the agreement.

The CPSA would also allow compensation to the gestational carrier for services that are rendered, expenses or medical risks that have been or will be incurred, time, and inconvenience. Compensation is defined as payment of any valuable consideration for time, effort, pain, and/or risk to health in excess of reasonable medical and ancillary costs. Compensation is limited to the duration of the pregnancy and eight weeks after birth. The law, however, does not allow compensation to purchase sperm, eggs, or embryos, or to pay for relinquishment of parental rights. Also, the compensation should not include payment based on the quality of the sperm, eggs, embryos, or genetic information.

For decades, those opposing the CPSA have prevented surrogate parenting contracts from becoming legal. Currently, New York is on the verge of changing its policy, with Governor Andrew Cuomo publicly declaring his support for the CPSA. Until then, however, individuals in New York must abide by current surrogacy laws that make surrogate parenting contracts unenforceable and limit compensation to the adoption of the child or payments for reasonable and actual medical fees and hospital expenses for artificial insemination or IVF.

Surrogacy Under Other State Laws

In addition to New York, Louisiana and Michigan currently restrict or limit compensation to surrogates as against public policy. These states impose criminal penalties for surrogacy compensation and/or limit surrogacy to heterosexual married couples.

There are also states that have specific legislation that supports surrogacy, notably California, Connecticut, Washington, D.C., Oregon, and Rhode Island, to name a few. Finally, there are states that have restrictions and complications in surrogacy arrangements imposed by statute or applicable case law, including Arizona, Texas, and North Carolina. These laws can apply different rules to traditional surrogacy arrangements or gestational surrogacy arrangements.

The complexity of state law may make a surrogacy assistance program very difficult to administer. Employees of certain states would not be able to participate, and expenses related to employees in other states would need to be reviewed based on, among other things, marital status, whether the parents are heterosexual or same-sex couples, the types of expenses to be reimbursed, and parental adoption rules.

an intended parent and has no genetic relationship to the child that she is carrying.

[12] ''Traditional surrogacy'' is when the surrogate mother uses her own eggs and either the sperm of the intended father or donor to create the child she is carrying for the intended parent(s).

[13] Part 4 of the CPSA allows gestational carrier agreements and requires that a gestational carrier must: (1) be at least 21 years old; (2) have undergone a medical evaluation; (3) have independent legal counsel; and (4) have health insurance that covers major medical treatments and hospitalization for the duration of the pregnancy and eight weeks after the birth of the child.

Statute or case law currently prohibits or extremely limits gestational surrogacy contracts, or a birth certificate naming both parents cannot be obtained.	Louisiana, Michigan, New York
Gestational surrogacy contracts currently are permitted, pre-birth orders are granted throughout the state, and both parents will be named on the birth certificate.	California, Connecticut, Washington, D.C., Delaware, Maine, New Hampshire, New Jersey, Nevada, Rhode Island, Vermont, Washington
Commercial surrogacy currently is permitted but results may be dependent on various factors and/or venue. In some states additional post-birth legal procedures may be required.	Alabama, Alaska, Arkansas, Colorado, Florida, Georgia, Hawaii, Illinois, Kansas, Kentucky, Massachusetts, Maryland, Minnesota, Missouri, Mississippi, Montana, North Carolina, North Dakota, New Mexico, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota, Texas, Utah, Wisconsin, West Virginia

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CONCLUSION

Despite technological advances that have allowed an increase in the use of medical fertility and surrogacy treatment and legal changes recognizing same-sex or LGBT relationships, the laws currently in place still make it difficult for an employer-sponsored group health plan or reimbursement plan to provide for certain fertility benefits. Unless it can be shown that the expenses qualify as medical care for the participant, his or her spouse, or dependent, it will not be possible for an employer to provide such benefits on a tax-favored basis. Also, under New York law, because compensation for gestational surrogacy is specifically prohibited (other than for certain adoption fees or medical fees and hospital expenses), providing for surrogacy benefits under an employer plan may inadvertently cause the employer or plan to violate New York law or similar state laws. In general, an employer should be careful how fertility and surrogacy benefits are provided under a group health plan, ensuring that those benefits are properly taxed and imposing restrictions and limitations on employees in different states to comply with applicable state laws.

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