M E M O R A N D U M

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To: NACA Membership
Date: June 4, 2014
Subject: Taxation of Attorney's Fees in Consumer Lawsuits

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This memo summarizes my preliminary research on the tax treatment of attorney's fees in consumer lawsuits. The memo (i) provides a conceptual framework of the important income tax principles that the Internal Revenue Service (the "IRS") believes govern taxation of recoveries and attorney's fees in consumer lawsuits; (ii) assesses alternative theories for conceptualizing attorney's fees that have been proposed by others; and (iii) offers some preliminary thoughts on avenues we should consider pursuing in order to change the current tax treatment of attorney's fees.

I. Basic Income Tax Principles

The Sixteenth Amendment, the Internal Revenue Code (the "Code"), and the Treasury Regulations cast a wide net for what income the government *may* tax. The basic rule is that the government has a right to tax "*all income* from whatever source derived, *unless excluded by law*."[1] Given this definition, there are two critical questions in determining taxable income: (1) What is the definition of "income" for tax purposes? (2) What does the law exclude from this definition that would otherwise be included?

The answer to the first question is that taxpayers' "income" includes all "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion."[2] Such income may be "realized in any form, whether in money, property, or services."[3]

One of the seminal Supreme Court cases dealing with the definition of "income" for tax purposes held that litigated recoveries fall into this category and rejected the argument that they constitute

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[1] Treas. Reg. § 1.61-1(a) (emphasis added).
[2] *Comm'r v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955).
[3] Treas. Reg. § 1.61-1(a).

"windfalls" rather than "income." In explaining its rationale, the Court noted that "Congress applied no limitations as to the source of taxable receipts, nor restrictive labels as to their nature. And the Court has given a liberal construction to this broad phraseology in recognition of the intention of Congress to tax all gains except those specifically exempted."[4]

Thus, under this definition, judgments and settlements are "income" for tax purposes. However, they may not be taxable depending on the answer to our second question: What does the law exclude from "income" that would otherwise be included?

The Code contains a labyrinth of rules answering this question. For our purposes, there are two primary ways that all or part of a settlement or judgment may be excluded from a plaintiff's taxable income: (1) statutory or regulatory exclusion from the definition of gross income and (2) deduction.

Congress has statutorily excluded from the definition of "income" "the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness."[5] While components of recoveries in some consumer lawsuits may fall into this category, many do not. The most relevant limitation for consumer recoveries is the Treasury Regulations' provision that "[e]motional distress is not considered a physical injury or physical sickness."[6]

The only other option for excluding part of such settlements from a plaintiff's taxable income is "deduction." Deductions are amounts that may be subtracted from taxpayers' total income when calculating how much of that income should actually be taxed. There are three types of deductions that could apply to a portion of a litigated recovery:

1. *Trade or Business Expenses.* Taxpayers may deduct the full amount of any trade or business expense from their taxable income.[7] While such expenses include the cost of hiring an attorney, few consumer lawsuits would be considered part of the plaintiff's trade or business. The requirements for constituting a trade or business are strict, and the Supreme Court has held that "the origin and character of the claim with respect to which an expense was incurred, rather than its potential consequences upon the fortunes of the taxpayer, is the controlling basic test of whether the expense was 'business' or 'personal.'"[8] Thus, barring some exceptional circumstances, most plaintiffs in consumer lawsuits may not deduct their attorney's fees from income as trade or business expenses.

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[4] *Comm'r v. Glenshaw Glass Co.*, 348 U.S. 426, 429-30 (1955).
[5] I.R.C. § 104(a).
[6] Treas. Reg. § 1.104-1(c)(1).
[7] I.R.C. § 62(a)(1).
[8] *U.S. v. Gilmore*, 372 US 39, 49 (1963).

2. *Attorney's Fees in Discrimination Lawsuits*. Taxpayers may deduct the full amount of their attorney's fees incurred in litigating discrimination, civil rights, employment, and whistleblower lawsuits from their taxable income.[9] Unless a consumer lawsuit also falls into one of these categories, this deduction would not apply.

3. *Expenses for the Production of Income*. Taxpayers may deduct expenses incurred for the production or collection of income from their taxable income.[10] This is a broad deduction that includes all attorney's fees in consumer lawsuits because they are incurred by the plaintiff in order to collect income.

Unfortunately, the third type of deduction is not as helpful to plaintiffs as the first two. While the first two are "above the line" deductions, the third is an "itemized below the line" deduction. There are a number of significant disadvantages to this type of deduction:

1. *Alternative Minimum Tax.* A taxpayer may subtract an itemized below the line deduction when computing taxable income under normal circumstances. However, the deduction may not be applied for purposes of calculating the Alternative Minimum Tax ("AMT").[11] The AMT is a tax applied concurrent with the regular income tax of individuals with incomes above certain specified thresholds. Accordingly, if a plaintiff's pre-recovery income is in the AMT range or if the recovery puts the plaintiff in that range, attorney's fees may not be deductible at all for purposes of calculating the AMT.

2. *Loss of Deductions and Credits*. Eligibility for and the amount of many other deductions[12] and credits[13] depend on a taxpayer's income before subtracting itemized below the line deductions. Thus, a taxpayer may lose eligibility for or entitlement to the full amount of certain deductions or credits if the attorney's fees portion of a recovery is significant.

3. *Floor*. Taxpayers may only take this itemized below the line deduction if its amount, together with all other itemized below the line deductions, exceeds 2% of their total income, with specified modifications.[14] In most situations, this means that at least 2% of attorney's fees will not be deductible at all.

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[9] I.R.C. § 62(a)(20).
[10] I.R.C. § 212.
[11] I.R.C. § 56(b)(1).
[12] *See*, *e.g.*, I.R.C. § 213(a) (deduction of medical expenses); I.R.C. § 221(b) (deduction for student loan interest); I.R.C. § 222(b) (deduction of tuition and education fees).
[13] *See*, *e.g.*, I.R.C. § 21(a) (credit for child and dependent care expenses); I.R.C. § 22(d) (credit for the elderly or disabled); I.R.C. § 25A(d) (Hope and Lifetime Learning credits); I.R.C. § 32(a) (Earned Income Tax Credit).
[14] I.R.C. § 67.

4. *Cap*. If a plaintiff's total amount of itemized below the line deductions exceeds a specified threshold, the allowable deduction is reduced based on a statutory formula.[15] For large recoveries, this reduction could significantly curtail the amount of attorney's fees that may be deducted.

The consequences of this analysis to plaintiffs in consumer lawsuits are quite severe. Absent alternative theories for conceptualizing attorney's fees, there are many limitations on their deductibility both for regular income tax and AMT purposes. Accordingly, many plaintiffs may incur tax liabilities that greatly diminish, and possibly exceed, their recoveries, once they have paid their attorney's fees.

The IRS has acknowledged that there are negative consequences to plaintiffs based on these rules. However, the IRS's position has been that the only way to correct this situation is legislative change (e.g., Congress adding an above the line deduction for all attorney's fees, not just those incurred in discrimination, civil rights, employment, and whistleblower lawsuits). Absent such change, the IRS believes it is bound to carry out the rules of income taxation as Congress enacted them, whether fair or not.[16]

II. Alternative Theories

Due to its impact on plaintiffs, the tax treatment of attorney's fees has long been disputed. As early as 1959, the Fifth Circuit was already addressing arguments that the taxation of attorney's fees should be different than that outlined above.[17] My research has shown three primary theories that taxpayers have used: (a) they are the attorney's income, not the plaintiff's; (b) they are the income of a partnership between the plaintiff and the attorney, not of either in an individual capacity; and (c) they should be treated as transaction costs, fully excludable from income, rather than deductions.[18] This section explains these theories, analyzes the IRS's view of them, and discusses their successes and failures in courts.

A. Attorney's Fees as the Attorney's Income

For over half a century, plaintiffs have argued, and the IRS has contested, the proposition that attorney's fees should be treated as their attorneys' income rather than their own. The argument

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[15] I.R.C. § 68.
[16] *See* Reply Brief for Petitioner at 17-19 *Banks* 543 U.S. 426 (2005) (Nos.03-892 and 03-907).
[17] *See Cotnam v. Comm'r*, 263 F.2d 119 (5th Cir. 1959).
[18] These theories were proposed in articles and lower courts long before the landmark Supreme Court decision in *Banks*, but were brought front and center in that case.

has generally gone as follows: Various states grant attorneys a legal interest in their fees under local law ("attorney's liens"). These liens create a property interest in the fees that effectively abrogates the plaintiff's right to such income. Accordingly, the attorney, rather than the plaintiff, has the real right to the income and should be taxed accordingly.

The IRS sees things differently. According to the IRS, any right an attorney has to attorney's fees is the product of a contract between the plaintiff and the attorney (e.g., retainer, contingency-fee agreement). Attorney's liens are merely the state's attempt to protect a specific type of contractual arrangement. However, the existence of the contract presumes that plaintiffs have the original right to the portion of the settlement or judgment that they then designate to their attorneys.

The fact that plaintiffs hold the original right to the entire amount of any litigated recovery is the critical factor in the IRS's analysis. There is a fundamental, judicially-created rule in tax law that says that a person who earns income cannot shift that income to someone else by contract or other means.[19] This rule is generally referred to as the "assignment of income doctrine." The purpose of this rule is to prevent taxpayers from assigning all or portions of their income to other taxpayers who would be taxed at lower rates or not at all. Accordingly, the IRS views it as a bedrock of its mission to prohibit tax avoidance.

Under the assignment of income doctrine, the only way to effectively transfer income is to convey the asset that produces the income. The classic metaphor is that of a tree (the asset) and its fruit (the income). For example, if a taxpayer owns a building, she cannot validly assign rents (the fruit) to another taxpayer unless she conveys the entire building (the tree) or part thereof (a branch, to continue the metaphor). In the case of attorney's fees, the IRS appears to believe that the income generating asset is the legal claim (the chose in action) itself. Accordingly, an assignment of the right to a portion of the income from the lawsuit (the fruit) is not an effective assignment.

Both sides have strong legal arguments supporting them, which led to a split in the circuits. The Fifth,[20] Sixth,[21] and Eleventh[22] circuits adopted the plaintiff-friendly interpretation, while the Third,[23] Fourth,[24] Seventh,[25] Ninth,[26] Tenth,[27] and Federal[28] circuits sided with the IRS. In the infamous 2005 *Banks* decision, the Supreme Court ended the controversy, affirming the IRS's view.

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[19] *See Lucas v. Earl*, 281 U.S. 111 (1930); *Helvering v. Horst*, 311 U.S. 112 (1940).
[20] *Cotnam v. Comm'r*, 263 F.2d 119 (5th Cir. 1959); *Srivastava v. Comm'r*, 220 F.3d 353 (5th Cir. 2000).
[21] *Estate of Clarks ex rel. Brisco-Whitter v. United States*, 202 F.3d 854 (6th Cir. 2000).
[22] *Foster v. United States*, 249 F.3d 1275 (11th Cir. 2001).
[23] *O'Brien v. Comm'r*, 38 T.C. 707 (1962), aff'd, 319 F.2d 532 (3rd Cir. 1963).
[24] *Young v. Comm'r*, 240 F.3d 369 (4th Cir. 2001).
[25] *Kenseth v. Comm'r*, 259 F.3d 881 (7th Cir. 2001).
[26] *Coady v. Comm'r*, 213 F.3d 1187 (9th Cir. 2000); *Benci-Woodward v. Comm'r*, 219 F.3d 941 (9th Cir. 2000).
[27] *Campbell v. Comm'r*, 274 F.3d 1312 (10th Cir. 2001).
[28] *Baylin v. United States*, 43 F.3d 1451 (Fed. Cir. 1995).

Importantly, the Court noted that its decision does not control the tax treatment of attorney's fees awarded under fee-shifting statutes. The conceptual reason for treating fee-shifting statutes differently is that they, arguably, transfer the proverbial tree to the attorney because the law itself, rather than contract, conveys the fees to the attorney.

The IRS still contends that this theory doesn't work even in cases of fee-shifting statutes for a number of reasons. First, in settlements, which constitute a majority of payments under lawsuits initiated under fee-shifting statutes, it is the contingency-fee agreement, rather than the statute, that entitles the attorney to a share of the award.[29] Second, even when attorney's fees are awarded by the court under fee-shifting statutes, they are awarded to the plaintiff rather than the attorney; plaintiffs then pay their attorneys that amount because of the contracts between them (e.g., retainer, contingency-fee agreement), not because the statute itself requires them to do so.

The IRS believes that its position applies even if attorney's fees are paid by the defendant directly to the plaintiff's attorney. The IRS's rationale is that, as mentioned above, the attorney's right to any payment is the product of contract between the attorney and the plaintiff; the fee-shifting statute itself merely entitles the plaintiff to the specified payment. When the defendant pays the plaintiff's attorney, it is effectively paying the plaintiff's contractual debt to his attorney for him. This benefit creates income to the plaintiff based on another important income tax principle that taxpayers' income includes debts paid on their behalf.[30]

Since *Banks*, a number of plaintiffs have litigated this issue in the Tax Court. In all such cases brought thus far, the Tax Court has sided with the IRS.[31] It is possible that an appeals court may overturn the Tax Court's position in the future, but it is clear where the IRS stands.

Thus far, the only flexibility the IRS has shown in its position has been its issuance of a private letter ruling ("PLR") issued to a taxpayer in 2010.[32] A PLR is a private ruling issued to an individual taxpayer telling that taxpayer, and that taxpayer only, how the IRS will treat its particular circumstances. The Code states explicitly that PLRs may not be cited as precedent,[33] and the IRS has stated in memos that its attorneys may contradict positions founds in PLRs.[34] In this particular 2010 PLR, the IRS told a plaintiff that attorney's fees awarded and paid directly to its pro bono counsel would not constitute income of the plaintiff.

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[29] This position was embraced by the Supreme Court in *Banks*.
[30] *See Old Colony Trust Co v. Comm'r*, 279 U.S. 716 (1929).
[31] *Vincent v. Comm'r*, T.C. Memo 2005-95; *Green v. Comm'r*, T.C. Memo 2007-39, aff'd 312 Fed.Appx. 929 (9th Cir. 2009); *Sanford v. Comm'r*, T.C. Memo 2008-158.
[32] *See* I.R.S. Priv. Ltr. Rul. 201015016, (April 16, 2010).
[33] I.R.C. § 6110(k).
[34] *See*, *e.g.*, I.R.S. Chief Counsel Notice 2002-043 (October 17, 2002).

On its face, the PLR looks like the IRS may be internally reconsidering its position. On closer review, however, the unique facts of the PLR allowed the IRS to rule as it did while remaining firmly committed to its generally strict approach. First, there was no contingency-fee agreement or other obligation on the plaintiff's part to pay the attorney under any circumstances, obviating any concern about payment of a debt on the plaintiff's behalf. Second, the attorney's fees were awarded by judgment, rather than settlement, obviating any concern that the attorney's right to the fees arose through contract rather than law. Accordingly, it is likely that the PLR was more of a reflection of the IRS's analysis of a peculiar set of facts than a rethinking of its position.

B. Attorney's Fees as Income of a Partnership between Plaintiff and Attorney

Under Federal income tax law, partnerships themselves do not pay tax. Rather, the partnership calculates its income and then allocates that income to its partners according to their percentage interests in the partnership. In the case of attorney's fees, one could argue that contingency fee agreements, retainers, or other agreements between plaintiffs and attorneys create partnerships between attorneys and plaintiffs in which the attorneys contribute their services and pay for legal expenses and plaintiffs contribute their legal claims and participation in the lawsuit. Under this theory, the partnership would be the recipient of the full amount of any settlement or judgment. It would then allocate that amount between the attorney and the plaintiff according to their percentage interests in the partnership, which would track the arrangements in the the agreement between the plaintiff and attorney.

This theory has been endorsed primarily by Robert W. Wood who has written many articles advocating its use.[35] Its most prominent use, however, was by one of the plaintiffs in the *Banks* case, Sigitas J. Banaitis, who argued in his brief that the attorney's fees were earned by a partnership between him and his attorney, rather than either in his individual capacity.

The IRS rejected this theory on a number of grounds. Most importantly, it argued that there was not a true partnership between the plaintiff and his attorney. The fact that the plaintiff retains the power to fire the attorney and to settle the case demonstrates that the plaintiff is the true owner of the legal claim. Additionally, the IRS argued that the plaintiff did not demonstrate enough of the indicia of a partnership for tax purposes, a somewhat amorphous list that is the product of regulation and judicial decisions.[36]

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[35] *See*, *e.g.*, Robert W. Wood, *Attorney-Client Partnerships with a Straight Face*, 129 Tax Notes 3 (October 18, 2010).
[36] *See* Reply Brief for Petitioner at 2-6 *Banks* 543 U.S. 426 (2005) (Nos.03-892 and 03-907).

While not fully rejecting the plausibility of this theory, the Supreme Court noted that it did not consider the relationship between a plaintiff and its attorney to be a partnership for tax purposes. The Court emphasized that the relationship was one of agency rather than partnership and agreed with the IRS that the plaintiff retains too much control to suggest the existence of a partnership.

There are other reasons this theory was only used by Mr. Banaitis as a last ditch effort in the Supreme Court and has not been used by plaintiffs at the trial court level. Proper tax filing for partnerships is extremely complex and includes many forms, bookkeeping, and special tax returns. There are fines for failure to comply with these rules in addition to noncompliance possibly demonstrating the lack of a partnership. Furthermore, there are non-tax concerns about a partnership between a plaintiff and attorney causing the plaintiff to be engaged in the unlicensed practice of law or the attorney sharing business with a non-lawyer. Thus, while the partnership theory may have some merit and has not been fully rejected by the Court, it would very likely create more problems than it would solve, even if accepted by a court.

C. Attorney's Fees as Transaction Costs

The last theory argues that attorney's fees should be treated as transaction costs rather than deductible expenses. If correct, the amount would, in most cases, be fully excludable from the plaintiff's income. To understand this distinction, some background is in order.

All theories reviewed up to this point (both those of the IRS and those countered by plaintiffs) suppose that the underlying legal claim produces income through settlement or judgment. The ownership, rather than the nature, of this claim is of utmost importance. The theory discussed in this section changes the emphasis and argues that the nature of the claim is critical. Under this view, the claim is a type of asset that is effectively disposed of if the defendant settles or if the court orders a judgment.

In general, when an asset is disposed of, the costs associated with the selling may be excluded from any gain realized on the disposition as transaction costs. The Code states that transaction costs may not be deducted[37] and the Supreme Court has held that such costs should instead be excluded from income.[38]

This theory was presented by Prof. Charles Davenport in an Amicus Brief in the *Banks* case.[39] The IRS did not respond in its own brief because the issue was not raised by the taxpayers.

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[37] *See* I.R.C. § 263.
[38] *Helvering v. Union Pacific,* 293 U.S. 282 (1934); *Spreckels v. Comm'r,* 315 U.S. 626 (1942).
[39] *See* Brief for *Amicus Curiae* Professor Charles Davenport in Support of Respondents *Banks* 543 U.S. 426 (2005) (Nos.03-892 and 03-907).

However, the Court expressed a great deal of interest and openness to this theory in oral arguments. In response to the Court's questions, the government insisted that the legal claim is never actually transferred to the defendant. Accordingly, there is no disposition of an asset and the rules for transaction costs do not apply.[40]

In *Banks*, the Court declined to rule on this theory. I have not found any cases in which it has been litigated since *Banks*, and it remains an alternative theory that could be argued in the future.

III. Possible Avenues for the NACA Tax Initiative

In pursuing its goal of changing the tax treatment of attorney's fees in consumer lawsuits, the NACA Tax Initiative must develop an action plan that fully considers the IRS's concerns and positions. The analysis above demonstrates the following primary concerns motivating the IRS's approach:

- All proceeds from a legal claim are the income of whoever has control over the legal claim at the time the payment is made. Control includes the right to settle or change representation.

- As long as a plaintiff has an obligation to pay his attorney, any payment made by the defendant to the attorney is treated as income to the plaintiff because it satisfies a debt that the plaintiff owes the attorney. Obligations are not limited to hourly fees. They include contingency agreements as well, even if the obligation to pay is conditioned upon success.

- While the current tax treatment may yield perverse results, Congress is the only entity that can change it.

- There is no partnership between a plaintiff and her attorney.

- Settlements and judgments do not constitute dispositions of legal claims.

Based on the above considerations, I believe there are five primary options that the NACA Tax Initiative should consider: (a) alternative client-attorney arrangements that address the IRS's concerns; (b) litigation; (c) legislative change; (d) regulatory change by the Treasury Department and IRS; and (e) seeking a ruling from the IRS for a particular set of circumstances that would be relevant to other plaintiffs. Each of these considerations is discussed below.

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[40] Transcript of Oral Argument at 13, *Banks*, 543 U.S. 426 (No. 03-907).

A. Alternative Client-Attorney Arrangements

One approach to changing the tax treatment of attorney's fees is to change the way in which they are earned by attorneys. Rethinking the traditional contingency-fee agreement in innovative ways may cause the IRS's concerns to be irrelevant. I believe there are two primary options to consider:

1. *Assignment of Claim to Attorney's Fees*. One option for addressing the IRS's concerns may be to replace the traditional contingency-fee agreement with an assignment of the plaintiff's right to attorney's fees under the relevant statute to the attorney. This assignment would be the attorney's entire compensation for representation. Following the tree-fruit metaphor discussed above, such an assignment would effectively convey a branch of the tree to the attorney. The attorney would have full control over that portion of the claim, including the right to settle or litigate, and the client would not owe any other amount to the attorney, obviating any concern about a debt being paid on the plaintiff's behalf.

2. *Assignment of Entire Claim to Attorney or Third Party for Contingent Price*. Another option is for the client to assign the entire legal claim to an attorney or a third-party intermediary for a contingent price. Such an assignment would effectively make the attorney or third party the plaintiff in the lawsuit. If there is a recovery, the attorney or third party would pay the "client" the contingent price specified in the assignment contract. This amount, however, would be fully deductible to the attorney or third party as a trade or business expense, a deduction unavailable to the plaintiff under a traditional contingency-fee agreement.

In addition to the tax implications of both options that need to be further explored, there are many non-tax issues that need to be assessed. To name a few: Can the fee-shifting claim be severed from the rest of the claim under all relevant statutes (e.g., FDCPA, FCRA)? Under what circumstances would potential "clients" need to be represented by separate counsel when effectively selling their claims, or part thereof, to attorneys? Would these arrangements violate state laws regarding barratry, champerty, and maintenance?

B. Litigation

Although the Tax Court has consistently sided with the IRS regarding the tax treatment of attorney's fees under fee-shifting statutes, there is reason to consider the prospect of litigation. First, it is possible that a district court, especially one with a jury, may be more sympathetic to a pro-taxpayer argument. Second, there are still a number of theories that have not been fully litigated post-*Banks*. In descending order of likelihood, I believe the following three theories have a chance of success:

1. *Attorney's Fees as Transaction Costs.* As described more fully above, Prof. Davenport's theory that attorney's fees should be treated as transaction costs has not been seriously tested in court. While it is a somewhat drastic reconceptualization of attorney's fees, the Supreme Court appeared receptive to it in oral argument in *Banks*.

2. *Fee-Shifting Statutes as Different.* Although the Tax Court has held that attorney's fees awarded under fee-shifting statutes are no different than those paid in other lawsuits, it is unclear whether the Tax Court or another court would be sympathetic to such an argument if the facts were better and the arguments more refined. The main challenge to such an approach would be proving that even attorney's fees paid out of settlements are not paid to satisfy a debt of the plaintiff.

3. *Takings Clause*. Another theory is to argue that, although the government may have a right to tax attorney's fees under the Sixteenth Amendment's broad definition of income, taxing such income is a "taking" under the Fifth Amendment and requires compensation of the amount taken (i.e., a dollar-for-dollar refund). There is a long line of jurisprudence that is dismissive of arguments that the the Fifth Amendment's "takings clause" could limit the Sixteenth Amendment's grant to tax income, but a recent Supreme Court decision may have opened the door to this argument.[41]

Litigating a case would involve a number of steps, including selecting a plaintiff, picking the correct venue (Tax Court or district court), and choosing counsel. This path could, and probably should, be pursued in conjunction with others.

C. Legislative Change

Congress could solve this entire issue by amending the Code to make all attorney's fees in consumer deductible above the line. Interestingly, two such bills were introduced in the Senate (one in 2007[42] and the other in 2009[43]) but both appear to have died in the Finance Committee. While the current deadlock in Congress leaves little hope for a legislative solution to this problem, this option should be pursued as fully as possible together with other approaches. In addition to traditional modes of lobbying, a compelling story published in a major publication could help draw attention to this issue.[44]

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[41] *See Koontz v. St. Johns Water Mgmt. Dist.,* 133 S.Ct. 2586 (2013) (Kagan, J., dissenting).
[42] S. 813, 110th Cong. (2007).
[43] S. 440, 111th Cong. (2009).
[44] For example, an article about the adverse tax consequences in discrimination lawsuits was published in *The New York Times* two years before Congress statutorily excluded attorney's fees in such cases from gross income. *See* Adam Liptak, *Tax Bill Exceeds Award To Officer in Sex Bias Suit*, N.Y. TIMES, Aug. 11, 2002, at A12.

D. Regulatory Change from the Treasury Department

Although the IRS has been adamant in its position against the deductibility of attorney's fees, the Treasury Department, the parent agency of the IRS, may be open to working with the IRS to issue regulations changing the tax treatment of attorney's fees in cases brought under fee-shifting statutes. Conversations with the Treasury Department and IRS asking for regulatory change should emphasize the fact that the current tax treatment of attorney's fees undermines Congress' goal of deputizing private attorneys general in consumer lawsuits, and therefore cannot possibly reflect Congress' intent. While this avenue will likely meet many challenges, it should be pursued in conjunction with others.

E. IRS Ruling

The final option that we may consider is seeking a private letter ruling from the IRS. As mentioned earlier, PLRs may not be cited as precedent, and therefore have no legal weight for any taxpayer other than that to which the PLR is directed. Instead, their value lies in the fact that they offer insight into the IRS National Office's views on a particular set of circumstances. One use of a PLR may be to seek the IRS's endorsement of a reworked client-attorney arrangement.

IV. Conclusion

The tax treatment of attorney's fees in consumer lawsuits presents a significant challenge to plaintiffs. The IRS has remained very resistant to changing its position, but the approaches discussed above may offer solutions that either obviate the IRS's concerns, challenge them, or change the legal framework in which they operate. Pursuing these avenues together can create synergies that will hopefully expedite substantive change. I encourage NACA's members to offer any comments or suggestions that they have.