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Laura A. Quigley

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REPARATION RIGHTS TAX RELIEF RESTORES HUMAN RIGHTS AS A CIVIL RIGHT IN TAX TORT REFORM

Professor Laura A. Quigley*†

"[D]amages that aim to substitute for a victim's physical or personal well-being-[are] personal assets that the Government does not tax and would not have taxed had the victim not lost them."¹

I. INTRODUCTION

A. *The 1996 Act Makes Nonphysical Personal Injury, Such as Discrimination Cases, Taxable*

The Small Business Job Protection Act of 1996 ("1996 Act") made damages from discrimination cases taxable, including recoveries for emotional distress.² This particular result arose from Congress's effort to raise revenue that would offset the provisions to increase the minimum wage³ and reversed the tax doctrines that the Supreme Court, the Treasury Department, and Congress itself had established from 1918–1996. Even as he signed the 1996 Act into law, President Clinton noted his reservations about the revenue offset provision in a comment that summarizes the heart of the problem: "Such damages are paid to compensate for injury, whether physical or not, and are designed to make victims whole, not to enrich them. These damages should not be considered a source of taxable income."⁴

* Visiting Assistant Professor of Law: Barry University Dwayne O. Andreas School of Law, Orlando, FL (8/04–8/05); Paralegal Program Director/Professor Florida Metropolitan University-South Campus, Orlando, FL; M.L.T. (L.L.M. Tax) Georgetown University Law Center, 1981; J.D. William & Mary, Marshall-Wythe School of Law, 1975; B.A. Economics, College of William & Mary, 1972.

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¹ O'Gilvie v. United States, 519 U.S. 79, 86 (1996).

² Pub. L. No. 104-188, § 1605, 110 Stat. 1755, 1838 (codified as amended at 26 U.S.C. § 104(a)(2) (Supp. II 1996)) (current version at 26 U.S.C. § 104(a)(2) (2002)).

³ Pub. L. No. 104-188, § 1605, 110 Stat. 1755, 1928–29 (codified as amended at 26 U.S.C. § 104(a)(2) (Supp. II 1996)) (current version at 26 U.S.C. § 104(a)(2) (2002)).

⁴ President's Signing Statement, 32 WEEKLY COMP. PRES. DOC. 1475 (Aug. 26, 1996), reprinted in 1996 U.S.C.C.A.N. 1677, 1862–64.

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In analyzing the 1996 Act's taxation of emotional distress recoveries in discrimination cases, this Article finds that Congress overstepped its constitutional authority by making these emotional distress recoveries an item of income. By conducting a review of the legislative, administrative, constitutional, and judicial history of gross income and the exclusion from income for personal injuries and reparation rights tax relief, this Article shows that emotional distress recoveries are not items of income and cannot be taxed. This Article also explains that the taxation of emotional distress recoveries under the 1996 Act originated from the tension between the civil rights movement and tort reform.

B. Overview of Parts II–VI

Part II of this Article focuses on the legislation and legislative history of §§ 61(a) and 104(a)(2) as they relate to dignitary torts. This Part establishes that the meaning of income is a constitutional concept, not a statutory concept. Part III of this Article then combines the administrative history of personal injury recoveries and reparation rights recoveries. This Part emphasizes the similarities between personal injury and reparation rights recoveries to indicate that both types of recoveries are not income.

Part IV of this Article concentrates on the unconstitutional aspects of taxing emotional distress recoveries as income items. This Part shows, under the U.S. Supreme Court's analysis, that emotional distress recoveries are not income and that a tax on these recoveries is a capitation or direct tax. Part V of this Article reviews the tension between the civil rights movement and tort reform. This Part displays the inconsistent treatment of emotional distress recoveries by tort reformers, who limit these recoveries as noneconomic damages while Congress taxes these recoveries as economic damages.

Part VI of this Article concludes that legislative, administrative, and judicial history indicate precedent supporting the conclusion that, under a variety of tax doctrines, emotional distress recoveries, like reparation rights recoveries, are not income items in the constitutional sense. These tax doctrines concern the legal concepts of the return of human capital, the reimbursement for the loss of personal or civil rights, the "in lieu of" test, and horizontal equity. Under each of these tax doctrines, the taxing of emotional distress recoveries as income is unconstitutional. Finally, this Part shows how excluding emotional distress recoveries from income in nonphysical personal injuries would help to eliminate the English common law sexual stereotypes surrounding mental injuries'

lack of importance, end the inconsistent tax treatment of these recoveries based on the distinction between physical and nonphysical injuries, stop the dual treatment of these recoveries as noneconomic damages under tort reform but as economic damages for tax purposes, and merge the interests of human rights' and civil rights' advocates and tort reformers.

II. DIGNITARY TORTS AND THE LEGISLATION AND LEGISLATIVE HISTORY OF §§ 61(A) AND 104(A)(2)

A. *The Meaning of Income is a Constitutional Concept, Not a Statutory Concept*

The Internal Revenue Code sets forth an expansive concept of gross income, which is subject to the limits of the U.S. Constitution. As the House and Senate Reports state: "Section 61(a) provides that gross income includes 'all income from whatever source derived.' This definition is based upon the 16th Amendment and the word 'income' is used in its constitutional sense."⁵

The definition of gross income has undergone very little legislative change from its inception to the present. Originally, § 213(a) of 1918 and subsequently § 22(a) of 1939 provided that all gain, profits, and income derived from any source whatever are income subject to taxation.⁶ Section 61 of 1954, now § 61(a) as promulgated in 1986, still provides that "gross income means all income from whatever source derived"⁷

B. *Until the 1996 Act, the Exclusion from Income Included Physical and Nonphysical Personal Injuries and Sickness, Such as Dignitary Torts*

The legislative history behind the exclusion from income statute, § 104(a)(2), was silent as to whether personal injuries or sickness exempted physical and nonphysical personal injuries and sickness until

⁵ H.R. REP. NO. 83-1337, at A 18 (1954), reprinted in 1954 U.S.C.C.A.N. 4017, 4155; S. REP. NO. 83-1622, at 168 (1954), reprinted in 1954 U.S.C.C.A.N. 4621, 4802; see also *Rutkin v. United States*, 343 U.S. 130, 138-39 (1952) (stating that the full exercise by Congress of its income taxing power refers just to the Sixteenth Amendment); *Merchants' Loan & Trust Co. v. Smietanka*, 255 U.S. 509, 519-20 (1921); James Edward Maule, *Gross Income: Overview and Conceptual Aspects*, 501-2nd TAX MGM'T, A-1, A-4 (2002).

⁶ Internal Revenue Act of 1939, Pub. L. No. 76-1, § 22(a), 53 Stat. 9 (1939) (codified at I.R.C. § 22(a) (1939)); Revenue Act of 1918, Pub. L. No. 65-254, § 213(a), 40 Stat. 1057, 1065 (1919) (codified at 18 U.S.C. § 213(a) (1918)).

⁷ Tax Reform Act of 1986, Pub. L. No. 99-514, § 61(a), 1986 U.S.C.C.A.N. (100 Stat.) 2085 (codified at I.R.C. § 61(a) (1986)); see also 26 U.S.C. § 61(a) (2002); Internal Revenue Code of 1954, Pub. L. No. 83-591, § 61, 68A Stat. 17 (1954) (codified at I.R.C. § 61 (1954)).

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1996.⁸ In 1996, the legislative history discussed the explicit changes that were expected when nonphysical personal injuries and nonphysical sickness became taxable and when emotional distress was not considered a physical injury or physical sickness.⁹

“Thus, the exclusion from gross income does not apply to any damages received (other than for medical expenses as discussed below) based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress.”¹⁰ The legislative history also broadly defined emotional distress to include symptoms, such as insomnia, headaches, and stomach disorders, that result from the emotional distress.¹¹

This bifurcation by Congress of personal injuries and sickness into physical and nonphysical injuries signifies a departure from almost eighty years of legislative, administrative, and judicial guidance. On its surface, this departure might appear to conform to reparation rights tax relief,¹² which generally originated from a physical loss. However, on closer inspection in Parts III.A, III.B, and IV.D, the change that makes emotional distress recoveries subject to tax departs radically from the constitutional safeguards of dignitary torts, such as reparation rights and civil rights discrimination cases, which encompass emotional distress recoveries as reimbursement for infringement of civil or personal rights.¹³

The pertinent exclusion from gross income underwent very little change from 1918–1996. Section 213(b)(6) of 1918 and then § 22(b)(5) of 1939 stated that gross income does not include “*amounts received, through accident or health insurance or under workmen’s compensation acts, as compensation for personal injuries or sickness, plus the amount of any damages received whether by suit or agreement on account of such injuries or sickness.*”¹⁴ From 1954 through mid-1996, § 104(a)(2) stated that gross

⁸ H.R. REP. NO. 767, at 9, 10, *reprinted in* 1939-1 C.B. 92 (1918).

⁹ Pub. L. No. 104-188, § 1605, 110 Stat. 1755, 1838 (codified as amended at 26 U.S.C. § 104(a)(2) (Supp. II 1996)); H.R. CONF. REP. NO. 104-737, at 300-02 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1677, 1792-94.

¹⁰ H.R. CONF. REP. NO. 104-737, at 301 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1677, 1793.

¹¹ *See id.*, *reprinted in* 1996 U.S.C.C.A.N. 1677, 1793 n.56.

¹² *See infra* text accompanying notes 20, 26.

¹³ *See infra* text accompanying notes 20, 26.

¹⁴ Internal Revenue Act of 1939, Pub. L. No. 76-1, § 22(b)(5), 53 Stat. 10 (1939) (codified at I.R.C. § 22(b)(5) (1939)) (emphasis added); Revenue Act of 1918, Pub. L. No. 65-254, § 213(b)(6), 40 Stat. 1057, 1066 (1919) (codified at 18 U.S.C. § 213(b)(6) (1918)).

income does not include “the amount of any damages received (whether by suit or agreement) on account of personal injuries or sickness.”¹⁵

Then in 1996, Congress changed § 104(a)(2) to state that gross income does not include:

*“[T]he 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;” . . . “For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. . . .”*¹⁶

III. THE ADMINISTRATIVE HISTORY OF PERSONAL INJURY AND REPARATION RIGHTS RECOVERIES

A. *The Treasury Department Did Not Consider Physical or Nonphysical Personal Injury Recoveries To Be Income Under a Return of Human Capital Concept*

Originally, the Treasury Department taxed accident insurance proceeds and damage awards for pain and suffering as income from 1915–1918.¹⁷ Then, the Attorney General issued an opinion regarding the phrase “gains or profits and income derived from any source whatever,” and concluded that accident insurance proceeds “merely take the place of capital in human ability which was destroyed by the accident . . . [and are] ‘capital’ as distinguished from ‘income’ receipts.”¹⁸ The Treasury Department followed this opinion by finding that accident insurance proceeds or amounts received for personal injuries in accidents were not income from 1918–1922.¹⁹

Subsequently, a Solicitor’s opinion in 1922 held that nonphysical personal injury recoveries, such as the alienation of affection recoveries,

¹⁵ Internal Revenue Code of 1954, Pub. L. No. 83-591, § 104(a)(2), 68A Stat. 30 (1954) (codified at I.R.C. § 104(a)(2) (1954)) (emphasis added).

¹⁶ 26 U.S.C. § 104(a)(2) (2002) (emphasis added); § 1605, 110 Stat. 1755, 1838.

¹⁷ T.D. 2135, 17 Treas. Dec. Int. Rev. 39, 42 (1915). The Treasury Department, Office of Commissioner of Internal Revenue, ruled that money paid by an accident insurance policy on account of accidents was gross income. It further ruled that damages received for pain and suffering were income. As such, the damages would be taxable as “‘gains or profits and income derived from any source whatever.’” See also T.D. 2690, 20 Treas. Dec. Int. Rev. 126 (1918) (promulgating Treas. Reg. § 33, revised, pt. I, at 130 (1918)).

¹⁸ 31 Op. Att’y Gen. 304, 308 (1918).

¹⁹ See generally T.D. 2747, 20 Treas. Dec. Int. Rev. 457 (1918) (revoking Regulations No. 33, revised, that were inconsistent with the 31 Op. Att’y Gen. 304, 308 (1918)).

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were not income.²⁰ This opinion did not apply the exclusion from income, § 213(b)(6), the predecessor of § 104(a)(2),²¹ because “the question is really more fundamental, namely, whether such damages are within the legal definition of income.”²²

The author agrees with the 1922 Solicitor’s opinion and contends that logic requires that an item must first be income before it can become taxable income. Thus, an item that is not income does not need to rely on an exclusion from income provision to avoid taxation. Because a nonphysical personal injury recovery is not an income item, it also does not need to rely on an exclusion from income statute to avoid the tax on income.

The Treasury Department again followed this 1922 Solicitor’s opinion by finding that nonphysical personal injury recoveries, being a loss of personal rights, were not income.²³ Specifically, the Treasury Department stated that “a promise to marry is a personal right not susceptible of any appraisal in relation to market values and . . . damages . . . [for] the invasion of such right [do] not constitute taxable income.”²⁴

²⁰ See generally Sol. Op. 132-I-1 C.B. 92 (1922) (modifying Solicitor’s Memorandum 957 and revoking Solicitor’s Memorandum 1384). Upon the request of the Treasury, Congress enacted § 213(b)(6) as part of the Revenue Act of 1918, which excluded from gross income amounts received for personal injuries or sickness. The legislative history was silent as to whether personal injuries or sickness exempted physical and nonphysical personal injuries and sickness. H.R. REP. NO. 767, 65th Cong. 2d Sess. at 9–10, reprinted in 1939-1 C.B. 92 (1918). This silence led to Solicitor’s Memorandum 1384, which decided that personal injuries meant physical injuries only. Sol. Mem. 1384, 2 C.B. 71 (1920). The Solicitor, using the § 213(b)(6) exclusion, then determined that the alienation of a wife’s affection was taxable. Even though it was found to be a personal injury, it was not a physical injury, did not constitute capital, and was not due to sickness. In 1922, the Solicitor was again confronted with the issue of whether alienation of affection, slander or libel of personal character, and surrender of custody of a minor child were excludable from income. This opinion did not base its decision on the § 213(b)(6) exclusion from income, but focused on the meaning of income to find that these personal nonphysical injury claims are not income. *Id.*

²¹ See 26 U.S.C. § 104(a)(2) (2002); § 1605, 110 Stat. 1755, 1838–39; § 104(a)(2), 68A Stat. 30; Internal Revenue Act of 1939, Pub. L. No. 76-1, § 22(b)(5), 53 Stat. 10 (codified at I.R.C. § 22(b)(5) (1939)); § 213(b)(6), 40 Stat. 1057, 1066 (1919).

²² Sol. Op. 132, I-1 C.B. 92, 93 (1922); see also *Eisner v. Macomber*, 252 U.S. 189, 207 (1920) (holding that a pure stock dividend is not taxed because it is not income, and stating the legal definition of income as “gain derived from capital, from labor, or from both combined”); BLACK’S LAW DICTIONARY 906 (4th ed. 1968) (defining income); *infra* text accompanying note 88.

²³ I.T. 1804, II-2 C.B. 61, 62 (1923).

²⁴ *Id.* The Treasury Department made this decision based upon Solicitor’s Opinion 132, *supra* note 20, and *Macomber*, 252 U.S. at 207 (stating that the legal definition of income is “gain derived from capital, from labor, or from both combined”).

The Treasury Department continued this same theme with reparation rights in 1928, finding that an award paid in accordance with the Settlement of War Claims Act for the loss of life “is not embraced in the general concept of the term ‘income.’”²⁵

B. The Treasury Department Finds that Personal Injury and Reparation Payments Are Not Income Because They Are a Reimbursement for the Loss of Civil or Personal Rights

The Treasury Department revenue rulings from the 1950s through the early 1990s, as a general rule, continued to hold that personal injury payments and reparation payments were not income.²⁶ The Treasury

²⁵ I.T. 2420, VII-2 C.B. 123, 124 (1928). The Treasury Department referenced the § 213(a) definition of income that all gains, profits, and income derived from any source whatever are income subject to taxation. However, this compensation was not income and thus not taxable because it restored the taxpayer to substantially the same financial and economic status as she possessed prior to the death of her husband. *Id.*

²⁶ See *Comm’r v. Glenshaw Glass Co.*, 348 U.S. 426, 432-33 (1955) (holding punitive damages to be taxable gross income); *Hawkins v. Comm’r*, 6 B.T.A. 1023, 1025 (1928), *acq.*, C.B. VII-1, 14 (finding that compensatory damages for injury to personal reputation were not income). See generally Rev. Rul. 54-19, 1954-1 C.B. 179 (holding that compensation for the loss of life under a state wrongful death statute is not embraced in the general concept of the term income, and citing I.T. 2420, *supra* note 25, and § 22(a) (successor to § 213(a) used in I.T. 2420)). Both sections provided that all gains, profits, and income derived from any source whatever are income subject to taxation. *Id.* See also generally Rev. Rul. 85-98, 1985-2 C.B. 51 (superseding Rev. Rul. 58-418, reaffirming that libel recoveries for injury to personal reputation are excludable, citing § 61, but using the § 104(a)(2) exclusion from gross income and finding punitive damages to be includible in gross income); Rev. Rul. 74-205, 1974-1 C.B. 21 (extending Rev. Rul. 63-136, Rev. Rul. 68-38, and Rev. Rul. 72-340 to replacement housing payments made under legislatively provided social benefit programs for promotion of the general welfare); Rev. Rul. 74-77, 1974-1 C.B. 33 (superseding Sol. Op. 132, reaffirming that damages for alienation of affections and for surrender of the custody of minor child are not income because they relate to personal or family rights, not property rights, and citing § 61, but obsoleted by Rev. Rul. 98-37 due to the 1996 Act amending § 104(a)(2)); Rev. Rul. 72-340, 1972-2 C.B. 31 (extending Rev. Rul. 63-136 for stipends paid to probationers to aid in acquiring training); Rev. Rul. 69-212, 1969-1 C.B. 34 (extending Rev. Rul. 58-370 to a widow’s pension); Rev. Rul. 68-38, 1968-1 C.B. 446 (extending Rev. Rul. 63-136 to a training program on an Indian reservation); Rev. Rul. 63-136, 1963-2 C.B. 19 (finding that benefit payments for training are not includible in gross income because they are similar to other unemployment relief payments made for the promotion of the general welfare, citing § 61, I.T. 3230, 1938-2 C.B. 136; Rev. Rul. 55-562, 1955-2 C.B. 21; and Rev. Rul. 57-102, 1957-1 C.B. 26); Rev. Rul. 58-500, 1958-2 C.B. 21 (extending Rev. Rul. 56-518 as clarified by Rev. Rul. 57-505); Rev. Rul. 58-418, 1958-2 C.B. 18 (holding that compensatory damages for libel and slander resulting in injury to personal reputation are excludable from gross income, citing § 61); Rev. Rul. 58-370, 1958-2 C.B. 14 (extending Rev. Rul. 56-518 and Rev. Rul. 57-505 for Nazi persecution, and restating that these payments are in the nature of reimbursement for deprivation of civil or personal rights, citing § 61); Rev. Rul. 56-518, 1956-2 C.B. 25 (clarified by Rev. Rul. 57-505, 1957-2 C.B. 50) (extending Rev. Rul. 55-132 to U.S. citizens or residents for Nazi persecution, citing § 61, the successor to § 22(a), and providing that “gross income means all income from whatever source derived . . .”)); Rev.

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Department based these rulings on the definition of gross income §§ 213(a), 22(a), 61, and 61(a), which define gross income. It did not base the rulings on §§ 213(b)(6), 22(b)(5), and 104(a)(2), which set forth exclusions from income. Due to this, the Treasury Department found that such payments are a reimbursement for the loss of civil or personal rights and thus did not meet the definition of income.²⁷ The author asserts, as stated in Part II.A, that if these payments are not income, they do not need exclusion from income statutes to avoid becoming taxable income.

For example, payments received by an American Prisoner of War were not includible in gross income, as they were merely reimbursement for the loss of personal rights.²⁸ Similarly, payments received for Nazi persecution were not includible in income, as they constituted reimbursement for the loss of personal rights or civil rights.²⁹

These rulings used the definition of income under *Hawkins v. Commissioner*³⁰ and the currently accepted, redefined, and broader definition of income of the U.S. Supreme Court under *Commissioner v. Glenshaw Glass Co.*,³¹ which referred to increases to wealth.³² Even using the most expansive definition of income, these rulings concluded that recoveries for all nonphysical injuries should not be items of income, thus negating the need to be excluded from income.³³

C. *Under the "In Lieu Of" Test, Payments Substituting for Actual Earnings are Income but Payments Substituting for Personal Assets Are Not Income*

In 1972, the IRS found a Title VII discrimination claim to be income under § 61 because the amount paid was actual earnings.³⁴ This ruling

Rul. 56-462, 1956-2 C.B. 20 (extending Rev. Rul. 54-19 to payments to Korean War prisoners); Rev. Rul. 55-132, 1955-1 C.B. 213 (holding that amounts received by an American Prisoner of War are in the nature of reimbursement for the loss of personal rights and are not includible in gross income, citing again to § 22(a)).

²⁷ See *supra* note 26.

²⁸ Rev. Rul. 55-132, 1955-1 C.B. 213; see also *supra* text accompanying note 26.

²⁹ Rev. Rul. 58-370, 1958-2 C.B. 14; see also *supra* text accompanying note 26.

³⁰ 6 B.T.A. at 1023 (finding that personal reputation damages are compensatory and thus not income).

³¹ 348 U.S. 426, 431 (1955) (stating that exemplary damages are income and defining income as "undeniable accessions to wealth, clearly realized").

³² *Id.*

³³ See *supra* notes 20, 26 and accompanying text.

³⁴ See generally Rev. Rul. 72-341, 1972-2 C.B. 32 (amplified by Rev. Rul. 84-92, 1984-1 C.B. 204 to include compensation for the Railroad Retirement Tax Act and holding that payments to employees under Title VII of the Civil Rights Act of 1964 for lost earnings were gross income under § 61).

relied on the “in lieu of” test, discussed in the U.S. Supreme Court case of *Hort v. Commissioner*,³⁵ which looked to the nature of the item for which the damages were a substitute.³⁶ Conversely, under the “in lieu of” test, also discussed in the U.S. Supreme Court case *O’Gilvie v. United States*,³⁷ emotional distress recoveries are not income because the government does not tax the reimbursement of something that would not otherwise be taxed.³⁸

D. Taxpayers Used the Exclusion From Income Statute, Not the Definition of Income Statute, in Support of Their Cases

Taxpayers used the exclusion from income §§ 22(b)(5) and 104(a)(2) in their cases rather than showing that their recoveries were not income under § 61(a), the definition of income.³⁹ These taxpayers used the exclusion from income provision at first because the exclusion from income statute granted them specific relief from taxation, or, as seen below, because their recoveries were items of income that needed a specific exclusion from income statute to avoid taxation. Due to this, the

³⁵ 313 U.S. 28 (1941).

³⁶ *Id.* at 32 (using the “in lieu of” test to find income because the cancellation of a lease was essentially a substitute for rental payments).

³⁷ 519 U.S. 79 (1996).

³⁸ *Id.* at 86 (finding that punitive damages were not excludable from income). The Court in *O’Gilvie* reviewed the history of the personal injury exclusion as based on a decision not to tax “damages that, making up for a loss, seek to make a victim whole” *Id.*; see also *Glenshaw Glass Co.*, 348 U.S. at 432 n.8 (“The long history of departmental rulings holding personal injury recoveries nontaxable [is based] on the theory that they roughly correspond to a return of capital . . .”).

³⁹ See also Rev. Rul. 85-143, 1985-2 C.B. 55 (not following *Roemer v. Comm’r*, 716 F. 2d 693 (9th Cir. 1983), *rev’g* *Roemer v. Comm’r*, 79 T.C. 398 (1982) (excluding libel suit recoveries under § 104(a)(2) as personal, and finding that a predominantly business and professional libel suit recovery is not excluded from gross income under § 104(a)(2)); Rev. Rul. 84-108, 1984-2 C.B. 32 (revoking Rev. Rul. 75-45, 1975-1 C.B. 47 and finding that wrongful death statutes where only punitive damages are recoverable are includible in gross income, but if the state’s statute provides that no punitive damages are recoverable, then recovery is excludable from gross income under the exclusion from income § 104(a)(2)); *supra* text accompanying note 26. See generally Rev. Rul. 85-98, 1985-2 C.B. 51; Rev. Rul. 85-97, 1985-2 C.B. 50 (amplifying Rev. Rul. 61-1 and stating that lost wages paid as damages for a personal injury sustained in an accident are excludable from gross income under § 104(a)(2)); Rev. Rul. 61-1, 1961-1 C.B. 14 (holding that a railroad employee’s settlement for personal injuries is not includible in gross income, even for the amount apportioned to time lost under the exclusion from income § 104(a)(2)); Rev. Rul. 103, 1953-1 C.B. 20 (advising that employer disability payments that are not a health or accident insurance plan in excess of workmen’s compensation are includible in gross income, unless made by the employer for personal injuries or sickness in satisfaction of a tort or tort-type liability, under the exclusion from income § 22(b)).

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Treasury Department and courts began basing their decisions and rulings on the statutory interpretation of this exclusion.⁴⁰

The U.S. Supreme Court cases of *United States v. Burke*⁴¹ and *Commissioner v. Schleier*⁴² arose from discrimination statutes that allowed remedies for back pay or liquidated damage recoveries but provided no relief for emotional distress recoveries.⁴³ In both cases, the parties based their arguments on the exclusion from income statute, § 104(a)(2).⁴⁴ In each of these cases, the taxpayers conceded that their discrimination case recoveries for back pay or liquidated damages were income items.⁴⁵ This appears to be a logical concession because these payments substituted for actual earnings or were considered windfalls under the “in lieu of” test, analyzed under Part III.C.

The *Burke* decision in 1992 discussed in dictum the tort-like nature of the remedies provided under the Civil Rights Act of 1991, which also allowed compensatory damages for emotional distress and punitive damages in marked contrast to the Civil Rights Act of 1964, which allowed only back pay damages.⁴⁶ Following this dictum, in 1993 the IRS held that compensatory damages, including back pay for claims of disparate employment discrimination, were excluded from gross income as tort-like damages for personal injury under § 104(a)(2).⁴⁷ Then, the *Schleier* decision in 1995 found no exclusion from tax for an age discrimination case’s limited remedies of back pay and liquidated damages. Based on this decision, the IRS suspended their 1993 ruling to invite public comment.⁴⁸

In 1996, the IRS ultimately abrogated their 1993 discrimination ruling⁴⁹ in light of § 104(a)(2), as amended by § 1605 of the 1996 Act.⁵⁰ The IRS acknowledged that the amended § 104(a)(2) restricted the exclusion from gross income to physical personal injuries or sickness and

⁴⁰ See *Comm’r v. Schleier*, 515 U.S. 323 (1995); *United States v. Burke*, 504 U.S. 229, 234 (1992); Rev. Rul. 96-65, 1996-2 C.B. 6; Rev. Rul. 93-88, 1993-2 C.B. 61; Notice 95-45, 1995-2 C.B. 330.

⁴¹ 504 U.S. 229 (1992).

⁴² 515 U.S. 323 (1995).

⁴³ *Schleier*, 515 U.S. at 323; *Burke*, 504 U.S. at 229.

⁴⁴ *Schleier*, 515 U.S. at 323; *Burke*, 504 U.S. at 229.

⁴⁵ See *Schleier*, 515 U.S. at 328; *Burke*, 504 U.S. at 233.

⁴⁶ *Burke*, 504 U.S. at 241.

⁴⁷ Rev. Rul. 93-88, 1993-2 C.B. 61.

⁴⁸ *Schleier*, 515 U.S. at 323; see also Notice 95-45, 1995-2 C.B. 330.

⁴⁹ Rev. Rul. 96-65, 1996-2 C.B. 6.

⁵⁰ 26 U.S.C. § 104 (a)(2) (2002).

provided that emotional distress shall not be treated as a physical injury or physical sickness.⁵¹

This 1996 ruling decided that back pay was not excluded from gross income as disparate treatment employment discrimination under the former § 104(a)(2) because it was not received due to personal injuries or sickness.⁵² However, prior to the 1996 Act, the IRS still found that emotional distress recoveries were excluded when received on account of personal injuries or sickness under the former § 104(a)(2), *Burke*, and *Schleier*.⁵³

The distinction made by the IRS between back pay and emotional distress recoveries displays the U.S. Supreme Court's interpretation in both *Burke* and *Schleier*: Recoveries for emotional distress qualify for the former § 104(a)(2) exclusion from income because when viewed in isolation, they stem from a tort-type right and result from a personal injury.⁵⁴ This distinction also highlights the constitutional aspect of emotional distress recoveries as not being income, which Part IV below discusses further.

E. Reparation Rights Tax Relief Should Guide Congress Back to Civil Rights Tax Relief

Reparation rights and discrimination cases have both a human rights and a civil rights component. Human rights embody the freedoms and benefits all human beings should be able to claim as a matter of right in their society at an international level.⁵⁵ Civil rights entail the rights of personal liberty guaranteed by the U.S. Constitution as well as U.S. legislation.⁵⁶

Thus, violations of the U.S. discrimination statutes cause a violation of both human rights and civil rights. These human rights and civil

⁵¹ *Id.*

⁵² Rev. Rul. 96-65, 1996-2 C.B. 6.

⁵³ *Id.*; see also *Schleier*, 515 U.S. at 332; *Burke*, 505 U.S. at 241; Rev. Rul. 93-88, 1993-2 C.B. 61; Douglas A. Kahn, *Taxation of Damages After Schleier – Where are We and Where Do We Go From Here?*, 15 QUINNIPIAC L. REV. 305, 330 (1995) ("If the ADEA had allowed damages to be awarded for pain and suffering, and if that added item were deemed sufficient to make a claim under the ADEA a tort or tort-type claim, then damages received by the taxpayer for pain and suffering would be received on account of a personal injury, and so would be excluded from income.") (citation omitted).

⁵⁴ See *supra* note 53.

⁵⁵ BLACK'S LAW DICTIONARY 758 (8th ed. 2004) (defining human rights).

⁵⁶ *Id.* at 263 (8th ed. 2004) (defining civil rights).

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rights violations cross more than one generation because they stem from social upheaval and longterm suffering.⁵⁷

The 1996 Act's statutory shift limits the exclusion from tax to physical personal injury and sickness, thereby taxing nonphysical personal injury and sickness, which includes emotional distress recoveries in discrimination cases. This shift represents a narrowing of our legislature's former humanitarianism policy.⁵⁸ In contrast, instances of America's reparation tax relief for POWs,⁵⁹ the Holocaust,⁶⁰ 9-11 victims,⁶¹ and the proposed African-American reparation legislation for

⁵⁷ Mark J. Wolff, *Sex, Race, and Age: Double Discrimination in Torts and Taxes*, 78 WASH. U. L.Q. 1341, 1344 (2000). Mr. Wolff stated:

[T]oday physicians, lawyers, and social scientists acknowledge that nonphysical injuries resulting from racial discrimination cause enduring intergenerational scars and may be more enduring and more severe than physical injuries caused by the loss of an arm or leg in a traffic accident. Additionally, both empirical studies and congressional policies now recognize the insidiousness of sexual harassment, age, and disability discrimination, as well as the long-term and sometimes permanently debilitating effects inflicted upon their victims.

Id. (citation omitted); see also Karen B. Brown, *Not Color-Or-Gender-Neutral: New Tax Treatment of Employment Discrimination Damages*, 7 S. CAL. REV. L. & WOMEN'S STUD. 223, 231 (1998) ("The result is codification of the notion that an injury to the physical part of an individual is real and tangible and, hence, legally perceptible. . . . Harm to an individual in the form of employment discrimination is not cognizable because it is not real (imaginary, not traceable to a cause), and it is intangible (incapable of measurement)."); Kahn, *supra* note 53, at 318. Mr. Kahn surmised:

On the other hand, the case for excluding damages received for nonphysical injuries (other perhaps than for mental damage) is less compelling. The plight of a person who suffers exclusively nonphysical injuries does not arouse the same degree of sympathy that attaches to a victim who suffers a serious physical injury.

Id.; Harold S. Peckron, *Reparation Payments – An Exclusion Revisited*, 34 U.S.F.L. REV. 705 (2000).

⁵⁸ Wolff, *supra* note 57, at 1401; see also Kahn, *supra* note 53, at 316.

⁵⁹ See *supra* text accompanying note 26.

⁶⁰ *Id.*; see also Holocaust Restitution Tax Fairness Act of 2002, Pub. L. No. 107-358, § 2, 116 Stat. 3015 (2002) (repealing the sunset of section 901); Peckron, *supra* note 57 at 705. See generally Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 803, 115 Stat. 149 (2001) (excluding from federal income tax restitution received by victims of Nazi regime).

⁶¹ See 26 U.S.C. § 104(a)(5) (2002); see also John M. Barkett, *Combating Terrorism in the Environmental Trenches: Terrorism and the Future of Torts; If Terror Reigns, Will Torts Follow?*, 9 WIDENER L. SYMP. J. 485, 543 (2003); Hillel Sommer, *Providing Compensation for Harm Caused by Terrorism: Lessons Learned in the Israeli Experience*, 36 IND. L. REV. 335, 365 (2003). See generally Victims of Terrorism Tax Relief Act of 2001, Pub. L. No. 107-134, §§ 101-116, 115 Stat. 2427 (2002) (providing income tax and estate tax relief to 9-11 victims and anthrax victims); Elbert Lin, Case Comment, *Korematsu Continued . . .*, 112 YALE L.J. 1911, 1913

slavery⁶² demand that Congress reinstate tax relief for civil rights cases to reinforce America's human rights resolve.

Tax doctrine indicates that reparations in the form of recoveries for the taking of human rights or civil rights are not income because they are a reimbursement for the loss of personal or civil rights.⁶³ Using this tax doctrine, recoveries for the taking of human rights in reparation cases and personal or civil rights in personal injury and discrimination cases are not income.⁶⁴

IV. THE UNCONSTITUTIONALITY OF TAXING EMOTIONAL DISTRESS RECOVERIES

A. *The Tax History of the U.S. Constitution*

The focus of America's revolution and the break with Britain was taxation, as shown in the well-known phrase allowing no taxation without representation.⁶⁵ America's first constitution, the Articles of Confederation, failed to provide enforcement powers for the national

(2003) (comparing Pearl Harbor with 9-11 as signifying losses of personal rights by using "threats to national security to deflect attention from race-based actions").

⁶² See also Tuneen E. Chisolm, *Sweep Around Your Own Front Door: Examining the Argument for Legislative African American Reparations*, 147 U. PA. L. REV. 677, 727 n.56 (1999) (citing Commission to Study Reparation Proposals for African Americans Act, H.R. 40, 105th Cong., § 2(b) (1997), which "propos[ed] to establish a commission to examine the institution of slavery . . . and the impact of these experiences on living African Americans . . ."); Kevin Hopkins, *Forgive U.S. Our Debts? Righting the Wrongs of Slavery*, 89 GEO. L.J. 2531 (2001); Van B. Luong, *Recent Development: Political Interest Convergence: African American Reparations and the Image of American Democracy*, 25 HAW. L. REV. 253, 258 (2002); Eric K. Yamamoto, *Racial Reparations: Japanese American Redress and African American Claims*, 40 B.C. L. REV. 477, 523 n.36 (1998) (referring to a section of the article "describing the reframing of reparations from compensation to 'repair'—that is, the repairing of tears in the structural and psychological fabric of a society resulting from the social and economic subordination of some of its members"). See generally African American Reparations Commission Act, H.R. 40, 105th Cong. (1997) (sponsored by Rep. John Conyers from 1989 forward).

⁶³ See *supra* Part III.B.

⁶⁴ See *supra* Part III.B.

⁶⁵ See JOHN BARTLETT, *FAMILIAR QUOTATIONS* § 327.7 (16th ed., 1992) (noting the phrase "taxation without representation is tyranny" was attributed to James Otis in 1763); Bruce Ackerman, *Taxation and the Constitution*, 99 COLUM. L. REV. 1, 6 (1999) ("During the revolutionary era, taxation was at the very center of popular consciousness. The break with Britain was motivated largely by this issue . . .").

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government to raise revenue from the states.⁶⁶ The Federalists' solution was the broad grant of power to Congress to impose and collect taxes.⁶⁷

Thus, the U.S. Constitution gave Congress broad powers of taxation, but this power was subject to an important income taxation limit. This constitutional limit directed that no capitation or other direct tax shall be imposed, unless in proportion to the census or apportioned among the several states.⁶⁸

Three reasons have been proposed for this limitation. First, there was a desire to limit the national government's taxation powers to protect private rights from oppressive taxation.⁶⁹ Second, it was important to protect state and local governments' rights to raise revenues through direct taxes, like real estate taxes.⁷⁰ Third, the limitation arose from the Great Compromise, which Benjamin Franklin proposed. The compromise espoused equal representation in the Senate and proportional representation in the House.⁷¹ Acceptance of this compromise led to the South's insistence on counting their slaves as three-fifths of a person in order to obtain greater representation in the House in exchange for paying an extra three-fifths share of direct taxes.⁷²

⁶⁶ See Ackerman, *supra* note 65, at 6.

⁶⁷ See Ackerman, *supra* note 65, at 5. The general taxing power and the uniformity rule provides: "The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises, shall be uniform throughout the United States." U.S. CONST. art. I, § 8, cl. 1.

⁶⁸ U.S. CONST. art. I, § 2, cl. 3; U.S. CONST. art. I, § 9, cl. 4, *amended by* U.S. CONST. amend. XVI. The direct tax clauses provide:

No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken. . . . The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration. . . . Representatives and direct Taxes shall be apportioned among the several States which may be included within this Union, according to their respective Numbers, which shall be determined by adding to the whole Number of free Persons, including those bound to service for a Term of Years, and excluding Indians not taxed, three fifths of all other Persons.

Id.

⁶⁹ See F. Patrick Hubbard, *Making People Whole Again: The Constitutionality of Taxing Compensatory Tort Damages For Mental Distress*, 49 FLA. L. REV. 725, 729 (1997).

⁷⁰ See *id.* at 730.

⁷¹ See Ackerman, *supra* note 65, at 8.

⁷² *Id.*

If the Great Compromise to slavery were the only reason for this limit, as some commentators contend, then a narrow reading of the direct tax clause as applying only to real estate or poll taxes may be warranted.⁷³ However, if the concerns about oppressive taxation and protecting the state and local governments' rights to raise revenue through direct taxes were also considerations that resulted in the limitation, then prohibition against all capitation and direct taxes is still important today.⁷⁴

Frederick Douglass stated his view that all the reasons were relevant:

I hold that the Federal Government was never, in its essence, anything but an anti-slavery government. Abolish slavery tomorrow, and not a sentence or syllable of the Constitution need be altered. It was purposely framed as to give no claim, no sanction to the claim, of property in man. If in its origin slavery had any relation to the government, it was only as the scaffolding to the magnificent structure, to be removed as soon as the building was completed.⁷⁵

B. An Emotional Distress Recovery Tax Under the 1996 Act Is a Direct Tax/Capitation Tax

Even those commentators who would view the direct tax apportionment clause narrowly still concede that a capitation type of tax is of equal vitality today.⁷⁶ A capitation tax has been defined as a direct tax, which is based on the simple fact of a person's existence.⁷⁷

⁷³ See *id.* at 53, 56; Calvin H. Johnson, *Apportionment of Direct Taxes: The Foul-Up In the Core of the Constitution*, 7 WM. & MARY BILL RTS. J. 1, 71, 72 (1998).

⁷⁴ See Hubbard, *supra* note 69, at 730.

⁷⁵ Frederick Douglass, *Address for the Promotion of Colored Enlistments (July 6, 1883)*, in THE LIFE AND WRITINGS OF FREDERICK DOUGLASS 365 (Philip S. Foner ed., 1950); see also Erik M. Jensen, *Taxation and the Constitution: How to Read the Direct Tax Clauses*, 15 J.L. & POL. 687, 706, 714 n.75 (1999); c.f. DON E. FEHRENBACHER, THE DRED SCOTT CASE: ITS SIGNIFICANCE IN AMERICAN LAW AND POLITICS 27 (Oxford Univ. Press 1978) ("[I]t is as though the framers were half-consciously trying to frame two constitutions, one for their own time and the other for the ages, with slavery viewed bifocally—that is, plainly visible at their feet, but disappearing when they lifted their eyes.").

⁷⁶ See *Fernandez v. Wiener*, 326 U.S. 340, 345 (1945) (holding that Congress may tax real estate or chattels only if the tax is apportioned); see also Ackerman, *supra* note 65, at 58; Johnson, *supra* note 73, at 71, 80.

⁷⁷ See *Pac. Ins. Co. v. Soule*, 74 U.S. 433, 444 (1868); see also *Gertz v. Robert Welch, Inc.*, 418 U.S. 323, 350 (1974) (involving a libel action and stating that "actual injury . . . [includes] . . . mental anguish and suffering"); *Breedlove v. Suttles*, 302 U.S. 277, 281 (1937), *overruled on another point by Harper v. Va. State Bd. of Elections*, 383 U.S. 663 (1966);

Therefore, it is a direct tax imposed on a person, as a person, rather than imposed on an activity or on real or personal property.⁷⁸

C. *The 1996 Act Failed To Apportion the Emotional Distress Recovery Tax*

Under the mechanics of apportionment, State X, which has twice the population of State Y, would have twice the aggregate liability of State Y. If an emotional distress recovery tax is apportioned and State X's per capita emotional distress awards are only one-half of State Y's, then the tax rates on the emotional distress awards in State X would have to be twice those in State Y to satisfy the apportionment requirement.⁷⁹ Thus, emotional distress awards are not apportioned under the 1996 exclusion from income statute, § 104(a)(2), because such a formula of apportionment was not included in the 1996 exclusion of income statute.

BLACK'S LAW DICTIONARY 264 (8th ed. 2004) (defining poll-tax and capitation tax); BLACK'S LAW DICTIONARY 563 (8th ed. 2004) (providing that emotional distress is another term for the lack of psychic well-being that can also be called numerous names, such as mental distress, mental anguish, mental suffering, pain and suffering, or a myriad of other intangible harms); BLACK'S LAW DICTIONARY 737 (8th ed. 2004) (defining health as the freedom from pain or sickness and the state of being sound or whole in body, mind, or soul, and the right to the enjoyment of health as a subdivision of the right of personal security, which is one of the absolute rights of persons); BLACK'S LAW DICTIONARY 1347-48 (8th ed. 2004) (defining personal rights as encompassing the rights of personal security, one of which is health); BLACK'S LAW DICTIONARY 852 (4th ed. 1968); BLACK'S LAW DICTIONARY 1137 (4th ed. 1968) (defining the legal meaning of mental as relating to or existing in the mind; intellectual, emotional, or psychic, as distinguished from bodily or physical); BLACK'S LAW DICTIONARY 1320 (4th ed. 1968); BLACK'S LAW DICTIONARY 1488 (4th ed. 1968); Frank J. Doti, *Personal Injury Tax Exclusion: An Analysis and Update*, 75 DENV. U.L. REV. 61, 63 (1997) ("From its inception, in my opinion, the exclusion for personal injury awards should have been limited to losses of human capital. By this I mean any losses to a person's birthright—an uninjured body and mind."); Hubbard, *supra* note 69, at 760 (stating that "[t]axing each human for the benefits of [or the compensation from not] possessing and enjoying emotional well-being would be effectively a poll tax [or capitation tax] because it would be laid upon persons without regard to their occupations or property," and emphasizing that psychic well-being is based on the simple fact of a person's existence, i.e., their uniquely human mental aspect and is a basic, natural, and personal right); Nicholas M. Whittington, *Against the Grain: An Interdisciplinary Examination of the 1996 Federal Statutory Changes to the Taxability of Personal Injury Awards*, 37 WASHBURN L.J. 153 (1997); Sharon E. Stedman, Note, *Congress's Amendment to Section 104 of the Tax Code Will Not Clarify the Tax Treatment of Damages and Will Lead to Arbitrary Distinctions*, 21 SEATTLE U. L. REV. 387, 389 (1997).

⁷⁸ See *supra* note 77 and accompanying text. But see also *infra* Part IV.E.

⁷⁹ Erik M. Jensen, *The Taxing Power, the Sixteenth Amendment, and the Meaning of "Incomes"*, 33 ARIZ. ST. L.J. 1057, 1067 (2001).

D. The 1996 Act's Taxation of Emotional Distress Recoveries as Income Is Unconstitutional

To categorize emotional distress recoveries as taxable income, these recoveries must first be considered income. However, emotional distress recoveries do not fall within the U.S. Supreme Court's concept that income⁸⁰ is comprised of undeniable accessions to wealth.⁸¹ They also do not fall within the Internal Revenue Code's concept of gross income under § 61(a),⁸² as all income from whatever source derived.⁸³

The Sixteenth Amendment to the U.S. Constitution allows Congress "to lay and collect taxes on incomes, from whatever source derived, without apportionment . . ."⁸⁴ This amendment only applies to items of income.⁸⁵ Thus, the Sixteenth Amendment does not apply to the taxation of recoveries meant to compensate a person for emotional distress. Without the protection of the Sixteenth Amendment, the taxation of emotional distress recoveries is a capitation or direct tax⁸⁶ done without apportionment upon the person who suffers emotional distress, which violates Article I, section 9 of the U.S. Constitution.⁸⁷

Income refers to gains or profits, which are true increases in the amount of wealth.⁸⁸ To restore the person to the condition in which the person originally existed⁸⁹ is not an enrichment that constitutes wealth. For example, a recovery to compensate a person for emotional distress does not increase the person's wealth, but merely restores that person to his or her previous condition.

As the U.S. Supreme Court recently explained in *O'Gilvie*,⁹⁰ tax policy excludes damages that substitute for "personal assets that the

⁸⁰ *Comm'r v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955).

⁸¹ *See id.*

⁸² 26 U.S.C. § 61(a) (2002).

⁸³ *Id.*

⁸⁴ U.S. CONST. amend. XVI.

⁸⁵ *Id.*; *see also* Hubbard, *supra* note 69, at 732 (stating that the Sixteenth Amendment "does not eliminate the apportionment requirement for direct taxes that do not involve income").

⁸⁶ Hubbard, *supra* note 69, at 760.

⁸⁷ *See* U.S. CONST. art. I, § 9, cl. 4, *amended by* U.S. CONST. amend. XVI; *see also* U.S. CONST. art. I, § 2, cl. 3.

⁸⁸ *Glenshaw Glass Co.*, 348 U.S. at 431; *see also* BLACK'S LAW DICTIONARY 778 (8th ed. 2004) (defining income); BLACK'S LAW DICTIONARY 906 (4th ed. 1968) (defining income).

⁸⁹ *See* *Albemarle Paper Co. v. Moody*, 422 U.S. 405, 418–19 (1975) (involving a Title VII race discrimination claim and stating the make whole concept).

⁹⁰ *O'Gilvie v. United States*, 519 U.S. 79, 86 (1996); *see also* *Glenshaw Glass Co.*, 348 U.S. at 432 n.8.

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government does not tax and would not have taxed had the victim not lost them.”⁹¹ If the government does not tax the joy of life, then recoveries for the lost joy of life should not be taxed.⁹² Thus, the current taxing of emotional distress recoveries under § 104(a)(2) has now unconstitutionally decreed that: “If you hurt and cry, I’ll tax your tears.”⁹³

E. An Emotional Distress Recovery Is Not an Income Item in the Statutory Sense

An emotional distress recovery, if taxed, is best viewed as a capitation tax on the person.⁹⁴ Even if an emotional distress recovery tax is considered a tax on personal property⁹⁵ or a tax on an activity,⁹⁶ an

⁹¹ *O’Gilvie*, 519 U.S. at 86.

⁹² See F. Phillip Manns, Jr., *Restoring Tortiously Damaged Human Capital Tax-Free Under Internal Revenue Code Section 104(a)(2)’s New Physical Injury Requirement*, 46 BUFF. L. REV. 347, 349–50 (1998) (“Damage payments are treated identically with the thing for which they substitute Similarly, other aspects of living, like the joy of life, are not taxed. Therefore, damages for lost joy of life should not be taxed either.”). See *infra* notes 95–101 for a discussion of Mr. Manns’ premise that recoveries from nontaxable items are converted into taxable items without the exclusion from income statute.

⁹³ Hubbard, *supra* note 69, at 726.

⁹⁴ See *supra* Part IV.B.

⁹⁵ See BLACK’S LAW DICTIONARY 1382 (4th ed. 1968); see also BLACK’S LAW DICTIONARY 1254 (8th ed. 2004) (stating that personal property in its broad and general sense is any movable or intangible thing that is the subject of ownership not in the realm of real estate, such as a right or interest in things personal); Joseph M. Dodge, *Taxes and Torts*, 77 CORNELL L. REV. 143 (1992) (arguing that an emotional distress damage award can be considered a monetary recovery that creates an economic dimension within a noneconomic harm by virtue of being granted monetary recoveries for those noneconomic harms). Mr. Dodge’s article was written before Mr. Hubbard’s article discussing the constitutional restraints of taxing emotional distress. Mr. Dodge recognizes the “in lieu of” test discussed in the Supreme Court’s concurring decision in *United States v. Kaiser*, 363 U.S. 299, 311 (1960), which states: “The principle at work here is that payment which compensates for a loss of something which would not itself have been an item of gross income is not a taxable payment.” However, Mr. Dodge counters that test because the tax base must look to the changes in objective net wealth and be equated with material resources, like money and property, which can be used by the government. Mr. Dodge has a logical extrapolation to the argument that if you cry, I will not tax your tears, by including it, but if you receive money for those tears, then I will tax the money. However, this extension still violates the court’s tax policy under *Kaiser*. This extension also does not take into account the duality of individuals as espoused in *United States v. Gilmore*, which recognizes that an individual has two personalities: “[O]ne is [as] a seeker after profit who can deduct the expenses incurred in that search; the other is [as] a creature satisfying his needs as a human and those of his family but who cannot deduct such consumption and related expenditures.” 372 U.S. 39, 44 (1963) (quoting SURREY & WARREN, CASES ON FEDERAL INCOME TAXATION 272 (1960)). Further, it violates constitutional policy, as demonstrated in Parts IV.A–D, which limits the tax base and what you can tax without apportionment.

emotional distress recovery tax is not a tax on the income from a person, property, or an activity, because it does not stem from income in the statutory sense.⁹⁷

Recovery for emotional distress does not constitute income in the general statutory sense, as all income from whatever source derived.⁹⁸

⁹⁶ BLACK'S LAW DICTIONARY 36, 292, 855 (8th ed. 2004) ("Activity, Common or Joint Enterprise: An activity is the collective acts of one person or of two or more people in a common or joint enterprise, which may be defined as a non-commercial joint venture"); see also Douglas A. Kahn, *The Constitutionality of Taxing Compensatory Damages for Mental Distress When There Was No Accompanying Physical Injury*, 4 FLA. TAX REV. 128, 129 (1999) (stating that emotional distress damage awards are income, even if emotional distress itself is not). Mr. Kahn depicts the litigation or settlement aspect leading to an award as transforming noneconomic harms into an economic or commercial environment. Mr. Kahn rebuts the unconstitutionality of taxing mental distress by questioning any reliance on the *Pollock* or *Macomber* cases or the return of human capital or noncommercial nature theories, taking the stance that taxing mental distress recoveries is constitutional. While this Article acknowledges that the dictionary definition of income in *Eisner v. Macomber*, 252 U.S. 189, 207 (1920), has been expanded under *Glenshaw Glass Co.*, 348 U.S. 426 (1955), to include an economic definition as well, this author uses the *Glenshaw Glass Co.* and post-*Glenshaw Glass Co.* cases' definition of income and emotional distress to contend that emotional distress recoveries are not an undeniable accession to wealth. Further, this author uses a narrow interpretation of *Pollock*, collectively *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429 (1895) ("*Pollock I*") and *Pollock v. Farmers' Loan & Trust Co.*, 158 U.S. 601 (1895) ("*Pollock II*"). A narrow reading of both *Pollock* decisions is that the 1894 tax, which the Supreme Court declared unconstitutional, was primarily a tax on income from property, and these two decisions addressed personal property taxes and real estate taxes as direct taxes requiring apportionment. The Court also held that if a tax on real estate or personal property is a direct tax, then it follows that a tax on the income from real estate or invested personal property is a direct tax. *Pollock I*, 157 U.S. at 579-83; *Pollock II*, 158 U.S. at 628, 634. In reaffirming the *Pollock* decisions, as modified by *Brushaber v. Union Pacific R.R.*, 240 U.S. 1, 24-25 (1916), which upheld the progressive income tax passed just after the passage of the Sixteenth Amendment, this Court said: "Congress may tax real estate or chattels if the tax is apportioned, and without apportionment it may tax an excise upon a particular use or enjoyment of property or the shifting from one to another of any power or privilege incidental to the ownership or enjoyment of property." Chief Justice Edward White, one of the four dissenters in the *Pollock* decisions, wrote the unanimous opinion in *Brushaber* that determined that the Sixteenth Amendment only overruled the *Pollock* decisions' effort to trace income back to its underlying asset, and he implied that the Sixteenth Amendment approved of the *Pollock* decisions' expansionary reading of the direct tax clauses to include capitation taxes and taxes on real estate and personal property, but not to include the income from real estate or personal property. Finally, this author uses not only a return of human capital or the noncommercial nature theories, but also utilizes the reparation rights tax relief analogy that finds a reimbursement for civil or personal rights not to be income. Thus, an emotional distress recovery is also not income as a reimbursement for a personal or civil right, which Mr. Kahn did not address. This author further concludes that intangible harms from all nonphysical injuries recoveries should not be items of income, thus negating the need to be excluded from income.

⁹⁷ See § 61(a), 1986 U.S.C.A.N. (100 Stat.) 2085; Internal Revenue Code of 1954, Pub. L. No. 83-591, § 61, 68A Stat. 17 (1954) (codified at I.R.C. § 61 (1954)); see also 26 U.S.C. § 61(a) (2002).

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Also, an emotional distress recovery does not fit into the statutory gross income subsections under compensation for services, including fees, commissions, fringe benefits, and similar items;⁹⁹ gross income derived from business;¹⁰⁰ or gains derived from dealings in property.¹⁰¹ Rather, an emotional distress recovery falls under such tax doctrines as a return of human capital, a reimbursement for the loss of personal or civil rights, the “in lieu of” test, or horizontal equity.¹⁰²

⁹⁸ See *supra* note 97 and accompanying text.

⁹⁹ 26 U.S.C. § 61(a)(1) (2002); see also BLACK’S LAW DICTIONARY 301 (8th ed. 2004) (defining compensation to include payment of damages to make the person whole). *But see also Kaiser*, 363 U.S. at 310 (“Payment . . . as compensation for a loss or injury that had been suffered . . . [is] not taxable either because not greater in amount than the loss or because the thing lost or damaged had no ascertainable market value and so it could not be said that there had been any net profit to the taxpayer through the effectual exchange of the thing lost for the payment received.”); *supra* Part III.C (explaining that compensation in the form of damages has been limited in case law by the “in lieu of” test).

¹⁰⁰ 26 U.S.C. § 61(a)(2) (2002); see *O’Gilvie v. United States*, 519 U.S. 79, 86 (1996) (emphasizing that no gain has been received when “damages that, making up for a loss, seek to make a victim whole, or, speaking very loosely, ‘return the victim’s personal with financial capital’”); Hubbard, *supra* note 69, at 763–64 (arguing that emotions do not have an economic dimension because happiness or sorrow cannot be bought and sold); see also BLACK’S LAW DICTIONARY 211 (8th ed. 2004) (defining business as a commercial enterprise carried on for profit, a particular occupation or employment habitually engaged in for livelihood or gain, commercial transactions, or by extension of a noncommercial nature, such as the court’s business or parliamentary business). *But see also* BLACK’S LAW DICTIONARY 778 (8th ed. 2004) (defining income); BLACK’S LAW DICTIONARY 906 (4th ed. 1968); *supra* note 84 (explaining that business, as used in a noncommercial sense, negates the concept of income as one of gain, earnings, or profit).

¹⁰¹ 26 U.S.C. § 61(a)(3) (2002); see also *supra* text accompanying note 96. Logically, there can be no gain when the measure of damages is the amount of money necessary to make the victim whole again. This is especially true when recoveries for emotional distress damages are not rendered in lieu of something that is otherwise taxable because emotional well-being, the lack of emotional distress, is not taxable as income. Hubbard, *supra* note 69, at 761.

¹⁰² See Part III.A–C, IV.F; see also *O’Gilvie*, 519 U.S. at 84 (“At that time, this Court had recently decided several cases based on the principle that a restoration of capital was not income; hence it fell outside the definition of ‘income’ upon which the law imposed a tax.”); Doti, *supra* note 77, at 62 (“Congress should have eliminated the section 104(a)(2) exclusion for lost wages and earning power in all cases Uncertainty and resulting litigation will continue until Congress limits the exclusion to damages attributable solely to losses of human capital.”). Gain or income is defined broadly to be an increase in wealth, clearly realized, over which the taxpayer has control, but a recovery that just repairs or reimburses for the loss suffered and merely substitutes for goods of a nontaxable nature, such as pleasure or pain, is not gain or income. See also Hubbard, *supra* note 69, at 760 (“Even if it were proper to treat payments of compensatory awards as taxable transactions, there would be serious equal treatment problems with an excise imposed only on awards for mental distress unaccompanied by a physical injury and imposed at a rate which varies with the taxpayer’s overall income.”); Laura Sager & Stephen Cohen, *Discrimination Against Damages for Unlawful Discrimination: The Supreme Court, Congress, and the Income Tax*, 35

F. *An Emotional Distress Recovery Is Not an Income Item Using the U.S. Supreme Court's Analysis*

Even if an emotional distress recovery tax is a capitation or direct tax that is not apportioned, this tax could still be considered constitutional if the emotional distress recovery is income in the constitutional sense.¹⁰³ This author contends that what Congress did in the 1996 Act, by making an emotional distress recovery taxable in a nonphysical personal injury, was to declare that an emotional distress recovery is income in a statutory sense. This declaration occurred in two instances: when Congress stated in § 104(a)(2) that emotional distress shall not be treated as a physical personal injury or physical sickness, and when Congress stated in legislative history that an exclusion from gross income does not apply to any damages received on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress. However, these statements do not give Congress the power to make emotional distress recoveries an item of taxable income in the constitutional sense. Thus, even if an emotional distress recovery may be defined to be income in the statutory sense, the tax on emotional distress recoveries is unconstitutional as long as the emotional distress recovery is not income in the constitutional sense.¹⁰⁴

Section 61(a)'s legislative history sets forth the statutory meaning of income, expressly subjecting the term income to a definition based on the U.S. Constitution.¹⁰⁵ Because the Sixteenth Amendment does not define

HARV. J. ON LEGIS. 447, 449-50, 497 (1998) ("Under this so-called 'in lieu of' principle, whether the harm is physical is irrelevant. Instead, in all personal injury cases, damages for lost earnings should be taxable and damages for pain and suffering should be excludable."). But see Patrick E. Hobbs, *The Personal Injury Exclusion: Congress Gets Physical but Leaves the Exclusion Emotionally Distressed*, 76 NEB. L. REV. 51, 56, 94 (1997) (advocating a total repeal of the personal injury exclusion both in its physical and nonphysical aspects).

¹⁰³ See Part IV.D; see also *Comm'r v. Obear-Nester Glass Co.*, 217 F.2d 56, 58 (1954) ("The [Sixteenth] Amendment allows a tax on 'income' without apportionment, but an unapportioned direct tax on anything that is not income would still, under the rule of the Pollock case, be unconstitutional."); *Helvering v. Indep. Life Ins. Co.*, 292 U.S. 371, 378 (1934) (holding that tax on the rental value of a building by its owner is a direct tax because income is not involved); *Taft v. Bowers*, 278 U.S. 470, 481 (1929) (stating that the "Sixteenth Amendment confers no power upon Congress to define and tax as income without apportionment something which theretofore could not have been properly regarded as income"); *Edwards v. Cuba R.R.*, 268 U.S. 628, 631-32 (1925) ("The Sixteenth Amendment, like other laws authorizing or imposing taxes, is to be taken as written and is not to be extended beyond the meaning clearly indicated by the language used."); *Pollack II*, 158 U.S. 601 (1895); *Pollack I*, 157 U.S. 429 (1895); Jensen, *supra* note 75, at 1147; Maule, *supra* note 5, at A-13.

¹⁰⁴ See Part IV.D; see also *supra* note 99 and accompanying text.

¹⁰⁵ See Part II.A.

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the phrase “taxes on incomes” or indicate whether income means gross income or net income,¹⁰⁶ constitutional interpretation rules become the focal point.

Constitutional interpretation generally includes a review of the text, the framer’s intent, the underlying purpose of the Constitution, judicial precedent, and consideration of justice and social policy.¹⁰⁷ Originalists view these items from the time of the Constitution’s adoption, and nonoriginalists view these items as evolving concepts.¹⁰⁸

In assessing the Constitution’s underlying purpose along with justice and social policy, a basic sense of fairness evolved in constitutional interpretation, as represented by the Due Process and Equal Protection Clauses.¹⁰⁹ The Equal Protection Clause, which provides that people in similar situations ought to be treated similarly, is like the basic tax policy of horizontal equity, which provides that people with similar incomes ought to pay similar taxes.¹¹⁰

In *Eisner v. Macomber*,¹¹¹ a definition of income in the constitutional sense appeared under the 1916 Act, and the Court found that there must be a gain before it is considered income in the constitutional sense.¹¹² In

¹⁰⁶ See Maule, *supra* note 5, at A-13.

¹⁰⁷ Majorie E. Kornhauser, *The Constitutional Meaning of Income and the Income Taxation of Gifts*, 25 CONN. L. REV. 1, 3 (1992).

¹⁰⁸ *Id.* at 4.

¹⁰⁹ See *id.* at 25–26.

¹¹⁰ *Id.*

¹¹¹ 252 U.S. 189 (1920).

¹¹² *Macomber*, 252 U.S. at 206–07; Kornhauser, *supra* note 107, at 9–10. The *Macomber* Court showed that the concept of income is not infinite. The Court stated:

A proper regard for [the Sixteenth Amendment] genesis, as well as its very clear language, requires also that this Amendment shall not be extended by loose construction, so as to repeal or modify, except as applied to income, those provisions of the Constitution that require an apportionment according to population for direct taxes upon property, real and personal. This limitation still has an appropriate and important function, and is not to be overridden by Congress or disregarded by the courts. . . . [I]t becomes essential to distinguish between what is and what is not “income” Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution, from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised.

Macomber, 252 U.S. at 206; see also Jensen, *supra* note 79, at 1144–45 (stating that while *Glenshaw Glass Co.* found *Macomber*’s definition of income to be too narrow in deciding that punitive damages were income even though they were not derived from labor or capital, *Macomber* still remains viable if interpreted to mean that a tax imposed on capital rather

*Merchants' Loan & Trust Co. v. Smietanka*¹¹³ and *Glenshaw Glass Co.*, this concept of income was broadened by application of the Constitution's intent to ultimately define income as all "accessions to wealth, clearly realized, and over which the taxpayers have complete dominion."¹¹⁴ Even though the seminal judicial decisions of *Macomber* and *Glenshaw Glass Co.* involved earlier versions of the statutory gross income provisions of the 1913, 1918, and 1939 Acts, the Court has held that the changes in the language from then until today do not change the analysis.¹¹⁵

Because recoveries for personal injury were a statutory exclusion from income from 1918 until 1996, the U.S. Supreme Court has not yet addressed the issue of whether compensatory damages, such as emotional distress recoveries, constitute income under the Sixteenth Amendment.¹¹⁶ The two most recent decisions of the U.S. Supreme Court involving taxation of discrimination both focused on statutory interpretation because the constitutional definition of income was not at issue.¹¹⁷

The opinions in *Burke*, *Schleier*, and *O'Gilvie* reaffirm the exclusion of emotional distress recoveries from income in a discrimination case or other tort-type case under the pre-1996 exclusion from income statute.¹¹⁸

than gain from capital is not a tax on income because *Macomber* survives statutorily under I.R.C. § 305(a) (2004) as to proportionate stock dividends). *Macomber* is still cited by the Supreme Court. See *Cottage Sav. Ass'n v. Comm'r*, 499 U.S. 554, 563 (1991); Jensen, *supra* note 75, at 709, 714 n.92.

¹¹³ 255 U.S. 509 (1921).

¹¹⁴ *Comm'r v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955); see *Smietanka*, 255 U.S. at 520 (holding that capital gains are income); see also *United States v. Burke*, 504 U.S. 229, 233 (1992); *James v. United States*, 366 U.S. 213, 219–20 (1961) (deciding that wrongful appropriations are income in the year received); Kornhauser, *supra* note 107, at 15–16.

¹¹⁵ *James*, 366 U.S. at 219 (claiming the changes in language are technical rather than substantive). This would also apply up until the present, as no significant changes were made to § 61(a) in 1986 or through today. See *Income Tax Law of 1913*, ch. 16, 38 Stat. 166; § 213(a), 40 Stat. 1057, 1065; see also Maule, *supra* note 5, at A-13.

¹¹⁶ See Hubbard, *supra* note 69, at 741.

¹¹⁷ See *Comm'r v. Schleier*, 515 U.S. 323, 328 (1995) (emphasizing that the taxpayer "concedes that his settlement constitutes gross income unless it is expressly excepted . . ."); see also *Burke*, 504 U.S. at 233 (stating "[t]here is no dispute that the settlement awards in this case would constitute gross income within the reach of [the statutory definition of income]"); Hubbard, *supra* note 69, at 743.

¹¹⁸ See *Burke*, 504 U.S. at 239, 241. In *Burke*, the Court stated:

No doubt discrimination could constitute a "personal injury" for purposes of § 104(a)(2) if the relevant cause of action evidenced a tort-like conception of injury and remedy. . . [such as] jury trials and for awards of compensatory and punitive damages . . . [W]e believe that Congress' decision to permit jury trials and compensatory and

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In *Burke* and *Schleier*, the Supreme Court stated in dicta that the intangible harms of discrimination are personal injuries.¹¹⁹ The Supreme Court case *O'Gilvie* implies in dictum that "damages that aim to substitute for a victim's physical or personal well being—personal assets that the Government does not tax and would not have taxed had the victim not lost them" are not income under the principle that a restoration of capital is not income.¹²⁰ The dicta in these cases can be used to predict that the U.S. Supreme Court would find an emotional distress recovery not to be income in a discrimination case, negating the need to address the recoveries under an exclusion from income statute.

V. OVERVIEW OF THE CIVIL RIGHTS MOVEMENT AND TORT REFORM AS IT PERTAINS TO PERSONAL INJURY REMEDIES

A. *The Three-Way Tension*

Since 1964, civil rights proponents have lobbied for broad compensatory relief, especially for emotional distress, but the business sector has lobbied against expansive compensatory relief due to the damage done to their bottom line profit.¹²¹ With the tension between civil rights and tort reform advocates and the added tension to preserve the government fisc, a balance between social and economic forces produced anti-discrimination statutes that offered inconsistent remedies.¹²²

B. *Civil Rights Remedies*

In 1964, the first generation of civil rights acts did not allow remedies for intangible harms, such as emotional distress.¹²³ The response was a second generation set of laws that offered broad compensatory remedies,

punitive damages under the amended Act signals a marked change in its conception of the injury redressable by Title VII "Monetary damages also are necessary to make discrimination victims whole for the terrible injury to their careers, to their mental and emotional health, and to their self respect and dignity."

Id. at 239–41, 239–41 n.12 (quoting, in part, H.R. REP. NO. 102-40, pt. 1, at 64–65 (1991), reprinted in 1991 U.S.C.C.A.N. 602, 603); see also *Schleier*, 515 U.S. at 332 n.6 ("We of course have no doubt that the intangible harms of discrimination can constitute personal injury, and that compensation for such harms may be excludable under § 104(a)(2).").

¹¹⁹ See *Schleier*, 515 U.S. at 332; *Burke*, 504 U.S. at 239.

¹²⁰ See *O'Gilvie v United States*, 519 U.S. 79, 86 (1996).

¹²¹ See Gerald A. Madek, *Tax Treatment of Damages Awarded for Age Discrimination*, 12 AKRON TAX J. 161 (1996).

¹²² *Id.* at 161–62.

¹²³ 42 U.S.C. §§ 2000e to 2000e-17 (2003) (Title VII of the Civil Rights Act of 1964); see also Madek, *supra* note 121, at 161.

including intangible harms such as emotional distress or liquidated damages.¹²⁴

The third generation of anti-discrimination laws provided for jury trials and a broad range of compensatory relief, which included emotional distress recoveries and punitive damages.¹²⁵ To curb this new wave of excludability from income, Congress stepped in to enact an amended § 104(a)(2) in 1996 to tax nonphysical personal injuries and to explicitly name discrimination claims as taxable, which includes the emotional distress recovery component.¹²⁶

C. Tort Reform Background

The civil rights era was also juxtaposed with massive tort reform at both the federal and state levels.¹²⁷ In the late 1960s, physician malpractice insurance premiums increased in response to a purported medical malpractice litigation crisis, which increased medical treatment costs.¹²⁸ In the 1970s, manufacturers' insurance rates surged due to an alleged overflow of products liability litigation.¹²⁹ In the 1980s, insurance companies refused to reissue policies to high-risk holders, asserting a general tort crisis.¹³⁰ By 1988, forty-eight states had participated in tort reform; forty-eight percent of these states imposing caps on the amounts recoverable, fifty-two percent attacking either the availability or amount of punitive damages, and twenty-one percent placing limits on noneconomic damages.¹³¹

The 1996 amendment to § 104(a)(2) came right during "this backdrop of developing congressional civil rights and tort reform legislation."¹³² "Congressional statements that 'substantial litigation' has occurred

¹²⁴ 42 U.S.C. §§ 3610-14 (1988). Section 3613(c) indicates that Title VIII of the Civil Rights Act of 1968 fair housing remedies are tort-like with jury trials and compensatory and punitive damages. 42 U.S.C. § 3613(c) (1988); *see also* The Age Discrimination in Employment Act, 29 U.S.C. §§ 621-34 (1999) (offering back pay and liquidated damages); Madek, *supra* note 121, at 171, 176 (asserting that liquidated damages often went undefined and thus could be labeled as either compensatory or punitive).

¹²⁵ *See* Civil Rights Act of 1991, Pub. L. No. 102-166, 105 Stat. 1071 (codified as amended in scattered sections of 42 U.S.C.); *United States v. Burke*, 504 U.S. 229, 234-35 (1992); *see also* Madek, *supra* note 121, at 179-80.

¹²⁶ *See* § 1605, 110 Stat. 1755, 1838, 1928-29; H.R. CONF. REP. NO. 104-737, at 300-02 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1677, 1792-94.

¹²⁷ *See* Wolff, *supra* note 57, at 1429.

¹²⁸ *Id.*

¹²⁹ *Id.*

¹³⁰ *Id.* at 1429-30.

¹³¹ *Id.* at 1430-31.

¹³² *Id.* at 1434.

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concerning cases not involving physical injury or physical sickness and that 'taxation . . . should not depend on the type of claim made,' clearly evidence legislative back door tort reform."¹³³

D. The Sexual Stereotypes of Emotional Distress Injury Must Be Dispelled

The forerunners of tort law were Trespass and Trespass on the Case.¹³⁴ In 1773, the distinction was made between whether the defendant intended or carelessly caused the harm. Trespass signified instances where the defendant directly caused the injuries to the plaintiff, and Trespass on the Case signified instances where the defendant indirectly caused the injury to the plaintiff.¹³⁵ Thus, the ancestor of negligence was the action of Trespass on the Case, "where the matter affected was not tangible or the injury was not immediate but consequential."¹³⁶

The English tort law then adopted the reasonable man standard in negligence actions,¹³⁷ which made the objective standard gender-biased.¹³⁸ At the time, nineteenth century England regarded women as emotional beings who were property and disenfranchised.¹³⁹

Thus, injury to emotions did not seem to constitute harm to the reasonable man.¹⁴⁰ This was seen most prominently in the early emotional distress decision of *Lynch v. Knight*.¹⁴¹ The *Lynch* case involved a defamation action, where Lord Wensleydale held that a husband suffers a monetary loss as a result of the loss of consortium of his wife, but that the wife suffers only emotional and mental injury from the loss of consortium of her husband.¹⁴² While this material/emotional

¹³³ *Id.* at 1437 (citing H.R. REP. NO. 104-586, at 142-44 (1996), reprinted in 1996 U.S.C.C.A.N. (110 Stat.) 1755, 1838-39); see Hubbard, *supra* note 69, at 745 (claiming that the reason why Congress limited this exclusion to physical personal injuries and physical sickness was not expressly stated in the Committee Reports, but speculation is that it was used as a tool for tort reform); see also Robert Cate Illig, *Tort Reform and the Tax Code: An Opportunity To Narrow the Personal Injuries Exemption*, 48 VAND. L. REV. 1459, 1461 (1995) (discussing the exclusion from 1918-1995).

¹³⁴ See Patrick Kelley, *Infancy, Insanity, and Infirmary in the Law of Torts*, 48 AM. J. JURIS. 179, 181 (2003).

¹³⁵ *Scott v. Shepherd*, 96 Eng. Rep. 525 (1773).

¹³⁶ 1 AM. JUR. 2D *Actions* § 23 (2003).

¹³⁷ *Vaughn v. Menlove*, 132 Eng. Rep. 490, 492 (1837); see also Wolff, *supra* note 57, at 1471.

¹³⁸ See Wolff, *supra* note 57, at 1471.

¹³⁹ *Id.* at 1476-77.

¹⁴⁰ *Id.*

¹⁴¹ See generally *Lynch v. Knight*, 11 Eng. Rep. 854, 863 (1861) (displaying the English Common Law sexual stereotypes).

¹⁴² *Id.*

dichotomy has been overturned by medical research that demonstrates that emotional and physical pain are not quantitatively different, victims of dignitary torts, such as discrimination, may still be stereotyped as weak and their emotional distress claims stereotyped as trivial.¹⁴³

This reasonable man gender bias may also be seen today in the intentional infliction of emotional distress cases.¹⁴⁴ In these cases, states often require the presence of physical illness or physical consequences, that the plaintiff must be placed in physical danger by the defendant's conduct, or that the plaintiff must show serious mental distress.¹⁴⁵

The emotional distress from the loss of dignity or other intangible harm in a nonphysical personal injury is as economically and socially important as physical personal injury, which now enjoys tax relief.¹⁴⁶ Reinstating nonphysical personal injury to a tax status equal to physical personal injury would again remove the reasonable man gender bias of the English common law concerning emotional distress.

The last vestiges of following the sexual stereotypes of the English common law system in our taxation of emotional distress recoveries need to be severed. Our U.S. Constitution, the tax doctrines found in reparation rights tax relief, and our U.S. Supreme Court cases require the conclusion that emotional distress recoveries are not income¹⁴⁷ because these recoveries are a return of human capital,¹⁴⁸ a mere restoration of civil or personal rights,¹⁴⁹ fall under the "in lieu of" test,¹⁵⁰ or fall under horizontal equity.¹⁵¹

¹⁴³ Wolff, *supra* note 57, at 1479-80.

¹⁴⁴ *Id.* at 1473; see also J. Martin Burke & Michael K. Friel, *Getting Physical: Excluding Personal Injury Awards Under the New Section 104(a)(2)*, 58 MONT. L. REV. 167, 184 (1997) (suggesting that the 1996 change to include in taxable income nonphysical personal injury recoveries was due to a fundamental distrust in the reality of emotional distress, or was done to establish a bright-line test for administrative convenience). Few tort reform proposals advocate eliminating emotional distress damages for intentional torts such as assault. However, most proposals criticize authorization of emotional distress damages where the claim is based primarily on negligence or strict liability torts. Thus, singling out nonphysical personal injuries as the avenue for tort reform is inconsistent with virtually all tort reform proposals. Hubbard, *supra* note 69, at 766 n.111.

¹⁴⁵ Wolff, *supra* note 57, at 1474.

¹⁴⁶ *Id.* at 1344.

¹⁴⁷ See *supra* Parts III.A-C, IV.F.

¹⁴⁸ See *supra* Part III.A.

¹⁴⁹ See *supra* Part III.B.

¹⁵⁰ See *supra* Part III.C.

¹⁵¹ See *supra* Part IV.F.

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E. *Dispelling the Sexual Stereotypes of Emotional Distress Injury Fosters Our Tort Reform and Civil Rights Movement*

Several commentators have remarked that taxable awards in discrimination cases have hindered the tort reform advocates' goal of limiting awards and claims.¹⁵² One commentator suggests that the taxability of awards in discrimination cases will prompt these discrimination claimants to seek higher monetary settlements to secure a fair settlement after taxation, with the employers bearing that increased cost.¹⁵³ Another commentator contends that the 1996 amendment taxing nonphysical personal injury cases will result in fewer negotiated settlements in employment discrimination and dignitary tort cases, causing more rather than less trials.¹⁵⁴ Yet another commentator postulates that jurors, knowing that these awards are taxable, will provide higher litigation awards, which in turn will lead to higher insurance premiums.¹⁵⁵ Finally, this author shows how the taxability of emotional distress recoveries in nonphysical personal injuries, such as discrimination cases, will cause litigation on constitutional grounds.

On the other hand, the proposed resurrection of the dual and equal exclusion for emotional distress recoveries in both physical and nonphysical personal injury and sickness claims dispels the sexual stereotypes from the English common law and allows emotional distress recoveries in nonphysical personal injury claims to be as economically or socially important as in physical personal injury claims.¹⁵⁶ This will also reinstate an equal protection of laws to ensure that emotional distress recoveries in nonphysical personal injury claims are treated as equal to physical personal injury claims.

Under the amended § 104(a)(2), emotional distress recoveries in nonphysical personal injuries are now taxable and therefore must be regarded as economic damages to sustain their taxability as income. However, under proposed federal tort reform, emotional distress

¹⁵² Carole N. Roche, *Recent Developement: Commissioner v. Schleier: Monetary Awards Resulting from Claims of Discrimination Under the Age Discrimination in Employment Act of 1967 ("ADEA") Are Not Excludable From Gross Income for Purposes of Income Taxation*, 26 U. BALT. L.F. 43, 45 (1995); see also Burke & Friel, *supra* note 144, at 188; John W. Dostert, *Commissioner v. Schleier: Adding Insult to "Personal Injury?"*, 74 N.C. L. REV. 1641, 1679, 1679 n.265 (1996).

¹⁵³ See Roche, *supra* note 152, at 45.

¹⁵⁴ See Burke & Friel, *supra* note 144, at 188.

¹⁵⁵ See Dostert, *supra* note 152, at 1679 n.265.

¹⁵⁶ See *supra* Part V.D.

recoveries are regarded as noneconomic damages.¹⁵⁷ Persons who are entitled to such recoveries now have these recoveries taxed as economic damages in nonphysical personal injuries even when tort reformers propose to limit emotional distress recoveries in medical malpractice cases as noneconomic damages. This inconsistency, defining emotional distress recoveries as economic damages for the purpose of taxation and then defining emotional distress recoveries as noneconomic damages for the purpose of limiting awards by tort reformers, cannot continue.

VI. CONCLUSION

As analyzed in Part III, the administrative history of personal injury rights and reparation rights recoveries provides precedent demonstrating that emotional distress recoveries are not income items. Thus, the use of the specific statutory exclusion from income, as discussed in Part II, is not necessary. This is because these recoveries have been held not to be income, as they constitute return of human capital or reimbursement for the loss of personal or civil rights.

The administrative history is based on court precedent. This court precedent, as illustrated in Part IV, is also founded upon the U.S. Constitution using rules of constitutional interpretation.

There appears to be no U.S. Supreme Court precedent that has reviewed the authority of Congress to define emotional distress recoveries as an income item in the constitutional sense or to tax emotional distress recoveries without apportionment. The dicta in *Burke*, *Schleier*, and *O'Gilvie* reaffirms that emotional distress recoveries are not income under the tax doctrines of the return of human capital, the reimbursement for the loss of personal or civil rights, or the "in lieu of" test. If emotional distress recoveries are not an income item in the constitutional sense, then Congress has no constitutional ability to place them in a taxable income category by statute or to tax them without apportionment.

In Part V, the resurrection of the dual and equal exclusion for emotional distress recoveries in both physical and nonphysical personal injury claims dispels the final vestiges of the sexual stereotypes found in the English common law. Further, the resurrection allows emotional distress recoveries in nonphysical personal injury claims to be as

¹⁵⁷ Catherine M. Sharkey, *Unintended Consequences of Medical Malpractice Damages Caps*, 80 N.Y.U. L. REV. 391, 512 nn.9, 22 (2005).

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economically and socially important as physical personal injury recoveries.

This resurrection also stops the inconsistent treatment of emotional distress recoveries, where tort reformers label these recoveries as noneconomic damages while Congress taxes these same recoveries under the guise of economic damages. The interests of human rights' and civil rights' advocates as well as the tort reformers can be merged by allowing a statutory exclusion for emotional distress recoveries in all personal injury and sickness claims.¹⁵⁸

This in turn will avoid litigation challenging the constitutionality of taxing emotional distress recoveries as an item of income. It will also avoid litigation challenging the taxation of emotional distress recoveries as a violation of the tax policy of horizontal equity, which is comparable to a violation of equal protection by failing to tax those similarly situated in a similar fashion.

Do Americans have the moral authority to punish international oppressors and terrorists that deny human rights and civil rights without affirming America's own commitment to civil rights? If the answer is no, then the solution requires reinstating the statutory, judicial, and administrative tax relief exclusions for emotional distress recoveries in nonphysical personal injury and sickness claims that existed in the United States from 1918–1996.

¹⁵⁸ See Luong, *supra* note 62, at 263 (proposing the political interest convergence theory "[b]ased on the premise that dominant culture constructs its social reality in ways that promote its own self-interests").