ANOTHER BIG ATTORNEYS' FEE CASE ON THE WAY

In the wake of *Estate of Arthur L. Clarks v.* US., Tax Analysts Doc No. 2000-1776, 2000 TNT 10-21 (6th Cir., Jan. 13, 2000), many practitioners are waiting to see what the IRS will do next. Watchers of this important area should know that another case is pending in the Ninth Circuit dealing with the attorneys' fee question. The pending case is *James T. Sinyard, et ux. v. Commissioner*, 9th Cir. Dkt. No. 99-71369. The Justice Department is arguing (not surprisingly) that a plaintiff must include in his gross income the contingent legal fee portion of a settlement. The underlying litigation arose out of two class action lawsuits against IDS Financial Services. The class actions involved age discrimination claims. The class plaintiffs signed contingency fee agreements with the law firm, calling for the firm to be paid one-third of any recovery. The agreement stated that any attorneys' fees awarded would be considered part of the plaintiff's total recovery.

Back in 1992, Mr. Sinyard received $862,900, of which $252,600 was allocable to attorneys' fees attributable to the taxable portion of his award. Sinyard simply netted the amount, not including the $252,600 in income on his 1992 tax return. The IRS determined a deficiency, and the matter wound up in Tax Court. The Tax Court held that the portion of the settlement proceeds attributable to attorneys' fees was includable in income, and only deductible as a miscellaneous itemized deduction. For the Tax Court decision, see Tax Analysts Doc. No. 98-29997, 98 TNT 195-10.

On appeal, the Ninth Circuit will have to decide whether the attorneys' fee portion of the settlement really belonged to Sinyard or not. Sinyard claims that the fee-shifting provisions in the Age Discrimination in Employment Act (ADEA), call for a reasonable attorneys' fee to be determined and awarded by the court *directly* to the attorneys.

The Justice Department, though, says that reliance on the ADEA provisions is misplaced. In this case, says the Justice Department, the attorneys' fees were paid in accordance with the terms of a settlement agreement. The ADEA provisions therefore don't control. According to the Justice Department, for the attorneys' fees to be paid under the ADEA, there must actually be a judgment for the plaintiffs in the case, and the district court must calculate the fee by making a lodestar computation. (This means that the court must determine the number of hours reasonably spent on the litigation, and multiply that figure by what the court determines is a reasonable hourly rate.)

Here, the court simply approved the settlement agreement providing for the payment of attorneys' fees in connection with the terms of the contingent fee agreements. Because the procedures under the ADEA were not followed, says the Justice Department, Sinyard would have to include this portion of his attorneys' fees in gross income.

We will wait to see what the Ninth Circuit does here. There has previously been a Ninth Circuit case suggesting that the Ninth Circuit will likely side with the government. See *Benci-Woodward, et al. v. Commissioner*, T.C. Memo 1998-395, Tax Court Dkt. No. 3769-96 (Nov. 9, 1998), now on appeal to the Ninth Circuit, 9th Cir. Dkt. Nos. 99-70136, 99-70137 and 99-70138 (filed May 4, 1999).

Note About Punitive Damages

The subject of punitive damages is not involved in the *Sinyard* case. Yet, think about the government's argument in the Ninth Circuit. Basically, it is arguing that since the attorneys' fees were not paid pursuant to a court order, the ADEA provisions cannot apply, and the attorneys' fees cannot be considered awarded pursuant to a court. Doesn't this same argument apply in the case of punitive damages? We've worried before that a court could take the position that punitive damages could be considered "awarded" merely because punitives were asked for in the complaint and the case was settled. Or, perhaps further along the chain of events, there might be a punitive damages award at trial which is then on appeal and the case is settled on appeal.

In both of these situations, the government has been taking the position that "punitive damages" have been paid. It seems to me that the position that the Justice Department is taking in the *Sinyard* case about the attorneys' fee provision could well work against the government (here, here!) when it comes to the punitive damages argument. Stay tuned for further information.