

SEX, RACE, AND AGE: DOUBLE DISCRIMINATION IN TORTS AND TAXES

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I. INTRODUCTION

It is truly uncommon when a tax statute casts off from its financial, economic, and accounting moorings in the Internal Revenue Code and sets sail in the murky waters and confusing undercurrents of American society's shifting social attitudes.¹ Section 104(a)(2), an octogenarian veteran of the Internal Revenue Code (Code),² is like such a seafaring vessel—heading upwind toward an emerging public policy that seeks to regulate private and public behavior in interpersonal relationships.

In its original form, this statutory provision excluded from income taxation all monetary damage awards for certain “personal injuries.”³ For approximately eighty years, the tax code afforded damages awarded on account of nonphysical personal injuries the same tax treatment as awards on

1. See Bertram Harnett, *Torts and Taxes*, 27 N.Y.U. L. REV. 614, 624 (1952) (“Personal injury claims are *sui generis* in the tax law for they have no customary commercial or investment connotations.”). The Internal Revenue Code (IRC or Code) has previously tread the waters of social policy in order to encourage action benefiting the public sector. See, e.g., I.R.C. § 23 (1998) (allowing personal credit for adoption expenses); I.R.C. § 117 (1998) (excluding qualified scholarships); I.R.C. § 127 (1998) (excluding educational assistance programs); I.R.C. § 131 (1998) (excluding certain foster care payments); I.R.C. § 170 (1998) (allowing deduction for charitable contributions and gifts to an organization); I.R.C. § 501(c)(3) (1998) (allowing exemptions for charitable organizations, including “[c]orporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes”); and I.R.C. § 501(i) (1998) (prohibiting racial and religious discrimination by certain social clubs by not allowing exemption to clubs that would otherwise qualify for exemption under § 501 but for their discriminatory policies). With one possible exception, Congress has not regulated relationships of a personal nature. See I.R.C. § 1041 (1998) (allowing for the nonrecognition of gain or loss in transfers of property between spouses).

2. I.R.C. § 104(a)(2) (1998) (codified as amended at 26 U.S.C. § 104(a)(2) (1998)). The section was originally codified as I.R.C. § 213(b)(6) in 1918. Revenue Act of 1918, § 213(b)(6), 40 Stat. 1057, 1065-66 (1919) (current version at 26 U.S.C. § 104(a)(2) (1998)).

3. Revenue Act of 1918, § 213(b)(6), 40 Stat. 1057, 1065-66 (1919) (current version at 26 U.S.C. § 104(a)(2) (1998)). The pertinent portion of this statute read as follows:

That for purposes of this title . . . the term “gross income”—

...

(b) Does not include the following items, which shall be exempt from taxation under this title:

...

(6) 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

Id.

account of personal physical injury.⁴ A brief hiatus between the enactment of § 213(b)(6), the precursor of § 104(a)(2), in the Revenue Act of 1918 and the *Solicitor's Opinion 132* in 1922 serves as the one exception.⁵ Only with the adoption of the Small Business Job Protection Act of 1996,⁶ did Congress limit the income tax exclusion to damages received from personal “physical” injuries or “physical” sickness.⁷

Nevertheless, today 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.⁸ 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.⁹

As the statute continues its rough passage through the rising swells of statutory, regulatory, and judicial interpretation, § 104(a)(2) could lose its bearings and wander off of its intended nondiscriminatory course. Society's

4. See 31 Op. Att'y Gen. 304, 308 (1918); I.R.C. § 104(a)(2) (1997); I.R.C. § 104(a)(2) (1996).

5. Sol. Op. 132, I-1 C.B. 92, 93, 94 (1922) (revoking Sol. Mem. 957, 1 C.B. 65, 65 (1919) (holding that amounts received in libel suit for damage were not within the statutory exemption without giving any guidance or analysis as to the holding) and Sol. Mem. 1384, 2 C.B. 71, 72 (1920) (holding that “the alienation of a wife's affections is not such a personal injury as to entitle the recipient of damages therefor to exemption [from income tax to the amount received]”)).

6. Pub. L. No. 104-188, 110 Stat. 1755 (codified as amended in scattered sections of 26 U.S.C.).

7. Small Business Jobs Protection Act of 1996, Pub. L. No. 104-188, § 1605, 110 Stat. 1755, 1838 (codified as amended at 26 U.S.C. § 104 (Supp. II 1996)). The pertinent revised part reads:

Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include—

...

(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness.

26 U.S.C. § 104 (Supp. II 1996).

8. See *infra* Part VI for more information on the medical and social scientific elements of nonphysical injuries. See also Louis E. Swanson et al., *African Americans in Southern Rural Regions: The Importance of Legacy*, 22 REV. BLACK POL. ECON. 109 (1994) (proposing that once discrimination negatively impacts the individual, the effects can spill over generationally).

9. See, e.g., H.R. REP. NO. 102-40, pt. 1, at 65-69 (1991), *reprinted in* 1991 U.S.C.C.A.N. 549, 603-07 (stating that as a result of sexual harassment and discrimination, women suffer from terrible humiliation, pain and suffering, psychological harm, sleeplessness, nausea, neck pains, nervousness, blotches and welts on legs and back, breathing difficulties, debilitating depression, gastro-intestinal disorder, weight loss, and may even encounter problems with pregnancy); S. REP. NO. 101-249, pt. 1, at 101 (1990) (stating that as a result of discrimination, older workers suffer from “psychological stress, including hopelessness, depression, . . . frustration,” and “physical, emotional, and psychological” problems that can shorten life span).

weakest groups are frequently the victims of nonphysical personal injuries and should possess the same inalienable rights to redress personal injury as historically enjoyed by dominant white males. Inequitable tax treatment based on the nonphysical nature of a victim's injuries is irrational, arbitrary, and without constitutional justification.

While the '50s provided a calm before the storm,¹⁰ the '60s cast our society into the turbulent seas of social and economic revolution, embracing both race and gender.¹¹ Spearheaded by the Warren Court¹² and the Civil Rights Act of 1964,¹³ the tempest of the sixties cleared the air and set the scene for major changes in the law.¹⁴ In the '70s American social

10. See William E. Nelson, *The Changing Meaning of Equality in Twentieth-Century Constitutional Law*, 52 WASH. & LEE L. REV. 3, 100 (1995) (concluding that *Brown v. Board of Education* sparked "goal-orientated" judgment and that not until the mid-60s did "rights-centered" adjudication become prevalent in the courtroom).

11. See, e.g., *Reitman v. Mulkey*, 387 U.S. 369, 370-73, 381 (1967) (ruling that an article within the California Constitution prohibiting the State from interfering with the absolute discretion of persons selling, leasing, or renting their home was unconstitutional because it involved the State in private racial discrimination); *McLaughlin v. Florida*, 379 U.S. 184, 184, 196 (1964) (determining that a Florida statute making it criminal for a black man and a white woman or a white man and a black woman to cohabit the same room at night if they were not married was invalid under the Equal Protection Clause of the Fourteenth Amendment).

12. See L. BRENT BOZELL, *THE WARREN REVOLUTION* 340 (1966) (concluding that "the Warren Era inaugurated a *revolution* in American jurisprudence"); JOHN D. WEAVER, *WARREN: THE MAN THE COURT THE ERA* 5 (1967) (stating that Warren's was the first, since the Marshall Court, to ring in "bold changes" affecting social, legal, and political structure). For a comprehensive historical background of the justices that presided on the Warren Court, see generally JOHN P. FRANK, *THE WARREN COURT* (1964).

13. Pub. L. No. 88-352, 78 Stat. 241 (codified as amended in scattered sections of 42 U.S.C.).

14. Before the 1964 Act came into existence, Congress sought to protect women financially with the passage of the Equal Pay Act of 1963 (EPA), 29 U.S.C. § 206(d) (1994). The Act was passed, in part, because of women's lower wage earnings, increasing employment, and rising divorce rate at the time, that made women, and sometimes their children, dependent on only one woman's earnings). See WALTER FOGEL, *THE EQUAL PAY ACT: IMPLICATIONS FOR COMPARABLE WORTH* 6 (1984). Civil rights protection, after the enactment of the 1964 Act, was next extended to the elderly. See Age Discrimination in Employment Act of 1967, Pub. L. No. 90-202, 81 Stat. 602 (codified as amended in scattered sections of 29 U.S.C.). The Age Discrimination in Employment Act (ADEA) was a natural succession of the Civil Rights Act of 1964 and the EPA. See JOSEPH E. KALET, *AGE DISCRIMINATION IN EMPLOYMENT LAW* 1-2 (2d ed. 1990). The Rehabilitation Act of 1973 finally allowed the disabled a means with which to redress discriminatory treatment at the national level. See Rehabilitation Act of 1973, Pub. L. No. 93-112, 87 Stat. 355 (codified as amended in scattered sections of 29 U.S.C.). Although the passage of the Rehabilitation Act of 1973 extended civil rights legislation to the disabled, its application was narrow because the scope of the statute only applied when government financed employers' perpetrated discrimination. See, e.g., 29 U.S.C. § 794 (1994). The Americans with Disabilities Act of 1990 (ADA) made the Rehabilitation Act more comprehensive by further extending protection to disabled individuals who were victimized by privately funded employers. See Americans with Disabilities Act of 1990, Pub. L. No. 101-336, 104 Stat. 327 (codified as amended at 42 U.S.C. §§ 12101-213 (1994)); 42 U.S.C. § 12112 (1994). Finally, with the enactment of the Civil Rights Act of 1991, victims of discrimination who brought their respective claims under Title VII, ADEA, or ADA were allowed to receive compensatory and punitive damages for wrongs suffered. See Civil Rights Act of 1991, Pub. L. No. 102-166, 105 Stat. 1071 (codified as amended in scattered sections of

consciousness became increasingly sensitive to economic disparity between races and genders, propelling these issues to the forefront of congressional policy and judicial action.¹⁵ Next, the self-interested '80s,¹⁶ known as the Decade of Greed, revealed the stress fractures caused by the social revolution of the '60s¹⁷ and by the progressiveness of the '70s.¹⁸ Indeed, the call for tort reform first emerged in the '80s,¹⁹ and it continues today to be an issue high on the agenda of many political groups.

Against the background of the civil rights struggle, this Article examines the eighty-year history of § 104(a)(2). The congressional purpose for the changes to § 104(a)(2) was to raise revenues needed to fund tax incentives created by the Small Business Job Protection Act of 1996. This Article attempts to uncover and elucidate the underlying reasons for the judicial interpretations and subsequent discriminatory amendments.²⁰

These conflicting claims set the debate over § 104(a)(2) against the background of society's emerging respect for the value and dignity of the person. Furthermore, it underscores the lack of legislative and judicial regard for the rights of the groups historically treated as barnacles on the hull of society: minorities, women, the elderly, and the disabled.²¹ More importantly,

42 U.S.C.).

15. See generally MYRA MARX FERREE & BETH B. HESS, *CONTROVERSY AND COALITION: THE NEW FEMINIST MOVEMENT ACROSS THREE DECADES OF CHANGE* (1994); ETHEL KLEIN, *GENDER POLITICS: FROM CONSCIOUSNESS TO MASS POLITICS* (1984).

16. See Robert G. Day, Note, *Administrative Watchdogs or Zealous Advocates? Implications for Legal Ethics in the Face of Expanded Attorney Liability*, 45 STAN. L. REV. 645, 669 (1993) (discussing the "decade of greed" as producing "the savings and loan debacle, the market crash of 1987, and financial scandals such as those involving Michael Milken and Ivan Boesky" and discussing how Congress passed the Securities Law Enforcement Remedies Act of 1990 in order to help "restore investor confidence in the integrity, fairness, and efficiency of the securities markets" which had been destroyed due to these financial scandals).

17. See generally Richard Delgado & Jean Stefancic, *The Social Construction of Brown v. Board Of Education: Law Reform and the Reconstructive Paradox*, 36 WM. & MARY L. REV. 547 (1995); Michael J. Klarman, *Brown, Racial Change, and the Civil Rights Movement*, 80 VA. L. REV. 7 (1994).

18. See generally ALBERT G. MOSLEY & NICHOLAS CAPALDI, *AFFIRMATIVE ACTION: SOCIAL JUSTICE OR UNFAIR PREFERENCE?* 4-12 (1996) (discussing the birth of the affirmative action revolution from the 1972 amendments to the Civil Rights Act of 1964 and Supreme Court decisions related to civil rights in the 1970s).

19. See James A. Henderson, Jr. & Theodore Eisenberg, *The Quiet Revolution in Products Liability: An Empirical Study of Legal Change*, 37 UCLA L. REV. 479 (1990).

20. For an alternate point of view on IRC history and discrimination, see J. Martin Burke & Michael K. Friel, *Getting Physical: Excluding Personal Injury Awards Under The New Section 104(a)(2)*, 58 MONT. L. REV. 167, 167 (1997) ("The 1996 amendments to § 104(a)(2) of the Internal Revenue Code are an understandable, but fundamentally incorrect, reaction to a statutory rule that was seen to have careened out of control with respect to nonphysical personal injuries.").

21. Although protection for these individuals has been established by passage of civil rights legislation, practices contrary to the spirit of these acts arguably persist. See, e.g., J. M. Balkin, *The Constitution of Status*, 106 YALE L.J. 2313, 2374 (1997) (concluding that "because law is a part of social structure, legal doctrines will usually be complicit in preserving status hierarchies even when

it uncovers preconceived false notions of nonphysical injuries— notions firmly attached to the seabed of a largely male, Caucasian, masculine-dominated judiciary and legislature. It dredges up the potent yet frequently unconscious prejudices that have conditioned the incongruous treatment of victims of personal injuries. Overall, this Article supports deliberate congressional action to ameliorate this discourant state of affairs.

This Article first provides the traditional scholarly survey of legislative history, statutory analysis, and governmental and judicial interpretations. Part II reviews the history of § 104(a)(2) and offers a substantive inquiry into the Supreme Court opinions in *United States v. Burke*,²² *Commissioner v. Schleier*,²³ and in the major cases leading up to these decisions. Part III then reviews the tax policy assumptions supporting § 104(a)(2) from a perspective of both before and after the 1996 amendments. Part IV chronicles the history and current status of various federally enacted civil rights statutes. This part then presents a historical overview of the emergence of tort reform at the federal and state levels—a reform in many ways diametrically opposed to that of civil rights legislation evolving and expanding the scope of protections and remedies. These two movements—civil rights and tort reform—elucidate the current status of § 104(a)(2). With respect to § 104(a)(2), tort reform takes place not in the traditional sense, Congress passing federal tort reform, but rather through the “back door”—tort reform in a taxing statute. Part V criticizes the judicial craftsmanship used in *United States v. Burke* and *Commissioner v. Schleier*.

Next, this Article departs from traditional legal analysis by examining the psychological, sociological, and economical consequences of the discrimination and arbitrary double standard that § 104(a)(2) imposes on the victims of nonphysical harm. In doing so, this Article studies socio-economic factors causing the evolution of § 104(a)(2) and employs relevant psychoanalytic and cognitive psychological theories. Part VI archives the well-documented negative psychological, physical, social, economical, and societal consequences that result from various forms of discrimination. Part VII applies psychoanalytic and cognitive theories of psychology to support the thesis that the 1996 amendment to § 104(a)(2) is a product of unconscious judicial and legislative discrimination. This Part also contains a

they claim to be dismantling them”); Reva Siegel, *Why Equal Protection No Longer Protects: The Evolving Forms Of Status-Enforcing State Action*, 49 STAN. L. REV. 1111, 1147-48 (1997) (“Once we appreciate that forms of status-enforcing state action we now deem morally reprehensible were once understood as morally defensible, it would seem to follow that we should evaluate the justifications for our current practices with a certain skepticism.”).

22. 504 U.S. 229 (1992).

23. 515 U.S. 323 (1995).

historic overview of the law of emotional distress that pertains to the current status of § 104(a)(2), especially when viewed under the psychoanalytic and cognitive theories of unconscious discrimination.

Finally, Part VIII concludes the Article, recommending that Congress take immediate action to remedy the tax discrimination leveled against victims of dignitary torts and raise revenues to support the exclusion by disallowing deductions for amounts paid to victims of discrimination by the tortfeasors.

In an effort to effectively influence the drafting of appropriate legislation, this Article will conclusively demonstrate that in the context of § 104(a)(2) there are no sustainable or well-founded tax or social policy justifications for treating victims of nonphysical injuries differently from those of physical injuries. Rather, broad social and congressional policy requires that victims of discrimination, in all its forms, be treated equally for tax purposes.

II. THE HISTORY OF § 104(a)(2)

The history of § 104(a)(2) presents an unusual account of a tax statute dealing not with familiar economic transactions but with interpersonal relations resulting in economic consequences. For the past eight decades, § 104(a)(2) has been the subject of inconsistent interpretation. Influenced by prevailing income definitions, public policy, accounting principles, and statutory interpretation, the Legislative, Judicial, and Executive (Treasury Department) Branches have fashioned various conflicting rationales justifying the general application and intent of § 104(a)(2). Sections A-L review the history of § 104(a)(2) offering a substantive examination of the major cases that played a role in shaping the current § 104(a)(2) exclusion for personal injury damages.

Section A lays out the events that lead to the enactment of § 213(b)(6), the predecessor of § 104(a)(2). Shortly before the enactment of § 213(b)(6) personal injury damage awards were purportedly excluded from income under a return of capital theory; the personal injury damage awards merely returned lost capital to the taxpayer. A mere return of lost capital could not be income under the prevailing definition at the time of these decisions because income was defined as derived from labor, capital, or a combination of both.²⁴ Moreover, Section A sets out two administrative opinions that narrowly interpret § 213(b)(6) as not providing an exclusion for damages from nonphysical personal injuries. The first decision, handed down in 1919,

24. *Stratton's Independence v. Howbert*, 231 U.S. 399, 415 (1913).

provides only the most general guidance.²⁵ The second decision, decided in 1920, applies the return of capital theory to disallow the exclusion for nonphysical personal injury damage awards.²⁶

Section B introduces two decisions, one from 1922,²⁷ and another from 1927,²⁸ which conclude that § 213(b)(6) allows the exclusion of damages for nonphysical injuries. Although these decisions favored plaintiffs who had received damages for nonphysical injuries, the decisions did not apply § 213(b)(6) and greatly misapplied, confused, and entangled the concept of income and human capital in reaching their respective conclusions.

Section C tracks the major § 104(a)(2) decisions from 1928 up until the Supreme Court's decision in *Glenshaw Glass v. Commissioner*.²⁹ Generally, these decisions dealt with injury to business rather than injury to an individual. Taxpayers could exclude damages as outside the concept of income under various theories—the return of capital theory, injury to personal rights theory, or the windfall theory. However, the courts once again failed to focus on the statutory language of § 213(b)(6). A 1944 decision articulated a new test for determining the taxability of business recoveries, phrased by the court as the “in lieu of what” test.³⁰ Under this test, if the damages took the place of lost capital, they were excluded from income. Courts continued to apply this test into the ‘80s.

Section D introduces *Glenshaw Glass* in which the Supreme Court redefined the concept of income.³¹ Income ceased to be narrowly defined as derived from labor, capital, or a combination of both. Rather, income became any “undeniable accessions to wealth, clearly realized, and over which the taxpayer [had] complete dominion [and control].”³² Thus, *Glenshaw Glass* broadly defined “income,” requiring taxpayers to qualify under a specific statutory exemption in order to exclude accessions to wealth. Finally, the decision in *Glenshaw Glass* compelled courts to analyze, interpret, and apply the § 104(a)(2) statutory exclusion in the personal injury context. Thereafter, because of the favorable tax treatment of damages for personal injuries, taxpayers sought to frame causes of action in tort law, even if those causes of action were also grounded in contract law. As a result, for the next forty-seven years, the Tax Court and the circuit courts of appeals would develop

25. Solicitor's Memorandum 957, 1 C.B. 65 (1919).

26. Solicitor's Memorandum 1384, 2 C.B. 71 (1920).

27. Solicitor's Opinion 132, 1-1 C.B. 92 (1922).

28. *Hawkins v. Comm'r*, 6 B.T.A.M (P-H) 1023 (1927).

29. 348 U.S. 426 (1955).

30. *Raytheon Prod. Corp. v. Comm'r*, 144 F.2d 110, 113 (1st Cir. 1944).

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

32. *Id.* at 431.

four innovative tests to filter out claims purportedly undeserving of the § 104(a)(2) exclusion. Sections E through H examine each one of these four tests.

Section E presents the first test used, beginning in 1961, to filter out undeserving claims under § 104(a)(2)—the “intent of the payor” test.³³ In applying this test courts looked to the complaint and the defendant’s statements made in the underlying case to determine whether the defendant transferred money to the plaintiff to redress contractual breaches or tortious injuries. If evidence indicated that the defendant intended the award to remedy a breach of contract, the taxpayer could not exclude the damages from income. If the evidence proved that the defendant intended the award to account for tortious injury, the taxpayer could exclude the damages from income.

Section F describes the test that the courts began using in 1972 to weed out meritless claims under § 104(a)(2)—the “nature of the claim” test.³⁴ Under this test, if the damages claimed were of a personal nature, the taxpayer could properly exclude the damage award from income.

Section G introduces the “tort or tort-type” test,³⁵ first used in 1980. Under this inquiry, the taxpayer could exclude awards under § 104(a)(2) only if the damage award redressed a tort or tort-type injury. The tort or tort-type test originated from the language of Treasury Regulation 1.104-1(c) which states that “damages received . . . means an amount received . . . [from an] action based on tort or tort-type rights.”³⁶ The tort or tort-type test would gain prominence in future § 104(a)(2) decisions. In fact, the first § 104(a)(2) Supreme Court decision, *United States v. Burke*, applied this test and denied the § 104(a)(2) exemption to a plaintiff seeking to exclude back pay received under Title VII of the Civil Rights Act of 1964 (Title VII) from income.³⁷

Section H presents “predominant nature of the claim” test, first emerging in 1982.³⁸ Under this test, income did not include an award based upon a claim whose predominant nature redressed personal injuries. This test notably diminished the influence of the intent of the payor test.

Section I discusses the historical underpinnings of the courts’ decisions to begin setting concrete principles with respect to § 104(a)(2). Section I first tracks the resurgence of the “nature of the claim” test in the 1983 Court of

33. *Agar v. Comm’r*, 290 F.2d 283 (2d Cir. 1961).

34. *Seay v. Comm’r*, 58 T.C. 32 (1972), *acquiesced*, 1972-2 C.B. 3 (1972).

35. *Whitehead v. Comm’r*, 41 T.C.M. (CCH) 365 (1980).

36. *Treas. Reg. § 1.104-1(c)* (1998).

37. 504 U.S. 229 (1992).

38. *Nussbaum v. Comm’r*, 45 T.C.M. (CCH) 346 (1982).

Appeals for the Ninth Circuit case, *Roemer v. Commissioner*.³⁹ The Ninth Circuit stressed that the nature of the injury must not be defined by the effect of the injury. Section I then discusses the 1986 Tax Court decision, *Threlkeld v. Commissioner*.⁴⁰ In *Threlkeld*, the judiciary accepted four major points as settled law. First, the excludability of the award is dependant upon the nature of the claim and not upon the validity of the claim.⁴¹ Second, no distinction is to be made between physical and nonphysical injury.⁴² Third, no distinction should be made between damages received for injury to professional reputation and damages received for injury to personal reputation.⁴³ Finally, the determination of “whether the damages received are paid on account of ‘personal injuries’ should be the beginning and the end of the inquiry.”⁴⁴

Section J establishes the 1989-1991 case law foundation for § 104(a)(2), where all major cases dealt with awards in connection with Title VII⁴⁵ and the Age Discrimination in Employment Act of 1967 (ADEA) claims.⁴⁶ Here, the decisions sharply depart from the concrete principles set out in *Roemer* and *Threlkeld* for determining whether damages could be excluded under § 102(a)(2).⁴⁷

Section K contains the § 104(a)(2) Supreme Court decisions of *United States v. Burke*,⁴⁸ decided in 1992, and *Schleier v. Commissioner*,⁴⁹ decided in 1995. This Section shows how these cases dramatically departed from prior Tax Court and court of appeals’ case analyses.⁵⁰

39. 716 F.2d 693 (9th Cir. 1983).

40. 848 F.2d 81 (6th Cir. 1988).

41. See *Threlkeld v. Comm’r*, 87 T.C. 1294, 1297 (1986) (citing *Bent v. Comm’r*, 87 T.C. 236 (1986); *Glynn v. Comm’r*, 76 T.C. 116, 119 (1981); *Seay v. Comm’r*, 58 T.C. 32, 37 (1972)).

42. See *Threlkeld*, 87 T.C. at 1297 (citing *Seay*, 58 T.C. at 40). The regulations stated that an “[a]mount received as the result of a suit or compromise for personal injury, being similar to the proceeds of accident insurance, is to be accounted for as income.” *Id.*

43. See *id.* at 1298.

44. *Id.* at 1299.

45. Civil Rights Act of 1964, §§ 701-716 (codified as amended at 42 U.S.C. §§ 2000e-2000e-15 (1994 & Supp. II 1996)).

46. Pub. L. No. 90-202, 81 Stat. 602 (codified as amended in scattered sections of 29 U.S.C.).

47. For more information on the effect of the Civil Rights Act and the ADEA on the *Roemer* and *Threlkeld* decisions, see *infra* Part IV. The judiciary decided these cases during a period when Congress was in the process of enacting the ADA and the Civil Rights Act of 1991. Tort reform was high on federal and state political agendas, and evidence shows that judicial tort reform caused departure from the § 104(a)(2) principles articulated in *Roemer* and *Threlkeld*. More importantly, these taxpayers in these decisions are the very same individuals to whom Congress attempts to extend further civil rights protections.

48. 504 U.S. 229 (1992).

49. 515 U.S. 323 (1995).

50. For an in-depth critique of the *Burke* and *Schleier* decisions, see *infra* Part V, that shows how the Supreme Court in *Burke* twisted, and in *Schleier* trivialized, the tort or tort-type test to come to decisions that dignified victims of dignitary torts.

Section L first discusses the 1989 attempt to amend § 104(a)(2) to disallow the exclusion of punitive damage awards from income if the injury in the underlying case was nonphysical. Next, this Section discusses the 1995 congressional attempt to limit the § 104(a)(2) exclusion to damages on account of physical injury or sickness.

Finally, Section M concludes by discussing the passage of the 1996 amendments to § 104(a)(2) that limited the exclusion to damages on account of physical injury or sickness. As will be demonstrated in Part III, no tax policy supports the current distinction made in § 104(a)(2).

A. Section 213(b)(6): The Early Years

1. The Income Tax Act of 1913 and the Enactment of § 213(b)(6)

Ratified in 1913, the Sixteenth Amendment to the U.S. Constitution provided the foundation for imposing federal income tax upon individuals and corporations.⁵¹ When Congress enacted the Income Tax Act of 1913, it did not provide an exclusion from income for damage awards resulting from personal injuries.⁵² In 1915, the Treasury issued *Treasury Decision 2135* which indicated that “an amount received as a result of a suit or compromise for ‘pain and suffering’ is held to be such income as would be taxable under the provision of law that includes ‘gains or profits and income derived from any source whatsoever.’”⁵³ Although *Treasury Decision 2135* did not deal generally with damage awards, it did foreshadow what would become the Treasury’s early position on such receipts. Treasury Regulation 33, issued under the Revenue Acts of 1916 and 1917, specifically required taxation of such damage awards.⁵⁴

51. U.S. CONST. amend. XVI (“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.”). The sixty-first Congress proposed to the state legislatures the Sixteenth Amendment to the United States Constitution on July 12, 1909, and it was ratified by thirty-six states by February 25, 1913. See BORIS I. BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES, AND GIFTS § 1.1.3 (3d ed. 1999). Income taxes had been levied previously during the Civil War, both by the Union and the Confederacy. *Id.* § 1.1.2. However, the federal government relied primarily on customs receipts, excise taxes, and the sale of land for revenues. See *id.* § 1.1.2. See also *Pollock v. Farmers’ Loan & Trust Co.*, 157 U.S. 429, 580-81, 583 (1895) (holding income tax of 1894 unconstitutional); *Springer v. United States*, 102 U.S. 586, 602 (1880) (upholding a civil war income tax).

52. Law of October 3, 1913, ch. 16, 38 Stat. 114, 166-81 (1915). The federal income tax produced \$35 million in revenues in its first fiscal year. See BITTKER & LOKKEN, *supra* note 51, § 1.1.1. See also *Brushaber v. Union Pacific R.R.*, 240 U.S. 1, 17-18 (1916) (upholding the constitutionality of the Income Tax Law of 1913).

53. T.D. 2135, 17 Treas. Dec. Int. Rev. 39, 42 (1915).

54. Treas. Reg. No. 33, revised, pt. I (1918). See also T.D. 2690, 20 Treas. Dec. Int. Rev. 126

In 1918, the Attorney General opined that individuals could exclude from taxation accident insurance proceeds received on account of personal injury.⁵⁵ In reaching this decision, the Attorney General first looked to the language of the Revenue Act of 1916, as amended by the Revenue Act of 1917, and concluded that no explicit exemptions or deductions applied to insurance proceeds from accidents.⁵⁶ The question therefore became whether “the proceeds of an accident insurance policy [are] ‘gains or profits and income’ according to the principles . . . laid down by the Supreme Court?”⁵⁷

In order to resolve the issue, the Attorney General⁵⁸ initially looked to the Supreme Court decisions in *Stratton’s Independence v. Howbert*,⁵⁹ which held that income was “gain derived from capital, from labor, or from both combined,”⁶⁰ and in *Doyle v. Mitchell Brothers Company*,⁶¹ which held that income was “something entirely distinct from principal or capital.”⁶² Next, the Attorney General examined the Supreme Court decisions of *Lynch v. Hornby*,⁶³ *Lynch v. Turrish*,⁶⁴ and *Southern Pacific Company v. Lowe*⁶⁵ for further interpretive direction on the issue.⁶⁶ The Attorney General found that these cases stood for the proposition that stock dividends are income except where the “final dividend [is] paid from the proceeds of sale of the entire capital assets of a corporation, and . . . [where the final dividend is] a mere readjustment of a capital indebtedness.”⁶⁷

In light of these Supreme Court opinions, the Attorney General contended that under general tax principles, amounts which restore capital must be withdrawn from gross receipts when figuring tax liabilities.⁶⁸ To further support this contention, the Attorney General looked beyond the Supreme Court’s language to dicta in the decision of the Court of Appeals for the Sixth

(1918). The regulations stated that an “[a]mount received as the result of a suit or compromise for personal injury, being similar to the proceeds of accident insurance, is to be accounted for as income.” Treas. Reg. No. 33, *supra*, at 130.

55. 31 Op. Att’y Gen. 304 (1918).

56. *See id.* at 304-05.

57. *Id.* at 307 (citing *Lynch v. Hornby*, 247 U.S. 339, 344 (1918); *S. Pac. Co. v. Lowe*, 247 U.S. 330, 335-39 (1918); *Lynch v. Turrish*, 247 U.S. 221, 230-31 (1918); *Stratton’s Independence v. Howbert*, 231 U.S. 399, 415 (1913)).

58. 31 Op. Att’y Gen. 304, 305 (1918).

59. 231 U.S. 399 (1913).

60. *Id.* at 415.

61. 247 U.S. 179 (1918).

62. *Id.* at 185.

63. 247 U.S. 339 (1918).

64. 247 U.S. 221 (1918).

65. 247 U.S. 330 (1918).

66. 31 Op. Att’y Gen. 304, 306-07 (1918).

67. *Id.* at 307.

68. *Id.* at 306.

Circuit in *Doyle v. Mitchell Brothers Company*.⁶⁹ In that case, the Sixth Circuit discussed the characterization of fire insurance money and found that the characteristics of these proceeds substituted for destroyed capital.⁷⁰ Finding no difference between fire insurance and casualty insurance, the Attorney General compared the burned house to destroyed human ability and concluded that “[w]ithout affirming that the human body is in a technical sense the ‘capital’ invested in an accident policy,” accident insurance proceeds were not taxable income but “merely take the place of *capital in human ability* . . . destroyed by the accident.”⁷¹ Because the damages are deemed to equal the lost capital, the damage award was excludable from income.⁷²

This line of reasoning excluding damages from income became known as the “human capital” or “return of capital” theory.⁷³ The Attorney General could have surpassed the finding in *Stratton’s Independence*—that income is “derived from capital, from labor, or from both combined”⁷⁴—to hold that the human body is not, even in the technical sense, the “capital” invested in an accident policy. Such a holding would insure no derivation of income from either capital or labor present upon receipt of accident proceeds. Under this alternative line of reasoning, insurance awards would be excluded from income in accordance with *Stratton’s Independence*.

Within a month of *31 Opinion Attorney General 304*, the Treasury in *Treasury Decision 2747*,⁷⁵ revised its initial position on Regulation 33. *Treasury Decision 2747* held that money received from either a personal injury, judgment, or settlement is sufficiently similar to accident insurance proceeds to be considered income.⁷⁶ This decision also supported *Stratton’s Independence*.⁷⁷ Like the Attorney General’s opinion, the Treasury decision acknowledges four Supreme Court decisions including *Doyle v. Mitchell Bros. Co.*, *Lynch v. Hornby*, *Lynch v. Turish*, and *Southern Pacific Co. v. Lowe*. The Treasury decision even went so far as to revoke any “provisions of treasury decisions and of regulations No. 33, revised, as are inconsistent herewith.”⁷⁸ The Treasury decision mentions neither the Sixth Circuit’s dicta

69. 235 F. 686 (6th Cir. 1916).

70. *See id.* *See also* 31 Op. Att’y Gen. 304, 307-08 (1918).

71. *Doyle*, 235 F. at 308.

72. *See id.*

73. For more information on these theories, see *infra* Part III.H.

74. 231 U.S. 399, 415 (1913).

75. T.D. 2747, 20 Treas. Dec. Int. Rev. 457 (1918).

76. *See* Treas. Reg. No. 33, pt. I (as amended in 1918).

77. *See* T.D. 2747, 20 Treas. Dec. Int. Rev. 457 (1918).

78. *Id.*

in *Doyle* nor the human capital theory.⁷⁹ Arguably, one cannot determine from this decision whether the Treasury bought into the Attorney General's human capital argument or whether it only agreed with the Attorney General's result, and instead, based its conclusion on *Stratton's Independence*.

Later that same year, upon request of the Treasury, Congress enacted § 213(b)(6) when it passed the Revenue Act of 1918.⁸⁰ Section 213(b)(6) excluded from gross income "[a]mounts 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."⁸¹ The Treasury hoped that the codification of this exclusion would earmark a clearer rule for taxpayer liability on amounts received related to personal damages.⁸² However, early interpretations of § 213(b)(6) wavered on what exact amount taxpayers could exclude from physical and nonphysical personal injury awards.

2. Early Interpretation of § 213(b)(6)

Without providing any guidance,⁸³ *Solicitor's Memorandum 957*, handed down in 1919, narrowly interpreted § 213(b)(6) as not providing an exclusion from income damage awards received in liable proceedings.⁸⁴ Then a 1920

79. *Id.*

80. Revenue Act of 1918, ch. 18, 40 Stat. 1057 (1919).

81. *Id.* at 1065-66.

82. Under the plain language of § 213(b)(6), "any damages received . . . on account of such injuries" were excludable.

83. See Douglas K. Chapman, *No Pain—No Gain? Should Personal Injury Damages Keep Their Tax Exempt Status?*, 9 U. ARK. LITTLE ROCK L.J. 407, 413-14 (1987) (stating that "[u]nfortunately, on the actual expression of intent, the silence of Congress is deafening"). The only reference to I.R.C. § 213 (b)(6) is contained in H.R. REP. NO. 65-767, at 9-10. See Patrick E. Hobbs, *The Personal Injury Exclusion: Congress Gets Physical but Leaves the Exclusion Emotionally Distressed*, 76 NEB. L. REV. 51, 65 (1997). The House Report states:

Under the present law it is doubtful whether amounts received through accident or health insurance, or under workman's compensation acts, as compensation for personal injury or sickness, and damages received on account of such injuries or sickness, are required to be included in gross income. The proposed bill provides that such amounts shall not be included in gross income.

H.R. REP. NO. 65-767, at 9-10. See Burke & Friel, *supra* note 20, at 168 (stating that the legislative history did not articulate any policy towards providing an exclusion from income damages received as a result of nonphysical injuries). But see Daniel Candee Knickerbocker, Jr., *The Income Tax Treatment of Damages: A Study in the Difficulties of the Income Concept*, 47 CORNELL L.Q. 429, 431 (1962) (stating that the committee reports that accompanied the statute led one to believe that damages as a result of physical injuries were solely to be exempt under the statute).

84. See Sol. Mem. 957, 1 C.B. 65, 65 (1919). According to Knickerbocker, since the committee

opinion, *Solicitor's Memorandum 1384*, held that “[t]he alienation of a wife’s affections is not such a personal injury as to entitle the recipient of damages therefor to exemption” from income tax for the amount received.⁸⁵ The Solicitor acknowledged that legally the alienation of a wife’s affections constitutes a personal injury.⁸⁶ Notwithstanding this statement, the Solicitor determined that the legislative history of § 213(b)(6) makes “it appear[] more probable” that the term personal injuries meant physical injuries.⁸⁷

Solicitor's Memorandum 1384 then completely abandoned the personal injury analysis used in *Solicitor's Memorandum 957* and applied the human capital (conversion of capital) theory.⁸⁸ While the Solicitor recognized that insurance policy proceeds may represent a conversion of capital lost through injury, the Solicitor also found that “[f]rom no ordinary conception of the term can a wife’s affections be regarded as constituting capital.”⁸⁹ As a result of both the Solicitor’s resort to the human capital analysis and belief that personal injuries include only physical injuries, the taxpayer could only claim an exclusion if the alienation manifested itself as a physical sickness under § 213(b)(6).⁹⁰ This distinction provided the earliest criterion for the physical and nonphysical dichotomy.

B. The Confusion Sets In: Solicitor’s Opinion 132 and Hawkins

The executive interpretations limiting the gross income exclusion to physical, personal injuries was short-lived. Subsequent executive opinions soon thereafter reincorporated the exclusion for nonphysical damage awards, albeit in a confusing and inconsistent manner. In the 1922 decision of *Solicitor's Opinion 132*, the Solicitor faced the issue of whether damages for alienation of affection, slander or libel of a personal character, and surrender of a minor child’s custody were excludable from income.⁹¹ Interestingly,

report accompanying § 213 (b)(6) led one to believe that the exclusion applied to damages on account of physical injuries, the Solicitor must have based his decision on the committee reports. Knickerbocker, *supra* note 83, at 431. See I.T. 1852, II-2 C.B. 66, 66 (1923) (stating that money received in action for annulment of marriage based upon fraud and deceit was not taxable); Sol. Mem. 1384, 2 C.B. 71, 72 (1920) (referencing § 213(b)(6) of the Revenue Act of 1918 as being “declarative of the conclusions” stated in *Treasury Decision 2747*).

85. Sol. Mem. 1384, 2 C.B. 71, 72 (1920).

86. *Id.* at 71 (citing *Leicester v. Hoadley*, 71 P. 318 (Kan. 1903)). See also *Tinker v. Colwell*, 193 U.S. 473, 487 (1904).

87. Sol. Mem. 1384, 2 C.B. at 71.

88. See *id.* at 71-72.

89. *Id.* at 72.

90. See *id.* at 71-72.

91. Sol. Op. 132, I-1 C.B. 92, 92-93 (1922) (modifying *Solicitor's Memorandum 957* and revoking *Solicitor's Memorandum 1384*).

Solicitor's Opinion 132 did not base its holding on the newly enacted § 213(b)(6) exclusion but rather, focused on the definition of income as articulated by the Supreme Court in *Eisner v. Macomber*⁹² and *Stratton's Independence*.⁹³ Thus, *Solicitor's Opinion 132* found that income is "derived from capital, from labor, or from both combined."⁹⁴

The Solicitor concluded that "no gain, and therefore no income, derived from the receipt of damages for alienation of affections or defamation of personal character . . . [or] money received in consideration of the surrender of the custody of a minor child" falls under the *Eisner* and *Stratton's Independence* definition of income.⁹⁵ According to the Solicitor, an individual derives neither gain nor profit from damages received for injury to personal, intangible, nonassignable, and nonappraisable rights.⁹⁶ The Solicitor believed that an invasion of a nontransferable personal right exists in the cases of alienation of affection, defamation of personal character, and surrender of a minor child's custody.⁹⁷ Invaded rights of this type cannot be accurately reduced to a monetary value because the violated rights and the monetary awards "can not be placed on opposite sides of an equation."⁹⁸ Therefore, damages received for alienation of affection, defamation of personal character, or surrender of a minor child's custody cannot be included as income under *Eisner* and *Stratton's Independence*.⁹⁹

Under closer inspection, the Solicitor's line of reasoning transcended *Eisner* and *Stratton's Independence* concept of gross income to include a new group of noneconomic personal rights, the damage or invasion of which cannot result in either gain or profit. To this end, *Solicitor's Opinion 132*

92. 252 U.S. 189 (1920).

93. *Sol. Op. 132*, I-1 C.B. at 93 (1922); *Eisner*, 252 U.S. at 207; *Stratton's Independence v. Howbert*, 231 U.S. 399, 415 (1913).

94. *Sol. Op. 132*, I-1 C.B. at 93.

95. *Id.* at 93-94 (superseded by Rev. Rul. 74-77, 1974-1 C.B. 33) (reiterating that damages received for alienation of wife's affections and custody of a minor child were non taxable). The Solicitor could have simply concluded that such damages were not derived from either capital or labor, or both combined. Instead, the Solicitor justified his conclusion under *Eisner* and *Stratton's Independence*.

Before applying the case facts, under *Eisner* and *Stratton's Independence*, the Solicitor noted that the end result in *Solicitor's Memorandum 1384* is correct. Moreover, the end result in *Solicitors Memorandum 957* may have been correct in a situation where a libel action is brought to redress defamation of personal character. *See id.* at 93. The Solicitor also stated that the *Solicitor's Memorandum 957* holding was not confined to the specific case facts "but apparently applied to libel generally . . . [though] Slander or Libel affecting business reputation or property rights . . . [were] not considered in this opinion." *Id.* at 93-94.

96. *Sol. Op. 132*, I-1 C.B. at 93.

97. *Id.* at 93-94.

98. *Id.* at 93.

99. *See id.* at 93-94.

implicitly discussed the return of capital theory, initially considered in *31 Opinion Attorney General 304*. The Solicitor characterized damages for alienation of affection, defamation of personal character, and surrender of a minor child's custody as monetary awards that attempt to *replace* a loss that is nontransferable and not susceptible of any appraisal. At the same time, therefore, the Solicitor concluded that damages for nontransferable personal rights violations could not be included as income under *Eisner* and *Stratton's Independence*, the Solicitor also applied the human capital theory, which included such damages as capital gains and therefore income under *Eisner* and *Stratton's Independence* but would ultimately exclude such damages because the total receipts were equivalent to the loss of capital incurred by the nontransferable, personal rights violations. Thus, at first glance, *Solicitor's Opinion 132* seems to move away from the human capital theory, but upon closer investigation it augments the initial human capital theory in *31 Opinion Attorney General 304*.

Following *Solicitor's Opinion 132*, the Board of Tax Appeals (BTA), in *Hawkins v. Commissioner* endorsed *Solicitor's Opinion 132's* inconsistent analysis.¹⁰⁰ In *Hawkins*, the board of directors voted to remove the company president and published statements defaming him.¹⁰¹ The ex-president then sued both the company and the individual board members for libel and slander.¹⁰² The case settled prior to trial.¹⁰³ The IRS declared the ex-president's award to be gross income and assessed a deficiency for the full amount of the settlement.¹⁰⁴ The BTA reversed and held that character and reputation, as personal attributes, could not be "capital or otherwise measurable,"¹⁰⁵ and therefore could not fall within the definition of income articulated by the *Eisner* Court. Nevertheless, the BTA needlessly and inconsistently applied the return of capital theory, reasoning that "[s]uch compensation as general damages adds nothing to the individual, . . . [and] is an attempt to make the plaintiff whole as before the injury."¹⁰⁶ The BTA thus

100. 6 B.T.A.M. (P-H) 1023, 1024 (1927).

101. *Id.* at 1023.

102. *Id.*

103. *Id.*

104. *See id.*

105. 6 B.T.A.M. (P-H) at 1025.

106. *Id.* *See also* Knickerbocker, *supra* note 83, at 434 (stating that "*Hawkins* also stands for the proposition that only compensatory damages do not represent income"). Interestingly, the Board of Tax Appeals failed to mention or rule upon the taxpayer's allegations of damage to his business reputation. The Board and the Solicitor chose to side step the issue, perhaps leaving the matter to a congressional resolution, which never occurred. For related decisions following *Hawkins*, see I.T. 2420, VII-2 C.B. 123 (1928) (holding insurance payment to widow on account of death of husband was compensation for loss of life not encompassed by the concept of income); *McDonald v. Comm'r*, 9 B.T.A.M. (P-H) 1340 (1928) (finding payments based upon breach of contract to marry are not

perpetuated the confusion concerning the application of the human capital rationale—first evident in *Solicitor's Opinion 132*—in addition to making no reference to § 213(b)(6) and departing from the confines of *Eisner*.

In 1928, the Treasury acquiesced to *Hawkin's*¹⁰⁷ analysis. Subsequently, numerous decisions allowed the exclusion of damages received for physical and nonphysical personal injuries under different theories: awards as a combination of either return of capital or injury to personal rights or awards as a windfall consequently outside the concept of income.¹⁰⁸ These

income). Professor Dodge puts a different spin on the early conception of income, stating that “the original concept of gross income excluded nonregular receipts, such as windfalls.” Joseph M. Dodge, *Taxes and Torts*, 77 CORNELL L.R. 143, 150 (1992). See Douglas A. Kahn, *Compensatory and Punitive Damages for a Personal Injury: To Tax or Not to Tax*, 2 FLA. TAX REV. 327 (1994). Khan states:

The exclusion of damages for nonphysical injuries thus was initially grounded on construction of the term ‘income’ (as employed in the Revenue Acts) rather than on the statutory antecedent to section 104(a)(2) Indeed, it was some 45 years later that the courts and the Service held that the statutory exclusion of damages for personal injuries applied equally to physical and nonphysical injuries.

Id. at 332.

107. See VII-1 C.B. 14 (1928).

108. See *Raytheon Prod. Corp. v. Comm’r*, 144 F.2d 110, 114 (1st Cir. 1944) (finding damages not taxable according to the return of capital theory); *Cent. R. Co. of N.J. v. Comm’r*, 79 F.2d 697, 699 (3d Cir. 1935) (finding value of property received in settlement of an action in equity was not income because “what . . . [the taxpayer] received was in the nature of a windfall”); *Farmers’ & Merchants’ Bank v. Comm’r*, 59 F.2d 912, 913-14 (6th Cir. 1932) (allowing an exclusion under an injury to business and return of capital theory); *Highland Farms Corp. v. Comm’r*, 42 B.T.A.M. (P-H) 1314, 1322 (1940) (finding punitive damages held not taxable under *Central R. Co.* windfall theory); *Clark v. Comm’r*, 40 B.T.A.M. (P-H) 333, 335 (1939) (relying on a return of capital theory to exclude from income damages received from settlement); *Theodate Pope Riddle v. Comm’r*, 27 B.T.A.M. (P-H) 1339, 1339, 1341 (1933) (involving an amount received as damages for personal injuries sustained in the 1915 sinking of the *Lusitania*, where the award of \$15,000 was held not taxable but where the interest paid on the award was held taxable). At least one commentator considers *Raytheon* to be the “interpretive authority” in the area of taxability of damage receipts. See Harnett, *supra* note 1, at 624.

In the late 1920s, damages for wrongful death were brought into the exclusionary fold of § 213(b)(6). See I.T. 2420, VII-2 C.B. 123 (1928). *I.T. 2420* decided the question of whether money plus interest, paid by the Mixed Claims Commission of the United States and Germany as compensation to a spouse for the death of her husband, was to be taxed as income. See *id.* The Income Tax Unit determined that an award received for loss of life is not embraced in the general concept of “income.” See *id.* at 124.

Revenue Ruling 54-19 followed *I.T. 2420* and held that amounts received by settlement of a claim under a state wrongful death act was not included in the decedent’s estate, nor was it taxable to dependents who received the proceeds of the recovery. 1954-1 C.B. 179, 180. *Revenue Ruling 55-132* held that amounts received by a prisoner of war from the United States do not qualify as reimbursement for the loss of personal rights and are excludable from the gross income of such individual. 1955-1 C.B. 213, 213. *Revenue Ruling 56-462* held payments under the War Claims Act to Korean prisoners were nontaxable as compensation to injury for personal rights. 1956-2 C.B. 20, 21. *Revenue Ruling 56-518* held as follows:

[C]ompensation paid by the Federal Republic of Germany to citizens or residents of the United States pursuant to claims filed under its laws on account of such persecution which resulted in damage to life, body, health, liberty, or to professional or economic advancement, are in the nature

administrative and judicial interpretations of § 213(b)(6) charted the wrong course for the statute as the cases that followed continued to emulate *Hawkin's* faulty reasoning.

Many courts applying a version of *Hawkin's* looked to the framing of the complaint and thus the taxpayer's cause of action to determine whether damages for injury to business reputation were taxable. In the 1932 case of *Farmers' & Merchant's Bank v. Commissioner*, the Sixth Circuit reversed the BTA and the Commissioner, holding that the full settlement award arising out of tortious injury to business goodwill was excludable from gross income under the return of capital theory.¹⁰⁹ The court saw "no legal distinction" between damage to intangible property like goodwill and damage to tangible property.¹¹⁰ In deciding whether the settlement was taxable, the court noted that the value of the money received "must be considered in the light of the claim from which it was realized and which is reflected in the complaint filed in its action."¹¹¹ Thus the taxpayer, by basing

of reimbursement for the deprivation of civil or personal rights and do not constitute taxable income to the recipients.

1956-2 C.B. at 25. *See also* Revenue Ruling 58-500, 1958-2 C.B. 21, 21 (holding that "payments made by the Federal Republic of Germany under the provisions of the Federal Restitution Law come within the ambit of Revenue Ruling 56-518"). Similarly, in *Revenue Ruling 58-370*, payments to former Austrian citizens persecuted by the Nazi regime were nontaxable. 1958-2 C.B. 14, 14. Significantly, the policy behind these exclusions may originate in a compassion or humanitarian theory of tax policy dealing with death. Perhaps, the Service thought that the taxpayers had been through enough and did not want to pursue any further litigation. *Cf. McDonald v. Comm'r*, 9 B.T.A.M. (P-H) 1340, 1342 (1928) (stating that based on the principles laid down in *Hawkins*, the Tax Court held that damages received from a breach of contract to marry would not be taxed as income). *See Knickerbocker, supra* note 83, at 439-40 (discussing the various cases and Revenue Rulings mentioned in this footnote and the theories behind excluding from income the respective damages in each case). *But see* Patricia T. Morgan, *Old Torts, New Torts and Taxes: The Still Uncertain Scope of Section 104 (a)(2)*, 48 LA. L. REV. 875, 885 (1988) (stating that the return of capital theory is irrelevant and that the "first and only inquiry is whether the recovery is for personal injury" when determining excludability of damages from income).

109. 59 F.2d 912, 913-14 (6th Cir. 1932). The petitioner, not a member of the Federal Reserve System, routinely charged customers for collection of checks on foreign banks. *Id.* at 913. The Federal Reserve Bank (Bank) demanded the petitioner clear checks at par. *Id.* The Bank notified its members that it would clear checks drawn on the petitioner bank at no charge. *Id.* For eighteen months, the Bank daily sent agents, with checks, to the petitioner and demanded payment in cash. *Id.* The petitioner thereupon received unfavorable publicity, as well as interference with operations and lost profits. *Id.* The government sought to tax a portion of the settlement award as earnings. *See id.*

110. *Id.* at 913 ("[W]e can see no legal distinction between compensation for destruction of or damage to incorporeal or intangible property, such as good will, and similar compensation for damage to tangible property.") (citing *Harris & Co. v. Lucas*, 48 F.2d 187, 188 (5th Cir. 1931) (stating that "[g]ood will is an asset that adds to the value of a going business and may pass to a purchaser")). This inevitably leads one to the conclusion that the opinion is based on a return of capital theory. *See Knickerbocker, supra* note 83, at 434 (stating that *Farmers'* represents the first time the courts struggled with the question of whether "recoveries in actions based on injuries to business reputation" would be taxable).

111. *Farmers'*, 59 F.2d at 913.

his claim on loss of goodwill, rather than lost profits, was able to exclude the award from gross income under a return of capital theory.¹¹²

While the Sixth Circuit was willing to defer to the filed petition without great reservation,¹¹³ future courts strictly scrutinized the taxpayer's complaint in the underlying case to assure that the damages sought to be excluded from income were deserving of the § 213(b)(6) exclusion. For example, in *Central R.R. Co. v. Commissioner*, the Court of Appeals for the Third Circuit¹¹⁴ reversed both the BTA and the Commissioner and held that property received pursuant to the settlement of a breach of fiduciary duty claim was not taxable under the windfall theory.¹¹⁵ Central Railroad brought suit against an executive officer who had organized separate corporations which engaged "surreptitiously" in business dealings adverse to the railroad.¹¹⁶ The issue was whether the property awarded to the Railroad reimbursed lost profits or presented a windfall for a breach of fiduciary duty.¹¹⁷

First, the court mentioned that § 22 (defining gross income) applied to the situation but "[d]amages recovered because of personal injuries or illness are exempt" from taxation along with damages recovered "for alienation of affections, breach of promise to marry, and libel and slander" because those damages are "of a *personal nature* and . . . not . . . within the statutory definition of income."¹¹⁸ The court then moved away from the discussion of the damages' personal nature and distinguished the receipt of damages in its case from the damages received in *Farmers'* because no facts in the taxpayer's complaint indicated "with the certainty required in the statement of a cause of action, that . . . [the taxpayer] sought reparation for profits which petitioner's misconduct prevented it from earning."¹¹⁹ The court refused to apply a return of capital theory where the taxpayer did not plead that the cause of action was for damages to restore what was lost due to a violation of rights. However, the court went on to agree with the taxpayer that what he received in the settlement did not fall under the definition of income articulated in *Eisner* but rather, was a windfall because "it was a penalty imposed by the law on a faithless fiduciary."¹²⁰ The court found that

112. In effect, the court disregarded the petitioner's receipt of the property and focused upon the origin of the payment rather than the reason for the receipt of such payment. *See id.*

113. *See id.* at 912-13.

114. 79 F.2d 697 (3d Cir. 1935).

115. *See id.* at 699-700.

116. *Id.* at 697.

117. *See id.* at 699.

118. *Id.* at 698 (emphasis added).

119. *Cent. R.R. Co.*, 79 F.2d at 698.

120. *Id.* at 699.

“the settlement was not based on a suit by the taxpayer to recover profits” and, thus, held that the Commissioner must exclude the award from income under the windfall theory.¹²¹

C. Raytheon: The “In Lieu of What” Test

In the 1944 case of *Raytheon Production Corp. v. Commissioner*,¹²² the Court of Appeals for the First Circuit affirmed the Tax Court¹²³ and articulated a new test to determine the taxability of business injury recoveries: “in lieu of what were the damages awarded?”¹²⁴ Raytheon Production Corporation had been one of the first manufacturers of a rectifying tube, making radio reception possible through alternating current rather than on batteries using direct current.¹²⁵ The Radio Corporation of America (RCA) had developed a competitive tube, and by 1928 most manufacturers were under RCA licenses.¹²⁶ In its licensing agreement, RCA required its licensees to buy their tubes from RCA.¹²⁷ By 1929, RCA

121. *Id.* at 699-700. While this taxpayer was successful in excluding his award under a windfall theory, after the 1955 Supreme Court decision of *Glenshaw Glass* the windfall theory was no longer available to taxpayers because the Supreme Court redefined the parameters of income to include any “undeniable accessions to wealth, clearly realized, and over which the taxpayers [had] complete dominion,” not specifically excluded by the Code. 348 U.S. 426, 431 (1955).

122. 144 F.2d 110 (1st Cir. 1944).

123. *Raytheon Prod. Corp. v. Comm’r*, 1 T.C. 952 (1943). Of the \$410,000 in damages the taxpayer received, the settlement agreement allocated \$60,000 for the value of Raytheon’s patent rights and the remaining \$350,000 of those damages as a lump sum settlement to end Raytheon’s antitrust violation suit. *See id.* at 958. The Tax Court asked “[f]or what did the petitioner receive the \$410,000?” and stated that for the amount to be excluded from taxation, Raytheon must show “that it was received as replacement of capital lost.” *Id.* at 958. Although the Tax Court looked to the settlement instrument for guidance in holding that the full amount was taxable, the Tax Court also deferred to the commissioner’s finding of a lack of evidence demonstrating “what the amount was paid for.” *Id.* at 958. The Tax Court based its holding on *Armstrong Knitting Mills v. Comm’r*, 19 B.T.A.M. (P-H) 318 (1930). In *Armstrong Knitting Mills*, the court found that where the taxpayer had received damages from a settlement of two claims—one for damages to business and one in contract—and where the settlement agreement did not specify what the damages were awarded for, the Commissioner’s determination controls. *Armstrong Knitting Mills*, 19 B.T.A.M. (P-H) at 322. Moreover, the *Armstrong* court found that the taxpayer has the burden of establishing that any part of the settlement was allocated as a return of capital. *See id.* at 322. The Tax Court dissent, however, found that the “charge was based in the illegal injury to plaintiff’s business and property, specifically its good will” and therefore, did not come within the line of cases that hold damages to be included as income where the suit in question was based on lost profits. *Raytheon*, 1 T.C. at 962-63.

124. *Raytheon*, 144 F.2d at 113. This ties in with the conversion of capital theory. If damages are awarded “in lieu of” lost profits, the damage award is taxable. Conversely, if damages are awarded “in lieu of” lost goodwill, such award, as a return of capital, is not taxable.

125. *See id.* at 111.

126. *See id.* The companies under license agreement with RCA included General Electric Company, Westinghouse, and American Telephone and Telegraph Company. *See id.*

127. *Id.*

monopolized the rectifying tube market through its license agreements and Raytheon was unable to compete.¹²⁸ The successor to Raytheon, born from a series of tax-free reorganizations, filed a federal antitrust claim against RCA asserting that RCA “conspired to destroy the business” by creating a monopoly.¹²⁹

The court began its opinion by holding that the application of § 213(b)(6) should not depend on whether the underlying claim is in tort or in contract. Rather, the court must ask “[i]n lieu of what were the damages awarded?”¹³⁰ Resting its decision on the framing of the complaint, the court found that the suit was not for lost profits but for the destruction of business reputation and for damage to “profitable interstate and foreign commerce.”¹³¹ Damages received for injury to the goodwill of a business were a return of capital and thus, not taxable. But where the recovery was greater than the recipient’s cost basis in the goodwill, any excess was taxable as gain.¹³² Unfortunately for Raytheon, because it could not establish a cost basis in the good will of the business, the court found the entire award taxable.¹³³

Ignoring what should have been the only inquiry under § 213(b)(6), namely whether the damages awarded were for personal injury,¹³⁴ courts continued to apply the “in lieu of what” test into the ‘80s.¹³⁵ While future

128. *Id.*

129. *Id.*

130. *Raytheon*, 144 F.2d at 113.

131. *Id.*

132. *See id.* at 114.

133. *See id.* When computing gain, a taxpayer has the burden of establishing basis. If the basis is wholly speculative it will be assigned a value of zero. As a result any amount received will be included in computing taxable income. *See infra* notes 440-44 and accompanying text.

134. *See Morgan, supra* note 108, at 885 (stating that the proper analysis for excludability under § 104(a)(2) is not whether the monies received are a nonpersonal “return-of-capital” or whether the monies received are “in lieu of” the damages).

135. *See, e.g., Bagley v. Comm’r*, 121 F.3d 393, 395 (8th Cir. 1997); *Delaney v. Comm’r*, 99 F.3d 20, 23-24 (1st Cir. 1996); *Alexander v. I.R.S.*, 72 F.3d 938, 942 (1st Cir. 1995); *Wolfson v. Comm’r*, 651 F.2d 1228, 1230 (6th Cir. 1981), *aff’g and remanding*, 37 T.C.M. (CCH) 1847-14, 1847-22 (1978); *Thompson v. Comm’r*, 89 T.C. 632 (1987); *Church v. Comm’r*, 80 T.C. 1104, 1107 (1983); *Fono v. Comm’r*, 79 T.C. 680 (1982); *Roemer v. Comm’r* 79 T.C. 398, 405 (1982), *rev’d*, 716 F.2d 693 (9th Cir. 1983); *Entwicklungs & Finanzierungs A.G. v. Comm’r*, 68 T.C. 749, 759 (1977); *Yates Indus., Inc. v. Comm’r*, 58 T.C. 961, 972 (1972), *aff’d without published opinion*, 480 F.2d 920 (3d Cir. 1973); *State Fish Corp. v. Comm’r*, 48 T.C. 465, 472 (1967), *supp. opinion*, 49 T.C. 13 (1967); *Young v. Comm’r*, 16 T.C. 1424, 1429 (1951); *Madson v. Comm’r*, 49 T.C.M. (CCH) 425, 427 (1985); *McKim v. Comm’r*, 40 T.C.M. (CCH) 9, 12 (1980). *See also* *Burke & Friel, supra* note 20, at 167. *Burke and Friel* believe:

[I]n some respects, the standard adopted by the *Schleier* Court is identical to the historic “in lieu of what” test of *Raytheon Production Corp. v. Commissioner*. That test arguably provides the narrowest interpretation of the “on account of” language, ensuring that only those damages for personal injury (damages in lieu of the human capital lost to the injury) are excludable.

Id. at 175.

courts did not apply this test in conjunction with the return of capital theory, they regularly focused on the nature of the recovery rather than on the nature of the injury and consistently failed to invoke the statutory exemption.

D. Glenshaw Glass: *Redefining Gross Income*

Congress codified all the revenue acts that had been passed from 1913 to 1939 in the Internal Revenue Code of 1939. Then, in 1954 the Code was recodified as the Internal Revenue Code of 1954.¹³⁶ Without changing any significant language Congress renumbered § 213(b)(6) as § 104(a)(2) in the 1954 Code.¹³⁷ Curiously, with the renumbering, courts finally began to apply § 104(a)(2), previously codified at § 213(b)(6), in damage cases. However, in 1955 with a new Supreme Court opinion, the concept of income dramatically changed and affected the application of § 104(a)(2).

For the first time since it defined income in *Eisner*, the Supreme Court dramatically expanded the concept of income in the landmark decision of *Commissioner v. Glenshaw Glass*.¹³⁸ In *Glenshaw Glass*, one of two consolidated opinions, the Court determined whether money received as exemplary damages for fraud and as punitive damages for antitrust violations constituted gross income.¹³⁹

In the original action, Glenshaw Glass brought suit against a corporation for antitrust violations.¹⁴⁰ Ultimately, the parties settled the suit, with Glenshaw Glass receiving approximately \$800,000 of which \$324,529.94 represented payment for punitive damages.¹⁴¹ Glenshaw Glass did not report the latter amount as income, and the Commissioner issued a deficiency.¹⁴² Both the Tax Court¹⁴³ and the Court of Appeals for the Third Circuit upheld the taxpayer's position that the punitive damages were excluded from gross

136. I.R.C. §§ 1 *et seq.* (1954).

137. Compare I.R.C. § 213(b)(6) (1919) with I.R.C. § 104 (a)(2) (1954). For more information on § 213(b)(6), see *supra* note 3.

138. 348 U.S. 426 (1955).

139. *Id.* at 427.

140. See *id.* at 427-28. Glenshaw Glass based its claims on the Supreme Court decisions in *Shawkee Mfg. Co. v. Hartford-Empire Co.*, 322 U.S. 271 (1944), and *Hazel-Atlas Glass Co. v. Hartford-Empire Co.*, 322 U.S. 238 (1944). See *Glenshaw Glass*, 348 U.S. at 428 n.2.

141. *Glenshaw Glass*, 348 U.S. at 428.

142. *Id.*

143. *Glenshaw Glass Co. v. Comm'r*, 18 T.C. 860, 870-71 (1952) (holding that where money is received in a lump sum to remedy various claims, an allocation of specific amounts to each of the several claims "is necessary and proper; . . . sums received in settlement of punitive damages claims do not constitute taxable income; . . . sums received in settlement of claims for anticipated profits are taxable income").

income.¹⁴⁴

In the other consolidated case, *Commissioner v. William Goldman Theatres*, Goldman sued a corporation for antitrust violations and received treble damages in the amount of \$375,000.00 of which Goldman reported \$125,000 as income for lost profits.¹⁴⁵ Again, the Tax Court upheld the taxpayer's position¹⁴⁶ as did the Third Circuit.¹⁴⁷

While the taxpayers in *Glenshaw Glass* and *William Goldman* relied on the *Eisner* definition of gross income—"the gain derived from capital, from labor, or from both combined"¹⁴⁸—the government argued and the Court agreed that *Eisner's* definition "was not meant to provide a touchstone to all future gross income questions."¹⁴⁹ Noting that the *Eisner* Court used the definition only to determine whether the distribution of a corporate stock dividend constituted a realized gain to the shareholder, the Court overturned the Tax Court and the Third Circuit holding that punitive and exemplary damages were taxable as "undeniable accessions to wealth, clearly realized, and over which the taxpayers [had] complete dominion."¹⁵⁰

Most importantly, while the *Glenshaw Glass* Court, expanded the definition of income to include punitive damages within the *Eisner* definition of income, the Court did not need to interpret the language of § 104(a)(2), which excluded from income "any damages received . . . on account of personal injury."¹⁵¹ In fact, in footnote eight, the Supreme Court left intact the treatment of personal injury recoveries as nontaxable.¹⁵² Thus, given the new

144. *Comm'r v. Glenshaw Glass Co.*, 211 F.2d 928, 933-34 (3d Cir. 1954) (finding windfalls are not income and punitive damages paid under the Clayton Act are not income).

145. 348 U.S. 426, 428-29 (1955). For the case concerning the antitrust violation, see *William Goldman Theatres, Inc. v. Loew's*, 164 F.2d 1021 (3d Cir. 1948).

146. See *William Goldman Theatres Inc. v. Comm'r*, 19 T.C. 637, 641 (1953) (finding one-third taxable and two-thirds not).

147. See *Comm'r v. William Goldman Theatres, Inc.*, 211 F.2d 928 (3d Cir. 1954).

148. *Glenshaw Glass*, 348 U.S. at 430 (1955) (citing *Doyle v. Mitchell Brothers Co. v. Comm'r*, 247 U.S. 179, 185 (1918), and *Stratton's Independence v. Howbert*, 231 U.S. 399, 415 (1913)).

149. *Id.* at 431 (citing *Helvering v. Bruun*, 309 U.S. 461, 468-69 (1940), and *United States v. Kirby Lumber Co.*, 284 U.S. 1, 3 (1931)).

150. See *Glenshaw Glass*, 348 U.S. at 430-31.

151. *Id.* at 427-29 (finding the facts of *Glenshaw Glass* related to fraud and antitrust violations not involving personal injury).

152. *Id.* at 432 n.8.

The long history of departmental rulings holding personal injury recoveries nontaxable on the theory that they roughly correspond to a return of capital cannot support exemption of punitive damages following injury to property . . . Damages for personal injury are by definition compensatory only. Punitive damages, on the other hand, cannot be considered a restoration of capital for taxation purposes.

Id. See, e.g., *Lukhard v. Reed*, 481 U.S. 368, 387 (1987) (Powell, J., dissenting); *United States v. Kaiser*, 363 U.S. 299, 311 (1960); *O'Gilvie v. United States*, 66 F.3d 1550, 1558 (10th Cir. 1995); *Starrels v. Comm'r*, 304 F.2d 574, 576 (9th Cir. 1962); *Kemp v. Comm'r*, 771 F. Supp 357, 358-59

and broader *Glenshaw Glass* concept of income, taxpayers could only achieve nontaxability for their recoveries by qualifying for the statutory exemption under § 104(a)(2). After *Glenshaw Glass*, taxpayers sought to frame causes of action in tort, even if also grounded in contract so that their damages could be excluded under § 104(a)(2) as personal injury awards. As a result the courts developed innovative tests to filter out claims purportedly undeserving of the § 104(a)(2) exclusion.

E. Agar: The Intent of the Payor Test

Six years after *Glenshaw Glass*, in *Agar v. Commissioner*, the taxpayer claimed that he received a settlement payment from his employer in avoidance of a libel suit.¹⁵³ The taxpayer excluded the full amount from income under § 104(a)(2).¹⁵⁴ The Tax Court affirmed the Commissioner's assessment of a deficiency on two grounds. First, the payments were extra or severance pay and not damages received in avoidance of a libel suit.¹⁵⁵ Second, the gravamen of the claim was for injury to the taxpayer's business reputation and therefore did not satisfy the statutory requirement of being on account of "personal injuries."¹⁵⁶

The Court of Appeals for the Second Circuit, affirming the determination of the Tax Court that the payments were in the nature of severance pay rather than damages in lieu of a libel suit, focused on the *intent of the payor* to determine the tax treatment of the settlement.¹⁵⁷ The Second Circuit reasoned that "[t]hrough petitioner may have believed that the company paid him to avoid litigation, . . . his belief was only evidence of the character of the payment; the ultimate inquiry is into the 'basic reason' for the company's payment."¹⁵⁸ The Second Circuit quoted from the testimony of the company

(N.D. Ga. 1991); *Roosevelt v. Comm'r*, 43 T.C. 77, 88 (1964).

153. See 290 F.2d 283 (2d Cir. 1961). *Agar's* claim was technically a claim for slander not libel because the statements made by the employees of the company were oral. See *id.* at 284 n.1.

154. See *id.* at 284.

155. *Id.*

156. *Agar v. Comm'r*, 19 T.C.M. (CCH) 116, 119-20 (1960). Before discussing its findings and arriving at its decision, the Tax Court first reemphasized the broadness of the statutory definition of income as articulated in *Glenshaw Glass*. See *id.* at 119. The Court then stated that "[i]n light of this principle, . . . petitioner must bring himself squarely within the exemption from tax upon which he bases his case; *i.e.* that the \$45,000 was received in settlement of his claim for damages resulting from injury to his *personal reputation*." *Id.* This holding exemplifies how taxpayers after *Glenshaw Glass* could no longer exclude their damage receipts based on an argument that such damages did not fall within the definition of income. Taxpayers must now prove that the damages received fall within the § 104(a)(2) exclusion.

157. See *Agar*, 290 F.2d at 284.

158. *Id.* at 284 (citing *Comm'r of Internal Revenue v. Duberstein*, 363 U.S. 278, 286 (1960) (stating that the most critical consideration in determining whether a gift is not taxable as income is the

president in the Tax Court: “‘We felt we owed Mr. Agar something . . . I would say it is severance.’”¹⁵⁹ After affirming the Tax Court on its first ground, the Second Circuit stated that it was not necessary to decide the second issue—whether a “dichotomy” existed for tax purposes between personal and business reputation.¹⁶⁰

In the 1962 case of *Starrels v. Commissioner*,¹⁶¹ taxpayers again attempted to exclude money received under a contract as damages awarded in lieu of a tort claim but the court looked to the intent of the payor to determine the taxpayer’s tax liability. The daughters of a World War II naval aviator entered into an agreement with Loew’s, Inc. for the production of a film and the distribution, advertisement, promotion, exploitation, and depiction of the life of their father.¹⁶² The agreement also required the daughters to provide Loew’s with family documents, photographs, and other information and material that could be helpful to the preparation of the motion picture.¹⁶³ In one provision, the sisters agreed to refrain from any future claims against the producers should the film’s portrayal of them or their father “constitute[] a violation of any of their rights, including their rights of privacy.”¹⁶⁴

In an attempt to fall within the § 104(a)(2) exemption, the taxpayers sought to exclude the amounts paid pursuant to the agreement, under the guise that the payments were received for their consent to and in lieu of future invasions of their privacy.¹⁶⁵ The Commissioner assessed a deficiency for the entire amount.¹⁶⁶ The Tax Court, relying on factually similar cases, found no evidence whatsoever that the resulting motion picture in fact invaded or damaged the payees rights to privacy and, therefore, upheld the

transferor’s intention)); *Bogardus v. Comm’r*, 302 U.S. 34, 44-45 (1937) (Brandeis, J., joined by Stone, Cardozo, Black, J.J., dissenting) (“[C]ategories of ‘gift’ and ‘compensation’ are not always mutually exclusive, but at times can overlap. What controls is not the presence or absence of consideration. What controls is the intention with which payment, however voluntary, has been made.”); *Jackson v. Comm’r*, 25 T.C. 1106, 1110 (1956) (“If the payment was made with the intention of requiting past services or employment more generously or completely, it is taxable.”). These three cases are unrelated to the subject of damage receipts in this type of inquiry.

159. *Agar*, 290 F.2d at 284.

160. *Id.* See Paul B. Stephan, III, *Federal Income Taxation and Human Capital*, 70 VA. L. REV. 1357, 1413-14 (1984) (“The efforts of some courts to separate personal and business defamation recoveries illuminate the inadequacy of the distinction . . . The paradox from which these decision makers attempted to escape was that business income ordinarily is taxable, and that compensation for injury to it seemingly should have the same status.”).

161. 35 T.C. 646 (1961), *aff’d*, 304 F.2d 574 (9th Cir. 1962).

162. *Id.* at 647.

163. *Id.*

164. *Id.*

165. See *id.* at 647-48.

166. See *id.* at 646.

Commissioner's decision.¹⁶⁷

On appeal, the Court of Appeals for the Ninth Circuit affirmed the Tax Court's decision stating that the court was "reasonably sure that the exemption . . . was not intended to reach advance payments for consent where no actual invasion of personal rights subsequently occurred."¹⁶⁸ Citing *Glenshaw Glass*, the Ninth Circuit noted with favor footnote eight and the departmental rulings referenced therein.¹⁶⁹ In addition, it reiterated an old rationale underlying the purpose of § 104(a)(2): "Damages paid for personal injuries are excluded from gross income because they make the taxpayer whole from a previous *loss of personal rights*—because, in effect, they restore a *loss to capital*."¹⁷⁰

In 1965, the Court of Appeals for the Tenth Circuit in *Knuckles v. Commissioner*, repudiated a taxpayer for an extreme attempt to convert a contract claim into a tort action to obtain a tax advantage under § 104(a)(2).¹⁷¹ The taxpayer entered into an employment contract with Perpetual Life Insurance Company (Perpetual), was fired within two years, and then commenced a suit for breach of employment contract.¹⁷² During settlement negotiations, Knuckles' attorney sought to couch the basis of the

167. See *Starrels*, 35 T.C. at 648. The Tax Court opined:

If the payments based on this agreement could be made tax exempt by merely referring to a right of privacy which was never invaded and possibly never intended to be invaded, the narrowly conceived statutory exclusion for damages on account of 'personal injuries' would be expanded beyond its normal meaning. We think Congress intended no such result.

Id. (internal citations omitted). See generally *Runyon v. United States*, 281 F.2d 590 (5th Cir. 1960); *Meyer v. United States*, 173 F. Supp. 920 (E.D. Tenn. 1959); *Ehrlich v. Higgins*, 52 F. Supp. 805 (S.D.N.Y. 1943).

168. *Starrels*, 304 F.2d at 576. Petitioner relied on *Gill v. Curtis Publishing Co.*, 239 P.2d 630 (1952), in order to assert that each family member had a "legally protected right in the privacy of each of the other members of the family." *Starrels*, 304 F.2d at 576. The court held, however, that such a right did not exist under this case. See *id.* The court reasoned that "the right of privacy is personal, and the payments involved could constitute 'damages received . . . on account of personal injuries' of Mrs. Starrels only if they compensated Mrs. Starrels for an invasion of her own privacy, rather than the privacy of her father." *Id.* The court felt that if it decided otherwise, the abuse under § 104(a)(2) would be a result contrary to what Congress intended under this section. See *id.* at 577.

169. See *Starrels*, 304 F.2d at 576 (citing *Comm'r v. Glenshaw Glass Co.*, 348 U.S. 426, 432 n.8 (1955)); Rev. Rul. 58-500, 1958-2 C.B. 21; Rev. Rul. 58-370, 1958-2 C.B. 14; Rev. Rul. 57-505, 1957-2 C.B. 50; Rev. Rul. 56-518, 1956-2 C.B. 25; Rev. Rul. 56-462, 1956-2 C.B. 20; Rev. Rul. 55-132, 1955-1 C.B. 213.

170. *Starrels*, 304 F.2d at 576 (citations omitted) (emphasis added). See Paul C. Feinberg, *Federal Income Taxation of Punitive Damages Awarded in Personal Injury Action*, 42 CASE W. RES. L. REV. 339, 374 (1992) (stating that *Starrels* and similar cases involving "consensual violations of personal rights support[] the view that section 104(a)(2) encompass[es] only payments which compensate for actual personal injury and, thus, restore a loss of capital").

171. 349 F.2d 610, 613 (10th Cir. 1965).

172. *Id.* at 611.

settlement in terms of a tort claim for personal injury.¹⁷³ Although Perpetual initially “refused to recognize any liability in tort,”¹⁷⁴ it ultimately permitted Knuckles to institute a civil suit based upon the employer’s liability for personal injury, which the court subsequently dismissed with prejudice.¹⁷⁵ Perpetual’s Board of Directors then rescinded its resolution terminating the taxpayer on grounds of incompetence, substituting it with one merely terminating Knuckles’ contract.¹⁷⁶ The Tax Court found that the amounts paid by the employer were for compensation under the employment contract and for injury to his business reputation, such that the damages were not within the exemption of § 104(a)(2).¹⁷⁷

The Tenth Circuit affirmed the Tax Court and citing *Agar* stated that “[t]he most important fact in making . . . [the § 104(a)(2)] determination, in the absence of an express personal injury settlement agreement, is the intent of the payor as to the purpose in making the payment.”¹⁷⁸ The Tenth Circuit found no mention of the claim for personal injury until late in the settlement negotiations and found that Knuckles presented no proof of the existence of any personal injury.¹⁷⁹ Quoting the Tax Court, the Tenth Circuit concluded that the tort claim for personal injuries “was an afterthought brought into being by the possible tax advantage which might result.”¹⁸⁰

F. Seay: The Nature of the Claim Test

Seven years after *Knuckles* in *Seay v. Commissioner*, the Commissioner found an entire settlement taxable where a taxpayer received a lump sum of \$105,000 in a settlement of which \$45,000 was explicitly allocated towards personal injuries.¹⁸¹ The Tax Court examined prior cases dealing with the question of what a taxpayer must prove in order to establish the nature of the payments received¹⁸² and held that the “determination of whether a

173. *See id.* at 612.

174. *Id.* *See* *Knuckles v. Comm’r*, 23 T.C.M. (CCH) 182, 182-83 (1964).

175. *See Knuckles*, 349 F.2d at 612.

176. *Id.*

177. *See id.*

178. *Id.* at 613.

179. *See id.*

180. *Id.* (internal quotations omitted).

181. 58 T.C. 32, 35-36 (1972), *acq.* 1972-2 C.B. 3. Following a dispute with management, the taxpayer who was the president of a corporation was let go because he could not be the president under the corporate bylaws without being a director. *Id.* at 33. The media published stories that embarrassed the taxpayer because they thought the taxpayer became the president of the corporation and was then let go. *Id.* at 34. The \$45,000 in question was determined by the settlement to be an award compensating the taxpayer for the damaging news articles. *Id.*

182. *See id.* at 36-37. The court looked to § 104(a)(2) which provides that in a settlement

settlement payment is exempt from taxation depends on the nature of the claim settled and not on the validity of the claim.”¹⁸³ The court found that the taxpayer proved his claim was for “personal injuries” within the meaning of § 104(a)(2).¹⁸⁴ Primarily, the court based this conclusion on the testimony of the chief settlement negotiator for each party whose testimony indicated that the payment was for personal injuries and a letter between the parties confirmed that settlement allocation.¹⁸⁵

Once again drawing on the nature of the claim test, the Tax Court determined that a taxpayer could not exclude back pay received in settlement of a job discrimination suit under Title VII in the 1975 case of *Hodge v. Commissioner*.¹⁸⁶ Numerous factors influenced the court in reaching its conclusion: the complaint did not allege personal injuries on account of discrimination; the prayer for relief did not request damages for personal

agreement, damages received “on account of personal injuries” are not to be included in income tax. However, the court did not find anything in the statute or regulations that would explain what the taxpayer had to show in order to satisfy his burden of proving that the damages were in fact “on account of personal injury.” *Id.* at 36. Therefore, the court applied the nature of the claim test developed in previous cases. *See id.* at 36-37.

183. 58 T.C. at 37. *Cf.* Rev. Rul. 72-341, 1972-2 C.B. 32. In *Revenue Ruling 72-341*, the Service considered a Title VII question where the United States Government sued a company based on alleged discrimination. *Id.* A settlement agreement ensued, under which the corporation was to divide a sum among the employees who had suffered economic loss as a result. *Id.* Here, the amount to be paid each employee was based on a formula based on the difference between actual earnings and expected earnings absent the discrimination. *Id.* The Service ruled that the amounts were wholly includable in taxpayer’s gross income, looking to “the nature of the item for which the damages were a substitute.” *Id.*

184. *Seay*, 58 T.C. at 37-38.

185. *Id.* at 38-39. The court distinguished both *Knuckles* and *Agar*. *See id.* at 37. In *Agar*, the *Seay* court found that while the taxpayer may have made a claim for personal injuries, the company did not make any settlement payment for that claim. *See id.* at 38. In *Knuckles*, the *Seay* court found that the claim was not a part of a negotiated settlement but an “afterthought based on the tax consequences of the claim.” *Id.* *See also* Rev. Rul. 75-45, 1975-1 C.B. 47 (addressing the question of whether an amount received by the executor of an estate was excluded under § 104(a)(2) or whether it was included as punitive damages under the regulations). In *Knuckles*, the insurance policy promised to pay certain sums to persons who were injured as passengers in a corporation’s airplane providing that the recipient release the company from any claims for damages, including claims under the state wrongful death statute. *See Seay*, 58 T.C. at 37. A series of court decisions in that state had established that payments under the wrongful death statute were punitive in nature. *See id.* The IRS gave a broad reading to the language of § 104(a)(2), emphasizing that the section excluded “the amount of any damages received . . . on account of personal injuries.” *Id.* In so reading the exclusion, the IRS found the amount completely excludable. *See id.* at 47-48. *Cf.* Sandy Kasten & Brad Seligman, *Tax Considerations in Settling Employment Cases*, CAL. LAW., Oct. 1985, 13, 16 (stating that the outcome in *Seay*, as opposed to in *Agar* and *Knuckles*, indicates that a taxpayer may minimize taxes on employment settlements if the taxpayer alleges “non-taxable damages in the complaint[,] . . . maintain[s] a consistent position regarding the claim for such damages throughout the litigation and settlement negotiations[,] . . . [and verifies that the] settlement agreement or judgment expressly allocate[s] specific dollar amounts of the total settlement between taxable and non-taxable damages”).

186. 64 T.C. 616, 616-17 (1975).

injuries; and the issue of personal injuries was not raised until three years after the complaint had been filed.¹⁸⁷ In addition, the court noted that the attorney who represented the defendant in the discrimination suit testified that the defendant's primary concern was the back pay settlement and that the formula used to determine the settlement amount was strictly based upon theories of back pay.¹⁸⁸ Noting that Title VII allows a court to order the payment of back pay compensation for services normally included in gross income, the court concluded that pursuant to Title VII, back pay was not excludable under § 104(a)(2).¹⁸⁹

Notably, the Tax Court clearly rejected the taxpayer's argument that Title VII redresses personal injury.¹⁹⁰ If Title VII does not redress a personal injury, then it logically follows that Congress passed Title VII of the Civil Rights Act purely as a statute to promote economic equality for disadvantaged groups in the employment market. Such reading of Title VII is extremely questionable since other Titles of the Civil Rights Act of 1964 recognize that a personal right is injured when the statute is violated.¹⁹¹ Arguably, if Congress passed Title VII purely to redress contractual harms, then it would not be within the spirit of the Civil Rights Act of 1964. However, the Tax Court in *Hodge* was not alone in believing that Title VII does not redress a victim for personal harms. Such reasoning unfortunately effected the outcome of several cases in the '80s and '90s.¹⁹²

187. *Id.* at 617-18.

188. *Id.* at 620. The petitioner cited to numerous cases purporting to bolster his argument that damages, while labeled back pay, were in reality a recovery for personal injuries when awarded under Title VII of the Civil Rights Act of 1964, and therefore, would be excludable from income under § 104(a)(2). *Id.* at 619 n.7 (citing *Kober v. Westinghouse Elec. Corp.*, 480 F.2d 240 (3d Cir. 1973); *United States v. N.L. Indus., Inc.*, 479 F.2d 354 (8th Cir. 1973); *Robinson v. Lorillard Corp.*, 444 F.2d 791 (4th Cir. 1971); *Bowe v. Colgate-Palmolive Co.*, 416 F.2d 711 (7th Cir. 1969); *United States v. Hayes Int'l Corp.*, 415 F.2d 1038 (5th Cir. 1969)). The court refused to give weight to these cases because they dealt with damages for discrimination that were not for back pay. *See Hodge*, 64 T.C. at 619-20. The court stated in footnote seven that "had we decided, as a matter of fact, that a portion of the recovery constituted personal injury damages instead of back pay, we would have also had to decide whether such recovery was excludable from gross income under section 104(a)(2)." *Id.* at 619-20 n.7.

189. *See Hodge*, 64 T.C. at 619, 619 n.6, 620. *See also Johnson v. Ga. Highway Express, Inc.*, 417 F.2d 1122, 1125 (5th Cir. 1969); Rev. Rul. 72-341, 1972-2 C.B. 32. It is clear that the element of back pay is remunerative in nature and is expressly provided for by the Civil Rights Act itself. 42 U.S.C. § 2000e-5(g) (1994 & Supp. II 1996). Under that section, if the court finds illegal employment practices, one available remedy is reinstatement with or without back pay. The demand for back pay is not in the nature of a claim for damages, but rather is an integral part of the statutory equitable remedy, to be determined through the exercise of the court's discretion and not by a jury. *Johnson*, 417 F.2d at 1125.

190. *See Hodge*, 64 T.C. at 618-19.

191. For more information on these titles of the Civil Rights Act, see *infra* Part IV.

192. *See id.*

G. Whitehead: *Tort or Tort-Type Test*

Five years after *Hodge*, in *Whitehead v. Commissioner*, a taxpayer, terminated from a teaching position, filed a grievance which was settled contingent on a release of all claims against the university—including tort actions such as defamation and loss of reputation arising from the termination.¹⁹³ The Commissioner determined that the entire award was taxable.¹⁹⁴ Finding that the settlement made in consideration of a variety of *potential* claims and that the release did not specify between tort and contract claims, the Tax Court rejected the taxpayer's § 104(a)(2) argument.¹⁹⁵ Citing to *Seay*, *Knuckles*, and *Agar*, the court ruled that the taxpayer had to establish that the nature of the underlying claim was tort or tort-type and that the most important fact in determining the nature of the claim settled was the intent of the payor in making the settlement payment.¹⁹⁶ Upon examining the settlement agreement, the court concluded that the payor did not intend to

193. 41 T.C.M. (CCH) 365, 365-67 (1980).

194. *Id.* at 365.

195. *Id.* at 368. In *Glynn v. Comm'r*, the court followed *Knuckles* and held that “[i]n a case such as this where the settlement agreement lacks express language stating that the payment was made on account of personal injuries, the intent of the payor in making the payment must be discerned.” 76 T.C. 116, 120 (1981). The dispute in *Glynn* revolved around contractual rights: the school, employing the taxpayer as a teacher, demanded that he resign, and the taxpayer alleged that he had suffered injury to his business reputation. *Id.* at 117-19. Looking to the evidence at hand, the Tax Court held that the amount received by the taxpayer in settlement of the dispute was not excludable under § 104(a)(2). *Id.* at 121. The court looked at several facts, including that the taxpayer was willing to resign once the school agreed to pay him his benefits, the taxpayer never threatened to sue, and the taxpayer never asked the school for an amount based on damage to his personal reputation. *Id.* at 120. The Tax Court took the position that payments for injury to professional reputation are not excludable from gross income. *Id.* The court stated that any damages alleged to have been paid because of such injury would not fall under the exclusion given to payments for injuries to *personal* reputation. *Id.* The court reasoned that such damages are “more properly. . . characterized as payments made in satisfaction of injuries to petitioner’s *business* reputation as compensation for past or future income which might have been or might be lost, and thus, being compensatory by nature, would be taxable as ordinary income.” *Id.*

196. *Whitehead*, 41 T.C.M. (CCH) at 368. For more information on tort-type rights, see *McKim v. Comm'r*, where the taxpayer had been fired from his position as a salesman and had brought an action against his former employer. 40 T.C.M. (CCH) 9, 10 (1980). As stated in his complaint, McKim’s claims were based upon commissions that were allegedly owed to him, as well as other benefits. *Id.* The parties eventually reached a settlement, whereby the taxpayer received \$18,000 in exchange for release of all claims. *Id.* at 11. Noting that “the law is settled that petitioner must show the nature of the claim which was the actual basis for settlement, not the validity of the claim,” the Tax Court examined the facts and circumstances of the case in order to determine the intent of the payor in making the settlement. *Id.* at 12. The court found that the employer had settled in order to avoid litigating a question relating to what share of commissions the taxpayer was entitled. *Id.* The court also found significant the fact that the employer had withheld federal and state income taxes from the settlement award. *Id.* at 13. The court held that the taxpayer did not show that the nature of the claim was for personal injuries, even though the taxpayer may have claims for personal injuries as well as for the commissions earned, and hence the amount received was includable in his gross income. *Id.*

compensate the taxpayer for tort-type damages.¹⁹⁷

The tort or tort-type test was derived from the language of Treasury Regulation 1.104-1(c) which stated that “damages received means an amount received from an action based on tort or tort-type rights.”¹⁹⁸ The tort or tort-type test would gain prominence in future § 104(a)(2) decisions.¹⁹⁹ In fact, the first § 104(a)(2) Supreme Court decision, *United States v. Burke*, would apply this test and deny the § 104(a)(2) exclusion to a Title VII plaintiff who sought to exclude back pay from income.²⁰⁰

H. Nussbaum: *Predominant Nature of the Claim Test*

In the 1982 case of *Nussbaum v. Commissioner*, a New York Times’ (Times) employee filed a grievance through the Newspaper Guild of New York, Local 3 AFL-CIO, upon termination from employment.²⁰¹ Pursuant to § 104(a)(2), the taxpayer sought to exclude from income the settlement award received from the Times.²⁰² The Tax Court examined the settlement agreement and found three facts significant in determining that the predominant nature of the claim did not arise from personal injury. First, the only claims the employer specified were in “the ‘predominant nature’ of . . . reinstatement, seniority, and breach of contract.”²⁰³ Second, the payment was made in lieu of future salary and no claim for personal injury was even brought to the employer’s attention.²⁰⁴ Third, the employer withheld federal,

197. *Id.*

198. Treas. Reg. § 1.104-1(c) (1998).

199. *Roemer v. Comm’r*, 79 T.C. 398, 405 (1982).

200. *United States v. Burke*, 504 U.S. 229 (1992).

201. 45 T.C.M. (CCH) 346, 346-47 (1982).

202. *Id.* at 347.

203. *Id.* at 348. The pertinent provision of the agreement reads as follows: “The Times will make a special payment to Rhoda Nussbaum . . . in full settlement, satisfaction and release of any and all claims . . . against The Times, including claims for reinstatement, seniority and breach of contract.” *Id.* at 347.

204. *Id.* In 1982, § 104(a)(2) was amended to codify rather than change the then current law specifically to exclude from gross income damages received for personal injuries or sickness whether the amounts are distributed as periodic payments or lump sums. Act of January 14, 1983, Pub. L. No. 97-473, 96 Stat. 2605 (1982) (current version at 26 U.S.C. § 104(a)(2) (1998)). In 1984, the Service reversed its position on punitive damages in *Revenue Ruling 84-108*. 1984-2 C.B. 32, *revoking* Rev. Rul. 75-45, 1975-1 C.B. 47.

Here, the Service considered two situations. The first was an insurance policy payment upon the death of a policyholder in exchange for a full release by the beneficiaries of any wrongful death claims. 1984-2 C.B. at 32-33. The decedent was killed while a passenger in his employer’s corporate airplane. *Id.* The terms of the insurance policy paid an award to the personal representative of the deceased regardless of whose fault the accident was if the personal representative released the corporation from further liability. *Id.* The State of Virginia’s actual statute did not allow punitive damages for wrongful death actions. *Id.*

The second situation involved the Alabama wrongful death statute that provided exclusively for

state, and local taxes and treated the payment as severance pay.²⁰⁵ In denying the taxpayer's exclusion, the court cited to the Tax Court's decision in

punitive damages. *Id.* Under the Alabama wrongful death statute, damages are determined exclusively upon the degree of responsibility of the party found liable for the death. *Id.* Looking to *Glenshaw Glass* and the Supreme Court's conclusion that punitive damages are not a substitute for any amounts lost by the plaintiff, the Service concluded that punitive damages do not compensate a taxpayer for a loss but rather add to the taxpayer's wealth. *Id.* at 33-34. The service also relied on *Rev. Rul. 57-54*, 1957-1 C.B. 298, to defeat a claim that these proceeds were excludable as insurance proceeds. 1984-2 C.B. at 33-34. Unlike an insurance policy, the sums awarded were contingent upon the degree of need of the survivors in the first case and the degree of fault of the liable party in the second place and found that in those cases punitive damages are not awarded "on account of personal injury" within the meaning of § 104(a)(2). *Id.*

Thus, damages under Virginia's wrongful death statute were found to be excluded under § 104(a)(2), while the punitive damages under Alabama's wrongful death statute were held to be included in gross income. 1984-2 C.B. at 34. The Service's conclusions were to take effect without retroactivity and any release signed before July 16, 1984 would not be subject to the new ruling. *See id.*

Revenue Ruling 84-108 was criticized in *Burford v. United States*, where the District Court for the Northern District of Alabama refused to defer to the Service's interpretation of § 104(a)(2) in regards to punitive damages under the Alabama wrongful death statute. 642 F. Supp. 635, 636 (N.D. Ala. 1986). Here, the taxpayer had brought a wrongful death action against the University of Alabama at Birmingham because her husband died during treatment at the school's hospital. *Id.* The taxpayer received \$62,203.00 in settlement, included the amount on her 1984 return, and later filed an amended return to exclude that amount. *Id.* The court called *Revenue Ruling 84-108* an "unwarranted administrative amendment of the clear language of the Internal Revenue Code," and read § 104(a)(2) as "express[ing] clearly the congressional intent to exclude wrongful death proceeds—regardless of whether those proceeds are classified as compensatory or punitive—from gross income." *Id.* The court thought that the Service had inappropriately relied on *Glenshaw Glass* where the punitive damages were awarded in addition to the amount necessary to compensate the plaintiff for his losses. *See id.* at 637. The court clearly read § 104(a)(2) to exclude from gross income all damages received under any wrongful death acts because those damages were personal injury proceeds. *See id.* at 638.

In *Revenue Ruling 85-98*, the taxpayer sued a newspaper for alleged defamation injuring his personal reputation as an individual. 1985-2 C.B. 51. The complaint stated that the taxpayer had suffered damage to his personal reputation, social standing, and family relationship, and that the article caused him embarrassment, shame, anxiety, and worry. *Id.* Following a prayer for both compensatory and punitive damages, the parties settled, awarding the taxpayer an unallocated lump sum payment. *Id.* The Ruling held that 25% of the award was allocated as compensatory damages, excluded under § 104(a)(2), and 75% of the award was allocated as punitive damages, included in the taxpayer's gross income. *Id.* at 52. In coming to its conclusion, the Service relied on *Rev. Rul. 58-418*, 1958-2 C.B. 18, and *Rev. Rul. 75-230*, 1975-1 C.B. 93, where amounts consisting of both compensatory and punitive damages were allocated between the two according to the best evidence accessible under the circumstances and facts of the case. 1985-2 C.B. at 51-52.

The most recent amendment prior to 1996 took place in 1989. *See Omnibus Budget Reconciliation Act of 1989*, Pub. L. No. 101-239, § 7641, 103 Stat. 2106, 2379 (current version at 26 U.S.C. § 1996). This amendment required punitive damages to be included in gross income unless the income arose from a physical injury or sickness. *Id.* ("Paragraph (2) shall not apply to any punitive damages in connection with a case not involving physical injury or physical sickness."). The Conference Report implies that Congress acted in response to the then current case law, holding that the taxpayer could exclude damages recovered as a result of a personal injury "even though there. . . [was] no physical injury, for example, in cases involving employment discrimination." 135 Cong. Rec. 30823, 31002 (1989). Interestingly, as will be discussed later, discrimination damages were also a reason given for the 1996 amendment. *See infra* notes 597-98 and accompanying text.

205. *Id.* at 348.

Roemer v. Commissioner,²⁰⁶ then on appeal to the Ninth Circuit.²⁰⁷ Here, the Tax Court elevated the importance of the predominant nature of the claim analysis in the application of § 104(a)(2) and thus, diminished the predominance of the intent of the payor test.²⁰⁸

I. *Roemer: The Nature of the Claim Test Revisited*

Roemer v. Commissioner, first decided in the Tax Court in 1982, concerned an action against a credit bureau that had grossly defamed a taxpayer in a credit report, causing diminished profit and damage to his professional and business reputation.²⁰⁹ The taxpayer, Roemer, developed a successful casualty insurance brokerage company and contemplated an expansion of his business into life insurance.²¹⁰ Roemer submitted an application seeking authorization from Penn Life Mutual Company (Penn) to form a partnership for the sale of life insurance.²¹¹ The credit bureau sent to Penn and other insurance companies a report impugning Roemer's honesty and erroneously stating that he "neglected his clients' affairs, was recently fired from his position as president of an insurance firm, and intentionally defaced property belonging to others."²¹² A jury awarded the taxpayer who had enjoyed an excellent reputation, both personally and professionally, \$40,000 in compensatory damages and \$250,000 in punitive damages.²¹³ In his tax return, Roemer included only a portion of the award as income, and the Commissioner issued a deficiency declaring the entire amount of the judgment taxable.²¹⁴

The Tax Court first stated that under Treasury Regulation 1.104-1(c), the term "damages received means an amount received from an action based on tort or tort-type rights" and emphasized that the regulation makes "no

206. 79 T.C. 398 (1982).

207. *Roemer v. Comm'r*, 716 F.2d 693 (9th Cir. 1983).

208. See *Nussbaum*, 45 T.C.M. at 348.

209. 79 T.C. 398, 400 (1982). Roemer enjoyed an annual gross income near \$300,000.00 before Retail Credit's defamation. *Id.* at 399-400. Roemer's lawyer estimated that his client had lost \$136,000.00 as a result of Retail Credit's defamatory acts. *Id.* at 406.

210. *Id.* at 400.

211. *Id.*

212. 79 T.C. at 400. When Roemer gained knowledge of the circulation of the defamatory report, he asked Retail Credit to issue a retraction. *Id.* Instead of retracting the defamatory statements, Retail Credit distributed a retraction containing additional defamatory "innuendoes" regarding Roemer's business and personal reputation as an agent. *Id.*

213. *Id.* at 399, 401, 403.

214. *Id.* at 403-04. In his federal income tax return for 1975, the taxpayer reported \$16,020.00 of the damage portion of the recovery as income, \$7,751.00 for costs and \$23,371.00 as interest income. *Id.* at 403. In his amended petition, the taxpayer alleged he had incorrectly reported \$16,020.00 of the damage portion of the recovery and \$7,751.00 of the costs. *Id.* at 403-04.

distinction between physical and mental or emotional injuries.”²¹⁵ The Tax Court then stressed that “[t]he law is settled that the tax consequences of an award for damages depend on the nature of the litigation and on the origin and character of the claims adjudicated, but not the validity of such claims.”²¹⁶ Therefore, the Tax Court found that “[t]he proper inquiry is in lieu of what were the damages awarded?”²¹⁷ Because the jury award did not apportion the damages, Roemer argued that although some part of the award was in lieu of his professional reputation being damaged, an “inextricable combination of damages to both professional and personal reputation” existed to exclude the entire award from income.²¹⁸ The Commissioner argued that Roemer’s damage was predominantly to his professional reputation, and thus the whole award should be taxable.²¹⁹

Before siding with the Commissioner, the Tax Court stated that for purposes of the § 104(a)(2) exclusion, a “distinction must be made” between awards received in lieu of damages to professional reputation and those to personal reputation.²²⁰ The Tax Court held that a taxpayer may exclude an award from gross income to the extent that the evidence proves that the award was received in lieu of damage to an individual’s personal reputation.²²¹ Based on allegations in Roemer’s complaint, testimony at the libel trial, and his lawyer’s closing statement, the Tax Court found that the “predominant nature” of Roemer’s claim *involved damages to his professional and business reputation*. Moreover, concluding that the whole award was taxable, the court found that the petitioner had failed to establish that the compensatory damages remedied personal injury within the meaning of § 104(a)(2).²²²

A year later, on appeal, the Ninth Circuit admonished the Tax Court for confusing the “nature of the claim” with the nature of the damages.²²³

215. 79 T.C. at 405.

216. *Id.* (citing *Woodward v. Comm’r*, 397 U.S. 572, 578 (1970); *United States v. Gilmore*, 372 U.S. 39, 49-50 (1963); *Seay v. Comm’r*, 58 T.C. 32, 36-37 (1972)).

217. *Id.*

218. *Id.*

219. *Id.*

220. 79 T.C. at 405.

221. *See id.* at 406. *See also* Stuart M. Schabes, Comment, *Roemer v. Comm’r*, 12 HOFSTRA L. REV. 211, 214 (1983) (criticizing the Tax Court in *Roemer* for making an unsubstantiated and unjustified distinction under the § 104(a)(2) exclusion, between awards received in lieu of damages to personal reputation and those to professional reputation).

222. *See id.* at 407-08.

223. *Roemer v. Comm’r*, 716 F.2d 693, 697 (9th Cir. 1983). The Ninth Circuit’s approach should not be confused with the “predominant nature of the claim” test used in *Nussbaum*, which focuses upon the tort and contract dichotomy to determine whether the claims being settled are primarily contract or tort. *See Nussbaum v. Comm’r*, 45 T.C.M. (CCH) 346, 348 (1982).

Stressing that under California law, a defamation claim flows from a personal attack on an individual,²²⁴ the court reasoned that the “nonpersonal consequences of a personal injury, such as a loss of future income, are often the most persuasive means of proving the extent of the injury that was suffered” but that “[t]he personal nature of an injury should not be defined by its effect.”²²⁵ Moreover, “[w]hen an individual recovers damages for a physical personal injury, the *lump-sum award is not allocated between the personal aspects of the injury and the economic loss occasioned by the personal injury*, nor is the taxpayer precluded from use of § 104(a)(2) when the predominant result of the injury is a loss of income.”²²⁶ Therefore, because Roemer’s “defamation suit was brought to remedy a personal injury[,] . . . the award should not be differentiated on the basis of the resulting damage to his personal life and his professional career.”²²⁷ In properly directing the inquiry to the nature of the claim rather than to the nature of the damage resulting therefrom, the Ninth Circuit held that the compensatory and punitive damages were to be excluded under § 104(a)(2) “on account of any personal injury.”²²⁸

Before the Ninth Circuit’s reversal of *Roemer* but after its decision in *Roemer*, the Tax Court decided *Church v. Commissioner*.²²⁹ In *Church*, a newspaper accused a taxpayer of being a communist, following a speech that the taxpayer delivered in opposition to lobbying groups.²³⁰ As a result of a successful libel suit, the jury awarded the taxpayer \$250,000 in compensatory damages and \$235,000 in punitive damages.²³¹

224. *Roemer*, 716 F.2d at 699. After a lengthy discussion on the history of § 104(a)(2), the Court of Appeals for the Ninth Circuit determined that the nature of the tort of defamation in California will be the subject of the inquiry under the nature of the claim test, and the intent of the payor test as developed in *Agar*, played no part in the outcome of the case because *Roemer* does not involve a settlement. *See id.* at 697 n.3. The Ninth Circuit then went on to discuss the history of the claim of defamation in California and determined that a defamation claim is indeed personal, especially in light of the fact that California has a separate claim for trade libel, which allows plaintiffs to remedy attacks made on their services or products. *See id.* at 699.

225. *Id.* This type of analysis can be traced as far back as *Raytheon Prod. Corp. v. Comm’r*, 144 F.2d 110, 113-14 (1st Cir. 1944), and *Farmers’ & Merchants’ Bank v. Comm’r*, 59 F.2d 912, 913 (6th Cir. 1932) (“[E]arnings before the injury, as compared with those afterward, were only an evidential factor in determining actual loss.”).

226. *Roemer*, 716 F.2d at 697 (emphasis added).

227. *Id.* at 700.

228. *Id.* For the proposition that taxability of damages depends on the underlying nature of the claim, see *United States v. Safety Car Heating and Lighting Co.*, 297 U.S. 88, 98 (1936) (stating that “[t]o determine what the respondent got we are to consider what it did, and not what it could have had if it had made another choice”). *But see* *Comm’r v. Miller*, 914 F.2d 586 (4th Cir. 1990) (punitive damages are received on account of defendant’s conduct and therefore are not excludable).

229. 80 T.C. 1104 (1983).

230. *Id.* at 1105.

231. *Id.* at 1106.

Finding that the trial court awarded compensatory damages on account of personal injury, the Tax Court held that the compensatory and punitive damages were excludable under § 104(a)(2).²³² The Tax Court distinguished the *Roemer and Church* opinions solely on the basis of whether the damages awarded were compensating business versus personal injury.²³³ Once again, the Tax Court focused its inquiry on the consequences flowing from the injury rather than the nature of the claim.²³⁴ Furthermore, the court stated that “personal injuries or sickness are not limited to physical trauma but include mental pain and suffering.”²³⁵ The “shattered dreams, ruined careers, and the mental anguish that follow are just as personal as, for instance, loss of [a] limb.”²³⁶ No monetary award can wash away the stigma that the taxpayer must deal with for life.²³⁷

The discrepancy between the Ninth Circuit’s decision in *Roemer* and the Tax Court’s ruling in *Church* prompted administrative rulings on the taxation of personal injury recoveries.²³⁸ In *Revenue Ruling 85-143* of 1985, the Service refused to acquiesce to the Ninth Circuit’s decision in *Roemer* and stated that it would follow the Tax Court’s *Roemer* decision.²³⁹ Accordingly, the Service found a valid distinction between compensatory damages awarded for damage to personal versus professional reputation.²⁴⁰ Damages awarded for injury to professional reputation are not awarded on account of personal injury.²⁴¹ Therefore, damages received in a libel action for injury to the taxpayer’s professional reputation, like in *Roemer*, are not excludable under § 104(a)(2).²⁴² Whether libel is a personal injury in a particular situation depends on the nature of the libel rather than the nature of the claim.²⁴³ Thus the characterization of a lawsuit brought under state law would not be controlling for federal income tax purposes.

Only one year later, the Tax Court abandoned its reasoning in *Roemer* and consequently, severely undercut support for the administrative interpretation distinguishing between personal and professional injury

232. *See id.* at 1110.

233. *See id.* at 1105-06, 1110.

234. 80 T.C. at 1108. The court examined the allegations in the complaint, the evidence adduced at trial, and the statements of counsel. *See id.* at 1107.

235. *Id.* at 1106.

236. *Id.* at 1109.

237. *See id.* at 1110.

238. Rev. Rule 85-143, 1985-2 C.B. 55; Rev. Rul. 84-108, 1984-2 C.B. 32.

239. 1985-2 C.B. 55.

240. *Id.* at 55-56.

241. *Id.* at 56.

242. *Id.*

243. *Id.*

damages in *Threlkeld v. Commissioner*.²⁴⁴ In *Threlkeld*, the taxpayer received an award of \$300,000 in damages pursuant to a settlement agreement that arose out of a suit for malicious prosecution.²⁴⁵ The agreement allocated specific amounts of the award to various injuries.²⁴⁶

Before it decided the taxability of the taxpayer's damage award, the Tax Court discussed the judiciary's disparate treatment of taxpayers who received damages for injury to personal reputation and those who received damages for injury to professional reputation.²⁴⁷ To illustrate the disparate effects that courts created, the Tax Court presented a hypothetical of a young surgeon who loses a finger as the result of a tortious act.²⁴⁸ The court stated that the surgeon's loss of a finger will cause "physical and emotional pain and suffering" as well as loss of future income, and "the surgeon will likely produce evidence of both" types of damages.²⁴⁹ However, because it is easier to calculate the loss of future income based on a present dollar value than physical and emotional pain and suffering, "the surgeon will quite predictably place greater emphasis on lost income as a measure of his damages and will perhaps, thereby, receive a greater recovery," the entire amount of which can be excluded from income.²⁵⁰ This surgeon's loss of future income award, compensating a physical injury incurred through a third party's tortious act, "raises no troubling questions [about] exclusion" under § 104(a)(2). However, a taxpayer who suffers and receives damages for nonphysical injuries also incurred through a third party's tortious act will likely be treated differently. Courts "have, in the past, ignored the personal nature of the claim and delved into an inquiry regarding the nature of the consequences of the injury."²⁵¹

This hypothetical highlights how courts distinguish between the taxability of physical and nonphysical personal injuries. It also illustrates how taxpayers receiving damages for a physical personal injury can apply § 104(a)(2) to all claims flowing therefrom without scrutiny, including claims for lost income. In contrast, taxpayers receiving damages for a nonphysical personal injury, such as reputation damage, must undergo a judicial inquiry to determine whether the components of the award are for injury to personal or professional reputation.

244. 87 T.C. 1294, 1296 (1986).

245. *Id.* at 1296.

246. *Id.* at 1295-96.

247. *Id.* at 1300.

248. *Id.*

249. *Threlkeld*, 87 T.C. at 1300-01.

250. *Id.*

251. *Id.*

With this seemingly inequitable hypothetical in mind, the Tax Court in *Threlkeld*, then changed tides and adopted the Ninth Circuit's four point *Roemer* test: (1) the excludability of the award is dependant upon the nature of the claim and not upon the validity of the claim;²⁵² (2) no distinction is to be made between physical and nonphysical injury;²⁵³ (3) no distinction should be made for damages received for injury to professional reputation and damages received for injury to personal reputation;²⁵⁴ and (4) "whether the damages received are paid on account of 'personal injuries' should be the beginning and the end of the inquiry."²⁵⁵

The Tax Court thus rejected the professional and personal distinction, concluding that the "appropriate question for purposes of § 104(a)(2) is whether the damages were received on account of personal injuries."²⁵⁶ In analyzing what constitutes a personal injury the court stated that the concept of personal injury has long included nonphysical as well as physical injuries. Specifically, personal injuries are "injuries resulting from invasions of rights that inhere in man as a rational being, that is, rights to which one is entitled by reason of being a person in the eyes of the law."²⁵⁷

In concluding that *Threlkeld*'s damage settlement in a malicious prosecution suit was received for personal injury and, therefore, was excludable under § 104(a)(2), the Tax Court, like the Ninth Circuit in *Roemer*, reviewed the "nature of the claim," applied a totality of the circumstances approach, and refused to find the settlement agreement allocating damages for specific injuries incurred from the malicious prosecution controlling of whether the claim was for a personal injury.²⁵⁸

The Sixth Circuit affirmed the Tax Court's decision in *Threlkeld* one year later, by expressly adopting the "nature of the claim" test and stating that it

252. *Id.* at 1297 (citing to *Bent v. Comm'r*, 87 T.C. 236 (1986); *Glynn v. Comm'r*, 76 T.C. 116, 119, *aff'd*, 676 F.2d 682 (1st Cir. 1981); *Seay v. Comm'r*, 58 T.C. 32, 37 (1972)).

253. *Id.* (citing *Seay v. Comm'r*, 58 T.C. 32, 40 (1972)).

254. *Id.* at 1298.

255. 87 T.C. at 1299.

256. *Id.* at 1305.

257. *Id.* at 1307-08 (quoting *Brown v. Dunstan*, 409 S.W.2d 365, 367 (Tenn. 1966) (quoting *Commerce Oil Refining Corp. v. Miner*, 199 A.2d 606, 610 (R.I. 1964))).

258. 87 T.C. at 1305-8. "In such cases, we must look to various factors, including the allegations in the State court pleadings, the evidence adduced at trial, a written settlement agreement, and the intent of the payer . . ." *Id.* at 1306. In a brief dissent, Judge Simpson stated that, "if the words of section 104(a)(2) have any meaning, they surely do not permit the exclusion of damages declared to be for injury to a professional reputation." *Id.* at 1309 (Simpson, J., dissenting). The Tax Court had a long tradition of drawing a distinction between damage to "personal" and "business" or "professional" reputation. *Threlkeld* was a departure from this history. *See, e.g.*, *Roemer v. Comm'r*, 79 T.C. 398, 405 (1982); *Draper v. Comm'r*, 26 T.C. 201, 203-04 (1956); *Agar v. Comm'r*, 19 T.C.M. (CCH) 116, 119 (1960).

was unreasonable to distinguish between injury to personal and professional reputation. Thereby, the Sixth Circuit also affirmatively rejected the Service's *Revenue Ruling 85-143*.²⁵⁹

Interestingly, the Tax Court's decision in *Roemer* and *Church* seems to be a brief hiatus from precedent. In *Bent v. Commissioner*, decided four months prior to the Tax Court's decision in *Roemer*, the Tax Court considered the taxability of damages recovered in 42 U.S.C. § 1983 settlement against her employer for violating the taxpayer's First Amendment rights to freedom of speech.²⁶⁰ Neither the release nor the settlement check made any allocation of the damage award among the various injuries.²⁶¹ The Commissioner argued that the entire settlement should be included as income because it represented to the employer three years of lost wages and attorney's fees.²⁶² The petitioner asserted that the First Amendment violation was a tort-type personal injury violation and, therefore, the damages awarded were excludable from income.²⁶³ The Tax Court held that the taxpayer received damages for personal injuries under the § 1983 claim for violation of the First Amendment and that the payor's intent was irrelevant.²⁶⁴ Thus, the Tax Court agreed with the petitioner that "[i]t is abundantly clear that 'lost earnings' is a proper element of compensatory damages that may be awarded under § 1983 in order to redress the party who has been injured by a deprivation of First Amendment rights under color of State law."²⁶⁵ The court treated lost wages as "an evidentiary factor in determining the amount by which . . . [the taxpayer] was damaged," rather than as "an independent basis for recovery" not associated with the taxpayer's nonphysical personal injury.²⁶⁶ Over one year later on appeal, the Third Circuit affirmed the Tax Court's decision in *Bent*, expressly agreeing with the Ninth Circuit's

259. See *Threlkeld v. Comm'r*, 848 F.2d 81 (6th Cir. 1988). Compare *id.* at 84 with Rev. Rul. 85-143, 1985-2 C.B. 55.

260. 87 T.C. 236 (1986).

261. *Id.* at 242.

262. *Id.* at 243.

263. *Id.*

264. *Id.* at 246.

265. 87 T.C. at 250. In *Metzger v. Comm'r*, an associate professor entered into a settlement agreement for a claim brought for breach of contract and violation of her right to be free from discrimination on account of national origin and gender under several federal statutes. 88 T.C. 834 (1987). The agreement called for half of the \$75,000 settlement to be paid for wages claims. See *id.* at 841-45. The Tax Court held that the petitioner could exclude half of the settlement that was allocated towards damages for her personal injury. *Id.* at 859-60. In deciding this, the Tax Court looked to the payor's intent and the nature of the claim and found that because the settlement was in exchange for release of all claims, half of the settlement was allocated toward the contract claims and half toward the statutory claims. See *id.* at 850, 859.

266. *Bent*, 87 T.C. at 251.

reasoning in *Roemer*.²⁶⁷

J. Dignitary Torts and § 104(a)(2)

Dignitary tort rights, such as those rights provided by Title VII, ADEA, Title IX, and § 1983, are congressional attempts to protect persons from various types of personal discrimination and the injuries resulting therefrom. These congressional protections provided a renewed focus on the historical problems and concerns courts have experienced in determining the taxability of nonphysical injuries. In *Thompson v. Commissioner*, published in 1989, the Tax Court decided a § 104(a)(2) claim awarding back pay and liquidated damages.²⁶⁸ In a Title VII and Equal Pay Act (EPA) class action sex discrimination suit for wage disparity, the taxpayer was awarded a total of \$66,795.19 in back wages under the EPA and Title VII and \$66,135.27 in liquidated damages under the EPA.²⁶⁹ The taxpayer reported only the back pay award as income and the Commissioner declared a deficiency for the liquidated damages.²⁷⁰

Focusing separately on the remedies available under the EPA and Title VII, the Tax Court concluded that the taxpayer's back pay recovery under the EPA was not in the nature of damages received under a tort or tort-type claim but was for breach of contract.²⁷¹ Returning to the "in lieu of what" test, it

267. *Bent v. Comm'r*, 835 F.2d 67 (1987). In affirming the Tax Court in *Bent*, the Court of Appeals for the Third Circuit agreed with the Ninth Circuit's opinion in *Roemer* and quoted extensively from it as follows:

The relevant distinction that should be made is between personal and nonpersonal injuries, not between physical and nonphysical injuries. I.R.C. § 104(a)(2) states that damages received on account of *personal* injuries are excludable; it says nothing about physical injuries. "[T]he words of statutes—including revenue acts—should be interpreted where possible in their ordinary everyday senses." *Crane v. Comm'r*, 331 U.S. 1, 6, 67 S. Ct. 1047, 1051, 91 L.Ed. 1301 (1947). The ordinary meaning of a personal injury is not limited to a physical one. Indeed, the Service has long said that certain nonphysical injuries are personal injuries and that all damages received for nonphysical personal injuries are excludable from gross income. Sol. Op. 132, 1—1 C.B. 92 (1922) (damages for alienation of affections, defamation of personal character, and surrender of child custody rights are damages for invasion of personal rights and not income).

Bent, 835 F.2d at 70 (quoting *Roemer v. Comm'r*, 716 F.2d 693, 697 (9th Cir. 1983) and citing *Memphis Cmty. Sch. Dist. v. Stachura*, 477 U.S. 299 (1986) (stating that mental anguish and emotional distress are "standard elements of compensatory damages" under § 1983)).

268. 89 T.C. 632, 633 (1987).

269. *See id.* at 633, 637. Thompson was the lead plaintiff against the United States Government Printing Office (GPO). *Id.* at 633. In 1982, the GPO in *Thompson v. Sawyer*, 678 F.2d 257 (D.C. Cir. 1982), *aff'g in part and rev'g in part*, *Thompson v. Boyle*, 499 F. Supp. 1147 (D.D.C. 1979), was found to have violated Title VII and the Equal Pay Act. *Id.*

270. 89 T.C. at 641-42. After trial, petitioner was allowed to amend its petition and assert that the back pay award was also excludable in light of the court's holding in *Threlkeld*. *Id.* at 642.

271. *See id.* at 646.

declared the back pay award taxable.²⁷² Distinguishing the instant case, the Tax Court found nothing in *Threlkeld* that converted a claim for back pay into one for personal injury solely because the suit involved a claim for tort-type personal injuries.²⁷³

In deciding whether the liquidated damages were taxable, the Tax Court employed the nature of the claim test.²⁷⁴ The Tax Court found that “[s]ince the right to be free from gender or sex discrimination is a personal right[,] . . . it follows that payments of damages made for violation of that right are damages for personal injuries.”²⁷⁵ Although here, the back pay award measured the liquidated damages, the liquidated damages were nevertheless compensation for a personal injury and excludable.²⁷⁶ The court’s reasoning was consistent with that of *Roemer*, *Threlkeld*, and *Bent* because evidence of nonpersonal damages can be used to measure the extent of a personal injury without changing the nature of the claim.

In affirming the Tax Court’s opinion in *Thompson*, the Court of Appeals for the Fourth Circuit noted that “[d]amages received on account of personal injuries or sickness are not limited to physical trauma.”²⁷⁷ The court applied the Ninth Circuit’s *Roemer* reasoning that excludability under § 104(a)(2) focuses on whether the nature of the claim is personal or nonpersonal, not on whether the injury is physical or nonphysical.²⁷⁸ The court stressed that the definition of a tort action—“a direct invasion of some legal right of the individual independent of contract”—justifies the dual holding that sex discrimination actions are tort or tort-type and that damages awarded for such violations are excludable as damages received on account of personal injuries.²⁷⁹ In concluding that the back pay award was taxable, however, the court noted that if the taxpayer was allowed to exclude her back pay award under § 104(a)(2) she would take an advantage over other co-workers

272. *See id.* (“[W]hether the rights created by the Equal Pay Act are considered as in the nature of contract and rights or some other right entitling a person to recover withheld pay, they are certainly not a claim for damages for the personal injury of sex discrimination.”).

273. 89 T.C. at 647.

274. *See id.* at 648 (relying on earlier cases such as *Metzger* and *Bent* to support the conclusion that a claim alleging violation of a person’s federal civil rights might properly be viewed as a tort claim to redress personal injuries).

275. *Id.* at 649.

276. *See id.* at 650. The opinion of the Court of Appeals for the Circuit Court of the District of Columbia in *Thompson v. Sawyer* supports the proposition that liquidated damages are compensatory rather than punitive. 678 F.2d 257, 281 (D.C. Cir. 1982).

277. *Thompson v. Comm’r*, 866 F.2d 709, 711 (4th Cir. 1989) (quoting *Bent v. Comm’r*, 835 F.2d 67, 70 (3d Cir. 1987), and citing *Church v. Comm’r*, 80 T.C. 1104, 1106 (1983)).

278. *See id.* at 712.

279. *Id.* at 712 (internal quotes omitted) (quoting BLACK’S LAW DICTIONARY 1335 (5th ed. 1979)).

reporting their total earned wages as gross income.²⁸⁰ Other cases, which did not follow the Fourth Circuit's reasoning, held the entire award of damages nontaxable.²⁸¹

Against this background, three analogous ADEA cases were decided. The Third Circuit decided *Rickel v. Commissioner* on April 3, 1990.²⁸² The Sixth Circuit decided *Pistillo v. Commissioner* on August 24, 1990.²⁸³ The Ninth Circuit decided *Redfield v. Insurance Co. of North America* on August 6, 1991.²⁸⁴ In all three cases, the taxpayers asserted both contract and tort claims.²⁸⁵ This combination of claims required the courts to analyze the application of § 104(a)(2) to the manner in which each taxpayer was granted the respective award. Finding the entire award of damages excludable under § 104(a)(2), the Third Circuit in *Rickel* stated that "whether the damages were paid on account of a personal injury is the beginning and the end of the inquiry."²⁸⁶ Drawing heavily upon *Rickel*, the Sixth Circuit in *Pistillo* concluded that "an age discrimination claim is an assertion of a tort or tort-type right, rather than an economic right arising out of a contract," and therefore, damages under the ADEA are excludable under § 104(a)(2).²⁸⁷ Adopting the reasoning of the Third and Sixth Circuits, the Ninth Circuit in *Redfield* held "that age discrimination damages are tort-type recoveries for

280. *Id.* at 712 (internal quotes omitted) (quoting BLACK'S LAW DICTIONARY 1335 (5th ed. 1979)).

281. In *Byrne v. Comm'r*, the taxpayer was awarded \$20,000 in a settlement after being discharged from employment for cooperating with the Equal Employment Opportunity Commission (EEOC) in investigating her employer. 90 T.C. 1000, 1001-02, 1004-05 (1988). The Tax Court focused on the release in applying the nature of the claim test. *See id.* at 1007 n.4. Although the taxpayer contended that under New Jersey state law she made personal injury tort claims, the court stated that no federal authority was found which characterizes the relevant Fair Labor Standards Act of 1938 (FLSA) provision as redressing personal or tort-like injuries. *See id.* at 1008 n.5. The Tax Court stated that the taxpayer did not justify her exclusive reliance on the tort analogy when the contract action appears to apply equally well to the facts here. *See id.* at 1009. The Tax Court thus concluded that the federal claim seems to contain the elements of both the state tort and contract action and equally apportioned the settlement between excludable damages and nonexcludable damages. *See id.* at 1009-11. On appeal to the Third Circuit, the court, relying on *Roemer* and *Bent*, rejected the split-allocation settlement, balanced the predominant nature of the claims, and found that the taxpayer's damages were excludable because the FLSA statutory scheme redressed violations of personal injury tort or tort-type rights. *See* 883 F.2d 211, 215 (3d Cir. 1989). The court refused to follow the New Jersey Supreme Court's holding, stating that such a characterization does not bind the court's determination of these claims for tax purposes because such an issue is a matter of federal law, particularly in light of the presence of the FLSA in this case. *See id.* at 216.

282. 900 F.2d 655 (3d Cir. 1990).

283. 912 F.2d 145 (6th Cir. 1990).

284. 940 F.2d 542 (9th Cir. 1991).

285. *See Rickel*, 900 F.2d at 656-57; *Pistillo*, 912 F.2d at 146-47; *Redfield*, 940 F.2d at 544.

286. *Rickel*, 900 F.2d at 661 (internal quotes omitted) (quoting *Threlkeld v. Comm'r*, 87 T.C. 1294, 1299 (1986)).

287. *Pistillo*, 912 F.2d at 149.

personal injuries . . . [and as] such, they come within the purview of I.R.C. § 104(a)(2), and are excludable from gross income for the purposes of federal income tax.”²⁸⁸ *Rickel*, *Pistillo*, and *Redfield* were among the first cases to apply *Roemer* and its progeny in the context of age discrimination and to decline to apportion the damages awarded.²⁸⁹

Against the weight of authority and by using strict statutory construction the Circuit Court of Appeals for the District of Columbia decided *Sparrow v. Commissioner*, a case involving the settlement of a racial discrimination claim filed under Title VII.²⁹⁰ The D.C. Circuit focused on the meaning of the term “damages” as the ultimately determinative, threshold inquiry.²⁹¹ The court interpreted § 104(a)(2) as containing a two-part conjunctive test: “(1) the amount received must be damages and (2) the amount received as damages must result from a personal injury or sickness.”²⁹²

In deconstructing § 104(a)(2), the court reviewed the legal definition of “damages” from a historical perspective and determined that the term “embodie[d] a monetary amount originally awarded at law, not in equity.”²⁹³ Noting that “neither the Revenue Act of 1918 nor its legislative history defined the meaning of damages,” the court concluded that the word “damages,” as used in § 104(a)(2) today, should be interpreted by the meaning ascribed to it when § 213(b)(6) was originally enacted.²⁹⁴ Stating that “not all awards of monetary relief are properly characterized as the legal relief traditionally awarded in courts of law,” the court discussed whether a Title VII back pay award constitutes damages under this definition.²⁹⁵ Concluding that Title VII limits its “relief to equitable remedies,” the court held “that an award of back pay under Title VII does not constitute the legal

288. *Redfield*, 940 F.2d at 547 (internal quotes omitted).

289. See *Rickel*, 900 F.2d at 658-59; *Pistillo*, 912 F.2d at 148-49; *Redfield*, 940 F.2d at 545-46.

290. 949 F.2d 434, 436 (D.C. Cir. 1991).

291. See *id.* at 437. Because the court focuses on damages from the outset, the taxpayer must jump over two hurdles in order to fit within the gambit of the statute. See *id.* at 437 n.5 (“After the taxpayer . . . [shows that the award constitutes damages], he must then show that the amount was received as a result of a personal injury.”).

292. *Id.* at 436. Judge Karen Henderson wrote the opinion for a three judge panel with Chief Judge Abner Mikva and Judge David E. Sentelle joining. See *id.* at 434.

293. See *id.* at 437. The court also pointed out that under the Seventh Amendment, plaintiffs have traditionally been allowed jury trials when seeking damages. See *id.* See also *Ross v. Bernhard*, 396 U.S. 531, 534 (1970); *Capital Traction Co. v. Hof*, 174 U.S. 1, 13 (1899); *Whitehead v. Shattuck*, 138 U.S. 146, 151 (1891). See generally *Curtis v. Loether*, 415 U.S. 189 (1974).

294. *Sparrow*, 949 F.2d at 436-37. To establish that in 1918 damages were a remedy at law, the court cites *Curtis v. Loether*, 415 U.S. 189, 194 (1974), *Rice & Adams Corp. v. Lathrop*, 278 U.S. 509, 513 (1929), *United States v. Or. Lumber Co.*, 260 U.S. 290, 293 (1922), *Friederichsen v. Renard*, 247 U.S. 207, 208 (1918), *Archer v. Greenville Sand & Gravel Co.*, 233 U.S. 60, 64-66 (1914), and *Javierre v. Central Altigracia*, 217 U.S. 502 (1910). *Id.*

295. *Sparrow*, 949 F.2d at 437-38 (citations omitted) (internal quotations omitted).

remedy of damages.”²⁹⁶ Because the monetary award failed the first prong of the court’s test, the D.C. Circuit was able to sidestep the most critical issue—whether a successful race discrimination claim is a “personal injury” within the meaning of § 104(a)(2).

Against the opinion and reasoning of numerous other courts of appeals, the D.C. Court—just as “a derelict on the waters of the law”—attempted to justify its reasoning by deviating from precedent.²⁹⁷ By analyzing the historical meaning of damages under § 104(a)(2), the D.C. Court distinguished its approach from the other courts which had addressed the same issues. However, the D.C. Circuit’s narrow construction, relying on the historical meaning of the word damages conspicuously failed to address, or read out of § 104(a)(2) the word “any” preceeding the word “damages” in the statute. Interestingly, this court’s lonesome methodology foreshadowed the Supreme Court’s approach, which would define the term “personal injury” by reference to the statutory remedies.²⁹⁸

K. Burke and Schleier: The Supreme Court Gets Involved

In 1991, after approximately seventy-four years of silence the Supreme Court entered the conflict by granting *certiorari* to review the 1990 Sixth Circuit opinion in *United States v. Burke*.²⁹⁹ Burke sought to exclude back pay damages received from the Tennessee Valley Authority under a Title VII sexual discrimination claim.³⁰⁰ The Federal District Court for the Eastern District of Tennessee determined that the settlement award was taxable, applying *Raytheon*’s “in lieu of what” test³⁰¹ and the “intent of the payor” test crafted in *Agar*.³⁰² The Sixth Circuit reversed the District Court and relied on *Threlkeld*’s reasoning that the appropriate inquiry to determine § 104(a)(2) excludability was whether the injury and claim were “personal and tort like

296. *Id.* at 437, 438.

297. *Id.* at 439-40 (quoting *Lambert v. California*, 355 U.S. 225, 232 (1957) (Frankfurter, J., dissenting)).

298. *See* *United States v. Burke*, 504 U.S. 229, 233-37 (1992).

299. 504 U.S. 229 (1992).

300. *Id.* at 230.

301. *Burke v. United States*, No. 88-508, 1990 WL 56155, at *6-7 (E.D. Tenn. Mar. 20, 1990). *See also* *Raytheon Prod. Corp. v. Comm’r*, 144 F.2d 110, 111-13 (1st Cir. 1944). The “in lieu of what” test was applied in several other opinions. *See, e.g.*, *Church v. Comm’r*, 80 T.C. 1104, 1107 (1983); *Fono v. Comm’r*, 79 T.C. 680, 692 (1982); *Yates Indus. Inc. v. Comm’r*, 58 T.C. 961, 972 (1972).

302. *See* *Burke v. United States*, 1990 WL 56155, at *6 (citing *Knuckles v. Comm’r*, 349 F.2d 610, 613 (10th Cir. 1965); *Byrne v. Comm’r*, 90 T.C. 1000, 1007 (1988); *Metzger v. Comm’r*, 88 T.C. 834, 847-48 (1987); *Fono v. Comm’r*, 79 T.C. 680, 694 (1982), *aff’d without opinion*, 749 F.2d 37 (9th Cir. 1984); *Glynn v. Comm’r*, 76 T.C. 116, 120 (1981)).

in nature.”³⁰³ Accordingly, the Court found that a discrimination claim qualified as a “personal injury” and excluded Burke’s damages.³⁰⁴

The Supreme Court on the other hand, defined the nature of a right according to the available remedy.³⁰⁵ The Court emphasized that one of the essential “hallmarks of traditional [common law] tort liability is the availability of a broad range of damages to compensate . . . ‘fairly for injuries caused by the violation of [a person’s] legal rights.’”³⁰⁶ Contrasting the broad remedial freedom found in common law tort, the Court determined that Congress had so circumscribed the available Title VII remedies that the remedies themselves did not “evidence[] a tort-like conception of injury and remedy.”³⁰⁷ Because the Court found that the remedies specifically provided under Title VII did not include the right to jury trial or compensatory and punitive damages, the Court concluded that a sex discrimination Title VII claim was not a tort or tort-type right.³⁰⁸ Therefore, the Court held that the back pay award due to the taxpayer because of the discriminator’s underpayments were not excludable under § 104(a)(2) as compensatory damages received on account of personal injuries.³⁰⁹ Although the Court acknowledged the adoption of the Civil Rights Act of 1991 that specifically amended the Title VII’s remedial scheme to include compensatory and punitive damages,³¹⁰ it “examine[d] the law [only] as it existed [under] . . . ‘unamended’ Title VII,”³¹¹ meaning as Title VII was found in the 1964 statute.

Under the amended Title VII, Congress permitted disparate treatment

303. *Burke v. United States*, 929 F.2d 1119, 1121 (6th Cir. 1991). Here, the court does not follow the formulation of *Sparrow* providing for damages as the ultimate inquiry. However, it is possible that the *Sparrow* analysis was the precursor of the two-prong test developed in *Schleier*.

304. *Burke*, 929 F.2d at 1121, 1123 (finding that the government could not establish that the harm to a victim of sexual discrimination was any less “personal” than the harm to victims of other nonphysical injuries already found to be “personal” within the meaning of § 104(a)(2)) (citing *Byrne v. Comm’r*, 883 F.2d 211, 216 (3d Cir. 1989) (relying on *Bent* and *Roemer* to extend the exclusion under § 104 to retaliatory discharge claims under the Fair Labor Standards Act)); *Roemer v. Comm’r*, 716 F.2d 693, 700 (9th Cir. 1983) (holding that an injury stemming from a defamation suit is “personal” under § 104(a)(2)); *Threlkeld v. Comm’r*, 87 T.C. 1294, 1308, *aff’d*, 848 F.2d 81 (6th Cir. 1988) (finding an injury from a malicious prosecution as personal under § 104(a)(2)).

305. *United States v. Burke*, 504 U.S. 229, 234-35 (1992). Justice Harry Blackmun delivered the Court’s majority opinion. *Id.* at 230.

306. *Id.* at 235 (quoting *Carey v. Phipus*, 435 U.S. 247, 257 (1978)).

307. *Id.* at 239.

308. *See id.* at 238, 240.

309. *See id.* at 229, 242. For cases holding similarly for different reasons, see *Thompson v. Comm’r*, 89 T.C. 632 (1987), *aff’d*, 866 F.2d 709 (4th Cir. 1989) (back pay is included but liquidated damages is excluded); *Hodge v. Comm’r*, 64 T.C. 616 (1975); and *Sparrow v. Comm’r*, 57 T.C.M. (CCH) 816 (1989), *aff’d*, 949 F.2d 434 (1991).

310. *See Burke*, 504 U.S. at 235, 241 n.12.

311. *See id.* at 237 n.8.

plaintiffs, not disparate impact plaintiffs, to seek compensatory and punitive damages, indicating recovery for a tort or tort-type injury.³¹² Accordingly, a year after the Supreme Court's decision in *Burke*, the IRS concluded in *Revenue Ruling 93-98*, that because Congress amended Title VII in 1991 to allow back pay and compensatory damages such damage awards in Title VII claims were now excluded from income in disparate treatment discrimination cases but were not excluded from income in disparate impact cases.³¹³ The Revenue Ruling thus consistently applied *Burke*, elevating the remedy over the nature of the personal invasion of the right at the essence of the wrong being redressed.

Just three years later, three cases lured the Supreme Court into revisiting the conflict. *Downey v. Commissioner*,³¹⁴ *Schmitz v. Commissioner*,³¹⁵ and *Schleier v. Commissioner*³¹⁶ all arose out of a class action suit filed by employees of United Airlines for age discrimination under the ADEA and share virtually identical underlying facts.³¹⁷ All of these taxpayers worked as pilots for United Airlines, which had a policy of forcing its pilots to retire at the age of sixty.³¹⁸ The parties' settlement agreement labeled half of each monetary award as back pay and the other half as liquidated damages under the ADEA.³¹⁹ Each taxpayer initially excluded the liquidated damages and reported only the back pay as income.³²⁰ In each case, the IRS issued a deficiency notice asserting that the entire award of damages was taxable.³²¹ The Tax Court, however, determined that the entire settlement award in each case was excludable under § 104(a)(2).³²²

In *Downey*, the Tax Court relied on *Burke* and found that liquidated damages were traditionally associated with tort claims³²³ and "serve a deterrent or punitive purpose [which] further support[ed] the conclusion that

312. *See id.* at 62-63.

313. *See* 1993-2 C.B. 61.

314. 33 F.3d 836 (7th Cir. 1994).

315. 34 F.3d 790 (9th Cir. 1994).

316. 515 U.S. 323 (1995).

317. *Downey*, *Schmitz*, and *Schleier* all stem from the same ADEA action in *Monroe v. United Air Lines, Inc.* *See Schleier*, 515 U.S. at 326-27. *Monroe v. United Air Lines, Inc.* was a consolidated ADEA class action by 115 individual plaintiffs that worked for defendant, United Airlines (United). 736 F.2d 394 (7th Cir. 1984).

318. *See Schleier*, 515 U.S. at 325; *Downey*, 33 F.3d at 837; *Schmitz*, 34 F.3d at 791.

319. *See Schleier*, 515 U.S. at 326; *Downey*, 33 F.3d at 837; *Schmitz*, 34 F.3d at 791.

320. *See* cases cited *supra* note 319.

321. *See Schleier*, 515 U.S. at 327; *Downey*, 33 F.3d at 837; *Schmitz*, 34 F.3d at 791.

322. *See Schmitz*, 34 F.3d at 791; *Schleier v. Comm'r*, No. 22909-90, 1993 WL 767976 (T.C. July 7, 1993); *Downey v. Comm'r*, 97 T.C. 150 (1991), *aff'd on recon.*, 100 T.C. 634 (1993).

323. *See Downey*, 100 T.C. at 637 (citing *United States v. Burke*, 504 U.S. 229, 238 (1992)).

a claim under the ADEA is tort like.”³²⁴ Based on *Downey*, the Tax Court granted summary judgment in favor of the petitioners in *Schmitz* and *Schleier*.³²⁵ The Commissioner seized upon the unique opportunity to argue virtually the same case in three different courts of appeal and appealed the Tax Court decisions to the Courts of Appeals for the Fifth, Seventh, and Ninth Circuits.

The Seventh Circuit in the 1994 case of *Downey*, then examined whether the remedies provided under the ADEA were broad enough to embody the taxpayer’s age discrimination claim as a tort or tort-type right and, therefore, whether the ADEA awards remedied a “personal injury” within the ambit of *Burke*.³²⁶ The Seventh Circuit first creatively quoted the statute as “only ‘damages received . . . on account of *personal injuries* or sickness.’”³²⁷ The Court substitutes the word “only” for the word “any” before “damages”—albeit outside the quotation marks—signalling its intention to read the exclusion very narrowly. Thus for the first time, the Seventh Circuit restricted the “expansive”³²⁸ impact of the word “any” in the context of a

324. *Id.* at 637. *See also Downey*, 97 T.C. at 171 (stating that the Commissioner argued that under *Trans World Airlines, Inc. v. Thurston*, 469 U.S. 111 (1985), ADEA liquidated damages were the equivalent of punitive damages and, therefore, not excludable under § 104(a)(2)). The *Downey* Tax Court also rejected these arguments, as it had in *Rickel v. Comm’r*, 92 T.C. 510, 521-22 (1989). *See* 97 T.C. at 171.

325. *Schmitz*, 34 F.3d at 791; *Schleier v. Comm’r*, No. 22909-90, 1993 WL 767976 (T.C. July 7, 1993).

326. *See Downey*, 33 F.3d at 839. Other courts of appeals have addressed the issue of whether ADEA claims are tort-type claims. *See Redfield v. Ins. Co. of N. Am.*, 940 F.2d 542, 546 (9th Cir. 1991) (finding ADEA awards are tort-type awards and therefore excludable and “[n]othing in the ADEA reflects congressional attempt to rewrite the terms of employment contracts”); *Pistillo v. Comm’r*, 912 F.2d 145, 150 (6th Cir. 1990) (finding award excludable although award represented lost wages); *Rickel v. Comm’r*, 900 F.2d 655, 658 (3d Cir. 1990) (“[I]t is judicially well-established that the meaning of ‘personal injuries’ in this context encompasses . . . nonphysical as well as physical injuries.”). These other courts of appeals’ decisions were prior to *Burke*, and therefore, the *Downey* court limited its discussion to *Burke*. *See Downey*, 97 T.C. at 150.

327. *Id.* at 838.

328. The Third Circuit in *Rickel v. Comm’r* characterized the difference between the 1989 proposed and congressionally enacted amendments as follows:

Congress’ recent amendment to § 104(a)(2) in the 1989 Omnibus Budget Reconciliation Act, 103 Stat. 2379 (1989), which added the provision that: “Paragraph (2) shall not apply to any punitive damages in connection with a case not including physical injury or physical sickness.” This action is significant to our analysis because the original bill introduced in the House of Representatives would have limited the § 104(a)(2) exclusion to cases involving physical injury or physical sickness. As the House Ways and Means Committee explained the bill, “some courts have held that the exclusion applies to damages in cases involving employment discrimination,” but that the “committee believes that such treatment is inappropriate where no physical injury or sickness is involved.” H.R. REP. NO. 247, 101st Cong., 1st Sess. 1354-55, *reprinted in* 1990 U.S.C.C.A.N. 2824-25. The Senate bill contained no such amendment to § 104(a)(2). In its final conference bill, Congress chose to implicitly endorse the courts’ *expansive interpretation* of § 104(a)(2) to encompass nonphysical injuries and merely circumscribe the scope of the exemption as to only

discrimination claim.

Noting that all prior court decisions holding ADEA claims to be tort-like “antedate[d] the Supreme Court’s explanation of § 104(a)(2) in *Burke*,”³²⁹ the Seventh Circuit stated that for any federal statutory antidiscrimination claim to be considered tort-type the federal antidiscrimination statute must provide for compensatory damages redressing the intangible elements of a personal injury.³³⁰ Finding that ADEA liquidated damages replace prejudgment interest, the court held that “whatever the appropriate characterization of ADEA liquidated damages (be they punitive or contractual), as a matter of law they do not compensate for the intangible elements of a personal injury” and therefore are taxable.³³¹

The Ninth Circuit decided *Schmitz*³³² on the same day that the Seventh Circuit decided *Downey*.³³³ Although addressing the same underlying facts³³⁴ and relying on the same Supreme Court decision,³³⁵ legislative history, and statutory language,³³⁶ the Ninth Circuit concluded that the ADEA liquidated damages provision was tort-like.³³⁷ Because the ADEA provides for jury

one type of remedy, i.e., punitive damages, and not other types of remedies typically available in employment discrimination cases, such as back pay. H.R. CONF. REP. NO. 386, 101st Cong., 1st Sess. 622-23, reprinted in 1990 U.S.C.A.N. 3225-26. Cf. *Lorillard v. Pons*, 434 U.S. 575, 580 (1978) (“Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change.”).

900 F.2d 655, 664 (3d Cir. 1990) (emphasis added).

329. *Downey*, 33 F.3d at 838 (citing *Redfield v. Ins. Co. of N. Am.*, 940 F.2d 542 (9th Cir. 1991); *Rickel v. Comm’r*, 900 F.2d 655 (3d Cir. 1990); *Pistillo v. Comm’r*, 912 F.2d 145 (6th Cir. 1990)).

330. *See id.* at 839. In reversing the Tax Court, the Court of Appeals for the Seventh Circuit approvingly referenced Justice Scalia’s concurring opinion in *Burke*, which argued that § 104(a)(2) excluded only awards for injuries to physical or mental health. *See id.* at 837-38.

331. *Id.* at 840.

332. 34 F.3d 790 (9th Cir. 1994).

333. 33 F.3d 836 (7th Cir. 1994).

334. *See id.* at 837; *Schmitz*, 34 F.3d at 790-91.

335. *See United States v. Burke*, 504 U.S. 229 (1992).

336. *See Schmitz*, 34 F.3d at 792.

337. *See id.* at 796. In affirming the Tax Court, the Ninth Circuit stated that in order to establish excludability, *Schmitz* had to show (1) that his underlying cause of action was tort-like within the meaning of *Burke* and (2) that he received the damages on account of a personal injury. *See id.* at 792. The Ninth Circuit initially set forth its test, modified by *Burke*, in *United States v. Hawkins*, 30 F.3d 1077, 1081-82 (1994). While the IRS contended that the taxpayer had not met the tort-like nature standard because the ADEA does not provide any damages for emotional distress or pain and suffering, the Ninth Circuit disagreed, stating that “*Burke* does not require that a statute provide the complete spectrum of tort remedies before it may be deemed to redress a tort-type right.” *Schmitz*, 34 F.3d at 793 (citing *Bennett v. United States*, 30 Fed. Cl. 396, 400 (1994)). Liquidated damages are neither solely punitive nor unrelated to an ADEA plaintiff’s underlying personal injury. *Schmitz*, 34 F.3d at 794. Because the judiciary traditionally awards liquidated damages to compensate victims for obscure or difficult to prove damages, such damages result in an exclusion from a plaintiff’s gross income. *See id.*

Interestingly, the Seventh Circuit in *Downey* expressly relies on *Burke* and rejects *Rickel*, *Pistillo*,

trials, one of the missing factors that the Supreme Court emphasized in *Burke*,³³⁸ and the ADEA's legislative history and case law indicates that Congress intended to allow victims of willful discrimination greater compensation than victims of nonwillful discrimination,³³⁹ the Ninth Circuit reasoned that ADEA liquidated damages served both a punitive and compensatory function.³⁴⁰ The court concluded that the ADEA's remedial scheme satisfied the broad range of remedies specifically identified in *Burke* as tort-like and, therefore, allowed exclusion of the taxpayer's liquidated damages and back pay received under the ADEA.³⁴¹

To resolve the circuit split, the Supreme Court granted *certiorari* in *Schleier*.³⁴² Following the Seventh and Ninth Circuits and the Supreme Court in *Burke*, the *Schleier* Court based its determination of § 104(a)(2)'s tax consequences initially on the range of remedies available under the statute, rather than on the nature of the claim or injury.³⁴³ The majority noted that the ADEA constricts the remedies available to plaintiffs in two important ways. "First, unlike the Fair Labor Standards Act of 1938 (FLSA),³⁴⁴ the ADEA specifically provides that 'liquidated damages shall be payable only in cases of willful violations' Second, . . . the ADEA does not permit a separate recovery of compensatory damages for pain and suffering or emotional

and *Redfield*, while the Ninth Circuit in *Schmitz* relies not on *Burke* but on the post-*Burke* ADEA decision of *Purcell v. Seguin State Bank & Trust Co.* and the *Downey* Tax Court, which held ADEA damages excludable even under the more restrictive test of *Burke*. See *Downey*, 33 F.3d at 838; *Schmitz*, 34 F.3d at 792-93. In *Purcell v. Seguin State Bank & Trust Co.*, Purcell received liquidated damages under the ADEA in a age discrimination suit and the Court of Appeals for the Fifth Circuit found that his award exceeded his injury. 999 F.2d 950, 955 (5th Cir. 1993). When it recalculated the damages, the Fifth Circuit found it improper to increase damages to reflect the liability a plaintiff would have for income taxes. See *id.* at 961. The Fifth Circuit upheld the Tax Court's decision in *Downey* holding that *Burke* does not apply to ADEA claims because there is no doubt that ADEA claims are tort-like injuries. See *id.* at 960. If damages were increased in ADEA awards to reflect income tax liability before the § 104(a)(2) exclusion, ADEA plaintiffs would clearly be awarded too much in damages.

338. *Burke*, 504 U.S. at 240-41.

339. See *Schmitz*, 34 F.3d at 793-94, 796. The Commissioner argued that because they are available under the ADEA only in cases of willful discrimination, liquidated damages were therefore, solely punitive and not compensatory. The court rejected the argument stating:

In enacting ADEA, Congress [attempted] to balance the need[s] to compensate victims and [to] deter discrimination with the need to protect businesses from crushing liability [W]e see nothing "peculiar" in Congress's decision to resolve these competing interests by compensating victims of willful discrimination at a higher rate than victims of "non-willful" discrimination.

Id. at 795.

340. See *id.* at 794.

341. See *id.*

342. 515 U.S. 323 (1995).

343. See *id.* at 325-26.

344. For more information on the Fair Labor Standards Act of 1938 (FLSA), see *infra* notes 495-500.

distress.”³⁴⁵

Highlighting the broad definition and sweeping scope of gross income under § 61(a) with “the default rule of statutory interpretation that exclusions from income must be narrowly construed,”³⁴⁶ the Court went on to analyze the “plain language of § 104(a)(2)” and focused its attention on the statutory language, “on account of personal injuries.”³⁴⁷ Using a hypothetical automobile accident as an example, the Court acknowledged that while the injured victim may have sustained medical expenses, lost wages, and pain and suffering, the entire amount received in a settlement was excludable because each discrete segment of the award constituted damages “on account of personal injuries.”³⁴⁸ As authority for the proposition that lost wages were excludable as personal injuries under the Code, the Court cited to the Tax Court’s decision in *Threlkeld*, referencing the hypothetical of the surgeon who lost a finger.³⁴⁹ In addition, the Court made the assertion in a footnote that while the language, “on account of personal injuries,” may be textually ambiguous on the issue of the excludability of pain and suffering, “it is by now clear that § 104(a)(2) encompasses recoveries based on intangible as well as tangible harms.”³⁵⁰ The opinion states with regard to the ADEA settlement at issue however, that “[w]hether one treats respondent’s attaining the age of 60 or his being laid off on account of his age as the proximate cause of respondent’s loss of income, neither the birthday nor the discharge can fairly be described as a ‘personal injury’ or ‘sickness.’”³⁵¹ While the pilot may have experienced “some psychological or ‘personal’ injury [from

345. *Schleier*, 515 U.S. at 326 (citing *Schmitz v. Comm’r*, 34 F.3d 790 (9th Cir. 1994); *Goldstein v. Manhattan Indus., Inc.*, 758 F.2d 1435, 1446 (11th Cir. 1985); *Johnson v. Al Tech Specialties Steel Corp.*, 731 F.2d 143, 147 (2d Cir. 1984); *Perrell v. Finance Am. Corp.*, 726 F.2d 654 (10th Cir. 1984); *Hill v. Spiegel, Inc.*, 708 F.2d 233 (6th Cir. 1983); *Pfeiffer v. Essex Wire Corp.*, 682 F.2d 684, 687-88 (7th Cir. 1982); *Fiedler v. Indianhead Truck Line, Inc.*, 670 F.2d 806 (8th Cir. 1982); *Slatin v. Stanford Research Inst.*, 590 F.2d 1292 (4th Cir. 1979); *Vazquez v. E. Air Lines, Inc.*, 579 F.2d 107 (1st Cir. 1978); *Dean v. Am. Sec. Ins. Co.*, 559 F.2d 1036 (5th Cir. 1977); *Rogers v. Exxon Research & Eng’g Co.*, 550 F.2d 834 (3d Cir. 1977)). *See generally* HOWARD C. EGLIT, 2 AGE DISCRIMINATION §§ 8.30-9.42 (1997 & Supp. 1999); KALET, *supra* note 14, at 110-11.

346. *Schleier*, 515 U.S. at 327-28 (citing *Burke*, 504 U.S. 229, 244, 248 (1992) (Scalia, J., and Souter, J., concurring in judgment respectively); *United States v. Centennial Sav. Bank FSB*, 499 U.S. 573, 583 (1991); *Comm’r v. Jacobson*, 336 U.S. 28, 49 (1949)).

347. *Schleier*, 515 U.S. at 329-30.

348. *Id.* at 329.

349. *Id.* at 329-33 (citing *Threlkeld v. Comm’r*, 87 T.C. 1294, 1300 (1986)).

350. *Id.* at 329 & n.4. While the Court cites to both the majority opinion and Scalia’s concurring opinion in *Burke* for support, Scalia actually posited that the 1989 amendment to § 104(a)(2) clarified the fact that Congress intended the phrase “personal injuries or sickness” to include both physical and psychological harm or disease and to exclude “injuries that affect neither mind nor body.” *United States v. Burke*, 504 U.S. 229, 244-45 n.3. (1992) (Scalia, J., concurring).

351. *Schleier*, 515 U.S. at 330.

United Airlines unlawful termination] comparable to the intangible pain and suffering caused by an automobile accident,” clearly the pilot did not recover back wages because of such injury.³⁵² In contrasting the automobile accident to age discrimination, the Court found an intervening factor in its hypothetical: “[while] the accident causes a personal injury which in turn causes a loss of wages . . . the discrimination [independently] causes both personal injury and loss of wages . . . The amount of back wages recovered [in age discrimination cases] is completely independent of the existence or extent of any personal injury.”³⁵³ The Court then concluded that the § 104(a)(2) personal injury exclusion does not include the pilot’s back wages award because the pilot did not recover “back wages . . . ‘on account of’ any personal injury and because no personal injury affected the amount of back wages recovered.”³⁵⁴

In contention, the taxpayer first argued that the plain meaning of § 104(a)(2) includes liquidated damages, “too obscure and difficult of proof for estimate” as compensation for the victims personal injuries rather than as penalty to the payor.³⁵⁵ While the Court acknowledged that the House Conference Report accompanying the 1978 amendments to the ADEA contains language supporting the pilot’s argument that the ADEA liquidated damages were compensatory,³⁵⁶ the Court decided that nevertheless, the

352. *Id.* at 330.

353. *Id.*

354. *Id.* at 331. It is inconceivable to think that turning age sixty is the proximate cause of anything.

It strains the imagination to say that while age discrimination caused plaintiff’s loss of wages, plaintiff’s “being fired” (by whom and why, we may ask) was a closer, independent, and more proximate cause sufficient to make age discrimination no longer a legally relevant cause of plaintiff’s lost wages. Remember, a defendant is liable under the ADEA only if the defendant takes some adverse employment action against the plaintiff, like reducing his pay or firing him on account of age. Yet, when we consider taxation, somehow the loss of wages was not “caused” by the age discrimination. If that really is true, the defendant is not liable under the ADEA—because the event of his birthday, or his “being fired” (and not the age discrimination), caused his loss of wages.

F. Philip Manns, Jr., *Down and Out: RIFed Employees, Taxes, and Employment Discrimination Claims After Burke and Schleier*, 44 U. KAN. L. REV. 103, 123-24 (1995). See also David B. Jennings, Note, *The Supreme Court Gets Tough with I.R.C. § 104(a)(2) Exclusions: Taxpayer Discrimination Awards Suffer Injury as a Result of Commissioner v. Schleier*, 40 ST. LOUIS U. L.J. 865, 888-89 (1996).

355. *Schleier*, 515 U.S. at 331 (internal quotations omitted) (citing *Overnight Motor Transp. Co. v. Missel*, 316 U.S. 572 (1942)).

356. *Schleier*, 515 U.S. at 332 n.5. Respondent’s argued in their brief that “[i]f Congress had wished to provide for an exclusively punitive remedy in the ADEA, it could just as easily have authorized victims of age discrimination to recover ‘fines,’ ‘penalties,’ ‘exemplary damages,’ or ‘punitive damages.’” Brief for Respondent at 16, *Commissioner v. Schleier*, 515 U.S. 323 (1995) (No. 94-500). The House Conference Report accompanying the ADEA Amendments of 1978 unequivocally supported Respondent’s position that liquidated damages constituted legal compensatory relief for

provisions of the ADEA were punitive in nature.³⁵⁷ Furthermore, the Court reasoned that because the ADEA only permitted liquidated damages for willful violations, they were punitive and not awarded “on account of personal injury or sickness.”³⁵⁸

Second, the taxpayer proposed that Treasury Regulation Section 1.104-1(c)³⁵⁹ makes ADEA actions tort or tort-type and thus, this liquidated damages award was excludable.³⁶⁰ The Court viewed the taxpayer’s contention based on the Commissioner’s regulation as an attempt to circumvent the plain meaning of the statute.³⁶¹ The Court found that the Treasury Regulation repeats the statutory requirement that the taxpayer receive the damage award for personal injuries or sickness and adds the requirement that the taxpayer receive the damages in a tort-type action.

Third, even if the liquidated damages were punitive in nature,³⁶² the taxpayer asserted that the Court’s decision in *Burke* considering the availability of jury trials and punitive damages as indicators that a claim may be in tort or of a tort-type, compelled it to hold the ADEA claim in this case to be tort or tort-type and thus the damages to be excludable because both jury trials and liquidated damages were available under the ADEA’s remedial scheme.³⁶³ The Court noted that *Burke* emphasized the lack of jury

difficult to estimate intangible injuries. Specifically, the Report stated the following in regards to providing liquidated damages for legal relief:

[A party must] have the factual issues underlying such a claim decided by a jury. The ADEA as amended by the act does not provide remedies of a punitive nature. The Conferees therefore agreed to permit a jury trial of the factual issues underlying a claim for liquidated damages because the Supreme Court had made clear that an award of liquidated damages under the FLSA was not a penalty but rather was available in order to provide full compensatory relief for losses that were “too obscure and difficult of proof for estimate other than by liquidated damages.”

H.R. CONF. REP. NO. 95-950, at 14 (1978), reprinted in 1978 U.S.C.C.A.N. 504, 535 (internal citations omitted) (quoting *Overnight Motor Transp. Co. v. Missel*, 316 U.S. 572, 583-84 (1942)). The above quotation from *Missel* and included in the House of Representatives’ Conference Report is particularly interesting in that the *Schleier* Court discounted this legislative history and rather indicated that Congress may not have been aware of the *Missel* Court’s statement. See *Comm’r v. Schleier*, 515 U.S. 323, 332 (1995).

357. *Schleier*, 515 U.S. at 331 (citing *Trans World Airlines, Inc. v. Thurston*, 469 U.S. 111, 126 (1985), and *Lorillard v. Pons*, 434 U.S. 575, 581 (1978)).

358. *Schleier*, 515 U.S. at 332. The Court in footnote six stated that it found “odd” Justice Sandra Day O’Connor’s assertion in the dissent, that the majority holding presumed intangible harms from discrimination were not personal injuries. See *id.* The majority further stated that while the intangible harms of discrimination could constitute a personal injury, liquidated damages under ADEA did not necessarily compensate the victim on account of such harms. See *id.*

359. See *Treas. Reg. § 1.104-1(c)* (1994). Promulgated in 1956, this regulation is long-standing. See also T.D. 6169, 1956-1 C.B. 63.

360. *Schleier*, 515 U.S. at 333.

361. See *id.*

362. See *id.*

363. See *id.* at 334.

trials and punitive damages as factors in deciding that a claim was not in tort or of a tort-type; however, the Court concluded that *Burke* had not decided whether the presence of jury trials, punitive damages, “or both of those factors[,] would be sufficient to bring a statutory claim within the coverage of the regulation.”³⁶⁴ The *Schleier* majority held that *Burke* is narrower than the taxpayer contended because in *Burke*, the determination of a tort or tort-type claim is not the beginning or the end of the analysis under § 104(a)(2).³⁶⁵ Rather, the majority interpreted *Burke* as holding that the presence of compensatory damages was the primary indicator of whether a claim was tort or tort-type.³⁶⁶ Therefore, because Congress limited the ADEA’s remedial scheme to economically motivated back wages and what the Court characterized as noncompensatory liquidated damages, ADEA damages were not tort or tort-type and were included in income.³⁶⁷ In consolation to the taxpayer, the *Schleier* majority noted that the presence of jury trials and liquidated damages made *Schleier* a “closer case than *Burke*.”³⁶⁸

The Court concluded that in order to qualify damages under § 104(a)(2), the action must first be based upon the violation of a tort or tort-type right, and the award must then be received on account of personal injury or sickness.³⁶⁹ Because the taxpayer could satisfy neither of the prongs, with respect to the back pay or the liquidated damages, the whole award was taxable.³⁷⁰

Shortly after *Schleier*, the Treasury issued *Revenue Ruling 96-65*, which made “back-pay and damages for emotional distress received to satisfy a claim for disparate treatment employment discrimination under Title VII of the Civil Rights Act” not excluded from gross income under § 104(a)(2).³⁷¹ *Revenue Ruling 96-65* made obsolete *Revenue Ruling 93-38* which had ruled that under Title VII as amended in 1991, back pay and compensatory damages were excluded from income in disparate treatment discrimination cases.³⁷²

The last in the trilogy of Supreme Court decisions concerning § 104(a)(2)

364. *Id.* at 335.

365. *See Schleier*, 515 U.S. at 336.

366. *See id.* at 335.

367. *See id.* at 336.

368. *Id.* at 333.

369. *See id.* The Court noted in footnote seven, that the Commissioner had in the past treated the tort or tort-type language in the regulation as encompassing the “on account of” language in the statute. *Id.* at 334 n.7 (citing *United States v. Burke*, 504 U.S. 229, 242 n.1 (1998) (Scalia, J. concurring)).

370. *See id.* at 336.

371. 1996-2 C.B. 6.

372. *See id.* at 6-7.

is the case of *O’Gilvie v. United States*³⁷³ decided in 1986. O’Gilvie concerned a jury award of punitive damages after trial. O’Gilvie died in 1983 of toxic shock syndrome and suit was brought resulting in an \$1,525,000 compensatory damage and \$10,000,000 punitive damage award.³⁷⁴ The Court extended its interpretation of the phrase “on account of personal injuries” to hold that the punitive damages were not excludable.³⁷⁵ Justice Breyer, building from the *Schleier* opinion, underscored the interpretation of the words “on account of personal injuries or sickness” as setting forth an independent statutory requirement.³⁷⁶ The Court considered the 1989 amendment to § 104(a)(2) which provided that the § 104(a)(2) exclusion did not apply to punitive damages in cases not involving physical injury or physical sickness.³⁷⁷ However, the Court determined that the amendment only related to the treatment of punitive damages in nonphysical injury cases and could not be interpreted as authority for excluding punitive damages in physical injury or physical sickness cases.³⁷⁸ Finding that the punitive damage award was not intended to compensate for the personal injury, the Court held that the independent requirement “on account of” was not satisfied and the punitive damages were not excludable.³⁷⁹

L. The 1996 Amendments

Although Congress amended § 104 five times between 1954 and the 1983,³⁸⁰ not until 1989 did Congress begin three attempts to limit the

373. 519 U.S. 79 (1996).

374. *Id.* at 454.

375. *Id.*

376. *Ogilvie*, 519 U.S. at 454-55.

377. *Id.* 454-58.

378. *Id.*

379. *Id.* 458.

380. Act of Jan. 14, 1983, Pub. L. No. 97-473, § 101(a), 96 Stat. 2605, 2605 (1982) (amending subsection (a)(2) by substituting “whether by suit or agreement and whether as lump sums or as periodic payments” for “whether by suit or agreement”); Foreign Service Act of 1980, Pub. L. No. 96-465, § 2206(e)(1), 94 Stat. 2071, 2162 (1980) (amending subsection (a)(4) by substituting reference to § 808 of the Foreign Service Act of 1980 for reference to § 831 of the Foreign Service Act of 1946); Tax Reform Act of 1976, Pub. L. No. 94-455, §§ 505(b), (e)(1), 1901(a)(18), 90 Stat. 1520, 1567, 1568, 1766 (1976) (amending subsection (a)(4) by striking out 60 Stat. 1021 following 22 U.S.C 1081, amending § 104 by adding subsection (a)(5); and amending §104 by adding subsection (b) while redesignating old subsection (b) to new subsection (c)); Self-Employed Individuals Tax Retirement Act of 1962, Pub. L. No. 87-792, § 7(d), 76 Stat. 809, 829 (1962) (amending subsection (a) by inserting sentence that requires contributions made on behalf of an individual who has been or is a § 401(c)(1) employee, “while he was such an employee to a trust . . . which is exempt from tax . . . , or under a plan described in section 403(a), . . . to . . . be treated as contributions by the employer which were not includible in the gross income of the employee”); Foreign Service Act Amendments of 1960, Pub. L. No. 86-723, § 51, 74 Stat. 831, 847 (1960) (amending subsection (a)(4) to provide for the

§ 104(a)(2) income exclusion to damages received on account of physical injury or sickness. First, the House Ways and Means Committee (House WMC) proposed limiting the exclusion to amounts received for physical injury³⁸¹ within the Omnibus Budget Reconciliation Act of 1989.³⁸² The House WMC noted that “[c]ourts have interpreted [the § 104(a)(2)] exclusion . . . broadly in some cases to cover awards for personal injury that do not relate to a physical injury or sickness.”³⁸³ In response, the House WMC stated that allowing an exclusion of damages received on account of nonphysical injury “is inappropriate,”³⁸⁴ without giving any reason but obviously targeting employment discrimination cases, based on its statement of present law.³⁸⁵ While the Senate did not adopt the House version of the amendment regarding § 104(a)(2), the conference agreement eliminated from the income exclusion punitive damages received for personal injuries not involving physical injury or sickness.³⁸⁶

Once again, while attempting to pass the Balanced Budget Act of 1995, the House WMC tried to limit the exclusion to damages on account of physical injury.³⁸⁷ This time however, the House WMC justified the change by arguing that receipts resulting from nonphysical injuries should be taxable because “[d]amages received on a claim not involving a physical injury or physical sickness are generally to compensate the claimant for lost profits or lost wages that would otherwise be included in taxable income.”³⁸⁸ Furthermore, the Committee called for the taxation of all punitive damages.³⁸⁹ The Senate amendment followed the House bill in relevant part,

exclusion from gross income disability annuities payable under § 831 of the Foreign Service Act of 1946).

381. H.R. REP. NO. 101-247, at 1354-55 (1989), *reprinted in* 1989 U.S.C.C.A.N. 1906, 2824-25.

382. Pub. L. No. 101-239, 103 Stat. 2106 (codified as amended in scattered sections of 26 U.S.C.).

383. H.R. REP. NO. 101-247, at 1354-55 (1989), *reprinted in* 1989 U.S.C.C.A.N. 1906, 2824-25. This statement is repeated in 1995 and 1996 when Congress attempted to limit the exclusion to damages received on account of physical injury. H.R. REP. NO. 104-280, pt. 2, at 318 (1995); H.R. CONF. REP. NO. 104-737, at 300-02 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1677, 1792-94.

384. *See id.*

385. H.R. CONF. REP. NO. 101-386, at 622-23 (1989), *reprinted in* 1989 U.S.C.C.A.N. 3018, 3225.

386. *Id.*

387. H.R. REP. NO. 104-280, pt. 2, at 318-20.

388. *Id.* at 319. The Committee also went on to state:

The confusion as to the tax treatment of damages received in cases not involving physical injury or physical sickness has led to substantial litigation, including two Supreme Court cases within the last 4 years. The taxation of damages received in cases not involving a physical injury or physical sickness should not depend on the type of claim made.

Id.

389. *See id.*

and the Conferees agreed to the House WMC proposals.³⁹⁰ The § 104(a)(2) amendment nevertheless failed because President Clinton vetoed the Balanced Budget Act of 1995.³⁹¹

The House WMC reiterated its 1995 position on nonphysical injuries and punitive damages³⁹² during passage of the Small Business Job Protection Act of 1996.³⁹³ Although the Senate called for taxation of punitive damages, it voiced no opinion on whether § 104(a)(2) should be limited to damages received on account of physical injuries.³⁹⁴ Nonetheless, the Conferees agreed to follow the House WMC bill.³⁹⁵ On August 20, 1996, the Small Business Job Protection Act of 1996 became law and amended § 104(a)(2) to limit the § 104(a)(2) exclusion to damages on account of physical injury or physical sickness and not allow an exclusion for punitive damages.³⁹⁶ Section 104(a)(2) thus silently eliminated equal protection for those taxpayers that Congress vocally attempted to protect from discrimination in the last thirty-five years.

M. Conclusion of Part II

Early administrative opinions on the exclusion of damage awards misapplied, confused, and entangled the concepts of human capital and income. This embroilment paved the way for courts' bewilderment in adjudicating damage award tax exclusion litigation. Conflicting decisions continued until the 1955 Supreme Court *Glenshaw Glass* decision, which redefined income to include any "undeniable accession to wealth, clearly realized, and over which the taxpayer [had] complete dominion and control."³⁹⁷ Because taxpayers after *Glenshaw Glass* needed to qualify under a specific statutory exclusion from income, courts finally began to analyze, to interpret, and to apply the § 104(a)(2) exclusion in the personal injury context. After *Glenshaw Glass*, taxpayers structured their settlements to fall within the statutory exclusion. As a result, judicial opinion backlash forced courts to craft tests to filter out undeserving claims under § 104(a)(2). In the

390. H.R. CONF. REP. NO. 104-350, at 1452 (1995).

391. See Message Returning Without Approval to the House of Representatives Budget Reconciliation Legislation, II PUB. PAPERS 1853-55 (1995).

392. H.R. REP. NO. 104-586, at 142-44 (1996).

393. Pub L. No. 104-188, 110 Stat. 1755 (codified as amended in scattered sections of 26 U.S.C.).

394. S. REP. NO. 104-281, at 115-16 (1996), reprinted in 1996 U.S.C.C.A.N. 1474, 1589-90.

395. H.R. CONF. REP. NO. 104-737, at 300-302 (1996), reprinted in 1996 U.S.C.C.A.N. 1677, 1792-94.

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

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

early and mid-'80s, some thirty years after *Glenshaw Glass*, concrete principles were set for analyzing § 104(a)(2) litigation. However, beginning in 1989, when all the major § 104(a)(2) cases began to deal with Title VII and ADEA damage awards, these principles crumbled.

In 1989, the courts began contorting the prior § 104(a)(2) analysis, and Congress began trying to amend § 104(a)(2) to disallow the exclusion of punitive damage awards from income where the underlying injury was nonphysical. Three years later in *Burke*, the Supreme Court began its short yet detrimental involvement in the § 104(a)(2) controversy, stirred up by the Commissioner in a multijurisdictional campaign. Between its 1992 decision in *Burke* and its 1995 decision in *Schleier*, the Supreme Court manufactured a § 104(a)(2) analytical framework that denigrated and marginalized victims of dignitary torts. Finally in 1996, the Treasury and Congress, influenced by the *Schleier* decision, limited the § 104(a)(2) exclusion to damages on account of physical injury or physical sickness.

III. IS § 104(a)(2) UNSUPPORTABLE?: THE POLICY (NON)JUSTIFICATIONS

This Part summarizes the policy justifications offered by scholars as explanations for the existence of the § 104(a)(2) exclusion. Sections A-H introduce and explain one theory or justification from the perspectives of before and after the 1996 amendments.

Commentators have attempted to explain the absence of the exclusion in the 1913 Act,³⁹⁸ its subsequent inclusion in the 1918 Act,³⁹⁹ and the Service's rationale in initially limiting the exclusion to physical personal injury

398. See, e.g., Dodge, *supra* note 106, at 150. Curiously, the exclusion did not appear in the first modern federal income tax law. One possibility is that the original concept of gross income excluded nonregular receipts, such as windfalls. *Id.* Another is that gross income viewed through the lens of either business accounting or trust accounting emphasizes a clear-cut distinction between capital and income and is often expressed in the "fruit and tree" metaphor. *Id.* Under this view, a recovery for personal injury is not the "fruit" or income, but rather, compensation for loss of part of the "tree" or capital). *Id.*

399. See J. Martin Burke & Michael K. Friel, *Tax Treatment of Employment-Related Personal Injury Awards: The Need for Limits*, 50 MONT. L. REV. 13, 14 (1989) (stating that the history surrounding the passage of § 213(b)(6) "suggests that Congress intended it to codify then-recent administrative decisions"). The statute was amended in 1942, Revenue Act of 1942, ch. 619, § 127, 56 Stat. 798, 825-26 (1942). Otherwise the statute remained unchanged until 1954. See Revenue Act of 1921, ch. 136, § 213(b)(6), 42 Stat. 227, 238 (1923); Revenue Act of 1924, ch. 234, § 213(b)(6), 43 Stat. 253, 268 (1925); Revenue Act of 1926, ch. 27, § 213(b)(6), 44 Stat. 9, 24-25 (1927); Revenue Act of 1928, ch. 852, § 22(b)(5), 45 Stat. 791, 798 (1929); Revenue Act of 1932, ch. 209, § 22(b)(5), 47 Stat. 169, 179 (1933); Revenue Act of 1934, ch. 277, § 22(b)(5), 48 Stat. 680, 687 (1934); Revenue Act of 1936, ch. 690, § 22(b)(5), 49 Stat. 1648, 1658 (1936); Revenue Act of 1938, ch. 289, § 22(b)(5), 52 Stat. 447, 458 (1938); Revenue Act of 1942, ch. 619, § 127, 56 Stat. 798, 825-26 (1942).

awards.⁴⁰⁰ Explanations for the exclusion comprise a wide range of theories including humanitarianism,⁴⁰¹ involuntariness of injury,⁴⁰² bunching of income,⁴⁰³ noncommercial zone,⁴⁰⁴ imputed income,⁴⁰⁵ national income pie,⁴⁰⁶ administrative convenience,⁴⁰⁷ and return of human capital.⁴⁰⁸ As discussed in Part II, the human capital rationale has been one of the most prevalent rationales, yet also the most misunderstood and misapplied.⁴⁰⁹ Before the 1996 amendment to § 104(a)(2), these explanations and criticisms of the income tax exclusion of damages for physical and nonphysical personal injuries provided fertile ground for tax policy discussion and debate. However, since Congress made the physical/nonphysical distinction in the 1996 Amendments, these theories fail to explain or to justify the current status of § 104(a)(2) because each justification, with the possible exception of the administrative convenience theory, equally supports an exclusion of damages for both physical and nonphysical injuries.⁴¹⁰

400. See Knickerbocker, *supra* note 83, at 431 (concluding that “[t]he statute and its accompanying committee report led, one must say inescapably, to the conclusion that the only objects of the legislative solicitude were recoveries on account of physical injuries”).

401. See discussion *infra* Part III.A.

402. See discussion *infra* Part III.B.

403. See discussion *infra* Part III.C.

404. See discussion *infra* Part III.D.

405. See discussion *infra* Part III.E.

406. See discussion *infra* Part III.F.

407. See discussion *infra* Part III.G.

408. See discussion *infra* Part III.H.

409. See *supra* notes 59-79, 86-90, 98-106 and accompanying text.

410. Furthermore, allowing an exclusion of any damage award may violate the principle of horizontal equity. Under this principle people who are in similarly situated “economic positions” should bear the same tax liability. See Renée Judith Sobel, *United States Taxation of its Citizens Abroad: Incentive or Equity*, 38 VAND. L. REV. 101, 103 (1985). The all-important inquiry under the principle of horizontal equity, is how “equal economic position” is defined. See Victor Thuronyi, *The Concept of Income*, 46 TAX L. REV. 45, 51 (1990). First, in order to define “equal economic position,” a discernible index of ability to pay needs to be used in order to assess tax liability. Such indices commonly used “include income, consumption, or wealth—or perhaps some combination of these or other factors.” Eric M. Zolt, *The Uneasy Case for Uniform Taxation*, 16 VA. TAX REV. 39, 87 (1996). Although the subject of some criticism, one traditional measure is the Haig-Simons tax base. See *id.* Under this formulation, “[p]ersonal income may be defined as the algebraic sum of (1) the market value of rights exercised in consumption and (2) the change in the value of the store of property rights between the beginning and end of the period in question.” HENRY C. SIMONS, *PERSONAL INCOME TAXATION* 50 (1938). This definition of personal income “seeks to tax individuals by measuring their consumption and net accretions in wealth [and] . . . focuses on all accretions with no distinction[s] as to source [or] . . . generally . . . as to use.” Zolt, *supra*, at 87. Moreover, “the amendment disserves the principle of horizontal equity by treating job bias victims less favorably than similarly situated ‘physically injured’ persons.” Karen B. Brown, *Not Color- Or Gender-Neutral: New Tax Treatment of Employment Discrimination Damages*, 7 S. CAL. REV. L. & WOMEN’S STUD. 223, 233 (1998). Nevertheless, because it increases net wealth and allows for greater consumption, damage recovery improves one’s economic position so that allowing a taxpayer to exclude the recovery from gross income violates horizontal equity. See also Steven R. Schneider, *Recent Development, Does Uncle*

A. Humanitarianism Theory

Humanitarianism theory reasons that Congress excluded the entire award because of “a feeling that the injured party, who has suffered enough, should not be further burdened with the practical difficulty of sorting out the taxable and nontaxable components of a lump-sum award.”⁴¹¹ Consistent with this theory, Boris I. Bittker and Lawrence Lokken note that many would consider it heartless to tax as income the compensation received by seriously injured individuals unless the tortfeasors had to pay correspondingly higher damages.⁴¹²

J. Martin Burke and Michael K. Friel criticize the humanitarianism theory as an inadequate justification for the exclusion.⁴¹³ While they agree with Bittker and Lokken that taxing compensation on account of severe physical injuries may be heartless, they find few humanitarian reasons to exclude damages on account of “a sprained ankle or a bruised arm; for defamation of personal or business reputation; for violation of free speech rights; for violation of open meeting laws; or for all manner of claims that can plausibly be shoehorned into a personal injury mold.”⁴¹⁴ Burke and Friel would likely agree that humanitarianism theory justifies amending § 104(a)(2) to allow exclusions for severe damages only. However, a statute that looks to the severity of an injury in order to determine tax liability would be extremely problematic. The courts and the IRS would have to make a case-by-case determination to see if an injury satisfies the criteria for exclusion. “Moreover, the difficulties inherent in classifying particular injuries as ‘serious’ border on the ridiculous when forced to account for differences in

Sam Deserve Part of Your Discrimination Award? The Taxability of Back Pay Awards Under IRC Section 104(A)(2), 46 WASH. U. J. URB. & CONTEMP. L. 345, 363 (1994) (stating that “[e]xcluding back pay violates . . . [the principle of horizontal equity because]. [c]laimants who receive awards of back pay representing lost wages are made better than whole if the award is not taxed; they would receive tax advantages not available to their co-workers”).

411. *Roemer v. Comm’r*, 716 F.2d 693, 696 (9th Cir. 1983) (citing Note, *Taxation of Damage Recoveries from Litigation*, 40 CORNELL L. Q. 345, 346 (1955)). The Respondent in *Schleier* relied upon this humanitarianism theory to justify the exclusion of ADEA awards. Brief for Respondent at 24, *Comm’r v. Schleier*, 515 U.S. 323 (1995) (No. 94-500).

412. See BITTKER & LOKKEN, *supra* note 51, § 13.1.1 (emphasis added).

413. Burke & Friel, *supra* note 399, at 43. Cf., F. Patrick Hubbard, *Making People Whole Again: The Constitutionality of Taxing Compensatory Tort Damages for Mental Distress*, 49 FLA. L. REV. 725, 741 (criticizing the humanitarian justification because punitive damages are not excludable and because many tort victims go uncompensated); Amy McNamer, Note, *Interest not Excludable Under Section 104(a)(1)*: *Pagliariulo v. Commissioner*, 48 TAX LAW. 1075, 1080-81 (1995) (arguing that the humanitarianism justification does not support the exclusion of the interest component of damages).

414. Burke & Friel, *supra* note 399, at 43. Although Burke and Friel do not accept the humanitarianism theory, they do acknowledge the existence of strong policy reasons for the exclusion of damages on account of racial discrimination. *See id.* at 44.

occupation, lifestyle, and other personal idiosyncrasies.”⁴¹⁵

Similarly, Douglas A. Kahn states that the humanitarianism justification for excluding damages is “weaker when the injury is exclusively nonphysical than when physical injury is involved.”⁴¹⁶ He argues that the “plight of a victim who has suffered only nonphysical injuries does not arouse anything like the sympathy that is engendered by a physical injury.”⁴¹⁷ Although he recognizes that victims of extreme mental harm “arouse substantial sympathy,” Kahn does not think that any case of extreme mental harm “attract[s] the degree of compassion that is felt for a victim of serious physical injury [like] the loss of a limb or a facial disfigurement.”⁴¹⁸

Even if it originally justified the exclusion, humanitarianism theory no longer supports such exclusion under the current version of § 104(a)(2). Presently, the statute completely denies tax relief to plaintiffs with the severe emotional injuries while allowing plaintiffs with a sprained ankle full tax relief. Few would honestly claim that a person with a minor physical injury deserves compassion while an individual who has suffered severe emotional injury does not.⁴¹⁹

B. Involuntariness of Injury Theory

The involuntariness of injury theory argues that damage awards are involuntary conversions and therefore should be exempt from taxation because other Code sections, such as § 1033, exempt involuntary

415. Jerome A. Ecker, *Keys To Effective Litigation: Equitable Exclusion of Civil Rights Damage Awards Under I.R.C. Section 104(a)(2)*, 11 REV. LITIG. 415, 442 (1992) (criticizing Burke and Friel).

416. See Kahn, *supra* note 106, at 357.

417. *Id.*

418. *Id.*

419. See 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, 410 (1997) (“[T]he compassion or humanitarianism policy that a taxpayer has suffered enough would justify excluding all compensatory damages from income.”). See also Clay R. Stevens, *Killing Two Birds with One Stone: Elimination of the Punitive Damage Exemption of Section 104(a)(2) Leads to Greater Efficiency and Raises Revenue*, 28 BEVERLY HILLS B.A. J. 168, 176 (1994) (“Because the humanitarian theory fails to provide any justification for differentiating between . . . [physically and nonphysically injured] taxpayers, applying the exclusion solely to taxpayers suffering physical injury causes other taxpayers in the same economic position to bear different tax burdens. Therefore, this arbitrary distinction violates horizontal equity.”). Nicholas M. Whittington, Note, *Against the Grain: An Interdisciplinary Examination of the 1996 Federal Statutory Changes to the Taxability of Personal Injury Awards*, 37 WASHBURN L.J. 153, 165-66 (1997) (“[W]hen applied to the humanitarian aid policy, [the amendment’s changes] show that Congress values the taxpayers in the small business group over the taxpayers in . . . emotional[ly] distress[ed] tort victims [group] . . . [stealing] an expenditure . . . from some tort victims to give an expenditure to small businesses and their employees.”).

conversions.⁴²⁰ This theory, however, is flawed because § 1033—unlike § 104 (a)(2), which excludes amounts from income permanently—provides only for tax deferral and requires the taxpayer to reinvest the compensation received for destroyed property in replacement property.⁴²¹ Regardless of the incongruence between § 104(a)(2) and § 1033, however, involuntariness of injury theory does not explain the distinction in § 104(a)(2) that would consider physical injury damages as a receipt from an involuntary transaction and nonphysical injury damages as a receipt from a voluntary transaction.⁴²² Realistically, both physical and nonphysical injuries are injuries arising from involuntary transactions.

C. Bunching of Income Theory

Very often, judgement awards are paid in a lump sum that represents several years of backpay or lost profits. Absent injury, these profits would have been subject to annual taxation. However, this injured taxpayer must declare the lump sum award in the taxable year he receives it, and this bunching of back pay or lost profits will normally send the plaintiff into a higher marginal tax bracket given the progressive rate of the federal income tax.⁴²³ Thus, under the bunching of income theory, a taxpayer should receive “relief from the bunching effect, perhaps by a form of income-averaging”⁴²⁴ or “wholesale exclusion from gross income” of the lump sum.⁴²⁵ As with the humanitarianism and involuntariness of injury theories, this theory fails to support the modern exclusion of nonphysical damages from income tax relief

420. See Mark W. Cochran, *Should Personal Injury Damage Awards Be Taxed?*, 38 CASE W. RES. L. REV. 43, 46-47 (1987); Kahn, *supra* note 106, at 347-48.

421. See Cochran, *supra* note 420, at 47; Lawrence A. Frolik, *Personal Injury Compensation as a Tax Preference*, 37 ME. L. REV. 1, 20 (1985); Kahn, *supra* note 106, at 347-48; Stedman, *supra* note 419, at 390-91; Steven Jay Stewart, Note, *Damage Award Taxation under Section 104(a)(2) of the I.R.C.—Congress Clarifies Application of the Schleier Test*, 47 SYRACUSE L. REV. 1255 (1997). See also Dodge, *supra* note 106, at 183-84 (“Involuntariness may be a legitimate rationale for deferral of income or perhaps deductibility of outlay, but not for total and permanent exclusion of a clearly-realized accession to wealth.”).

422. See Stedman, *supra* note 419, at 410.

423. See Cochran, *supra* note 420, at 49.

424. Kahn, *supra* note 106, at 348. See Frolik, *supra* note 421, at 11-12; Brent B. Nicholson, *Recent Developments Concerning the Taxation of Damages Under Section 104(a)(2) of the Internal Revenue Code*, 61 ALB. L. REV. 215, 236 (1997). The elimination of the income averaging provisions by the Tax Reform Act of 1986 indicates that Congress cares little about income bunching. See Stedman, *supra* note 419, at 393. The flatter tax rates enacted in 1986 also serve as an additional indicator of Congress’s lack of concern about income bunching. See Chapman, *supra* note 83, at 429; Malcolm L. Morris, *Taxing Economic Loss Recovered in Personal Injury Actions: Towards Capital Idea?*, 38 U. FLA. L. REV. 735, 756-57 (1986); Stewart, *supra* note 421, at 1264.

425. Cochran, *supra* note 420, at 49.

because bunching results from lump sum awards for physical injuries just as it does for nonphysical injuries.

D. Noncommercial Zone Theory

Under the noncommercial zone theory, tax laws are intended to tax commercial transactions. Although a victim of either physical or nonphysical injury must actively petition for compensation, such petition directly results from the injury not any “voluntary entrance into the commercial market.”⁴²⁶ Damage awards, therefore, should be exempt from taxation since the compensation received by the injured party does not originate from a voluntary commercial transaction.⁴²⁷ This theory fails to explain the § 104(a)(2) exclusion because neither victims of physical nor nonphysical injuries receive compensation as a result of a voluntary commercial transaction.⁴²⁸

E. Imputed Income Theory

Under the imputed income theory, damages are exempt from taxation because the award to a victim resembles intangible gains that would not otherwise be taxed. One commentator notes that while “imputed income is [generally] exempt because of the difficulties inherent in defining and administering such [intangible income,]” personal injury damages are not inherently difficult to define nor difficult to administer.⁴²⁹ Even if personal injuries are easy to define and administer, unlike most intangibles, the imputed income theory still fails to justify the current statutory exclusion because awards for physical and nonphysical injuries compensate plaintiffs for intangibles that would not otherwise be taxed.⁴³⁰ Congress does not tax a good personal or business reputation any more than it taxes a healthy ankle or positive self-image or self-confidence.

426. *Id.* at 349.

427. *See* Kahn, *supra* note 106, at 348.

428. Kahn, however, supports the physical and nonphysical distinction. *See id.* at 358 (stating that “[a] physical-nonphysical division would be a surrogate for a commercial-noncommercial distinction, and any imprecision in the reach of the exclusion would be relatively minor and justified by the administrative convenience of having a bright-line standard”).

429. Robert Cate Illig, Note, *Tort Reform and the Tax Code: An Opportunity to Narrow the Personal Injuries Exemption*, 48 VAND. L. REV. 1459, 1465 (1995). For support of this proposition, see Cochran, *supra* note 420, at 48; Stedman, *supra* note 419, at 392. Examples of imputed income include the value of the use of a personally owned home and the fruits of one’s labor. *See Inclusion Of Damages Under the Age Discrimination in Employment Act*, 109 HARV. L. REV. 319, 326 (1995).

430. *See* Stedman, *supra* note 419, at 410 (stating “because [all] compensatory damages may compensate a taxpayer for an intangible, the imputed income theory is justified”).

F. National Income Pie Theory

Professor Joseph M. Dodge discusses the national income pie theory, under which all damage receipts may be excludable from gross income. Here, the purpose of the tax base is to allocate among taxpayers national income,⁴³¹ which “is limited to economic activity that generates gain or profit.”⁴³² Moreover, national “income cannot result from a mere transfer, which would include damage recoveries of all kinds as well as gratuitous transfers.”⁴³³ Dodge, however, criticizes this theory for its weakness as a matter of positive law, because the Code includes as income receipts of transfers absent a specific exclusionary provision.⁴³⁴ In addition, the national income pie theory does not support the inclusion of nonphysical damage receipts while supporting the exclusion of physical damage receipts because, under this theory, all kinds of damage recoveries are excludable.

G. Administrative Convenience Theory

The administrative convenience theory argues that injury damages should not be taxed because determining the allotment to different categories of recovery would place “a significant administrative burden on taxpayers and the Service.”⁴³⁵ Dodge denounces this theory because it is just as administratively convenient to tax all damages as it is to exclude them all.⁴³⁶ Another commentator argues that courts have not had difficulty properly allocating portions of the monetary recovery for personal injuries.⁴³⁷ Even if one argues that administrative convenience was a valid justification for the § 104(a)(2) exclusion prior to the 1996 amendments when both physical and nonphysical injury damage awards were excludable, the current version of § 104(a)(2) is even more administratively inconvenient to implement because damages arising out of nonphysical injury are taxed and damages arising out

431. See Dodge, *supra* note 106, at 147.

432. *Id.*

433. *Id.*

434. See *id.* at 147-48 (“On the normative level, the ‘pie’ theory is generally inferior to other theories such as the ‘ability to pay’ and ‘standard of living’ theories for constituting an income- or consumption-tax base.”).

435. Kahn, *supra* note 106, at 354.

436. See Dodge, *supra* note 106, at 150.

437. See Robert M. Elwood, *Supreme Court’s Ruling On Taxation of Discrimination Damages Provides Little Resolution*, 83 J. TAX’N 148, 151 (1995). See also Morris, *supra* note 424, at 744 (stating that the administrative convenience theory lacks merit because “numerous instances [exist] where taxpayers and the government make difficult allocations for tax purposes . . . [and] the addition of one more would not cause the system to collapse”).

of physical injury are not taxed.⁴³⁸ Regardless of the congruent result, however, Congress explicitly redrafted § 104(a)(2) along physical and nonphysical lines, not along any underlying policy advocating administrative convenience. Furthermore, the distinction may, in the future, actually burden the judiciary and the Service with constantly having to decide what constitutes a physical injury and what does not.⁴³⁹

H. Return of Human Capital Theory

The return of human capital theory is the most prevalently used, the most misunderstood, and the most misapplied theory. Under the return of human capital theory, recoveries for personal injuries represent a return of human capital rather than any gain, and therefore are not taxed.⁴⁴⁰ Because the restoration of human capital only returns the victim to the same position he or she occupied before the injury, thus making the individual whole again, he or she does not receive a taxable gain.⁴⁴¹ Here, the human body is likened to a piece of property.⁴⁴² Similar to a suit for damage to property, it is important for an individual to establish a tax basis for recovery because as a matter of positive law, the plaintiff has the burden of establishing his or her tax basis, and especially in an instance where the basis is difficult to calculate,⁴⁴³ the court may determine that the tax basis equals zero.⁴⁴⁴

Professor Dodge proffers that a human's tax basis may be "equal to the sum of human-capital expenditures, which might include such items as outlays for food, education, preventive health care, vitamins, and minerals."⁴⁴⁵ Unfortunately, Dodge contends, these expenditures are not accounted for nor would it be feasible to perform an accounting of such expenditures during life.⁴⁴⁶ Accordingly, every plaintiff's tax basis equals

438. See H.R. CONF. REP. NO. 104-737, reprinted in 1996 U.S.C.C.A.N. 1474, 1677. See also Burke & Friel, *supra* note 20, at 178 ("The 1996 amendments, as filtered through the committee report, . . . [both] place enormous weight on whether the 'origin' of a claim lies in a physical injury, and . . . deny this all-important physical injury status to a significant, but undefined range of physical 'symptoms' grouped under the term 'emotional distress.'").

439. See Burke & Friel, *supra* note 399, at 185-86.

440. See Cochran, *supra* note 420, at 45.

441. See *id.*

442. See *id.* See also Mary L. Heen, *An Alternative Approach to the Taxation of Employment Discrimination Recoveries under Federal Civil Rights Statutes: Income from Human Capital, Realization, and Nonrecognition*, 72 N.C. L. REV. 549, 555-60 (1994) (comparing human capital to investment capital).

443. See Cochran, *supra* note 420, at 45-46.

444. If the basis is equal to zero, then any amount received will be over the basis and thus taxable income. See Kahn, *supra* note 106, at 343.

445. Dodge, *supra* note 106, at 152.

446. See *id.*

zero unless the plaintiff can perform the impossible accounting of human-capital outlays.⁴⁴⁷ Dodge notes that “the sentimentalist would argue that the taxpayer, given the unfortunate circumstance of being injured, should be given the benefit of the doubt by a presumption that the basis lost as a result of the personal injury equals the amount realized” especially since most of the above outlays are “non-deductible personal expenses and not capital expenditures.”⁴⁴⁸ Dodge criticizes this “basis equals recovery” view first as “nonsensical” where the injured party is a young child⁴⁴⁹ and second as inconsistent with the Code’s treatment of human capital.⁴⁵⁰ Specifically, the Code does not afford deductions for taxpayers uncompensated for their injuries and does not include any depreciation deduction to offset wages earned by the taxpayer.⁴⁵¹ Therefore according to Dodge, “[o]n the merits, human capital should not be treated as a conventional asset with basis.”⁴⁵²

Professor Paul B. Stephan, III, takes a different view from that of Dodge. According to Stephan, human capital is defined as the “present value of the flow of future satisfactions that an individual can command in the course of his life.”⁴⁵³ The concept of human capital can be compartmentalized into two distinct components: (1) an endowment given from “the biological and social inheritance that accompanies a person into the world;”⁴⁵⁴ and (2) personal acquisition and other “changes resulting from lifetime events.”⁴⁵⁵ While we are born with the former, the latter results from personal effort. The personal acquisition portion would require an “impossible” accounting of outlays as explained by Dodge.⁴⁵⁶

The endowment portion of Professor Stephan’s human capital theory can have a tax basis equivalent to its value or a basis of zero.⁴⁵⁷ Assigning a zero basis to the endowment portion may be justified because of the difficulty in calculating depreciation in human capital where a positive basis is accorded. However, “[h]uman capital has an ascertainable useful life, and the normal pattern of capital cost recovery would permit an annual deduction to amortize

447. *See id.*

448. *Id.*

449. *Id.*

450. *See id.* at 152-53.

451. *See Dodge, supra* note 106, at 152-53.

452. *Id.* at 153. Furthermore, human capital is not treated as a conventional asset with basis because an individual will never realize appreciation in human capital. *See* Laura Sager & Stephen Cohen, *Discrimination Against Damages for Unlawful Discrimination: The Supreme Court, Congress, and the Income Tax*, 35 HARV. J. ON LEGIS. 447, 478 (1998).

453. Stephan, *supra* note 160, at 1358.

454. *Id.* at 1359.

455. *Id.* at 1389.

456. *See supra* notes 445-47 and accompanying text.

457. *See* Stephan, *supra* note 160, at 1390.

the taxpayer's basis. If everyone's human capital had a nonzero basis, then separate calculations of these values for depreciation purposes would be necessary."⁴⁵⁸ Professor Stephan believes that it is possible to dispense with deducting depreciation while assigning a positive basis to the endowment portion. In order to do so, a uniform value must first be assigned to everyone's endowment. "If we then used straight-line methods and a standard . . . life expectancy, everyone would have the same deduction every year, in which case the deduction could be ignored."⁴⁵⁹ Therefore, Professor Stephan argues that the use of a positive basis for the endowment component eliminates the need to undertake the "impossible" accounting of outlays required by the personal acquisition component under his human capital theory.⁴⁶⁰

On the other hand, if accounting of human capital expenditures is the sole means of establishing basis, then the human capital theory is weak given that the taxpayer must prove the basis in order to avoid the Service's assumption that the basis is zero. If Professor Stephan's theory of adopting a standard positive basis in the endowment component is sound, then the human capital theory may justify the original passage of § 104(a)(2). What the human capital theory fails to explain is the physical and nonphysical distinction in the current § 104(a)(2). Emotions, mentality, and dignity are as much a part of our biological endowment as are our legs, arms, and eyes.⁴⁶¹

I. Conclusion of Part III

None of these theories can explain the current status of § 104(a)(2). Under the theories discussed, victims of nonphysical injuries deserve the § 104(a)(2) exclusion as much as victims of physical injuries. In fact, as will be discussed in Part IV, not only are the traditional policy justifications insufficient to support the current status of § 104(a)(2), but also broader

458. *Id.*

459. *Id.*

460. For a variation of the endowment as basis theory, see Frank J. Doti, *Personal Injury Income Tax Exclusion: An Analysis and Update*, 75 DENV. U. L. REV. 61, 63, 80 (stating that human capital equals a "person's birthright—an uninjured body and mind" and concluding that § 104(a)(2) personal injuries should "be limited to human capital losses to the body, mind, and reputation of the victim of a tort or tort-like claim").

461. See Stedman, *supra* note 419, at 410 ("[U]nder the return of capital theory, compensatory damages would compensate taxpayers for loss of their human capital of mental and physical well-being."); Whittington, *supra* note 419, at 165 ("Application of the human capital theory results in the changes made by the amendment violating this principle of income and suggests that Congress does not believe that emotional distress is a reduction in capital.").

social policy supports the equal treatment of victims of nonphysical and physical injuries under § 104(a)(2).

IV. SECTION 104(a)(2) IN BROADER CONTEXT: RECOGNIZING NONPHYSICAL INJURIES VERSUS TORT REFORM

If the law can be made to articulate rather than mask social domination, if it can be made to reveal . . . the effect of . . . male dominance, then perhaps substantive rather than merely formal equality can be won through civil rights law.⁴⁶²

This Article has thus far presented the history of and lack of justification for leaving out nonphysical injury damages from § 104(a)(2)'s physical injury damages income exclusion. Parts II and III provided a conventional legal survey of § 104(a)(2) case law and legislative history as well as potential theories explaining this discriminatory exclusion. The analysis in Part IV, however, departs from traditional tax analysis and § 104(a)(2) scholarship to better explain what gave rise to the 1996 amendments to § 104(a)(2). Because § 104(a)(2) deals not with familiar economic transactions but with interpersonal relations resulting in economic consequences, departure from the traditional tax analysis is necessary to examine what conditioning factors influenced the enactment of the 1996 amendments to § 104(a)(2). This Part discusses the civil rights movement and tort reform as conditioning factors that are relevant to the current status of § 104(a)(2).

Understanding the origins of the nonphysical damages exclusion requires studying the socio-economic factors generating the historical evolution of § 104(a)(2). Section A familiarizes the reader with major civil rights legislation. Specifically, subsections A.1–A.5 look at the purposes for enacting the Civil Rights Act of 1964, the ADEA, the Equal Employment Opportunity Act of 1972 (EEOA), the Rehabilitation Act of 1973, the Americans with Disabilities Act of 1990 (ADA), and the Civil Rights Act of 1991, respectively. Section B examines the rise of tort reform at both the state and federal level. Section C examines tort reform in the context of § 104(a)(2), demonstrating how the civil rights movement and tort reform influenced the current status of § 104(a)(2). This Part further demonstrates that judicial and congressional tort reform efforts functioned as a backlash to civil rights legislation and spawned the 1996 amendments to § 104(a)(2).

462. WENDY BROWN, *STATES OF INJURY: POWER AND FREEDOM IN LATE MODERNITY* 130 (1995) (emphasis added).

A. Civil Rights Legislation

1. Civil Rights Act of 1964

Although the Thirteenth and Fifteenth Amendments granted black males freedom from slavery and the right to vote,⁴⁶³ and the Nineteenth Amendment⁴⁶⁴ afforded all women the right to vote, the white, male-dominated nation continued to resist the movement for equality by manipulating the law within political, economic, and social spheres.⁴⁶⁵ Not

463. U.S. CONST. amend. XIII, § 1 (“Neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States, or any place subject to their jurisdiction.”); U.S. CONST. amend. XV, § 1 (“The right of citizens of the United States to vote shall not be denied or abridged by the United States or by any State on account of race, color, or previous condition of servitude.”). Although dignity is at the heart of the Thirteenth Amendment, motivation behind its passage is said to lie elsewhere. According to one commentator, the Thirteenth Amendment was enacted shortly after the Civil War partly as a means to punish the South and partly from a feeling of obligation to the Blacks who had fought along side the North in their battle with the Confederacy. *See generally* GEORGE H. HOEMANN, WHAT GOD HATH WROUGHT: THE EMBODIMENT OF FREEDOM IN THE THIRTEENTH AMENDMENT (1982). Ulterior motives have also been cited for the passage of the Fifteenth Amendment. *See* A. CAPERTON BRAXTON, THE FIFTEENTH AMENDMENT: AN ACCOUNT OF ITS ENACTMENT 15-17 (5th ed. 1934). The South realized that the political power of Southern whites would increase if blacks were included in the determination of electoral votes yet kept from the polls. *See id.* at 16. Moreover, Republicans felt that the freed slaves would be forever gracious to the Republican party for their freedom, thus increasing its own political power. *See id.* at 17.

464. U.S. CONST. amend. XIX, cl. 1 (“The right of citizens of the United States to vote shall not be denied or abridged by the United States or by any state on account of sex.”).

465. Shortly after the enactment of the Fifteenth Amendment, Mississippi, South Carolina, Louisiana, Alabama, and Virginia held constitutional conventions to effectuate disfranchisement of blacks, and North Carolina, Texas, and Georgia followed suit without conventions. *See* DERRICK A. BELL, JR., RACE, RACISM AND AMERICAN LAW 135 (2d ed. 1980). Moreover, Florida, Tennessee, and Arkansas disfranchised minorities through the state legislatures’ use of a combination of the poll tax and registration, multiple-box or secret ballot rules. *Id.* at 135-36. Anecdotal accounts illustrate how these laws institutionalized discrimination in voting. In Fayette County, Tennessee, in 1959, 0.05% of the blacks in the county were reregistered to vote and fewer actually went to vote. *Tent City: “Home of the Brave,”* reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT 87 (Peter B. Levy ed., 1992) [hereinafter *Tent City*]. Blacks who tried to exercise their right encountered resistance as government officials erected barriers such as an “all-white primary” to deter blacks from voting. *See id.* at 87. By 1960, when black voter registration drives commenced in full, the racist establishment refused to concede defeat, and “they set in motion the machinery of reprisal: economic strangulation, threats, police harassment and sometimes even gunfire from their cowardly ambush.” *Id.* at 86.

As a retaliatory reaction to the Thirteenth Amendment, former Confederate states introduced broad vagrancy ordinances known as “Black Codes” in an attempt to maintain control over the newly freed slaves. *See* Gary Stewart, *Black Codes and Broken Windows: The Legacy of Racial Hegemony in Anti-Gang Civil Injunctions*, 107 YALE L.J. 2249, 2257-59 (1998) (“[T]he prospect of being arrested and charged with vagrancy deterred black laborers from leaving their former masters’ plantations.”). Other forms of social repression included segregation. *See* BELL, *supra*, at 83 (“By 1900, all the southern states had segregated railroad trains, and the laws were being extended to cover all travel facilities. Local transportation facilities, street-and horsecars were next. Then quite quickly, separation of the races in all public facilities and private facilities open to the public was mandated.”).

until the '50s and '60s did the three branches of government undertake significant political, economic, and social change to promote equality in many human endeavors.

In the 1954 case of *Brown v. Board of Education*, the Warren Court overruled the separate but equal doctrine established in *Plessy v. Ferguson*⁴⁶⁶ holding racially-motivated segregation of public school children unconstitutional under the Fourteenth Amendment's Equal Protection Clause.⁴⁶⁷ The Executive Branch soon followed suit when, in 1961, President John F. Kennedy issued Executive Order 10, that directed federally funded contractors to take affirmative measures to eliminate racial discrimination in their employment endeavors.⁴⁶⁸ In 1964, Congress, faced with a mounting revolt by the historically underprivileged racial minority,⁴⁶⁹ enacted the Civil

466. 163 U.S. 537 (1896).

467. 347 U.S. 483, 492-93 (1954) (“[W]e cannot turn the clock back to 1868 when the [Fourteenth] Amendment was adopted, or even to 1896 when *Plessy v. Ferguson* was written. We must consider public education in the light of its full development and its present place in American life throughout the Nation.”). The Court “conclude[d] that in the field of public education the doctrine of ‘separate but equal’ has no place.” *Id.* at 495

468. Exec. Order No. 10,925, 3 C.F.R. 448 (1959-1963). The executive branch played an important role in the civil rights movement. The inauguration of President John F. Kennedy stirred the public's expectations for social change. See ROBERT WEISBROT, *FREEDOM BOUND: A HISTORY OF AMERICA'S CIVIL RIGHTS MOVEMENT* 49 (1990). Kennedy had initially intended to effect change gradually, but civil rights leaders and public sentiment urged him to move more forcefully. See JAMES N. GIGLIO, *THE PRESIDENCY OF JOHN F. KENNEDY* 159 (1991). President Kennedy became a “vigorous advocate” of the civil rights movement, appointing over “forty blacks to top administration posts” and instituting fifty-seven voting-rights suits during his administration. *Id.* at 159, 163-64. He became a champion of the cause, evidenced by his support of the Civil Rights Bill of 1963. See *id.* at 159. After President Kennedy's assassination, President Johnson continued in his predecessor's footsteps, aware that the nation's political agenda had been altered by the civil rights movement. See WEISBROT, *supra*, at 87.

In certain cases, the Executive Branch took more drastic measures, such as sending the National Guard to escort black students to white schools. *Cooper v. Aaron*, 358 U.S. 1, 9 (1958). In 1957 the Governor of Arkansas called out the National Guard to prevent nine black students from entering an all-white high school. *Id.* After a court ordered the Guard to be withdrawn, threats of violence lead President Eisenhower to call on paratroopers to enforce integration. See *id.* at 9-12. The troops remained for one year. See *id.* at 12. In 1963, in order to enforce the Supreme Court's 1955 order to admit black students into the University of Alabama, President Kennedy called on the Alabama National Guard to ensure the safety of the black students in the wake of Governor George Wallace's repeated assertions that he would not allow blacks into the University. See E. CULPEPPER CLARK, *THE SCHOOLHOUSE DOOR: SEGREGATION'S LAST STAND AT THE UNIVERSITY OF ALABAMA* 182-83, 229-31 (1993).

469. Most believe that the Civil Rights Movement began with Rosa Parks simply asserting herself. Robert D. Loevy, *Introduction: The Background and Setting of the Civil Rights Act of 1964*, reprinted in *THE CIVIL RIGHTS ACT OF 1964*, at 1, 22 (Robert D. Loevy ed., 1997). While riding a city bus in Montgomery, Alabama, on the first of December, 1955, Rosa Parks was ordered to give up her seat so that a white man could sit down. Rosa L. Parks, *Recollections*, reprinted in *DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT*, *supra* note 465, at 52. She refused and was arrested for “suspicion.” *Id.* at 53. Although such arrests had occurred numerous times before, the black leadership believed that the time was right to reject this treatment; E. D. Nixon, a black leader, recalled that he “felt that the

Negroes in Montgomery were at last anxious to move, prepared to sacrifice and ready to endure whatever came." E. D. Nixon, *How It all Started*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 54. See also Parks, *supra*, at 51-52. Pamphlets were distributed throughout the Black community recounting the story of Rosa Parks and announcing a bus boycott. See Woman's Political Council, *Leaflet*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 57. Black leaders had no idea whether such a move would be supported by the black masses. See David J. Garrow, *The Montgomery Bus Boycott and the Women Who Started It: The Memoir of Jo Ann Gibson Robinson*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 55-56. To their surprise, the boycott lasted one year. See Garrow, *supra*, at 57. By December of 1956, the Montgomery bus lines were desegregated. See Hollinger F. Barnard, *Outside the Magic Circle: The Autobiography of Virginia Foster Durr*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 61. The Black leadership constituted four main groups: The National Association for the Advancement of Colored People (NAACP), The Student Nonviolent Coordinating Committee (SNCC), The Congress of Racial Equality (CORE), and The Southern Christian Leadership Conference (SCLC). See *Tent City*, *supra* note 465, at 85.

The NAACP focused on legal battles against formal segregation. See Loevy, *supra*, at 21. One such fight occurred in Little Rock, Arkansas. DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 48. The NAACP fought to integrate the main high school. See MARK V. TUSHNET, *MAKING CIVIL RIGHTS LAW: THURGOOD MARSHALL AND THE SUPREME COURT, 1936-1961*, at 259 (1994). Elizabeth Eckford, one of the nine black children who tried to attend classes at Central High School, describes her encounters with law enforcement officers as she proceeded to enter the all-white Central High School in Little Rock, Arkansas. See Elizabeth Eckford, *The First Day: Little Rock, 1957*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 44-46.

The SNCC directed student protests; sit-ins were their most effective form of peaceful, nonviolent protests against segregation. See Loevy, *supra*, at 38. At a Woolworth's store in Greensboro, North Carolina, four black men sat down at an all-white counter on February 1, 1960, attempted to order coffee and donuts, and were refused service. See Franklin McCain, *Interview*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 66. The men refused to leave until they were served. See *id.* News of this protest disseminated throughout the South. See *id.* at 67. Within days, similar protests occurred at lunch counters all over the South. See Loevy, *supra*, at 37. In 1961, CORE decided to launch "Freedom Rides." See DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 75. Fresh from a Supreme Court victory, activists assembled and rode busses through the South to test the newly espoused rights in *Boynton v. Commonwealth of Virginia*. See *id.* See also *Boynton v. Commonwealth of Virginia*, 364 U.S. 454 (1960) (holding that interstate passengers had a right to expect food service at designated layover terminals regardless of their skin color). CORE felt that such endeavors would anger the segregationists and cause them to mobilize in protests. See DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 75. Such protests would cause the national attention, forcing the federal government to act. See *id.*

The SCLC, led by Martin Luther King, Jr., concentrated on peaceful marches and boycotts to provoke racist, violent reactions from the establishment. See DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 107. The marches on Birmingham and Washington, D.C., became the most famous. See *id.* In the Spring of 1963, the black leadership chose to march on Birmingham, Alabama, because among other things, the town's sheriff had previously demonstrated his dislike and hostility towards the Civil Rights Movement. See *id.* Again, black leaders correctly predicted that black nonviolent protests would encourage the sheriff to react with excessive force, that such force would be captured on film by the national media and shown throughout the country, and that such pressure would force the President to act. See *id.* at 107-08, 114. When the blacks marched on Birmingham, the sheriff used sickeningly excessive force, that was shown on nationwide television. See *id.* President Kennedy proposed in the Summer of 1963 what would soon become the Civil Rights Act of 1964. See *id.* at 117. The March on Washington, D.C., organized to support the proposed civil rights legislation, induced over 200,000 Americans to fill the Lincoln Memorial complex. See *id.* at

Rights Act of 1964⁴⁷⁰ to prohibit discrimination based on sex, color, race, religion, or national origin.⁴⁷¹

The Civil Rights Act of 1964 applied to public voting (Title I),⁴⁷² public

119-20. This march climaxed with Martin Luther King, Jr.'s now world-famous "I Have a Dream" speech, in which he proclaimed that "I have a dream that my four children will one day live in a nation where they will not be judged by the color of their skin but by the content of their character." *See id.* at 122. Martin Luther King, Jr., *I Have a Dream*, reprinted in DOCUMENTARY HISTORY OF THE CIVIL RIGHTS MOVEMENT, *supra* note 465, at 124.

470. Pub. L. No. 88-352, 78 Stat. 241 (codified as amended in scattered sections of 42 U.S.C.). The Civil Rights Act of 1964 was not the first legislative attempt to protect minorities. The initial congressional civil rights endeavor occurred with the enactment of the Civil Rights Act of 1866, ch. 31, 14 Stat. 27 (1868), which prohibited discrimination based on race and national origin in an attempt to guarantee former slaves the same property and contractual rights enjoyed by whites. Moreover, from 1870 through 1875, Congress enacted a series of civil rights legislation. *See, e.g.*, Enforcement Act of 1870, ch. 114, 16 Stat. 140 (1871) (protecting the rights of black men by making it a federal crime to conspire in order to deprive any citizen of any right guaranteed by federal law); Act of Feb. 28, 1871, ch. 99, 16 Stat. 433; Civil Rights (Ku Klux Klan) Act of 1871, ch. 22, 17 Stat. 13 (1873) (responding directly to widespread violence against newly freed slaves by organizations such as the Ku Klux Klan); Civil Rights Act of 1875, ch. 114, 18 Stat. 335 (providing for equal enjoyment of facilities and accommodations and outlawing racial discrimination in state jury selection). For other congressional civil rights attempts, see Civil Rights Act of 1957, Pub. L. No. 85-315, 71 Stat. 634 (creating the Commission on Civil Rights and authorizing the Attorney General to bring suits to put an end to discriminatory practices); The Civil Rights Act of 1964, Pub. L. No. 88-352, 78 Stat. 241 (making it criminal to interfere with persons attempting to comply with court orders relating to civil rights and providing that the Attorney General could inspect voting records that officers of elections were required by the Act to retain).

471. Civil Rights Act of 1964, Pub. L. No. 88-352, § 703, 78 Stat. 241, 255-57 (codified as amended at 42 U.S.C. § 2000e-2(b) (1994 & Supp. II 1996)). The Act states:

It shall be an unlawful employment practice for an employer-

- (1) to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual's race, color, religion, sex, or national origin; or
- (2) to limit, segregate, or classify his employees in any way which would deprive or tend to deprive any individual of employment opportunities or otherwise adversely affect his status as an employee, because of such individual's race, color, religion, sex, or national origin.

Id. With the exception of Title VII, sex is not mentioned anywhere else in the text of the Act. Ironically, in an effort to weaken the proposed bill, "sex" was added to the protections mandated by the act. Congressman Howard Smith of Virginia introduced the amendment to add the word "sex" to Title VII right after the word "religion." 110 CONG. REC. 2547, 2577 (daily ed. Feb. 8, 1964). The proposal by Congressman Smith surprised other members of the House because he had previously been opposed to the bill. *See id.* at 2578. Congressman Smith was evidently not entirely serious in his intentions. He referred to a letter he claimed to have received from a lady, who wished to air her grievances after she heard that Congressman Smith was going to propose the amendment. *See id.* at 2577. The excerpt read by Congressman Smith described a gender "imbalance" based on the existence of 2,661,000 more females than males in the United States. *Id.* The letter stated that the number imbalance interfered with the "right" of every woman to have a husband of her own and urged Congress and the President to take action to assist females in "obtaining their 'right' to happiness." *Id.* Congressman Smith found it necessary to assure members of the House that he was "serious about this thing" during the debate. *Id.*

472. Civil Rights Act of 1964, Pub. L. No. 88-352, § 101, 78 Stat. 241, 241 (codified as amended at 42 U.S.C. 1971 (1994 & Supp. II 1996)). Title I, designed to remedy the problems in operation and enforcement of the Civil Rights Acts of 1957 and 1960, addressed the problem of judicial delays that

had occurred under prior acts with regard to voting rights litigation. H.R. REP. NO. 88-914, at 19 (1964), *reprinted in* 1964 U.S.C.C.A.N. 2355, 2394. Section 101 of Title I sanctioned the Attorney General to enter into “agreements with appropriate State or local authorities” to ensure that there is no unlawful employment of “any literacy test as a qualification for voting in any election.” Civil Rights Act of 1964, Pub. L. No. 88-352, § 101, 78 Stat. 241, 241 (codified as amended at 42 U.S.C. § 1971(a)(2)(C) (1994 & Supp. II 1996)). Section 101 authorized the Attorney General to file actions in front of a three-judge panel challenging patterns or practices of unlawful discrimination in the voting process. *Id.* § 101. In furtherance of the pro-civil rights goals of the ‘60s, in seeking to remove impediments to registration for minorities, and in an effort to give blacks full franchise, Congress amended Title I by enacting the Voting Rights Act of 1965, Pub. L. No. 89-110, 76 Stat. 446 (codified as amended at 42 U.S.C. §§ 1971, 1973-1973bb-1 (1994 & Supp. II 1996)). Section 4 of the Voting Rights Act prohibited the use of literal tests and other devices as qualifications for voting in any federal, state, or local elections in those states or political subdivisions within its scope. *Id.* § 4. Section 4 also forbids denial of the vote to Spanish-speaking Americans having received at least a sixth grade education in American flag schools. *Id.* Section 9 of the Voting Rights Act provides an administrative process that functions separately from the judiciary in locating and abolishing discriminatory practices and assuring immediate registration of minorities deprived of their right to vote. *Id.* § 9. Moreover, miscellaneous provisions are directed at certain abuses related to the voting rights issues. *Id.* §§ 11-19. Section 10 of the Voting Rights Act authorizes the Attorney General to challenge in federal courts the constitutionality of poll taxes that are used in state elections as preconditions to voting. *Id.* § 10. Finally, section 16 of the Voting Rights Act calls for a study of voting discrimination against military personnel. *Id.* § 16.

Oversight of the polls became one of the major tenets of the Voting Rights Act in effectuating its stated purpose. Nevertheless, “[r]egardless of the terms of civil rights laws, their effect might have been muted in the absence of sufficient staff to enforce them,” crippling the effects of the laws. *See* HARRELL R. RODGERS, JR. & CHARLES S. BULLOCK, III, *LAW AND SOCIAL CHANGE: CIVIL RIGHTS LAWS AND THEIR CONSEQUENCES* 27, 31 (1972) (noting the number of attorneys in the Department of Justice’s Civil Rights Division increased from a total of 20 in 1963 to 50 just “patroll[ing] the South during the 1966 general elections[.] . . . approximately 600 Federal officials [watched over] . . . the 1966 elections, and 1,500 [participated] . . . in Southern elections in 1966 and 1967,” and detailing state-by-state the effects of the Voting Rights Act before and after the enactment of the Civil Rights Act of 1965) (citations omitted). In order to perfect its provisions, Congress amended the Voting Rights Act in 1970, 1975, and 1982. Voting Rights Act Amendments of 1970, Pub. L. No. 91-285, 84 Stat. 314, 315 (amending Title I, § 3 by striking out the words “five years” wherever they appear and inserting the words “ten years”); Voting Rights Act Amendments of 1975, Pub. L. No. 94-73, 89 Stat. 400, 400-02 (expanding section 4 of the Act to safeguard against language barriers for minorities); Voting Rights Act Amendments of 1982, Pub. L. No. 97-205, 96 Stat. 131, 132-34 (extending special coverage provisions, adopting a new procedure by which a jurisdiction can exempt itself from coverage under special provisions, amending Section 2 to extend the language assistance provisions for an additional seven years, and adding a section governing assistance to voters who are blind, disabled, or unable to read or write). *See also* QUIET REVOLUTION IN THE SOUTH: THE IMPACT OF THE VOTING RIGHTS ACT, 1965-1990, at 30 (Chandler Davidson & Bernard Grofman eds., 1994) (“[E]xtensions and amendments of the act in all three years reflected a strong bipartisan consensus . . . although there were initial attempts by presidents Nixon and Reagan in 1970 and 1982, respectively, to sabotage extension of various important provisions of the act.”). Unfortunately minorities continue to face voting barriers as their votes are sometimes rendered meaningless due to the device of “racially polarized voting,” that occurs when:

election laws or practices, either singly or in concert, combine with systematic bloc voting among an identifiable group to diminish the voting strength of at least one other group. The idea is that one group, voting cohesively for its preferred candidates, is systematically outvoted by a larger group that is also cohesive. If both groups . . . vote as opposing blocs, then *racially polarized voting* occurs.

Id.

accommodations (Title II),⁴⁷³ public facilities (Title III),⁴⁷⁴ public education (Title IV),⁴⁷⁵ federally assisted programs (Title VI),⁴⁷⁶ and public and private employment of 15 or more employees affecting interstate commerce (Title VII).⁴⁷⁷ In order to compel compliance with the Act's provisions and to deter future discrimination, the Act provided a broad range of remedial relief,

473. Civil Rights Act of 1964, Pub. L. No. 88-352, §§ 201-207, 78 Stat. 241 (codified as amended at 42 U.S.C. §§ 2000a-2000a-6 (1994 & Supp. II 1996)). Section 201 of Title II prohibits discrimination on the basis of race, color, religion, or national origin in public accommodations which have a nexus with interstate commerce, including hotels, restaurants, theaters, and gas stations. *Id.* § 201. Section 204 of Title II allows for injunctive relief and attorneys fees to remedy violations. *Id.* § 204. The Supreme Court has ruled that the scope of Title II extends to privately owned accommodations. *See, e.g., Daniel v. Paul*, 395 U.S. 298, 304-05 (1969) (holding that a privately owned snack bar in a privately owned recreational facility engaged in selling food to interstate travelers and therefore was a public accommodation under Title II); *Heart of Atlanta Motel v. United States*, 379 U.S. 241, 250 (1964) (holding that Title II applies to privately owned hotels that serve interstate travelers and upheld the constitutionality of the statute as within congressional powers derived from the Commerce Clause); *Katzenbach v. McClung*, 379 U.S. 294, 303-04 (1964) (holding that Congress was within its powers to find that discrimination in family-owned restaurants which receive a substantial amount of their food from out of state had a direct impact on interstate commerce).

474. Civil Rights Act of 1964, Pub. L. No. 88-352, §§ 301-304, 78 Stat. 241, 246 (codified as amended at 42 U.S.C. §§ 2000b-2000b-3 (1994 & Supp. II 1996)). Section 301 of Title III allows the Attorney General to "institute for or in the name of the United States a civil action in any appropriate district court of the United States against such parties and for such relief as may be appropriate" where there has been a violation of Title III by "any public facility which is owned, operated, or managed by or on behalf of any State or subdivision thereof, other than a public school or public college as defined in section 2000c." *Id.* § 301.

475. Civil Rights Act of 1964, Pub. L. No. 88-352 §§ 401-410, 78 Stat. 241, 246-49 (codified as amended at 42 U.S.C. §§ 2000c-2000c-9 (1994 & Supp. II 1996)). Section 407 of Title IV grants the Attorney General authority to institute desegregation and "such relief as may be appropriate," when in furtherance of public policy, and when private parties are unable "to bear the expense of the litigation or to obtain effective legal representation; or whenever [the Attorney General] . . . is satisfied that the institution of such litigation would jeopardize the personal safety, employment, or economic standing of such person or persons, their families, or their property." *Id.* § 407

476. Civil Rights Act of 1964, Pub. L. No. 88-352, §§ 601-605, 78 Stat. 241, 252-53 (codified as amended at 42 U.S.C. § 2000d (1994 & Supp. II 1996)). Section 601 of Title VI makes it unlawful for a "program or activity receiving federal financial assistance" to discriminate "on the ground of race, color, or national origin." *Id.* § 601. Section 602 of Title VI directs "[e]ach Federal department and agency which is empowered to extend Federal financial assistance to any program or activity, by way of grant, loan, or contract other than a contract of insurance or guaranty, . . . to effectuate the provisions of section 2000d." *Id.* § 602.

477. Civil Rights Act of 1964, Pub. L. No. 88-352, §§ 701-716, 78 Stat. 241, 253-66 (codified as amended at 42 U.S.C. §§ 2000e-2000e-15 (1994 & Supp. II 1996)). Section 703 of Title VII makes it unlawful to discriminate in employment on the basis of "race, color, religion, sex, or national origin." *Id.* § 703. Section 706 of Title VII provides as follows:

[If the court finds that an employer] engaged in or is intentionally engaging in an unlawful employment practice charged in the complaint, the court may enjoin the respondent from engaging in such unlawful employment practice, and order such affirmative action as may be appropriate, which may include, but is not limited to, reinstatement or hiring of employees, with or without back-pay.

Id. § 706.

including a measure in Title VII authorizing the courts to “order such affirmative action as may be appropriate, which may include reinstatement or hiring of employees, with or without back pay” where an employer’s discriminatory intent is shown.⁴⁷⁸ In addition, the Act created the Community Relations Service to assist people in resolving disagreements stemming from discrimination,⁴⁷⁹ and established the Equal Employment Opportunity Commission (EEOC) to arbitrate or recommend federal litigation for employment discrimination claims.⁴⁸⁰

478. *Id.* § 706.

479. Civil Rights Act of 1964, Pub. L. No. 88-352, § 1002, 78 Stat. 241, 267 (codified as amended at 42 U.S.C. § 2000g-1 (1994 & Supp. II 1996) (providing “assistance to communities and persons therein in resolving disputes, disagreements, or difficulties relating to discriminatory practices . . . which impair the rights of persons in such communities under the Constitution or laws of the United States or which affect or may affect interstate commerce”)).

480. Civil Rights Act of 1964, Pub. L. No. 88-352, §§ 705-706, 78 Stat. 241, 258-61 (codified as amended at 42 U.S.C. §§ 2000e-4 to -5 (1994 & Supp. II 1998)). For a thorough accounting of the responsibilities, jurisdiction, and budget analysis of the EEOC, see generally U.S. COMMISSION ON CIVIL RIGHTS, FUNDING FEDERAL CIVIL RIGHTS ENFORCEMENT: A REPORT OF THE UNITED STATES COMMISSION ON CIVIL RIGHTS 36-46 (1995). The numerous claims handled annually by the Commission serve as evidence of the stark reality of discrimination. From 1991 to 1997, between 49,584 and 62,811 charges were filed under Title VII. See The U.S. Equal Employment Opportunity Commission, *Title VII of the Civil Rights Act of 1964 Charges 1991-1997*, available at <http://www.eeoc.gov/stats/vii.html> (last visited Feb. 12, 2001).

The Act also gave duties to other agencies. Section 402 of Title IV directs the Commissioner of Education to conduct a survey addressing the lack of available educational avenues for individuals due to certain immutable qualities. Civil Rights Act of 1964, Pub. L. No. 88-352, § 402 (codified as amended at 42 U.S.C. § 2000c-1 (1994 & Supp. II 1996)). Furthermore, this section directed that a report be given to the President and Congress within two years of passage of the Act. *Id.* § 402. Section 403 of Title IV directs the Commissioner of Education to render assistance to any governmental body charged with the execution of public education. *Id.* § 403. Section 404 of Title IV authorizes the Commissioner of Education to provide training to any governmental body charged with providing public education to improve the abilities and faculties of educators. *Id.* § 404. Section 405 of Title IV authorizes the Commissioner of Education to fund seminars and individual training sessions to assist education professionals with managing change incident to desegregation. *Id.* § 405. Section 501 of Title V empowers the Commission on Civil Rights to hold hearings. *Id.* § 501. Section 504 of Title V dictates that the Commission shall explore any allegations of violations of the Act. *Id.* § 504. This section also directs the Commission to explore all incidences of deprivation, either in fact or by administration, of civil rights because of “race, color, religion, or national origin;” empowers the Commission to assess the discriminatory impact of the current laws and regulations of the Federal Government; permits the Commission to collect information about illegal discrimination “in such areas, including but not limited to voting, education, housing, employment, the use of public facilities, and transportation, or in the administration of justice;” vests the Commission with the authority to pursue all allegations of infractions that impair an individual’s voting ability on account of “race, color, religion, or national origin;” and excludes the Commission from investigating private social clubs. *Id.* Finally, section 504 of Title V directs the Commission to produce as many reports on the findings of the Commission as either the Commission, the President, or Congress so desires. *Id.* Section 602 of Title VI mandates that each federal department will authorize grants to the public only if the party receiving those benefits complies with Section 601 of Title VI, stating that “[n]o person in the United States shall, on the ground of race, color, or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving

Although Congress minimally debated providing injunctive and equitable relief,⁴⁸¹ Congress did express considerable concern over what appropriate affirmative action entailed as provided under some of the Act's provisions.⁴⁸² Specifically, Congresspersons and Senators attacked Title VII for requiring racial balancing as a remedy because they feared Title VII's breath would require preferential treatment including racial quotas, that would result in discrimination against nonminorities.⁴⁸³ Proponents argued that the Act,

Federal financial assistance." *Id.* § 602. Section 715 of Title VII instructs the Secretary of Labor to conduct an investigation of circumstances which promote discrimination in employment and the subsequent effects of that discrimination on not only the national economy but also the direct victims of discrimination. *Id.* § 715. Section 801 of Title VIII empowers the Secretary of Commerce to initiate a review of voting practices in such areas of the country as directed by the Commission on Civil Rights. *Id.* § 801.

481. See H.R. REP. NO. 88-914, at 19 (1963), *reprinted in* 1964 U.S.C.C.A.N. 2355, 2391. See also *Additional Views Of Hon. George Meader*, 1964 U.S.C.C.A.N. at 2415-19 (discussing the effects of injunctive relief as affording too much power to the government, circumventing individual rights and liberties, and costing great amounts of money over a period of time); Minna J. Kotkin, *Public Remedies for Private Wrongs: Rethinking the Title VII Back Pay Remedy*, 41 HASTINGS L.J. 1301, 1314 (1990) (concluding that "Congress never gave serious thought to the question of monetary relief" as the impact of the remedial scheme adopted without its original administrative enforcement component was never discussed). The Senate did not debate the addition of the words "any other equitable relief" when they were added by amendment on the Senate Floor in 1972. 118 CONG. REC. 3839, 3979 (1972). The only explanation of legislative intent appears in *Section-by-Section Analysis of H.R. 1746, Accompanying the Equal Employment Opportunity Act of 1972—Conference Report*, 118 CONG. REC. 7001, 7166-69 (1972) stating:

The provisions of [§ 706(g)] . . . are intended to give the courts wide discretion exercising their equitable powers to fashion the most complete relief possible. In dealing with the present section 706(g) the courts have stressed that the scope of relief under that section of the Act is intended to make the victims of unlawful discrimination whole, and that the attainment of this objective rests not only upon the elimination of the particular unlawful employment practice complained of, but also requires that persons aggrieved by the consequences and effects of the unlawful employment practice be, so far as possible, restored to a position where they would have been were it not for the unlawful discrimination.

Id. at 7168.

482. See H.R. REP. NO. 88-914, at 19 (1963), *reprinted in* 1964 U.S.C.C.A.N. 2355, 2391. Members of the House opposed to the bill issued a minority report asserting that employers could be "forced . . . to hire in a 'racially balanced' manner—so long as the potential employee had a modicum of skill—else be in violation of law." *Id.* at 2442. This concern was repeatedly raised in the Senate by opponents to the bill. See, e.g., 110 CONG. REC. 5871, 5877-78 (1964) (statement of Sen. Byrd); 110 CONG. REC. 7045, 7091 (1964) (statement of Sen. Stennis); 110 CONG. REC. 7770, 7774, 7778 (1964) (statement of Sen. Tower); 110 CONG. REC. 7770, 7878-79 (1964) (statement of Sen. Russell); 110 CONG. REC. 8169, 8175 (1964) (statement of Sen. Smathers); 110 CONG. REC. 8495, 8500 (1964) (statement of Sen. Smathers); 110 CONG. REC. 13,050, 13,076 (1964) (statement of Sen. Sparkman).

483. See H.R. REP. NO. 88-914, at 19 (1963), *reprinted in* 1964 U.S.C.C.A.N. 2355, 2391. "[T]he bill, under the cloak of protecting the civil rights of certain minorities, will destroy civil rights of all citizens of the United States who fall within its scope." *Id.* at 2433. The Committee on Judiciary Substitute for H.R. 7152 called the bill "a not too subtle system of racism-in-reverse." *Id.* at 2441. Representative Alger also stated his opinion that Congress "cannot enforce preferential treatment for the Negro by making jobs available to him for which he is not qualified because of injustices practiced upon his forbears, without doing violence to the rights and freedoms of all our other citizens." 110 CONG. REC. 1580, 1645 (1964).

prohibiting all racial discrimination,⁴⁸⁴ used affirmative action relief to make victims of discrimination whole, not to set racial quotas.⁴⁸⁵ Proponents of the Act denied that preferential treatment could be ordered as relief under Title VII,⁴⁸⁶ based on the language “[n]o order of the court shall require the . . . hiring, reinstatement, or promotion of an individual . . . if such individual . . . was refused employment or advancement . . . for any reason other than discrimination on account of race, color, religion, sex, or national origin.”⁴⁸⁷

Nevertheless, the Act that Congress eventually passed represented a major step in the eradication of discrimination, affording victims a means with which to redress their harms within the justice system and assistance doing so. The social impact of the Act was equally significant.⁴⁸⁸ The Act served as a catalyst for further civil rights legislation because the concentrated attention that Congress and the judiciary devoted to questions of civil rights during the ‘50s and ‘60s increased the average American’s awareness of, and sensitivity to, discrimination as well as encouraged legal action to remedy problems of discrimination.⁴⁸⁹

2. Age Discrimination in Employment Act of 1967

In 1963, Congress considered adding “age” as a protected class under the Civil Rights Act of 1964 but ended up omitting the word to assure timely passage of the Act.⁴⁹⁰ Consequently, the passage of the ADEA in 1967⁴⁹¹ to

484. 110 CONG. REC. 7188, 7213 (1964) (finding Title VII does not require any “employer [to] maintain a racial balance in his work force [and] . . . any deliberate attempt to maintain a racial balance, whatever such balance may be, would . . . violat[e] . . . Title VII because maintaining such a balance would require an employer to hire or to refuse to hire on the basis of race”).

485. 110 CONG. REC. 1957, 1994, 2547, 2558 (1964) (stating that opponents wrongly suggest that the bill establishes racially based job quotas when, in fact, “[i]t is a matter of an individual’s rights having been violated”). Senator Humphrey stated that Title VII does not “in any way authorize the Federal Government to prescribe . . . a ‘racial balance’ of job classifications . . . or ‘preferential treatment of minorities.’” 110 CONG. REC. 5411, 5423 (1964). Senator Clark stated, “The bill does not make anyone higher than anyone else. It establishes no quotas.” 110 CONG. REC. 13,050, 13,080 (1964).

486. 110 CONG. REC. 6490, 6563 (1964) (“[T]he court cannot order preferential hiring or promotion consideration for any particular race, religion, or other group. Its power is solely limited to ordering an end to discrimination which is in fact occurring.”); *Id.* at 6490, 6549 (stating that “the last sentence of section 707(e), . . . makes clear what is implicit throughout the whole title[:] . . . that employers may hire and fire, promote and refuse to promote for any reason, good or bad, provided only that individuals may not be discriminated against because of race, religion, sex, or national origin”).

487. 42 U.S.C. § 2000e–5(g) (1976).

488. For a comprehensive presentation of the events leading to, the impact of, and the current status of the Civil Rights Act of 1964, see generally THE CIVIL RIGHTS ACT OF 1964, *supra* note 469.

489. MICHAEL LES BENEDICT, CIVIL RIGHTS AND CIVIL LIBERTIES 64 (1987). See also U.S. COMMISSION ON CIVIL RIGHTS, *supra* note 480, at 2–4.

490. See Michael W. Reschke, *The Age Discrimination in Employment Act: Procedural and*

deter age discrimination in America's work environment surprised few. Congress found that arbitrary age limits unfairly disadvantage older workers, causing prolonged unemployment, a deterioration of skills and morale, and the attendant decrease in future employability.⁴⁹² Accordingly, Congress designed the ADEA to "promote employment of older persons based on their ability rather than age; . . . [to] prohibit arbitrary age discrimination in employment; . . . and [to] help employers and workers find ways of meeting problems arising from the impact of age on employment."⁴⁹³

Although initial drafts of the ADEA incorporated remedies similar to Title VII's,⁴⁹⁴ the final version of the ADEA used the enforcement scheme of

Substantive Issues in the Aftermath of the 1978 Amendments, 1979 U. ILL. L. F. 665. Age discrimination provisions were proposed to be included in Title VII of the Civil Rights Act of 1964, but failed to pass. 110 CONG. REC. 13,427, 13,490-92 (1964); 110 CONG. REC. 9873, 9911-13 (1964); 110 CONG. REC. 2547, 2596-99 (1964).

491. Pub. L. No. 90-202, 81 Stat. 602 (1967) (codified as amended at 29 U.S.C. §§ 621-634 (1994)). See also *Age Discrimination Hearings Before the Subcomm. on Labor of the Senate Comm. on Labor and Public Welfare*, 90th Cong. 23 (1967) (evidencing age discrimination prior to the enactment of the Civil Rights Act of 1964). Congress directed the Secretary of Labor to study the problem of age discrimination and the Secretary of Labor subsequently made a report to Congress. Report of the Secretary of Labor, *The Older American Worker: Age Discrimination in Employment* (1965). See also Fair Labor Standards Amendments of 1966, Pub. L. No. 89-601, § 606, 80 Stat. 830, 845 (containing specific recommendations by the Secretary of Labor).

492. Pub. L. No. 90-202, § 2, 81 Stat. 602, 602 (1967) (codified as amended at 29 U.S.C. § 621(a) (1994)). The stated findings of Congress are that:

- (1) in the face of rising productivity and affluence, older workers find themselves disadvantaged in their efforts to retain employment, and especially to regain employment when displaced from jobs;
- (2) the setting of arbitrary age limits regardless of potential for job performance has become a common practice, and certain otherwise desirable practices may work to the disadvantage of older persons;
- (3) the incidence of unemployment, especially long-term unemployment with resultant deterioration of skill, morale, and employer acceptability is, relative to the younger ages, high among older workers; their numbers are great and growing; and their employment problems grave;
- (4) the existence in industries affecting commerce, of arbitrary discrimination in employment because of age, burdens commerce and the free flow of goods in commerce.

Id.

493. *Id.* (codified as amended at 29 U.S.C. § 621(b) (1994)). Protection for this group is necessary because society in general is getting older. FRANK B. HOBBS & BONNIE L. DAMON, 65+ IN THE UNITED STATES 2-2 (1996) (stating that the "elderly population increased 11-fold between 1900 to 1994," compared with only a 3-fold increase for those under age 65). Half of the population of the United States was under twenty in 1860. *Id.* at 2-1. In 1994, half of the population was thirty-four or older and, at a minimum, half of the population is projected to be thirty-nine or older by the year 2030. In addition, the ratio of elderly to working-age persons is expected to double between 1990 and 2050. *Id.* America faces the challenge of determining "how to maintain the quality of life with advancing age." *Id.* at 1-3. For an in-depth study of the characteristics, needs, and impact of an aging population in American Society, see generally SHEILA R. ZEDLEWSKI ET AL., URBAN INSTITUTE REPORT 90-5, THE NEEDS OF THE ELDERLY IN THE 21ST CENTURY (1990).

494. See KALET, *supra* note 14, at 2 (stating that "[t]he original intent of the ADEA drafters was

the Fair Labor Standards Act of 1938 (FLSA).⁴⁹⁵ Thus, the ADEA provides for liquidated damages⁴⁹⁶ and “legal or equitable relief as may be appropriate to effectuate the purposes of” the Act.⁴⁹⁷ In 1978, amendments to the Act tolled the statute of limitations for an additional period up to one year,⁴⁹⁸ relaxed the notice requirements of the original Act,⁴⁹⁹ and expressly granted jury trials to resolve “a civil action in any court of competent jurisdiction for such *legal or equitable* relief as will effectuate the purposes of” the ADEA.⁵⁰⁰

3. *Griggs v. Duke: Disparate Impact Theory and a Stronger Equal Employment Opportunity Commission*

In the 1971 landmark decision, *Griggs v. Duke Power Co.*,⁵⁰¹ the Supreme Court secured disparate impact theory in Title VII plaintiffs’ arsenals.⁵⁰² Noting that Congress enacted Title VII to equalize employment opportunities and to remove favoritism for white employees, the Court established a new standard to be employed by employers under the Act.⁵⁰³ First, *Griggs* called for the plaintiff to initially make a prima facie showing that a facially neutral employment practice disproportionately affected

merely to accord age the same protected status as that extended to race and sex under Title VII”).

495. Fair Labor Standards Act of 1938, ch. 676, § 1, 52 Stat. 1060, 1060 (codified as amended at 29 U.S.C. §§ 201-219 (1994)); Note, *The Age Discrimination in Employment Act of 1967*, 90 HARV. L. REV. 380, 381 (1976). One of the reasons for incorporating the enforcement procedures of the FLSA was to prevent overburdening the EEOC. *See id.* By adopting the FLSA provisions, the Wage and Hour Division of the Department of Labor would have a duty to handle complaints under the 1967 Act. *See id.*

496. Fair Labor Standards Act of 1938, ch. 676, § 16, 52 Stat. 1060, 1069 (codified as amended at 29 U.S.C. § 216(b) (1994)). FLSA provides: “Any employer who violates the provisions . . . of this title shall be liable to the employee or employees affected in the amount of their unpaid minimum wages, or their unpaid overtime compensation, as the case may be, and in an additional equal amount as liquidated damages.” 29 U.S.C. § 216(b). Under *Overnight Motor Transp. Co. v. Missel*, the imposition of liquidated damages was held mandatory. 316 U.S. 572, 583-84 (1942). However, Section 2(e) of the Portal to Portal Act of 1947 (PPA) modified the FLSA by allowing liquidated damage awards only upon a showing of bad faith. Portal to Portal Act, ch. 52, § 11, 61 Stat. 84, 89 (codified as amended at 29 U.S.C. § 260 (1994)).

497. *See* Age Discrimination in Employment Act, Pub. L. No. 90-202, § 7(b), 81 Stat. 602, 604 (1967) (codified and amended at 29 U.S.C. § 626(c) (1994)).

498. *See* Age Discrimination in Employment Act Amendments of 1978, Pub. L. No. 95-256, § 4(c), 92 Stat. 189, 191 (codified and amended at 29 U.S.C. § 626(e) (1994)).

499. *See id.* § 4(b) (codified and amended at 29 U.S.C. § 626(d) (1994)).

500. *See* Age Discrimination in Employment Act, Pub. L. No. 90-202, § 7(c), 81 Stat. 602, 604 (1967) (codified and amended at 29 U.S.C. § 626(c) (1994)).

501. 401 U.S. 424 (1971).

502. *Id.* at 431 (finding that Title VII of the Civil Rights Act of 1964 “proscribes not only overt discrimination but also practices that are fair in form, but discriminatory in operation”).

503. *Id.* at 429-30.

minority workers.⁵⁰⁴ Thereafter, the burden shifted to the employer to establish that “business necessity” compelled the challenged practice.⁵⁰⁵ Thus, after *Griggs*, the plaintiff no longer had to prove that the employer acted with discriminatory intent to prevail under Title VII.⁵⁰⁶

Although *Griggs* became one of the civil rights movement’s greatest legal victories, it became only symbolic when Congress found faulty “the machinery created by the Civil Rights Act of 1964” to enforce Title VII.⁵⁰⁷ Determining that employment discrimination “is a far more complex and pervasive phenomenon” than originally expected to be,⁵⁰⁸ Congress passed the Equal Employment Opportunity Act (EEOA)⁵⁰⁹ to empower the EEOC “to issue complaints and hold hearings, to issue cease-and-desist orders against discriminatory practices, and to seek enforcement of its orders in the Federal Courts.”⁵¹⁰ Vested with these new powers, the EEOC became the

504. *Id.* at 429-33.

505. *Id.* at 432 (stating that “Congress has placed on the employer the burden of showing that any given requirement must have a manifest relationship to the employment in question”). After *Albemarle Paper Co. v. Moody*, it was settled that if the employer succeeded in discharging the burden, the plaintiff still prevailed upon directing to the court’s attention an alternatively less discriminatory practice that would suffice the needs of the business. 422 U.S. 405, 425 (1975).

506. 401 U.S. at 431. See also Developments in the Law, *Employment Discrimination*, 109 HARV. L. REV. 1568, 1572 (1996) (stating that the “first major development pursuant to . . . [Title VII] was the evolution of the disparate impact theory of discrimination, which the Supreme Court enunciated in *Griggs v. Duke Power Co.* and which Congress later codified in the Civil Rights Act of 1991”) (internal footnotes omitted). Congress supported the *Griggs* decision in the Civil Rights Act of 1972. See H.R. REP. NO. 92-238, at 21-22 (1971), reprinted in 1972 U.S.C.C.A.N. 2137, 2156-67; S. REP. NO. 92-415, at 14 (1971). One commentator has tried to explain the reason behind the congressional support in *Griggs*.

Griggs harmed big business, which saw itself faced with Title VII lawsuits simply for having “bad numbers,” and in 1971-72 a majority in Congress probably did not agree with the sweeping reconceptualization of Title VII in *Griggs*. However, the Labor Committees in both chambers were significantly to the left of their chamber medians and probably preferred *Griggs* to any bill their chambers would have passed. Hence, no committee-generated bill contained a *Griggs* provision, and both committees inserted language in their reports for the 1972 amendments to Title VII that strongly approved of *Griggs*.

William N. Eskridge, Jr., *Overriding Supreme Court Statutory Interpretation Decisions*, 101 YALE L. J. 331, 370-71 (1991) (internal footnotes omitted).

507. H.R. REP. NO. 92-238, at 3 (1971), reprinted in 1972 U.S.C.C.A.N. 2137, 2139.

508. See *id.* at 2144. Significantly, “[d]uring the first 5 years of its existence, the . . . [EEOC received] more than 52,000 charges . . . [of which] 35,445 were recommended for investigation . . . [Of those,] . . . reasonable cause was found in over 63% of the cases, but in less than half of these cases was the Commission able to achieve a totally or even partially successful conciliation.” *Id.* at 2139-40. Of the charges recommended for investigation, approximately 56% involved racial discrimination, 23% alleged gender discrimination, and the remainder claimed discrimination based on national origin or religion. See *id.* at 2139.

509. Pub. L. No. 92-261, 86 Stat. 103 (1972) (codified as amended at 42 U.S.C. § 2000e-5 (1994)).

510. H.R. REP. NO. 92-238, at 9 (1971), reprinted in 1972 U.S.C.C.A.N. 2137, 2145. The alleged victim is also at liberty to proceed privately with a suit if the Commission “finds no reasonable cause,

gatekeeper for all Title VII claims in federal court and ultimately the Supreme Court, which eventually became swamped with cases involving Title VII, affirmative action, and the Equal Protection Clause.⁵¹¹

fails to make a finding of reasonable cause, or takes no action in respect to a charge, or has not within 180 days issued a complaint nor entered into a conciliation or settlement agreement which is acceptable to the person aggrieved" *See id.* at 2147. Furthermore, jurisdiction of "Pattern or Practice" suits was transferred to the EEOC. *See id.* at 2149.

511. The history of affirmative action in the Supreme Court is clouded with divisiveness. In *Regents of the University of California v. Bakke*, the first affirmative action case decided by the Supreme Court, strict scrutiny was applied, and the Court found unconstitutional a medical school's use of a quota system which reserved sixteen slots in the incoming class for minorities. 438 U.S. 265, 289 (1978). The Court, however, held that because the school had a "substantial interest that legitimately may be served by a properly devised admissions program involving the competitive consideration of race and ethnic origin . . . [the portion of the] California court's judgment [that] enjoins petitioner from any consideration of the race of any applicant must be reversed." *Id.* at 320. In contrast, the dissent applied intermediate scrutiny and looked to the government's goal of diversity as a substantial interest justifying affirmative action. *See id.* at 357-62. Although Justices Blackmun, Brennan, White, and Marshall agreed that rational basis should not apply to the case at hand, they believed that the proper standard of review should not be strict in the popular sense of the term. *See id.* at 358-59, 361-62. Because the white group was burdened by the admissions program, rather than the black group, the dissenters applied a standard that was "strict—not "'strict" in theory and fatal in fact.'" *Id.* at 357, 361-62 (citing Gerald Gunther, *The Supreme Court, 1971 Term—Foreword: In Search of Evolving Doctrine on a Changing Court: A Model for a Newer Equal Protection*, 86 HARV. L. REV. 1, 8 (1972) ("The Warren Court embraced a rigid two-tier attitude. Some situations evoked the aggressive 'new' equal protection, with scrutiny that was 'strict' in theory and fatal in fact.")).

In *United Steelworkers of America v. Weber*, a steelworkers' union and a steel corporation set up a program that reserved fifty percent of all training positions for minorities and that was to remain in place until the discrepancy between the percentage of blacks in the labor force (39%) and the percentage of blacks in skilled positions (1.83%) was remedied. 443 U.S. 193, 198-99 (1979). The Court carved out a four-prong test for affirmative action programs holding that the Court does not bar private, voluntary race-conscious affirmative action arrangements provided they are temporary and do not become a roadblock to the advancement of white employees. *See id.* at 208. Concluding that the *Weber* plaintiffs met their test and that Congress did not exclude such a program through the wording of Title VII, the five-member Court majority upheld the affirmative action plan. *See id.* Chief Justice Burger and Justice Rehnquist dissented because to them Title VII prohibited *any* and *all* discrimination on the basis of race. *See id.* at 216, 218, 254, 255. *See also* Fullilove v. Klutznick, 448 U.S. 448, 454, 473, 480 (1980) (upholding business set-aside programs because Congress could use racial classifications, not under- or over-inclusive, but temporary and narrowly tailored classifications in order to remedy effects of past discrimination, that it should suffice that Congress had resolved to abrogate practices that "might result in perpetuation of the effects of prior discrimination which had impaired or foreclosed access by minority businesses to public contracting opportunities").

In a series of cases that followed, the Court developed criteria under which affirmative action programs could survive a challenge. *See, e.g.,* Johnson v. Transp. Agency, Santa Clara County, Cal., 480 U.S. 616, 619-23, 641-2 (1987) (holding that an employment program which allowed for race and gender to be considered in hiring and promoting decisions did not violate Title VII); *United States v. Paradise*, 480 U.S. 149, 153-67, 185-86 (1987) (upholding a district court order that required fifty percent of all new hires to be black and subsequent order that fifty percent of all promotions be given to blacks, where through 1972 no black individual had been employed as a state trooper in Alabama, on the grounds that the orders were temporary and did not force the layoffs or the hiring of unqualified individuals as required under the Equal Protection Clause of the Fourteenth Amendment); *Local Number 93, Int'l Ass'n of Firefighters, AFL-CIO v. City of Cleveland*, 478 U.S. 501, 530 (1986) (holding that section 706(g) of Title VII of the Civil Rights Act of 1964 allows a court to approve a

4. *The Rehabilitation Act of 1973 and the Americans with Disabilities Act of 1990*

With the passage of the Rehabilitation Act of 1973 (REHAB), Congress extended civil rights protections to individuals with both mental and physical disabilities.⁵¹² REHAB prohibited federal contractors, recipients of federal financial assistance, and participants in federal programs from discriminating against individuals with disabilities.⁵¹³ Although REHAB afforded the disabled some protection from discrimination, it did not protect the disabled from discrimination by privately funded entities and programs. Not until after significant findings showed the severe effects of discrimination against the disabled did Congress pass the ADA⁵¹⁴ to provide a “clear and

consent decree to resolve Title VII compliance problems and provide relief that may benefit an individual who was not the victim of the defendant’s past discriminatory acts); *Local 28 of the Sheet Metal Workers’ Int’l Ass’n v. Equal Employment Opportunity Comm’n*, 478 U.S. 421, 482 (1986) (holding that a court “may, in appropriate circumstances, order preferential relief benefiting individuals who are not the actual victims of discrimination as a remedy for violations of Title VII” and more specifically, upholding a court-imposed 29% racial minority membership goal in a union that had discriminated in the past with respect to recruitment, selection, training, and admissions). For Supreme Court decisions holding affirmative action programs unconstitutional, see *Wygant v. Jackson Bd. of Educ.*, 476 U.S. 267, 269-70, 284 (1986) (holding a collective bargaining agreement unconstitutional under the Equal Protection Clause of the Fourteenth Amendment where the agreement provided preferential treatment to minority teachers in times of lay-offs); *Firefighters Local Union No. 1784 v. Stotts*, 467 U.S. 561, 565-68, 583 (1984) (holding that a court order forcing an employer to lay off senior employees in favor of junior employees, in order to preserve a particular percentage of blacks in the work force, violates Title VII).

512. Rehabilitation Act of 1973, Pub. L. No. 93-112, 87 Stat. 355 (codified as amended at 29 U.S.C. §§ 701-797(b) (1994)).

513. See Pub. L. No. 93-112, § 504, 87 Stat. 355, 394 (1973) (codified as amended at 29 U.S.C. § 794(a) (1994)). Section 794(a) states:

No otherwise qualified individual with a disability in the United States, . . . shall, solely by reason of her or his disability, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance or under any program or activity conducted by any Executive agency or by the United States Postal Service.

Id.

514. Pub. L. No. 101-336, 104 Stat. 327 (1990) (codified as amended at 42 U.S.C. §§ 12101-12213 (1994)); § 2, 104 Stat. at 328-29 (codified as amended at 42 U.S.C. § 12101(a) (1994)) (stating that Congress established from “census data, national polls, and other studies . . . that people with disabilities, as a group, occupy an inferior status in our society, and are severely disadvantaged socially, vocationally, economically, and educationally”). The legislative history of the ADA shows that Congress recognized that “historically, society has tended to isolate and segregate individuals with disabilities, and . . . such forms of discrimination against individuals with disabilities continue to be a serious and pervasive social problem.” STAFF OF HOUSE COMM. ON EDUCATION AND LABOR, 101ST CONG., *THE AMERICANS WITH DISABILITIES ACT 6* (Comm. Print 1990). Congress noted the magnitude of the problem and the number of Americans affected in the *Hearings Before the Comm. on Labor and Human Resources and the Subcomm. on the Handicapped*, 101st Cong. 201-02 (1989). This report stated:

[O]ver 36 million people in this country are disabled by reason of some physical or mental

comprehensive national mandate for the elimination of discrimination against individuals with disabilities.”⁵¹⁵ The ADA made it unlawful for public and private organizations to discriminate against the disabled in employment (Title I),⁵¹⁶ in public services (Title II),⁵¹⁷ in accommodations (Title III),⁵¹⁸

handicapping condition. The mere existence of these conditions does not for many of these individuals prevent them from interacting freely with others in society, or from performing the tasks that others perform on a daily basis. But persons with disabilities are all too often not allowed to participate because of stereotypical notions held by others in society— notions that have, in large measure, been created by ignorance and maintained by fear.

Id. at 201.

515. Americans with Disabilities Act of 1990, Pub. L. No. 101-336, § 2(b)(1), 104 Stat. 327, 329 (1990) (codified as amended at 42 U.S.C. § 12101(b)(1) (1994)).

516. *Id.* §§ 101-108, 104 Stat. at 330-37 (1990) (codified as amended at 42 U.S.C. §§ 12111-12117 (1994)). Section 102 of the Act states that “[n]o covered entity shall discriminate against a qualified individual with a disability because of the disability of such individual in regard to job application procedures, the hiring, advancement, or discharge of employees, employee compensation, job training, and other terms, conditions, and privileges of employment.” *Id.* § 102. Section 101 defines a “covered entity” as any employer type entity. *Id.* § 101. The Act covers entities with more than 15 people working each business day at least 20 hours. *Id.* Section 102 defines “qualified individual with a disability [as] an individual with a disability who, with or without reasonable accommodation, can perform the essential functions of the employment position that such individual holds or desires.” *Id.* § 102. By using a broad definition of discrimination, the Act is designed to thwart all variations of discrimination, even those remotely tangential to the employment relationship. *Id.* § 102. The Act also prohibits medical exams used as a pretext or screening process unless there is a job-related necessity. *Id.* § 102. Furthermore, the Act prohibits even an investigation by the employer of an employee as to the nature and extent of the disability. *Id.* § 102. Section 103 of the Act provides that an employer generally can defeat an accusation of discrimination by demonstrating a “business necessity, and [that] such performance cannot be accomplished by reasonable accommodation.” *Id.* § 103. Section 104 of the Act declares that the Act “shall not include any employee or applicant who is currently engaging in the illegal use of drugs, when the covered entity acts on the basis of such use.” *Id.* § 104. Employers may prohibit the use of drugs or alcohol on the job and require drug testing. *Id.* § 104. However, an employer may not use the fact that an individual has completed, or is currently in, a drug rehabilitation program to discriminate against them. *Id.* § 104.

517. Americans with Disabilities Act of 1990, Pub. L. No. 101-336, §§ 201-246, 104 Stat. 327, 337-53 (codified as amended at 42 U.S.C. §§ 12131-12165 (1994)). Section 202 of the Act provides that no public entity shall discriminate against a person with a disability. *Id.* § 202. A public entity is defined as “(A) any State or local government; (B) any department, agency, special purpose district, or other instrumentality of a State or States or local government; and (C) the National Railroad Passenger Corporation.” *Id.* § 201. Any entity that procures new equipment, builds new facilities, or fails to make accommodations to current equipment or facilities violates the law. *Id.* § 303. In general, there is a simultaneous violation of this Act and section 504 of the Rehabilitation Act of 1973; section 203 of the ADA states that “[t]he remedies, procedures, and rights set forth in section 505 of the Rehabilitation Act of 1973 (29 U.S.C. 794a) shall be the remedies, procedures, and rights this title provides.” *Id.* § 203.

518. Americans with Disabilities Act of 1990, Pub. L. No. 101-336, §§ 301-310, 104 Stat. 327, 353-65 (codified as amended at 42 U.S.C. §§ 12181-12189). Section 302 of the Act provides that “[n]o individual shall be discriminated against on the basis of disability in the full and equal enjoyment of the goods, services, facilities, privileges, advantages, or accommodations of any place of public accommodation by any person who owns, leases (or leases to), or operates a place of public accommodation.” *Id.* § 302. Among others, a public accommodation includes “an inn, hotel, motel, or other place of lodging, . . . restaurant, bar, or other establishment serving food or drink, . . . motion picture house, theater, concert hall, stadium, . . . or other place of public gathering, . . . bakery, grocery

and in telecommunications (Title IV).⁵¹⁹

5. *Civil Rights Act of 1991*

In 1989, at the same time Congress was passing the ADA, the Supreme Court decided seven cases that weakened affirmative action programs and civil rights protections.⁵²⁰ Two of these cases—*City of Richmond v. J.A.*

store, clothing store, . . . or other sales or rental establishment, . . . laundromat, . . . bank, . . . funeral parlor . . . or other service establishment.” *Id.* § 301. However, private clubs and religious institutions are specifically exempted from this act by section 307. *Id.* § 307. Any entity that procures new equipment, builds new facilities, or fails to make accommodations for current equipment or facilities violates the law. *Id.* § 303. An individual may be discriminated against in various forms that includes “denial of participation, . . . participation in unequal benefit, . . . [or] separate benefit.” *Id.* § 302. Furthermore, access “shall be afforded to [the] individual with a disability in the most integrated setting appropriate to the needs of the individual.” *Id.* § 302.

519. Americans with Disabilities Act of 1990, Pub. L. No. 101-336, §§ 401-402, 104 Stat. 327, 366-69 (codified as amended at 47 U.S.C. §§ 225, 611 (1994)). Section 401 amends Title II of the Communications Act of 1934, § 401, Pub. L. No. 101-336, § 201, 48 Stat. 1064, 1070 (codified as amended at 47 U.S.C. § 201 (1994)). This section of the Act requires that all common carriers establish and maintain communication equipment for the disabled. *Id.* § 401. This service is to be provided 24 hours a day, 7 days a week, and at no additional cost to the disabled. *Id.* The Act also “prohibit[s] relay operators from failing to fulfill the obligations of common carriers by refusing calls or limiting the length of calls that use telecommunications relay services.” *Id.* A common carrier is defined as an entity “engaged in interstate communication by wire or radio.” *Id.*

520. First, in *Price Waterhouse v. Hopkins*, the Court held that an employer does not violate Title VII when an employer can prove that it would have made the same decision without the existence of an impermissible motive. 490 U.S. 228, 258 (1989). Second, in *Patterson v. McLean Credit Union*, the Supreme Court held that 42 U.S.C. § 1981, which prohibits discrimination on the basis of race in making and enforcing private contracts, does not prohibit racial harassment by an employer because the acts of the employer do not impair the right of the employee to “make” or to “enforce” contracts. 491 U.S. 164, 170-71 (1989). Third, in *Lorance v. AT&T Technologies Inc.*, the Supreme Court held that the statute of limitations for challenging seniority plans that are discriminatory begins to run when the employer adopts the plan rather than on the date when the injury occurs. 490 U.S. 900, 911-12 (1989). Fourth, in *Martin v. Wilks*, a group of white firefighters brought a reverse discrimination claim against Birmingham, Alabama (City) and Jefferson County Personnel Board (County) in reaction to a consent decree providing that the City and County promote blacks under an affirmative action program. 490 U.S. 755, 759 (1989). The consent decrees were entered into when a group of black firefighters and the NAACP sued the city of Birmingham, Alabama, and Jefferson County Personnel Board for discriminating in their hiring practices under Title VII of the Civil Rights Act of 1964. *See id.* At first, a group of white firefighters tried to challenge putting the consent decrees into effect. *See id.* at 758-59. The district denied the intervening motion and the decrees went into effect. *See id.* When the subsequent group of white firefighters challenged the operational decree as violating federal law the district court allowed the second group of white firefighters to proceed in their action and declared that the decrees would only provide an affirmative defense to the claim of the second group of white firefighters. *See id.* at 760. The Court of Appeals for the Eleventh Circuit reversed the decision of the district court on the grounds that the second group of white firefighters were “neither parties nor privies to the consent decrees” and therefore, “their independent claims of unlawful discrimination are not precluded.” *Id.* at 761. The Supreme Court granted certiorari and affirmed the decision of the Eleventh Circuit. *See id.* at 761. Fifth, in *Independent Federation of Flight Attendants v. Zipes*, the Supreme Court held that under Title VII attorney’s fees could only be collected from losing intervenors where there is a showing that the intervenor acted frivolously, unreasonably, or without

*Croson Co.*⁵²¹ and *Wards Cove Packing Co. v. Atonio*⁵²²—caused especially devastating consequences.

The Supreme Court decision of *City of Richmond v. J.A. Croson Co.* marked the trend in the Court itself and circuit courts of appeals generally advancing strict scrutiny when racial classifications were made to employ any statute or program, including affirmative action efforts.⁵²³ This case concerned the constitutionality of a minority business set-aside program, voluntarily established by the City of Richmond, Virginia, which sought to remedy the effects of past discrimination in the construction business.⁵²⁴ Unlike previous decisions regarding affirmative action programs, a majority of the Court applied strict scrutiny as the standard of review.⁵²⁵ Therefore, the City of Richmond needed to show that its program was narrowly tailored to remedy the past effects of discrimination.⁵²⁶ The Court held that City of Richmond needed specific evidence of “identified discrimination in the Richmond construction industry” in order for the program to survive review.⁵²⁷

Richmond argued in response that it would subvert federalist principles to hold that the federal government without such evidence of “identified discrimination” has a compelling interest in remedying the effects of racial discrimination in its own public works program, but a city government does not share the same compelling interest under the same standards.”⁵²⁸ The Court disagreed and held Richmond’s program unconstitutional.⁵²⁹ Although voluntary set-aside programs may survive under *Croson*, “[i]n the extreme case, [where] some form of narrowly tailored racial preference might be necessary to break down patterns of deliberate exclusion,”⁵³⁰ the decision, in practical terms, paralyzed affirmative action programs. As a result of *Croson*, several lower courts struck down city, county, and state set-aside programs, and several state and local governments decided to abandon their affirmative

foundation. 491 U.S. 754, 765-66 (1989). Cases six and seven are discussed *infra* notes 521-35.

521. 488 U.S. 469 (1989).

522. 490 U.S. 642 (1989).

523. See George R. La Noue, *The Impact of Croson on Equal Protection Law and Policy*, 61 ALB. L. REV. 1 (1997).

524. See *Croson*, 488 U.S. at 478.

525. See *id.* at 507-08. Specifically, the Court chose not follow *Fullilove v. Klutznick* which held that Congress did not need to make specific findings of discrimination in order to engage in nationwide race-conscious relief. See *id.* at 488-93.

526. See *id.* at 508.

527. *Id.* at 500.

528. *Id.* at 489 (quoting Brief for Appellant at 32). Here, Richmond was attempting to persuade the Court to apply the *Fullilove* analysis to city set-aside programs.

529. See *id.* at 511.

530. *Croson*, 488 U.S. at 509.

action programs rather than “attempt to defend or restructure them.”⁵³¹

The Supreme Court, in *Wards Cove Packing Company, Inc. v. Atonio*, overruled key aspects of the disparate impact theory articulated in *Griggs*. The Court first held that the “proper basis for the initial inquiry” in disparate impact analysis is “between the racial composition of the qualified persons in the labor market and the persons holding at-issue jobs” and not between one section of the employer’s labor force and another.⁵³² Second, in order to establish a *prima facie* case of disparate impact under Title VII, the Court held that a “plaintiff must demonstrate that . . . the application of a specific or particular employment practice . . . has created the disparate impact under attack.”⁵³³ Third, the Court held that to prove business necessity the defendant must show that “a challenged practice serves, in a significant way, the legitimate employment goals of the employer.”⁵³⁴ Fourth, the Court emphasized that while “the employer carries the burden of producing evidence of a business [necessity]. . . for his employment practice,” the disparate impact plaintiff still carries the burden of persuasion.⁵³⁵

Thereafter, the legislature found that because “the Supreme Court[‘s decision] in *Wards Cove* . . . weakened the scope and effectiveness of Federal civil rights protections . . . additional remedies under Federal law [were] needed to deter unlawful harassment and intentional discrimination in the workplace . . . and . . . to provide additional protections against unlawful discrimination in employment.”⁵³⁶ Thus, Congress passed the Civil Rights Act of 1991⁵³⁷ to strengthen the effectiveness of civil rights legislation.⁵³⁸

531. Paul K. Sonn, Note, *Fighting Minority Under-representation in Publicly Funded Construction Projects After Croson: A Title VI Litigation Strategy*, 101 YALE L.J. 1577, 1577 (1992) (discussing detailed effects of *Croson*).

532. *Id.* at 650-51.

533. *Id.* at 657.

534. *Id.* at 659.

535. *Id.* One commentator explains that the outcome of *Wards Cove* may be due to the “political orientation of the Supreme Court.” Girardeau A. Spann, *Color-Coded Standing*, 80 CORNELL L. REV. 1422, 1479 (1995).

When *Griggs* was decided in 1971, the Court was still similar to the Warren Court. Chief Justice Warren had retired only two years earlier. By 1989, however, when *Wards Cove* was decided, Justices Black, Douglas, Harlan, and Stewart had been replaced by Chief Justice Rehnquist, and Justices O’Connor, Scalia, and Kennedy. The 1989 Court was much more conservative on racial issues than the immediate post-Warren Court had been. A measure of the 1989 Court’s racial conservatism is provided by the fact that none of the four replacement Justices has ever voted in favor of the minority position in an affirmative action case that the Court has decided on constitutional grounds. Now that Justices Brennan and Marshall have been replaced by Justices Souter and Thomas, the present Supreme Court is even more conservative on racial issues. *See id.* at 1479-80.

536. Civil Rights Act of 1991, Pub. L. No. 102-166, § 2, 105 Stat. 1071, 1071.

537. *Id.*

538. *Id.* § 3.

Several sections of the 1991 Act directly overruled or responded to the Supreme Court's holding in *Wards Cove*.⁵³⁹ Section 105 of the Act restored and codified the *Griggs* rule.⁵⁴⁰ In addition, the Act extended jury trials to cases originating under Title VII⁵⁴¹ and provided compensatory and punitive damages for claims brought under Title VII, the ADA, and the ADEA.⁵⁴² Unfortunately, however, the Act did nothing to remedy the debilitating effects of *Croson*.

In short, society's longstanding cry for justice culminated in the Civil

539. See H.R. REP. NO. 102-40, at 2-4 (1991), reprinted in 1991 U.S.C.C.A.N. 694, 694-96. First, the 1991 Act overrules *Patterson v. McLean Credit Union*, 491 U.S. 164 (1989). "Section 12 of the Act amends Section 1981 to reaffirm that the right 'to make and enforce contracts' includes the enjoyment of all benefits, privileges, terms and conditions of the contractual relationship." *Id.* at 694-95. Second, Congress nullified the holding in *Pricewaterhouse v. Hopkins*, 490 U.S. 228 (1989). Section 5 of the 1991 Act states that any case where an employer relies "on prejudice in making employment decisions is illegal. At the same time, [however,] the Act makes clear that, in considering the appropriate relief for such discrimination [in a mixed motives case], a court shall not order the hiring, retention or promoting of a person not qualified for the position." *Id.* at 695. Third, [s]ection 6 of the Act eliminates the possibility of the errant outcome of *Martin v. Wilks*, 490 U.S. 755 (1989), "by encouraging the giving of notice to persons who might be adversely affected by a proposed court order, . . . affording them a reasonable opportunity to challenge the order [but barring] subsequent lawsuits challenging the court order, except under certain circumstances." *Id.* Fourth, "[s]ection 7 of the Act overrules *Lorance [v. AT&T Technologies]*, 490 U.S. 900 (1989), and permits person[] [sic] to challenge discriminatory employment practices when those practices actually harm them." *Id.* Fifth, [s]ection 10 of the Act overrules the Supreme Court's holding in *Library of Congress v. Shaw*, 478 U.S. 310 (1986), to "expressly waive[] [sic] the Government's immunity from interest . . . [and] clarifies that courts may award interest or other compensation to prevailing parties and their counsel for delayed payment of monetary relief by the federal government." *Id.* at 727. Sixth, [s]ection 9 of the Act addressed three Supreme Court cases that attacked fee recovery through the following means: (1) permitting prevailing plaintiffs to recover reasonable costs for experts who assist them in their case unlike *Crawford Fitting Co. v. J.T. Gibbons, Inc.*, 482 U.S. 437 (1987); (2) permitting prevailing parties to recover reasonable attorney's fees incurred defending the original proceeding against a subsequent challenge, unlike *Independent Federation of Flight Attendants v. Zipes*, 491 U.S. 754 (1989); and (3) forbidding settlement "through a court order or stipulation of dismissal unless the parties or their counsel attest to the court that a waiver of all or substantially all attorney's fees was not compelled as a condition of the settlement, unlike *Evans v. Jeff D.*, 475 U.S. 717 (1986). *Id.* at 696. Section 9 also overrode the Court's holding in *Marek v. Chesny*, 473 U.S. 1 (1985), allowing "plaintiffs who reject an offer of settlement more favorable than what is thereafter recovered at trial [to] . . . recover[] [sic] attorney's fees incurred for services performed after the offer is rejected." *Id.*

540. See Civil Rights Act of 1991, Pub. L. No. 102-166, § 105, 105 Stat. 1071, 1074-75 (codified at 42 U.S.C. § 2000e-2(k) (1994)).

541. *Id.* at § 102, 105 Stat. at 1073 (codified at 42 U.S.C. § 19819(c) (1994)).

542. See H.R. REP. NO. 102-40, pt. 2, at 28-29 (1991), reprinted in 1991 U.S.C.C.A.N. 694, 722. The pertinent language provides:

[T]he Act amends Title VII to grant victims of intentional discrimination the right to recover compensatory damages, and, in egregious cases, punitive damages as well . . .

A number of other laws banning discrimination, including . . . [the ADA and the ADEA] are modeled after, and have been interpreted in a manner consistent with, Title VII.

The Committee intends that these other laws modeled after Title VII be interpreted consistently in a manner consistent with Title VII as amended by this Act.

Id.

Rights Act of 1964,⁵⁴³ the ADEA,⁵⁴⁴ REHAB,⁵⁴⁵ the ADA,⁵⁴⁶ and the Civil Rights Act of 1991.⁵⁴⁷ These statutory enactments fundamentally changed federal law to reflect societal value for each individual's right to equality, to be treated with dignity, and to be afforded the opportunity to develop fully his or her potential in political, economic, social, and legal contexts.⁵⁴⁸ However, while the civil rights movement flourished between the '60s and early '90s, in the '80s and '90s, a diametrically opposed movement mounted in Congress that directly effected individuals protected by civil rights legislation. This movement was tort reform.

B. Tort Reform

While the civil rights era brought forth the above-mentioned civil measures, the era also marked a turning point in congressional action. Three circumstances gave rise to massive tort reform at both the federal⁵⁴⁹ and the state⁵⁵⁰ legislative level. First, a purported medical malpractice litigation crisis in the late '60s caused increases in physician's malpractice insurance and, in turn, increased medical treatment costs throughout the country.⁵⁵¹ Next, an alleged overflow of products liability litigation in the '70s increased manufacturers' insurance rates.⁵⁵² Third, a supposed general tort crisis in the

543. Pub. L. No. 88-352, 78 Stat. 241 (1964) (codified as amended in scattered sections of 42 U.S.C.).

544. 29 U.S.C. §§ 621-634 (1994 & Supp. II 1996).

545. *Id.* §§ 701-797(b).

546. 42 U.S.C. §§ 12101-12213 (1994 & Supp. II 1996).

547. Pub. L. No. 102-166, 105 Stat. 1071 (codified as amended in scattered sections of 42 U.S.C.).

548. See JOSEPH PARKER WITHERSPOON, ADMINISTRATIVE IMPLEMENTATION OF CIVIL RIGHTS 23 (1968) ("This federal action has resulted . . . from a vital, profound shift in the real structure and dynamism of our pluralistic society, and it has produced a fundamental change in our federal system.")

549. For articles discussing various state tort reform, see Drier, *Analysis: 1987 Product Liability Act*, 41 RUTGERS L. REV. 1279 (1989); Graham, *1987 Oregon Tort Reform Legislation: True Tort Reform or Mere Restatement?*, 24 WILLAMETTE L. REV. 83 (1988). See also Peter A. Bell, *Legislative Intrusions into the Common Law of Medical Malpractice*, 35 SYRACUSE L. REV. 939, 943 (1984) (discussing massive state medical malpractice limitations); Nancy L. Manzer, Note, *Tort Reform Legislation: A Systematic Evaluation of Caps on Damages and Limitations on Joint and Several Liability*, 73 CORNELL L. REV. 628, 633 (1988).

550. See Note, "Common Sense" Legislation: *The Birth of Neoclassical Tort Reform*, 109 HARV. L. REV. 1765, 1767 (1996).

551. See SENATE SUBCOMM. ON EXECUTIVE REORGANIZATION, 91ST CONG., REPORT ON MEDICAL MALPRACTICE: THE PATIENT VERSUS THE PHYSICIAN (Comm. Print 1969); PATRICIA M. DANZON, MEDICAL MALPRACTICE: THEORY, EVIDENCE, AND PUBLIC POLICY 97-117 (1985). But see W. John Thomas, *The Medical Malpractice "Crisis": A Critical Examination of a Public Debate*, 65 TEMP. L. REV. 459, 526 (1992) (discussing tort reform and concluding that the tort system is not solely to be blamed for the perceived medical malpractice crises).

552. See U.S. DEP'T OF COMMERCE INTER-AGENCY TASK FORCE ON PRODUCTS LIABILITY, FINAL REPORT (1978); *Impact on Product Liability: Hearings Before the Senate Select Comm. on Small*

'80s caused companies to refuse to reissue policies to high-risk holders.⁵⁵³

Additionally, the judiciary may have been acting in concert with federal and state legislatures in discouraging law suits. While the judiciary did not absolutely abandon the aggrieved plaintiffs, the courts were cognizant of the titanic amounts of tort litigation flowing through the gates and worked to decrease that amount.⁵⁵⁴

During the '80s states endeavored to drain tort litigation from the ever-increasing dockets of the judiciary and limit the overall risk associated with insurance companies.⁵⁵⁵ From January to June of 1986, nineteen states established tort reform committees.⁵⁵⁶ Ten states placed limits on noneconomic and punitive damages.⁵⁵⁷ Thirteen states minimized the exposure of defendants by imposing limitations on liability or establishing immunities from suit.⁵⁵⁸ Nine states reevaluated and modified their doctrines of joint and several liability.⁵⁵⁹ Four states sought to limit access to the court system by shortening their respective statutes of limitations.⁵⁶⁰ Eleven states ratified dram shop laws.⁵⁶¹ In an effort to promote alternative dispute resolution, seventeen states enacted laws to encourage nonjudicial resolution of disputes.⁵⁶² Seven states provided for structured or periodic payments

Business, 94th Cong. pt. 1, at 1, 733-35, pt. 2, at 1473-74, 1582 (1976); *Impact on Product Liability: Hearings Before the Senate Select Comm. on Small Business*, 95th Cong. pt. 4, at 1787, pt. 5, at 2187 (1977). See also STEPHEN D. SUGARMAN, *DOING AWAY WITH PERSONAL INJURY LAW 85-87* (1989) (discussing congressional action on tort reform). But see U.S. DEP'T OF COMMERCE, INTERAGENCY TASK FORCE ON PRODUCT LIABILITY: FINAL REPORT (1977), reprinted in 9 LOUIS R. FRUMER & MELVIN I. FRIEDMAN, *PRODUCTS LIABILITY* app. G, at 667 (1998) (finding that one of the major reasons behind the products liability crisis was the liability ratemaking procedure). For findings on the alleged overflow of products liability litigation, see U.S. DEP'T OF COMMERCE INTERAGENCY TASK FORCE ON PRODUCTS LIABILITY, FINAL REPORT (1978); *Impact on Product Liability: Hearings Before the Senate Select Comm. On Small Business*, 94th Cong. pt. 1, at 1, 733-35, pt. 2, at 1473-74, 1582 (1977); *Impact on Product Liability: Hearings Before the Senate Select Comm. on Small Business*, 95th Cong. pt. 4, at 1787, pt. 5, at 2187 (1977).

553. For findings on the supposed general tort crisis, see REPORT OF THE TORT POLICY WORKING GROUP ON THE CAUSES, EXTENT AND POLICY IMPLICATIONS OF THE CURRENT CRISIS IN INSURANCE AVAILABILITY AND AFFORDABILITY 6-15 (1986). But see George L. Priest, *The Current Insurance Crisis and Modern Tort Law*, 96 YALE L.J. 1521, 1523 (1987) (stating that one of the theories behind the insurance rate crises blames the insurance industry for price fixing).

554. See *id.* at 1523-24, 1532-34.

555. See *id.* at 1523.

556. See *id.*

557. Glenn Blackmon & Richard Zeckhauser, *State Tort Reform Legislation: Assessing Our Control of Risk*, reprinted in *TORT LAW AND THE PUBLIC INTEREST* 272, 274 tbl. 2 (Peter H. Schuck ed., 1991).

558. *Id.*

559. *Id.*

560. *Id.*

561. *Id.*

562. Blackmon & Zeckhauser, *supra* note 557, at 274 tbl.2.

methods of damages awards.⁵⁶³ Finally, four states discouraged plaintiffs' suits by imposing limitations on attorneys' ability to collect contingency fees.⁵⁶⁴

The states also looked at the insurance industry, concerned that they bore the brunt of the rising tides of tort litigation.⁵⁶⁵ In addition to controlling the tort litigation presumably causing higher insurance costs, the states began rigorously policing the insurance industry itself.⁵⁶⁶ Twelve states regulated insurance rates and insurance suppliers.⁵⁶⁷ Additionally, twelve states imposed limits on the insurance industry's ability to limit midterm policy cancellation.⁵⁶⁸ Ten states created insurance industry alternatives like self-insurance.⁵⁶⁹ Finally, five states limited the amount of damages that could be collected through collateral sources.⁵⁷⁰

This restrictive movement continued, and by 1988, forty-eight states participated in tort reform.⁵⁷¹ Twenty-three states limited the availability of extravagant damage awards by imposing caps on the amounts recoverable.⁵⁷² Thirty-six states passed measures limiting governmental liability.⁵⁷³ Thirty states hobbled the doctrine of joint and several liability.⁵⁷⁴ Twenty-five states made material alterations to their collateral source rule.⁵⁷⁵ Twenty states established legislation allowing defendants to make periodic damage payments to prevailing plaintiffs.⁵⁷⁶ Finally, twenty-five states attacked punitive damage awards by limiting either their availability or amount.⁵⁷⁷

With the onset of the '90s, concerns about overly abundant litigation incentives remained steady. For example, in 1990, Congress introduced the Civil Rights Act of 1991. Although the 1991 Act deceptively sounds as benevolent as its '60s counterparts, the 1964 and 1991 Civil Rights Acts are actually polar opposites. While 1964 Act sought to vindicate rights, the 1991 Act protected the perpetrators by imposing a \$150,000 cap on punitive

563. *Id.*

564. *Id.*

565. *Id.*

566. *Id.*

567. Blackmon & Zeckhauser, *supra* note 557, at 274 tbl.2.

568. *Id.*

569. *Id.*

570. *Id.*

571. Joseph Sanders & Craig Joyce, "Off to the Races": *The 1980s Tort Crisis and the Law Reform Process*, 27 HOUS. L. REV. 207, 220-22 (1990).

572. *Id.*

573. *Id.*

574. *Id.*

575. *Id.*

576. Sanders & Joyce, *supra* note 574, at 220-22.

577. *Id.*

damages to prevent what Congress perceived as a leviathan of overly inflated recovery awards.⁵⁷⁸ Notwithstanding the abundant testimony on the severe personal and economic tribulations Title VII plaintiffs endure in bringing actions, opponents to the implementation of compensatory and punitive damages argued that “strengthening Title VII’s existing remedial scheme would ‘open the floodgates’ to many frivolous lawsuits, [would] produce multi-million dollar awards, and [would] scuttle Title VII’s goal of encouraging voluntary settlement.”⁵⁷⁹ When the Act finally passed, Congress capped damages at different amounts based on the number of individuals employed by the discriminator.

Similarly, tort reform effected the passage of the ADA. Although the ADA provoked surprisingly little controversy in Congress, extensive debate did occur on the issue of whether Title I should permit compensatory and punitive damages and jury trials.⁵⁸⁰ House bill, H.R. 2273,⁵⁸¹ and Senate bill, S. 933,⁵⁸² were originally incorporated by reference the enforcement provisions of Title VII of the Civil Rights Act of 1964 and 42 U.S.C. § 1981. Thus, these referenced provisions permitted compensatory and punitive damages and jury trials⁵⁸³ in legal actions brought where “any individual . . . believes that he or she is being or about to be subjected to discrimination on the basis of disability.”⁵⁸⁴ Although the Senate passed S. 933 within four months,⁵⁸⁵ negotiations between the Bush Administration forced proponents of S. 933 to eliminate compensatory and punitive damages and jury trials prior to its passage.⁵⁸⁶ Unlike the Senate bill, the House bill proceeded slowly because four separate committees reviewed the bill.⁵⁸⁷ Also, the Bush

578. See 136 CONG. REC. H6810-13 (daily ed. Aug. 2, 1990). In 1991, sponsors elected to introduce a bill without a cap on damages. See Nicole L. Gueron, Note, *An Idea Whose Time Has Come: A Comparative Procedural History of the Civil Rights Acts of 1960, 1964, and 1991*, 104 YALE L.J. 1201, 1204 (1995).

579. H.R. REP. NO. 102-40, at 70 (1990), reprinted in 1991 U.S.C.C.A.N. 549, 608.

580. 1 HENRY H. PERRITT, JR., *AMERICANS WITH DISABILITIES ACT HANDBOOK* 19 (3d ed. 1997).

581. H.R. 2273, 101st Cong. (1989).

582. S. 933, 101st Cong. (1989).

583. See *Hearings Before the Comm. on Labor and Human Resources and the Subcomm. on the Handicapped*, supra note 514, at 3 (“[U]nder . . . [S. 933], relief for employment discrimination includes . . . compensatory and punitive damages, and the right to a jury trial available under § 1981”). See also *Johnson v. Ry. Express Agency*, 421 U.S. 454 (1975).

584. H.R. 2273, 101st Cong. (1989); S. 933, 101st Cong. (1989).

585. See 135 CONG. REC. 19,903 (1989) (passing by a vote of 76 yeas to 8 nays).

586. See H.R. REP. NO. 101-485(II), at 164, reprinted in 1990 U.S.C.C.A.N. 267, 441 (1990); 135 CONG. REC. 19,903 (1989).

587. See generally H.R. REP. NO. 101-485(I), at 1, reprinted in 1990 U.S.C.C.A.N. 267, 267 (1990) (Committee on Public Works and Transportation); H.R. REP. NO. 101-485(II), at 1, reprinted in 1990 U.S.C.C.A.N. 267, 303 (1990) (Committee on Education and Labor); H.R. REP. NO. 101-

Administration refused to support incorporation of future Title VII amendments resulting from pending civil rights legislation into the ADA because this scheme was not part of the original bargain struck with supporters of S. 933.⁵⁸⁸ Nevertheless, H.R. 2273 came to resemble S. 933 and incorporated Title VII remedies, as may be amended, into Title I of the ADA.⁵⁸⁹

In 1989, Congress again amended § 104(a)(2) to deny the exclusion for punitive damages in cases involving nonphysical personal injuries, thus making taxable any punitive damages awarded in discrimination or sexual harassment cases not involving a physical injury.⁵⁹⁰ In 1994, a resurgence of conservatism allowed Republicans to take control of the Senate and to solidify their House platform in a Contract with America. In the early months of the newly composed House and Senate, the Republican majority seized on Tenet Nine of the Contract with America⁵⁹¹ introducing a series of “Common Sense” tort reform acts which promised an overall reconstruction of tort law including caps on punitive damage awards, a revision of products liability law, and application of the English Rule of fee shifting.⁵⁹² While these bills

485(III), at I, *reprinted in* 1990 U.S.C.C.A.N. 267, 445 (1990) (Committee on the Judiciary); H.R. REP. NO. 101-485(IV), at 1, *reprinted in* 1990 U.S.C.C.A.N. 267, 512 (1990) (Committee on Energy and Commerce).

588. See PERRITT, *supra* note 580, at 23-24.

589. See H.R. REP. NO. 101-485, at 23 (1990), *reprinted in* 1990 U.S.C.C.A.N. 267, 445-46.

590. Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 7641(a), 103 Stat. 2106, 2379 (codified as amended at 26 U.S.C. § 104(a)(2) (1994)).

591. The Contract with America has been cited as the “centerpiece of the republican party’s strategy in the 1994 Congressional campaigns.” Carl Tobias, *Common Sense and Other Legal Reforms*, 48 VAND. L. REV. 699, 700 (1995). Tenet Nine or point nine of the Contract with America was the Common Sense Legal Reforms Act of 1995 (CSLRA), H.R. REP. NO. 104-50 (1995). Tenet Nine would have imposed numerous procedural and substantive tort reforms. See *id.* See also Elsa F. Kramer, *Tort Reform: Does it Make “Common Sense” for Indiana?*, RES GESTAE, Feb. 1995, at 8.

592. Common Sense Legal Reforms Act of 1995, H.R. 10, (1995); The Common Sense Legal Standards Reform Act of 1995, H.R. 956 (1995). The Common Sense Product Liability Reform Act of 1996 called for a cap on punitive damages to the extent of the greater of \$250,000 or double the amount of compensatory damages. This was approved by the Joint Conference Committee. H.R. CONF. REP. NO. 104-481, at 34-35 (1996). The House and the Senate had earlier passed different versions of this legislation, namely, the Common Sense Product Liability Act of 1995 and the Product Liability Fairness Act of 1995. See Thomas A. Eaton & Susette M. Talarico, *Testing Two Assumptions About Federalism and Tort Reform*, 14 YALE J. ON REG. 410 n.4 (1996). Subsequently, however, President Clinton vetoed H.R. 956 on May 2, 1996, thus putting an end for the time being to the various Common Sense Product Liability Reform Acts and Common Sense Legal Standards Reform Act of 1995. See *President’s Message on Returning Without Approval to the House of Representatives, The Common Sense Legal Reform Act of 1995*, 32 WEEKLY COMP. PRES. DOC. 780, 780-81 (May 6, 1996). See also John F. Harris, *Clinton Vetoes Product Liability Measure*, WASH. POST, May 3, 1996, at A14. Prior to the 1994 attempts at passing tort reform, Congress began to involve itself in tort reform by passing and attempting to pass products liability reform. To address “questionable insurer ratemaking and reserving practices” in products liability, Congress passed the Product Liability Risk Retention Acts of 1981 to permit product manufacturers to purchase insurance on a group basis at

were met with a general lack of enthusiasm and eventually failed, they spawned other acts that would ultimately succeed such as the Securities Litigation Reform Act of 1995,⁵⁹³ and charted a larger, more active path for the federal government in an area of law traditionally governed by state law.

Against this backdrop of developing congressional civil rights and tort reform legislation, courts had to determine whether § 104(a)(2) applied to monetary awards and settlements under the remedial provisions of these acts. Amidst this tension, the Supreme Court decided *Burke*⁵⁹⁴ and *Schleier* which virtually eliminated the exclusion for damages received in discrimination suits.⁵⁹⁵ Meanwhile, Congress attempted in 1989, 1995, and 1996 to limit the § 104(a)(2) exclusion to damages received on account of physical injury or physical sickness despite full knowledge of the severe psychological and emotional effects of discrimination.⁵⁹⁶

C. Tort Reform and a Taxing Statute

After almost eighty years of administrative, regulatory, and judicial pronouncements excluding nonphysical injury awards under § 104(a)(2), the final step in judicial and legislative “back-door” tort reform occurred in a taxing statute. In 1989, the first congressional attempt to limit the § 104(a)(2) exclusion to physical injury or physical sickness awards was predicated on the statement that “some courts have held that the exclusion applies to damages *in cases involving employment discrimination . . . where there is no physical injury or sickness.*”⁵⁹⁷ The Conferees made this statement even though the courts and the IRS consistently interpreted the exclusion to apply to awards on account of both physical and nonphysical injuries for the past seventy years.⁵⁹⁸ Although Congress did not limit the § 104(a)(2) exclusion to physical injury or physical sickness awards in 1989, it did pass

more favorable rates or to self-insure through insurance cooperatives. See Pub. L. No. 97-45, 95 Stat. 949, 949 (1981) (codified at 15 U.S.C. §§ 3901-05 (1994)).

593. Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (placing limitations upon the conduct of private actions being brought under the Securities Act of 1933 and the Securities Exchange Act of 1934). See also Robert L. Rabin, *Federalism and the Tort System*, 50 RUTGERS L. REV. 1, 1-3 (1997).

594. 504 U.S. 229 (1992).

595. 515 U.S. 323 (1995).

596. See *supra* Part II.L.

597. H.R. REP. NO. 101-247, at 1354-55 (1989), reprinted in 1989 U.S.C.C.A.N. 1906, 2824-25 (emphasis added).

598. See *Knuckles v. Comm’r*, 349 F.2d 610 (10th Cir. 1965); *Starrels v. Comm’r*, 304 F.2d 574 (9th Cir. 1962); *Agar v. Comm’r*, 290 F.2d 283 (2d Cir. 1961); *Raytheon Prod. Corp. v. Comm’r*, 144 F.2d 110 (1st Cir. 1994); *Cent. R.R. Co. v. Comm’r*, 79 F.2d 697 (3d Cir. 1935); *Farmers’ & Merchants’ Bank v. Comm’r*, 59 F.2d 912 (6th Cir. 1932).

amendments denying the income exclusion for punitive damages awards received for nonphysical personal injuries, thus taxing any punitive damages awarded in discrimination cases not involving a physical injury.⁵⁹⁹

Ironically, Congress considered the amendment to limit the tax exclusion to only physical injuries at the same time that it enacted the ADA.⁶⁰⁰ Additionally in 1990, congresspersons attempted to provide additional remedies for victims of discrimination.⁶⁰¹ The hearings preceeding the Civil Rights Act of 1991 established that the current, available protections and remedies completely failed to carry out the congressional goal to eradicate all forms of discrimination and make discrimination victims whole.⁶⁰² As a consequence, the 1991 amendments provided for compensatory and punitive damages and for jury trials.⁶⁰³ Nonetheless, the House WMC continued to believe that allowing an income tax exclusion for damages from discrimination “*is inappropriate where no physical injury or sickness is involved.*”⁶⁰⁴ Such inconsistent congressional policy is duplicitous behavior. On the one hand, Congress recognized the legal right to be protected from discrimination while, on the other hand, failed to recognize the injury of discrimination for tax purposes.

In 1995, Republicans once again attempted to pass a bill limiting the § 104(a)(2) exclusion to damage awards on account of physical injury or physical sickness.⁶⁰⁵ While the provision amending § 104(a)(2) passed both the House and Senate,⁶⁰⁶ a larger dispute over the budget resulted in a Presidential veto of the bill.⁶⁰⁷ In 1996 as part of the Small Business Job Protection Act, an almost identical bill passed both the House and the Senate and was signed by President Clinton.⁶⁰⁸

Both the 1995 and 1996 legislative histories reflect a clear misconception of the law. Both years, the Conferees vaguely refer to *Schleier* to support

599. Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 7641(a), 103 Stat. 2106, 2379 (codified as amended at 26 U.S.C. § 104(a)(2) (1994)).

600. Americans with Disabilities Act of 1990, Pub. L. No. 101-336, § 2(b), 104 Stat. 327, 329 (codified at 42 U.S.C. § 12101(b) (1994)).

601. S. 2104, 101st Cong. § 2(b)(2) (1990); H.R. 4000, 101st Cong. § 2(b)(2) (1990).

602. See H.R. REP. NO. 102-40, at 66-74 (1991), reprinted in 1991 U.S.C.C.A.N. 549, 604-12.

603. Civil Rights Act of 1991, Pub. L. No. 102-166, § 102, 105 Stat. 1071, 1072-74 (1991) (codified at 42 U.S.C. § 1981a (1994)).

604. H.R. REP. NO. 101-247, at 1354-55 (1989), reprinted in 1989 U.S.C.C.A.N. 1906, 2824-25 (emphasis added).

605. See H.R. REP. NO. 104-280, pt. 2, at 318-20 (1995).

606. See H.R. CONF. REP. NO. 104-737, at 300-01 (1996), reprinted in 1996 U.S.C.C.A.N. 1474, 1792-94.

607. See President Veto of Balanced Budget Act H.R. 2491, 31 WEEKLY COMP. PRES. DOC. 2140-42 (Dec. 6, 1995).

608. Pub. L. No. 104-188, § 1605, 110 Stat. 1755, 1838-39 (1996).

their position that § 104(a)(2) should be limited to awards for physical injury.⁶⁰⁹ The conference reports stated that the “[c]ourts have interpreted the exclusion from gross income of damages received on account of personal injury or sickness broadly in some cases to cover awards for personal injury that do not relate to a physical injury or sickness.”⁶¹⁰ In light of the Supreme Court’s opinions in *Burke* and *Schleier*, such error is particularly glaring.⁶¹¹

Specifically, *Burke* recognized that since the change from § 213(b)(6) to § 104(a)(2) in 1954, both the courts and the IRS have interpreted personal injuries to include “in accord with common judicial parlance and conceptions, . . . nonphysical injuries to the individual, such as those affecting emotions, reputation, or character, as well.”⁶¹² In addition, the Supreme Court stated that the 1989 congressional amendment to § 104(a)(2) supports such an interpretation because the elimination of the income exclusion for punitive damage awards for nonphysical injuries implies congressional acceptance of the fact that “other damages (i.e., compensatory) would be excluded in cases of both physical and nonphysical injury.”⁶¹³ The Court also noted that “Congress rejected a bill that would have limited the § 104(a)(2) exclusion to cases involving “physical injury or physical sickness.”⁶¹⁴ The *Schleier* opinion likewise acknowledged that regardless of the facial ambiguities in the text of § 104(a)(2), “it is by now clear that § 104(a)(2) encompasses recoveries based on intangible as well as tangible harms.”⁶¹⁵

According to the House Reports in 1995 and 1996, the House WMC’s limited the § 104(a)(2) tax exemption to personal physical injuries or sickness for three reasons: (1) damages received for nonphysical injury or sickness generally tends to compensate a claimant for lost profits or wages otherwise taxable as personal income”; (2) confusion about the tax treatment of damages received in nonphysical injury or sickness cases has led to “substantial litigation, including two Supreme Court cases within the last four years”; and (3) taxation of damages received on account of nonphysical injury or sickness “should not depend on the type of claim made.”⁶¹⁶ The first

609. H.R. CONF. REP. NO. 104-737, at 300-02 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1474, 1792-94.

610. *See* H.R. CONF. REP. NO. 104-737, at 300 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1474, 1792.

611. *United States v. Burke*, 504 U.S. 229, 235-36 n.6 (1992).

612. *Id.*

613. *Id.*

614. *Id.*

615. *Comm’r v. Schleier*, 515 U.S. 323, 329 n.4 (1995).

616. H.R. CONF. REP. NO. 104-737, at 300-01 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1474, 1792-94.

reason reveals a fundamental congressional misconception grounded in the personal and business dichotomy. The confusion relates to the distinction between the measurement and consequences of an injury and the nature and substance of the injury. No one would suggest that the damage award received by the surgeon for her lost finger, measured primarily upon proof of the consequent lost earning capacity, adequately offsets the loss of her finger. Equally absurd is a suggestion that a damage award for employment discrimination, based primarily upon evidence of lost wages, adequately compensates for the loss of a person's dignity. The fact that discrimination occurs within the employment or business context does not transform the nature of the injury and consequent damage award into that resembling income lost. Rather, the loss of income is a by-product of the reduced earning capacity suffered because of the discriminatory injury to human dignity. Both examples demonstrate inadequate attempts to monetarily compensate individuals for irreparable injury to the human person.

Congressional statements that "substantial litigation" has occurred 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.⁶¹⁷ Such statements indicate congressional fears of opening a floodgate of litigation and fraudulent pleading by taxpayers who wish to qualify their damages under § 104(a)(2). A potential flood of litigation is no justification for denying redress for injured rights. Moreover, courts had developed legal rules, such as the totality of the circumstances test in *Threlkeld*, to filter out fraudulent claims undeserving of the § 104(a)(2) exclusion. Interestingly, Congress may have been responding to the courts continuing struggle over whether a taxpayer was deserving of the § 104(a)(2) exclusion and therefore attempted to make a bright-line rule to eliminate or at least lessen the amount of § 104(a)(2) litigation in federal courts. Nevertheless, the elimination of "substantial litigation" over § 104(a)(2) issues does not justify the disparate effect a bright-line rule has on dignitary tort victims.

The decisions in *Wards Cove*, *Burke*, and *Schleier* also demonstrate back-door tort reform but, in the judicial context. These cases and the 1989 and 1996 amendments to § 104(a)(2) discourage plaintiffs from bringing discrimination claims in the federal courts. Especially in the case of a disparate impact claim, *Wards Cove* explicitly discourages plaintiffs from bringing actions absent a showing of discriminatory intent.⁶¹⁸ While the

617. H.R. REP. NO. 104-586, at 142-44 (1996), *reprinted in* 1996 U.S.C.C.A.N. (110 Stat.) 1755, 1838-39.

618. *See supra* notes 530-35 and accompanying text.

decision was couched in language of shifting burdens of proof and persuasion, this decision substantively closed the courthouse doors to most disparate impact plaintiffs.⁶¹⁹

Burke, *Schleier*, and the amendments to § 104(a)(2) economically discourage victims of discrimination or of sexual harassment from prosecuting claims to redress their injuries. Prior to the 1989 amendment, plaintiffs who were awarded damages for personal physical or nonphysical injuries could exclude back pay, compensatory damage awards, and punitive damages awards from income tax under § 104(a)(2). After the 1989 amendment, these same plaintiffs could only exclude back pay, compensatory damages and punitive damages received for physical injuries. Before *Burke*, Title VII plaintiffs could exclude back pay awards and compensatory damages from gross income⁶²⁰ and courts made no distinction between Title VII disparate treatment and disparate impact cases. After *Burke*, however, Title VII disparate treatment plaintiffs could exclude back pay and compensatory damages from income, but back pay awards in disparate impact claims were taxable under *Burke*'s tort or tort-type test, because the statutory relief for disparate impact plaintiffs did not authorize compensatory damages or punitive damages.⁶²¹ Because the ADA incorporated the remedial scheme of the 1991 amendments, Title VII plaintiffs who brought race, national origin, sex, religion, and disability discrimination claims against employers under disparate impact theory were taxed on back pay awards.⁶²² However, after *Burke*, ADEA plaintiffs who successfully prosecuted their discrimination claims, arguably, still had some chance of excluding their back pay and liquidated damage awards from taxation.⁶²³

In 1995, however, the Supreme Court decided *Schleier*, holding ADEA back pay and liquidated damages taxable.⁶²⁴ Arguably, after *Schleier* only

619. *See id.*

620. *See Burke v. United States*, 929 F.2d 1119, 1124 (6th Cir. 1991). *But see Sparrow v. Comm'r*, 949 F.2d 434, 437 (D.C. Cir. 1991) (holding Title VII damages taxable).

621. *See Rev. Rul. 93-88*, 1993-2 C.B. 61. Under the IRS's analysis of the *Burke* decision, because disparate impact plaintiffs were only provided back pay under 42 U.S.C. § 1981(a)(1), the ruling held that the same discrimination was not tort or tort-type. *See* 1993-2 C.B. 62-63. However, because disparate treatment plaintiffs were allowed compensatory and punitive damages under 42 U.S.C. § 1981(b)(3), the Service held under *Burke* that the awards were excludable because the same discrimination was a tort or tort-type right. *See* 1993-2 C.B. at 62-63. *See also United States v. Burke*, 504 U.S. 229, 242 (1992) (holding pre-1991 Title VII back pay in both disparate impact and disparate treatment cases taxable).

622. *See Rev. Rul. 93-88*, 1993-2 C.B. 61.

623. *See Schmitz v. Comm'r*, 34 F.3d 790, 796 (9th Cir. 1994). *But see Downey v. Comm'r*, 33 F.3d 836, 840 (7th Cir. 1994).

624. 515 U.S. 323, 336-37 (1995).

compensatory damages awarded in cases of intentional discrimination brought under Title VII remained potentially nontaxable under § 104(a)(2). Shortly thereafter, however, *Revenue Ruling 96-65* made back pay and emotional distress damages received for disparate treatment employment discrimination claims under Title VII taxable.⁶²⁵ Lastly, in 1996, Congress completely eliminated the exclusion for damages received for dignitary torts not involving physical injury or physical sickness by amending § 104(a)(2).⁶²⁶

D. Conclusion of Part IV

The major federal statutes serve as landmarks reflecting an expansive congressional policy to deter acts which violate a human's physical person, equality, dignity, and spirit. The resistance to this civil rights legislation and symbolic posture of the established social order is expressed in the context of § 104(a)(2). Lawmakers and the judiciary—as will be demonstrated in the Part V—creatively rationalized and legitimized their behavior by resolving conflicts that marginalized the rights of the powerless minorities and maintained a position of the privileged.⁶²⁷

V. DECONSTRUCTING THE INJUSTICE OF THE TAXATION OF “DIGNITARY” TORTS

Since 1922, the courts and the IRS have generally agreed that § 104(a)(2) excluded from income those damage awards received for physical and nonphysical personal injuries. However, in 1989 the courts and Congress began incrementally narrowing the applicable scope of § 104(a)(2).⁶²⁸ In narrowing the scope of § 104(a)(2), the Supreme Court in *Burke* sharply departed from § 104(a)(2) precedent in coming to its decision. Thereafter, the Supreme Court in *Schleier* built on the *Burke* analysis and twisted *Burke*'s

625. 1996-2 C.B. 6.

626. Pub. L. No. 104-88, § 1605, 110 Stat. 1755, 1838-39 (1996) (codified as amended at 26 U.S.C. § 104(a)(2) (Supp. II 1996)).

627. See *Plessy v. Ferguson*, 163 U.S. 537 (1896) (establishing the doctrine of separate but equal in upholding segregation in public schools). The federal government also has an inconsistent history in the area of gaining compliance with civil rights legislation. See ROOGERS & BULLOCK, *supra* note 472, at 195. Efforts by the federal government have been largely symbolic—recognizing injuries and providing for remedies that were rarely enforced. See *id.* The plans each federal agency puts forth do not reflect the agencies' actual compliance and have been referred to as merely “paper documents.” See U.S. COMMISSION ON CIVIL RIGHTS, FEDERAL TITLE VI ENFORCEMENT TO ENSURE NONDISCRIMINATION IN FEDERALLY ASSISTED PROGRAMS 99 (1996) (“[M]ost Federal agencies only are enforcing Title VI ‘on paper.’”).

628. For more information on the incremental narrowing of § 104(a)(2), see *infra* Part IV.

holding to come to its unique conclusion. The remedy driven reasoning developed by the Supreme Court in *Burke* and *Schleier* created an irrational and scientifically unsupported tort hierarchy which privileged certain plaintiffs recovering in tort with tax exclusion while denigrating discrimination victims as unworthy of the tax exclusion. *Burke* and *Schleier* then paved the way for the 1996 amendments to § 104(a)(2). The Conferees looked to the holding of *Schleier* to justify their position on and congressional amendment to § 104(a)(2), limiting its provision to exclude only damage awards on account of physical injury and physical sickness.⁶²⁹

A. *The Precedent*

The seventy-four years of precedent leading to *Burke* illustrates the extent to which the Supreme Court deviated from the original analysis of damages falling within the § 104(a)(2) exclusion. In the 1922 *Solicitor's Opinion 132*,⁶³⁰ which the BTA confirmed in the 1927 *Hawkins v. Commissioner* opinion,⁶³¹ damages for nonphysical personal injuries had consistently been determined to be excludable under § 104(a)(2).⁶³² Courts have since *Hawkins* properly recognized the excludability of monetary awards for both physical and nonphysical aspects of personal injuries.⁶³³ Personal injuries invariably result in both physical and nonphysical harm, regardless of the cause-and-effect sequence. Thus, any distinction is at best artificial and most likely sophistic.

The Ninth Circuit's 1983 decision in *Roemer v. Commissioner* reaffirmed that a court must analyze the nature of the claim and not the economic consequences of a personal injury.⁶³⁴ In examining the "nature of the tort" of defamation to determine whether the taxpayer claimed a personal injury, the court reviewed the historical development of the tort of defamation under the applicable state law of California.⁶³⁵ After reviewing the "unhappy tangle of illogical rules derived from [the] haphazard historical development of

629. For more information on how Congress misused *Schleier* to justify the § 104(a)(2) amendments, see *infra* Part IV.

630. I-1 C.B. 92, 94 (1922).

631. 6 B.T.A.M. (P-H) 1023, 1024-25 (1927).

632. See, e.g., *Threlkeld v. Comm'r*, 87 T.C. 1294, 1297 (1986).

633. See *Threlkeld v. Comm'r*, 87 T.C. 1294, 1297 (1986).

634. 716 F.2d 693 (9th Cir. 1983). In *Roemer*, the taxpayer and his wife appealed a Tax Court decision holding his damage award for defamation not excludable under § 104(a)(2). See *id.* at 695-96. The Ninth Circuit held the award excludable because defamatory statements attack an individual's good name. See *id.* at 700. The court recognized that nonpersonal consequences of a personal injury, such as loss of future income, may be the most persuasive means of proving the extent of the injury suffered, but the nature of an injury should not be defined by its effect. See *id.* at 699.

635. See *id.* at 697-700.

§ 104(a)(2),”⁶³⁶ the court excluded damages “from gross income to the extent a taxpayer can show that the damages, including amounts for lost income, were received for an injury to the individual’s personal reputation.”⁶³⁷ In essence, the court focused on whether the claim and injury that the damages redressed were personal. The court emphasized that under § 104(a)(2) courts should only distinguish “between personal and nonpersonal injuries, not between physical and nonphysical injuries [because] . . . § 104(a)(2) states that damages received on account of personal injuries are excludable; it says nothing about physical injuries.”⁶³⁸ The court further expressly rejected an argument that later became the focus of the *Burke* analysis:

[I]njury to the person should not be confused with the derivative consequences of the defamatory attack, i.e., the loss of reputation in the community and any resulting loss of income. The nonpersonal consequences of a personal injury, such as loss of future income, are often the most persuasive means of proving the extent of the injury that was suffered. The personal nature of an injury should not be defined by its effect.⁶³⁹

Finding that Roemer’s defamation award remedied a personal injury, the court held all damages excludable from gross income under § 104(a)(2).⁶⁴⁰ The Ninth Circuit methodologically focused on the statutory term “personal injury” to determine whether the taxpayer’s claim and injury were of a personal nature.

Building on *Roemer* in 1986, the Tax Court decided *Threlkeld v. Commissioner* by examining the nature of the taxpayer’s injury rather than the nature of the consequences flowing from that injury.⁶⁴¹ The court emphasized that determining whether the injury claimed is personal “more accurately reflects the inquiry required by the *plain meaning* of the

636. *Id.* at 698.

637. *Id.* at 696.

638. *Id.* at 697.

639. *Id.* at 699.

640. *See Roemer*, 716 F.2d at 700-01 (emphasis added). The court noted that punitive damages are usually includable as gross income. *See id.* at 700 (citing *Comm’r v. Glenshaw Glass Co.*, 348 U.S. 426 (1955)). Accordingly, the court reprimanded “the Commissioner [for his] liberal[] interpret[ation of] § 104(a)(2) to exclude punitive damages as well as all compensatory damages where there has been a personal injury.” *Id.* (citing Rev. Rul. 75-45, 1975-1 C.B. 47). Additionally, the court refused for § 104(a)(2) tax purposes to distinguish between damages awarded for injury to professional reputation and personal reputation. *See id.* at 698. Once it is determined that the nature of the claim redresses a personal injury, all damages are excludable under the statute.

641. 87 T.C. 1294, 1299 (1986). In *Threlkeld*, the petitioner received a settlement in a civil lawsuit for malicious prosecution. *Id.* at 1295. The court held that all of the petitioner’s damages were excludable because they flowed from the personal injury of malicious prosecution. *See id.* at 1307-08.

statute.”⁶⁴² Moreover, it defined personal injuries as “injuries resulting from invasions of rights that inhere in man as a rational being, that is, rights to which one is entitled by reason of being a person in the eyes of the law.”⁶⁴³ In discussing what constitutes a personal injury, the court stated that the concept has long included nonphysical as well as physical injuries.⁶⁴⁴

This reasoning went virtually unchallenged until 1992,⁶⁴⁵ when the D.C. Circuit decided *Sparrow v. Commissioner*.⁶⁴⁶ Clearly conflicting with the holdings of the Third,⁶⁴⁷ Fourth,⁶⁴⁸ Sixth,⁶⁴⁹ and Ninth Circuit Courts of

642. *Id.* at 1308 (emphasis added).

643. *Id.* at 1307 (analyzing personal injury with reference to *Brown v. Dunstan*, 409 S.W.2d 365, 367 (Tenn. 1966), and quoting *Commerce Oil Ref. Corp. v. Miner*, 199 A.2d 606, 610 (1964) (holding action for malicious abuse of process constituted “injuries to the person” under statute of limitations)).

644. *Id.* at 1297.

645. *See, e.g., Horton v. Comm’r*, 33 F.3d 625, 630 (6th Cir. 1994) (“At no point do we inquire into the nature of the damages involved. Rather the narrow scope of our gaze is properly limited to the ‘origin and character of the claim, . . . and not to the consequences that result from the injury.’”) (quoting *Threlkeld*, 87 T.C. at 1299 (1986)); *Burke v. United States*, 929 F.2d 1119, 1121 (6th Cir. 1990) (“To determine whether the injury complained of is personal, we must look to the origin and character of the claim . . . , and not to the consequences that result from the injury Thus, our inquiry is limited to whether injuries resulting from sex discrimination in violation of Title VII are ‘personal injuries.’”); *Pistillo v. Comm’r*, 912 F.2d 145, 148 (6th Cir. 1990) (“[r]elying substantially” on the Tax Court’s decision in *Threlkeld* and the Third Circuit decision in *Rickel*); *Rickel v. Comm’r*, 900 F.2d 655, 658 (3d Cir. 1990) (“The nonpersonal consequences of a personal injury, such as a loss of future income, are often the most persuasive means of proving the extent of the injury that was suffered. The personal nature of an injury should not be defined by its effect.”) (quoting *Roemer v. Comm’r*, 716 F.2d 693, 699 (9th Cir. 1973)); *Threlkeld v. Comm’r*, 848 F.2d 81, 84 (6th Cir. 1988) (agreeing with the Ninth Circuit decision in *Roemer* and the Third Circuit decision in *Bent* and holding that “the nonpersonal consequences of a personal injury, such as a loss of future income are often the most persuasive means of proving the extent of the injury that was suffered, and that the personal nature of an injury should not be defined by its effect”); *Bent v. Comm’r*, 835 F.2d 67, 70 (3d Cir. 1987) (“The nonpersonal consequences of a personal injury, such as a loss of future income, are often the most persuasive means of proving the extent of the injury that was suffered. The personal nature of an injury should not be defined by its effect.”) (quoting *Roemer v. Comm’r*, 716 F.2d 693, 699 (9th Cir. 1983)); *Thompson v. Comm’r*, 89 T.C. 632, 648 (1987) (“[W]e must look to the origin and character of the claim . . . and not to the consequences that result from the injury.”) (quoting *Threlkeld v. Comm’r*, 87 T.C. 1294, 1299 (1986)), *aff’d*, 866 F.2d 709 (4th Cir. 1989); *Metzger v. Comm’r*, 88 T.C. 834, 857 (1987) (“To determine whether the injury complained of is personal, we must look to the origin and character of the claim, and not to the consequences that result from the injury.”) (citing *Glynn v. Comm’r*, 76 T.C. 116, 121 (1981) (“[I]t should be evident that the consequences of a dispute are not necessarily commensurate with its origin.”)), *aff’d without opinion*, 845 F.2d 1013 (3d Cir. 1988); *Seay v. Comm’r*, 58 T.C. 32, 38 (1972).

646. 949 F.2d 434 (D.C. Cir. 1991). In *Sparrow*, the taxpayer argued that § 104(a)(2) excluded from income tax payments of Title VII settlements. *See id.* at 435. The Court of Appeals for the District of Columbia Circuit held that unlike common law personal injury damages, Title VII provides only equitable remedies such as back pay and gives the plaintiff no right to a jury trial. *See id.* at 437-38. Therefore, the damages were taxable under § 104(a)(2). *See id.* at 438.

647. *See Rickel v. Comm’r*, 900 F.2d 655, 657-64 (3d Cir. 1990); *Bent v. Comm’r*, 835 F.2d 67, 70 (3d Cir. 1987).

648. *See Thompson v. Comm’r*, 866 F.2d 709, 712 (4th Cir. 1989) (excluding liquidated damages but including back pay in gross income).

Appeals⁶⁵⁰ that excluded damages for age discrimination under § 104(a)(2), the D.C. Circuit found Title VII back pay taxable, holding that the language excluding from gross income “any damages received . . . on account of personal injuries”⁶⁵¹ under § 104(a)(2) creates a two part conjunctive test for the taxpayer. The court declared that in order to exclude damages under § 104(a)(2), “the amount received must be damages” and “the amount received as damages must result from personal injury or sickness.”⁶⁵²

The court first defined the meaning of “damages” under § 104(a)(2) to have the same meaning as “damages” under the original 1918 codification of § 213(b)(6).⁶⁵³ Even though the Revenue Act of 1918 and its legislative history failed to define “damages” under § 213(b)(6), because damages were a legal remedy in 1918, the court concluded that § 104(a)(2) “damages” today must comply with the historical definition and conception of the term as a monetary sum awarded at law.⁶⁵⁴ According to *Sparrow*, personal civil violations involving discriminatory acts must provide for nonequitable remedies other than back pay or injunctions in order to fall within the historical definition of damages under § 104(a)(2).⁶⁵⁵ Having deconstructed the term damages to a narrow historical definition, the court made a hegemonic analysis of the remedial provisions of pre-1991 Title VII.⁶⁵⁶ Equating pre-1991 Title VII back pay remedy to the equitable remedy of restitution, the court held that the Title VII award fell outside the historical definition of legal damages.⁶⁵⁷

The court’s “clear”⁶⁵⁸ conclusion that damages under § 104(a)(2) must fit within its historical definition ignores the fact that actions for sex discrimination did not exist until the latter half of the twentieth century.⁶⁵⁹ The court’s holding that damages excluded under § 104(a)(2) are confined to a monetary sum awarded at law, and that back pay under Title VII did not fall within the court’s narrow definition of damages, lacks any policy analysis or justification.⁶⁶⁰ In fact, given the strong congressional and social

649. See *Pistillo v. Comm’r*, 912 F.2d 145, 149-50 (6th Cir. 1990); *Burke v. Comm’r*, 929 F.2d 1119, 1121-22 (6th Cir. 1991).

650. See *Redfield v. Ins. Co. of N. Am.*, 940 F.2d 542, 547 (9th Cir. 1991).

651. *Sparrow*, 949 F.2d at 436.

652. *Id.*

653. See *id.* at 436-37.

654. See *id.* at 436-38.

655. *Id.* at 437.

656. See *id.* at 437.

657. See *Sparrow*, 949 F.2d at 438.

658. *Id.* at 437.

659. See Ronald K.L. Collins, *Language, History and the Legal Process: A Profile of the “Reasonable Man”*, 8 RUTGERS-CAM. L.J. 311, 317-18 (1977).

660. The D.C. Circuit repeatedly cited to *Curtis v. Loether*, 415 U.S. 189 (1974), and *Albemarle*

policy in favor of eradicating discrimination in all forms, a broad reading of damages is preferable.⁶⁶¹ The *Sparrow* court marginalized sexual discrimination claims, constricted legislative prerogatives in formulating remedies for personal civil wrongs, and denigrated victims a second time through tax law.

The *Sparrow* court further stated that because Congress designed Title VII to place the victim of employment discrimination in exactly the same position he would have been in absent the discrimination, excluding back pay from income would violate the purpose of the statute by giving the victim of discrimination a tax benefit not received by other co-workers not subject to similar discrimination and success in the court system.⁶⁶² In short, such tax benefit would place the victim in a better position—not an equal position—

Paper Co. v. Moody, 422 U.S. 405 (1975), to support its holding that Title VII back pay damages were not legal damages awarded at law. *Sparrow*, 949 F.2d at 437-40. In *Curtis*, the Supreme Court held that Title VIII provided for the enforcement of legal rights and remedies in an action at law and therefore, either party to the action was entitled to a jury trial under the Seventh Amendment. *Curtis*, 415 U.S. at 195. In fact, the Court reasoned that “[t]he statute sounds basically in tort . . . [and] merely defines a new legal duty . . . authoriz[ing] the courts to compensate a plaintiff for the injury caused by the defendant’s wrongful breach.” *Id.* at 195 (emphasis added). Furthermore, the court indicated skepticism concerning the characterization of back pay damages as an equitable remedy. *See id.* at 197 (citing Comment, *The Seventh Amendment and Civil Rights Statutes: History Adrift in a Maelstrom*, 68 Nw. U. L. REV. 503, 524-27 (1973) (“Whatever may be the merit of the ‘equitable’ characterization in Title VII cases, there is surely no basis for characterizing the award of compensatory and punitive damages here as equitable relief.”)).

Moreover, in *Albemarle Paper Co.*, Justice Rehnquist characterized the Title VII remedy in a concurring opinion:

To the extent that an award of back pay is thought to flow as a matter of course from a finding of wrongdoing, and thereby becomes virtually indistinguishable from an award for damages, the question (not raised by any of the parties, and therefore quite properly not discussed in the Court’s opinion), of whether either side may demand a jury trial under the Seventh Amendment becomes critical.

422 U.S. 405, 442 (1975) (Rehnquist, J., concurring) (emphasis added).

661. The court acknowledges the purpose of Title VII by quoting from *Albemarle Paper Co.*, which identified Title VII’s central statutory purposes to “eradicat[e] discrimination throughout the economy and mak[e] persons whole for injuries suffered through past discrimination.” *Sparrow*, 949 F.2d at 440 (quoting *Albemarle Paper Co.*, 422 U.S. at 421). The court also found relevant Senator Williams’ statement in the congressional record that Congress intended the back pay provisions in the Equal Employment Opportunity Act, currently codified at 42 U.S.C. § 2000e-5(g):

to give the courts wide discretion exercising their equitable powers to fashion the most complete relief possible. In dealing with the present section 706(g) the courts have stressed that the scope of relief under that section of the Act is intended to make the victims of unlawful discrimination whole, and that the attainment of this objective rests not only upon the elimination of the particular unlawful employment practice complained of [through cease and desist orders], but also requires that persons aggrieved by the consequences and effects of the unlawful employment practice be, so far as possible, restored to a position where they would have been were it not for the unlawful discrimination.

Id. at 440-41 (quoting 118 Cong. Rec. 7168 (1972)) (emphasis added).

662. *Sparrow*, 949 F.2d at 441 (stating that a tax benefit would “place[e] him in a better position than had he not allegedly been discriminated against”).

than where the Title VII plaintiff would have been absent the “alleged” discrimination.⁶⁶³ While the court recognized that “such a result might seem fair” under the circumstances, the court ultimately reasoned that such preferable tax treatment “would be contrary to congressional intent as evidenced by the explicit provisions of Title VII.”⁶⁶⁴

This argument assumes that after being the involuntary victim of insidious racial or sexual discrimination in the workplace and losing career employment, mere payment of lost incremental back wages places the victim in the same position as if the discrimination had not occurred. The effects of discrimination are psychological, physical, social, and economic, as well as severe and permanent. The court’s use of the word “*allegedly*”⁶⁶⁵ in relation to the taxpayer’s discrimination claim denigrates the seriousness of personal injuries suffered by victims of discrimination. Finally, the court’s comment that a tax exclusion would give the taxpayer more than Title VII authorizes and place him in a “*better position*”⁶⁶⁶ than other taxpayers similarly situated but not victims of discrimination is not legally or scientifically supportable. The suggestion that money alone sufficiently redresses racial discrimination and that providing compensatory back pay tax free to a victim of discrimination will place the *victim* in a better position than he would have been absent the discrimination is troubling.

B. The Deviation

Because of a conflict in the courts of appeals with regard to the taxation of Title VII damages, the Supreme Court in 1992 granted certiorari and interpreted § 104(a)(2) for the first time in *United States v. Burke*.⁶⁶⁷

In *Burke*,⁶⁶⁸ the Supreme Court examined a Title VII disparate impact sex discrimination claim and held that the taxpayer’s settlement award did not fall within the § 104(a)(2) statutory exclusion.⁶⁶⁹ First, the Court observed that neither the “text” nor the “legislative history” provided an explanation of

663. *Id.*

664. *Id.*

665. For the direct quote, see *infra* note 630.

666. *Sparrow*, 949 F.2d at 441.

667. *United States v. Burke*, 504 U.S. 229, 229 (1992).

668. 504 U.S. 229 (1992).

669. *See id.* at 230-31, 242. Evidence deduced through early discovery led the district court in denying defendant Tennessee Valley Authority’s motion for summary judgment to find that the factual evidence established a *prima facie* case of disparate treatment. Thereafter serious negotiations culminated in the settlement of five million dollars. *See* Brief for Respondent at 4, *United States v. Burke*, 504 U.S. 229 (1992) (No. 91-42).

the term “personal injuries.”⁶⁷⁰ Next, the Court selectively reiterated part of the 1960 regulation § 1.104-1(c), entitled “Damages received on account of personal injuries or sickness” which defines “damages received” and provides guidance on what constitutes “personal injuries or sickness.”⁶⁷¹ The Treasury Regulation defined “damages received” for “personal injuries or sickness” as an amount received from the prosecution of a legal suit upon a *tort or tort-type right*; the latter phrase is only illustrative while the former circumscribed.⁶⁷² Thus, in excluding damages redressing tort or tort-type rights, the regulation does not purport to comprehensively describe the term personal injury. Consequently, monetary awards from personal injury violations of tort-type rights are deductible as are legal actions based upon tort violations.

The Supreme Court also recognized that “tort” had been broadly defined as a “civil wrong, other than breach of contract,” that provides damages to redress the “violation of . . . legal rights.”⁶⁷³ At this juncture the Court could have soundly concluded that discrimination is properly classified as a civil personal injury and not as a contractual wrong by reasoning that (1) Title VII provides a cause of action redressing the violation of a “new legal duty” providing for monetary damages measured by back pay, (2) discrimination is “an invidious practice that causes grave harm to its victims,”⁶⁷⁴ (3) there is “[n]o doubt [that] discrimination . . . constitute[s] a ‘personal injury’ for purposes of § 104(a)(2) and (4) ‘under the logic of the common law

670. *Id.* at 234.

671. Treas. Reg. § 1.104-1(c) (1991). This treasury regulation states in full as follows:

Damages received on account of personal injuries or sickness. Section 104(a)(2) excludes from gross income the amount of any damages received (whether by suit or agreement) on account of personal injuries or sickness. The term “damages received (whether by suit or agreement)” means an amount received (other than workmen’s compensation) through prosecution of a legal suit or action based upon tort or tort type rights, or through a settlement agreement entered into in lieu of such prosecution.

Id.

672. *Id.*

673. 504 U.S. at 234-35 (quoting PROSSER & KEETON ON THE LAW OF TORTS, § 54, at 360 (5th ed. 1984)). Similar to Title VII, the Supreme Court in *Curtis v. Loether*, reasoned that “a damages action under . . . Title VIII is analogous to a number of tort actions recognized at common law [because] the statute merely defines a new legal duty, and authorizes the courts to compensate a plaintiff for the injury caused by the defendant’s wrongful breach.” 415 U.S. 189, 195 (1974). In addition, the Court commented that the lower court analogized Title VIII to the common-law duty of innkeepers not to refuse lodging without justification. *See id.* at 195-96 n.10. Then the Supreme Court stated that a suit to remedy racial discrimination was similar to actions for intentional infliction of mental distress and defamation. *See id.* (“Indeed, the contours of the latter tort are still developing, and it has been suggested that ‘under the logic of the common law development of the law of insult and indignity, racial discrimination might be treated as a dignitary tort.’”) (quoting C. GREGORY & H. KALVEN, CASES AND MATERIALS ON TORTS 961 (2d ed. 1969)).

674. *United States v. Burke*, 504 U.S. 229, 238 (1992).

development of the law of insult and indignity, racial discrimination . . . [is] treated as a dignitary tort.”⁶⁷⁵ Rather, the Court acknowledged the “nature of the claim,”⁶⁷⁶ but engaged in the most cursory analysis possible to enthrone a hegemonic remedy ratiocination as controlling the § 104(a)(2) exclusion.

The Court established that the appropriate test for applying the § 104(a)(2) income exclusion is whether the taxpayer can “show that Title VII, [as] the legal basis for their recovery of back pay, redresses a tort-like personal injury in accord with the foregoing principles.”⁶⁷⁷ First, the Court noted that a Title VII plaintiff, unlike other tort-like personal injury plaintiffs, is not entitled to a jury trial.⁶⁷⁸ As a practical matter this fact offers little insight into the nature of a racial discrimination claim and whether such injury, if proven, constitutes a personal injury. In fact, the absence of jury trials from Title VII may have reflected a legislative concern that the jury system could be used to undermine rather than promote the goals of Title VII.⁶⁷⁹ Second, after recognizing in passing that “[i]t is beyond question that discrimination in employment on the basis of sex, race, or any of the other classifications protected by Title VII is . . . an invidious practice that causes grave harm to its victims[,]” the Court stated that the existence of individual harm “does not automatically imply . . . a tort-like ‘personal injury’ for purposes of federal income tax law.”⁶⁸⁰ This statement therefore requires that a taxpayer must suffer a personal injury and, in addition, that personal injury must be tort-like for the purposes of federal income tax law.

Arguably, no basis for such a condition exists under the plain meaning of § 104(a)(2) itself. The history of the words “tort or tort-type” arise in regulation § 1.104-1(c) directly relating to the definition of damages, not personal injury.⁶⁸¹ Once the Court constructed this new analytical framework

675. *Id.* at 239-40.

676. *Id.* at 237.

677. *Id.*

678. *See id.* at 238 (“Title VII plaintiffs, unlike ordinary tort plaintiffs, are not entitled to a jury trial.”).

679. In discussing the legislative history on the jury trial issue concerning Title VIII, the Supreme Court observed that “[t]he legislative history on the jury trial question is sparse, and what little is available is ambiguous.” *See, e.g., Curtis v. Loether*, 415 U.S. 189, 191 (1974); MISCELLANEOUS PROPOSALS REGARDING THE CIVIL RIGHTS OF PERSONS WITHIN THE JURISDICTION OF THE UNITED STATES: HEARING BEFORE SUBCOMM. NO. 5 OF THE HOUSE COMM. ON THE JUDICIARY, 89th Cong., at 1183 (1966).

680. *Burke*, 504 U.S. at 238 (citations omitted). Other courts applied a different approach focusing on the origin and nature of the claim and the legally protected rights being violated. *See Roemer v. Comm’r*, 716 F.2d 693, 697 (“[W]e must look to the nature of the tort of defamation to determine whether the award should have been reported as gross income.”); *Threlkeld v. Comm’r*, 87 T.C. 1294, 1307 (1986) (citations omitted) (quoting the Tennessee Supreme Court stating that the exclusion applied to invasions of rights that one possess by virtue of being a person under the law).

681. This inclination of the Court to “graft” onto Section 104(a)(2) new prerequisites for

and statutory hurdle for evaluating damages received to compensate a successful plaintiff's discrimination claim, the back pay award predictably failed to qualify for excludability.⁶⁸² The Court continued to reason that because back pay solely remedied racial discrimination under Title VII,⁶⁸³ unlike other common law torts' remedial schemes, the legal right protected by Title VII was not a "tort-like personal injury"⁶⁸⁴ excludable under § 104(a)(2).⁶⁸⁵

The Supreme Court constructed a contextually indefensible method of interpretation that denied a tax exclusion to the successful plaintiff in any disparate impact Title VII discrimination suit.⁶⁸⁶ The Court's remedy driven analysis defined the nature of the claimed injury by reference to the range of remedies afforded to the Title VII plaintiff.⁶⁸⁷ Using a legislatively created statutory remedy to characterize the nature of a claim, instead of examining the nature of the claim itself by looking at the legal right protected and resulting injury, the Court denigrated and marginalized discrimination claims. Indeed, the Court recognized discrimination as being a cognizable personal injury.⁶⁸⁸ Congress intended Title VII actions to eradicate discrimination by employers against individuals in vulnerable minority groups.⁶⁸⁹ Therefore, the Court could have as easily reasoned when an

excludability occurred again in *Commissioner v. Schleier*, 515 U.S. 323, 346 (1995).

682. *Burke*, 504 U.S. at 237-42.

683. *See id.* at 238.

684. *Id.* at 241.

685. *See id.* at 242.

686. While the court's decision was handed down on May 26, 1992, after the enactment of the Civil Rights Act of 1991, Pub. L. No. 102-166, 105 Stat. 1071, the Court stated that it was "examin[ing] the law as it existed prior to November 21, 1991, the effective date of the 1991 Act [and that u]nless otherwise indicated, all references are to the 'unamended' Title VII." 504 U.S. 229, 237 n.8 (1992). Interestingly, the amendments under the Civil Rights Act of 1991 provided victims of intentional discrimination with compensatory damages for future pecuniary losses, emotional pain and suffering, mental anguish, loss of enjoyment of life, punitive damages, other nonpecuniary losses, and the right to a jury trial. *See* Civil Rights Act of 1991, Pub. L. No. 102-166, § 102(b)-(c), 105 Stat. 1071, 1073. In responding to the taxpayer's argument that the 1991 amendments evidenced congressional intent that Title VII's remedial scheme was tort-like in nature, the Court stated that it "believe[d] that Congress's decision to permit jury trials and compensatory and punitive damages under the amended Act . . . mark[s a] change in its conception of the injury redressable by Title VII, and cannot be imported back into analysis of the statute as it existed at the time of this lawsuit." *Burke*, 504 U.S. at 241 n.12.

687. *Burke*, 504 U.S. at 234-35, 237-41.

688. In *Burke*, the Court labeled discrimination as an "invidious practice" doing "grave harm" to its "victims." *Id.* at 238. The Court was willing to acknowledge the extent of the injury and the personal nature of the injury but once again utilized the remedial scheme to subvert it in favor of other common-law torts.

689. In *Burke*, the Court did recognize that Title VII of the Civil Rights Act of 1964 "makes it an unlawful employment practice for an employer 'to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual's race,

employer discriminates in employment and consequently injures an individual, Congress selected back pay as the measure to make the aggrieved personal injury victim whole and thus, did not intend the nature of back pay to be determinative of the underlying claim or injury suffered.⁶⁹⁰

The Supreme Court clearly had alternatives available to it that would not have resulted in marginalizing discrimination claims. The Court's approach, however, erected hurdles for a class of discrimination plaintiffs where none had previously existed. Furthermore, it placed victims of discrimination in an insular subordinate class requiring them to pay tax on their claims while other personal injury claimants enjoyed a favorable tax exclusion.

Any hope for a course correction quickly dissipated three years later. After the Supreme Court decision in *Burke*, another conflict arose, this time among the Fifth, Seventh, and Ninth Circuit courts.⁶⁹¹ These cases involved the exclusion of back pay and liquidated damages received in a successful age discrimination claim under the ADEA by United Airlines (United) employees.⁶⁹² Addressing the conflict, the Supreme Court in *Commissioner v. Schleier*, further contorted the unsupportable analytical framework of *Burke* in its holding that a settlement award based upon an ADEA discrimination claim was also not excludable from income tax under § 104(a)(2).⁶⁹³

The Court began its analysis by purporting to apply the "plain language of § 104(a)(2),"⁶⁹⁴ its implementing regulation,⁶⁹⁵ and the Court's "reasoning in *Burke*."⁶⁹⁶ The Court then concluded that these three factors "convince us that a recovery under the ADEA is not excludable from gross income."⁶⁹⁷

color, religion, sex, or national origin." *Id.* at 237-38.

690. Lower courts have repeatedly recognized that the nature of the injury, not the effect of the injury, best defines the tort. *See, e.g.,* *Roemer v. Comm'r*, 716 F.2d 693, 699 (9th Cir. 1983); *Threlkeld v. Comm'r*, 87 T.C. 1294, 1299 (1986).

691. *See* *Downey v. Comm'r*, 33 F.3d 826 (7th Cir. 1994); *Schmitz v. Comm'r*, 34 F.3d 790 (9th Cir. 1994); *Schleier v. Comm'r*, 26 F.3d 1119 (5th Cir. 1994).

692. *Schleier v. Comm'r*, 515 U.S. 323, 325 (1995). The ADEA provides for back pay to redress all successful claims as well as for liquidated damages in willful violation cases. *Monroe v. United Airlines, Inc.*, 736 F.2d 394, 397-98 (7th Cir. 1984).

693. *See id.* at 336-37. In this case, the jury found United's violations willful. *Id.* at 326 (noting the case was tried before a jury and the jury held for the plaintiffs, but the case was reversed by the Seventh Circuit on appeal).

694. *Schleier*, 515 U.S. at 327. The plain meaning approach to statutory interpretation is grounded in the principle that the provision being interpreted is unambiguous. *See* Mary L. Heen, *Plain Meaning, the Tax Code, and Doctrinal Incoherence*, 48 HASTINGS L.J. 771, 774 (1997).

695. *See Schleier*, 515 U.S. at 327 (referring to Treas. Reg. § 1.104-1(c)).

696. *Id.* This begs the question: if the Court in *Burke* applied the plain language of the statute, then why is its decision acknowledged as nonexhaustive? At least at some unconscious level, the Court may be recognizing the extent that *Burke* departed from plain language requirements of § 104(a)(2).

697. *Id.*

The Court found that Treasury Regulation § 1.104-1(c), requiring that damages be received in a tort type action, does not substitute for § 104(a)(2)'s requirement that the damage award be received "on account of personal injuries or sickness."⁶⁹⁸ Rather, Treasury Regulation § 1.104-1(c) is an added requirement.⁶⁹⁹ "The statutory requirement is only repeated in the regulation."⁷⁰⁰ To address whether ADEA damages are received in a tort-type like action, the Court noted that in *Burke* it emphasized that Title VII did not provide for jury trials and compensatory and punitive damages like other tort or tort-type rights.⁷⁰¹ Here, the petitioner argued that, unlike the Title VII plaintiff in *Burke*, the ADEA provides plaintiffs with jury trials and liquidated damages.⁷⁰² The *Scheier* Court retreated from that emphasis in *Burke* stating: "We did not, however, indicate that the presence of either or both of those factors would be sufficient to bring a statutory claim within the coverage of the regulation."⁷⁰³

The Court also conducted an analysis of whether awards and liquidated damages are excludable under the "plain language" of the damage award.⁷⁰⁴ The Court found that under its previous decision in *Trans World Airlines v. Thurston*, "Congress intended for liquidated damages to be punitive in nature" under the ADEA.⁷⁰⁵ Even though Congress modeled parts of the ADEA on FLSA, which the Court had earlier interpreted in *Overnight Motor Transportation Co. v. Missel* "might provide [liquidated damages as] compensation for some 'obscure' injuries," the Court stated that the ADEA's liquidated damages provisions significantly departed from FLSA in that respect.⁷⁰⁶ The Court held ADEA damages punitive and thus not received

698. *Scheier*, 515 U.S. at 333.

699. *Id.*

700. *Id.*

701. *Id.* at 334-35.

702. *See id.* at 335.

703. *Id.*

704. *Scheier*, 515 U.S. at 329.

705. *Id.* at 332 (quoting *Trans World Airlines, Inc. v. Thurston*, 469 U.S. 111, 125 (1985)).

706. *Id.* at 331 (citing *Overnight Motor Trans. Co. v. Missel*, 316 U.S. 572 (1942) and *Thurston*, 469 U.S. at 126). In *Thurston*, the Court addressed the definition of the term "willful violation" as required to receive the liquidated damages under section 7(b) of the ADEA, 29 U.S.C. § 626(b). *Id.* at 125. The Supreme Court noted that § 7(b) of the ADEA provides that those remedies should be enforced in accordance with FLSA. *See id.* The Court noted, however, that unlike FLSA, liquidated damages were only allowed in cases of willful violations. *Id.* The Court held that this provision made the ADEA plaintiff's damages punitive in nature. *Id.*

The legislative history of the ADEA indicates that Congress intended for liquidated damages to be punitive in nature. The original bill proposed by the administration incorporated § 16(a) of the FLSA, which imposes criminal liability for a willful violation. See 113 Cong. Rec. 2199 (1967). Senator Javits found "certain serious defects" in the administration bill. He stated that "difficult problems of proof . . . would arise under a criminal provision," and that the employer's invocation

“on account of personal injury or sickness.”⁷⁰⁷

Legislative history for the ADEA’s 1978 Amendments, however, supports a very different interpretation of the ADEA’s liquidated damage provision.⁷⁰⁸ Because liquidated damages are legal relief, a party is entitled to have the factual issues underlying such a claim decided by a jury.⁷⁰⁹ Further, the ADEA as amended, does not provide remedies of a punitive nature.⁷¹⁰ The Conferees therefore agreed to permit a jury trial of the factual issues underlying a claim for liquidated damages because the Supreme Court made clear that a liquidated damage award under FLSA is not a penalty but rather is available in order to provide full compensatory relief for losses that are “too obscure and difficult of proof for estimate other than by liquidated damages.”⁷¹¹ An even more reasonable point of view is that without the personal injury of discrimination, there would be no damage award for back pay or liquidated damages *on account of personal injury*.⁷¹²

Another unusual departure from precedent by the Court was its observation that “[r]espondent seeks to circumvent the plain language of § 104(a)(2) by relying on the Commissioner’s regulation interpreting that section,”⁷¹³ when in fact taxpayers, the Commissioner, and courts had referred to regulation § 1.104-1(c) for nearly four decades.⁷¹⁴ Courts normally give deference to longstanding regulations that have been relied upon for such an extended period of time.⁷¹⁵ The Court went on to note that

of the Fifth Amendment might impede investigation, conciliation, and enforcement *Id.* [sic] at 7076. Therefore, he proposed that “the [FLSA’s] criminal penalty in cases of willful violation . . . [be] eliminated and a double damage liability substituted.” *Ibid.* Senator Javits argued that his proposed amendment would “furnish an effective deterrent to willful violations [of the ADEA],” *ibid.*, and it was incorporated into the ADEA with only minor modification, S. 788, 90th Cong., 1st Sess. (1967).

Id. at 125-26. The opinion went on to note that “[t]he record makes clear that TWA officials acted reasonably and in good faith in attempting to determine whether their plan would violate the ADEA.” *Id.* at 129.

707. *Schleier*, 515 U.S. at 332.

708. See H.R. CONF. REP. NO. 95-950 (1978).

709. Age Discrimination and Employment Act Amendments of 1978, Pub. L. No. 95-256, 92 Stat. 189 (codified as amended at 29 U.S.C. § 626(c) (1994)).

710. See *id.*

711. H.R. CONF. REP. NO. 95-950, at 7, 14 (1978), reprinted in 1978 U.S.C.C.A.N 504, 528, 535 (quoting *Overnight Motor Trans. Co.*, 316 U.S. at 583-84).

712. Compare *Schleier*, 515 U.S. at 330 (“In age discrimination, the discrimination causes both personal injury and loss of wages, but neither is linked to the other. The amount of back wages recovered is completely independent of the existence or extent of any personal injury.”).

713. *Id.* at 333.

714. *United States v. Burke*, 504 U.S. 229, 234 (1992) (stating that “[s]ince 1960 . . . IRS regulations formally have linked identification of a personal injury for purposes of a § 104(a)(2) to traditional tort principles”).

715. *United States v. Correll*, 389 U.S. 299, 305-06 (1967).

“[w]e have long recognized that considerable weight should be accorded to an executive department’s construction of a statutory scheme it is entrusted to administer, and the principle of deference to administrative interpretations.”⁷¹⁶ Furthermore, *Chevron, U.S.A. Inc v. Natural Resources Defense Council*⁷¹⁷ held that where Congress has not explicitly spoken on the precise issue the administrative agency regulation should be followed if it is a permissible interpretation.⁷¹⁸ The Court did not even attempt to address or distinguish *Chevron*, it rather reconstructs the statute and “graft[s] on. . . [an] additional requirement.”⁷¹⁹

The *Schleier* Court, referencing its decision in *Burke*, again applied its remedy analysis to characterize an ADEA discrimination claim award as distinguishable from a damage recovery “on account of” personal injury.⁷²⁰ The effect of the Supreme Court’s strained construction of the “plain language” of the statute indirectly stigmatized and isolated victims of discrimination and privileged all other individuals receiving damages “on account of” personal injury.

The *Burke-Schleier* analysis also assumes that Title VII’s and ADEA’s remedial schemes fairly restitute all the rights, claims, and injuries at stake, even given the fact that courts have been traditionally unable to determine the nature of “liquidated damages,” let alone what right such remedy necessarily implicates.⁷²¹ Nevertheless, the Court once again pushed a nonphysical personal civil injury claim beyond the borders of the § 104(a)(2) exclusion.

O’Connor’s dissent confronts the incongruity of *Schleier* with the Court’s former opinion in *Burke*.⁷²² Justice O’Connor reminded her colleagues that eight Justices in *Burke* conceded that discrimination inflicts a personal injury under § 104(a)(2).⁷²³ O’Connor charged that the majority has created a per se rule that discharge based upon discrimination cannot be fairly described as a

716. *Chevron, U.S.A. Inc. v. Natural Res. Def. Council*, 467 U.S. 837, 844 (1984) (citing *Aluminum Co. of Am. v. Cent. Lincoln Peoples’ Util. Dist.*, 467 U.S. 380, 389 (1984); *Blum v. Bacon*, 457 U.S. 132, 141 (1982); *Union Elec. Co. v. EPA*, 427 U.S. 246, 256 (1976); *Inv. Co. Inst. v. Camp*, 401 U.S. 617, 626-27 (1971); *Unemployment Comp. Comm’n v. Aragon*, 329 U.S. 143, 153-54 (1946); *NLRB v. Hearst Publ’n, Inc.*, 322 U.S. 111, 131 (1944); *McLaren v. Fleischer*, 256 U.S. 477, 480-81 (1921); *Webster v. Luther*, 163 U.S. 331, 342 (1896); *Brown v. United States*, 113 U.S. 568, 570-71 (1885); *United States v. Moore*, 95 U.S. 760, 763 (1878); *Edwards’ Lessee v. Darby*, 25 U.S. (12 Wheat.) 206, 210 (1827)).

717. 467 U.S. 837 (1984).

718. *See id.* at 866.

719. *Schleier v. Comm’r*, 515 U.S. 323, 346 (1995) (O’Connor, J., dissenting).

720. *See id.* at 334-36.

721. *See Downey v. Comm’r*, 33 F.3d 836, 839-40 (7th Cir. 1994) (recognizing a split over the nature of liquidated damages).

722. *Schleier*, 515 U.S. at 337-41 (O’Connor, J., dissenting).

723. *See id.* at 340 (O’Connor, J., dissenting).

personal injury or sickness.⁷²⁴ O'Connor recognized that this improperly assumes that personal injuries under § 104(a)(2) include only tangible injuries.⁷²⁵ Although the majority did not address this assumption, its reasoning that personal injuries arising from a car accident are distinguishable from personal injuries arising from discrimination assumes that a relevant difference between the two exists under the "plain meaning" of the § 104(a)(2).⁷²⁶

O'Connor then recognized a second suitable analysis within the "plain meaning" of § 104(a)(2) and *Burke*. She stated that if "the harms caused by discrimination constitute personal injury, then amounts received as damages for such discrimination are received 'on account of personal injuries' and should be excludable."⁷²⁷ While O'Connor was properly critical of the majority opinion in *Schleier*, she also deconstructed the underlying reasoning in *Burke*. Instead of focusing on the remedial scheme of the discrimination statutes, the Court could have looked at the nature of the injury and the right violated to determine whether the award flows from the personal injury or sickness.⁷²⁸ O'Connor revealed that *Burke* and *Schleier* improperly privileged a remedial statutory analysis over the effects of discriminatory tax claims.

In order to understand the Supreme Court's adherence to this unworkable, strained construction, one must understand the differences between these tangible and intangible claims. Besides the Court's error that Title VII's and ADEA's remedial schemes clearly distinguished between car accident and discrimination claimants, the Court failed to recognize its own discriminatory policy produced by labelling these claims as other than "tort or tort-type" injuries, and as injuries more similar to contract and equity.⁷²⁹ The antidiscrimination laws protect groups of people from societal denigration and victimization, but nothing protects these groups from conscious or unconscious judicial marginalization.

724. *See id.*

725. *See id.* at 341 (O'Connor, J., dissenting).

726. *See id.* at 341-42 (O'Connor, J., dissenting).

727. *Schleier*, 515 U.S. at 342 (offering analysis in place of the logic of the majority) (O'Connor, J., dissenting).

728. *See id.* (offering similar reasoning while labeling the logic of the majority as hard to follow) (O'Connor, J., dissenting).

729. *See infra* Part VII.B.

VI. EMPIRICAL STUDIES ESTABLISH THE EQUALITY OF PHYSICAL AND NONPHYSICAL INJURIES

I have heard that Title VII is supposed to make victims “whole” for the harm they have suffered because of discrimination. Well, I was not “made whole.” Not only did I have to pay a lot of medical bills and suffer a great deal of medical harm because of the harassment, but I was robbed of my dignity. Today, in 1990, several years after leaving West Bend, I am finding the healing process is far from over. Title VII did not make me “whole” for the harm I suffered.⁷³⁰

Today, there is no medical question that the effects of racial, ethnic, gender, age, and disability discrimination can damage an individual.⁷³¹ The harms caused by these various forms of discrimination result in negative psychological, physical, social, economical, and societal consequences.⁷³² Many times the negative psychological effects emanating from the infliction of discrimination also cause physical harms.⁷³³ Discrimination victims’ social relations often become stressed and break apart.⁷³⁴ With that pain and suffering also comes economic harm as individuals, who are displaced from work or not hired because of prejudice, find themselves struggling to make ends meet.⁷³⁵ Consequently, local, state, and federal governments must expend valuable resources to help victims of discrimination recover.⁷³⁶ What seems to begin as a personal injury results into what is truly a societal wound.

A. Racial Discrimination

Race-based stigmatization is “one of the most fruitful causes of human misery.”⁷³⁷ Individuals victimized by racism may experience negative mental

730. H.R. REP. NO. 102-40, at 67 (1991), *reprinted in* 1991 U.S.C.C.A.N. 549, 605.

731. *See generally* discussion *infra* Part IV.

732. *See id.*

733. *See id.*

734. *See id.*

735. *See id.*

736. *See, e.g.,* Mark McWilliams, *The Ticket to Work and Work Incentives Improvement Act: An “E” Ticket for Adults with Disabilities*, 79 MICH. B.J. 1680 (2000).

737. PHILIP MASON, RACE RELATIONS 2-3 (1970). *See also* James H. Carter, *Racism’s Impact on Mental Health*, 86 J. NAT’L MED. ASS’N 543 (1994); Patricia J. Falk, *Novel Theories of Criminal Defense Based upon the Toxicity of the Social Environment: Urban Psychosis, Television Intoxication, and Black Rage*, 74 N.C. L. REV. 731, 774 (1996) (stating that the majority of social scientists agree that black individuals’ mental and physical health suffer negative effects as a result of racism) (citing Chester M. Pierce, *Psychiatric Problems of the Black Minority*, in AMERICAN HANDBOOK OF PSYCHIATRY 512 (Silvano Arieti ed., 2d ed. 1974)). Although several studies conducted assess the effects of racism, scientists blame racism as somewhat accountable for a deficiency of research on this

effects such as “psychotic and neurotic depression, hostility, anger, . . . states of violence coupled with lowered self-esteem and ego destruction,” hypertension, aggression, retreat, withdrawal,⁷³⁸ self-hate, distrust, and resentful anxiety.⁷³⁹ Instances of racial discrimination may even result in the individual experiencing Post-Traumatic Stress Disorder (PTSD).⁷⁴⁰ Furthermore, mental disorders resulting from racism can cause an individual to turn to drugs and alcohol.⁷⁴¹ Discrimination victims may also suffer physical disease such as heart disease, diabetes, and arterial sclerosis as result of its traumatic psychological effects.⁷⁴²

topic. See Falk, *supra*, at 779 (“[R]acism in the research process itself may be partially responsible for the lack of a better developed body of work on the effects of racism on mental and physical health.”). Racism is also said to occur in psychiatric treatment. See Jeanne Spurlock, *Black Americans*, in CROSS-CULTURAL PSYCHIATRY 163, 168 (Albert Gaw ed., 1982) (warning that the role bias plays in assessment of psychiatric patients “cannot be overemphasized”); Harold Rosen & Jerome D. Frank, *Negroes In Psychotherapy*, 119 AM. J. PSYCHIATRY 456, 457 (1962) (stating that psychiatrists must “be alert to the possibility of unconscious prejudice. This may manifest itself either directly or through reaction formation . . . [in which the psychiatrist] may, for example, subtly reject Negro patients so that they stop coming to see him”).

738. Eugene Cash, Jr., *Extra-Dimensional Systemic Frustrations That Endanger the Mental Health of Black People*, in KEY MENTAL HEALTH ISSUES IN THE BLACK COMMUNITY 2 (Eugene Cash, Jr. et al. eds., 1976). For a discussion of the effects of racism on self-esteem, see Judith R. Porter & Robert E. Washington, *Black Identity and Self-Esteem: A Review of Studies of Black Self-Concept, 1968-1978*, 5 ANNUAL REV. OF SOCIO. 53, 53-74 (1979).

739. See Rosen & Frank, *supra* note 737, at 457.

740. See Falk, *supra* note 737, at 759-61. The effects of racism may become so extreme that victim suffers from paranoia and becomes schizophrenic. See *id.* at 775. See also Mary Ann Dutton & Lisa A. Goodman, *Posttraumatic Stress Disorder Among Battered Women: Analysis of Legal Implications*, 12 BEHAV. SCI. & L. 215 (1994); *Cultural and Historical Perspectives in Counseling Blacks*, in COUNSELING THE CULTURALLY DIFFERENT: THEORY AND PRACTICE 141, 146 (Derald Wing Sue ed., 1981) (stating that it was historically reported that “[b]lacks suffered from a high rate of schizophrenia, a claim that is still made today because of this group’s precarious racial position in the United States”).

741. See Richard Delgado, *Words That Wound: A Tort Action for Racial Insults, Epithets, and Name-Calling*, 17 HARV. C.R.-C.L. L. REV. 133, 137-38 (1982) (stating that minority communities experience much higher rates of narcotic use and admissions to psychiatric hospitals than the rest of society). Research also suggests that in general, overall psychological functioning and the quality of life are impaired due to racial discrimination. See Falk, *supra* note 737, at 776; Shawn O. Utsey, *Assessing the Stressful Effects of Racism: A Review of Instrumentation*, 24 J. BLACK PSYCHOL. 269, 270 (1998) (“Racism, in one form or another, permeates many aspects of African American life and, as such, significantly infringes on the quality of life enjoyed by African Americans.”).

742. See CASH, *supra* note 738, at 2; Delgado, *supra* note 741, at 137-39. See generally Earnest Harburg et al., *Socio-Ecological Stress, Suppressed Hostility, Skin Color, and Black-White Male Blood Pressure: Detroit*, 35 PSYCHOSOMATIC MED. 276, 276 (1973). Studies have concluded that high blood pressure and coronary heart disease are more common in blacks than their white counterparts due to racism. See Falk, *supra* note 737, at 776-77; Utsey, *supra* note 741, at 270. For a large, cross-sectional study conducted on the effects of racism on blood pressure, see Nancy Krieger & Stephen Sidney, *Racial Discrimination and Blood Pressure: The CARDIA Study of Young Black and White Adults*, 86 AM. J. PUB. HEALTH 1370, 1375 (1996) (studying the blood pressure results of 4,086 black and white men and women between the ages of twenty-five and thirty over a seven-year period and concluding that “internalized responses to racial discrimination may be associated with elevated blood pressure”).

Once discrimination negatively impacts the individual, the effects can spill over generationally. Family members of the discriminated-against party may be effected because discrimination can hinder a victim's ability to act as a proper parent.⁷⁴³ As a result “[s]elf-conscious, hypersensitive parents, preoccupied with the ambiguity of their own social position, are unlikely to raise confident, achievement-oriented, and emotionally stable children.”⁷⁴⁴

Moreover, “economic exploitation and poverty have been central features of racial domination—poverty is its long-term result.”⁷⁴⁵ Workers who are discharged as a result of racism face short-term and possibly long-term economic hardships as a result of job loss. In fact, these same individuals may encounter racism as they attempt to regain employment.

But the struggle of racial minorities to survive economically in the United States does not begin upon discharge from employment. Racism plays a part in creating staggering income disparities in existing job markets.⁷⁴⁶ Therefore, those racial minority members must deal with the economic effects of being underpaid in their employment.

B. Sexual Discrimination

[W]hen I was pregnant with my second child, the [sexual] harassment was still going on. My health continued to decline, and I started to lose weight. My OB-GYN, who was aware of my horrendous working conditions, told me that for the sake of my health and the health of the

For smaller cross-sectional studies, see Cheryl A. Armstead et al., *Relationship of Racial Stressors to Blood Pressure Responses and Anger Expression in Black College Students*, 8 HEALTH PSYCHOLOGY 541, 544, 553 (1989) (studying twelve male and fifteen female black college students, where the subjects were exposed to neutral, racist, and anger provoking film stimuli, and concluding that “there may be a heightened sensitization and vigilance for racism that cause greater anger reactivity to racist stimuli than to anger provoking, nonracist stimuli”); Sherman A. James et al., *John Henryism and Blood Pressure Differences Among Black Men. II. The Role of Occupational Stressors*, 7 JOURNAL OF BEHAVIOR MEDICINE 259, 259-60 (1984); Christopher Sempos et al., *Divergence of the Recent Trends in Coronary Mortality for the Four Major Race-Sex Groups in the United States*, 78 AM. J. PUB. HEALTH 1422, 1423 (1988). In addition to having higher blood pressure levels, “American blacks have . . . higher morbidity and mortality rates from hypertension, hypertensive disease, and stroke than do their white counterparts.” Delgado, *supra* note 741, at 139.

743. See Delgado, *supra* note 741, at 137-38.

744. *Id.* at 138-39.

745. Kimberlé Williams Crenshaw, *Race, Reform, and Retrenchment: Transformation and Legitimation in Antidiscrimination Law*, 101 HARV. L. REV. 1331, 1352 (1988).

746. See Theodore J. Davis, Jr., *Income Inequalities Between Black and White Populations in Southern Nonmetropolitan Counties*, REV. BLACK POLITICAL ECON., Spring 1994, at 155 (concluding that median family income for black Americans was only sixty percent that of white Americans due to structural, institutional, and socio-cultural factors). See also JOHN W. WORK, RACE, ECONOMICS, AND CORPORATE AMERICA 59-72 (1984) (discussing several theories of why black workers are underpaid in the job market as opposed to white workers).

child I was carrying, I had to take a medical leave of absence from work.⁷⁴⁷

Sexual harassment is a form of sex discrimination⁷⁴⁸ that pervades our society.⁷⁴⁹ Those who are harassed suffer from psychological effects such as stress, uncontrolled anger, alienation, helplessness, fright, tension, nervousness, distress, irritability, depression, persistent sadness, guilt, lability, anergia, hyperenergia, mood swings, impulsivity, emotional flooding, anxiety, fear of loss of control, escape fantasies, compulsive thoughts, rage episodes, obsessional fears, crying spells, vulnerability, diminished self-confidence, and decreased self-esteem and concentration.⁷⁵⁰

747. Crenshaw, *supra* note 745.

748. See U.S. EQUAL EMPLOYMENT OPPORTUNITY COMMISSION, SEX DISCRIMINATION: EMPLOYMENT DISCRIMINATION PROHIBITED BY TITLE VII OF THE CIVIL RIGHTS ACT OF 1964, AS AMENDED AND THE EQUAL PAY ACT OF 1963 Tab B (1998). The EEOC states that sexual harassment constitutes "[u]nwelcome sexual advances, requests for sexual favors, and other verbal or physical conduct of a sexual nature . . . when submission to or rejection of this conduct explicitly or implicitly affects an individual's employment, unreasonably interferes with an individual's work performance or creates an intimidating, hostile or offensive work environment." *Id.*

749. A 1987 survey of approximately 13,000 federal employees, of which 8,523 responded, concluded that in the twenty-four months prior to the survey 0.8% of the female and 0.3% of the male respondents were the victims of either an actual or attempted rape or assault. See U.S. MERIT SYSTEMS PROTECTION BOARD, SEXUAL HARASSMENT IN THE FEDERAL GOVERNMENT: AN UPDATE 9, 16-17 (1988). Nine percent of the women and three percent of the men surveyed reported that they were asked to perform sexual favors. See *id.* at 16-17. Unwanted touching, was experienced by twenty-six percent of women and eight percent of men surveyed. Twenty-eight percent of women and nine percent of men described receiving unwanted sexual looks or gestures. See *id.* Unwanted letters, telephone calls, or materials of a sexual nature were reported by twelve percent of the women and four percent of the men. See *id.* Women reported receiving unwanted pressure for dates fifteen percent of the time whereas four percent of men reported such unwanted pressure. See *id.* Finally, thirty-five percent of the women and twelve percent of the men reported receiving unwanted sexual teasing, jokes, remarks, or questions. See *id.*

750. See Sharyn Lenhart, *Physical and Mental Health Aspects of Sexual Harassment*, in SEXUAL HARASSMENT IN THE WORKPLACE AND ACADEMIA: PSYCHIATRIC ISSUES 21, 29 (Diane K. Shrier ed., 1996); VULNERABLE WORKERS: PSYCHOSOCIAL AND LEGAL ISSUES 191-92 (Marilyn J. Davidson & Jill Earnshaw eds., 1991) [hereinafter VULNERABLE WORKERS]. See also MICHELE A. PALUDI & RICHARD B. BARICKMAN, ACADEMIC AND WORKPLACE SEXUAL HARASSMENT: A RESOURCE MANUAL 29 (1991) (listing shock, denial frustration, embarrassment, confusion, shame, and powerlessness as negative psychological effects resulting from sexual harassment); Peggy Crull, *Stress Effects of Sexual Harassment on the Job: Implications for Counseling*, 52 AM J. ORTHOPSYCHIATRY 539, 541 (1982) (conducting a study of 262 women that sought crisis intervention in sexual harassment situations and finding that ninety percent of all victims suffered from psychological stress, tension, nervousness, and persistent anger); Mary P. Koss, *Changed Lives: The Psychological Impact of Sexual Harassment*, in IVORY POWER: SEXUAL HARASSMENT ON CAMPUS 73, 80-81 (Michele A. Paludi ed., 1990) (listing the sequence of cognitive reactions that victims of sexual harassment encounter as confusion and self-blame, fear and anxiety, depression and anger, and disillusionment and describing the changes in the victim's beliefs about herself, co-workers, and work in general at each stage). Some negative psychological effects from sexual harassment have been compared to those experienced by rape and incest victims. See Vita C. Rabinowitz, *Coping with Sexual Harassment*, in IVORY POWER: SEXUAL HARASSMENT ON CAMPUS, *supra*, 103, 106 (stating that the guilt and self-blame that women

Psychiatric disorders in the form of “anxiety disorders, (especially . . . post traumatic stress disorder), somatization disorders, sleep disorders, sexual dysfunction disorders, psychoactive substance-induced disorders, depressive disorders, [and] adjustment disorders . . . have been reported in association with sexual harassment experiences.”⁷⁵¹ Negative psychological effects resulting from harassment have led victims to experience physiological and health effects such as heart disease, blood vessel disease, kidney disease, arthritis, “diabetes mellitus, ulcers and stomach disorders, skin disorders, chest and back pains, headaches and migraines, insomnia, tiredness and loss of sexual interest.”⁷⁵² Other physical effects resulting from harassment are “gastrointestinal disturbances, jaw tightening, teeth grinding, dizziness, nausea, diarrhea, muscle spasms, pulse changes, . . . weight loss, tiredness, increased perspiring, loss of appetite, binge eating, decreased libido, delayed recovery from illness, sleep disruption, . . . increased respiratory and urinary tract infections; and recurrence of chronic illness.”⁷⁵³

Many of the psychological and physiological effects of sexual harassment disrupt the victims’ relationships with family, friends, and co-workers.⁷⁵⁴ Physical relationships with a significant other can deteriorate because of “[i]rritability, depression, and sexual dysfunction on the part of the victim.”⁷⁵⁵ Victims may also experience difficulties in parenting their children.⁷⁵⁶ Those who are harassed also suffer negative interpersonal

experience in conjunction with sexual harassment is the same as that experienced in victims of incest and rape).

751. Lenhart, *supra* note 750, at 29-30.

752. VULNERABLE WORKERS, *supra* note 750, at 192.

753. Lenhart, *supra* note 750, at 29. Victims, who testified in support of amending Title VII to provide plaintiffs compensatory and punitive damages, complained that they personally suffered from eating disorders and experienced nausea, diarrhea, cramping, neck pains, and breathing difficulties in consequence of harassment and discrimination. See H.R. Rep. NO. 102-40, at 66-67 (1991), reprinted in 1991 U.S.C.A.N. 549, 604-05.

754. See VULNERABLE WORKERS, *supra* note 750, at 193 (“The negative psychological and emotional effects of sexual harassment, [including] . . . uncontrollable anger, anxiety, irritability, fear and depression, . . . affect the victims’ relationships . . . outside the workplace. Additionally, the physiological and medical outcomes experienced by the victims of sexual harassment . . . quite likely limit the individuals’ desire and ability to interact with others.”) See also STEPHEN J. MOREWITZ, SEXUAL HARASSMENT AND SOCIAL CHANGE IN AMERICAN SOCIETY 160 (1996) (“As a result of sexual harassment, the victims may be less willing or able to have social relationships with others. This process is similar to those who are *sexually assaulted or raped*.”) (emphasis added).

755. Lenhart, *supra* note 750, at 32. See also PALUDI & BARICKMAN, *supra* note 750, at 29 (listing withdrawal, fear of new people and situations, lack of trust, lack of focus, self-preoccupation, changes in social network patterns, negative attitudes and behavior in sexual relationships, potential sexual disorders associated with stress and trauma, and changes in dress or in physical appearance as effects of sexual harassment that lead to negative social, interpersonal, and sexual conflicts); VULNERABLE WORKERS, *supra* note 750, at 193 (stating that reports of divorce, marital strain, and sexual problems resulting from sexual harassment are not uncommon).

756. See VULNERABLE WORKERS, *supra* note 750, at 193 (“[V]ictims’ relationships with sons,

outcomes that limit a person's capability to work and form friendships with co-workers.⁷⁵⁷ As a result of the harassment, the victim's attitude towards work and productivity are negatively affected.⁷⁵⁸

Sexual harassment economically strains the victim, the nation, and corporate America. Incidents of sexual harassment have caused workers to be discharged, demoted, given low evaluations, paid unfair wages, denied promotions and training opportunities, not hired, and given poor job references.⁷⁵⁹ Such practices may result in severe economic hardships to sexual harassment victims. The federal government incurs losses as a result of sexual harassment. The U.S. Merit Systems Protection Board conservatively estimated that sexual harassment in government employment cost the U.S. government \$267.3 million between May 1985 and May 1987 as a result of low individual productivity (\$76.3 million), low work group productivity (\$128.2 million), sick leave (\$26.1 million), and employee turnover expenditures (\$36.7 million).⁷⁶⁰ Similar factors cause private

daughters and mothers have been strained as a result of sexual harassment."); Lenhart, *supra* note 750, at 32 ("Discomfort with the sexualized nature of the harassment and backlash can cause further discomfort in the parent-daughter relationship.").

757. See VULNERABLE WORKERS, *supra* note 750, at 194 ("The emotional and psychological trauma experienced by the victim of harassment may render that person less willing and able to interact with others at work . . . Co-workers' actions and attitudes also seem to contribute to the negative social and interpersonal outcomes experienced by the victims of harassment.").

758. See Donna J. Benson & Gregg E. Thomson, *Sexual Harassment on a University Campus: The Confluence of Authority Relations, Sexual Interest and Gender Stratification*, 29 SOCIAL PROBLEMS 236, 248 (1982) ("The practice of sexual harassment both reflects and reinforces the devaluation of women's competence and helps erode their commitment to competitive careers."). See also VULNERABLE WORKERS, *supra* note 750, at 194-95; L. Camille Hébert, *The Economic Implications of Sexual Harassment for Women*, 3 KAN. J.L. & PUB. POL'Y, Spring 1994, at 47 ("In fact, the physical and psychological effects of sexual harassment on women may become so pronounced and so damaging to job performance that employers may acquire 'legitimate' reasons to take adverse job action against the affected employee.").

759. VULNERABLE WORKERS, *supra* note 750, at 195-96. See also MOREWITZ, *supra* note 754, at 162 (stating that workers who are discharged or quit because of sexual harassment incur up front costs for "themselves and their family members" and consequential costs "including uncompensated sick leave and the use of health services to cope with the stresses of unwanted sexual overtures on the job"); David E. Terpstra & Susan E. Cook, *Complainant Characteristics and Reported Behaviors and Consequences Associated with Formal Sexual Harassment Charges*, 38 PERSONNEL PSYCHOL. 559, 561-71 (1985) (studying eighty-one sexual harassment charges filed with the Illinois Department of Human Rights from July 1, 1981, through June 30, 1983, and concluding that of the seventy-six women in the study, sixty-six percent had been discharged, sixteen percent voluntarily quit, eleven percent had been demoted, and eight percent had been denied promotions due to sexual harassment). Many professionals, including scientists, engineers, lawyers, and teachers may be discouraged from filing claims because of being blacklisted when applying for future positions. See *id.* at 566-67.

760. U.S. MERIT SYSTEMS PROTECTION BOARD, *supra* note 749, at 40. The U.S. Merit Systems Update "defines 'decline in individual productivity' to be a loss in the quality or quantity of work performed by an individual." *Id.* at 41. Job turnover costs arose from 36,647 sexual harassment victims leaving their position in the two-year span of the study. See *id.* at 40. The cost of employee sick leave due to sexual harassment was determined somewhat differently. The victims of sexual harassment

employers to experience reductions in their bottom lines.⁷⁶¹

C. Age Discrimination

The sudden cessation of productive work and earning power of an individual, caused by compulsory retirement, often leads to physical and emotional illness and premature death.⁷⁶²

Age discrimination differs from “the insidious discrimination based on race or creed prejudices and bigotry . . . aris[ing instead] . . . because of assumptions that are made about the effects of age on performance.”⁷⁶³ As a result of age discrimination, older workers are fired, not hired, forced to retire, reassigned to undesirable positions, and given poor evaluations to justify future dismissal.⁷⁶⁴ Such employment discrimination causes minority

were questioned as to how much, if any, sick leave they took because of sexual harassment. *See id.* at 41. The U.S. Merit Systems’ Board found that thirteen percent of the victims used sick leave because of sexual harassment. *See id.* The Board then plugged that percentage into an equation with the average government employee salary to the “average cost of reduced productivity was \$110.89 per female victim and \$263.69 per male victim.” *Id.* These averages were then used in determining the “cost of decline in work group productivity.” *Id.*

761. *See* Anita Bernstein, *Law, Culture, And Harassment*, 142 U. PA. L. REV. 1227, 1261 (1994) (“An employer who condones sexual harassment—whose main criterion for employees becomes their willingness to tolerate harassment—will likely end up with workers who have weaker traditional qualifications and who are, therefore, less productive.”). *See also* ANDREA P. BARIDON & DAVID R. EYLER, *WORKING TOGETHER: THE NEW RULES AND REALITIES FOR MANAGING MEN AND WOMEN AT WORK* 172 (1994) (stating that an average Fortune 500 company that employs 23,750 individuals incurs \$6.7 million a year in costs associated with absenteeism, reduced productivity, and employee turnover resulting from sexual harassment); Terpstra & Cook, *supra* note 759, at 560-61 (stating that in addition to the costs associated with litigating a sexual harassment action, hidden costs derived from sexual harassment may materialize as a result of increased stress, decreased work productivity, absenteeism, and employee turnover). Corporate studies show that workers’ attitudes toward their jobs are directly related to revenue. *See* Sue Shellenbarger, *Companies Are Finding It Really Pays to Be Nice to Employees*, WALL ST. J., July 22, 1998, at B1. Sears Roebuck conducted a study showing that if employee attitudes improve by five percent, customer satisfaction rises to cause a one-half percent rise in revenue. *See id.* This increase in revenue, therefore, can be traced to a happier work force. *See id.* Less turnover cuts training costs and experienced employees who are happy and dedicated to their jobs are forty percent more efficient than trainees would be in their first six months on the job. *See id.* The cost of replacing an employee is estimated from thirty percent of an annual salary for entry level employees to five times the annual salary for executives. CAROL A. HACKER, *THE HIGH COST OF LOW MORALE . . . AND WHAT TO DO ABOUT IT* xvi (1997).

762. S. REP. NO. 95-493, at 4 (1978), *reprinted in* 1978 U.S.C.C.A.N. 504, 507 (based on information received from the American Medical Association).

763. 113 CONG. REC. 34,718, 34,742 (1967) (“Studies have shown, however, that the job performance of the older worker at many tasks does not decrease significantly with age. Even after 55, the older worker is usually able to keep up with the pace set by his younger coworkers.”). *See also* S. REP. NO. 103-40, pt. 1, at 82 (1993) (“Two nationwide surveys conducted by Louis Harris & Associates, in 1975 and in 1981, found nearly identical results: 8 out of 10 Americans believe that ‘most employers discriminate against older people and make it difficult for them to find work.’”).

764. S. REP. NO. 103-40, pt. 1, at 82 (1993).

group reactions among older workers, including “bitterness, resentment, and self-hatred.”⁷⁶⁵

Victims forced into retirement may suffer negative psychological and emotional effects such as neurotic depression, restlessness, weariness, dejection, hypochondria, self-depreciation,⁷⁶⁶ frustration, bitterness, and general psychological malaise.⁷⁶⁷ Furthermore, displacement from work may shorten a victim’s life-span, resulting in premature death.⁷⁶⁸

Retirement may dramatically affect one’s social relations particularly if the individual depended on co-workers to satisfy social needs.⁷⁶⁹ The reduction in income and loss of interaction patterns accompanied with employment could lead to feelings of isolation and a loss of personal identity.⁷⁷⁰ Moreover, “[t]he more autocratic the family structure of the retirant, the greater is the deterioration of his status and the more intense is . . . [the individual’s] morbidity in retirement.”⁷⁷¹

Employment-based age discrimination threatens “the welfare of many older persons who depend on their earnings for their support.”⁷⁷² Even though older workers may receive Social Security benefits upon retirement and may possess pension plans to help fund retirement, statistical evidence shows that these funding mechanisms do not properly sustain retirants.⁷⁷³

765. MILTON L. BARRON, *THE AGING AMERICAN: AN INTRODUCTION TO SOCIAL GERONTOLOGY AND GERIATRICS* 62 (1961).

766. See Norman Cameron, *Neuroses of Later Maturity*, in *MENTAL DISORDERS IN LATER LIFE* 201, 219 (Oscar Kaplan ed., 2d ed. 1956). See also W. Ferguson Anderson & R. Davidson, *Concomitant Physical States*, in *MODERN PERSPECTIVES IN THE PSYCHIATRY OF OLD AGE* 84, 85 (John G. Howells ed., 1975) (noting that “depression following retirement is a frequently encountered condition”).

767. See Gordon F. Streib, *Morale of the Retired*, 3 *SOCIAL PROBLEMS* 270, 270 (1956).

768. S. REP. NO. 95-493, at 4 (1978), reprinted in 1978 U.S.C.C.A.N. 504, 507; S. REP. NO. 103-40, pt. 1, at 83 (1993) (“[M]edical evidence suggests that forced retirement can so adversely affect a person’s physical, emotional, and psychological health that a lifespan may be shortened.”). Retirement sufficiently disrupts daily life patterns that it “may disturb . . . [an individual’s] physiology sufficiently to induce organic illness and premature death.” BARRON, *supra* note 806, at 85. Moreover, “expectation[s] of physical and mental morbidity and impending death are so dramatically intensified by the formality of retirement that . . . [these fears] become ‘self-fulfilling prophecies,’ expressed in hypochondria and functional symptoms of illness.” *Id.* Edmund C. Payne, *Depression and Suicide*, in *MODERN PERSPECTIVES IN THE PSYCHIATRY OF OLD AGE*, *supra* note 766, at 290, 293 (“Increased suicide rates are positively correlated with situations involving stress, instability, and threatened deprivation. The elderly are especially vulnerable to stress involving occupational and economic factors.”).

769. See BARRON, *supra* note 765, at 84.

770. See *id.*; Cameron, *supra* note 766, at 219.

771. BARRON, *supra* note 765, at 84.

772. S. REP. NO. 103-40, pt. 1, at 82 (1993).

773. See *id.* Increasingly, older persons are receiving maximum Social security benefits; however, most older people still “receive less than the maximum.” *Id.* Moreover, the number of persons aged sixty-five and older earned annually less than \$15,000 in 1998. *Id.* (according to the 1990 edition of

Therefore, not only must the victim face the physical and psychological consequences of age discrimination, the victim will also often have to deal with potential or actual poverty.⁷⁷⁴

Furthermore, “[s]ociety as a whole suffers from mandatory retirement.”⁷⁷⁵ As older workers are forced to retire, Social Security and pension plan funds are drained.⁷⁷⁶ Moreover, the economy as a whole suffers as the skilled labor force and the gross national product are reduced from older workers being forced to retire.⁷⁷⁷

D. Disability Discrimination

When I was 5 my mother proudly pushed my wheelchair to our local public school, where I was promptly refused admission because the principal ruled that I was a fire hazard. . . . When I was 19, the house mother of my college dormitory refused me admission into the dorm because I was in a wheelchair and needed assistance. When I was 21 years old, I was denied an elementary school teaching credential because of “paralysis of both lower extremities sequelae of poliomyelitis.” . . . In 1981, an attempt was made to forcibly remove me and another disabled friend from an auction house because we were “disgusting to look at.” . . . These are only a few examples of discrimination I have faced in my 40-year life. I successfully fought all of these attempted actions of discrimination through immediate aggressive confrontation or litigation. But this stigma scars for life.⁷⁷⁸

the U.S. Senate Special Committee on Aging’s report entitled “Aging America: Trends and Projections”). “Most older persons do not have substantial holdings in savings, stocks, insurance policies, or bonds.” *Id.* For many, retirement income from public or private sources is unavailable or inadequate to support a comfortable existence. S. REP. NO. 95-493, at 3 (1978), *reprinted in* 1978 U.S.C.C.A.N. 504, 507. For some, the opportunity to continue working has become a question of economic survival. *See id.* In 1975, 14.6 percent of persons age sixty-five and older had annual incomes below the poverty level. *See id.*

774. *See* Streib, *supra* note 767, at 273 (“[L]ow morale may be due *either* to retirement *or* to low socio-economic status. When the two factors are found in combination, they result in the most devastating effect, for over two out of three among those persons who are both poor and retired have low morale.”).

775. S. REP. NO. 95-493, at 4 (1978), *reprinted in* 1978 U.S.C.C.A.N. 504, 507.

776. *See* MARTIN LYON LEVINE, AGE DISCRIMINATION AND THE MANDATORY RETIREMENT CONTROVERSY 32 (1988).

777. *See id.* *See also* S. REP. NO. 95-493, at 4 (1978), *reprinted in* 1978 U.S.C.C.A.N. 504, 507 (“In hearings before the House Select Committee on Aging, Professor James Schulz of Brandeis University testified that mandatory retirement of willing and able employees costs the nation three-tenths of 1 percent of its annual gross national product. This represents 4.5 billion 1976 dollars.”).

778. H.R. REP. NO. 101-485, pt. 2, at 29-30 (1990), *reprinted in* 1990 U.S.C.C.A.N. 267, 311

Many studies document “[t]he severity and pervasiveness of discrimination against people with disabilities.”⁷⁷⁹ Disabled individuals are discriminated against in employment, “public accommodations, public services, transportation, and telecommunications.”⁷⁸⁰ As a result, the disabled experience causes feelings of isolation and helplessness as well as low levels of self-satisfaction.⁷⁸¹ Disability discrimination robs victims of their dignity and self-respect and the everyday horror caused by disability discrimination often scars victims for life.⁷⁸²

Disability discrimination also shuts the disabled out of mainstream society, causing social suffering as well.⁷⁸³ For the most part, the disabled do not attend theaters, movies, musical performances, grocery stores, restaurants, or places of worship because they are made to feel too unwelcome and too self-conscious about their disability, not only by the architectural restrictions of these everyday venues, but also by the words and actions of the strangers around them.⁷⁸⁴ In fact, a survey conducted in 1986 by Louis Harris, concluded that close to two-thirds of disabled Americans did not go to one movie in the past year; three-fourths did not frequent a single theater or music performance in the past year; two-thirds did not attend a sporting event in the past year; seventeen percent do not eat in restaurants; and thirteen percent of disabled Americans never shop at grocery stores.⁷⁸⁵

As a result of being discriminated against in the job market, individuals with disabilities must struggle to survive economically in today’s society.⁷⁸⁶

(citation omitted).

779. H.R. REP. NO. 101-485, pt. 2, at 30 (1990), *reprinted in* 1990 U.S.C.C.A.N. 267, 311-12 (“Discrimination against people with disabilities . . . includes adverse actions taken against individuals with histories of a disability, . . . adverse actions taken against those regarded by others as having a disability, [and] . . . discrimination against persons associated with individuals with disabilities.”).

780. H.R. REP. NO. 101-485, pt. 2, at 29 (1990).

781. *Id.* at 41. *See also* National Council on the Handicapped, Report on Employment Issues Related to Persons with Disabilities (June 10, 1987) (on file with author) (finding that employment for individuals with disabilities “is critical in determining independence, self-sufficiency and quality of life”).

782. *See* H.R. REP. NO. 101-485, pt. 2, at 41 (1990) *reprinted in* 1990 U.S.C.C.A.N. 267, 311, 323.

783. *See id.*

784. H.R. REP. NO. 101-485, pt. 2, at 34-35.

785. *See* LOUIS HARRIS AND ASSOCIATES, THE ICD SURVEY OF DISABLED AMERICANS: BRINGING DISABLED AMERICANS INTO THE MAINSTREAM 37-40 (1986) (on file with author) [hereinafter LOUIS HARRIS POLL ICD 1] (cited in H.R. REP. NO. 101-485 (1990), *reprinted in* 1990 U.S.C.C.A.N. 267); Robert L. Burgdorf Jr., *The Americans with Disabilities Act: Analysis and Implications of a Second-Generation Civil Rights Statute*, 26 HARV. C.R.-C.L. L. REV. 413, 423 (1991).

786. *See* H.R. REP. NO. 101-485, pt. 2, at 32 (“Individuals with disabilities experience staggering levels of unemployment and poverty. According to a recent Louis Harris poll ‘not working’ is perhaps the truest definition of what it means to be disabled in America.”).

In 1984, fifty percent of disabled American adults maintained household incomes of \$15,000 or less.⁷⁸⁷ Two-thirds of Americans with disabilities between the ages of 16 and 64, roughly 8.2 million people, do not work even though an abundant majority of these individuals do want to work.⁷⁸⁸

E. Conclusion to Part VI

Scientific studies, statistical evidence, and anecdotal accounts document the harmful effects of particular types of discrimination. Various forms of discrimination frequently cause the same type of suffering. A victim of age discrimination may suffer the same psychological effects that a victim of sexual harassment suffers. Disability discrimination may cause an individual to suffer the same harmful physical effects that racial discrimination causes an individual to suffer. Ethnic discrimination victims may experience the same economic effects that age discrimination victims experience. Gender discrimination may effect the same social costs that disability discrimination causes.

In the end, the victim, the family, friends of the victim, and society as a whole suffer the negative effects of each type of discrimination. With such cumulative evidence available to Congress and the courts, one would think that today's enlightened decision makers would support equal tax treatment of victims with physical and nonphysical injuries. Yet they do not.

VII. WAS UNCONSCIOUS DISCRIMINATION AT THE HEART OF THE CHANGE TO § 104(A)(2)?

How is it conceivable that on the one hand Congress has enforced the policy of ridding the workplace of the societal scourge of invidious discrimination in all its forms, and on the other hand simultaneously enacted legislation repealing a seventy-eight-year-old tax exclusion for victims of discrimination and thus singles out for taxation the very victims of discrimination for whom Congress intended to provide compensatory redress? Further, why did the taxing amendment follow on the heels of the

⁷⁸⁷ *See id.*

⁷⁸⁸ *See id.*; LOUIS HARRIS POLL ICD 1, *supra* note 785, at 47, 50-51. Americans with disabilities who do work are often undercompensated in comparison to workers that are not disabled. H.R. REP. NO. 101-485, pt. 2, at 32 (1990), *reprinted in* 1990 U.S.C.C.A.N. 267, 314. A census taken in 1980 showed that disabled men earned twenty-three percent less than the nondisabled men and disabled women earned thirty percent less than nondisabled women. *See id.* By 1988, the disparity had widened to thirty-six and thirty-eight percent respectively. *See id.* Of those disabled individuals that do work, twenty-five percent live in poverty. LOUIS HARRIS POLL ICD 1, *supra* note 785, at 25.

1991 Civil Rights Amendment, which expanded the protections and remedies provided for discrimination victims in order to ensure that they are made whole?

Certainly it would be difficult, if not impossible, to find a member of Congress who would publicly advocate enacting tax laws that single out victims of discrimination for taxation while providing a tax benefit to other taxpayers. One could not assert with intellectual integrity that a fundamental tax distinction exists in personal injuries between the physical injury of a sprained ankle and the severe psychological injury resulting from racial discrimination.⁷⁸⁹ Finally, it would be intellectually dishonest to suggest that some important and overriding tax policy requires a distinction between physical and nonphysical injuries for taxation.⁷⁹⁰ Nevertheless, between 1989 and 1996, both the Supreme Court and Congress incrementally constructed and ultimately eliminated this seventy-eight-year-old tax exclusion for the victims of dignitary torts.

What is the explanation for the change to § 104(a)(2)? A case can be made that unconscious discrimination played a part in the 1996 amendments to § 104(a)(2). In making this case, Part VII uses both psychoanalytic and cognitive theories of psychology to argue that unconscious judicial and legislative discrimination influenced the 1996 amendment to § 104(a)(2). Section A introduces the psychoanalytic and cognitive theories of unconscious discrimination, while Section B begins with an historic overview of the law of emotional distress pertinent to the current status of § 104(a)(2), and then applies the psychoanalytic and cognitive theories of unconscious discrimination to the current status of § 104(a)(2). In all of this Part, I draw on the pioneering work on unconscious racism by Charles R. Lawrence.

A. *The Psychoanalytic (Freudian) and Cognitive Approaches to Unconscious Discrimination*

1. *Psychoanalytic Approach*

As is broadly recognized, and as Lawrence so powerfully portrays, racially discriminatory acts are often the product of unconscious bias and stereotyping.⁷⁹¹ Lawrence cites both Freudian and cognitive theories that

789. For more information on the lack of distinction, see *infra* Part VI.

790. For more information on the lack of such tax policy, see *infra* Part III.

791. See Charles R. Lawrence, *The Id, the Ego, and Equal Protection: Reckoning with Unconscious Racism*, 39 STAN. L. REV. 317, 322 (1987). Lawrence employs these theories to establish

offer insights into the unconscious nature of racist beliefs and acts, but his theory may be expanded here to embrace all discriminatory beliefs and acts (including those based on gender, age, and physical disability).⁷⁹²

Psychoanalytic theory, as developed originally in Sigmund Freud's theory of personality, states that the mind protects itself from anxiety associated with guilt by refusing to identify "ideas, wishes, and beliefs" conflicting with socially acceptable behavior.⁷⁹³ In Freud's theory, this self-protection of the conscious mind is called "repression." And it includes both primary and secondary mental processes. Repression's primary process occurs in the Id, deep below conscious awareness.⁷⁹⁴ The Id comprises the desires of the human instincts, which seek only gratification; its ultimate end is pleasure.⁷⁹⁵ Repression's secondary process occurs in the Ego, which includes both conscious and unconscious dimensions.⁷⁹⁶ The Ego articulates what the

a test that would get around the intent requirement of the doctrine of discriminatory purpose established in *Washington v. Davis*, 426 U.S. 229 (1976). See *id.* at 319. See also Paul Brest, *The Supreme Court, 1975 Term—Foreword: In Defense of the Antidiscrimination Principle*, 90 HARV. L. REV. 1, 14 (1976) ("Race-dependent decisions need not be race-conscious, but may reflect unconscious racially selective indifference. Such indifference violates the anti-discrimination principle when its effect is to deny benefits to minority persons, or impose burdens on them, which would not be denied or imposed if they were white."). Lawrence calls this test the Cultural Meaning Test. See Lawrence, *supra*, at 356. The Cultural Meaning Test identifies unconscious discrimination through conduct or symbols containing a cultural meaning that provides evidence for such discrimination. See *id.* By looking at the historical and social context of the government action, the court applies heightened scrutiny if the preponderance of the evidence shows that a significant part of the population would determine that unconscious discrimination influenced the government action. See *id.* Courts would analyze historical and social empirical data surrounding the alleged discrimination to determine whether unconscious discrimination occurred. See *id.*

Lawrence also argues that since overt discrimination is unconstitutional, legislation will be drafted so as to be constitutional. See *id.* However, unconscious discrimination still may predominate legislation. See *id.* As a result, this method of thought, in allowing unconscious discrimination, becomes the new norm in the legislative process. See *id.* When opponents of this discrimination identify it, such legislation is shown to have its own cultural meaning that creates the same stigma as overt discrimination. See *id.* Among other things, Lawrence's theory has been used to make constitutional challenges against crack cocaine sentencing guidelines. See, e.g., David A. Sklansky, *Cocaine, Race, and Equal Protection*, 47 STAN. L. REV. 1283, 1307-11 (1995). Arguably, under the Cultural Meaning Test, the 1996 amendments to § 104(a)(2) would trigger heightened scrutiny and result in the statute's unconstitutionality.

792. See Lawrence, *supra* note 791, at 322-23.

793. *Id.* at 322. Lawrence notes that "Freudian theory states that the human mind defends itself against the discomfort of guilt by denying or refusing to recognize those ideas, wishes, and beliefs that conflict with what the individual has learned is good or right." *Id.* Actually, Freudian theory takes a wider view of psychic defense: it is not just defense against guilt, but defense against anxiety." LEVINE, *supra* note 776, at 137-38 (discussing Lawrence's article).

794. SIGMUND FREUD, *THE EGO AND THE ID* 15 (James Strachey ed. & Joan Riviere trans., 1960) [hereinafter FREUD]. See also Lawrence, *supra* note 791, at 331.

795. See FREUD, *supra* note 794, at 15. See also Lawrence, *supra* note 791, at 331.

796. See FREUD, *supra* note 794, at 7. Lawrence states that "[t]he, secondary process, or Ego, happens under conscious control and is bound by logic." Lawrence, *supra* note 791, at 331. This is not entirely true. The Ego "controls the approaches to motility" and from the Ego "proceed the

conscious self considers “reason and common sense.”⁷⁹⁷ Repression occurs at the level of the Ego when its alleged “reason and common sense” blocks passions deeply seated in the Id from entering fully into consciousness.⁷⁹⁸ When this happens, powerful unconscious ideas actually influence consciousness, but do not themselves become explicitly conscious. At a very deep level within the self, “certain forces” oppose such an occurrence.⁷⁹⁹

According to Lawrence, psychoanalytic theory can be used to explain how racism is the product of unconscious repression. Thus, “racial antagonism finds its source in the unconscious, since people who are “asked to explain the basis of their racial antagonism . . . either express an instinctive, unexplained distaste at the thought of associating with the out-group as equals or . . . cite reasons that are not based on established facts and are often *contradicted by personal experience.*”⁸⁰⁰ Such behavior reveals poor “reality-testing.”⁸⁰¹ The inadequacy of reality-testing usually preserves a misguided attitude that remains basic to the “individual’s makeup.”⁸⁰² In addition, when threatened by adequate reality-testing, such individuals avoided the truth by legitimizing the misguided attitude with “*socially acceptable pseudoreasons.*”⁸⁰³

repressions, . . . by means of which it is sought to exclude certain trends in the mind not merely from consciousness but also from other forms of effectiveness and activity.” See FREUD, *supra* note 794, at 7. These trends “stand in opposition to the ego, and the analysis is faced with the task of removing the resistances which the ego displays against concerning itself with the repressed.” *Id.* Freud notes that patients in analysis have trouble removing the resistance and upon being told that a resistance exists, patients do not know what the resistance is or how to describe it. *Id.* This leads Freud to the conclusion that “[w]e have come upon something in the ego itself which is also unconscious, which behaves exactly like the repressed—that is, which produces powerful effects without itself being conscious and which requires special work before it can be made conscious.” *Id.* A part of the ego is thus unconscious. *See id.* at 8.

797. See FREUD, *supra* note 794, at 15. The ego and the id are not separate. The “ego is that part of the id which has been modified by the direct influence of the external world.” *See id.* at 15.

798. *See id.* at 4, 15. *See also* Lawrence, *supra* note 791, at 331-32.

799. See FREUD, *supra* note 794, at 15. If “certain forces” did not exist to oppose unconscious ideas, “it would then be apparent how little they differ from other elements which are admittedly psychical.” *Id.* Freud calls an idea a psychical element. *See id.* This psychical element is sometimes unconscious for an extended period of time. *See id.* In fact, its conscious state is transitory. *See id.* However, the idea can become conscious once again and is then termed *latent* or *unconscious*. *See id.* Repression is “[t]he state in which the ideas existed before being made conscious . . . [and] the force which instituted the repression and maintains it is perceived as *resistance* during the work of analysis.” *Id.* To Freud, in the descriptive sense, there are two different types of unconscious. *See id.* at 5. The latent unconscious, which he calls *preconscious*, is capable of becoming conscious. *See id.* The repressed unconscious, which he calls *unconscious*, cannot become conscious. *See id.* The *unconscious* is the “prototype of the unconscious.” *Id.*

800. Lawrence, *supra* note 791, at 332 (emphasis added).

801. *Id.*

802. *Id.*

803. *Id.* (emphasis added).

Unlike the case of explicitly conscious irrational behavior which does not even try to justify its distaste of an out-group, and which consciously refuses to allow its prejudice to be contradicted by personal experience, unconscious racism (and by extension unconscious prejudice in general), claims to be logical and rational, even when it maintains “rigidly stereotyped thinking” that projects neurotic conflict.⁸⁰⁴

For example, Lawrence points to studies that show racists hold out two general stereotypes: (1) the out-group is “dirty, lazy, oversexed, and without control of their instincts (a typical accusation against blacks);” and (2) the outgroup is “pushy, ambitious, conniving, and in control of business, money, and industry (a typical accusation against Jews).”⁸⁰⁵ These stereotypes result, he claims, from neurotic conflict that arises when either instinctive drives cannot be “master[ed]” under “socially approved patterns of behavior,” or “when an individual cannot live up to the aspirations and standards of his [sic] own conscience.”⁸⁰⁶

Lawrence states that, since overt racism has been socially rejected in today’s society, then “hidden prejudice [must] . . . become the more prevalent form of racism.”⁸⁰⁷ The ego “must adapt” to this new social order and “repress or disguise racist ideas.”⁸⁰⁸

2. Cognitive Approach

In contrast to psychoanalytic theorists, cognitive psychologists “do not embrace the Freudian belief that instinctual drives dominate individuals’ concepts, attitudes, and beliefs. Instead, they view human behavior, including racial prejudice, as growing out of the individual’s attempt to understand his (or her) relationship with the world . . . while at the same time preserving his (or her) personal integrity.”⁸⁰⁹

Cognitive theorists believe that individuals categorize all things as part of their attempt to understand the complexities of life.⁸¹⁰ Such categorization produces discriminatory stereotypes, because “[w]hen a category . . . correlates with a continuous dimension . . . there is a tendency to exaggerate

804. *Id.* at 333.

805. *Id.* (citing G. ALLPORT, *THE NATURE OF PREJUDICE* 196-98 (1954); J. KOVEL, *WHITE RACISM: A PSYCHOHISTORY* 51-92 (1970); G. SELZNICK & S. STEINBERG, *THE TENACITY OF PREJUDICE: ANTISEMITISM IN CONTEMPORARY AMERICA* 170-71 (1969)).

806. Lawrence, *supra* note 791, at 333-34.

807. *See id.* at 335.

808. *Id.* at 335 (emphasis added).

809. *Id.* at 336.

810. Lawrence, *supra* note 791, at 337-38.

the differences between categories on that dimension and to minimize the differences within each category.”⁸¹¹ “Individuals learn cultural attitudes and beliefs about race very early in life, at a time when it is difficult to separate the perceptions of one’s teacher (usually a parent) from one’s own.” Thus, people create social categories and assign to each category content characteristics “generated over a long period of time within a culture and transmitted to individual members of society by . . . ‘assimilation’ . . . [which] entails learning and internalizing preferences and evaluations.”⁸¹² A racist category will therefore be formed by associating external features with certain undesirable or offensive character traits.

When someone with racist categories confronts an individual who for external reasons falls within a different category than one’s self, that person then assumes that the other person carries the stereotypical character traits that correspond to the racist categories. Only after receiving sufficient information conflicting with the stereotype, can such presumptions about that particular individual be eliminated.⁸¹³ However, when the individual deals with interpreting the behavior of a stereotyped group “en masse,” that stereotype will almost never be broken down.⁸¹⁴ Moreover, the individual, who experiences events that further illustrate and support the stereotype of a

811. *Id.* at 337. See also Donald T. Campbell, *Enhancement of Contrast as Composite Habit*, 53 J. ABNORMAL & SOC. PSYCHOL. 350, 355 (1956) (conducting a series of experiments with nonsense syllables and coming to similar conclusions as did Tajfel & Wilkes); Henri Tajfel, *Cognitive Aspects of Prejudice*, J. SOC. ISSUES, Autumn 1969, at 83-86 (discussing the 1963 experiments conducted by Tajfel and Wilkes and their application to aspects of prejudice); Henri Tajfel & A.L. Wilkes, *Classification and Quantitative Judgment*, 54 BRIT. J. PSYCHOL. 101, 104 (1963) (conducting a series of experiments and finding that individuals over- and underestimated the lengths of lines once they were told that the longer four lines were in “Group A” and the shorter four were in “Group B”). The cognitive approach includes three claims. See Linda Hamilton Krieger, *The Content of Our Categories: A Cognitive Bias Approach to Discrimination and Equal Employment Opportunity*, 47 STAN. L. REV. 1161, 1187-88 (1995). First, stereotyping is a form of categorization used by prejudiced and nonprejudiced individuals. See *id.* at 1188. Second, stereotypes “bias a decision maker’s judgment long before the ‘moment of decision,’ as a decision maker attends to relevant data and interprets, encodes, stores, and retrieves it from memory. *Id.* These biases “‘sneak up on’” the decision maker, distorting bit by bit the data upon which his decision is eventually based.” *Id.* Third, stereotypes “operate beyond the reach of decision maker self-awareness. Empirical evidence indicates that people’s access to their own cognitive processes is in fact poor. Accordingly, cognitive bias may well be both unintentional and unconscious.” *Id.*

812. Lawrence, *supra* note 791, at 337-38. See also Jody David Armour, *Hype and Reality in Affirmative Action*, 68 U. COLO. L. REV. 1173, 1181-82 (1997) (“Stereotypes are deeply ingrained in children’s memories at an early age For example, Dr. Phyllis Katz reports a chilling case of a three-year-old child, who upon seeing a black infant said to her mother, ‘Look mom, a baby maid.’”). Discrimination can also be learned through exposure to the “media and an individual’s parents, peers, and authority figures.” Lawrence, *supra* note 791, at 323.

813. See Lawrence, *supra* note 791, at 339.

814. *Id.*

particular group, only strengthens that internal stereotype.⁸¹⁵ After the reinforcement occurs, the individual rejects that he or she ever had a previous stereotype of the group and, instead, focuses on the actual observed event as a reason for not preferring a certain group.⁸¹⁶

Cognitive theory makes three claims.⁸¹⁷ First, stereotyping is a form of categorization used by both prejudiced and nonprejudiced individuals.⁸¹⁸ Second, stereotypes “bias a decision maker’s judgment long before the ‘moment of decision,’ as a decision maker attends to relevant data and interprets, encodes, stores, and retrieves it from memory. These biases ‘sneak up on’ the decision maker, distorting bit by bit the data upon which his decision is eventually based.”⁸¹⁹ Third, stereotypes “operate beyond the reach of decision maker’s self-awareness. Empirical evidence indicates that people’s access to their own cognitive processes is, in fact, poor. Accordingly, cognitive bias may well be both unintentional and unconscious.”⁸²⁰

*B. Application of the Psychoanalytic Theory and Cognitive Theory to
§ 104(a)(2)*

Psychoanalytic and cognitive theories may be used to explain unconscious discrimination based on race, sex, age, disability, national origin, or religion.⁸²¹ Using both these theories, this section will begin by revealing the actual historical existence of unconscious discrimination by the law in the case of emotional distress, which is a nonphysical injury. Then it will argue that this historical discrimination by the law toward treatment of emotionally distressed plaintiffs, who have suffered nonphysical injury, is detrimental to the rights of victims of nonphysical injuries under § 104(a)(2).

815. *See id.* at 338.

816. *See id.* at 338-39.

817. *See* Krieger, *supra* note 811, at 1187-88.

818. *See id.* at 1188.

819. *Id.*

820. *Id.* *See also infra* Part VII.A.2.

821. Although Lawrence narrowed the scope of his article to unconscious racism, he noted that “[i]t has been argued that sexism is even more deeply imbedded in our culture than racism and, thus, less visible . . . This would indicate that until the dominant ideology wholly rejects sexism, sexist attitudes may be repressed and held at an unconscious level less often than racist attitudes.” Lawrence, *supra* note 791, at 322 n.22 (citations omitted). Martin Lyon Levine, while discussing unconscious ageism, believes that Lawrence has “the argument backwards” under Freudian theory. LEVINE, *supra* note 776, at 138. Levine argues that sexist and ageist attitudes are “more likely to be repressed than racist attitudes, because . . . the relationship with the other sex . . . [and] the relationship with the older generation [are] . . . highly conflict-ridden experience[s]” for young children. *Id.* Levine concludes that “in a Freudian theory of repression, unlike Lawrence’s theory, commonly held unconscious sexism and unconscious ageism are hypotheses worth considering.” *Id.*

1. *History of Gender Bias in the Law of Mental Injury*

Male judges and lawyers influenced by early modern Western male philosophers like Descartes, Rousseau, and Hobbes, laid the foundation for unconscious but very real discrimination against women in modern Western legal systems.⁸²²

One important example of a standard in the law biased against women was the allegedly objective “reasonable man” standard, established in the 1837 English tort case of *Vaughan v. Menlove*: “Negligence is the omission to do something which a reasonable man . . . would do, or doing something which a prudent and reasonable man would not do.”⁸²³ This standard is “male-biased” because courts and society in general “view the male perspective as the objective or normative one.”⁸²⁴

Early common law decisions concerning emotional distress evidenced this gender bias, perhaps most notably in the 1861 English case of *Lynch v. Knight*.⁸²⁵ *Lynch* concerned a defamation action in which a female plaintiff claimed that defendant’s slanderous remarks concerning her morality caused her husband to expel her from the family home, and thus she suffered from loss of consortium.⁸²⁶ The court dismissed the case, because it found that the expulsion was not a foreseeable response to the defamatory remark.⁸²⁷ Although the technical holding seems gender neutral, “the opinions of the judges in *Lynch* displayed a consciousness of gender difference and used the dichotomy of physical and emotional harm to marginalize the interests of women.”⁸²⁸

In reaching his decision, Lord Wensleydale found that a husband suffers

822. See Elizabeth Handsley, *Mental Injury Occasioned by Harm to Another: A Feminist Critique*, 14 LAW & INEQ. J. 391, 458 (1996). See also Leslie Bender, *A Lawyer’s Primer on Feminist Theory and Tort*, 38 J. LEGAL EDUC. 3, 20 (1988) (“Men have and have had the power to set the standards in law and in our ideology and have used that power to subordinate women.”). See also Anita Bernstein, *Treating Sexual Harassment with Respect*, 111 HARV. L. REV. 445, 457 (1997) (“Rousseau denounced women as incapable of thought and unsuited to education; . . . Hobbes, Locke, and Adam Smith, . . . presume[d] the absence of women’s thought, consent, and decision making.”).

823. 132 Eng. Rep. 490 (P.C. 1837). *Vahghan* is noted for establishing the reasonable or prudent man standard. See *id.* at 493-94. See also *Blyth v. Birmingham Waterworks Co.*, 156 Eng. Rep. 1047, 1049 (Ex. 1856). But see Warren A. Seavey, *Negligence—Subjective or Objective?*, 41 HARV. L. REV. 1, 27 (1927) (stating that the reasonable man may not be completely defined by use of objective standards).

824. Leslie Bender, *Teaching Torts As If Gender Matters: Intentional Torts*, 2 VA. J. SOC. POL’Y & L., Fall 1994, at 142.

825. 11 Eng. Rep. 854 (H.L. 1861).

826. See *id.* at 858.

827. See *id.* at 863.

828. Martha Chamallas & Linda K. Kerber, *Women, Mothers, and the Law of Fright: A History*, 88 MICH. L. REV. 814, 816 (1990).

pecuniary harm as a result of loss of consortium because a wife's services are material. He stated, however, that, when a wife suffers from loss of consortium, her loss is emotional and mental.⁸²⁹ Therefore, he stated, the wife could not recover damages because "the law cannot value, and does not pretend to redress, [mental pain or anxiety] when the unlawful act complained of causes that alone."⁸³⁰ Lord Wensleydale reasoned that the husband, who alone has all the property of the married parties, may repair [his loss] by hiring another servant [to replace the loss of his wife's services]; but the wife sustains only the loss of the comfort of her husband's society and affectionate attention, which the law cannot estimate or remedy."⁸³¹

Lord Campbell alternately compared the injuries sustained by a husband and a wife when their spouse commits adultery. Campbell considered the injuries sustained by a husband due to his wife's adultery similar to that of property loss.⁸³² A wife's adulterous act completely deprived the husband of his property permanently, regardless of his subjective response.⁸³³ Thus, on the one hand, the court viewed the husband's loss as an objective and complete loss of the value of a wife.⁸³⁴ But, on the other hand, the court considered the same injury to a wife as not permanent, as dependent on the wife's subjective response, and of a class of hurt feelings that could not be compensated.⁸³⁵ "This legally constructed asymmetry resulted in gender disadvantage to women."⁸³⁶

Chamallas and Kerber point out that:

By locating the wife's injury within her own mind, the court could dismiss the harm and blame the victim for not mitigating her own injuries This subjective/objective dichotomy resembles the gendered nature of the material/emotional dichotomy in the loss of consortium: the harm to the woman is conceived of as subjective; the same harm to the man is viewed as objective.⁸³⁷

Although the opinion is discriminatory, the rule of law established in *Lynch*, namely that mental disturbance alone is not actionable, was adopted by later courts but, without reliance on such discriminatory reasoning.⁸³⁸

829. *Lynch*, 11 Eng. Rep. at 863.

830. *Id.* at 863.

831. *Id.*

832. *Id.* at 860.

833. *See id.*

834. *See id.*

835. *See Lynch*, 11 Eng. Rep. at 863.

836. Chamallas & Kerber, *supra* note 828, at 818.

837. Chamallas & Kerber, *supra* note 828, at 818-19.

838. Martha Chamallas, *The Architecture of Bias: Deep Structures in Tort Law*, 146 U. PA. L.

Instead, subsequent decisions dealing with claims for emotional distress disallowed recovery for various other reasons.⁸³⁹

Prosser and Keeton have noted that these earlier cases denied relief to plaintiffs because “mental disturbance cannot be measured in terms of money, and so cannot serve in itself as a basis for the action; . . . its physical consequences are too remote, and so not ‘proximately caused’; . . . there is a lack of precedent, and . . . a vast increase in litigation would follow.”⁸⁴⁰ Though these reasons have also been rejected over time, courts more recently have been reluctant to allow damages for mental disturbance because of a belief that these claims are trivial, may be fraudulent, and impose disproportional financial burdens on defendants whose actions are merely negligent.⁸⁴¹ To alleviate those concerns, the majority of courts today do not allow recovery in emotional disturbance cases without the presence of physical illness or consequences.⁸⁴² The modern trend is to allow relief only where there is accompanying physical injury.⁸⁴³ Some courts, however, have allowed recovery where the mental disturbance is caused by witnessing harm to another.⁸⁴⁴

Although the law has allowed damages for mental distress resulting from infliction of physical harm, the same cannot be said for fright-based physical injury cases resulting in mental distress.⁸⁴⁵ Courts historically required plaintiffs who wished to succeed on a fright-based physical injury claim to

REV. 463, 491 (1998).

839. *See id.* at 491-95.

840. W. PAGE KEETON ET AL., PROSSER & KEETON ON THE LAW OF TORTS, § 54, at 360 (5th ed. 1984) [hereinafter PROSSER & KEETON]. *See also* Chittick v. Philadelphia Rapid Transit Co., 73 A. 4 (Pa. 1909); Mitchell v. Rochester Ry. Co., 45 N.E. 354, 354 (N.Y. 1896) (“If it be admitted that no recovery can be had for fright occasioned by the negligence of another, it is somewhat difficult to understand how a defendant would be liable for its consequences. . . . [I]t is obvious that no recovery can be had for injuries resulting therefrom.”); Spade v. Lynn & Boston R.R. Co., 47 N.E. 88, 89 (Mass. 1897) (“The number of actions brought is very great. This should lead courts well to consider the grounds on which claims for compensation properly rest, and the necessary limitations of the right to recover. . . . [Otherwise,] this would open a wide door for unjust claims, which could not successfully be met.”); Lehman v. Brooklyn City R.R. Co., 47 Hun. 355 (1888); Victorian Rys. Comm’rs v. Coultas, 13 App. Cas. 222 (P.C. 1888).

841. *See* Dulieu v. White & Sons, 2 K.B. 669 (1901). Note the distinction here and the opposite principal of law applied in physical injury tort cases; for example, “the tortfeasor takes the plaintiff as he finds him.” The victim with the eggshell skull is compensated in full even when the tortfeasors conduct to another would not have resulted in such grave consequences or damages. This principal of law has long been followed and applies in negligence as well as intentional tort cases. Why should it not be applied in discrimination cases that result in nonphysical as well as physical harms—is it such a long reach for the law to develop this consistent application?

842. *See* PROSSER & KEETON, *supra* note 840, § 54, at 361.

843. *See id.* § 54, at 363.

844. *See, e.g.,* Dillon v. Legg, 441 P.2d 912 (Cal. 1968).

845. PROSSER & KEETON, *supra* note 840, § 54, at 362-63.

show “impact.”⁸⁴⁶ Thus, the plaintiff had to produce evidence showing that he or she was physically touched in some way during the events that led to the shock.⁸⁴⁷

While the impact rule seemed gender neutral, upon historical scrutiny one realizes that the requirement of “impact” in fright-based physical injury cases has disparate effects. Prosser and Keeton note that fright-based physical injury cases frequently involved miscarriages by pregnant women and even came to typify such claims.⁸⁴⁸ But fright-based miscarriages often did not involve impact.⁸⁴⁹ Therefore, the fright-based physical injury plaintiff who suffered the traumatic experience of a miscarriage was denied relief, while the plaintiff who was slightly touched brought a successful action under the “impact” rule.⁸⁵⁰

Fortunately, the “impact” rule has been eliminated in almost all jurisdictions.⁸⁵¹ Now, some jurisdictions follow the physical injury rule that allows recovery upon showing of physical injury without focusing on how the injury is brought about.⁸⁵² Other states follow the zone of danger rule that allows recovery where the plaintiff is physically put in danger by the defendant’s acts.⁸⁵³ A minority of states follow a more liberal rule that allows recovery for fright-based physical injury upon a showing of serious mental distress.⁸⁵⁴

Gender bias plays an even stronger role in claims where fright results from witnessing peril or harm to another. In 1968, the California Supreme Court decided the landmark decision of *Dillon v. Legg*.⁸⁵⁵ In this case, the court allowed a mother who witnessed her child killed by an automobile to recover damages for her mental distress, despite the fact that the mother herself was in a completely safe area and in no physical danger at the time of the accident.⁸⁵⁶ In order to reach such a result, the court departed from the zone of danger rule and allowed recovery where the plaintiff could prove that she was in physical proximity to the scene of the accident, personally observed the accident, and was closely related to the victim.⁸⁵⁷ The *Dillon*

846. *See id.* § 54, at 363.

847. *See* Handsley, *supra* note 822, at 399-400.

848. PROSSER & KEETON, *supra* note 840, § 54, at 363 & n.38.

849. *See id.*

850. *See id.* at 363-64.

851. *See* Chamallas & Kerber, *supra* note 828, at 820.

852. *See id.*

853. *See* Handsley, *supra* note 822, at 401.

854. *See* Chamallas & Kerber, *supra* note 828, at 820-21.

855. 441 P.2d 912 (Cal. 1968).

856. *See id.* at 914.

857. *See id.* at 920-21.

holding, therefore, no longer required plaintiffs to be in actual physical danger themselves and took a step to redress harms that result from caring for others and developing relationships.

Although some jurisdictions follow *Dillon* and have further developed the foreseeability guidelines of that case,⁸⁵⁸ feminist scholars have proffered that gender bias has prevented other jurisdictions from accepting the rule of *Dillon*.⁸⁵⁹ In these jurisdictions, causes of action for emotional distress

858. See PROSSER & KEETON, *supra* note 840, § 54, at 366 & n.74. See also *D'Amico v. Alvarez Shipping Co.*, 326 A.2d 129, 132 (Conn. 1973) ("Manifestly the shock and anguish of seeing their child killed in the torturous occurrence in which they all were involved must have been great and not only foreseeable, . . . but also an understandable and foreseeable direct consequence of the tortious act."); *Leong v. Takasaki*, 520 P.2d 758, 762 (Haw. 1974) ("Because other standards exist to test the authenticity of plaintiff's claim for relief, the requirement of resulting physical injury, like the requirement of physical impact, should not stand as another artificial bar to recovery, but merely be admissible as evidence of the degree of mental or emotional distress suffered."); *Barnhill v. Davis*, 300 N.W.2d 104 (Iowa 1981); *Dziokonski v. Babineau*, 380 N.E.2d 1295, 1299 (Mass. 1978) ("The threat of fraudulent claims cannot alone justify the denial of recovery in all cases. Whether a plaintiff's injuries were a reasonably foreseeable consequence of the defendant's negligence and whether the defendant caused those injuries are best left to determination in the normal manner before the trier of fact."); *Culbert v. Sampson's Supermarkets Inc.*, 444 A.2d 433, 437 (Me. 1982) ("We now reject the notion that the plaintiff must allege or prove physical injuries or physical manifestations of the distress, . . . as well as emotional and mental trauma, in order to prevail."); *Miller v. Cook*, 273 N.W.2d 567, 569 (Mich. 1978) ("[W]e conclude that in Michigan a cause of action does not exist for damages for mental anguish sustained upon learning of an intentional tort committed at a non-contemporaneous time upon an immediate family member."); *Portee v. Jaffee*, 417 A.2d 521 (N.J. 1980) ("[N]egligent infliction of emotional distress requires . . . (1) the death or serious physical injury of another caused by defendant's negligence; (2) a marital or intimate, familial relationship between plaintiff and the injured person; (3) observation of the death or injury at the scene of the accident; and (4) resulting severe emotional distress."); *Sinn v. Burd*, 404 A.2d 672, 677, 687 (Pa. 1979) ("The restrictiveness of the zone of danger test is glaringly apparent where it is allowed to deny recovery to a parent who has suffered emotional harm from witnessing a tortious assault upon the person of his or her minor child [W]e are satisfied that public policy demands that we not permit the application of the zone of danger concept to deny recovery merely because of the nature of the damage."); *D'Ambra v. United States*, 338 A.2d 524, 531 (R.I. 1975) (holding "that a nonnegligent mother, who although suffering no physical impact suffers serious mental and emotional . . . from actually witnessing the death of her nonnegligent minor child as a direct result of the defendant's negligence, may maintain an action for negligent infliction of emotional distress"); *General Motors Corp. v. Grizzle*, 642 S.W.2d 837, 844 (Tex. 1982) (holding that appellant "could not recover for her mental injury because she neither saw, heard, or otherwise sensorily perceived the accident"). However, some courts require physical injuries to sustain a cause of action for mental distress. *Compare Corso v. Merrill*, 406 A.2d 300 (N.H. 1979) ("[T]he harm for which plaintiff seeks to recover must be susceptible to some form of objective medical determination and proved through qualified medical witnesses.").

859. See Chamallas & Kerber, *supra* note 828, at 821-23; Handsley, *supra* note 822, at 461 ("Requirements tying injury to physical phenomena, such as the impact rule, the zone of danger rule, the *Dillon* criteria, and the physical manifestation rule begin to make sense as products of an inability to come to terms with the relationship among the mind, the body, and the emotions."); Deborah K. Hepler, *Providing Creative Remedies to Bystander Emotional Distress Victims: A Feminist Perspective*, 14 N. ILL. U. L. REV. 71, 83-84 (1993) ("Tort law from a feminist perspective would focus on interdependence and collective responsibility rather than individuality, and on safety and help for the injured party rather than on 'reasonableness' and economic efficiency.").

resulting from peril or harm to another are not generally accepted because “[s]ociety’s interest in protecting the parent-child relationship . . . has been offset by an equal interest in preserving the underlying bias against the rights of women.”⁸⁶⁰

Elizabeth Handsley explains the denigrated status of claims for emotional distress resulting from peril or harm to another from an epistemological standpoint.⁸⁶¹ She proposes that “[t]he law has applied a masculine epistemology to claims relating to mental injury.”⁸⁶² As a result, the law has “insisted on a mind-body split to differentiate mental from other injuries” and “relied on scientific evidence to prove the reality and/or seriousness of the injury, rather than paying attention to the common experiences of women (and men) in this society.”⁸⁶³ Because of this masculine epistemology, *Dillon* is not generally accepted because mental harm as a result of injury to another is an “injury to an interest defined as peculiarly feminine: that of caring and relationships.”⁸⁶⁴

2. *Psychoanalytic Theory and § 104(a)(2)*

Historically, the unconscious has played an integral role in creating overtly and covertly sexist attitudes in tort law. The reasonable man standard established in *Vaughan*, and the opinions regarding emotional stress claims in *Lynch*, both exemplify overtly sexist attitudes produced by the unconscious. The “reasonable man” standard adopted from *Vaughan* was decided in nineteenth century England, a society where women were not equal to men, were regarded as property, and were disenfranchised.⁸⁶⁵ Given the fact that women were not treated as equals, traits associated with men comprised the “reasonable man” standard.⁸⁶⁶ This trait-association evidences poor “reality testing” that fulfills the psychological function of preserving male dominance over females. At that time, male dominance was preserved by the use of socially accepted pseudo-reasons (i.e. women are not equal to men and are property) that are themselves overtly sexist and were clearly established to preserve male dominance. For example, Lord Wensleydale and Lord Campbell relied on the notion that women are property of their husbands in order to reach their respective decisions. By so doing, they

860. Hepler, *supra* note 859, at 97-98.

861. See Handsley, *supra* note 822, at 460, 486.

862. *Id.* at 392.

863. *Id.* at 486-87.

864. *Id.* at 486.

865. See Collins, *supra* note 659, at 317-18.

866. See Handsley, *supra* note 822, at 392.

accepted the Cartesian subjective/objective dichotomy, which in turn created the material/emotional dichotomy in tort law.⁸⁶⁷

The gender-biased “reasonable man” standard established in *Vaughan* may have played a role in *Lynch*. In patriarchal cultures, women have been considered as emotional beings, while men have not.⁸⁶⁸ Arguably, since the “reasonable man” is comprised of male traits, the “reasonable man” would not be considered an emotional being.⁸⁶⁹ Injury to emotions, therefore, may not constitute harm to the “reasonable man.” As a result, any claim brought for harms to emotions alone would be dismissed because the female plaintiff, unlike the objectively “reasonable man,” would be seen as someone unique with an “eggshell psyche,” weak, feeble, and suffering from self-inflicted harm.⁸⁷⁰ In that light, the *Lynch* opinion appears to have been a product of unconscious sexism associated with the “reasonable man” standard that demeaned women’s position in society. Despite the more liberated status of women in today’s society, the rule of law established in *Lynch* enjoyed such historical acceptance that its deep impact still affects the tort of emotional distress.

Because overt sexism has been socially rejected in today’s society, covert sexism has become the more prevalent form.⁸⁷¹ The ego must adjust to new societal norms, and therefore it must repress or disguise sexist ideas or feelings seated deeply in the unconscious.

Ego-disguise is arguably evidenced today in renaming the “reasonable man” standard to the “reasonable person” standard which uses policy-oriented justifications to deny claims for emotional distress, and which use judicially crafted rules to limit the type of plaintiffs who can recover for emotional harm. This judicial wizardry, though purporting to be neutral, unconsciously preserves what sexist reasoning had previously attempted to maintain, even though it uses nice language that better conforms to a changing society. “As our social sensitivity to sexism developed, our legal institutions did the ‘gentlemanly’ thing and substituted the neutral word ‘person’ for ‘man.’ . . . Although tort law protected itself from allegations of

867. See Chamallas & Kerber, *supra* note 828, at 818-19.

868. See Michele A. Paludi & Lisa A. Strayer, *What's in an Author's Name? Differential Evaluations of Performance as a Function of Author's Name*, 12 SEX ROLES 353, 353 (1985).

869. See Handsley, *supra* note 822, at 392.

870. Leslie Benton Sandor & Carol Berry, *Recovery for Negligent Infliction of Emotional Distress Attendant to Economic Loss: A Reassessment*, 37 ARIZ. L. REV. 1247, 1252 (1995).

871. See Tracy Anbinder Baron, Comment, *Keeping Women Out of the Executive Suite: The Courts' Failure to Apply Title VII Scrutiny to Upper-Level Jobs*, 143 U. PA. L. REV. 267, 304 (1994); Susanne M. Browne, Note, *Due Process and Equal Protection Challenges to the Inadequate Response of the Police in Domestic Violence Situations*, 68 S. CAL. L. REV. 1295, 1330-31 (1995).

sexism, it did not change its content and character.”⁸⁷²

Despite the name change, the “reasonable person” standard, for example, has been criticized as keeping the same gender as the “reasonable man” standard. Handsley notes that “the law generally expects and rewards ‘reasonableness’—a trait culturally associated with men—and fails to require us to be consciously caring and responsible towards each other—traits culturally associated with women.”⁸⁷³

Nineteenth-century cases following *Lynch* did not rely on overtly sexist rationale. Instead, those cases reached similar results with the use of gender neutral justifications. In the 1940s, gender-neutral justifications were definitively rejected,⁸⁷⁴ which revealed the conscious bias of those nineteenth-century rationales. But, in a society beginning to reject such discriminatory assumptions, this change may have only produced the repression of sexist beliefs.

The impact rule prevented fright-based physical injury plaintiffs who suffered miscarriages (the type of plaintiffs who typified claims for mental disturbance with resulting physical injury) from recovery, while the infrequent plaintiff who suffered dust in the eye and smoke inhalation

872. Bender, *supra* note 824, at 22. See also Lucinda M. Finley, *A Break in the Silence: Including Women's Issues in a Torts Course*, 1 YALE J.L. & FEMINISM 41, 57 (1989) (finding that the reasonable person “standard is an example of a supposedly neutral rule which may actually be suffused with the male perspective and with notions of the male ideal”).

873. Handsley, *supra* note 822, at 392.

874. See G. EDWARD WHITE, *TORT LAW IN AMERICA: AN INTELLECTUAL HISTORY* 105 (1980). The new line of justifications for denying redress for emotional harm claims are based in beliefs that such claims are trivial, may be fraudulent, impose disproportional financial burdens on defendants whose actions are merely negligent, and inflict great administrative burdens upon the court system. See Handsley, *supra* note 822, at 424. These justifications may also be the product of unconscious sexist attitudes. They have been heavily criticized because the rule does not necessarily address the concerns. Medical advances have shown that claims for emotional injury are far from trivial. See *id.* at 425. Furthermore, insinuations that all physical injuries are more severe than all mental injuries is illogical. See *id.* at 425-26. The rule barring all claims based solely upon emotional injury does little or nothing to prevent trivial claims from reaching the courts. See *id.* at 427. The contention that emotional injuries are somehow more easily feigned than physical injuries lacks any sound logical basis, since viable means such as medical expert testimony, are available to assure genuineness of claims without resorting to the physical and nonphysical distinction. See *id.* Moreover, the tort system does not concentrate on the effects that compensation will have on the wrongdoer, but rather on the need for compensation itself. See *id.* at 433. A deserving plaintiff should never be denied recovery simply because of the burden that recovery may impose upon the tortfeasor. See *id.* The rule disallowing mental harms has no bearing on the apprehension evident in courts that too many claims would result otherwise. See *id.* at 436-37. The courts fail to realize that “unjust rules which are out of step with social standards are more likely to give rise to litigation”. *Id.* at 437. This is due to the fact that society, and in turn the legal profession, will become dissatisfied and attempt to overturn such rules. See *id.* It is argued that “[a] clear rejection of restrictive liability rules . . . may in fact reduce the volume of litigation . . . because defendants will . . . be more inclined to settle.” *Id.*

successfully brought an action.⁸⁷⁵

Although the impact rule has been rejected in almost all states, a similar result may be reached under the zone of danger rule.⁸⁷⁶ Under this rule, a woman can still suffer a miscarriage from fright and not recover. If she is not within a zone of physical danger, recovery may be denied.⁸⁷⁷ Both the impact rule and the zone of damage rule are suspect because these legal rules do not “tie recovery to the degree of tortiousness in the defendant’s act, nor to the extent of harm suffered.”⁸⁷⁸ Although troubling, results such as these are not surprising since “in a gendered world, injuries are socially constructed so that the gender of the person claiming a loss can affect the legal conceptualization of the harm.”⁸⁷⁹

Although the law has changed since *Lynch* and its progeny, the foundational decisions impeding legal recognition of emotional harms are deeply entrenched in the law. Even today the majority of courts follow the material/emotional dichotomy by not allowing recovery in emotional disturbance cases without physical illness or consequences,⁸⁸⁰ and regard individuals who bring claims for emotional distress as weak, feeble, worthless, and suffering from self-inflicted harm.⁸⁸¹

Given this historical background, it is not surprising that the present day § 104(a)(2) treats individuals with physical injuries differently from individuals with nonphysical injuries. In contrast to law’s material/emotional dichotomy, however, medical research over the past 138 years has demonstrated that emotional and physical pain are not quantitatively different.⁸⁸² So why is there a major discrepancy between the law and medical research? Perhaps legal lack of knowledge about medical studies in the field of pain research is not the real reason why § 104(a)(2) still persists in maintaining its physical versus nonphysical distinction. Perhaps instead

875. PROSSER & KEETON, *supra* note 840, § 54, at 363-64. *See also* Porter v. Delaware L. & W.R. Co., 63 A. 860 (Del. 1906) (recovering damages under the impact rule for dust in the eye); Morton v. Stack, 170 N.E. 869 (Ohio 1930) (recovering for smoke inhalation).

876. PROSSER & KEETON, *supra* note 840, § 54, at 364-65.

877. *See, e.g.*, Bourhill v. Young, 1943 App. Cas. 92 (appeal taken from Second Division of Court of Session 1941 S.C. 395).

878. Handsley, *supra* note 822, at 434.

879. Chamallas & Kerber, *supra* note 828, at 816. *See also* Carl Tobias, *Gender Issues and the Prosser, Wade, and Schwartz Torts Casebook*, 18 GOLDEN GATE U. L. REV. 495, 505-06 (1988) (stating that “nearly all of the cases included in the notes introducing historical material on the independent cause of action for mental distress [of the Prosser, Wade, and Schwartz Torts Casebook] involve[d] females who appear gullible, stupid, or weak, thus reaffirming notions of women’s inferiority”).

880. PROSSER & KEETON, *supra* note 840, § 54, at 361.

881. *See* Sandor & Berry, *supra* note 870, at 1252.

882. *See* WHITE, *supra* note 874, at 102-04.

the real reason is the discriminatory perception that those who bring claims involving emotional distress are weak and suffer from self-inflicted harms. Such a perception would be a product of the both overtly and covertly unconscious sexism flowing from *Lynch* and its progeny, coupled with other forms of unconscious discrimination by the courts and the Congress concerning the current status of § 104(a)(2).

The case law that led up to the 1996 amendments to § 104(a)(2),⁸⁸³ the legislative attempts in 1989 and 1995 to change § 104(a)(2),⁸⁸⁴ and the 1996 amendments to § 104(a)(2)⁸⁸⁵ all exhibit covertly unconscious discrimination. As we have seen, because our society does not condone race, sex, age, disability, nationality, or religious discrimination, hidden prejudice has had to become the more common form of discrimination. The jumps in logic, grafting on of language, contortion of analytical framework, and de-evolution of the term damages in § 104(a)(2) case law leading up to the 1996 amendments,⁸⁸⁶ backdoor judicial and legislative tort reform,⁸⁸⁷ and the couching of the discriminatory 1996 amendment in a taxing statute, all evidence ego-adaptation, repression, and disguise of discriminatory ideas, through the use of subterfuges that ease the guilt of deeply seeded unconscious discrimination.

3. *Cognitive Theory and § 104(a)(2)*

Under the cognitive theory, because society views emotional-distress plaintiffs as weak, feeble, and suffering from self-inflicted injury, an individual will learn (through the process of assimilation) early on in life that people who claim to suffer from emotional harm have a weak psyche.⁸⁸⁸ Thus victims of dignitary torts such as Title VII, ADEA, and ADA plaintiffs may be stereotyped in a similar manner, because their various claims all involve redress for emotional harms.

Black men have been stereotyped as “lazy/undisciplined/always late/ . . . unqualified but protected by affirmative action/ . . . [and] less intelligent than other racial or ethnic groups.”⁸⁸⁹ Black women have been categorized as “incompetent/educationally deficient/aggressive/militant/hostile/lazy/sly and

883. *See supra* Part II.A-K.

884. *See supra* Part II.L.

885. *See id.*

886. *See* Part II.A-K.

887. *See supra* Part IV.B-C.

888. *See supra* Part VII.A.2.

889. FEDERAL GLASS CEILING COMMISSION, GOOD FOR BUSINESS: MAKING FULL USE OF THE NATION'S HUMAN CAPITAL 71 (1995).

untrustworthy.”⁸⁹⁰ Women as a group have been perceived as weak and emotional.⁸⁹¹ The aged have been labeled “unhappy . . . disengage[d] from society, . . . inflexible and set in their ways, and hav[ing] lessened intelligence, levels of information and knowledge, and productivity.”⁸⁹² The disabled have been looked upon as dependent, childlike,⁸⁹³ “less intelligent, less able to make the ‘right’ decisions, less ‘realistic,’ less logical, and less able to determine his own life than a nondisabled person.”⁸⁹⁴

Under cognitive theory, these stereotypes are learned through assimilation and may or may not be rebutted, depending on the individual’s experience with a member of an out-group.⁸⁹⁵ But when a black man who is seen as unqualified, a black woman who is looked upon as lazy, a woman who is stereotyped as emotional and weak, an elderly person who is regarded as unproductive, and a disabled person who is thought to be less intelligent, bring claims to redress emotional harms resulting from discrimination, these stereotypes are resurrected and reinforced by the law that regards emotional distress claimants as weak, feeble, and suffering from self-inflicted harm.⁸⁹⁶ Thus, at the same time that racial prejudices are being reinforced, prejudice towards emotional distress victims as a class is being strengthened. Individual prejudice toward emotional distress victims as a class is reinforced as they are categorized into the the stereotyped shortcomings associated with out-group plaintiffs.⁸⁹⁷

When a decision maker believes that the § 104(a)(2) exclusion should be limited to damages awarded on account of physical injuries, probably, that person views such decisions as unrelated to race, sex, age, disability, national origin, or religious discrimination, as well as to discrimination against emotional distress victims.⁸⁹⁸ The decision maker simply perceives the victim of physical injury as more deserving of a tax break than the victim of a nonphysical injury.⁸⁹⁹ “Moreover, he has probably also learned an explicit lesson of which he is very much aware: Good, law-abiding people do not

890. *Id.*

891. See CATHARINE A. MACKINNON, *SEXUAL HARASSMENT OF WORKING WOMEN* 155-56 (1979).

892. LEVINE, *supra* note 776, at 125.

893. See Mary D. Romano, *Sex and Disability*, in *DISABLED PERSONS AS SECOND-CLASS CITIZENS* 64, 67 (Myron G. Eisenberg et al. eds., 1982).

894. Constantina Safiliou-Rothschild, *Disabled Persons’ Self-Definitions and Their Implications for Rehabilitation*, in *THE SOCIOLOGY OF PHYSICAL DISABILITY AND REHABILITATION* 39, 39 (Gary L. Albrecht ed., 1976).

895. See *supra* Part VII.A.2.

896. See *id.*

897. See *id.*

898. Compare Lawrence, *supra* note 791, at 343.

899. See *id.*

judge others on the basis of race[,]" gender, age, disability, national origin, or religion.⁹⁰⁰ "Even the most thorough investigation of conscious motive will not uncover the . . . stereotype[s] that has influenced his decision."⁹⁰¹ The decision maker remains unaware of powerful stereotypes including those embodied in the modern legal tradition that have biased the decision.⁹⁰²

C. Conclusion to Part VII

The conscious and unconscious gender bias examined in this Part explains the historically disparate treatment of all tort plaintiffs with nonphysical damages. Gender bias, like racial, age, and disability biases is deep-seeded in a tort law. It is rooted in allegedly able-bodied, white, male norms, like the reasonable man/person standard.

Because § 104(a)(2) concerns nonphysical damages, it is directly subject to this historical bias. Given the fact that § 104(a)(2) excludes plaintiffs who bring dignitary claims, unconscious sexism, racism, and ageism play a role (in addition to the discriminatory material/emotional dichotomy). Thus the currently discriminatory status of § 104(a)(2) is explained.

VIII. CONCLUSION: A CALL FOR CHANGE

The Twentieth Century has witnessed the struggle for equality by many oppressed groups marginalized by the dominance of a primarily white male power structure. In the wake of centuries of discrimination against people of color and women, of sustained prejudice against the aged, and of the daily hurdles faced by the physically and mentally challenged, the new goal of equal treatment and access has been articulated for all people by Congress in various federal legislative enactments during the last half of the Twentieth Century.⁹⁰³ The inherent dignity and legitimate aspirations of each and every human being have become a new focal point in society's collective

900. *Id.*

901. *Id.* See also Krieger, *supra* note 811, at 1216-17. Krieger argues that "[a] substantial body of empirical and theoretical work supports the proposition that cognitive biases in social judgment operate automatically and must be controlled, if at all, through subsequent 'mental correction.'" *Id.* at 1216. If this is true then the stereotypes we learn through assimilation are projected unconsciously. Lawrence does not go so far as to say this in his cognitive theory breakdown. See Lawrence, *supra* note 791, at 336-39. However, he does allude to this in a hypothetical in the "Unconscious Racism in Everyday Life" section. See *id.* at 343. Even though Lawrence does not state whether he is applying psychoanalytic theory or cognitive theory in the hypothetical, language in the paragraph such as "mass media," "portrayed in the stereotyped roles," and "lesson is not explicit" supports the proposition that he is applying the cognitive theory. See *id.*

902. *Id.*

903. See discussion *supra* Part IV.4.

consciousness.

In light of this new and worthy goal, we have reviewed the history of § 104(a)(2). In reaching decisions, early administrative opinions misapplied, confused, and entangled the concepts of human capital and income.⁹⁰⁴ This embroilment paved the way for future bewilderment in the adjudication of damage award exclusion tax litigation. Perplexity continued until the 1955 Supreme Court decision of *Glenshaw Glass*, which redefined income to include any “undeniable accession to wealth, clearly realized, and over which the taxpayer [had] complete dominion and control.”⁹⁰⁵ After *Glenshaw Glass*, taxpayers structured their settlements to come within the statutory exclusion. As a result, the courts backlashed and crafted tests to filter out undeserving claims under § 104(a)(2). It was not until the early and mid 80’s, some thirty years after *Glenshaw Glass*, that concrete principles were set for analyzing § 104(a)(2) litigation.

The historical judicial precedents lend support to the argument that the § 104(a)(2) exclusion should apply to nonphysical personal injuries. The Ninth Circuit in *Roemer* focused on whether the nature of the claim was tort or tort-like in determining the applicability of the exclusion.⁹⁰⁶ The court properly looked to the nature of the claim in interpreting regulation § 1.104-1(c). This regulation has been consistently analyzed and interpreted by courts until the Supreme Court reversed the analysis in the *Burke* case.⁹⁰⁷

In *Threlkeld*, the Tax Court further developed *Roemer*, by examining the nature of the taxpayer’s injury rather than the nature of the economic consequences flowing from the injury.⁹⁰⁸ In analyzing what constitutes a personal injury, the court stated that the concept has long included nonphysical as well as physical injuries. The court elucidated the definition of personal injury as injuries arising from the violation of rights that inhere in a human being, legally protected by virtue of being a person in the eyes of the law.⁹⁰⁹

It was against this background that the courts decided the ADEA cases of *Rickel*, *Pistillo* and *Redfield*, where the Third, Sixth, and Ninth Circuits respectively held that the age discrimination personal injury damage awards were fully excludable under § 104(a)(2).⁹¹⁰

Beginning in 1989, however, when all the major § 104(a)(2) cases began

904. See discussion *supra* Part II.A-B.

905. *Comm’r v. Glenshaw Glass*, 348 U.S. 426, 431 (1955).

906. See discussion *supra* Part II.I.

907. See *supra* notes 299-311 and accompanying text.

908. See *supra* notes 244-58 and accompanying text.

909. See *supra* notes 256-57 and accompanying text.

910. See *supra* notes 282-89 and accompanying text.

to deal with Title VII and ADEA damage awards, previous principles were abandoned. Facing a perceived flood of federal discrimination litigation, the courts began contorting the prior § 104(a)(2) analysis. In *Sparrow*, the D.C. Circuit changed course and rejected *Threlkeld*, *Roemer*, and their progeny and focused on the nature of Title VII's damages in order to determine the applicability of the § 104(a)(2) exclusion.⁹¹¹ It was also in 1989 that Congress amended § 104(a)(2) to disallow the exclusion of punitive damage awards from income where the underlying injury was nonphysical.⁹¹²

Three years later, in *Burke*, the Supreme Court began its short, yet detrimental, involvement in § 104(a)(2). In *Burke*, the Supreme Court contorted the "tort or tort-like test" from an analysis of the nature of the claim as inferred from the injury to an analysis of the nature of the claim as inferred from Title VII's remedial scheme. The Court's remedial focus emerged as the hegemonic sword of domination in its analysis, mortally wounding the personal nature of a gender discrimination claim.⁹¹³ Then in 1995, the Supreme Court further twisted the tort or tort-like test, and grafted on new independent prerequisites for excludability in *Schleier*.⁹¹⁴

Between its 1992 decision in *Burke* and its 1995 decision in *Schleier*, the Supreme Court manufactured a § 104(a)(2) analytical framework that denigrated and marginalized victims of dignitary torts. *Burke* and *Schleier* created an irrational and scientifically unsupported tort hierarchy, privileging certain successful tort plaintiffs with income exclusion over similarly situated tort-like discrimination plaintiffs. The Court determined that plaintiffs with successful discrimination claims, unlike certain tort plaintiffs suffering physical injuries, were unworthy of the tax exclusion, despite the fact that the effects of discrimination can be as or more severe and permanent than any physical injuries.

Although the members of today's society look back on the strides of the civil rights era with a high degree of social pride, unknown to most is the reality that the civil rights revolution precipitated the backlash that caused the double discrimination against civil rights plaintiffs and legally sanctioned today by § 104(a)(2). In 1996, the Treasury and Congress, influenced by the *Schleier* decision, limited the § 104(a)(2) exclusion to damages on account of physical injury or physical sickness.⁹¹⁵ The 1996 amendments to § 104(a)(2) targeted people who suffered from discrimination by not allowing those

911. See *supra* notes 290-98 and accompanying text.

912. See *supra* note 386 and accompanying text.

913. See discussion *supra* Parts II.K, V.B.

914. See *id.*

915. See *supra* note 396 and accompanying text.

successful claimants' damage awards to fall under its exclusion. Such individuals excluded from § 104(a)(2) already have proved that they were victims of discrimination by prevailing in their dignitary tort claims under state and federal statutes. Congress's distinction covering those plaintiffs with physical personal injuries and excluding those plaintiffs with nonphysical personal injuries, once again discriminates against the dignitary tort victim.

Personal injuries resulting from discrimination, even in the mildest form, are the result of an invasion or violation of a person's dignity. This personal injury results in damage to nonappraisable, priceless, and intangible personal human capital. As Professor Stephan postulates, human capital is valued based upon a person's future satisfactions.⁹¹⁶ Thus, human capital includes the expectations and aspirations that a person can command as part of a full and productive life. Acts of discrimination cause irreparable injury to human capital, and monetary damages are transfers of property that while inadequate, attempt to restore human capital and redress the injury. Just as no amount of money can adequately compensate for an injury to priceless human capital, money is also inadequate to replace and redress a person's severed finger, arm, or leg.⁹¹⁷

The scientific studies, statistical evidence, and anecdotal accounts discussed in Part VI document the harmful effects of age, disability, race, and gender discrimination. These forms of discrimination frequently cause the same type of psychological, physical, and economic suffering to victims as well as the same type of social costs to society-at-large. In the end, the victim, the family, friends and associates of the victim and society as a whole suffer the negative effects of each type of discrimination.

With such cumulative evidence available to Congress and the courts, one would think that today's enlightened decision makers would support equal tax treatment of victims with physical and nonphysical injuries. The policy justifications to support taxing statutes show clearly that victims of nonphysical injuries deserve the § 104(a)(2) exclusion as much as victims of physical injuries.⁹¹⁸ Yet the double discrimination continues. Unconscious discrimination likely manifested in back door legislative and judicial tort reform and influenced the elimination of the § 104(a)(2) exclusion for victims of discrimination.⁹¹⁹ Major federal statutes serve as powerful landmarks defining an expansive congressional policy to deter acts that

916. See *supra* note 453 and accompanying text.

917. See discussion *supra* Part III.H.

918. See discussion *supra* Part III.

919. See discussion *supra* Part VII.

violate the dignity, equality, and spirit of a human person. Yet resistance to this civil rights legislation covertly appeared in the context of the amendment to § 104(a)(2). Through a restrictive interpretation of § 104(a)(2), lawmakers and the judiciary rationalized and legitimized resolving conflicts that marginalize the rights of minorities and, in a subtle way, reassert their own position of privilege.⁹²⁰

By recognizing, rather than marginalizing, the severe personal injuries suffered by victims of discrimination, Congress should amend § 104(a)(2). Returning the income tax exclusion for victims of discrimination would be consistent with the overall congressional policy to eliminate discrimination.⁹²¹ Moreover, reinstatement of the exclusion for victims of nonphysical injuries could be made virtually revenue neutral if Congress were to disallow the income tax deduction for payments made by the tortfeasor. Disallowing the tax deduction for discrimination payments would also be consistent with the broader and more pervasive congressional policy to rid our society of discrimination in all its forms. Providing a tax benefit through a deduction to tortfeasors who violate federal laws prohibiting discrimination is inconsistent with the primary congressional policy of eliminating discrimination. The government and ultimately all taxpayers collectively should not subsidize payments incurred by those who discriminate through an income tax deduction. Congress should deny deductions to those who discriminate in the same manner as it does for those who traffic in drugs.⁹²² These activities are extremely harmful to society and should not be economically subsidized by the tax law.

As a matter of policy, taxing statutes should not be inconsistent with other congressional policies. Legislators and scholars need to examine tax laws carefully to determine if in application the statute furthers an activity or enterprise condemned by society. The proposed amendment to § 104(a)(2) would send an important message, reinforcing in the Twenty-First Century, Congress's commitment to eradicating discrimination in America.

920. See discussion *supra* Part VII.

921. See discussion *supra* Part IV.A.

922. See I.R.C. §§ 280E, 25A(b)(2)D.