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Wrongful Life And Wrongful Birth Lawsuits Raise Tax Issues

A wrongful birth action is brought by parents to recover for the birth of an unhealthy child. The parents' right to recover is based on the defendant's negligent deprivation of the parents' right not to conceive the child or to prevent the child's birth. See [Is 'Wrongful Birth' Malpractice?](#) A wrongful life action is brought by the child and essentially parallels a wrongful birth action.



Image via healthcare.gov

State laws vary in allowing one type of suit, both, or neither. See [A Wrongful Birth?](#) But if a parent or child sues and recovers a settlement or judgment, is it taxable? You might assume the answer would be clear.

After all, damages for personal physical injuries (like an auto accident or slip and fall case) are tax-free. See [IRS Issues New Rules For Tax-Free Legal Settlements](#). So are damages for physical sickness. But punitive damages and interest are taxable, as are damages for mere emotional distress. See [IRS To Collect on Italian Cruise Ship Settlements](#).

Emotional Distress? Up until 1996, just about anything qualified as excludable personal injury damages, including emotional distress, defamation or invasion of privacy. See [Don't Fail To Consider Taxes](#)

[When Settling Litigation](#). In 1996, the tax code was changed so only recoveries for personal **physical** injuries or **physical** sickness qualify. See [Is Physical Sickness the New Emotional Distress?](#) Frustrated tax lawyers and accountants have repeatedly asked for regulatory guidance, and the U.S. Tax Court faces many cases over what's taxed. See [Taxpayer Advocate 2009 Annual Report to Congress](#).

If your damages aren't physical enough, they are taxed. Unfortunately, the IRS is notoriously tough on just what is physical. Traditionally it means injuries you can see like bruises or broken bones.

How do wrongful life and wrongful birth damages stack up to this standard? For a wrongful life claim, a plaintiff child's personal physical injury or physical sickness may be evident at the time of suit. Damages are usually assessed based on the additional medical and special needs of the child. Arguably that goes a long way toward the tax-free standard.

The causal connection may be even more attenuated in a wrongful birth claim. It may be possible to argue that a defendant's actions constituted physical harm to the mother and thus should be tax-free. With both types of cases, though, be careful, as the tax authorities aren't clear.

Pay attention to the particular language in the settlement agreement as it can matter. So can tax reporting. Consider these issues **before** the settlement documents are finalized. See [Don't Fail To Consider Taxes When Settling Litigation](#). After all, there's a big difference between taxable and tax-free.

For more, see:

[Arizona joins states banning wrongful birth litigation](#)

[IRS Issues New Rules For Tax-Free Legal Settlements](#)

[Damages Are Taxable, Even for "Political Discrimination" Says IRS](#)

[AMT Problems For Attorney Fees Remain](#)

[Will BP Oil Spill Victims Pay Tax On \\$7.8B Settlement?](#)

[Bar Is Burned Down, Condemned, Then Taxed!](#)

[Duke Lacrosse Tax Lien Highlights How Lawsuits Are Taxed](#)

[Tax Issues in Employment Mediations](#)

[Six Tax-Wise Ways To Reduce Your Legal Bills](#)

[Tax-Free Physical Sickness Recoveries in 2010 and Beyond](#)

[Watch Your Mail For 1099s](#)

[Address Taxes When You Mediate Civil Disputes](#)

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