Dodge's Darts Don't Pass Inspection

To the Editor:

In the February 21 issue of *Tax Notes* (p. 986), Prof. Joseph Dodge trashes the article in which I argued that, despite the 1996 changes to section 104(a)(2), recoveries for nonphysical personal injuries aren't automatically taxable ("Are Recoveries for Nonphysical Injuries Automatically Taxable?" *Tax Notes*, Dec. 6, 2004, p. 1439). Prof. Dodge condemns me for everything from mischaracterizing authority to giving "aid and comfort" (his phrase) to tax protesters.

I probably should just let this go, but, with charges like that, it's hard not to respond. (Besides, in the March 7 issue (p. 1219), Robert Wood praises Prof. Dodge's "admirable job of refuting [my] article.") I'll discuss three things: the interpretation of Rev. Rul. 74-77;[1] the relationship of my article to tax protests; and the tendency of scholars to read their own theories into the law.

Rev. Rul. 74-77 and Section 104(a)(2)

I used Rev. Rul. 74-77 to illustrate the general point that some recoveries for nonphysical personal injuries were historically understood to be nontaxable not because of a statutory exclusion like section 104(a)(2), but because they weren't considered to be income. Maybe I shouldn't have spent so much time on a now-officially-obsolete ruling that deals with recoveries for alienation of affections. (After all, who really cares about such an antediluvian cause of action?) But since Prof. Dodge challenges my interpretation at length, a few comments are in order.

First, Prof. Dodge is absolutely right on one point: I should have noted that, in the Cumulative Bulletin, Rev. Rul. 74-77 is cataloged under "Section 104 — Compensation for Injuries or Sickness." Even if a heading doesn't reflect anything that follows — and nothing in the body of Rev. Rul. 74-77 makes any mention of section 104 — we should still pay attention to the heading. It's a relevant datum, and I apologize for the omission.

But it's only one datum, and Prof. Dodge then gets just about everything else wrong in his description of Rev. Rul. 74-77. He says, for example, that "[t]he ruling is listed in the Cumulative Bulletin as being 'under' section 104 (not section 61), and the caption refers to 26 CFR 1.104-1 (not any of the section 61 regulations)."

Not true. Right after the citation to reg. section 1.104-1 are cites to section 61 and reg. section 1.61-1. And the ruling is listed under section 61 as well, with a cite to the section 61 regulations.[2]

OK, we all make mistakes, and that's a trivial one.[3] But Prof. Dodge also sees in the ruling a connection to section 104(a)(2) that just isn't there. In noting that Solicitor's Opinion 132, which had been issued in 1922,[4] was being superseded, the IRS explained that "the position stated therein is set forth in the current statute and regulations in this Rev. Rul." Prof. Dodge says that passage "obviously refers to 'statute and regulations,' namely, section 104(a)(2) and reg. section 1.104-1, both 'set forth' at the top of the ruling." And thus, concludes Dodge, we know — *obviously* — that this is really a 104(a)(2) ruling.

Wrong again. Prof. Dodge sees what he wants to see, but section 104(a)(2) *isn't* "set forth" in the ruling, either "at the top" or in the text. Yes, there's a reference "at the top" to the umbrella provision, section 104, and a regulation (section 1.104-1) that fleshes out four of the subsections of 104(a).[5] But there's no mention at all of section 104(a)(2). *None*. I did a *National Treasure*-type search to see if "104(a)(2)" might have been written in invisible ink in the C.B., but no luck.

Most important, if Prof. Dodge were right that the ruling is "obviously" grounded in section 104(a)(2), even though that subsection isn't mentioned,[6] one might have expected a paraphrase of the statute in the body of the ruling, or maybe even a quotation of relevant language. You know, statutory language occasionally matters when a statute is involved. But there's nothing like that in Rev. Rul. 74-77. As I noted in my article, the ruling simply says that "amounts received by the taxpayer as damages for

[1]1974-1 C.B. 33, *declared obsolete in* Rev. Rul. 98-37, 1998-2 C.B. 133, *Doc 98-25235, 98 TNT 153-11*.

[2]1974-1 C.B. 22.

[3]It's a peculiar mistake, nonetheless, given the point Prof. Dodge is making about the importance of headings.

[4]I-1 C.B. 92 (1922).

[5]Four of the subsections deal with "injuries or sickness." If the heading for Rev. Rul. 74-77 really has any significance by itself, the ruling could just as well be interpreted, under Prof. Dodge's analysis, as "under" section 104(a)(1), 104(a)(3), or 104(a)(4).

[6]I think the "obvious" interpretation of the clunky passage dealing with the supercession of Sol. Op. 132 is something like this: A lot had changed since 1922, including the codification of the revenue statutes and the Supreme Court's decision in *Glenshaw Glass*, and people might have reasonably wondered whether such an old opinion remained good law. Rev. Rul. 74-77 said *yes*, the Internal Revenue Code and Treasury regulations then in effect — that is, the "current statute and regulations" — hadn't changed anything. So why then catalog the ruling under section 104 as well as section 61? I can think of one good reason: If someone wanted authority about recoveries of this sort, that's where he might look.

alienation of affections or for the surrender of the custody of his child . . . are not income.'' One doesn't need section 104(a)(2) to conclude that a recovery is *not income*.

To be fair, I should note that Prof. Dodge does make one attempt to tie the ruling to statutory language. He writes, ''The text of the ruling states that the damages were for violation of a 'personal' right, and were compensatory in nature,'' and ''[t]hat characterization of the facts brings them directly within the then-applicable version of section 104(a)(2).'' The word ''personal'' does appear in the ruling, but that's about it. What the ruling actually says is that the damages ''relate to personal or family rights, not property rights.'' The difference between ''personal or family rights'' and ''property rights'' is not the distinction that, by 1974, had become important in determining whether a recovery is for a personal injury.[7] Furthermore, the last time I looked, the term ''family,'' or ''family rights,'' doesn't appear in section 104(a)(2). But if the word ''personal'' is enough to convince Prof. Dodge that the ruling is based on section 104(a)(2), so be it.

I'd nevertheless be a lot more comfortable with Prof. Dodge's position if he were simply to say, ''This ruling must have been issued under the authority of section 104(a)(2), even though nothing in the ruling says so.'' That could be right. Or he might say that nothing important turns on the interpretation of Rev. Rul. 74-77. That could be right, too. Instead, he conjures up connections to section 104(a)(2) that aren't justified by anything in the ruling.

The 'In Lieu of' test and Protesting Taxes

In my article, I suggested that, in determining whether a recovery is taxable, it might make sense to ask what the recovery takes the place of. The ''in lieu of'' test isn't perfect, but it's not crazy and it has authority behind it. Nevertheless, Prof. Dodge not only concludes that the test is improper, he charges that ''[p]roponents of the 'substitute for' theory are essentially (and I assume unintentionally) giving aid and comfort to tax protestors who claim that wages are not income under section 61.''

I should be thankful for the parenthetical, I guess: I'm only a dupe, or so it's ''assume[d],'' not a willful participant in tax protests. And if I'd known that tax protesters were poring over *Tax Notes* for subversive ideas, I'd have been more careful in my choice of topics.

I'm being sarcastic, of course, and, for this charge of Prof. Dodge's, sarcasm isn't a sufficient response. I'll therefore be blunt: The idea that my article is giving comfort to someone who claims that wages paid in Federal Reserve notes aren't income, or to others making equally preposterous claims, is ludicrous.

Reading One's Own Theories Into the Law

One of the points in my article was that some commentators ignore or downplay legal authority that conflicts with their conceptions of what the law should be. When old cases and rulings don't fit modern theoretical constructs, the cases and rulings tend to disappear from, or to be disparaged in, the commentary.

For example, in disputing the legitimacy of the ''in lieu of'' test, Prof. Dodge writes that ''[d]amages received for pain and suffering are no different from wages received for [a] dangerous and miserable job.'' Now, I understand how one might think that should be the case, but I also know that lots of reasonable folks, including judges, have thought otherwise over the years — that there's a potentially important difference between a recovery for invasion of privacy, say, and amounts received for selling one's life story. If one voluntarily relinquishes one's right to privacy in exchange for cash, one has income. In contrast, if privacy is involuntarily invaded and the victim is compensated, the result isn't so clear, except for any lost-income component of the recovery — which is what the 1996 amendments to section 104(a)(2) were directed at.

Should we be telling someone whose privacy has been invaded that the full amount of his recovery is automatically taxable? Prof. Dodge would obviously say ''yes.'' But in my article I explained why the 1996 amendments don't necessarily repudiate the old authority.

Maybe Prof. Dodge is right about what the law should be, but that's not the point. Just because Prof. Dodge considers a line of authority ''hash'' doesn't mean that the rest of us are obligated to push it to the side and devour only filets mignon.[8] Indeed, lawyers have an obligation not to ignore concoctions, as distasteful as they might be, that could be healthy for their clients. And those of us in the academy should be telling our students that, even if we don't recommend it, hash is sometimes still on the menu.

Very truly yours,

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[7]Under the regulations the key concern is (and was) whether a ''tort or tort type right[]'' is involved. Treas. reg. section 1.104-1(c).

[8]Why does the term ''hash'' have such negative connotations anyway? I actually like many types of hash — but only legal varieties, I hasten to add.