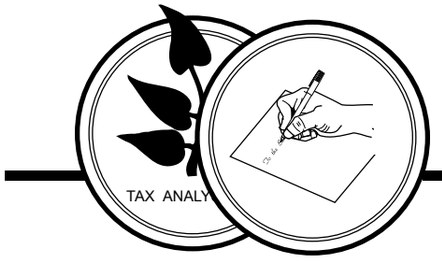

letters to the editor

Further Thoughts on The Bad *Biehl* Decision

To the Editor:

I read with interest Stephen Cohen and Laura Sager's article, "Kafka at the Tax Court: The Attorney's Fee in Employment Litigation," *Tax Notes*, Sept. 9, 2002, p. 1503. I agree that *Biehl v. Commissioner*, 118 T.C. No. 29, *Doc No. 2002-13103 (36 original pages), 2002 TNT 105-4*, is important. It is noteworthy not because of its result (one comes to expect bad results in attorneys' fee tax cases these days), but because *Biehl* considers whether attorneys' fees can be brought within the rubric of a qualified reimbursement arrangement under section 62(a)(2)(A).

> ***The message to employees in employment litigation who face this tax issue seems clear: You just can't win.***

I am no expert on those plans, but I think Cohen and Sager make a convincing case that this argument might have been a way out of the woods for many plaintiffs in employment actions. Of course, the negative effects of treating attorneys' fees as a miscellaneous itemized deduction (primarily AMT effects) are not limited to employment actions. And, it "might have" been a solution because the Tax Court didn't buy it. I thought it most interesting that the Tax Court in *Biehl* suggests that this reimbursement provision doesn't work with a former employee, saying the expense for which reimbursement is sought must be incurred in the course of the current employer-employee relationship.

One of the other techniques suggested to resolve the attorneys' fee mess in appropriate cases is to have the recipient report both the gross amount of the recovery (that is, both the client's and the attorney's portion), on that Schedule C, and to deduct the attorneys' fees on a Schedule C. That would obviate the AMT as well as the breakage that results from the 2 percent threshold on miscellaneous itemized deductions, plus phaseout of deductions and exemptions for high-income taxpayers. Of course, it would accomplish these feats at the cost of self-employment tax. The Schedule C can still be attractive in some cases, where there is a trade or business. The courts have not viewed this plan with favor, at least in employment litigation. As the First Circuit Court of Appeals pointed out in *Alexander v. Commissioner*, 72 F.3d 938 (1st Cir. 1995), an employee can hardly be said to be in the trade or business of suing his employer.

So, returning to *Biehl*, some courts may think that the lawsuit activity does not rise to the level of a trade or business, given the employment connection between plaintiff and defendant. While this employment connection may nix the Schedule C idea, *Biehl* says it is just not good enough to give rise to the kind of employer-employee relationship that section 62(a)(2)(A) requires. The message to employees in employment litigation who face this tax issue seems clear: You just can't win.

Fortunately, there are a few states (and corresponding circuit courts) where a more favorable brand of equity applies.

Very truly yours,

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