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Plaintiff Wins Roundup Weedkiller Appeal But Faces IRS Taxes

The California Court of Appeals has upheld a whopping verdict against Roundup. In 2018, jurors awarded $289 million to a man they say got cancer from Roundup weedkiller. Plaintiff Dewayne Johnson was awarded $39 million in compensatory damages, and $250 million in punitive damages. Later, the Judge reduced the $250 million punitive verdict to just under $40 million That left Mr. Johnson slated to collect $78.5 million, about half compensatory and half punitive damages. But Bayer, which now owns Roundup, appealed. The appeals court refused to reverse the decision, but it did slash the damages again. The court denied Monsanto/Bayer's motion for a new trial on condition that Johnson accept a settlement of $10.2 million in compensatory damages, plus the same amount in punitive damages. The appeal is still a win for plaintiffs, and it may influence even more suits. There are already vast numbers of cases.

How will this $20.4 million be taxed, you might ask? Johnson will have to contend with new tax rules that make how legal settlements are taxed even trickier than in the past. Under the tax bill passed in late 2017, there is a new tax on litigation settlements: no deduction for legal fees. Amazingly, many legal fees simply can't be deducted. That means Mr. Johnson must pay tax even on monies his attorney collects. That is so even though the attorney must also pay tax on the same money. If you are a plaintiff with a contingent fee lawyer, the IRS treats you as receiving 100% of the money, even if the defendant pays your lawyer *directly*. If your case is fully nontaxable, say a physical injury case that settles before trial, that causes no tax problems. But if your recovery is taxable, all *or in part*, you could be taxed on more money that you actually collect.

Up until the end of 2017, you could claim a tax deduction for your legal fees. In 2018 and thereafter, there is often *no* deduction for these legal fees. Not all lawyers' fees face this terrible tax treatment. If the lawsuit concerns the plaintiffs' trade or business, the legal fees are a business expense. Similarly, if your case involves claims against your employer, or certain whistleblower claims, those legal fees are also protected. By protected, I mean taxed to the plaintiff as gross income, but then immediately subtracted above the line.

The net result—if you can manage to claim the tricky above the line tax deduction properly on your tax return—is that you have a wash. If you recover $1 million and your lawyer takes 40%, you net $600K. And you are taxed on $600K. That seems fair, but that is only if you qualify for the above the line deduction. Mr. Johnson in the Roundup case won't qualify. He can try to work around the rules. And sometimes advice on the taxation of damage awards *before* the case settles can make a difference. But you need to be creative, to document it, and the IRS may not agree.

Awards of pre- or post-judgment interest can produce the same tax problems as punitive damages, with no deduction for legal fees. Meanwhile, defendants like Monsanto can deduct the whole verdict, even the punitive part. With the $20.4 million settlment, how much tax will Mr. Johnson pay? Let's assume that the combined contingent fees and costs Mr. Johnson pays might total 50%. If so, he gets to keep half of his $10.2 million compensatory award. His lawyer gets the other half. So Mr. Johnson collects $5.1 million that should be tax free.

What about the punitive damages? He gets half of that too, another $5.1 million. But here's where taxes get strange. He is taxed on the whole $10.2 million of punitive damages. And even though he only gets to keep $5.1 million of the punitive damages (his lawyer gets the other half), Mr. Johnson pays tax on the entire $10.2 million, with no deduction for legal fees. If you tally it, he gets cash of $10.2 million, and he pays tax on $10.2 million.

That might seem fair, except that his compensatory damages for his physical sickness are supposed to be tax-free. Compensatory damages for physical injuries or physical sickness are tax free, one of the key rules governing how settlement awards are taxed. But exactly what injuries are "physical" can sometimes seem like a chicken or egg issue. Here, the taxes are high as a result of the tax law that killed off tax deductions for many legal fees. Many plaintiffs have to get creative to deduct their legal fees under the new tax law just to get back to even.

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