

August 3, 2021

The Honorable Ron Wyden
Chairman
Senate Finance Committee
Washington, DC 20510

The Honorable Mike Crapo
Ranking Member
Senate Finance Committee
Washington, DC 20510

The Honorable Richard Neal
Chairman
House Ways and Means Committee
Washington, DC 20515

The Honorable Kevin Brady
Ranking Member
House Ways and Means Committee
Washington, DC 20515

Re: The End Double Taxation of Successful Consumer Claims Act

Dear Chairmen Wyden, Neal, and Ranking Members Crapo, Brady:

We, the undersigned public interest organizations, write in strong support of the End Double Taxation of Successful Consumer Claims Act, S. 766, H.R. 4457, introduced by Sen. Catherine Cortez Masto and Rep. Steven Horsford. For too long, taxpayers have been subject to unexpected penalties when they successfully hold bad actors accountable in court. The bill would ensure consumers in these cases are not unfairly taxed on funds they do not receive.

Specifically, when consumers win or settle a legal claim, they are often able to recover their legal expenses under various state and federal laws. These recovered funds are not paid to the consumers but to their attorneys for their work.

Under current tax law, when a consumer successfully brings a case, their entire recovery is considered taxable income. This includes recovered legal fees, which the consumer does not actually receive.¹ These funds go to the consumer's attorney to compensate them for their work. The attorney, in turn, pays taxes on the fees. This creates an unfair result as both the consumer and their attorney must pay income taxes on the same set of funds. It is unlikely that double taxing consumer recoveries in this manner has ever been the IRS or Congress's intent.

This illogical tax treatment can cause problems for many consumer-taxpayers. In some cases, consumers' tax bills may be higher than what they actually recover in cases.² Recovered legal fees can also artificially inflate a consumer's income and make it appear that they earned more than they actually have, thus creating obstacles to getting their tax refunds, certain tax credits, and income-dependent benefits.

Additionally, double taxing recovered legal expenses can make settlement difficult as consumers must focus on mitigating the financial consequences of unfair double taxation. This creates greater

¹ I.R.S. Pub. No. 525, *Taxable and Nontaxable Income* (2021), <https://www.irs.gov/pub/irs-pdf/p525.pdf>.

² Joanna Laine, *Consumer Protection and Tax Law: How the Tax Treatment of Attorney's Fees Undermines the Fair Debt Collection Practices Act*, 40 NYU Rev. L & Social Change 721, 753 (2016), https://socialchangenyu.com/wp-content/uploads/2016/10/laine_digital_9-29-copy.pdf.

costs for consumers, businesses, and our court system alike.

Congress has acted before to lift a similar tax penalty from victims of discrimination.³ Recognizing that unfair taxes could have a chilling effect on individuals with legitimate claims, Congress amended the tax code in 2004 in a bipartisan effort so individuals with employment and civil rights claims would not be taxed on their recovered legal expenses.⁴ The End Double Taxation of Successful Consumer Claims Act would similarly bring the tax code back in line with the congressional intent behind consumer protection laws.

Voters across all demographics also agree that tax fairness for Americans in these situations is necessary. A 2020 survey of 1,000 likely voters found that 83% of Democrats and 81% of Republicans support changing the tax code so consumers are not double taxed on awarded legal fees.

We appreciate all of your efforts to remove this consumer tax burden and restore common-sense fairness. We look forward to working with you on this important legislation.

Sincerely,

American Association for Justice
Americans for Financial Reform
Center for Justice & Democracy
Consumer Action
Consumers for Auto Reliability and Safety
Consumer Federation of America
Consumer Reports
National Association of Consumer Advocates
National Association of Consumer Bankruptcy Attorneys
National Consumer Law Center (on behalf of its low income clients)
National Consumers League
National Employment Lawyers Association
Public Citizen
Public Good Law Center
Public Justice
Tax March
U.S. PIRG
Woodstock Institute

³ Chuck Grassley, *Grassley Works To End Unfair Taxation In Civil Rights Cases*, May 12, 2003, <https://www.grassley.senate.gov/news/news-releases/grassley-works-end-unfair-taxation-civil-rights-cases>

⁴ Laine, at 763-65; 26 U.S.C. 62(a)(20).