Downey v. Commissioner, 100 T. C. 634 (1993)

All damages received from an ADEA claim, including both liquidated and nonliquidated damages, are excludable from gross income as tort-like personal injury damages.

Summary

Burnes P. Downey, an airline pilot, settled his age discrimination lawsuit against his former employer under the Age Discrimination in Employment Act (ADEA) for $120,000, half allocated to nonliquidated damages and half to liquidated damages. The Tax Court initially held these damages excludable under IRC section 104(a)(2). Upon reconsideration following the Supreme Court's decision in United States v. Burke, which held backpay under Title VII taxable, the Tax Court reaffirmed its original holding. The court reasoned that the ADEA's remedies, including liquidated damages, reflect a tort-like conception of injury, distinguishing it from Title VII's limited remedies.

Facts

Burnes P. Downey, an airline pilot, filed a lawsuit against his former employer, alleging age discrimination under the ADEA after being denied a position as a second officer due to his age. The lawsuit included claims for unlawful age discrimination and willful violation of the ADEA. The parties settled for $120,000, with $60,000 allocated to nonliquidated damages (backpay) and $60,000 to liquidated damages. The settlement agreement required tax withholdings on the nonliquidated damages portion.

Procedural History

The Tax Court initially held in Downey v. Commissioner, 97 T. C. 150 (1991), that both the liquidated and nonliquidated damages from the ADEA settlement were excludable from gross income under IRC section 104(a)(2). Following the Supreme Court's decision in United States v. Burke, the Commissioner moved for reconsideration. The Tax Court granted the motion but reaffirmed its original holding in the supplemental opinion.

Issue(s)

1. Whether all damages received from a claim under the Age Discrimination in Employment Act (ADEA), including both liquidated and nonliquidated damages, are excludable from gross income under IRC section 104(a)(2).

Holding

1. Yes, because the ADEA's remedies, including liquidated damages, evidence a tort-like conception of injury and remedy, making discrimination under the ADEA a tort-

like personal injury for purposes of IRC section 104(a)(2).

Court's Reasoning

The Tax Court reaffirmed its original holding by distinguishing the ADEA from Title VII, as analyzed in United States v. Burke. The court noted that the ADEA provides a broader range of remedies, including liquidated damages, which serve both compensatory and punitive functions, reflecting a tort-like conception of injury. The availability of liquidated damages under the ADEA, unlike the sole focus on backpay under Title VII, led the court to conclude that ADEA claims redress tort-like personal injuries. The court emphasized that the nature of the claim, not just the type of damages, determines the tax treatment under IRC section 104(a)(2). Concurring opinions suggested a potential distinction between willful and nonwillful ADEA violations, while dissenting opinions argued for the taxation of nonliquidated damages as backpay.

Practical Implications

This decision allows taxpayers to exclude all damages received from ADEA claims from their gross income, impacting how similar discrimination claims under other statutes might be treated for tax purposes. It may influence legal strategies in ADEA litigation, as plaintiffs might seek settlements structured to maximize the exclusion of damages from income. Businesses and their tax advisors must consider this ruling when negotiating settlements involving ADEA claims. Subsequent cases have applied this ruling, although legislative changes to Title VII post-Burke have altered the landscape for discrimination claims under that statute. The distinction between willful and nonwillful violations under the ADEA remains a potential area for future litigation and clarification.

