

Office of Chief Counsel
Internal Revenue Service
Memorandum

Number: **200809001**

Release Date: 2/29/2008

CC:ITA:B04:

FILEN-143364-07

UILC: 104.03-00; 6041.03-00

date: November 27, 2007

to: James M. Grimes
Director of Compliance (W&I)

from: Michael J. Montemurro
Chief, Branch 4
Office of Associate Chief Counsel
(Income Tax & Accounting)

subject:

LEGEND

Entity =

Tort =

C =

X =

You have inquired whether certain payments that Entity has made to settle claims of Tort are excludable from gross income under § 104(a)(2) of the Internal Revenue Code and, therefore, not subject to information reporting requirements under § 6041. This Service Center Advice responds to your request for assistance. This advice may not be used or cited as precedent.

Section 61 provides that gross income includes all income from whatever source derived, except as otherwise excluded in subtitle A. Generally, § 104(a)(2) excludes

from gross income the amount of any damages received on account of personal physical injuries or physical sickness. The exclusion also applies to any damages for emotional distress attributable to a physical injury or physical sickness. H.R. Conf. Rep. No. 737, 104th Cong. 2d Sess. 301 (1996). Punitive damages and interest are included in income under § 61.

Section 6041(a) provides that, generally, all persons engaged in a trade or business that pay another person \$600 or more of fixed or determinable income in the course of that trade or business must file an information return setting forth the amount of the payment and the recipient of that payment. Payments that are excludable from the recipient's gross income under § 104(a)(2) are not subject to information reporting under § 6041.

You have inquired about the tax treatment of payments made by Entity to settle claims of Tort asserted by C. C has alleged that Entity's agent(s) X caused physical injury through Tort while he was a minor under the care of X. A substantial amount of time has elapsed since the alleged Tort occurred. C alleges that he continues to struggle with the trauma resulting from the alleged Tort. Because of the passage of time and because C was a minor when the Tort allegedly occurred, C may have difficulty establishing the extent of his physical injuries. Under these circumstances, it is reasonable for the Service to presume that the settlement compensated C for personal physical injuries, and that all damages for emotional distress were attributable to the physical injuries. Consequently, the Service should concede that compensatory damages paid to settle the claim are excludable from gross income for federal income tax purposes. In addition, the Service should not assert that information reporting is required for such payments under § 6041.

Any portion of a damage award that is allocable to punitive damages or interest, however, is includible in the gross income of C under § 61. A payor that pays punitive damages or interest must issue a Form 1099 and furnish a copy of that form to C, if the payor's aggregate payments to C of interest and punitive damages from the settlement and other payments described in § 1.6041-1(a)(1)(i)(B) of the Income Tax Regulations during the calendar year equal \$600 or more.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call _____ if you have any further questions.

cc: