

# Pleading the 16th

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No man, it has often been said, is above the law. Now, thanks to three judges on the federal appeals bench in Washington, no tax is above the law either. The judges have ruled that compensatory damages awarded in a lawsuit don't count as "income" even under the expansive language of the 16th Amendment. As a result, the government's attempts to tax such monies are unconstitutional. The success of what was once considered a quixotic case is likely to spur other litigation trying to whittle away at other nooks and crannies of the tax code. All of which is to the good.

The plaintiff in this case, Marrita Murphy, had launched a whistleblower action against the New York Air National Guard. She won her case in the secretary of labor's office, and an administrative judge awarded her \$70,000 in compensatory damages for a combination of emotional distress and damage to her reputation. She initially paid income taxes of \$20,665 on that award, but eventually asked for a refund on the grounds that compensatory awards don't count as "income" under the 16th Amendment.

Income tax law has traditionally recognized that compensatory damages for, say, a physical injury or destroyed property aren't truly "income." Such awards simply use money to return a person to the way things were before, instead of providing a windfall or compensating for some service. The novelty in this latest ruling is that it extends the same theory to awards that compensate for less tangible damage. It won't necessarily apply to the biggest civil awards, since punitive damages still count as taxable income as a "windfall"; the headline-grabbing verdicts are almost always punitive.

The ruling does, however, set a precedent because the judges have shown that the tax code isn't a creature unto itself. As much as Congress might prefer otherwise, taxation is subject to some constitutional limitations. One wonders from the reaction to this ruling whether some people have been in denial on this point. One former commissioner of internal revenue, Donald C. Alexander, told Bloomberg News that "Tax protesters will love it because it's what they've been arguing for years. They will claim this destroys the income tax. A case like this does serious damage to the system even though it involves one provision."

Our guess is that tax protesters are going to have a hard time using this ruling against the income tax, as the people spoke, for better or worse, when, in the 16th amendment, they delegated to Congress the "power to lay and collect taxes on incomes, from whatever source derived." But the ruling underscores that the delegation is not unlimited; the Constitution still imposes limits on Congress's power to tax. This isn't a conservative issue, it's a constitutional issue. A judge appointed by President Clinton, after all, joined colleagues appointed by Presidents Reagan and George W. Bush on this ruling.

If, per Mr. Alexander, "the system" is in trouble when a court points up that fact, that's a sign of how out of control the taxers on Capitol Hill have become. Time and a higher court will tell whether Ms.

Murphy gets to keep her \$20,665 in tax payments. We wish her luck. Whatever the final result, Ms. Murphy has performed a service by offering three judges an opportunity to give the IRS a scare. No other person or institution in America is above the law, and there's no reason the IRS should be the exception.