NOT YET SCHEDULED FOR ORAL ARGUMENT

No. 05–5139

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

MARRITA MURPHY, *et al.*,

Appellants

v.

INTERNAL REVENUE SERVICE, *et al.*,

Appellees

ON APPEAL FROM THE ORDER OF
THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

BRIEF FOR THE APPELLEES

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CERTIFICATE OF PARTIES, RULINGS AND RELATED CASES

A. *Parties and Amici*. The parties in the District Court and in this Court are Marrita Murphy, Daniel J. Leveille, the Internal Revenue Service and the United States of America. The No FEAR Coalition appears on appeal as an amicus curiae.

B. *Rulings under Review*. The rulings under review are the memorandum opinion of the District Court (Judge Royce C. Lamberth) dated March 22, 2005 (reported at 362 F. Supp. 2d 206) (JA 19-35) and the court's accompanying order entered that same day (JA 36-37).

C. *Related Cases*. This case was not previously before this Court or any court other than the district court below. Counsel are unaware of any related cases pending in this Court or in any other court.

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GLOSSARY

Add.	Addendum attached hereto
ALJ	Administrative Law Judge
APA	Administrative Procedures Act
The Board	Department of Labor, Administrative Review Board
The Code	Internal Revenue Code (26 U.S.C.)
Doc.	Document in the district court record
DOL	Department of Labor
I.R.C.	Internal Revenue Code (26 U.S.C.)
IRS	Internal Revenue Service
JA	Joint Appendix
NYANG	New York Air National Guard
SBJPA	Small Business Job Protection Act

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JURISDICTIONAL STATEMENT

Marrita Murphy and Daniel J. Leveille ("taxpayers") brought this tax refund suit in the district court, seeking to recover $20,865 (plus interest) of federal income taxes they had paid when they filed their 2000 joint return on April 11, 2001. (JA 6-13.)[1] Before bringing suit,

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[1] "JA" references are to the Joint Appendix filed with the appellants' brief. "Doc." references are to the documents in the original record on

(continued...)

they filed a timely administrative refund claim, as is required by I.R.C. § 6511(a), by way of a third amended tax return submitted on October 8, 2002. (JA 8.) On December 18, 2002, the claim for refund was denied by the Internal Revenue Service (IRS). (JA 9.) This refund suit was commenced on November 23, 2003, within the two-year time period set forth at I.R.C. § 6532(a)(1). (JA 6-13.) The district court had jurisdiction under I.R.C. § 7422 and 28 U.S.C. § 1346(a)(1).

On March 22, 2005, the district court entered an order granting summary judgment to the Government.[2] (JA 36-37.) The order

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[1](...continued)
appeal, as numbered by the Clerk of the district court.

[2] In the district court, the Government filed a motion to dismiss the IRS as a party. (Doc. 9.) The Government argued that the IRS is not a separately suable entity in this tax refund action, and that the United States was the only properly named defendant. The district court, however, denied the motion, holding that the Administrative Procedures Act (APA), at 5 U.S.C. § 702(a), allows a suit against an administrative federal agency where the complainant seeks relief other than monetary damages. (JA 22-23.) We submit that the district court erred in this regard. It is true that taxpayers, in their original complaint, requested non-monetary relief, *viz.*, declaratory and injunctive relief, respecting their liability for the taxes in issue. But the Government's sovereign immunity was not waived in this case for declaratory and injunctive relief respecting taxpayers' liability, and was waived only for a suit for a tax refund. *See* 28 U.S.C. § 2201; I.R.C.
(continued...)

disposed of all claims of all parties and is final and appealable. On April 6, 2005, taxpayers filed a timely notice of appeal. (JA 4.) *See* 28 U.S.C. § 2107(b); Fed.R.App.P. 4(a)(1). This Court's jurisdiction rests upon 28 U.S.C. § 1291.

STATEMENT OF THE ISSUES

Prior to its amendment in 1996, I.R.C. § 104(a)(2) provided for the exclusion from gross income of damages received on account of both physical and nonphysical tort injuries. In 1996, § 104(a)(2) was amended to eliminate the exclusion for damages received on account of nonphysical injuries. The questions presented are:

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[2](...continued)
§ 7421(a); *Bob Jones University v. Simon*, 416 U.S. 725 (1974); *Flora v. United States*, 357 U.S. 63, 75 (1958). The statutes waiving sovereign immunity for a tax refund suit allow that it be brought against the United States only. *See* I.R.C. § 7422(f)(1); 28 U.S.C. § 1346(a)(1). *See also Gomez v. United States*, 2003-1, USTC (CCH) ¶ 50,519 (9th Cir. 2003); *Loofburrow v. CIR*, 208 F. Supp. 2d 698, 702 (S.D. Tex. 2002); *Lehman v. USAIR, Group, Inc.*, 930 F. Supp. 912, 916 (S.D.N.Y. 1996); *Wiltgen v. United States*, 813 F. Supp. 1387, 1388 (N.D. Iowa 1992). Thus, taxpayers' request for non-monetary relief here was specifically barred, and the APA accordingly did not, as the district court held, allow taxpayers' suit to be brought against the IRS. Only the United States was a properly named defendant.

1. Whether the district court correctly held that the 1996 amendment was not an unconstitutional expansion of Congress's power to lay taxes under the Sixteenth Amendment.

2. Whether the district court correctly held on summary judgment that the civil damages of $70,000 awarded in 2000 to compensate Ms. Murphy for her "mental pain and anguish" and "injury to professional reputation" were not received on account of personal physical injuries or physical sickness, and thus were not excludable from income under I.R.C. § 104(a)(2).

STATUTES AND REGULATIONS

The relevant statutes and regulations are set forth in an Addendum to this brief, *infra*.

STATEMENT OF THE CASE

Taxpayers brought this suit for a refund of federal income tax paid for the year 2000, arguing that under I.R.C. § 104(a)(2) they were entitled to, but did not originally claim, an exclusion from income of $70,000, which represented a portion of the civil damages awarded to Ms. Murphy in a prior labor dispute. (JA 6-13.) In an opinion reported

at 362 F. Supp. 2d 206, the district court, granting the Government's motion for summary judgment, held that those damages were not excludable from taxpayers' income. (JA 19-37.) Taxpayers now appeal.

STATEMENT OF THE FACTS

A. The labor dispute and award of civil damages to Ms. Murphy

In 1994, taxpayers filed administrative complaints with the U.S. Department of Labor ("DOL") against their former employer, the New York Air National Guard ("NYANG"), alleging that NYANG discriminated against them by engaging in conduct prohibited under the whistleblower protection provisions of six federal environmental statutes. (*See Leveille v. New York Air National Guard*, 1995 WL 848112, *3 (DOL Off. Adm. App.), copy attached in Addendum, *infra* at pp. 54-63.) The Secretary of Labor dismissed Mr. Leveille's complaint as untimely filed. (*Id.*) On December 11, 1995, the Secretary ruled in favor of Ms. Murphy on her discrimination complaint, finding that NYANG illegally blacklisted her when, because of her protected activity, it gave unfavorable employment references to a company known as Documented Reference Check, and also to the U.S. Office of

Personnel Management. (*Id.*) The Secretary remanded Ms. Murphy's case to the administrative law judge ("ALJ") to make recommendations on compensatory damages and attorney's fees and costs owed to her. (*Id.* at *9.)

On October 25, 1999, the DOL, Administrative Review Board ("the Board") issued a Decision and Order on Damages in which it adopted as reasonable the damages recommendations of the ALJ. (*See* 1999 WL 966951, *5 (DOL Adm. Rev. Bd.), copy attached in Addendum, *infra* at pp. 64-69.) In Section I of its decision, the Board observed that the ALJ had "compared this case to other whistleblower cases in which damages had been awarded for mental anguish and recommended an award of $45,000 for mental distress." *Id.* at *1. It also noted that the ALJ "recommended an award of $25,000 for damage to [Ms. Murphy's] professional reputation." *Id.*

In Section II of its decision, entitled "Compensatory damage for emotional distress or mental anguish," the Board provided a detailed review of the ALJ's recommendation of damages. (*Id.* at *2–*4.) It held that the environmental statutes in issue provided for the award of tort-

like remedies with respect to discriminatory conduct "not only for direct pecuniary loss, but also for such harms as impairment of reputation, personal humiliation, and mental anguish and suffering." (*Id.* at *2.) The Board observed that Ms. Murphy "testified that she experienced a variety of medical and personal problems after learning that she had been blacklisted by the Air National Guard, including severe anxiety attacks, inability to concentrate, a feeling that she no longer enjoyed 'anything in life,' and marital conflict." (*Id.* at *3.) The Board, noting that "any attempt to set a monetary value on intangible damages such as mental pain and anguish involves a subjective judgment," concluded that the "ALJ's recommendation of an award of $45,000 for emotional distress is reasonable, and we adopt it." (*Id.* at *4.) Similarly, it agreed with the ALJ's recommendation of a $25,000 award to Ms. Murphy for "damage to [her] professional reputation." (*Id.*) Thus, the Board awarded Ms. Murphy damages for mental pain and anguish, and for injury to professional reputation, in the amounts of $45,000 and

$25,000, respectively.[3] (*Id.* at *5.) It is undisputed that these amounts were received by taxpayers during calendar year 2000.

B. Taxpayers' filing of their federal income tax return for the year 2000, and their administrative claim for refund

On their federal income tax return for 2000, taxpayers reported $70,000 as other income, reflecting the aforementioned damages awards for mental pain and anguish and injury to reputation. (JA 8, ¶ 7.) Subsequently, taxpayers filed amended returns (Form 1040X) for 2000, seeking a refund of federal income tax in the amount of $20,865.00 that was paid in connection with the award of such damages. (JA 8, ¶¶ 8, 9, 10.) Taxpayers asserted that the damages awards were excludable from their income under I.R.C. § 104(a)(2), because the amounts were

[3] The Board also adopted the ALJ's recommendations that Ms. Murphy be awarded $529.28 for past medical expenses and $10,000 for future medical expenses, as well as attorney's fees and costs. (1999 WL 966951 at *5.) In explaining its award of future medical expenses, the Board explained that "[i]t is difficult to determine in advance how many hours of counseling Complainant will require, but based on the amount she has already incurred, $10,000 for future medical expenses is a reasonable approximation." Only the award of damages for mental pain and anguish and injury to professional reputation are at issue in this tax case.

allegedly received on account of physical injuries or physical sickness sustained by Ms. Murphy. (JA 9, ¶ 13.)

The IRS denied taxpayers' claim for refund on the ground that taxpayers had not demonstrated that the damages were received on account of a physical injury or physical sickness as required by I.R.C. § 104(a)(2). (JA 9, ¶ 14.) Taxpayers thereafter requested an administrative appeal of the denial of their refund claim. (JA 9, ¶16.) When the IRS did not take action on taxpayers' appeal within 180 days, taxpayers filed the instant refund action in the district court. (JA 6-13.)

C. The district court proceedings

The Government filed a motion for summary judgment in the district court (Doc. 10), arguing that the damages were awarded to Ms. Murphy on account of nonphysical injuries, *i.e.*, mental pain and anguish, and injury to her professional reputation, and thus were not, as a matter of law, excludable from income under I.R.C. § 104(a)(2). The Government noted that income is broadly construed under the internal revenue laws, and any accession to wealth is includable in gross income unless expressly excluded by statute. It pointed out that

§ 104(a)(2) was amended in 1996 to narrow the income exclusion available for personal injury damages such that only amounts received on account of *physical* personal injuries or *physical* sickness are excludable, and the damages awarded to Ms. Murphy were not awarded on account of physical injury or physical sickness.

Taxpayers opposed the grant of summary judgment to the Government and filed a cross-motion for partial summary judgment (Docs. 19-21), in which they argued that amended § 104(a)(2) was unconstitutional, or, alternatively, that there was a triable issue as to whether the damages Ms. Murphy received were to compensate her physical injuries. Taxpayers' constitutional argument, to the extent relevant to this appeal, was that the Sixteenth Amendment, while granting Congress the power to tax income, did not permit a tax on personal injury damages, regardless whether they were to compensate physical or non-physical injuries.[4] They maintained that amounts that

[4] Taxpayers also argued below that, § 104(a)(2), as amended in 1996, resulted in an unconstitutional retroactive application of law, and that it violated the due process and takings clauses of the Fifth Amendment. The district court rejected these arguments (*see* JA 30-33), and taxpayers do not address these issues in their opening brief on appeal to (continued...)

compensate for a personal injury are a "return of human capital," and not gain, and therefore cannot be taxed as income under the Sixteenth Amendment. Taxpayers further argued that the court should ask "in lieu of" what the damages were awarded and since they were awarded "in lieu of" human capital, the damages are not subject to tax. Finally, taxpayers contended that, in any event, their evidence, *i.e.*, affidavits from a treating psychologist and a treating dentist, established at least a triable issue of fact as to whether Ms. Murphy sustained physical injuries attributable to the unlawful conduct of NYANG, *viz.*, "somatic" and "body" injuries, such as dental injury from grinding her teeth (bruxism), for which she received the damages in issue.

In a memorandum opinion, the district court, as relevant here, held that the damages in issue received by taxpayers constituted gross income subject to taxation, unless subject to exclusion under I.R.C. § 104(a)(2). (JA 26-27.) The court observed that longstanding Supreme Court precedent, which has been handed down since ratification of the

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[4](...continued)
this Court. The issues are therefore waived. *World Wide Minerals, Ltd. v. Republic of Kazakhstan*, 296 F.3d 1154, 1160 (D.C. Cir. 2002); *Teny v. Reno*, 101 F.3d 1412, 1415 (D.C. Cir. 1996).

Sixteenth Amendment, establishes a broad definition of income for purposes of the income tax, including all income from whatever source derived and all economic gains not otherwise exempted by statute. (JA 26, 34.) The court concluded that, as amended in 1996, "§ 104(a)(2) does not pose a constitutional problem under the Sixteenth Amendment." (JA. 35.)

The court noted that the "in lieu of" test relied upon by taxpayers was applied in cases of settlement and not where damages are awarded by an administrative body. (JA 34.) Furthermore, the court observed, the damages were awarded "in lieu of" nonphysical injuries and therefore fell outside of the exclusion provided for by amended I.R.C. § 104(a)(2). (JA 34-35.)

Finally, the district court also rejected taxpayers' contention that a material issue of fact exists whether the damages in issue were paid to Ms. Murphy on account of physical injury or physical sickness. (JA 28-29.) It observed that the legislative history to the 1996 amendment to § 104(a)(2) explicitly eliminated employment discrimination or injury to reputation accompanied by a claim of emotional distress from the

purview of the income exclusion. (JA 29.) The court thus held, with respect to the $25,000 in damages paid with respect to Ms. Murphy's harm to her professional reputation, that "this award is not specifically exempted by statute, and thus falls within the broader definition of taxable income." (*Id.*)

With regard to the $45,000 in damages paid with respect to Ms. Murphy's mental pain and anguish, the court noted that, for purposes of I.R.C. § 104(a)(2), emotional distress is not considered a physical injury or physical sickness and that only damages that are attributable to a physical injury or physical sickness are excludable. It reasoned as follows:

> Here, Murphy's mental anguish manifested into a physical problem, bruxism, but this was only a symptom of her emotional distress, not the source of her claim. Plaintiff's emotional distress is not "attributable[“] to her physical injury; in fact, it is the other way around. Because the statute clearly provides damages must be received "on account of personal physical injury or physical sickness," and because mental pain and anguish and damage to reputation are not physical injuries, plaintiff's emotional distress damages are not included within the statutory exemption under § 104(a)(2).

The court entered an order granting summary judgment to the Government, from which taxpayers now take this appeal. (JA 36-37.)

SUMMARY OF ARGUMENT

Taxpayers seek a refund with respect to their 2000 federal income tax on the ground that civil damages awarded to Ms. Murphy with respect to her mental pain and anguish ($45,000) and injury to her professional reputation ($25,000) are excludable from gross income under I.R.C. § 104(a)(2). Prior to its amendment in 1996, § 104(a)(2) allowed an exclusion from gross income for damages received on account of nonphysical personal injuries. As amended in 1996, § 104(a)(2) allows an exclusion from gross income only for damages received "on account of physical personal injuries or physical sickness." Further, § 104(a) expressly provides that emotional distress is not a physical injury.

1. Taxpayers assert that the 1996 amendment to I.R.C. § 104(a)(2) is unconstitutional, arguing that personal injury damages, whether paid in respect of a physical or nonphysical injury, are not income within the meaning of the Sixteenth Amendment and cannot be

taxed by Congress. This argument ignores the many Supreme Court cases beginning with *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955), that have consistently held that Congress's power to tax "income" is broad-sweeping and extends to the receipt of anything of value, measurable in money (*i.e.*, "accessions to wealth"), over which the taxpayer has dominion and control, and that all receipts constitute gross income unless specifically exempted.

Because Congress is assumed to legislate in light of constitutional limitations, taxpayers have a particularly large hurdle to clear to show that the narrowing of the income exclusion for personal injury damages violates constitutional limits. Taxpayers contend that, since first enacted in 1918, the exclusion has been based on an understanding that such damages are not constitutionally taxable. The upshot of that argument is that the exclusion is entirely unnecessary in the first place, since there would never had been a need for it. Congress plainly did not believe that the exclusion was unnecessary, and the Supreme Court, in considering the scope of the exclusion on three occasions in the 1990's did not even remotely suggest that the exclusion was unnecessary for

the reason that such damages were not income. The Tax Court and three federal courts of appeals recently have rejected constitutional challenges to the 1996 amendment to I.R.C. § 104(a)(2) wherein the taxpayers argued that the amendment either violated their Fifth Amendment due process rights as an unlawful retroactive application of law, or violated their Fifth Amendment right to equal protection.

None of the cases relied upon by taxpayers have held that the exclusion of compensatory damages from gross income is constitutionally mandated. Their contention that such damages are a restoration of "human capital" and do not represent a taxable "gain" has no merit. Cases they cite generally note that Congress or the IRS had allowed the exclusion for that policy reason, but that is a far cry from saying that such an exclusion is constitutionally required. The vague concept of "human capital" refers to the abstract worth a person has in his or her well-being. Because people do not pay cash or its equivalent to acquire their well-being, they have no basis in it for purposes of measuring a gain (or loss) upon the realization of compensatory

damages. The tax basis in "lost" "human capital" is zero, and any related receipt of damages thus amounts to a "gain" on that "capital."

2. Taxpayers argue, in the alternative, that the damages in issue were received "on account of" Ms. Murphy's *physical* personal injuries and thus are excludable under amended I.R.C. § 104(a)(2). That contention was correctly rejected on summary judgment. The record establishes, as a matter of law, that the damages awards in issue were for nonphysical personal injury, *viz.*, for mental pain and anguish and injury to professional reputation. Such damages are the quintessential type of compensatory damages that Congress, in 1996, expressly provided are no longer excludable from income under § 104(a)(2).

The fact that Ms. Murphy may have suffered from bruxism (grinding of her teeth) stemming from her nonphysical injuries does not aid taxpayers. The Supreme Court has construed the "on account of" phrase in I.R.C. § 104(a)(2) as requiring a *direct* causal link between the physical injury and the damages recovery in order to qualify for the income exclusion, and has explicitly rejected the contention that a "but for" connection between the damages received and the personal injury is

sufficient. Thus, even assuming that bruxism is a physical injury, it is of no consequence that "but for" the civil wrongs perpetuated against Ms. Murphy, she would not have suffered from bruxism. The damages in issue were awarded to compensate directly only her emotional injuries.

Moreover, as the legislative history to the 1996 amendment to I.R.C. § 104(a)(2) makes clear, Congress intended to include in the definition of emotional distress any physical symptoms that may stem from such emotional distress. Bruxism plainly was a symptom of the mental pain and anguish Ms. Murphy suffered and thus was not a physical personal injury for purposes of amended § 104(a)(2).

The order of the district court is correct and should be affirmed.

ARGUMENT

I. The 1996 amendment to I.R.C. § 104(a)(2), which limited the exclusion from gross income allowable thereunder, was not an unconstitutional expansion of Congress's power to lay taxes under the Sixteenth Amendment

Standard of Review

Whether I.R.C. § 104(a)(2), as amended in 1996, is constitutional is reviewable *de novo* by this Court. *Eldred v. Reno*, 239 F.3d 372, 374 (D.C. Cir. 2001).

A. Congress's broad power to tax income

In 1913, the States ratified the Sixteenth Amendment to the U.S. Constitution, thereby eliminating the constitutional impediment to imposing a direct tax on income without apportionment,[5] and conferring upon "[t]he Congress . . . the power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the

[5] As originally adopted, the Constitution empowered Congress to impose taxes, but required that a direct tax on income be apportioned. *See* U.S. Const. art I, § 8, cls. 1, 18 and § 9, cls. 4; *see also Pollock v. Farmers' Loan & Trust Co.*, 158 U.S. 601 (1895) (holding that income tax enacted in 1894 was an unconstitutional unapportioned direct tax).

several States, and without regard to any census or emuneration." U.S. Const. amend. XVI. Not long thereafter, Congress enacted an income tax law in which it defined gross income as "income derived from any source whatever." Revenue Act of 1913, § II(B), 38 Stat. 167. That definition has remained substantively unchanged ever since, except that, after being brought into the 1954 Internal Revenue Code at § 61(a), its language was altered slightly to mirror precisely that of the Sixteenth Amendment, such that gross income means all income "from whatever source derived." *See* 1 Boris I. Bittker & Lawrence Lokken, *Federal Taxation of Income, Estates, and Gifts*, ¶ 5.1 at p. 5-2 (3d ed. 1999). Thus, the House Report regarding the enactment of the 1954 Code, H.R. Rep. No. 1337, 83d Cong., 2d Sess. at A18 (1954), noted that the definition of gross income in § 61(a) "is based upon the 16th Amendment and the word 'income' is used in its constitutional sense," and further affirmed the "all-inclusive nature of statutory gross income." The Senate Report is to the same effect. S. Rep. No. 1622, 83d Cong., 2d Sess. at 168 (1954).

In *Eisner v. Macomber*, 252 U.S. 189, 207 (1920), *citing Doyle v. Mitchell Bros. Co.,* 247 U.S. 179 (1918), the Supreme Court held that "income may be defined as the gain derived from capital, from labor, or from both combined." It is upon this definition that taxpayers largely base their argument. The Court later made clear, however, in *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955), that the definition in *Eisner* "was not meant to provide a touchstone to all future gross income questions," and it announced that gross income includes "all gains except those specifically exempted." Moreover, in *Glenshaw Glass*, the Court made clear that the concept of gross income was broad, stating that it includes any "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." *Id.* at 431. And, the Court further made clear that it understood the broad definition of income in I.R.C. § 61 to be based upon the Sixteenth Amendment and that the term "income" was used in its constitutional sense. *Id.* at 433 n. 11.

Since *Glenshaw Glass*, the Supreme Court has repeatedly emphasized the breadth of the reach of I.R.C. § 61 and that receipts are

income unless specifically exempted. Thus, in *Commissioner v. Jacobson*, 336 U.S. 28, 49 (1949), the Court observed that "[t]he income tax is described in sweeping terms and should be broadly construed in accordance with an obvious purpose to tax income comprehensively." Then in *United States v. Burke*, 504 U.S. 229, 233 (1992), the Court observed that "[t]he definition of gross income under the Internal Revenue Code sweeps broadly," including all income "subject only to the exclusions specifically enumerated elsewhere in the Code." And, most recently, in *Commissioner v. Banks*, 543 U.S. 426, 125 S. Ct. 826, 831 (2005), the Court stated that the definition of gross income in I.R.C. § 61 "extends broadly to all economic gains not otherwise exempted." *See also Commissioner v. Schleier*, 515 U.S. 323, 327-328 (1995); *Commissioner v. Kowalski*, 434 U.S. 77, 82-83 (1977); *Helvering v. Clifford*, 309 U.S. 331, 333 (1940).

This Court has similarly recognized the breadth of I.R.C. § 61. *Sparrow v. Commissioner*, 949 F.2d 434, 436 (D.C. Cir. 1991) ("section 61 states a rule of inclusion," and thus "unless another portion of the Internal Revenue Code specifically excludes an accession to wealth from

taxation, a taxpayer must include it in his income"). *See also Roemer v. Commissioner*, 716 F.2d 693, 696 n. 2 (9th Cir. 1983) (at time of *Eisner*, income thought to have been "gain" from capital or labor, but *Glenshaw Glass* made "clear that the Eisner definition of income was not exclusive and that other realized accessions to wealth may be taxable income"); *Huddell v. Levin*, 355 F. Supp. 64, 87 (D. N.J. 1975) ("Although Congress may have initially excluded personal injury awards from taxation because of constitutional reservations, it has since been clearly established that Congress can constitutionally tax any gain . . . .")

In addition, the Supreme Court "ha[s] also emphasized the corollary to § 61(a)'s broad construction, namely, the 'default rule of statutory interpretation that exclusions from income must be narrowly construed.'" *Schleier*, 515 U.S. at 327-328 (quoting *Burke*, 504 U.S. at 248 (Souter, J., concurring in judgment)); *Jacobson*, 336 U.S. at 49; *Lindsey v. Commissioner*, 422 F.3d 684, 687 (8th Cir. 2005).

B. The income exclusion for physical personal injury damages is constitutional

The exclusionary provision of the Code at issue here is I.R.C. § 104(a)(2). Prior to its amendment in 1996, it excluded from gross income "the amount of any damages received (whether by suit or agreement . . .) on account of personal injuries or sickness." As then in effect, § 104(a)(2) was held to encompass damages compensating all personal injuries, including non-physical personal injuries, *e.g.,*"those affecting emotions, reputation, or character." *Burke*, 504 U.S. at 236 n. 6; *see also Schleier*, 515 U.S. at 329-330.

Section 104(a) was amended on August 20, 1996, by the Small Business Job Protection Act ("the SBJPA"), Pub. Law No. 104-188, § 1605(a), 110 Stat. 1755, 1838, 1996-3 C.B. 155, 238. As amended, § 104(a)(2) expressly limits the type of personal injury damages excludable from taxation to those received "on account of personal

physical injuries or physical sickness." [6] In pertinent part, I.R.C. § 104(a), as amended, provides as follows:

> SEC. 104. COMPENSATION FOR INJURIES OR SICKNESS
>
> (a) IN GENERAL. — Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include —
>
> * * * *
>
> (2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness;
>
> * * * *
>
> For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraph (A) or (B) of section 213(d)(1)) attributable to emotional distress.

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[6] The amendment was made effective to any "amounts received after the date of the enactment of this Act, in taxable years ending after such date." *See* SBJPA § 1605(d), Pub. L. No. 104-188, 110 Stat. at 1839, *reprinted in* 1996-3 C.B. at 239. The damage amounts at issue in the case at bar were received by taxpayers in calendar year 2000, years after the date of enactment of the SBJPA on August 20, 1996. The 1996 amendment thus applies in this case.

The legislative history of the 1996 amendment makes clear that, in using the term "emotional distress," Congress intended to include "symptoms (*e..g*, insomnia, headaches, stomach disorders) which may result from such emotional distress." The legislative history further made clear that by restricting the exemption from gross income to amounts paid on account of physical injuries, the exclusion did not apply to damages received "based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress." *See* H.R. Rep. No. 104-586, at 144, *reprinted in* 1996-3 C.B. at 482; H.R. Conf. Rep. No. 104-737, at 301, *reprinted in* 1996-3 C.B. at 1041.

Here, the DOL Board of Review awarded Ms. Murphy the damages in issue as a result of injuries she suffered to her emotional well-being (mental pain and anguish) and professional reputation. (*See* 1999 WL 966951, *5.) These are the very damages—those received on account of non-physical injuries—that no longer qualify for exclusion under § 104(a)(2). Taxpayers contend, however (Br. 16-30), that Congress exceeded its taxing powers under the Sixteenth Amendment

when it limited the exclusion for personal injury damages to only damages compensating *physical* injuries. In their view, damages awarded to compensate personal injuries, whether physical or non-physical, are not "income" within the meaning of the Sixteenth Amendment and cannot be taxed. The amicus curiae makes the same argument, but writes separately to acknowledge that, under its argument, § 104(a)(2) "is meaningless" because "[c]ompensatory damages payments are not income and cannot be taxed, no matter what Congress says or does not say." (Amicus Br. 3; fn. omitted.) Taxpayers and the amicus curiae are incorrect.

C. Damages awarded on account of injury are income irrespective of any compensatory purpose.

The 1996 amendment is presumed to be constitutional, because Congress is "assume[d] to legislate[ ] in light of constitutional limitations." *Rust v. Sullivan*, 500 U.S. 173, 191 (1991). *See also Almendarez - Torres v. United States*, 523 U.S. 224, 237-238 (1998); *United States v. X-Citement Video, Inc.*, 513 U.S. 64, 73 (1994); *Yates v. United States*, 354 U.S. 298, 319 (1957). As a consequence, taxpayers have a particularly large hurdle to clear to show that the narrowing of

the income exclusion for personal injury damages violates constitutional limits.

Taxpayers' narrow view of income flies in the face of the considerable Supreme Court precedent cited above reaffirming again and again since *Glenshaw Glass* that the Code's definition of gross income (which mirrors the language of the Sixteenth Amendment) is an expansive, broad-sweeping concept, and includes any accession to wealth, unless explicitly exempted by Congress. It is evident from this abundance of authority that Congress's power to tax "income" under the Sixteenth Amendment extends to the receipt of anything of value, measurable in money (*i.e.*, "accessions to wealth"), over which the taxpayer has dominion and control. Thus, as the Supreme Court recently made clear in *Banks*, 125 S. Ct. at 831, the term "gross income" "extends broadly to all economic gains not otherwise exempted." Economic damages received by a taxpayer, such as those received by taxpayer here, plainly constitute economic gain, for the taxpayer unquestionably has more money after receiving the damages than she had prior to receipt of the award. And, this is so irrespective of any

compensatory purpose the award of damages may have had. As the court of appeals in *Roemer*, 716 F.2d at 696 n.2 , observed, the "money received as compensation" for an injury to "a person's health and other personal interests" is "considered a realized accession to wealth," but Congress, "in its compassion," has excluded certain damages from income in I.R.C. § 104(a)(2).

Section 104(a)(2) is an exclusionary provision that exempts a form of otherwise taxable income from tax. Taxpayers have no entitlement to statutory exclusions because Congress is free to create, abolish, or limit them. Had Congress wished to tax personal injury damages to their full extent, it could have done so consistent with its constitutional powers of taxation. *See* 1 Bittker & Lokken, ¶ 5.6, 5-37 - 5-41; *Burke*, 504 U.S. at 233-234. In amending I.R.C. § 104(a)(2) in 1996, Congress did not broaden the scope of what constitutes income—the Supreme Court had already made clear the considerable breadth of that scope—rather, it simply narrowed the scope of the income exclusion that it previously had permitted as a matter of legislative grace. In other words,

Congress merely changed the law to require the recognition of income realized by a taxpayer that theretofore did not require recognition.

According to taxpayers (Br. 23), "the statutory exclusion for personal injuries which was contained in the tax code from 1918 until 1996 was based on an understanding by the authors of that code, from its very inception, that such compensatory damages were not constitutionally taxable." As the amicus curiae candidly acknowledges (Amicus Br. 3), the upshot of taxpayers' argument is that I.R.C. § 104(a)(2) (and, presumably, all of § 104) is entirely unnecessary. Indeed, if taxing compensatory personal injury damages "were not constitutionally taxable," there would be no need for an exclusion. But Congress quite plainly did not believe that the exclusion was unnecessary. And, the Supreme Court, on three occasions, has considered the scope of the § 104(a)(2) exception. *See Burke, supra; Schleier, supra; O'Gilvie v. United States*, 519 U.S. 79 (1996). In none of those cases was it even suggested that the exclusion was unnecessary for the reason that damages having a compensatory purpose were not income in the first instance.

Moreover, the Tax Court and three federal courts of appeals recently have rejected constitutional challenges to the 1996 amendment to I.R.C. § 104(a)(2) wherein the taxpayers argued that the amendment either violated their Fifth Amendment due process rights as an unlawful retroactive application of law, or violated their Fifth Amendment right to equal protection. *See Lindsey v. Commissioner*, 422 F.3d 684, 688 (8th Cir. 2005), *aff'g*, 87 T.C.M (CCH) 1295 (2004); *Young v. United States*, 332 F.3d 893, 895-896 (6th Cir. 2003); *Venable v. Commissioner*, 86 T.C.M. (CCH) 254, 258 (2003), *aff'd*, 94 A.F.T.R. 2d (RIA) 2004-6408 (5th Cir. 2004) (per curiam); *Polone v. Commissioner*, 86 T.C.M. (CCH) 698, 709, 711 (2003), *on appeal*, (9th Cir.) (No. 04-72672). Congress's power under the Sixteenth Amendment to tax non-physical personal injury damages was apparently so obvious to the parties and the courts in those cases that it was presumed by them.[7]

[7] In *Young*, the taxpayer also sought to challenge the amendment on the ground that the withdrawal of the exclusion for nonphysical personal injury damages amounted to a "direct" or "capitation" tax in violation of Article I, Section 9, Clause 4 of the Constitution. That challenge too was unsuccessful.

Taxpayers nevertheless contend (Br. 16-22) that there is an "unbroken line of cases" supporting their view that Congress lacks the power under the Sixteenth Amendment "to tax compensation to restore a loss." To be sure, as taxpayers note, a number of cases have observed that compensatory damages are not includable in income given the particular circumstances presented and the relevant statutes at issue. Contrary to taxpayers' suggestion, however, none of the cases have held that the exclusion of compensatory damages from gross income is constitutionally mandated. And, certainly, none of the cases in any way suggested that compensation for the loss of human capital cannot be taxed under the Sixteenth Amendment. Instead, the cases generally note that it was the policy of Congress or the IRS to exclude from tax damages that represent the return of capital. Indeed, it was that policy that drove I.R.C. § 104(a)(2) in the first instance. But that is a far cry from saying that such exclusion is constitutionally required.[8] On the

[8] It is in this manner that taxpayers seek to gain mileage out of *Glenshaw Glass*, 348 U.S. at 432, n.8. There, in the context of differentiating punitive damages from compensatory personal injury damages, the Supreme Court noted that the policy of the IRS was not to include compensatory personal injury damages in income. The fact that (continued...)

other hand, it is taxpayers who seek to ignore the long line of cases cited above (at pp. 21-23) that indicate that any economic gain not otherwise exempted is income.

Taxpayers' reliance on the legislative history of earliest predecessor of I.R.C. § 104(a)(2) is likewise misplaced. In this regard, taxpayers look to an opinion of the Attorney General, 31 OP. Atty. Gen. 304, 308 (1918), and the House Report regarding the enactment of the exclusion, H.R. Rep. No. 767 at 9-10 (1918). Like the "unbroken line of cases" cited by taxpayers, however, neither the Attorney General's opinion nor the House Report give the slightest indication that taxing compensatory personal injury damages would be unconstitutional. Instead, like those cases, the opinion and report do no more than reflect

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[8](...continued)
the Government, as a matter of policy, has historically excluded personal injury recoveries from gross income, based on a make-whole or restoration-of-human-capital theory, does not mean that such an exclusion is mandated by the Sixteenth Amendment. The Court did not in any way suggest that this policy was constitutionally required.

that it was a policy decision to exclude such damages from tax.[9] Congress, of course, is free to change that policy, in whole or in part.

Indeed, taxpayers put the cart before the horse when they contend (Br. 22-27) that the Congressional intent behind original enactment of the exclusion necessarily dictates how the Sixteenth Amendment should be construed. At best, it provides some indication of what Congress *believed* gross income meant in 1918 and of the policy behind allowing an exclusion for personal injury recoveries. The Supreme Court, however, is charged with determining constitutional limitations. *Marbury v. Madison*, 5 U.S. 137 (1803). Ever since 1955, when *Glenshaw Glass* was decided, as discussed above, the Supreme Court has consistently pronounced that the statutory definition of gross

[9] Taxpayers note that in that in *Dotson v. United States*, 87 F.3d 682, 685 (5th Cir. 1996), the court stated that when the original exclusion for personal injury damages was enacted it was believed that such damages could not be constitutionally taxed. But the only authority the court cited for this proposition was the House report discussed above. As noted above, that report simply does not establish that Congress believed taxing compensatory personal injury damages would be unconstitutional. In any event, it is clear *Dotson* was not suggesting that that same view holds today. As discussed in detail above, it plainly does not.

income is co-extensive with that of the Sixteenth Amendment, and is so broad-sweeping as to encompass all "accessions to wealth."

Taxpayers' insistence (Br. 19-22) that damages awarded for emotional distress and harm to reputation (or any personal injury damages for that matter) only restore human capital and do not produce a "gain" or increase in wealth is unavailing. Familiar to the tax law is the idea that a taxpayer need not recognize in income any value received in respect of property that represents a return of his capital investment, *i.e.*, recovery of his tax "basis" in the property. Thus, of the amount realized on the disposition of property, the taxpayer must recognize in income only the amount that exceeds his tax basis. I.R.C. §§ 1001, 1011(a), 1012; *Lary v. United States*, 787 F.2d 1538, 1540 (11th Cir. 1986); *Hawkins v. Commissioner*, 713 F.2d 347, 354 (8th Cir. 1983); *Campbell v. Commissioner*, 504 F.2d 1158, 1164 (6th Cir. 1974).

The vague concept of "human capital," however, refers to the abstract worth a person has in his or her well-being. Because people do not pay cash or its equivalent to acquire their well-being, they have no basis in it for purposes of measuring a gain (or loss) upon the

realization of compensatory damages.[10] No doubt, the damages awarded to Ms. Murphy here were intended, in an amorphous sense, to make her "whole" by replacing her diminished emotional well-being with a monetary payment. But since her basis in her "lost" "human capital" was zero, all damages received amounted to "gain" on that "capital." Thus, contrary to taxpayers' assertion (Br. 20-22) that they realized no accession to wealth when they received the award of damages of $70,000 to compensate Ms. Murphy's injury to her well-being and reputation, in a concrete sense, taxpayers, upon their receipt of those damages, were better off by $70,000 than they were before they

[10] Even as amended in 1996, I.R.C. § 104(a)(2) allows taxpayers to exclude that part of any damages received on account of non-physical personal injury that they can show was expended for medical treatment stemming from the non-physical injury. *See* current I.R.C. § 104(a), flush language. Taxpayers do not seek to exclude any portion of the award in issue on the ground that they can substantiate medical expenses. Morever, Ms. Murphy was specifically awarded amounts, not at issue, for past and future medical expenses. (*See* 1999 WL 966951, *5.)

received that amount.[11] As explained in 1 Bittker & Lokken, ¶ 5.6 at p. 5-40:

> Taxing a recovery for personal injury or deprivation may be a harsh response to the taxpayer's misfortune, but it is not significantly different from taxing wages and salaries without allowing an offsetting deduction for the exhaustion of the taxpayer's physical prowess and mental agility during this [sic] working life. Taxpayers claiming deductions for "human depreciation" have been summarily told by the courts that Congress has not granted such an allowance. Thus, if the courts were writing on a clean slate, the personal injury issue could be analogized to the human depreciation issue. Since defamation or alienation of

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[11] Taxpayers rely (Br. 25) on one commentator's view that, because damages compensating mental distress are intended to restore a victim to the status quo, such damages are not income under the Sixteenth Amendment. F. P. Hubbard, *Making People Whole Again: The Constitutionality of Taxing Compensatory Tort Damages for Mental Distress*, 49 Fla. L. Rev. 725, 766 (1997). Professor Hubbard acknowledges, however (while taxpayers do not), that the Supreme Court has never ruled that taxing compensatory damages violates the Sixteenth Amendment. He admits that the "Supreme Court has not had to address the issue of whether compensatory damages constitute income under the Sixteenth Amendment. Instead the Court has focused on matters of statutory interpretation." *Id.* at 741.

Moreover, another commentator has reached the precise opposite conclusion, and has posited that "contrary to the contention of the detractors, the different treatment that Congress ordered in section 104(a)(2), depending upon whether the tortious act caused a physical injury, is constitutional and valid." D. A. Kahn, *The Constitutionality of Taxing Compensatory Damages for Mental Distress When There Was No Accompanying Physical Injury*, 4 Fla. L. Rev. 128 (1999).

> affections [or any other personal injury] does not entail the loss of something for which the taxpayer paid cold cash, this analogy implies that compensation for such a wrong is an accession to the taxpayer's wealth that must be included in gross income unless Congress chooses to grant an explicit exemption. [Footnotes omitted.] [[12]]

Plainly, therefore, taxpayers' contention (Br. 27-30) that Ms. Murphy's personal injury award is not income because it was received "in lieu of" or "in the nature of" her well-being is beside the point. As demonstrated above, such damage payments are subject to tax.

In sum, Congress, as a matter of legislative grace and tax policy, allows certain accessions to wealth to be excluded from gross income.

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[12] As suggested in this quotation, the "human capital" concept has been advanced to support the highly discredited contention that wages are not income within the meaning of the Sixteenth Amendment, grounded on reasoning that wages constitute nothing more than the return of the personal capital exhausted by one's labor. That argument has been uniformly rejected as frivolous. *E.g.*, *United States v. Connor*, 898 F.2d 942, 943-944 (3d Cir. 1990); *Coleman v. Commissioner*, 791 F.2d 68, 70 (7th Cir. 1986); *Connor v. Commissioner*, 770 F.2d 17, 20 (2d Cir. 1985); *Perkins v. Commissioner*, 746 F.2d 1187, 1188 (6th Cir. 1984); *United States v. Richards*, 723 F.2d 646, 648 (8th Cir. 1983); *Lonsdale v. Commissioner*, 661 F.2d 71, 72 (5th Cir. 1981); *Abrams v. Commissioner*, 82 T.C. 403, 413 (1984); *Reading v. Commissioner*, 70 T.C. 730 (1978). *See also Cullinane v. Commissioner*, 77 T.C.M. (CCH) 1192, 1193 (1999) (noting that "[c]ourts have consistently held that compensation for services rendered constitutes taxable income and that taxpayers have no tax basis in their labor").

Congress had, until 1996, excluded accessions to wealth realized in the form of personal injury damages, but in 1996 amended I.R.C. § 104(a)(2) to restrict that exclusion to only *physical* personal injury damages. Taxpayers' attempt in this case to expand the pre-amendment Congressional policy into a *constitutional* mandate is unavailing.[13]

[13] The amicus curiae posits (Br. 5-9) that amended I.R.C. § 104(a)(2) will undercut the effectiveness of the civil rights laws. Whether or not that is so, it simply is irrelevant to the question before this Court, *i.e.*, the validity of the 1996 amendment. Congress has chosen to limit the exclusion for personal injury to physical personal injury and if the amicus curiae believes that such a decision has unintended consequences, its proper course of action is to bring such concern to the attention of Congress.

II. The district court correctly held on summary judgment that the civil damages awarded to compensate Ms. Murphy for her "mental pain and anguish" and "injury to professional reputation" were not received on account of personal physical injuries or physical sickness, and thus were not excludable from income under I.R.C. § 104(a)(2).

Standard of Review

A district court's decision on summary judgment is reviewed by this Court *de novo*. *Nat'l Ass'n of Home Builders v. Norton*, 415 F.3d 8, 13 (D.C. Cir. 2005); *Hagelin v. Federal Election Com'n*, 411 F.3d 237, 242 (D.C. Cir. 2005).

Taxpayers contend (Br. 32-47) that, even if the 1996 amendment to I.R.C. § 104(a)(2) is constitutional, they nevertheless are entitled to exclude from income the $70,000 in damages awarded to Ms. Murphy. They argue that she, in fact, did receive the damages "on account of physical injuries or physical sickness," as that phrase is used in I.R.C. § 104(a)(2). The court correctly concluded (JA 26-29) that, as a matter of law, the award did not represent damages to compensate physical injury or physical sickness.

An amount may be excluded from gross income under I.R.C. § 104(a)(2) only when it is received (1) through prosecution or settlement of an action based upon tort or tort-type rights, *and* (2) on account of personal physical injuries or physical sickness. *See Schleier*, 515 U.S. at 337. The two requirements are independent and must both be satisfied in order for the exclusion to apply. *Ibid.*

The Supreme Court has construed the "on account of" phrase in I.R.C. § 104(a)(2) as requiring a *direct* causal link between the physical injury and the damages recovery in order to qualify for the income exclusion. *See Schleier*, 515 U.S. at 329-331. Then, in *O'Gilvie*, 519 U.S. at 82, the Supreme Court rejected the contention that the phrase "on account of" in § 104(a)(2) requires a mere showing of a "but for" connection between the damages received and the personal injury. The Court observed that a "but for" analysis would "bring virtually all personal injury law suit damages within the scope of the provision, since: 'but for the personal injury, there would be no lawsuit, and but for the lawsuit, there would be no damages.'" *Ibid.* The Court held, instead, that the causal link must be direct.

Thus, as the Eighth Circuit recently held in *Lindsey*, 422 F.2d at 688, "a taxpayer can satisfy the second criterion only by establishing 'a direct causal link' between the damages and the personal injuries or physical sickness sustained." There, in circumstances similar to those here, the taxpayer argued that damages he received that were labeled in a settlement agreement as compensating for tortious interference with contract, emotional distress, and harm to professional reputation, actually were to compensate his physical injuries which he also suffered as a result of the conduct of the tortfeasor. The Eighth Circuit, holding for the Government, noted that the payor did not award the damages for physical injury, and there thus was no "direct causal link between any physical sickness suffered by [the taxpayer] and damages paid out to him." 422 F.3d at 688-689.

The record conclusively establishes that Ms. Murphy's damages award was for nonphysical personal injury. In the section explaining its award of damages, entitled "Compensatory damage for emotional distress or mental anguish" (1999 WL 966951, *2–*4), the Board observed that Ms. Murphy testified "that she experienced a variety of

medical and personal problems . . . including severe anxiety attacks, inability to concentrate, a feeling that she no longer enjoyed 'anything in life,' and marital conflict," and that "[h]er description of mental anguish was supported by a psychologist, Dr. Carter, who testified about the substantial effect the negative references had on Complainant" (*id.* at *3). The Board observed that "[a]ny attempt to set a monetary value on intangible damages such as mental pain and anguish involves a subjective judgment" (*id.* at *4), and found the "ALJ's recommendation of an award of $45,000 for emotional distress is reasonable, and we adopt it" (*id.*). In a separate section, the Board further found that the ALJ's recommendation of an award of $25,000 for injury to professional reputation was reasonable. (*Id.*) In the conclusion of its order, the Board stated that it was awarding Ms. Murphy "$45,000 for mental pain and anguish" and "$25,000 for injury to professional reputation." (*Id.* at *5.) Nowhere in the Board's order is there the slightest indication that the Board intended to award damages to Ms. Murphy for any injury other than for mental pain and anguish and injury to professional reputation. Quite obviously, neither

mental pain and anguish nor injury to professional reputation constitute a physical personal injury. Indeed, such damages clearly are the quintessential type of damages that Congress, in 1996, expressly provided are no longer excludable from income. I.R.C. § 104(a)(2); flush language to § 104(a); H.R. Rep. No. 104-586, at 144, *reprinted in* 1996-3 C.B. at 482; H.R. Conf. Rep. No. 104-737, at 301, *reprinted in* 1996-3 C.B. at 1041.

Accordingly, the fact that Ms. Murphy suffered from bruxism, or teeth-grinding, does not aid her here.[14] Even assuming that bruxism qualifies as a physical personal injury, taxpayers fail to confront the essential point that, notwithstanding her physical problems, the Board awarded her damages, not to compensate those particular injuries, but explicitly with respect to nonphysical injuries, *viz.*, her mental pain and anguish and damaged professional reputation. It simply does not

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[14] Throughout their brief on appeal, taxpayers vaguely refer to "somatic" injuries suffered by Ms. Murphy, which they assert are physical injuries. To be sure, in his affidavit (JA 38-42), Dr. Carter, stated that Ms. Murphy suffered "somatic" injury, and a somatic injury is a physical one. Dr. Carter, however, did not specify what "somatic" injury Ms. Murphy suffered. Indeed, it appears that the only injury that Ms. Murphy suffered that could possibly be considered a "somatic" injury was bruxism.

matter that "but for" NYANG's violation of the whistleblower statutes in issue, Ms. Murphy would not have suffered from bruxism. The damages in issue were awarded to compensate directly only Ms. Murphy's emotional injuries—damages which Congress has expressly said do not qualify any longer for the income tax exclusion in I.R.C. § 104(a)(2).

Even if it is assumed that, by way of the award of damages for mental pain and anguish, the Board meant to compensate Ms. Murphy with respect to her bruxism, and that bruxism qualifies as a physical injury, taxpayers still would not be entitled to exclude the damages. As the legislative history of the 1996 amendments make clear, in specifically providing that emotional distress is not a physical personal injury, Congress meant to include "physical symptoms (e.g., insomnia, headaches, stomach disorders) which may result from such emotional distress."[15] H.R. Rep. No. 104-586, at 144 & n.24, *reprinted in* 1996-3

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[15] The legislative history also provides that the exclusion was not meant to apply to damages received "based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress." H.R. Rep. No. 104-586, at 144, *reprinted in* 1996-3 C.B. at 482; H.R. Conf. Rep. No. 104-737, at 301, *reprinted in* 1996-3

(continued...)

C.B. at 482 & n.24; H.R. Conf. Rep. No. 104-737, at 301 & n.56, *reprinted in* 1996-3 C.B. at 1041 & n.56.[16] Thus, as the district court correctly concluded here (JA 29), a physical symptom of a nonphysical injury does not qualify for the exclusion. And, as the district court further correctly concluded, Ms. Murphy's bruxism plainly was a symptom of the metal pain and anguish she suffered. Indeed, it is difficult to conceive how being blacklisted can result in a purely physical injury, as opposed to a physical manifestation of mental pain and anguish. Not surprisingly, therefore, taxpayers' own evidence establishes that bruxism is a symptom of emotional distress. Dr.

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[15](...continued)
C.B. at 1041. Plainly, therefore, the damages Ms. Murphy received for damage to her professional reputation do not qualify as physical personal injuries and, although they do not clearly so state, we do not understand taxpayers to contend otherwise.

[16] Taxpayers contend (Br 41-45) that because bruxism is not specifically enumerated in the legislative history to be a symptom of emotional distress, it should be viewed as a separate personal physical injury for which Ms. Murphy received damages. The symptoms enumerated in the legislative history are obviously mere examples of injuries that are directly attributable to emotional stress and not a complete list thereof. *See Lindsey*, 422 F.3d at 688 (finding that symptoms of emotional stress within the meaning of § 104(a) include hypertension, periodic impotency, fatigue, and indigestion).

Kurzer, Ms. Murphy's dentist, stated in his affidavit (JA 44, ¶ 11) that it was his professional opinion "that bruxism can be the result of a substantial increase in stress and that stress is the number one cause of bruxism."

Taxpayers assert (Br. 34, 39-41) that the meaning of the 1996 amendment was plain and therefore the district court erred by consulting the amendment's legislative history. In this regard, taxpayers posit that there is no ambiguity with respect to the meaning of the phrase "physical injuries." Whether or not this is so, the district court did not consult the legislative history to determine what was meant by the phrase "physical injury," but, instead, to determine what Congress meant by the use of the phrase "emotional distress" when it provided in the flush language of I.R.C. § 104(a) that "emotional distress shall not be treated as a physical injury." We submit that the most natural reading of the phrase "emotional distress" would include all symptoms of such distress, be they physical or nonphysical. But the precise contours of what Congress meant by "emotional distress" is hardly crystal clear and resort to the legislative history plainly was

warranted. Moreover, the legislative history, does not, as taxpayers seem to contend (Br. 41), rewrite the statute. It merely clarifies what "emotional distress" means. The district court was thus correct to hold (JA 29) that because the physical injury suffered by Ms. Murphy was attributable to her emotional distress (and not "the other way around"), it was not a physical injury for purposes of § 104(a)(2).

CONCLUSION

The order of the district court is correct and should be affirmed.

Respectfully submitted,

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It is hereby certified that this brief was mailed to the Clerk by First Class Mail on this 21st day of December, 2005. It is also certified that service of this brief has been made on counsel for the appellants and on counsel for the amicus curiae on this 21st day of December, 2005, by sending two copies thereof to each, by First Class Mail in envelopes, properly addressed as follows:

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ADDENDUM

Table of Contents to Addendum

STATUTES AND REGULATIONS

Internal Revenue Code of 1986 (26 U.S.C.):

SEC. 61. GROSS INCOME DEFINED.

(a) General Definition.—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, fringe benefits, and similar items;
(2) Gross income derived from business;
(3) Gains derived from dealings in property;
(4) Interest;
(5) Rents;
(6) Royalties;
(7) Dividends;
(8) Alimony and separate maintenance payments;
(9) Annuities;
(10) Income from life insurance and endowment contracts;
(11) Pensions;
(12) Income from discharge of indebtedness;
(13) Distributive share of partnership gross income;
(14) Income in respect of a decedent; and
(15) Income from an interest in an estate or trust.

SEC. 104. COMPENSATION FOR INJURIES OR SICKNESS.

(a) In General.—Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include—

(1) amounts received under workmen's compensation acts as compensation for personal injuries or sickness;

(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness;

(3) amounts received through accident or health insurance (or through an arrangement having the effect of accident or health insurance) for personal injuries or sickness (other than amounts received by an employee, to the extent such amounts (A) are attributable to contributions by the employer which were not includible in gross income of the employee, or (B) are paid by the employer);

(4) amounts received as a pension, annuity, or similar allowance for personal injuries or sickness resulting from active service in the armed forces of any country or in the Coast and Geodetic Survey or the Public Health Service, or as a disability annuity payable under the provisions of section 808 of the Foreign Service Act of 1980; and

(5) amounts received by an individual as disability income attributable to injuries incurred as a direct result of a terrorist or military action (as defined in section 696(c)(2)).

For purposes of paragraph (3), in the case of an individual who is, or has been, an employee within the meaning of section 401(c)(1) (relating to self-employed individuals), contributions made on behalf of such individual while he was such an employee to a trust described in section 401(a), which is exempt from tax under section 501(a), or under a plan described in section 403(a), shall, to the extent allowed as deductions under section 404, be treated as contributions by the employer which were not includible in the gross income of the employee. For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraph (A) or (B) of section 213(d)(1)) attributable to emotional distress.