

Practice Update

Tax Reform: New Act Eliminates Deduction for Settlement of Sexual Harassment Claims Subject to a Confidentiality Agreement

January 12, 2018

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In a little noticed and controversial provision, the Tax Act created a new Internal Revenue Code provision (Code Sec. 162(q)), that eliminates a business expense deduction for: (1) “any settlement or payment related to sexual harassment or sexual abuse, if the settlement or payment is subject to a nondisclosure agreement,” and (2) “attorney’s fees related to” such settlement or payment.

This change is effective for all amounts paid or incurred after Dec. 22, 2017, the date of enactment.

Thus, *effective immediately*, the Tax Act denies a deduction for *any* settlement, payout, or attorney fees *related to* sexual harassment or sexual abuse if the payments are subject to a *confidentiality* agreement.

Code Section 162(q) is very broadly drafted and begs more questions than it answers, such as what is considered a settlement or payment *related to* sexual harassment or sexual abuse, or how the deduction would be impacted if multiple claims are asserted and settled. Further, there is a dearth of guidance beyond the flush language. Indeed, Sen. Robert Menendez (D-NJ) who introduced the original

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Senate amendment was critical of the final version and issued a statement saying he plans to introduce legislation to,

fix an egregious error...that failed to accurately reflect the legislative intent.... [which] at best has led to confusion, and at worst will inadvertently lead to sexual misconduct victims being further victimized. This is outrageous and maddening, and what inevitably can occur when members are forced to vote on haphazardly rushed legislation before even getting a chance to read it.

Under pre-Tax Cuts and Jobs Act law, there was no rule denying a business expense deduction for a payment to settle a sexual abuse or harassment suit subject to a confidentiality agreement, or attorney's fees related to the settlement. In general, taxpayers may deduct ordinary and necessary business expenses paid or incurred in carrying on any trade or business, subject to certain exceptions. Payment of a judgment or settlement of a suit or claim arising out of a business matter is generally deductible as a business expense.

Based on Sen. Menendez's comments, we hopefully will see further guidance and refinement in the future, whether through a technical corrections bill, IRS regulations or other promulgation. It is unclear at this time whether any such changes would be retroactive to the date of enactment or prospective only. While this is certainly an important issue, additional clarification is necessary to ensure the intent of the provision is accomplished.

Until there is further guidance, please contact a member of the Akerman Tax Group if such circumstances arise.

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