DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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[redacted]

Attention: [redacted]

Dear [redacted]:

This letter is in response to your inquiry concerning the request for a private letter ruling submitted by the [redacted]. The [redacted] successfully represented certain clients in an inverse condemnation proceeding. As prevailing plaintiffs, the [redacted] clients became entitled to an award of attorneys' fees under the Uniform Relocation Assistance and Real Property Acquisition Policies Act (URA), 42 U.S.C. §§ 4601-55. In March 2003, the [redacted] requested a ruling that attorneys' fees recovered by *pro bono* counsel for vindicating the constitutional rights of these clients not be included in the gross income of these clients under § 61(a) of the Internal Revenue Code. Relying on well-established legal principles, the IRS advised the [redacted] that it would rule adversely; subsequently, the [redacted] withdrew its request.

In a fundraising letter dated October 30, 2003, the [redacted] challenged the IRS position as unsupported by either the facts or the law. Neither challenge has any merit. The traditional American rule is that a prevailing litigant may not ordinarily recover attorneys' fees unless authorized by statute. *Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 247, 257 (1975). However, the Congress has enacted statutes, such as the URA, that relieve prevailing parties of the burden of paying litigation costs in vindicating certain important rights and shift the burden to the losing party. These statutes typically shift the burden only if attorneys' fees are actually incurred by the client and do not permit the recovery of fees by *pro se* plaintiffs.

To recover incurred attorneys' fees, the [redacted] clients would have had to satisfy the court that, in the least, an implied agreement existed that the representation, although nominally *pro bono*, would be undertaken on condition that the clients would seek and remit to the [redacted] any attorneys' fees recovered under the URA. *Preseault v. United States*, 52 Fed. Cl. 667 (2002).

The Supreme Court of the United States has ruled definitively that attorneys' fees recovered under fee shifting statutes belong to the prevailing party (generally plaintiffs), not to the lawyers. *See Venegas v. Mitchell*, 495 U.S. 82, 87 (1990) and *Evans v. Jeff D.*, 475 U.S. 717, 730 (1986). These cases involved awards recovered under the Civil Rights Attorney's Fees Awards Act of 1976, 42 U.S.C. § 1988. We believe the same principle applies to the attorneys' fees to which the [redacted] clients became entitled for vindicating their claim of unconstitutional taking against the government.

The [redacted] suggestion that no court supports the IRS' view is incorrect. This principle has been applied by the courts in holding that a taxpayer must include in gross income attorneys' fees recovered under a similar fee-shifting statute. In *Sinyard v. Commissioner*, T.C.M. 1998-364, *aff'd*, 268 F.3d 756 (9th Cir. 2001), the courts, agreeing with the IRS, concluded that the taxpayers must include in their gross income the attorneys' fees recovered from the defendant under the Age Discrimination in Employment Act (ADEA). In reaching its conclusion, the Ninth Circuit cited approvingly the opinions of the Supreme Court in *Evans* and *Venegas*. The [redacted] requested the ruling after the Ninth Circuit rendered its opinion in *Sinyard*.

The [redacted] letter suggests that other organizations have received similar awards and have not been told that the fees belong to their clients. The IRS' position is that the client owns the entire cause of action, including any claim for attorneys' fees, and must include in gross income the entire amount of a settlement or judgment, undiminished by any fees paid to the attorney. Some courts disagree with the IRS' view. Recently, the government requested the Supreme Court to review the adverse opinions in *Banks v. Commissioner*, 345 F.3d 373 (6th Cir. 2003), and *Banaitis v. Commissioner*, 340 F.3d 1074 (9th Cir. 2003). Accordingly, a favorable ruling to the [redacted] or any other similarly-situated organization would be inconsistent with the IRS' litigating position. The majority of appellate courts agree with the IRS, and we anticipate that the Supreme Court will resolve the conflict among the circuits.

I hope this information is helpful. If you have any questions, please call [redacted] Identification Number [redacted], at [redacted].

Sincerely,

Robert A. Berkovsky
Branch Chief,
Office of Associate Chief Counsel
(Income Tax & Accounting)