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BY ELECTRONIC MAIL

Pacific Life Insurance Company
700 Newport Center Drive
Newport Beach, CA 92660
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RE: Tax Opinion Regarding Attorney Fee Structure Program

Ladies and Gentlemen:

You have requested our opinion regarding the federal income tax treatment of certain periodic payments made to a plaintiff's attorney pursuant to the traditional attorney fee structure program which you administer. You also have asked us to consider the impact of the recent generic legal advice memorandum (the "**2022 GLAM**" or "**GLAM**") issued by the Internal Revenue Service (the "**IRS**") on December 9, 2022 addressing a different structure for deferral of attorney fees.

For the reasons discussed below, we conclude that your program meets the requirements of a "Standard Fee Structure" and the attorneys who participate in the program should be taxable on each periodic payment in the year each such payment is received. The analysis in the 2022 GLAM does not change this conclusion.

I. BACKGROUND

A. Standard Attorney Fee Structures

1. General Structure

In a "**Standard Fee Structure**," a plaintiff will agree to receive a settlement or damages award as a series of periodic payments over several years rather than as a lump-sum payment in the year the lawsuit is resolved. (This arrangement is informally referred to as a "structure.") The plaintiff's attorney (who has been retained on a contingent fee basis) also will agree to receive his or her fee as each periodic payment is made. Rather than make the periodic

payments itself, the defendant[1] will assign its obligation to a third-party "assignment company," to which it pays a lump-sum for assuming the obligation. The assignment company then uses the payment to acquire an asset that will produce an income stream sufficient to fund the future periodic payments to the plaintiff and the attorney. The defendant in turn is released from its obligations to make any future payments. In a variation on the Standard Fee Structure, an attorney may agree at the outset of his/her representation of the plaintiff (or sometime thereafter, but in either case prior to the plaintiff's recovery) to structure his or her fee regardless of whether the plaintiff chooses to structure.

The plaintiff and defendant subsequently enter into a settlement agreement that will, among other things, state the schedule of periodic payments to be made. The defendant then enters into an assignment agreement with the assignment company, pursuant to which the assignment company will assume the defendant's obligation to make the periodic payments. The assignment agreement will state that the assignment company owns the asset which funds the periodic payments and that neither the plaintiff nor the attorney has any rights against the assignment company other than those of an unsecured general creditor.

2. Qualified Assignments

A plaintiff who has suffered a physical injury or sickness typically will structure his or her settlement as a "qualified assignment" pursuant to Section 130 of the Internal Revenue Code of 1986, as amended (the "**Code**"). To be a qualified assignment under Section 130, the plaintiff's damages must be on account of a personal physical injury or physical sickness within the meaning of Section 104(a)(2) of the Code (and thus excluded from gross income). In addition, the periodic payments the plaintiff receives (i) must be fixed and determinable as to amount and timing, (ii) cannot be accelerated, deferred, increased, or decreased by the recipient, and (iii) must be funded by a "qualified funding asset," which is either an obligation of the U.S. government (*i.e.*, T-Bills) or an annuity contract issued by a life insurance company.[2] If these requirements are met, the assignment company is not taxable on the lump-sum payment it receives from the defendant.[3]

As part of the arrangement, the plaintiff will consent to the defendant's assignment of its obligation to remit the periodic payments to the assignment company. The plaintiff, the defendant, the assignment company, and the attorney are all parties to the arrangement.

B. Pacific Life's Arrangement

You have represented to us the following facts, which we have accepted as true without independent verification:

Pacific Life Insurance Company ("**Pacific Life**") issues life insurance policies and annuity contracts which are used as the qualified funding asset for qualified assignments. Through its wholly-owned assignment company, Pacific Life & Annuity Services, Inc. ("**PLASI**"), Pacific

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[1] References to a "defendant" also include the defendant's insurer.

[2] See Section 130(c) and (d).

[3] See Section 130(a).

Life administers a Standard Fee Structure program (the "**Pacific Life Program**" or "**Program**") for claimants who enter into qualified assignments and whose attorneys (each, an "**Attorney**") wish to receive some or all of their contingent fee income (the "**Fee**") as the claimant receives each periodic payment to which it is entitled under the qualified assignment.

A claimant who enters into a qualified assignment must sign a Qualified Assignment and Release Agreement (a "**QAR**") which names PLASI as the assignee and Pacific Life as the annuity issuer. The Attorney is a signatory to the QAR and must approve the QAR as to form and content. In addition, an Attorney whose client does not enter into a qualified assignment also may participate in the Program and receive his or her Fee in periodic payments pursuant to a stand-alone qualified assignment. In either case, the claimant must acknowledge that any funds paid to the Attorney are for the claimant's convenience (because such funds satisfy the claimant's obligation to pay the Attorney). PLASI generally requires that the settlement agreement between the claimant and defendant reference the qualified assignment, and the Attorney has no right to its Fee nor to any periodic payments until after the settlement agreement is executed.

The Attorney must complete an Acknowledgment and Hold Harmless Agreement for Attorney Fees (the "**Acknowledgment**"), which (in pertinent part) states as follows:

> I understand and acknowledge that the payments to be received by me as attorney fees are being made to me at the direction of the claimant in order to discharge the claimant's liability to me for attorney fees in exchange for service rendered. Nothing contained in any agreement or applicable law results in either me or my firm having any ownership interest in any portion of the annuity or the settlement other than the right to receive the payments in the future when such payments would otherwise be made to the claimant.
>
> I understand and agree that regardless of the consequences my firm and I will be paid in accordance with the periodic payment terms of the above described settlement agreement. I further understand and agree that such periodic payments may not be accelerated, deferred, increased or decreased and may not be anticipated, sold, assigned or encumbered.

In addition to signing the Acknowledgment, the Attorney also must complete an Individual Single Premium Settlement Annuity Application (the "**Application**"). According to Pacific Life's internal Procedures Manual for Structured Settlements (dated April 2022), the Attorney must be designated as the "Measuring Life" on the Application. However, PLASI is designated as the owner of the annuity (which serves as the qualified funding asset) on the Application.

II. ANALYSIS

A. General Rules Regarding Income Recognition Rules: The Constructive Receipt, Economic Benefit, and Cash Equivalence Doctrines

Gross income includes amounts received as compensation for services, including contingent attorneys' fees. See Sec. 61(a)(1) (income includes "[c]ompensation for services, including fees"). Under Section 451(a), the amount of any item of gross income must be included in income for the taxable year in which the taxpayer receives the income, unless under the method of accounting the taxpayer uses in computing taxable income, such amount is to be properly accounted for as of a different period. For a taxpayer who computes and reports income under the cash receipts and disbursements method (*i.e.*, a "cash basis" taxpayer), income from gains, profits, and compensation are includible in gross income when actually received unless the constructive receipt doctrine, the economic benefit doctrine, or the cash equivalence doctrine otherwise accelerates the taxpayer's recognition of income. See Treas. Regs. Sec. 1.446-1(c)(1)(i) ("under the cash receipts and disbursements method in the computation of taxable income, all items which constitute gross income, whether in the form of cash, property, or services, are to be included for the taxable year in which actually or constructively received") (internal parentheses omitted); Treas. Regs. Sec. 1.451-1(a) ("Gains, profits, and income are to be included in gross income for the taxable year in which they are actually or constructively received by the taxpayer unless includible for a different year in accordance with the taxpayer's method of accounting"). All individual taxpayers report income under the cash method, as do most law firms.

As further discussed below, these doctrines may apply regardless of whether the income is actually reduced to the taxpayer's possession.

1. Constructive Receipt Doctrine

A taxpayer is in constructive receipt of income if the income is credited to the taxpayer's account, set apart for the taxpayer, or otherwise made available so that the taxpayer may draw upon it at any time, or so that the taxpayer could have drawn upon it if notice of intention to withdraw had been given. Treas. Regs. Sec. 1.451-2(a); Rev. Rul. 66-45, 1966-1 C.B. 95 (interest on nonnegotiable savings certificates, payable only upon the surrender and redemption of the certificates, is includable in a cash-basis taxpayer's income in each taxable year in which the taxpayer either has the right to redeem the certificate or could have had such a right through a written demand for payment). If the taxpayer's control of its receipt of such income is subject to substantial limitations or restrictions, income is not constructively received. Treas. Regs. Sec. 1.451-2(a).

A taxpayer will not recognize income under the constructive receipt doctrine merely because the taxpayer seeks deferral of payments as part of a negotiated settlement, as long as the deferred payment agreement is binding between the parties and is made prior to the time the taxpayer acquires an absolute and unconditional right to receive the payment. Reed v. C.I.R., 723 F.2d 138, 142 (1st Cir. 1983) ("a taxpayer-seller has the right to enter into an agreement with the buyer that he, the seller, will not be paid until the following year. As long as the deferred payment agreement is binding between the parties and is made prior to the time when the taxpayer-seller

has acquired an absolute and unconditional right to receive payment, then the cash basis taxpayer is not required to report the sales proceeds as income until he actually receives them") (internal citations omitted).

In addition, an existing agreement which "has been amended or modified to provide for deferred payment of an amount ***not yet due*** serves to postpone" the recognition of that income. Reed, 723 F.3d at 143 (emphasis added). However, if the taxpayer possesses the right to receive the income before a deferral mechanism is established, the taxpayer must currently recognize the full amount of the payments as income. See Williams v. U.S., 219 F.2d 523, 527 (5th Cir. 1955) ("when the lumber company's bid was accepted, and it desired and offered to comply with it by paying the full purchase price, the taxpayers were then in constructive receipt of it, and that the self imposed limitation of the escrow device did not in fact and in law change the situation so as to make the funds any less available to, and constructively received by them"); Rev. Rul. 69-50, 1969-1 CB 140 (taxpayer cannot defer recognition of non-employee compensation for services rendered by unilaterally electing to do so where it has the unrestricted right to receive the compensation in the year services are rendered).

The IRS has applied these principles in the structured settlement context. In Revenue Ruling 2003-115, 2003-2 C.B. 1052, the IRS held that constructive receipt and economic benefit doctrines did not apply to the settlement of claims under the September 11 Victim Compensation Fund where claimants irrevocably elected to receive periodic payments while control of receipt of payment was subject to substantial restrictions. Relying in part on Revenue Ruling 2003-115, in PLR 200836019 (Sept. 5, 2008) the IRS held that an employment discrimination plaintiff who receives periodic payments under a non-qualified structured settlement arrangement (*i.e.*, a structure that does not satisfy the requirements of Section 130) is not in actual or constructive receipt of the periodic payments until he or she receives each payment. Instead, in accordance with Section 451, the taxpayer includes each payment in income for the taxable year in which the payment is received. Both Revenue Ruling 2003-115 and PLR 200836019 involve assignment companies which assumed payment obligations and then purchased annuities to fund the periodic payments to the claimant(s).

Accordingly, an Attorney in a Standard Fee Structure should not recognize his or her Fee in the year of settlement under the constructive receipt doctrine.

2. Economic Benefit Doctrine/Section 83 of the Code

a) Economic Benefit Doctrine Generally

The economic benefit doctrine applies where funds are irrevocably set aside for the taxpayer's benefit and there are no material contingencies restricting the taxpayer's right to utilize the amount. See IRS Gen. Couns. Mem. 337333 (Nov. 21, 1966) ("Pursuant to the [economic benefit doctrine] the creation by an obligor or a fund in which the taxpayer has vested rights will result in immediate inclusion by the taxpayer of the amount funded. A 'fund' is created when an amount is irrevocably placed with a third party, and a taxpayer's interest in such fund is 'vested' if it is nonforfeitable"); C.I.R. v. Smith, 324 U.S. 177, 181 (1945) ("The Revenue Act is broad

enough to include in taxable income any economic or financial benefit conferred on the employee as compensation whatever the form or mode by which it is effected").

In contrast to constructive receipt, under the economic benefit doctrine the taxpayer need not have the power to take immediate possession nor have something that is readily convertible into cash in order to recognize income currently; rather, the critical issue is that the assets set aside are certain to be available to provide the future payments. In Sproull v. C.I.R., 16 T.C. 244 (1951), the Tax Court held that the economic benefit doctrine applied where a corporation, in 1945, placed $10,500 in trust for the benefit of its president, representing additional compensation for services previously rendered. The funds were to be paid to the taxpayer in two installments over the following two years (*i.e.*, in 1946 and 1947). The court ruled that the taxpayer was taxable on the full $10,500 in 1945, when the funds were irrevocably placed in trust, and not in the subsequent years when he actually received the amounts. The Court of Appeals for the Ninth Circuit reiterated this point in Minor v. U.S., 772 F.2d 1472, 1474 (9th Cir. 1985), where it stated that "In cases where courts or the IRS have found a current economic benefit to have been conferred, the employer's contribution has always been secured or the employee's interest has been nonforfeitable." Minor involved a deferred compensation plan for physicians established by the medical practice that employed them. The medical practice was the settlor of a trust established to provide for the future obligations to the physicians, and the trust purchased retirement annuity policies to provide for the payment of benefits under the plan. The participants had no right, title or interest in the trust agreement or any asset held by the trust and thus no rights greater than those of a general creditor of the medical practice. As a result, the physicians were not taxable upon the funding of the trust. See 772 F.2d at 1473, 1476.

Consistent with the reasoning of Minor, Revenue Ruling 2003-115 holds that claimants of the September 11 Victim Compensation Fund did not realize the economic benefit of the full amount of their claim when approved as long as they irrevocably elected to receive their award as periodic payments prior to their claims becoming "substantially complete." In the ruling, (i) the assignment company assumed the original obligor's payment obligation, (ii) the assignment company acquired an annuity contract to fund its payment obligation, and (iii) the victim's rights against the assignment company were limited to those of a general creditor.

b) Deferred Compensation Rulings

Between 1960 and 1972, the IRS issued several revenue rulings addressing the treatment of deferred compensation plans. Although these rulings deal primarily with the constructive receipt doctrine, they also establish how the economic benefit doctrine applies to deferred compensation arrangements. The rulings establish the following general requirements for deferral of income: (i) the arrangement must be entered into prior to the point in time when the recipient's right to the income has materialized; (ii) the election to defer must be irrevocable, such that the recipient cannot obtain the benefit of the amounts deferred until they are due and payable under the terms of the plan; (iii) the asset securing the obligation (either cash, an insurance policy, or an annuity contract) must be owned, both legally and beneficially, by the payor; and (iv) the asset securing the obligation must be subject to the claims of the payor's general creditors.

(i) Revenue Rulings Involving Deferred Salaries or Fees

In Revenue Ruling 60-31, 1960-1 C.B. 147, the IRS considered the tax treatment of five scenarios involving deferred compensation arrangements. The first two scenarios involved arrangements between employers and employees. In the first scenario, the employer credited each participant's compensation to a "bookkeeping reserve account," had only a contractual obligation to make payments when due, and the parties did not intend that the amounts in reserve be held in trust for the taxpayer. In the second scenario, the employer credited a certain portion of its annual net earnings to separate accounts for plan participants, was under only a mere contractual obligation to make the future payments, and no amounts were held in trust. The IRS held that the employees in each scenario were taxable on the compensation credited under each plan in the year of receipt. In the third scenario, an author and a publisher executed an agreement under which the author granted the publisher the exclusive right to publish his book; simultaneously with that agreement, the parties executed a "supplemental" agreement pursuant to which the publisher would pay the taxpayer no more than "$100x" per year and the excess would be carried over by the publisher to succeeding accounting periods. The amounts were not segregated on the publisher's books. The IRS held that the author could defer recognition of income on the excess payments in income until the taxable year in which they were received, and noted that the supplemental agreement was made before any amounts were earned. In the fourth and fifth scenarios, the taxpayers provided services to a third party which placed the amounts earned in escrow for the taxpayers' future benefit; the IRS held that the taxpayers were taxable on the amounts in the year the service recipient placed the amounts in an escrow account which was set aside for their exclusive benefit.

In Revenue Ruling 69-650, 1969-2 C.B. 106, an employee elected (pursuant to his employment contract) to defer receipt of a portion of his scheduled salary for distribution following the termination of his employment. The contract provided that the employee's election to defer receipt was irrevocable and required the employer to establish a "deferred compensation account" to which was credited the amount the employee elected to defer. The amounts deferred would eventually be satisfied from the general corporate funds, subject to the claims of the employer's other creditors. The IRS held that portion of the employee's compensation which was deferred pursuant to the contract was includible in the employee's income only in the later taxable years in which it was received. The IRS considered a substantially similar arrangement in Revenue Ruling 71-419, 1971-2 C.B. 220; there, fees payable by a corporation to its directors were deferred pursuant to an "unfunded deferred compensation plan" which required the corporation to maintain a separate memorandum account to which the deferral amount was credited. The election to defer fees continued from year to year unless a director terminated the election by written request; however, any amounts previously deferred could not be paid to him until he ceased being a director. Citing Revenue Ruling 60-31, the IRS held that since the plan was unfunded and the corporation's obligations under the plan were unsecured, the directors were not taxable on amounts deferred under the plan until they were paid.

(ii) Revenue Rulings Involving the Use of an Insurance Policy or Annuity Contract as a Funding Asset

During the same time period, the IRS issued similar rulings involving deferred compensation arrangements where the payor's future obligations are funded by an insurance policy

or annuity contract owned by the payor. In Revenue Ruling 68-99, an individual entered into an employment contract which provided for the payment of a pension commencing on the termination of the individual's employment. The employer in turn entered into a contract with an insurance company for insurance on the employee's life to fund the future payments. All rights to benefits under the insurance contract were solely the property of the employer and the proceeds of the contract were payable by the insurance company only to the employer. (Although the ruling does not say so, presumably the insurance policy was an asset subject to the claims of the employer's creditors.) The IRS held that the employee was not taxable upon the employer's purchase of the insurance contract because the transaction did not "produce a present economic benefit to the employee."

Similarly, in Revenue Ruling 72-25, 1972-1 C.B. 127, an employer purchased an annuity contract to fund its deferred compensation liability; the employer was the applicant, owner, and beneficiary of the annuity contract, and the contract was subject to claims of the employer's general creditors. The employee had no legal rights to the annuity contract: the benefits under the arrangement "[we]re not subject in any manner to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance, or liable for the debts, contracts, liabilities, engagements or torts of the taxpayer or his beneficiary." The IRS held that the employee did not acquire a present interest in either the amounts credited by the employer to the plan or in the annuity contract used to fund the arrangement.

(iii) The "Rabbi Trust" Private Letter Ruling

In PLR 8113107 (Dec. 31, 1980), the IRS approved a deferred compensation arrangement where a congregation created and funded an irrevocable grantor trust[4] (to which it contributed cash) to fund future payments to its rabbi. The assets held in the trust were the general assets of the congregation and subject to the claims of its creditors. The IRS held that because the assets of the trust estate were subject to the claims of the congregation's creditors and were not paid or made available to the rabbi, the funding of the trust did not constitute a taxable event to the rabbi. This ruling became the basis for Revenue Procedure 92-64, 1992-2 C.B. 422, which provides model grantor trust (the so-called "rabbi trust") language for use in executive compensation arrangements. The letter ruling and the subsequent revenue procedure are significant insofar as they effectively obsolete Revenue Ruling 69-50, 1969-1 C.B. 140, which held that non-employee physicians constructively received amounts credited to them pursuant to a deferred compensation plan administered by the non-profit corporation whose patients the physicians cared for because the patients previously compensated the corporation for the physicians' services, thus conferring upon the physicians an indirect economic or financial benefit. (In this sense, the ruling appears to assume that the amounts paid to the corporation by the physicians' patients and earmarked for the physicians were not subject to the claims of the corporation's general creditors.)

c) Judicial Authorities Addressing Deferred Compensation Arrangements Involving Annuity Contracts

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[4] Under Section 671, if for income tax purposes the grantor of a trust is treated as the "owner of any portion of a trust," the trust is a "grantor trust" and the grantor is taxable on the items of income, deductions, and credits which are allocable to the portion of the trust of which the grantor is considered the owner.

A side-by-side comparison of the decisions in U.S. v. Drescher, 179 F.2d 863 (2nd Cir. 1950) and Goldsmith v. U.S., 586 F.2d 810 (Ct. Cl. 1978) illuminates the difference between a deferred compensation plan funded by an annuity which results in an immediately taxable economic benefit to the taxpayer versus one that does not.

In Drescher, an employer purchased from an insurance company a non-forfeitable, single-premium annuity contract which named the employee as the annuitant. The employer retained possession of the contract and deducted the amount of the single premium it paid as part of the compensation paid to the employee. The policy also gave the employee (as the annuitant) an option to accelerate the date on which monthly payments commence, but the option was required to be exercised by the annuitant in writing and endorsed on the policy; thus, the option could not be exercised as long as the employer retained possession of the policy. The contract itself was not assignable and it and all of the payments due under it were free from "the claims of all creditors to the fullest extent permitted by law." Accordingly, the court held that the employee received a present economic benefit—namely, "the obligation of the insurance company to pay money in the future to him or his designated beneficiaries on the terms stated in the policy." 179 F.2d at 865; see also Brodie v. C.I.R., 1 T.C. 275, 281-82 (1942) (same holding in a similar circumstance where "the contract so purchased was issued in the name of the annuitant and was delivered to him and was part of the plan for his additional remuneration").

In Goldsmith, on the other hand, a hospital purchased a life insurance endowment policy to fund a deferred compensation arrangement between it and a physician. The policy was issued on the life of the physician and named the hospital as the owner and beneficiary. The arrangement had two components: (i) the physician would receive benefits upon reaching age 65, and (ii) the physician's children would receive a death benefit if he died before retirement while still employed. The hospital had no obligation to "set aside, earmark, or entrust any fund or money with which to pay its obligations", the physician was to "be and remain simply a creditor of the Hospital in the same manner as any other creditor having a general claim for unpaid compensation" when the benefits became payable, and "at no time" was the physician to "be deemed to have any right, title, or interest in or to any specified asset or assets of the Hospital, including…any life insurance or annuity contract." 586 F.2d at 393-94. The court concluded that the physician did not realize an economic benefit upon the employer's purchase of the policy:

> The taxpayer in the instant case had no rights in the withheld sums either against his hospital or the insurance company. The hospital was the sole owner and beneficiary of the policy, and the taxpayer could rely only on the credit of the hospital and the strength of its promise. In the event of the hospital's bankruptcy, he would be an unsecured, general creditor; his claim against its assets would have rested on no firmer ground than those of other creditors similarly situated. [Unlike] in Llewellyn v. Commissioner, 295 F.2d 649 (7th Cir. 1961), whose facts are similar to the instant case, the taxpayer-doctor was held in constructive receipt because he

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> owned the annuity policies procured by his hospital under the agreement.

Id. at 818-19 (certain internal citations to authority omitted). However, the court did conclude that the physician was currently taxable on the death benefit component of the arrangement because it represented "the familiar undertakings of a life insurance company"; therefore, "To the extent of these promises [*i.e.*, the death benefit], the deferred compensation agreement provided the taxpayer with a current economic benefit as valuable as comparable promises by a life insurance company." Id. at 821. Accordingly, the "[t]axability [of the death benefit component] is as plain as the taxability of an insurance premium paid by an employer, in other than a qualified pension or group plan, on a policy of which the employee is a beneficiary." Id.; see also Centre v. C.I.R., 55 T.C. 16 (1970) (where employer acquired an insurance policy to fund its obligation to make deferred compensation payments and was the owner and beneficiary of the policy prior to the employee's termination but assigned the policy to him upon termination, the employee was not taxable under the economic benefit doctrine while the employer paid the premiums during his employment but did become taxable when the insurance policy was assigned to him).

As a timing matter, the Goldsmith court noted that the deferral was "part of the bargain struck by the parties before the taxpayer acquire[d] the right to the deferred sums." Id. at 400 n.3. The court also rejected the notion that the arrangement lacked economic substance because its purpose was to defer income. Id. at 403 (stating that although "all such agreements might be contended to be devices without business purpose created solely for their effect on taxes," in light of the IRS's prior rulings and applicable judicial decisions, "the Government may not be heard to urge constructive receipt of deferred compensation on the ground that the plan was put into effect at the 'individual desire' or 'option' of the taxpayer").

Therefore, the recipient of deferred compensation payments should not recognize income at the time a payor acquires a life insurance policy or annuity contract to fund its payment obligations as long as the payor is and remains the owner of the policy or contract and the beneficiary thereunder. In addition, the Goldsmith court's language on timing (as quoted above) is especially instructive for arrangements that fall outside the traditional employer/employee context: the deferral arrangement must be put into place "before the taxpayer ***acquires the right*** to the deferred sums." Id. at 400 n.3 (emphasis added).

d) Section 83 of the Code

Section 83 generally provides that where, in connection with the performance of services, property is transferred to any person other than the person for whom the services are performed, gross income of the party providing the services shall include (i) the fair market value of the property transferred (determined without regard to any restriction other than a restriction which by its terms will never lapse), minus (ii) the amount (if any paid) for such property, at the first time the rights of the person having the beneficial interest in such property are transferable or are not subject to a substantial risk of forfeiture. Treasury Regulations Section 1.83-3(e) provides that the term "property" includes (i) real and personal property other than either money or an unfunded and unsecured promise to pay money or property in the future as well as (ii) a beneficial

interest in assets (including money) which are transferred or set aside from the claims of creditors of the transferor, for example, in a trust or escrow account.

The IRS has recognized that Section 83 generally codifies the economic benefit doctrine. See IRS Pub. 5528 (Rev. 6-2021), Cat. No. 37690C, "Nonqualified Deferred Compensation Audit Technique Guide," at p. 6 (stating that Section 83(a) "codified elements of the economic benefit doctrine by providing that, generally, if property is transferred to a person as compensation for services, such person will be taxed at the time of receipt of the property when it is either transferrable or not subject to a risk of forfeiture").

3. Cash Equivalence Doctrine

Finally, the doctrine of cash equivalence applies where a taxpayer receives a right to income in the future that is readily convertible into cash in the present. See Cowden v. C.I.R., 289 F.2d 20, 24 (5th Cir. 1961) ("if a promise to pay of a solvent obligor is unconditional and assignable, not subject to set-offs, and is of a kind that is frequently transferred to lenders or investors at a discount not substantially greater than the generally prevailing premium for the use of money, such promise is the equivalent of cash and taxable in like manner as cash would have been taxable had it been received by the taxpayer rather than the obligation"); see also Watson v. v. C.I.R., 613 F.2d 594, 597 (5th Cir. 1980) (applying Cowden to hold that a letter of credit constituted income in the year received).

Where an attorney receives a promise to pay structured attorneys' fees, that promise should not give rise to immediately taxable income under the cash equivalence doctrine unless it is a right that is unconditional, freely transferable, and readily saleable. The Acknowledgment specifically prohibits the transfer of the attorneys' rights to receive the periodic payments thereunder; as such, an Attorney should not recognize income under the Standard Fee Deferral under the cash equivalence doctrine.

4. Judicial Authority Addressing Attorney Fee Arrangements—Childs v. C.I.R.

In Childs v. C.I.R., 103 T.C. 634 (1994), aff'd, 89 F.3d 856 (11th Cir. 1996), the Tax Court rejected the Commissioner of Internal Revenue's argument that an attorney constructively receives or obtains the economic benefit of his or her full fee when an assignment company assumes the defendant insurer's obligation to make future fee payments and acquires an annuity as the funding asset to fund that portion of the plaintiff's periodic settlement payments related to the fee. (Although most of the discussion in Childs dealt with Section 83, the Court acknowledged that its reasoning applied to the other tax doctrines.) In Childs, a group of attorneys, all of whom were cash basis taxpayers, represented plaintiffs in two related personal injury lawsuits. The contingent fee agreements between the attorneys and the plaintiffs provided that the attorneys could not recover fees unless and until the plaintiffs recovered damages. During settlement negotiations and before any agreements were reached regarding the claims, the parties decided that the legal fees would be paid in a structured format whereby the assignment company would pay directly to the attorneys a portion of the corresponding periodic payments under the plaintiffs' structured settlements. Once finalized, the agreements, in pertinent part, prohibited the

attorneys from accelerating, deferring, increasing, or decreasing any of the periodic payments, conferred no ownership interests in the funding assets (annuities acquired by the assignment company) to the attorneys, and limited any rights of the attorneys with respect to the payments from the assignment company to those of a general creditor. Despite these restrictions, the IRS argued that the attorneys constructively received and obtained the economic benefit of a fee equal to the amount of the annuities "set aside" for them in the year the annuities were purchased.

Ruling against the IRS, the Tax Court held that the attorneys did not constructively receive their fees prior to actual payment: at no time did the attorneys have a right to demand or receive immediate payment of their fees, even after the funding annuities were purchased, and at no time were funds or other property set aside for them to draw upon at a time of their choosing. The court observed that under the settlement and contingent fee agreements, the attorneys were entitled to nothing until (i) the settlements became effective and (ii) the plaintiffs actually received each of their periodic settlement payments. Regarding when the parties' rights to the income materialized, the court held that the plaintiffs did not "recover" their damages until either the parties' negotiated settlement was approved by the court or when the settlement agreement became effective, and that the attorneys in turn had no right to receive any moneys prior to such time as their clients "recovered" amounts from their claims. See 103 T.C. at 654 ("'Recovered' implies amounts that petitioners' clients actually received, rather than amounts that petitioners' clients had a right to receive. Petitioners' clients recovered no money from the litigation until after April 25, 1986, the date of the judgment in the Garrett litigation approving the Garrett release agreement").[5] Because the settlement agreements (which established the structured fee arrangement) were entered into before the attorneys "acquired an absolute and unconditional right to receive payment," the attorneys, as cash basis taxpayers, were not required to report the periodic payments as income until each payment was received. See 103 T.C. at 655.[6]

In also rejecting the applicability of the economic benefit doctrine, the Court dismissed the notion that a guarantee (namely, the insurance company's guarantee of the assignment company's obligations) either secures or funds a promise to pay. By definition, a guarantee is just a promise to pay; in the Court's view, the mere promise of the related life insurance company's guarantee, without more, and regardless of the insurance company's solvency or rating, did nothing to actually secure the attorneys' claims to payment. See 103 T.C. at 652.[7] Similarly, because the assignment company owned the annuities funding the settlement

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[5] See also Priv. Ltr. Rul. 201232024 (May 15, 2012) (noting that prior to a judgment or settlement being final, a legal claim is still "contingent or doubtful in nature").

[6] Specifically, the Childs court stated: "The right of petitioners to receive payment of fees existed only after the Jones release agreement became effective, since any rights arising from the fee agreement were dependent on amounts recovered for petitioners' clients. Petitioners had no right to receive any moneys prior to such time as their clients 'recovered' amounts from their claims. Petitioners never had the right to receive immediate payment, and no fund or property was set aside for petitioners which they could draw from at a time of their choosing. Because each of the deferred payment agreements was binding between the parties and was made prior to the time when petitioners acquired an absolute and unconditional right to receive payment, petitioners, who were on a cash basis, were not required to report the proceeds as income until actually received." 103 T.C. at 655 (citing Oates v. C.I.R., 18 T.C. 570, 584-85, aff'd 207 F.2d 711 (7th Cir. 1953) (discussed in greater detail *infra*).

[7] If an obligor's payment to another party to assume the obligor's promise to make periodic payments were viewed as conferring an economic benefit on the claimant (*e.g.*, as if the original obligor set aside the amount paid from the reach of the original obligor's creditors), the economic benefit doctrine would apply any time a novation of

payments, and the annuities were subject to claims of the assignment company's general creditors, the promise to pay the attorneys' fees was not funded. Id. at 653. The court also held that an unsecured and unfunded right to future payments is not considered "property" for the purposes of Section 83 of the Code. Id. at 655. Thus, the attorneys were not assured the benefit of the future payments and did not obtain a nonforfeitable economic or financial benefit in the annuities.[8]

The U.S. Court of Appeals for the Eleventh Circuit affirmed the Tax Court's decision without issuing its own opinion. See 89 F.2d 856 (11th Cir. 1996).[9]

5. Conclusion

None of the income recognition doctrines or judicial authorities discussed above should render an Attorney taxable on its contingent fee in the year that the settlement agreement is executed. The Pacific Life Program is squarely within the parameters of the Tax Court's decision in Childs. The deferral arrangement is entered into prior to the time the client's right to recovery becomes final. Furthermore, as set forth in the Acknowledgment and Application, no amount is irrevocably set aside for any Attorney from which he or she has the right to draw upon at will and the Attorney has no rights with respect to receipt of the periodic payments beyond those of a general creditor of PLASI. Accordingly, an Attorney participating in the Pacific Life Program should be taxable on his or her Fee as each periodic payment is received.

B. Section 409A of the Code

1. General Rule and Independent Contractor Exception

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an obligor's promise to make periodic payments occurred pursuant to a structured settlement with a personal injury claimant under Section 130. Although such a result would not give rise to immediate taxable income to a claimant, due to the exclusion under Section 104(a)(2), such result would cause the claimant to recognize income on the deemed investment earnings as if he received a non-taxable lump sum payment and then purchased an annuity contract. This clearly is not the result under applicable law. See Rev. Rul. 2003-115 (no economic benefit is conferred on a claimant where assignment company assumes the obligation to make periodic payments pursuant to an assignment meeting the requirements of Section 130(c)).

[8] See also Shuster v. Helvering, 121 F.2d 643, 645 (2d Cir. 1941) (L. Hand, J.) (it is "absurd" to consider an obligor's unfunded, unsecured promise to make future payments as the receipt of property upon which the taxpayer is immediately taxable; under this view, "all future payments which should become due under a contract of employment must be charged at once at their discounted value; so too of a lease, or of any other contract providing for serial payments. To argue that all these are income as soon as the obligor becomes bound, especially when the taxpayer, as here, keeps his books on a cash basis, is so fantastic as to deserve no discussion").

[9] We note that prior to Childs, the IRS issued a Technical Advice Memorandum that reached a contrary conclusion on a similar attorney fee structure. Tech. Adv. Mem. 9134004 (May 7, 1991). Under the attorney fee structure at issue there, the defendant's liability insurer remained contingently liable for the attorney's fee payments; in Childs, however, the defendant's insurer was released from liability. It is not clear whether this distinction is material post-Childs. Regardless, Childs is the governing law in this area and effectively nullifies TAM 9134004 to the extent that the IRS's analysis therein adopted the positions rejected in Childs. The IRS has also cited Childs favorably in more recent guidance. See e.g. PLR 200836019 (employment discrimination plaintiff who received periodic payments under a structured settlement not eligible for Section 130 treatment is not in actual or constructive receipt and did not realize the economic benefit of the settlement amount until each periodic payment is received), referenced previously; Field Serv. Adv. Mem. 200151003 (Jul. 5, 2001). As far as the authors are aware, the IRS has not sought to relitigate the issues presented in Childs in the almost thirty years since it was handed down.

Section 409A(a)(1), added to the Code in 2004, provides certain requirements for the deferral of income recognition in nonqualified deferred compensation arrangements. In general, payments received under deferred compensation arrangements are currently includible in gross income unless such payments are either subject to a substantial risk of forfeiture or if the more stringent requirements of Section 409A(a)(2), (3) and (4), including requirements regarding the timing of the election to defer, are met. However, Treasury Regulations Section 1.409A-1(f)(2) provides the requirements of Section 409A do not apply if, during the year in which a service provider (such as an attorney) obtains a legally binding right to deferred payments, the service provider is actively engaged in the trade or business of providing substantial services, other than either as an employee or as a director of a corporation, and the service provider provides these services to two or more service recipients to which the service provider is not related and that are not related to one another. A "plan" under Section 409A includes any arrangement or agreement that provides for the deferral of compensation (to the extent not otherwise excluded by the Code provision).

2. Conclusion

Assuming an Attorney provides legal services to two or more unrelated service recipients in the year the claim is settled, Section 409A should not apply to any of the periodic payments received.

C. The 2022 GLAM

In the 2022 GLAM, the IRS posited that an attorney retained on a contingent fee basis cannot defer recognition of its fee where it assigns its right to receive the fee on the eve of settlement to a third party which in turn invests the funds and agrees to make a future lump-sum payment to the attorney. The IRS reasoned that such an arrangement: (i) is not covered by the Tax Court's decision in Childs; (ii) is invalid as an anticipatory assignment of income under the Supreme Court's decision in Lucas v. Earl, 281 U.S. 111 (1930) and its progeny; (iii) results in the attorney realizing the economic benefit of his fee at the time he assigns it to the third party, because the amount transferred to the third party is not subject to the claims of the client's creditors; and (iv) is subject to Section 409A, because the attorney is not eligible for the "independent contractor" since the deferred payment is made by the third party rather than the client (as the recipient of the attorney's services).

The hypothetical scenario presented in the 2022 GLAM is materially different from a traditional attorney fee structure. Consequently, none of the arguments the GLAM raises against its hypothetical scenario apply to the traditional arrangement. By contrast (and as previously stated), the Pacific Life Program provides for a deferral that is virtually identical to the arrangement the Tax Court (and, by its affirmance, the U.S. Court of Appeals for the Eleventh Circuit) approved in Childs as well as the long-established authorities governing the economic benefit doctrine.[10]

[10] In footnote 1 of the GLAM, the IRS states that "[b]ecause no written opinion is available for reference, it is not clear that the Eleventh Circuit affirmance of Childs would have much, if any, persuasive authority in the Eleventh Circuit or any of the other federal Circuit Courts of Appeals." However, there are many reasons why a court of appeals may not issue a precedential opinion, not the least of which is that it agrees with the lower court's reasoning and holding and sees no reason to supplement it. In footnote 11, the GLAM states that it "does not address" whether

1. Status of General Legal Advice Memorandums

According to section 33.1.2.2.3.5 (04-12-2013) of the Internal Revenue Manual, a general legal advice memorandum is a memorandum written by an Associate Chief Counsel for use by other IRS personnel. A general legal advice memorandum may be appropriate where a common set of facts applies to a significant number of taxpayers and advice with respect to facts representative of those common facts will assist IRS personnel (including field personnel) in resolving cases more efficiently. When legal advice is requested by a Division Counsel executive (as appears to be the case here), the Associate Chief Counsel must conduct a pre-submission conference with the Division Counsel executive and the program manager. The purpose of a pre-submission conference is to confirm that issuing a general legal advice memorandum is appropriate and to define the issues on which advice is needed.

Unlike a revenue ruling, a general legal advice memorandum does not set out an official ruling or position of the IRS and may not be referenced in other documents as precedent. As such, a subsequent decision to adopt a different position on the same or similar legal issue will not require a general legal advice memorandum to be withdrawn or revoked; rather, a new memorandum setting out current advice will be issued. In addition, and unlike a private letter ruling, a general legal advice memorandum does not bind any taxpayer. The 2022 GLAM likely was issued in response to a request received by the Division Counsel, Tax Exempt & Governmental Entities and a determination by an Associate Chief Counsel executive that issuing advice in the form of a general legal advice memorandum would promote efficiency, the consistent treatment of similarly situated taxpayers, and sound tax administration. However, the specific impetus for the 2022 GLAM is not generally known.

2. The 2022 GLAM's Deferral Arrangement vs. a Standard Fee Structure

The 2022 GLAM does not address a Standard Fee Structure. There are no references in the 2022 GLAM to an attorney fee structure, structured settlements or qualified assignments, and the GLAM does not cite Revenue Ruling 2003-115 or PLR 200836019, which directly address deferred payments in the litigation settlement context. In addition, because the scope of the matters raised in the 2022 GLAM was discussed between the Associate Chief Counsel and the Division Counsel in a pre-submission conference prior the 2022 GLAM's issuance, it is reasonable to conclude that the 2022 GLAM is not intended to reach topics that it does not specifically address.

Rather than a Standard Fee Structure, the 2022 GLAM addresses a situation (presumably based on actual facts) where a plaintiff opted to accept a single cash payment (of $1,500,000) in settlement of a personal injury lawsuit and the attorney entered into a proprietary deferred compensation arrangement for its fee (of $450,000) with a third party (the "**Deferral**

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the Tax Court's treating the insurance companies as the "obligors" in Childs is "now incorrect" in light of C.I.R. v. Banks, 543 U.S. 426 (2005), discussed *infra*. However, Banks did not involve an assignment company or the timing of income received by a plaintiff and/or its attorney; rather, it held only that the plaintiff *is taxable* on all amounts received from the defendant (whether retained or paid by the attorney) in the first instance. In other words, Banks addresses "who" income is taxable to, not "when" it is taxable.

Arrangement") at the same time the settlement was negotiated. Regarding the timing of these various events, the GLAM states that the attorney negotiated the settlement on behalf of the client "[d]uring pendency of the of the case but before trial", the attorney entered into the Deferral Agreement with the third party on June 30, 2021, the settlement agreement was executed on July 1, 2021, the attorney delivered wire instructions for its fee on July 15, and the fee was paid by the defendant to the third party on August 1. Upon receipt of the $450,000 fee, the third party placed the funds in a rabbi trust, invested them in an investment vehicle of the attorney's choosing, and agreed to make a future lump-sum payment to the attorney on August 1, 2031 of $450,000 plus accumulated investment income. Under the terms of the Deferral Arrangement, the attorney is an unsecured creditor of the third party and has no right to assign, accelerate, defer, change the terms or time of, or transfer or sell the future payment, and third party is the sole owner of the funds held in the trust. The attorney also was permitted to take a loan from the third party, which it did on August 1 in the amount of $200,000; in the event the attorney defaulted on the loan, the third party could reduce the future lump-sum payment by the unpaid principal and interest.

The Standard Fee Structure differs from the Deferral Arrangement in several significant respects, two of which are especially crucial. First, in a Standard Fee Structure where both the plaintiff and the attorney agree to structure, the attorney does not assign any rights to a third party; rather, the defendant assigns its obligations to the assignment company and the attorney merely consents to receiving its fee in installments, as the plaintiff receives each of its periodic payments pursuant to the qualified assignment. Second, a Standard Fee Structure does not involve the placement of the fee amount in a rabbi trust,[11] as is the case in the Deferral Arrangement. This difference is significant because a rabbi trust, unlike a typical assignment company, does not assume a payment obligation of the defendant; rather, it merely agrees to be the vehicle for making future payments to the attorney.

The 2022 GLAM takes the position that the Deferral Arrangement was an improper attempt by a taxpayer to divert income to a third party. At the outset, the GLAM (i) states that Deferral Arrangement is not covered by Childs and (ii) concludes that the full $450,000 is taxable to the attorney in the year the full cash settlement became payable to the plaintiff because that is when the attorney's right to receive its fully "funded" payment became absolute. This conclusion appears to be based on the IRS's belief that compensation income is never assignable to a third party; in other words, a taxpayer cannot *permanently shift* to another taxpayer any amount of compensation it has an absolute right to receive for services it has already performed by directing the compensation to someone (or something) else. The GLAM primarily relies on Lucas v. Earl, 281 U.S. 111 (1930), which holds that a husband is taxable on compensation for services he performed, even though he had previously entered into a contract with his wife stating that she was entitled to half of it;[12] U.S. v. Basye, 410 U.S. 441 (1973), which holds that physicians were taxable on fee income earned by their partnership but placed in a retirement plan, the terms of which could result in amounts earned by some physicians being forfeited and subsequently paid to other

[11] As discussed previously, a rabbi trust, which is authorized by Revenue Procedure 92-64, is a grantor trust established to support the non-qualified deferred compensation benefits of an employer to its employees.

[12] For the tax years at issue in Earl (1920 and 1921), married couples could not file joint income tax returns as a single economic unit; hence, the outcome of Mr. Earl's assigning half of his compensation income to his wife is that, as a result of the graduated marginal tax rates, he would have paid less income tax. See Raymond v. U.S., 355 F3d 107, 111 n.7 (2d Cir. 2004).

physicians; and Kochansky v. C.I.R., 92 F3d 957 (9th Cir. 1996), which holds that a contingent fee earned by an attorney was taxable to him, even though when the fee materialized, half of it was paid to his ex-wife pursuant to a divorce settlement. For essentially the same reasons, the GLAM posits that the attorney received the economic benefit of the fee (under both the traditional economic benefit doctrine and Section 83 of the Code) in 2021—when the right to receive a sum certain of $450,000, in cash, from the insurer became absolute and unalterable (or, in technical terms, funded and nonforfeitable, and beyond the reach of creditors)—thus rendering the attorney immediately taxable on the amount.

In addition, the 2022 GLAM posits that the Deferral Arrangement failed the requirements of Section 409A of the Code (which establishes requirements for deferred compensation plans to be respected) and that the attorney was not eligible for the "independent contractor" exception under the Section 409A regulations. The GLAM concludes that this failure is yet another basis for denying deferral treatment.

3. Viability of the 2022 GLAM's Arguments

Several aspects of the GLAM's analysis appear to extend the scope of the authorities it discusses. Perhaps most importantly, the GLAM glosses over the distinction between a *deferral* of income and the *permanent shifting* of income to another taxpayer. This distinction is critical under existing law. In addition, the GLAM's discussion of the independent contractor exception to Section 409A does not apply to a Standard Fee Structure.

a) Anticipatory Assignment of Income Doctrine

(i) Permanent Shift of Income

The anticipatory assignment of income doctrine does not apply where the same taxpayer—here, the Attorney—is the only taxpayer who will receive the amount that was directed to the third party. In this sense, the GLAM effectively treats a taxpayer's *deferral* of its own income as if it were *permanently shifting* that income to a different taxpayer, the effect of which is to eliminate the taxpayer's tax liability on that income.[13] As a technical point, the two are fundamentally different. The Lucas, Basye, and Kochansky decisions involved either an outright exclusion of income (in Lucas, via the taxpayer's overt attempt to divert half his income for services to his wife, and in Kochansky, via the payment of half of the taxpayer's fee income to his ex-wife pursuant to a divorce settlement) or high likelihood that income would be shifted (in Basye, via the possibility that a physician would separate employment prior to the vesting of his or her retirement benefits, which benefits would in turn be received by other physicians). The court

[13] In C.I.R. v. Banks, *supra*, the Supreme Court applied the assignment of income doctrine to hold that a plaintiff (as the "owner" of the legal claim) in an employment discrimination lawsuit must include in income the amount of the contingent fee received by his lawyer. However, the court specifically described the anticipatory assignment of income doctrine as preventing the ***exclusion*** of income from taxation: "A taxpayer cannot ***exclude*** an economic gain from gross income by assigning the gain in advance to another party. The rationale for the so-called anticipatory assignment of income doctrine is the principle that gains should be taxed to those who earned them." 543 U.S. at 433 (emphasis added; internal citations and quotation marks omitted). Thus, anticipatory assignment of income doctrine is used to determine which of two taxpayers is taxable on a particular item of income.

in Basye stated the principle this way: "The entity earning the income – whether a partnership or an individual taxpayer – cannot ***avoid*** taxation by entering into a contractual arrangement whereby that income is ***diverted*** to some other person or entity. Such arrangements…have frequently been held ineffective as a means of ***avoiding*** tax liability." 410 U.S. at 449-50 (emphasis added). Although the GLAM correctly notes that the court said in passing "the tax laws permit no such easy road to tax avoidance or deferment," the emphasized language makes clear that the court was concerned only about the exclusion of income from taxation through the permanent diversion of that income to another taxpayer.

However, in an arrangement where the taxpayer is certain to be taxed on the income—such as in a Standard Fee Structure—the risk of income shifting (and thus avoidance of taxation) does not exist. The fact that a third party which assumes an obligation may be interjected into the arrangement does not change this.[14]

(ii) Distinguishing the Permanent Shift of Income From the Deferral of Income—Oates v. C.I.R.

The Tax Court and the U.S. Court of Appeals for the Seventh Circuit recognized the distinction between a deferral of income and the permanent shifting of income to another party in Oates v. C.I.R., 18 T.C. 570 (1952), aff'd 207 F.2d 711, 714 (7th Cir. 1953). In Oates, the taxpayers were retired insurance salesmen who were eligible to receive to receive certain commissions in retirement from the insurance carrier whose policies they sold. The contract between the salesmen's agency and the carrier provided that upon retirement, the agents were to receive commissions on renewal premiums "as they were earned" during the nine-year period following the date of retirement; however, the stream of payments tended to decline sharply due to fewer and fewer insurance policies being renewed each year. 18 T.C. at 573. To rectify this harsh consequence, the carriers and the agents amended their agreement to level the potential payments of terminal commissions over a period more nearly in accord with the life expectancy of the retired salesmen. See id. at 575. The IRS asserted that the retired salesmen were taxable on the entire amount of commissions that would have been due and payable under the prior arrangement.

The Tax Court rejected this assertion, and instead held that because the arrangement between the carrier and the salesmen was amended "prior to the time when such amounts were determined and prior to the time the taxpayer had acquired any right to receive [the amounts]," the taxpayers were permitted to recognize the commissions under their revised deferral arrangement. The Tax Court rejected the IRS's argument that the assignment of income line of cases (specifically Lucas v. Earl, and others) were relevant, because the salesmen were not trying to shift the income to another party: "We fail to see where those cases have any application here. Those are cases where the income had been assigned to another and the taxpayer was contending that the assignment relieved him of taxation on the income and that the income was taxable to the one to whom it had been assigned. We have no such question here." 18 T.C. at 585. The Seventh Circuit affirmed the Tax Court's decision; regarding the applicability of the assignment of income

[14] See, e.g., Rev. Rul. 75-457, 1975-2 C.B. 196 (permitting the substitution of an obligor under an installment note without causing the acceleration of gain to the holder of the note).

doctrine, the court echoed the Tax Court's conclusion: "[The taxpayer] made no assignment; he took no dominion over the accrued commissions other than to agree to receive them in case installments as they matured under the contract." 207 F.2d at 714. Although the GLAM cites Oates, its analysis does not fully develop the decision's significance.

b) Economic Benefit/Section 83

Once the scope of the assignment of income doctrine is clarified, the 2022 GLAM's conclusions regarding the traditional economic benefit doctrine and Section 83 with respect to Standard Fee Structures necessarily fall away: if there is no anticipatory assignment and a valid deferral arrangement (be it a Standard Fee Structure or otherwise) is entered into prior to the time the plaintiff's recovery has materialized and before any payments by the defendant under the settlement agreement are due and payable, the Attorney cannot have realized the economic benefit of the fee unless the assignment company sets aside funds for the payments which are not subject to the claims of its general creditors.

The GLAM also misconstrues the law in stating that the deferred amount paid to the attorney must be subject to the claims of the ***client's*** creditors in order to avoid the economic benefit doctrine or Section 83.[15] First, none of the cases the GLAM relies on establish such a strict rule; to the contrary, they leave the point open—in Sproull, *supra*, the court held that the taxpayer was taxable on the funds set aside for him in part because "No one else had an interest in or control over the moneys" (see 16 T.C. at 248); in Drescher, *supra*, the court noted that the contract at issue stated that "Neither this contract nor any payment hereunder may be assigned, and the contract and all payments shall be free from the claims of all creditors to the fullest extent permitted by law" (see 179 F.2d at 864); and Our Country Home Enters. v. C.I.R., 145 T.C. 1 (2015) involved a split-dollar life insurance policy such that there were only two parties to the arrangement, an employer and an employee (and in any event such arrangements are specifically governed under the detailed rules in Treasury Regulations Section 1.61-22 rather than Section 83 or the regulations thereunder). Consistent with Sproull and Drescher, the Tax Court in Pulsifer v. C.I.R., 64 T.C. 245, 246 (1975), stated that the amount must be "beyond the reach of the payor's [creditors]."[16] Essentially, the GLAM confuses a sufficient condition for a necessary one—while an amount still subject to the service recipient's creditors is *sufficient* to avoid the economic benefit doctrine (or Section 83), it is not *necessary*. Therefore, in a Standard Fee Structure where there is no anticipatory assignment of income and the periodic payments are subject to the general creditors of the assignment company, existing law is clear that the economic benefit doctrine does not apply.

Revenue Ruling 2003-115 (which the GLAM does not cite) also supports the conclusion that the claims of creditors of an assignee of the original obligor must be taken into account in applying the economic benefit doctrine. As explained previously, the ruling holds that the economic benefit doctrine does not apply where the United States (the original obligor that

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[15] The 2022 GLAM suggests that Banks (which was decided after Childs) somehow changes the result in Childs by establishing that the client retains all rights with respect the claim. For the reasons discussed herein, however, this characterization is irrelevant for purposes of the economic benefit doctrine and Section 83.

[16] In place of the word "creditors," the Pulsifer opinion uses the word "debtors." This almost certainly is a scrivener's error, as the payor's "debtors" would be parties that are indebted to the payor, not the other way around.

established the September 11th Victim Compensation Fund) assigned to an assignment company its obligation to make periodic payments to victims. As in a Standard Fee Structure, (i) the assignment company assumed the original obligor's payment obligation, (ii) the assignment company acquired an annuity contract to fund its payment obligation, and (iii) the annuity contract was "subject to claims of the ***general creditors of the assignment company***." (Emphasis added.) The ruling notes that if a victim had realized the economic benefit of the lump sum paid to the assignment company, only the lump sum, and not the subsequently earned investment income, would be excluded from the victim's income under Section 104(a)(2) or Section 139F of the Code. This clearly is not the result under applicable law.

c) Section 409A

The 2022 GLAM's discussion of the independent contractor exception of Section 409A does not apply to Standard Fee Structures. Section 409A(a)(1), added to the Code in 2004, provides certain additional requirements for the deferral of income recognition in nonqualified deferred compensation arrangements. Under the provision, payments received under deferred compensation arrangements are currently includible in gross income unless such payments are either subject to a substantial risk of forfeiture or if the more stringent requirements of Section 409A(a)(2), (3) and (4), including requirements regarding the timing of the election to defer, are met. However, Treasury Regulations Section 1.409A-1(f)(2) generally provides that the regime of Section 409A does not apply under a plan between a service provider and a service recipient if the service provider is actively engaged in providing services other than as an employee and also provides significant services to two or more unrelated service recipients. A "plan" under Section 409A includes any arrangement or agreement that provides for the deferral of compensation (to the extent not otherwise excluded by the Code provision).

In both a Standard Fee Structure and the GLAM's Deferral Arrangement, the service recipient is the client and the service provider is the attorney. The Supreme Court in C.I.R. v. Banks, 543 U.S. 426, 436 (2005) stated this outright. However, in a Standard Fee Structure, both the plaintiff and the attorney are parties to any "plan," "agreement," or "arrangement" involving the deferral of the attorney's fee, and it can be presumed that the attorney provides services to more than one client. Consequently, Standard Fee Structures qualify for the independent contractor exception and are not governed by Section 409A.

4. Conclusion

The 2022 GLAM has not changed the validity of Standard Fee Structures under existing law. As explained previously, the GLAM does not have precedential effect: it is not binding on the IRS or on any particular taxpayer, the IRS is free to disregard it (and may do so without issuing a formal retraction) if its thinking on the issue changes, and it is not binding on any court. While the GLAM appears to question the validity of the Childs decision in at least two places (namely, by noting in footnotes that the Eleventh Circuit affirmed Childs without issuing a precedential opinion and that Banks may call part of Childs into question; both points are addressed in footnote 10 herein), the GLAM explicitly states that Childs "does not apply" to the Deferral Arrangement—in other words, despite briefly buzzing around it, the GLAM ultimately leaves Childs alone. That said, while the GLAM may have implications for situations where an attorney

seeks to defer its fee through an arrangement with a third party and a rabbi trust, it does not call into question to the long-settled income tax treatment of a Standard Fee Structure.

III. OPINION

Given the facts that have been represented to us, and in light of the foregoing authorities, we are of the opinion that an Attorney who participates in a Standard Fee Structure through the Pacific Life Program should be taxable on his or her Fee only in the year in which each periodic payment is received.

IV. OTHER MATTERS

This opinion letter reflects our best legal judgment with respect to the federal income tax matters described in Section III hereof, but it has no binding effect or official status of any kind. As such, it is possible that the IRS or a court considering the same issues may take a contrary position. We express no views relating to any federal income tax matter except on the basis of the facts which have been represented to us as set forth above. Any changes in such facts could require a reconsideration and modification of our views.

In preparing this opinion, we have relied solely upon existing provisions of the Code, existing and proposed regulations under it, and current administrative positions and judicial decisions. Those laws, regulations, administrative authorities and judicial decisions are subject to change at any time. Any such changes could affect the validity of the opinion set forth above. Also, future changes in federal income tax laws and the interpretation thereof can have retroactive effect. For the avoidance of doubt, this opinion does not address any tax consequences arising under foreign, state or local laws.

The discussion of tax matters contained in this opinion is limited in scope, and addresses only those specific issues topics raised herein. Additional issues may exist which affect the tax treatment of the matters described herein or the parties thereto. This opinion does not consider or provide any conclusions with respect to such additional topics or issues.

This opinion is solely for the benefit of the recipient hereof and may not be relied upon by any other person without our written consent.

Respectfully,

FLASTER GREENBERG P.C.

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