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Income Taxes And The Computation Of Lost Future Earnings In Wrongful Death And Personal Injury Cases - Neff v. United States' Platisv. United States

Income Taxes And The Computation Of Lost Future Earnings In Wrongful Death And Personal Injury Cases

Neff v. United States[1]

Platis v. United States[2]

Historically, damages recovered in personal injury and wrongful death actions have been highly variable, even in cases with strikingly similar facts. Variance which is the product of a jury's discretionary power is a tolerable component of our judicial system, but variance which is the product of divergent judicial reasoning must be critically examined. Two recent federal district court cases illustrate such an inconsistent judicial approach in the computation of lost future earnings in wrongful death and personal injury cases. *Platis v. United States*[3] involved a suit under the Federal Tort Claims Act, requiring the application of the Utah wrongful death statute[4] in the computation of compensatory damages. The decedent had a life expectancy of 31.6 years at the time of his death. He had earned $7,614 as a cost accountant in the year before his death; he was survived by a wife and ten year old child. The court's final decree awarded $295,000 to the plaintiffs: $220,000 to the widow and $75,000 to the child. In *Neff v. United States,*[5] also brought under the Federal Tort Claims Act, damages were based on the New York wrongful death statute,[6] which is similar to that of Utah, and the facts seemed to auger well for a larger recovery than in *Platis.* The decedent had a life expectancy of forty years at the time of his death. Furthermore, his gross earnings the year before his death amounted to $10,000, and, as an airline pilot, he had the probability of a much higher income in the future. He was

1. 282 F. Supp. 910 (D.D.C. 1968).
2. 288 F. Supp. 254 (D. Utah 1968).
3. *Id.*
4. UTAH CODE ANN. § 78-11-7 (1953).
5. 282 F. Supp. 910 (D.D.C. 1968).
6. N.Y. DECED. EST. LAW §§ 130, 132 (McKinney 1949).

survived by a wife and five children, ages four to ten. The final award was $334,149.21: $94,339.21 for the widow and $239,750 to be divided among the five children.

The disparity in the sums awarded in these two cases is apparent: the individual beneficiaries of the decedent with the longer life expectancy and the brighter financial future recovered substantially smaller amounts. The principal reason for this result is found in the different methods used by the two courts to compute damages based on lost future earnings. *Platis* based its calculation of this element of damages on the decedent's *gross* earnings. In contrast, *Neff* used the decedent's *net* earnings, arrived at by deducting an amount representing the decedent's prospective federal income tax liability.

THE ROOT OF THE PROBLEM: SECTION 104(a)(2) OF THE INTERNAL REVENUE CODE

Over the years there has been considerable controversy over the question of whether damages recovered in various legal actions are taxable as income to the recipient.[7] Although "damages received . . . on account of personal injuries or sickness" are excluded from federal gross income by Section 104(a)(2) of the Internal Revenue Code,[8] judicial decisions on damages in other related actions have depended on an interpretation of the basic concept of income.[9] The distinction generally followed is that damages which merely compensate for what can be termed a loss of capital are not taxable, whereas all other types of damages fall within the plaintiff's taxable income.[10] This was the rationale used to justify the statutory exclusion afforded personal injury damages in Section 104(a)(2): "Damages paid for personal injuries are excluded from gross income because they make the taxpayer whole from a previous loss of personal rights — because, in effect, they restore a loss to capital."[11]

Damages recovered under state wrongful death statutes have always been excluded from federal income taxation.[12] Early decisions were based on the general concept of income rather than on any specific

7. *See* Rev. Rul. 19, 1954-1 CUM. BULL. 179; McWeeney v. New York, N.H., & Hart. R.R., 282 F.2d 34, 39 (2d Cir.), *cert. denied,* 364 U.S. 870 (1960); Comment, *The Taxability of Recoveries in Personal Injury Cases,* 39 MARQ. L. REV. 56 (1955). *See generally* Knickerbocker, *The Income Tax Treatment of Damages: A Study in the Difficulties of the Income Concept,* 47 CORN. L.Q. 429 (1962).

8. INT. REV. CODE of 1954, § 104(a)(2). This section was originally enacted in 1918.

9. *See* Knickerbocker, *The Income Tax Treatment of Damages: A Study in the Difficulties of the Income Concept,* 47 CORN. L.Q. 429 (1962).

10. In Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955), the Supreme Court held that punitive damages in anti-trust and fraud actions were income because, unlike damages for personal injuries, they could not be viewed as a restoration of lost capital.

11. Starrels v. Commissioner, 304 F.2d 574, 576 (9th Cir. 1962). But damages for wrongful death and personal injury seem to go beyond a strict "loss to capital" concept when they begin to compensate for loss of future earnings, which could be viewed as future profits as well as capital.

12. Rev. Rul. 19, 1954-1 CUM. BULL. 179.

statutory exclusion.[13] However, recent cases have based the exemption on Section 104(a)(2).[14] This development finds support in the expansion which the federal income tax Regulations have given to Section 104(a)(2): "The term 'damages . . .' means an amount received . . . through prosecution of a legal suit or action based upon tort or tort type rights. . . ."[15] In addition, many states by statute exclude "tort-type" damage recoveries from state income taxation.[16]

Defense attorneys, in an attempt to utilize the exclusion of wrongful death and personal injury damages from "income" as a means of reducing their clients' liability, have advanced a persuasive argument. Since the recipient of "tort-type" damages will not have to pay federal income taxes on the award, in order to avoid over-compensation of the plaintiff, the loss of future earnings element of the award should be based on the plaintiff's or decedent's future *net* earnings after taxes, not on his potential gross earnings.[17] *Neff* accepts this argument,[18] while *Platis* and the majority of American courts reject it.[19]

THE BARRIER OF "SPECULATIVENESS": THE LEGACY OF *Stokes v. United States*

Compensation for loss of future earnings is a recognized element of damages in both personal injury and wrongful death actions. In a personal injury action, the plaintiff is allowed to recover, *inter alia,* the wages he would have earned but for the injury.[20] Death actions provide similar compensation, although the details vary from state to

13. I.T. 2420, VII-2 CUM. BULL. 123 (1928). *See generally* Knickerbocker, *The Income Tax Treatment of Damages: A Study in the Difficulties of the Income Concept,* 47 CORN. L.Q. 429 (1962).

14. *E.g.,* Brooks v. United States, 273 F. Supp. 619 (D.S.C. 1967); Anderson v. United Airlines, Inc., 183 F. Supp. 97 (S.D. Cal. 1960).

15. Treas. Reg. § 1.104-1(c) (1956).

16. *E.g.,* CAL. REV. & TAX. CODE § 17138(a)(2) (West Supp. 1969); MD. ANN. CODE art. 81, § 280(a) (Supp. 1968) (net taxable income is adjusted gross income of individual under federal law); N.Y. TAX LAW § 359(2)(e) (McKinney 1966); PA. STAT. ANN. tit. 72, § 3402-303(B)(5) (Purdon 1964).

17. A collateral, yet distinct argument is often made in these cases. The defense will often request that a general instruction be made to the jury informing them that the award they will reach is not taxable. *E.g.,* Dempsey v. Thompson, 363 Mo. 339, 251 S.W.2d 42 (1952). Some cases merely involve a comment of defense counsel to that effect made before the jury. *E.g.,* Hall v. Chicago & N.W. Ry., 5 Ill. 2d 135, 125 N.E.2d 77 (1955). In either situation the purpose is to prevent the jury from arbitrarily increasing the award in the mistaken belief that the plaintiff will have to pay taxes on it. Most cases have held that neither the instruction nor the comment is proper. *See, e.g.,* Prudential Ins. Co. of America v. Wilkerson, 327 F.2d 997 (5th Cir. 1964) (personal injury); New York Cent. R.R. v. Delich, 252 F.2d 522 (6th Cir. 1958) (wrongful death); Hall v. Chicago & N.W. Ry., 5 Ill. 2d 135, 125 N.E.2d 77 (1955) (personal injury); Bergfeld v. New York, Chicago, & St. Louis R.R., 103 Ohio App. 87, 144 N.E.2d 483 (1956) (wrongful death). *Contra,* Dempsey v. Thompson, 363 Mo. 339, 251 S.W.2d 42 (1952) (personal injury). *See generally* Annot., 63 A.L.R.2d 1393 (1959); Nordstrom, *Income Taxes and Personal Injury Awards,* 19 OHIO ST. L.J. 212 (1958); Note, *Income Taxation and Damages for Personal Injuries,* 50 KY. L.J. 601 (1962).

18. 282 F. Supp. at 924.

19. 288 F. Supp. at 278. *See* Annot., 63 A.L.R.2d 1393 (1959).

20. *See* Rhone v. Fisher, 224 Md. 223, 167 A.2d 773 (1961); Dempsey v. Thompson, 363 Mo. 339, 251 S.W.2d 42 (1952); RESTATEMENT OF TORTS §§ 906, 910, 924 (1939); Nordstrom, *Income Taxes and Personal Injury Awards,* 19 OHIO ST. L.J. 212, 216 (1958).

state depending upon the particular type of death statute in force.[21] The general rule, however, is that the plaintiff may recover the pecuniary losses suffered because of the death and that the damages recovered are based upon the decedent's future earnings.[22] It is in determining just what these future earnings would have been in both types of cases that the income tax problem arises.

Given that the basic theory of tort damages is compensation — the return to the plaintiff of what has been taken away by the tortfeasor — it is difficult to understand how a plaintiff in a personal injury action can be allowed to recover a tax-free award amounting to his full wages when, had he not been injured, he would have had to pay taxes on those wages. Similarly, it is difficult to understand how a plaintiff in a wrongful death action can be entitled to receive a tax-free award based on the decedent's prospective earnings before taxes when the plaintiff's recovery is defined in most jurisdictions as being limited to the actual pecuniary loss suffered as a result of the death.[23] In both instances, it seems clear that the plaintiff is recovering more than he is entitled to recover; he receives a tax-free award based on taxable income from which taxes are not subtracted. Nonetheless, until relatively recently, courts had uniformly held that estimating future income taxes was "too conjectural" an issue from which to determine damages.[24] This position was first enunciated in 1944 in *Stokes v. United States*,[25] and has been frequently relied on in denying consideration of income taxes when computing loss of future earnings in both personal injury and wrongful death actions.[26] The "too conjectural" rationale seems to be supported by two separate lines

21. There appear to be three basic situations. (1) Under the so-called survival statute, the decedent's cause of action inures to his estate. Thus the decedent's estate recovers for medical expenses and pain and suffering to the date of death, plus the additional element of loss of future earnings. *See* Chase v. Fitzgerald, 132 Conn. 461, 45 A.2d 789 (1946). (2) Under the so-called wrongful death statute, or Lord Campbell's Act, a new cause of action for the death arises in the decedent's family or heirs. The recovery is usually the pecuniary loss to the heirs caused by the death, which losses include the decedent's future earnings. *See* United States v. Guyer, 218 F.2d 266 (4th Cir. 1954); Brooks v. United States, 273 F. Supp. 619 (D.S.C. 1967); Jennings v. United States, 178 F. Supp. 516 (D. Md. 1959). (3) Many states have both types of statutes. *E.g.*, MD. ANN. CODE art. 67, §§ 1-6 (1967) (wrongful death); MD. ANN. CODE art. 93, § 112 (Supp. 1968) (survival). To prevent duplication of recovery, recovery under the survival statute is limited to what the deceased would have recovered had he lived, while the loss of future earnings element is recoverable only under the wrongful death statute in a separate action. *See* Rhone v. Fisher, 224 Md. 223, 230, 167 A.2d 773, 777 (1961) (dicta). *See generally* W. PROSSER, TORTS § 121, at 924 (3d ed. 1964); Duffy, *The Maldistribution of Damages in Wrongful Death*, 19 OHIO ST. L.J. 264, 266, 268, 269 (1958).

22. *E.g.*, Metzger v. S.S. Kirsten Torm, 245 F. Supp. 227 (D. Md. 1965). *See* W. PROSSER, TORTS § 121 (3d ed. 1964).

23. *See* note 22 *supra* and accompanying text.

24. Phoenix Indemnity Co. v. Givens, 263 F.2d 858, 863 n.4 (5th Cir. 1959) (personal injury); Chicago & N.W. Ry. v. Curl, 178 F.2d 497 (8th Cir. 1949) (personal injury); Stokes v. United States, 144 F.2d 82 (2d Cir. 1944) (personal injury); Culley v. Pennsylvania R.R., 244 F. Supp. 710 (D. Del. 1965) (wrongful death); Christopher v. United States, 237 F. Supp. 787 (E.D. Pa. 1965) (personal injury); Jennings v. United States, 178 F. Supp. 516 (D. Md. 1959) (wrongful death); Dempsey v. Thompson, 363 Mo. 339, 251 S.W.2d 42 (1952) (personal injury); Bergfeld v. New York, Chicago, & St. Louis R.R., 103 Ohio App. 87, 144 N.E.2d 483 (1956) (wrongful death). *See* Annot., 63 A.L.R.2d 1393 (1959).

25. 144 F.2d 82 (2d Cir. 1944).

26. *See* authorities cited note 24 *supra*.

of argument: first, it is bad policy to let a jury decide on an element of damages without sufficient guidelines to insure the reasonableness of its decision;[27] and second, if the jury were allowed to subtract prospective taxes from prospective earnings, the practical difficulties involved, such as the consideration by the jury of conflicting testimony of economic experts, would be more than the court could practicably undertake.[28]

However, the strength of the "too conjectural" argument can be seriously questioned. At the time *Stokes* was decided, tax rates were extremely high. By early 1944, the maximum personal income tax rate had been increased to ninety-four per cent.[29] However, taxes had been at a high level for only a short time, and it seemed likely that at the end of the war they would be immediately reduced to their low pre-war level. This expectation did not materialize. Income tax rates have remained high, and today, twenty-five years after *Stokes,* few dispute that federal income taxes at substantial rates are a permanent fixture.

Faced with a similar economic situation in the commonwealth countries, the House of Lords, overturning years of decisions declaring that subtraction of income taxes when computing damages for loss of future earnings was too speculative,[30] held that lost future earnings would be computed on the basis of net earnings after taxes.[31]

POLAR VIEWS: *Jennings* AND *Floyd*

The courts are well aware of the growing forcefulness of the arguments favoring the deduction of prospective income taxes. This awareness is evidenced in part by the proliferation of less than cogent arguments to rationalize adherence to the majority rule. *Jennings v. United States*[32] is a case in point. Uneasy about relying entirely on the "too conjectural" argument, but not wishing to depart from the weight of authority, the *Jennings* court pointed to other factors to justify not making the deduction. Events of the decedent's future life which could have affected his tax liability, such as the birth of other children, made the applicable tax rate unpredictable. Furthermore, the court pointed out that the plaintiffs were not really being overcompensated by the failure to deduct income taxes because they would be taxed on any income which the award would earn and would be liable for a large legal fee.

27. *See* Dempsey v. Thompson, 363 Mo. 339, 251 S.W.2d 42 (1952).

28. *See* McWeeney v. New York, N.H., & Hart. R.R., 282 F.2d 34 (2d Cir.), *cert. denied,* 364 U.S. 870 (1960).

29. *See* G. FITE & J. REESE, AN ECONOMIC HISTORY OF THE UNITED STATES (2d ed. 1965).

30. *E.g.,* Billingham v. Hughes, [1949] 1 K.B. 643.

31. British Transport v. Gourley, [1956] A.C. 185, 203:

> The obligation to pay tax . . . is almost universal in its application. That obligation is ever present in the minds of those who are called upon to pay taxes, and no sensible person any longer regards the net earnings from his trade or profession as the equivalent of his available income. . . . [T]here is, I think, no element of remoteness or uncertainty about its incidence.

32. 178 F. Supp. 516 (D. Md. 1959). The case involved the Maryland wrongful death statute, MD. ANN. CODE art. 67, §§ 1–6 (1967).

Other courts have responded to the challenge by adopting what might be denominated the "ostrich" theory of judicial responsibility.[33] *Christopher v. United States*[34] is a classic example. Without even an attempt to formulate a reasoned decision, the *Christopher* court peremptorily dismissed the government's contention that damages recoverable by the plaintiff should be reduced by projected income taxes supporting its ruling only with a brief footnote citation to an out of date annotation.[35]

In contrast to *Jennings,* a number of courts have, in recent years, decided that income tax liability should be a factor in determining loss of future earnings in death actions.[36] The leading case is *Floyd v. Fruit Industries.*[37] In addition to pointing out that a failure to make the deduction would result in over-compensation of the plaintiff, *Floyd* stressed the point that predicting the prospective taxes of the deceased was no more speculative than predicting his earning capacity and personal expenditures, predictions that have traditionally been made in wrongful death cases. The essence of the decision was the adoption of a policy directly contrary to the *Stokes* rationale; the court took the position that the practical problems involved did not override the essential justice of making the deduction.

Despite the limited success of the *Floyd* approach in wrongful death actions,[38] there is no substantial American authority to the effect that income taxes should be considered in computing loss of future earnings in a personal injury action.[39] However, there is no logical reason for not extending the *Floyd* rule to personal injury actions, since the rationale of compensation in both wrongful death and personal injury actions is the same. Regardless of which type of action is involved, the compensation awarded is, at least theoretically, the plaintiff's actual loss.

There does, however, seem to be an important drawback to the *Floyd* approach. A plaintiff in a wrongful death or personal injury action receives his losses computed to present value; that is, he receives

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33. *See, e.g.,* McWeeney v. New York, N.H. & Hart. R.R., 282 F.2d 34 (2d Cir.), *cert. denied,* 364 U.S. 870 (1960), where the court used an inflation argument to justify not making the deduction.

34. 237 F. Supp. 787 (E.D. Pa. 1965) (purporting to apply Maryland law).

35. *Id.* at 797 n.3.

36. Cox v. Northwest Airlines, Inc., 379 F.2d 893 (7th Cir. 1967); United States v. Sommers, 351 F.2d 354 (10th Cir. 1965); O'Connor v. United States, 269 F.2d 579 (2d Cir. 1959); Gill v. United States, 285 F. Supp. 253 (E.D. Tex. 1968); Brooks v. United States, 273 F. Supp. 619 (D.S.C. 1967); Moffa v. Perkins Trucking Co., 200 F. Supp. 183 (D. Conn. 1961); Meehan v. Central R.R., 181 F. Supp. 594 (S.D.N.Y. 1960); Floyd v. Fruit Industries, 144 Conn. 659, 136 A.2d 918 (1957).

37. 144 Conn. 659, 136 A.2d 918 (1957). The case involved the Connecticut survival statute, under which the measure of damages is the loss to the decedent had he lived. CONN. GEN. STAT. ANN. §§ 45-280, 52-599 (1960).

38. *E.g.,* Neff v. United States, 282 F. Supp. 910 (D.D.C. 1968). Some of the later decisions do not seem to be as well reasoned as the *Floyd* case. For example, in Brooks v. United States, 273 F. Supp. 619, 630 (D.S.C. 1967), the court supported its decision to deduct taxes in part by observing that the case was a wrongful death action and involved a non-jury trial. Neither of these factors seem particularly germane. *But see* Wright, *Foreword* to *Symposium — Damages for Personal Injuries,* 19 OHIO ST. L.J. 155, 157 (1958).

39. *But cf.* McWeeney v. New York, N.H., & Hart. R.R., 282 F.2d 34 (2d Cir.), *cert. denied,* 364 U.S. 870 (1960). As noted, the English rule now requires the deduction. *See* note 31 *supra* and accompanying text.

that sum which, if invested at a reasonable rate of interest, will produce interest income which, together with the sum originally awarded, will adequately compensate plaintiff for the losses resulting from the death or injury.[40] In effect, then, part of the plaintiff's compensation is the interest which will subsequently be generated by the amount the court awards. However, although the lump sum awarded to the plaintiff is not taxable, any interest earned on it *is* taxable.[41] Thus, since the plaintiff will in fact pay taxes on a portion of his award, the *Floyd* rationale causes him to "pay" twice — once when prospective federal income taxes are subtracted from gross earnings to determine net future earnings and again when taxable interest is earned on the discounted damage award. The problem becomes particularly severe in a factual situation such as that in *Neff,* where, because of the long life expectancy of the deceased, a large portion of the award will be reflected in subsequent interest. The courts are, thus, faced with a dilemma: to follow *Floyd* may result in short-changing the plaintiff, while to follow *Jennings* and refuse to subtract taxes at all usually results in over-compensation.

COMPROMISE SOLUTIONS TO THE *Floyd-Jennings* DILEMMA

The Court of Appeals for the Second Circuit, beginning with the case of *McWeeney v. New York, New Haven & Hartford Railroad,*[42] has developed a novel compromise formula, incorporating some of the better aspects of the *Floyd* and *Jennings* approaches. The *McWeeney* court declared that income taxes would not be subtracted from lost future earnings in wrongful death or personal injury actions unless the amount of taxes involved was sufficiently large to demand such a deduction:

> There may be cases where failure to make some adjustment for the portion of a plaintiff's or decedent's earnings that would have been taken by income taxes would produce an improper result. . . .
>
> For example, if a plaintiff or a plaintiff's decedent, had potential earnings of $100,000 a year, more than half of which would have been consumed by income taxes, an award of damages based on gross earnings would be plainly excessive. . . .[43]

The rationale underlying *McWeeney* is that such deductions are improper in the normal cases because of the speculative nature of the

40. *See* McWeeney v. New York, N.H., & Hart. R.R., 282 F.2d 34, 37 (2d Cir.), *cert. denied,* 364 U.S. 870 (1960); Nordstrom, *Income Taxes and Personal Injury Awards,* 19 OHIO ST. L.J. 212, 217-18 (1958).

41. Rev. Rul. 29, 1965-1 CUM. BULL. 59. *See* Jennings v. United States, 178 F. Supp. 516 (D. Md. 1959), where this argument was used to justify a denial of the deduction.

42. 282 F.2d 34 (2d Cir.), *cert. denied,* 364 U.S. 870 (1960). It is notable that the Second Circuit also decided the *Stokes* case. *See* note 25 *supra* and accompanying text.

43. *Id.* at 38.

deduction and because over-compensation of the plaintiff is offset by attorney's fees, inflationary effects, and the fact that the plaintiff will have to pay taxes on the interest earned by the award. However, if the amount of prospective taxes involved becomes very large, then the cumulative effect of these factors is not sufficient to override the injustice of refusing the deduction.

The *McWeeney* approach has produced some interesting results in the Second Circuit. In *McWeeney,* a personal injury action, the deduction was denied because the plaintiff's earning capacity was only $5,000 per year. Subsequently, deductions were also denied where a decedent's earnings capacity was $10,000 per year[44] and where the decedent was a longshoreman, whose income was, presumably, quite modest.[45] Yet the deduction has been made when the decedent's earning capacity was about $16,000 per year,[46] a sum considerably removed from the $100,000 income cited in *McWeeney* as an example of when the deduction should be made. In *Cunningham v. Rederiet Vindeggen A/S and M/S Trolleggen,*[47] the Second Circuit, clarifying *McWeeney,* stated that:

> The crucial issue is not . . . simply whether libellant would ever have received any of that portion of decedent's future earnings which would have been withheld for taxes. Rather, the crucial issue is whether a court can predict with sufficient certitude just what portion of decedent's earnings would have been placed beyond libellant's reach by future tax laws so as to permit the court justly to reduce the damage awarded which libellant would otherwise be entitled to.[48]

The court seems to suggest that the higher the decedent's income, the easier it is to predict the taxes he would have had to pay, and thus the more unjust it is to deny the deduction. Implicit in this reasoning is the questionable premise that unpredictable future events will not alter the high-income decedent's tax liability to the same extent that they would alter the lower income decedent's tax liability. Thus, while the approach adopted by the Second Circuit is a practical compromise of a difficult problem, the result appears to be that the individual defendant's right to objective justice depends on the size of the plaintiff's, or his decedent's, bank account.[49]

The recent case of *Beaulieu v. Elliot*[50] offers another compromise solution. *Beaulieu* was a personal injury case in which the court determined that the plaintiff had lost $10,750 in wages between the time of the accident and the time of the trial and remanded for a

44. *In re* Marina Mercante Nicaraguense, S.A., 364 F.2d 118 (2d Cir. 1966); Montellier v. United States, 315 F.2d 180 (2d Cir. 1963).

45. Cunningham v. Rederiet Vindeggen A/S and M/S Trolleggen, 333 F.2d 308 (2d Cir. 1964).

46. Leroy v. Sabena Belgian World Airlines, 344 F.2d 266 (2d Cir. 1965).

47. 333 F.2d 308 (2d Cir. 1964).

48. *Id.* at 314.

49. *See generally* 14 VAND. L. REV. 639 (1961).

50. 434 P.2d 665 (Alaska 1967).

more explicit finding of his lost future earnings. The court held that the computation of the final award could reflect the plaintiff's income tax liability only with respect to the wages lost *before* the trial; projected post-trial earnings would not be subject to the deduction. The reason for this distinction appears to be that the income tax liability of a plaintiff between accident and trial is a known quantity, not subject to the "too conjectural" objection. It is arguable, however, that a plaintiff's income tax liability on wages lost during the period between accident and trial is still quite speculative. *Beaulieu* seems to overlook the fact that there is more involved in the "too conjectural" argument than the mere uncertainty of the applicable tax rates. Changes in the plaintiff's individual circumstances, such as his job and marital status, might have materially altered his tax liability by affecting the exemptions and deductions available to him under the Internal Revenue Code. Theoretically, the Anglo-American legal system measures damages by an educated guess as to what would have occurred, not what actually happened subsequent to the accident.[51]

CONCLUSION

It is increasingly clear that the courts are floundering in the face of the problem of whether to deduct income taxes from prospective earnings when calculating personal injury and wrongful death damages. The *Stokes* rule of simply denying all consideration of income taxes gave consistent, if unjust, results. Today, at least in wrongful death actions, many courts are aware of the injustice of an absolute denial of consideration of income taxes. This realization has taken three forms. Some courts, as in *Jennings,* have carried forward the old rule, adding new justifications to the "too conjectural" argument. Other courts, as in *Floyd,* have disagreed and have allowed prospective taxes to be considered. The Second Circuit, realizing the drawbacks of both these approaches, has attempted a compromise. It is submitted that none of these approaches achieves a truly satisfactory result.

One solution to the problem may be to take the *Floyd* rationale one step further. *Floyd* makes the deduction because of the patent injustice of forcing the defendant to pay a sum greater than the plaintiff's actual loss, thereby giving the plaintiff a windfall. What *Floyd* overlooks is the fact that the interest the damage award earns is taxable. Since these awards are discounted on an annuity basis, so that interest to be earned on the amount awarded is part of the total compensation, the plaintiff is in fact paying taxes on part of his recovery. To achieve the best result after making the *Floyd* deduction, an amount which represents the tax liability of the plaintiff on the

51. *See* Slater v. Mexican Nat'l R.R., 194 U.S. 120 (1904), where Mr. Justice Holmes indicated that the Mexican system of awarding tort damages, having the defendant pay the plaintiff each year for his actual losses that year due to the injury, was alien to the American system. The American system is based on what might happen, not what actually happens. *See generally* Lawless, *Computation of Future Damages: A View from the Bench,* 54 GEO. L.J. 1131 (1966).

interest element of the damage recovery must be added back to the award.[52] Although such a computation would require the same estimation of future tax rates as is required for the *Floyd* deduction, it would be considerably less speculative because the farther into the future the calculations proceed, the less the amount of interest paid,[53] since the recipient of the award will presumably use the original sum to defray living expenses over the years. While the speculative problem increases with time, the practical effects of any discrepancy decrease. A court willing to go as far as *Floyd* should have little hesitancy in taking this final step to rationality.

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52. *See* Morris & Nordstrom, *Personal Injury Recoveries and the Federal Income Tax Law,* 46 A.B.A.J. 274, 328 (1960). This amount, when added back to the award, would have to be reduced to its present value in order to avoid over-compensating the plaintiff.

53. Nordstrom, *Income Taxes and Personal Injury Awards,* 19 OHIO ST. L.J. 212, 227 (1958).