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Senate District A



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SPONSOR STATEMENT

Senate Bill 300

"An Act relating to an attorney's lien, to court actions, and to other proceedings where attorneys are employed; and providing for an effective date."

SB 300 eliminates a double taxation issue affecting many Alaskan taxpayers.

Because of a peculiarity in Alaskan law, Alaskans who win in court may pay federal income tax on phantom income. When Alaskans file their federal tax return, they must report any litigation recovery allocated to attorney fees as gross income, even though they receive no economic benefit from those fees. As a consequence, the federal government taxes that portion of the prevailing side's award twice; once as income to the client and again as income to the client's attorney. Incredibly, there is no federal tax deduction to offset this inequity.

Under current Alaska lien law <AS 34.35.430>, attorneys have a "subordinate lien" or ownership interest in the "cause of action". Other states, like Oregon, use different language to specify that as long as an attorney has filed an appropriate lien and is owed money by the winning client, all fee awards or payments made to the client belong exclusively to the attorney. In so vesting the attorney with the property interests of the award, those states avoid the unfair tax burden currently imposed on Alaskans. Instead, any portion of an award retained to pay attorney contingency fees, isn't reportable income to the client.

SB 300 changes Alaskan law to prevent the IRS from taxing Alaskans on income they don't receive. This bill recognizes that fee awards passing through to one's attorney are income to the attorney. And as such, the attorney is responsible for paying federal income tax on that portion of their income.