No Corporate Tax Deduction for Sexual Harassment or Sexual Abuse Settlements?

By Stephen Turanchik, Stephen Harris & Leslie Abbott

According to the recent Description of the Chairman’s Modification to the “Tax Cuts and Jobs Act” prepared by the Staff of the Joint Committee on Taxation companies will not be able to claim an income tax deduction for any settlement, payout, or attorneys’ fees related to sexual harassment or sexual abuse if such payments are subject to a nondisclosure agreement. This would be a significant departure from current law, where corporate taxpayers generally are allowed to deduct employment-related settlement amounts, including attorneys’ fees, as ordinary and necessary business expenses.

Paul Hastings’ Takeaway
Employers typically require confidentiality when they settle any type of employment-related claim. If this proposal becomes law, employers will have tough choices to make. Several possible options include:

1. Employers demand confidentiality and suffer the loss of deduction (which will be mitigated by the lower corporate tax rate);
2. Employers demand confidentiality and require the accused to contribute to the settlement to mitigate the loss of deduction;
3. Employers demand confidentiality and value cases lower from a settlement perspective;
4. Employers demand confidentiality and specifically allocate as much settlement consideration as possible to non-harassment or abuse claims (of course, it is too early to tell whether this will be permissible);
5. Employers let the accused decide whether to demand confidentiality and contribute to the settlement if they do; and
6. Employers may forgo settlement confidentiality as to sexual harassment claims to preserve the corporate tax deduction, perhaps, coupled with a policy or practice of transparency with regard to these issues.

We will keep our clients informed of any final changes in the law related to this issue.
If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings Los Angeles lawyers:

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