# Computation of Lost Future Earnings in Personal Injury and Wrongful Death Actions

The computation of lost future earnings has created a great deal of confusion and led to inconsistent holdings in both federal and state courts, but few jurisdictions have taken a less definitive position than Indiana. The purpose of this Note is to discuss the cases in which Indiana has dealt with four interrelated issues concerning the type of evidence admissible in computing lost future earnings in personal injury and wrongful death actions, as well as those cases decided by the federal courts and other state courts. The four issues to be discussed are as follows: (1) To what extent may expert testimony of future inflationary trends be used in the computation of lost future earnings? (2) To what extent may expert testimony as to probable increased productivity be used in the computation of lost future earnings? (3) May a jury be instructed that every award made to a party in a personal injury or wrongful death action for lost future earnings will not be subject to federal taxation? (4) May evidence of the impact of income taxes on future earnings be introduced to decrease any award for lost future earnings? The first two issues are often dealt with interchangeably by the courts. Therefore, they will be discussed together in this Note with distinctions being drawn whenever possible. Similarly, the third and fourth issues raising evidentiary questions relating to the impact of the tax laws on future awards will be discussed together as they raise comparable problems.

As a final matter, it is critical to an intelligible discussion of the issues in this Note to understand the basic system of damages in this country. Damages in wrongful death and personal injury litigation are based upon the theory of pecuniary reparation. The objective is to place the injured person in the same position, as nearly as possible with a monetary award, as he or she should have been in had the wrong not occurred.[1] This Note will explore how this system of damages is affected by the four factors to be discussed.

## I. Inflationary and Productivity Factors

### *A. Introduction*

Professors Harper and James suggest that the confusion surrounding awards of present damages for future loss is insoluble where there is a lump sum recovery.

Future trends in the value of money are necessarily

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[1]*See* G. Parmele, Damage Verdicts, § 2 at 37-38 (1927); *see also* Chesapeake & O. Ry. v. Kelly, 241 U.S. 485 (1916).

> unknown and so always render such damages speculative in a way we cannot escape. If the estimates represent a straight-line projection of present living costs, they will be frustrated by fluctuations either way. If prophecy of change is heeded, frustration will follow if no change, or the opposite change, occurs. When courts have consciously grappled with the problem they have either found all prophecy too speculative and so, perforce, have taken the equally speculative course of betting on a continuance of the status quo; or they have made intuitive and not always very wise judgments that present conditions represent a departure from some imaginary norm to which they think we shall rapidly return.[2]

The courts often compound the problem by confusing inflation with productivity factors and by using the terms "inflation," "growth factor," "earnings increase factor," or "economic trends" to include both concepts of economic growth. To an economist, inflation is the percentage of rate of increase in the price level. "Productivity," on the other hand, depends on the industry a person is in. To ascertain the increase in productivity, the economist must assess "the contribution to wages that will derive for attendant increases in technologies peculiar to that industry."[3] Bascially, productivity appears to be a factor based on a worker's increased skill and output as he gains experience at a particular job and also the current improvements in technology which increase his output.[4] This Note will make distinctions whenever possible.

The United States Supreme Court has ostensively dealt with these factors in *Grunenthal v. Long Island Railroad*,[5] but the decision has not provided useful guidelines for lower courts. In *Grunenthal*, the Court upheld a damage award in an FELA case based upon projections of increased wage growth. The Court quoted the trial judge's conclusion that the plaintiff had presented "convincing testimony not refuted . . . demonstrating the steady wage increases in recent time for work equivalent to that rendered by plaintiff, and the strong likelihood that similar increases would continue."[6] This language does not elucidate whether the court was referring to inflation, productivity or both. As a result, the case has created confu-

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[2]II. F. HARPER & F. JAMES, THE LAW OF TORTS, 1325-26 (1956).

[3]Rall, *How to Prepare the Economic Evaluation Report*, TRIAL, April 1977, at 49.

[4]*See* Rall, *supra* note 3, at 47-53. *See also* Huddell v. Levin, 395 F. Supp. 64, 84 n.20 (1975); Hoffman v. Sterling Drug, Inc., 374 F. Supp. 850, 853 (M.D. Pa. 1974).

[5]393 U.S. 156 (1968).

[6]*Id.* at 160.

sion in the lower courts and has not been followed.[7] Furthermore, the case has been distinguished on the grounds that *Grunenthal* involved the question of whether a federal court had abused its discretion in approving the award as found by the jury, thus the issue as to the prejudicial nature of the testimony on future inflation was not raised.[8] The Supreme Court's opinion in *Grunenthal* is indicative of the confusion generated by these issues in other jurisdictions.

### *B. Indiana*

Indiana has no reported decisions dealing directly with the admissibility of expert testimony and the use of inflationary and productivity factors in the computation of lost future earnings. However, there are several reported decisions in Indiana that indicate at least a tacit recognition of evidence of this type.

In *King's Indiana Billiard Co. v. Winters*,[9] the court of appeals upheld an award that the appellants contended was excessive, stating:

> The jury in assessing damages for loss of earnings is not limited to the amount being earned by the plaintiff at the exact time of his injury but may fairly compensate the plaintiff for such loss of earnings as he actually has and will sustain. . . .
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> . . . .
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> And, furthermore, the court on appeal will consider the diminished purchasing power of the dollar at the time the verdict is rendered.[10]

However, there was no evidence from the opinion that any testimony as to future economic trends had been offered. Also, while many reviewing courts have used judicial notice of inflation in justi-

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[7]One recent example is Henderson v. S.C. Loveland Co., 396 F. Supp. 658 (N.D. Fla. 1975), in which the court referring to the above quote, stated:

> While not clear from the decision, that evidence may not have been tied to inflation. In the case before this court, allowance was, of course, based on inflation. As appears from it's decision, there was no evidence before it of prior increases for work equivalent to that performed by plaintiff other than cost of living increases. *Penrod* and other recent Fifth Circuit decisions, though neither mentioning nor distinguishing *Grunenthal*, come several years after it. Without undertaking further to reconcile these decisions, if they need reconciliation, this court is constrained to follow, and will follow, the categorical statement of these recent decisions of the Fifth Circuit that the effect of future inflation is not to be considered in calculating future damages.

*Id.* at 660.

[8]*See* Raines v. New York R.R., 129 Ill. App. 2d 294, 263 N.E.2d 895 (1970), *rev'd on other grounds*, 51 Ill. 2d 428, 283 N.E.2d 230, *cert. denied*, 409 U.S. 983 (1972).

[9]123 Ind. App. 110, 106 N.E.2d 713 (1952).

[10]*Id.* at 124-25, 106 N.E.2d at 719.

fying an award claimed to be excessive, this question is distinct from the question of whether the jury should be allowed to consider the effects of possible future inflationary trends.[11]

In a more recent case, *State v. Daley*,[12] the court of appeals upheld the lower court's award based largely upon the uncontroverted testimony of an expert economist who had used an expected five percent wage increase factor in his computation of lost future earnings. Noting that the jury had apparently accepted the economist's projections as an accurate and fair calculation of the decedent's projected future earnings, the court stated: "An awareness of general inflation and a constant depreciation and cheapening of money is within the zone of discretion given to the trier of facts when assessing damages."[13]

In a subsequent case, *Richmond Gas Corp. v. Reeves*,[14] the court of appeals upheld a $250,000 verdict in a wrongful death action based upon a testimony of an actuary who had used a two percent annual wage increase factor in computing the projected future earnings of the twenty-six year old decedent. The court again emphasized, as it had in *Daley*, that the jury could consider such factors as general inflation and the constant depreciation and cheapening of money when assessing damages.[15]

It is significant that the *admissibility* of expert testimony on future inflationary trends or increased productivity was not raised in any of the above actions and that the court of appeals did not, in fact, decide this issue. Therefore, the results in the above cases may well be explained as an application of the liberal Indiana rule that damages will not be deemed excessive on review unless they are flagrantly outrageous and extravagant.[16] Thus, a subsequent case, which raised the admissibility issue, might well be distinguishable.[17] For this reason, it is necessary to look to other jurisdictions that

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[11]*See, e.g.*, Carol v. United States, 410 F. Supp. 378, 396-97 (D.R.I.), *aff'd*, 548 F.2d 366 (1st Cir. 1976).

[12]153 Ind. App. 330, 287 N.E.2d 552 (1972).

[13]*Id.* at 337, 287 N.E.2d at 556.

[14]158 Ind. App. 338, 302 N.E.2d 795 (1973).

[15]*Id.* at 369, 302 N.E.2d at 815.

[15]*See* State v. Daley, 153 Ind. App. 330, 287 N.E.2d 552 (1972), where the rule was set out that in order for damages to be ruled excessive on review they "must be so excessive as to strike mankind, at first blush, as being beyond all measure, unreasonable and outrageous, and such as manifestly show the jury to have been actuated by passion, partiality, prejudice, or corruption." *Id.* at 337, 287 N.E.2d at 556 (quoting Coleman v. Southwick, 9 Johns 45 (N.Y. Sup. Ct. 1812). *See also* Richmond Gas Corp. v. Reeves, 158 Ind. App. 338, 302 N.E.2d 795 (1973).

[17]For a case making a similar distinction, *see* Raines v. New York R.R., 129 Ill. App. 2d 294, 263 N.E.2d 895, *rev'd on other grounds*, 51 Ill. 2d 428, 283 N.E.2d 230, *cert. denied*, 409 U.S. 983 (1972).

have engaged in an in depth analysis of the factors favoring and opposing the use of inflationary and productivity factors in the computation of lost earnings for a more thorough discussion of these factors.

### *C. Federal Courts*

*1. First Circuit.*—Although it has never addressed the issues of inflation and productivity factors separately, the First Circuit has rejected the admission of any evidence concerning the future trends of such factors for computations of future losses. The court in *William v. United States*[18] refused to increase future earnings by what it viewed as "some multiple taken out of the thin air in the name of future inflation."[19] The court argued that if evidence of the effect of future inflationary trends were considered, it would likewise be necessary to make an adjustment for possibly inflated expenses as well as earnings, and the court viewed both of these elements as too speculative. In a later decision, the court stated that consideration of "economic trends" would require the judge and jury to "take on the 'joint role of soothsayer and mathematical analyst in order to foretell what the future held for the deceased.' "[20] The most recent decision from a district court in the First Circuit adopted the rationale used by the court of appeals in rejecting any evidence concerning future inflationary trends and added the argument that the plaintiff could place his award in investments that gain a higher return than the statutory interest rate and thereby reduce any adverse effects of inflation.[21]

*2. Second Circuit.*—The Second Circuit has also held that inflation should not be considered in computing lost future earnings. In

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[18]435 F.2d 804 (1st Cir. 1970). *Williams* was a wrongful death action brought under the FTCA.

[19]*Id.* at 807. No reference was made in the opinion as to what, if any, expert testimony had been presented on the question of future inflation.

[20]Turcotte v. Ford Motor Co., 494 F.2d 173, 184 (1st Cir. 1974) (citing Romano v. Duke, 111 R.I. 459, 463, 304 A.2d 47, 51 (1973). *Turcotte* was an action brought under the Rhode Island wrongful death statute, which authorized a consideration of economic trends. Thus, while bound by state law to allow the use of inflationary and productivity factors, the court did note its general disapproval of such a statute.

[21]Caron v. United States, 410 F. Supp. 378, 396-97 (D.R.I. 1976). While *Caron* was a personal injury action governed by Michigan law, the district court noted that it found Michigan law on the evidentiary issue no different than the existing law in the First Circuit. The court also rejected the appellant's contention that prior decisions permitting the court to take judicial notice of inflation indicated such evidence was admissible. The court stated that such cases stood only for the proposition that the courts may take notice of rising prices due to past inflation in order to justify large verdicts against a charge of excessiveness. This is what the language in the Indiana decisions appears to suggest.

*McWeeney v. New York, New Haven & Hartford R.R.*,[22] the Second Circuit noted in dictum that although "some courts have sanctioned instructions permitting the jury to take into account inflation between the injury and the trial, there is little or no authority in favor of charging the jury to take future inflation into account."[23] The court thus justified the trial court's refusal to give any instruction on income taxes, in part on the ground that any windfall to the plaintiff would be offset by lack of adjustment for inflation. Judge Lumbard, concurring in part and dissenting in part, added that such evidence is too speculative and that any plaintiff receiving a large amount could invest the award in a manner that would give him some protection against both inflation and deflation.[24] However, the court of appeals did indicate in a subsequent case that it felt the courts might have to reconsider the propriety of receiving evidence on inflation if inflation should continue at its present pace.[25]

Nevertheless, two recent cases based on Connecticut law permitted extensive expert testimony on the question of inflation. In *Perry v. Allegheny Airlines, Inc.*,[26] the plaintiff's expert economist was permitted to use estimates of prospective future earnings testified to by the decedent's employer and to make "certain assumptions concerning future rates of inflation and interest" in arriving at the net economic loss for future earnings.[27] The opinion did not specify what these assumptions were or upon what they were based.

The Connecticut District Court was later faced with the converse of the question of whether the fact finder should consider inflation in evaluating the loss of future earning capacity, that being whether inflation should be considered in setting the interest rate by which the already assessed dollar amounts for the loss of future earning capacity were to be discounted to their present value. The district court approved the use of such an "inflation adjustment" in setting a discount rate.[28]

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[22]282 F.2d 34 (2d Cir.), *cert. denied*, 364 U.S. 870 (1960). The court's main focus in this case was whether the evidence should be limited to plaintiff's net income in an FELA action.

[23]*Id.* at 38.

[24]*Id.* at 42-43 (Lumbard, C.J., dissenting in part & concurring in part).

[25]Yodice v. Koninklijke, Nederlandsche Stoomboot Maatschappij, 443 F.2d 76 (2d Cir. 1971), *cert. denied*, 411 U.S. 933 (1973).

[26]489 F.2d 1349 (2d Cir. 1974).

[27]*Id.* at 1351.

[28]Feldman v. Allegheny Airlines, Inc., 382 F. Supp. 1271 (D. Conn. 1974), *aff'd in part, rev'd and remanded on other grounds*, 524 F.2d 384 (2d Cir. 1975). The district court had relied on an economic expert's calculation in which the expert had used average earnings of 4.14% as representative of a prudent, non-sophisticated investment and subtracted 2.87% as the yearly inflation rate, yielding a 1.27% difference, which was rounded up to 1.5%.

However, the court of appeals, in affirming the district court's decision, made it clear that the case should not be considered a precedent for cases arising under federal law, stating: "As a matter of federal law we do not necessarily vouchsafe either the principle of making an 'inflation adjustment' in setting a discount rate or the means by which it was done in this instance."[29] The court of appeals avoided an analysis of the reliability and speculativeness of the evidence provided by the plaintiff's economist by relying on the state's law giving the court the flexibility to consider inflation. Apparently the court of appeals agreed with the district court that the Connecticut law requiring discounting to present value for destruction of future earnings capacity compelled the court to "engage in economic forecasting despite the inexactitude of the dismal science's soothsaying."[30] Finally, another factor in the willingness of the court in both decisions to permit the inflation adjustment was the requirement under Connecticut law that future income taxes be deducted from any award.[31] Thus, the converse of the argument previously used in *McWeeney* was not available to the court in *Feldman.* It therefore appears that although the two recent cases based on Connecticut law seem to indicate more of a readiness to accept evidence incorporating inflationary and productivity factors, the Second Circuit's present position as expressed in *McWeeney* is that such evidence is too speculative.[32]

*3. Third Circuit*—The Third Circuit's Position, while not totally clear, appears to be that evidence of inflationary trends and increased productivity may only be admitted after a strict foundation has been laid to insure as much reliability in such projections as possible. The Third Circuit has also exhibited more of a readiness to accept evidence as to productivity increases than as to inflationary trends. In *Magill v. Westinghouse Electric Corp.*,[33] the court rejected an actuary's computations that incorporated an "earnings increase factor," stating that "the lack of foundation for the earnings

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[29]524 F.2d at 387.

[30]382 F. Supp. at 1293 n.30.

[31]The court of appeals noted that it felt the district court had appropriately hypothesized the Connecticut Supreme Court's favorable reaction to discount rate adjustment, "since Connecticut, unlike most jurisdictions, reduces what would otherwise be inflated judgments for wrongful death injuries by requiring deduction of income taxes payable on future earnings." 524 F.2d at 387.

[32]This conclusion is supported by Judge Friendly's concurring opinion in *Feldman*, where, after pointing out that utilization of an inflation rate in determining the discount rate gives nearly the same result as does first considering inflationary effects on future income and then discounting to present value, he expressed his concern that such method poses the problem of potential speculativeness in calculating damages. *Id.* at 390-93.

[33]464 F.2d 294 (3d Cir. 1972).

increase factor was a fatal defect."[34] In dicta, the court did indicate a greater willingness to accept evidence of productivity factors as opposed to inflationary factors, noting that it considered evidence of promotions or pay raises as a proper foundation upon which to gauge an increase in future earnings.[35]

A somewhat stronger case rejecting the use of inflationary trends as too speculative was *Frankel v. United States.*[36] In rejecting the offered evidence of inflationary trends, the court specifically criticized the use of an unusual time period by the plaintiff's expert in making his projections. Furthermore, the court indicated that the government's present attempts to control inflation and the fact that any award could be invested so as to offset the effects of inflation were factors weighing against admissibility.[37] The court's criticism at least impliedly indicates that such evidence might have been permitted if a proper foundation had been laid.[38] This conclusion is further supported in a subsequent court of appeals decision, *Hoffman v. Sterling Drug, Inc.*,[39] in which the court rejected evidence offered by the plaintiff's expert as too conjectural. In *Hoffman*, no evidence was introduced in the case as to the probablility or magnitude of future inflationary trends. The court specifically criticized the economic expert's attempt to isolate a five year period of extreme inflation as the basis for a projection over twenty-six years without introducing any evidence to support such a projection.[40]

On remand after the Third Circuit's decision, the plaintiff argued that the court of appeals in *Magill* and the present case had found error in admitting testimony based on such a brief span of time and that they should not be precluded from introducing evidence of economic trends from a twenty year time span.[41] The court first noted that the confusion that existed in this area was

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[34]*Id.* at 300.

[35]However, the court specifically noted that the concept of inflation and the declining value of the dollar had almost been universally rejected as providing support for the earnings increase factor. Also central to the court's holding was the fact that the expert used was only an actuary and the method of calculations used was one used by accountants for a somewhat different purpose. *Id.* at 300-01.

[36]321 F. Supp. 1331 (E.D. Pa. 1970), *aff'd. sub nom.*, Frankel v. Heym, 466 F.2d 1226 (3d Cir. 1972). In *Frankel* the district court noted that inflationary considerations had been used in the justification of an award by considering present inflationary trends as compared to awards in the past, but they had not been used to project future earnings.

[37]The plaintiff's expert had used the decade of the 1960's, one of the more inflationary times in the history of our country, as the basis for his projection. *Id.* at 1346.

[38]*See also* Griffin v. United States, 500 F.2d 1059, 1070 (3d Cir. 1974).

[39]485 F.2d 132, 144 (3d Cir. 1973).

[40]*Id.* at 143-44.

[41]374 F. Supp. 850, 853 (M.D. Pa. 1974).

partially due to an imprecision of terms used, acknowledging that often the expressions "earnings increase factor" and "economic trends" are incorrectly used interchangeably by the courts. The former actually constitutes merit raises predicted over the plaintiff's life expectancy, while the latter reflects economic trends separate from the individual's employment situation.

The district judge indicated that the trial court error in the original *Hoffman* trial and in *Magill* was not the court's refusal to allow evidence on future economic trends "but rather our admission into the record of an earnings increase factor based on insufficient evidence. A close reading of *Magill* bears this out. Judge Adams' opinion in *Magill* carefully distinguishes between future earning power and future inflation."[42] On remand, the trial court rejected the defendant's argument that *Frankel* precluded all evidence on economic trends in computing loss of future earnings and stated that despite the difficulties involved the earnings increase factor of a particular plaintiff must be separated from future economic trends. Thus, the court would allow the plaintiff to present evidence to the jury as to the earnings increase factor but would not allow into evidence any testimony as to future economic trends, regardless of the foundation laid for it.[43]

However, a recent decision by another district court in the Third Circuit, *Huddell v. Levin*,[44] interprets *Magill* and *Hoffman* as standing merely for the proposition that a proper foundation must be laid to support the expert's opinion by showing specific evidence of long-range inflationary trends and wage increases in a particular job. The court rejected the defendant's argument that *Hoffman* and *Magill* prohibited the admission of testimony based upon growth rates while permitting the jury to consider future growth of earning capacity. In distinguishing *Huddell* from *Magill* and *Hoffman*, the court stated that it interpreted the two cases to mean merely that there must be competent evidence of probable future salary or economic trends, and evidence alone that growth had occurred in the past was not sufficient for this purpose. Thus, while *Magill* and *Hoffman* had disallowed the expert testimony for, in essence, not laying a proper foundation, the expert used in *Huddell* gave "the jury substantial evidentiary support for an award of damages based upon future growth of earnings. A more highly qualified expert in

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[42]*Id.* at 854.

[43]*Id.* at 855.

[44]395 F. Supp. 64, 83-84 (D.N.J. 1975), *remanded on other grounds*, 537 F.2d 726 (3d Cir. 1976) (quoting Hoffman v. Sterling Drug, Inc., 485 F.2d 132, 144 (3d Cir. 1973)). *Huddell* was a wrongful death action brought under New Jersey law in which the court upheld an award based on expert testimony using a six percent "growth rate" factor, which was made up of a three percent inflation factor and a three percent standard of living increase.

this field could not have been produced."[45] The two most recent district court decisions from the Third Circuit have concurred with the district court's interpretation in *Huddell* of the decisions in *Magill* and *Hoffman*, stating: "[B]oth cases imply clearly that future increases in earnings is a proper matter for the jury so long as there is sufficient competent evidence of 'probable future salary trends or economic trends.' "[46]

*4. Fourth Circuit.*—The Fourth Circuit has not dealt directly with the issues under consideration, but a district court did consider them in *Scruggs v. Chesapeake & Ohio Railway.*[47] The court permitted the use of evidence regarding inflationary and productivity factors, stating that such factors were clearly relevant to the question of lost future earnings. The court reasoned that since inflation is a universally discussed topic, the jury was likely to consider whether there was testimony directed to the issue or not. Therefore, it was proper to admit expert testimony to guide the jury, since they would take it into account in any event.[48] The district court concluded that inflation and productivity factors are relevant evidence and are no more speculative than other factors used to determine future damages.

*5. Fifth Circuit.*—The Fifth Circuit has considered the issue more often than any other circuit. It has rejected the use of productivity and inflationary factors as too speculative. However, there has been some indication in dicta that the court may accept evidence as to increased productivity provided a strict foundation is first laid to insure the reliability of such evidence. In *Johnson v. Penrod Drilling*

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[45]*Id.* at 83-84. The court of appeals, when remanding, did quote with approval a recent New Jersey decision, Tenore v. Nu Car Carriers, Inc., 67 N.J. 466, 481-84, 341 A.2d 613, 621-23 (1975), in which the New Jersey court had indicated that so long as the plaintiff had an opportunity to offer expert testimony to give the jury informed guidelines in their deliberations, such evidenced was no more conjectural than other evidence often introduced to the jury. Furthermore, consideration of well informed estimates of future inflationary trends would lead to fairer damage awards. *Id.* at 83-84.

[46]Thomas v. American Cystoscope Makers, Inc., 414 F. Supp. 255, 270 (E.D. Pa. 1976) (quoting Hoffman v. Sterling Drug, Inc., 485 F.2d 132, 144 (3d Cir. 1973)). *See also* Vizzini v. Ford Motor Co., 72 F.R.D. 132 (E.D. Pa. 1976).

[47]320 F. Supp. 1248, 1250-51 (W.D. Va. 1970). *Scruggs* was an action brought by the widow of a deceased employee in which an economic expert had testified that he had projected a five percent wage increase each year based on a two percent productivity increase and a three percent inflationary increase.

[48]*Id.* at 1250-51. *See also* Plant v. Simmons Co., 321 F. Supp. 735 (D. Md. 1970). The only other cases found in the Fourth Circuit were Scheel v. Conboy, 551 F.2d 41, 43 (4th Cir. 1977), and Whalen v. Marini, 542 F.2d 1170 (4th Cir. 1976). In both cases, the court merely rejected any testimony by economic experts on future economic loss because of the speculativeness of determining in each case whether any future economic loss had in fact occurred.

*Co.*,[49] the Fifth Circuit, en banc, rejected the use of expert testimony by an economist on the question of inflation. The court took judicial notice that inflationary conditions had existed for a number of years, but concluded that inflation was not a predictable condition for the future. In reaching this conclusion, the court considered two factors. First, past increases in inflation do not necessarily foretell future inflationary trends but could as easily lead to a recession. Second, the government has launched strong counter measures aimed at curbing inflation.[50] The court also pointed out that inflation is accompanied by high interest rates, which could compensate for failure to compute an inflationary surcharge in wage rate calculations.[51] To support its conclusion, the court cited Professors Harper and James' treatise on torts.[52]

Finally, the court intimated that the admission of testimony on future trends would open the door to other similarly speculative and debatable offsets, such as possible future taxes or future deflation.[53] In conclusion, the court stated: "We expressly disapprove the district court's attempt to take into account, in computing the plaintiffs' future lost earnings, inflationary trends in this nation's economy for the next several decades."[54] The *Johnson* decision has been followed by a multitude of Fifth Circuit decisions,[55] including its most recent decision in *Higginbotham v. Mobil Oil Corp.*[56] The

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[49]510 F.2d 234, 235-41 (5th Cir. 1975). In *Johnson* the plaintiff's economist projected an annual wage of 4.8% and the defendant's expert had countered that such a figure was too high, and that it was impossible to predict inflationary trends accurately.

[50]Judicial notice was also taken of price controls temporarily instituted in 1971 and current legislative advocacy of tax rebates as a means of counteracting a contemporaneous business recession in support of the proposition that, since government policies might intervene at any time to change or control the direction of the economy. The assumption of inflation over the next 34 year period was totally speculative.

[51]510 F.2d at 236.

[52]*Id.* at 239. *See* note 2 *supra* and accompanying text.

[53]510 F.2d at 241-42 (citing McWeeney v. New York, N.H. & H. Ry., 282 F.2d 34 (2d Cir.), *cert. denied*, 364 U.S. 870 (1960) & Sleeman v. Chesapeake & O. Ry., 414 F.2d 305 (6th Cir. 1969)).

[54]510 F.2d at 241.

[55]*See* David v. Hill Eng'r Inc., 549 F.2d 314, 331-35 (5th Cir. 1977) (also specifically disallowing productivity factor as too speculative); Matter of S/S Helena, 529 F.2d 744, 753 (5th Cir. 1976); Lacaze v. Olendorff, 526 F.2d 1213, 1222 (5th Cir. 1976); Petition of M/V Elaine Jones, 513 F.2d 911, 912 (5th Cir. 1975); Standefer v. United States, 511 F.2d 101, 107 (5th Cir. 1975); Robertson v. Douglas Steamship Co., 510 F.2d 829, 839 (5th Cir. 1975); Consolidated Mach., Inc. v. Protein Prod. Corp., 428 F. Supp. 209, 227 (M.D. Fla. 1976); Henderson v. S. C. Loveland Co., 396 F. Supp. 658, 662 (N.D. Fla. 1975). *Cf.* Law v. Sea Drilling Co., 510 F.2d 242, 251 (5th Cir. 1975) (recognizing *Penrod* but applying pre-*Penrod* law).

[56]545 F.2d 422, 433-34 (5th Cir. 1977).

plaintiff's expert economist used a five percent annual straight-line estimated salary increase to calculate the probable future earnings of the decedent.[57] On appeal, the defendant argued that the five percent straight-line annual increase amounted to a hidden inflation-based award. Plaintiff contended that such a figure represented awards in recognition of performance and experience. In reversing and remanding the case to the district court to give the plaintiff an opportunity to prove her damages for loss of her husband's future earnings, the court set out the following standard:

> We believe that *Johnson v. Penrod Drilling Co.* and its progeny likewise stand for the proposition that courts may not simply assume that projected wage increases—whether calculated from the decedent's past earning experience or by some other means—would have been granted solely in "recognition of performance and experience." To the contrary, to recover at all for future raises plaintiff must bear the difficult burden of proving what portion of the increases would have been given other than as an automatic hedge against inflation.[58]

While the opinion clearly implies that evidence of increased productivity may be allowed, the court concludes with the cautioning statement: "It remains, of course, within the trial judge's discretion to reject any testimony concerning future wage increases as too speculative . . . ."[59]

*6. Sixth Circuit.*—Although early Sixth Circuit decisions flatly rejected the use of inflationary or productivity factors as too speculative, recent decisions indicate a trend toward allowing the jury to consider future inflation under certain circumstances. The outstanding case in this area is *Sleeman v. Chesapeake Railway Co.*,[60] an FELA injury case. The district judge did not discount Sleeman's award for future earning capacity, because an economist had testified in other cases in his court that there was "jurisdiction for offset of discount to present worth of future earnings by increased

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[57]The economist had arrived at the five percent figure by calculating the annual percentage increases in the decendent's salary from the time he began working for his employer until death. *Id.* at 435.

[58]545 F.2d at 434-35.

[59]*Id.* at 435. Justice Godbold dissented, criticizing the court's original decision in *Johnson* and stating that where evidence of past wage increases are introduced a court should clearly be entitled to conclude that the pattern of past earnings increases is of sufficient duration and uniformity to be a reliable basis for an inference with respect to the future, despite the fact it may embrace in that pattern certain cost of living increments. *Id.* at 437.

[60]414 F.2d 305, 307-08 (6th Cir. 1969).

earning and appreciation factors."[61] The court of appeals found that the district court's decision lacked evidentiary support. The court recognized that the economic history of the nation since the 1930's would appear to make the exclusion of such factors somewhat unfair to the plaintiff, but suggested that the inflation versus deflation debate, which has raged inconclusively at the highest levels of government, was unlikely to be resolved in one personal injury trial. As a result, the court of appeals would not allow the trial courts of its circuit to explore such unresolved speculative issues.[62]

In a recent Sixth Circuit decision, *Bach v. Penn Central Transportation Co.*,[63] the court modified its position in *Sleeman*. The court indicated that the district court was correct in rejecting specific testimony offered by plaintiff's economic expert[64] as being too speculative to be admissible. However, the court of appeals held that the trial court had committed reversible error in instructing the jury that it could not consider the effect of inflation based on the jurors' knowledge of it. In rejecting the economist's evidence, the court stated:

> In recent history inflation has been so persistent that it is difficult to conceive that the purchasing power of the dollar might remain constant through the year 2000. On the other hand, the predictive abilities of economists have not advanced so far that they can forecast with any certainty the existence and rate of inflation for the next thirty years. Limited use of economists and other experts may be appropriate in some cases to show that raises in income or promotions would most probably occur.[65]

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[61]Sleeman v. Chesapeake & O. Ry., 290 F. Supp. 817, 829 (W.D. Mich. 1967).

[62]414 F.2d at 308. The court also cited with approval the same passages from Harper & James that had been cited by the Fifth Circuit in *Johnson*. *See* note 2 *supra* and accompanying text.

In a later decision, Willmore v. Hertz Corp., 437 F.2d 357, 360 (6th Cir. 1971), the court modified its position somewhat when it found the appellant's reliance on *Sleeman* with references to future fluctuation in purchasing power was misplaced, as the court was applying state law. The court noted that the discussion in *Sleeman* of the consideration of current economic trends in awarding future damages was actually dictum, because the reversal resulted from the district court's failure to reduce future damages to their present worth. However, there was no indication in the *Willmore* opinion that expert testimony was actually offered. *See also* Petition of United States Steel, 436 F.2d 1256, 1280 (6th Cir. 1970), *cert. denied*, 402 U.S. 987, *rehearing denied*, 403 U.S. 924, 940 (1971).

[63]502 F.2d 1117, 1122 (6th Cir. 1974).

[64]The economist had projected the exact income the decedent would have received through the year 2002 based on his knowledge of the railroad industry and estimates of future inflation. *Id.* at 1122.

[65]*Id.*

The language quoted above implies that evidence as to productivity increases might well be allowed.

The opinion contained even stronger dicta indicating that the court might accept a more generalized exposition of the economic factors involved in computing future cost earnings:

> We do not hold, however, that the jury may never consider inflation and future increases in income in determining damages. . . . If a jury is not permitted to consider decreases in the purchasing power of money, appellant would be woefully damaged if inflation should continue at its present or at any other substantial rate. . . . The court's role is to keep such extrapolations within reasonable bounds and insure they conform to evidence. . . .
>
> . . . Inflation is a fact of life within the common experience of all jurors. Admittedly, if the jury considers this issue without expert testimony, their calculations will be even more imprecise.[66]

This language, though dicta, would suggest that the Sixth Circuit may be moving away from its position in *Sleeman*. After its decision in *Bach*, the Sixth Circuit may allow the jury to consider future inflation based on either the jurors' own knowledge or on general information supplied by an economist, so long as the economist's evidence is not in the form of precise computations of damages set forth by economic analysis.

*7. Seventh Circuit.*—The Seventh Circuit has never directly addressed the question of whether expert testimony would be allowed concerning the use of inflationary and productivity factors in the computation of future lost earnings. However, in *Wetherbee v. Elgin, Joliet & Eastern Railroad*,[67] the court of appeals did express concern regarding the increasing size of personal injury awards:

> The way the amounts awarded in verdicts in personal injury cases have been rapidly increasing is a matter of concern to all who are interested in a fair and orderly administration of justice. . . . Even allowing for the decreased purchasing power of the dollar, many of the recent large awards for damages are not justified.[68]

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[66] *Id.*

[67] 191 F.2d 302 (7th Cir. 1951).

[68] *Id.* at 309. The reference to allowing for decreased purchasing power of the dollar refers to the use of comparison of past awards with present awards to determine if such award is excessive and has no bearing on the question of whether inflationary and productivity factors may be considered in computing lost future earnings. *See* Frankel v. United States, 321 F. Supp. 1331, 1345-46 (E.D. Pa. 1970), *aff'd*, 466 F.2d 1226 (3d Cir. 1972).

This would indicate that the court would not be anxious to approve any new methods of computations that would encourage juries to return even higher verdicts.

*8. Eighth Circuit.*—The Eighth Circuit has essentially adopted the same position followed by the Sixth Circuit. Thus, while the use of specific evidence is rejected as too speculative, the use of evidence of productivity increases is permitted if a proper foundation is provided. The Eighth Circuit has also shown a willingness to allow the jury to consider the dollar's diminished or increased purchasing power. The court first addressed the issue in *Riha v. Jasper Blackburn Corp.*,[69] a diversity action brought under Nebraska law. After quoting extensively from the Sixth Circuit's opinion in *Bach* v. *Penn Central Transportation Co.*,[70] the court concluded that even under the more liberal approach suggested by *Bach*, the evidence of future inflation was too speculative to be admitted under both federal and Nebraska law.[71] In *Johnson v. Serra*,[72] a diversity action brought under Minnesota law, the court cited *Bach* again in holding that the lower court had abused its discretion in allowing the plaintiff's expert to testify using computations that provided for an annual wage increase.[73] The court noted that such evidence was too conjectural and speculative and therefore lacked sufficient probative value to outweigh the danger that it would lead the jury to assess damages on an improper basis. Furthermore, the court indicated that it viewed inflationary forecasts of economists as only personal opinions of the meaning of past trends, which may well be faulty indicators of the future.[74]

The court went on to point out that nearly all federal courts dealing with federally created claims, such as FELA or Jones Act cases, have rejected testimony, jury instructions, or trial court consideration of any kind of future inflationary trends in damage assessments, while some state courts, or federal courts applying state laws, have permitted consideration of inflation. The court concluded its discussion of the question with the following statement:

> In sum, Dr. Foster's testimony in the instant case, as that in the Bach case, lacked sufficient evidentiary founda-

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[69]516 F.2d 840 (8th Cir. 1975). In *Riha*, the plaintiff's expert had used a 4.4% inflationary factor and a 7% annual wage increase factor in his computations. *But see* Beanland v. Rock Island & P. R.R., 480 F.2d 109, 117 (8th Cir. 1973) (Bright, J., concurring).

[70]502 F.2d 1117, 1122 (6th Cir. 1974).

[71]516 F.2d at 845.

[72]521 F.2d 1289 (8th Cir. 1975).

[73]*Id.* at 1293. The expert had taken the average wage increases for teamsters since 1947 (a 5.6% increase) and used the annual yield on conservative investments (4.1%) to yield a differential of 1.5% in his computation.

[74]*Id.* at 1294.

> tion—*as projections of distant future inflationary trends inevitably must.* His testimony on future inflationary projections to the year 2002 should, therefore, have been excluded as speculative and the excessive verdict obviously derived from it must be reduced or, in the alternative, a new trial granted.[75]

*9. Ninth Circuit.*—Two recent decisions by the Ninth Circuit clearly indicate that expert testimony on changing economic trends is admissable where a proper foundation is laid. In *United States v. English*,[76] a wrongful death action under California law, the court of appeals found that the trial court had erred in not reducing the award to present value, but in dictum approved the admissability of expert testimony on the effect of inflation on future damages. While recognizing it was controlled by California law, the court of appeals stated it would be compelled to reach the same result under federal law for several policy reasons. First, the court acknowledged that it is somewhat speculative to attempt to forecast future inflationary trends, but the court suggested that most predictions about future income are equally suspect. The court reasoned that since it is more likely that there will be changes in the value of the dollar than not, it is better to try to predict these changes than to ignore them altogether. Second, the court recognized that many of the cases in other districts originally rejecting the use of evidence pertaining to inflation awards were decided at a time when inflation was not considered as such an integral part of our economic lives. Thus, to ignore inflation was viewed to be the same as predicting it would not occur, or that its effect would be de minimis. Although recognizing that the administrative convenience of ignoring inflation has some appeal when inflation rates are low, the court stated that "to ignore inflation when the rates are high is to ignore economic reali-

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[75] *Id.* at 1296-97 (citations omitted) (emphasis added). While *Riha* and *Serra* appear to adequately express the Eighth Circuit's view on the question of admissibility of evidence as to future inflationary trends, notice should be taken of two subsequent cases allowing such evidence. In Raney v. Honeywell, Inc., 540 F.2d 932 (8th Cir. 1976), a case decided under Iowa law, the court upheld an award based on computations made by plaintiff's expert that relied upon an inflationary rate and a discount rate of six percent to cancel each other out. The court distinguished *Raney* from *Riha* and *Serra*, noting that they both had been based on state laws that did not permit such evidence, whereas Iowa law permitted evidence of inflation to be considered by the jury in determining the diminution in the plaintiff's earning capacity. The other case was Morrow v. Greyhound Lines, Inc., 541 F.2d 713 (8th Cir. 1976), in which an award based on expert testimony on inflation was affirmed because the appellant failed to make any objection on that ground to the admissibility of the testimony at the trial court.

[76] 521 F.2d 63 (9th Cir. 1975).

ty."[77] The court concluded on a cautionary note, making it clear that juries could not use inflation as an excuse not to reduce an award to present value. Furthermore, the court added that consideration of inflation was proper only where sound and substantial economic evidence is offered to support any estimates on the future purchasing power of the dollar.[78]

The court put what had been dicta into practice in *Burlington Northern, Inc. v. Boxberger*,[79] although no reference was made to the prior decision. The court held that it was within the trial court's discretion to determine whether the expert's sources of information were sufficiently reliable to warrant reception of the opinion and that under the circumstances presently before the court, the expert's testimony clearly did not reach the level of the "rampant speculation" they had condemned in previous decisions.[80] The court also noted that the asserted defects in the expert's assumptions were questions for the jury, and the defendant had been protected by competent cross-examination.

*10. Tenth Circuit.*—The Tenth Circuit, in perhaps one of the most complete reviews of recent cases dealing with the questions under discussion, adopted the position of the Ninth Circuit, permitting evidence of inflationary and productivity factors to be admitted

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[77]*Id.* at 75.

[78]The court specifically stated:

> By today's holding that the trier of facts in awarding damages may take into consideration estimated changes in the purchasing power of money, we do not mean to imply that the lower court may use our holding as an excuse not to discount an award to its net present value. In other words, the court may not assume that the discount rate and the inflation rate will net to zero. The lower court must first estimate future income and expenses, taking into account estimated changes in the purchasing power of the dollar, and then discount this future net income stream to its present value. Nor do we intend to have our holding of today read as authorizing the court to arbitrarily draw an estimate of inflation out of thin air. As with any other element of damages, we must require the estimate of future inflation to be supported by competent evidence. The court is to be especially wary of the pitfalls signposted by the court in *Bach*, which are inherent in making predictions about the future of economic conditions. By our holding we allow the trier of fact in awarding damages to take into account only such estimates of future changes in the purchasing power of money as are based on sound and substantial economic evidence, and can be postulated with some reliability.

*Id.* at 75-76 (citations omitted).

[79]529 F.2d 284 (9th Cir. 1975). *Boxberger* was an FELA case arising under Oregon law in which the plaintiffs had computed lost future earnings based on the assumption that a 4.8% compound annual increase in railroad employee's earnings over the next 34 years would occur. The expert's estimate was based upon government data on the average earnings of railroad engineers.

[80]*Id.* at 287.

upon the laying of a proper foundation.[81] In *Steckler v. United States*,[82] an action brought under the Federal Torts Claim Act, the trial court had heard testimony by plaintiff's economist as to a future inflationary factor of 9.5%.[83] Nevertheless, the court rejected the plaintiff's contention that there should be an increase in the award based on the anticipated inflation, concluding that an award reflecting the effect of inflation on future earning capacity would be improper as too speculative. The court of appeals, while noting that the lower court was justified in rejecting the 9.5% inflation factor, stated that it was not justified in altogether rejecting the evidence of an infaltionary trend. Although the court acknowledged that the majority of courts do require a reduction to present value in calculating damages for future benefits lost and at the same time do not allow the effects of inflation on future benefits to be considered, the court stated that this position was inconsistent and often criticized. The court reviewed the various recent decisions and concluded that it would follow the approach of the Ninth Circuit.[84] Thus, the Tenth Circuit will consider evidence of inflationary trends in conjunction with the problem of discounting the ultimate inflated sum so as to reduce it to its present value.

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[81]However, in a decision from a district court in the Tenth Circuit, DeWeese v. United States, 419 F. Supp. 170 (D. Colo. 1976), which was rendered before the Fourth Circuit had an opportunity to consider the issue, Judge Winner presented one of the strongest and most vehement arguments against the use of an inflationary factor in the computation of lost future earnings. Judge Winner stated that he was unconvinced anyone could foretell economic conditions 45 years down the road, noting the 45 years ago the United States was at the bottom of the Great Depression, that in 1931 a transcontinental telephone call cost about $20 and one could mail 4,000 letters for the same amount, whereas today such a call could be made for $1.50, but only 155 letters could be mailed for $20. After acknowledging that much of the uncertainty in this area was the result of cases confusing inflation and reasonable job progression he concluded:

> The divergent views create a quagmire . . . I think that inflationary trends and predictions espoused by "econometrists" testifying as advocates have no place in a lawsuit. The award of damages in a wrongful death or personal injury case is an approximation at best, and testimony confidently predicting economic conditions many years in the future is more likely to be wide of the mark than it is to approximate justice. Of course, the long range price trend has been on the upside historically, but where it is going in the future is anyone's guess.

*Id.* at 174-75.

[82]549 F.2d 1372 (10th Cir. 1977).

[83]The 9.5% factor did not include any factor for proficiency increases or promotions.

[84]In remanding, the court indicated that the trial court should determine a reasonable annual percentage rate for computing probable wage inflation from the evidence, suggesting that the Bureau of Labor Statistics Reports would be a reliable rough guide for the trial court's consideration of a reasonable inflation rate.

### *D. State Courts*

*1. State Courts Not Allowing Consideration of Economic Trends.*—The state courts that have addressed the question of the admissibility of expert testimony dealing with inflationary and productivity factors in computing future lost earnings have more readily accepted such testimony than the federal courts. Perhaps the most often cited state decision disallowing such testimony is *Raines v. New York Central Railroad.*[85] The court in *Raines* had allowed the plaintiff's expert to testify to the jury as to past economic trends, describing inflation, the increase in prices and wages, and the devaluation of the purchasing power of the dollar. On direct examination, the expert witness also testified that in his opinion the inflationary spiral would continue to affect the price level by approximately two to four percent. The plaintiff argued on appeal that such testimony was permissible based on previous Illinois decisions that held that a reviewing court would take judicial notice of the decline in purchasing power of money in considering an issue of excessive damages. The appellate court rejected this argument on the grounds these cases were easily distinguishable and did not justify permitting a jury to consider the effect of possible future inflationary trends. However, the Illinois Supreme Court later reversed the appeallate court decision, stating that before evidence of future inflationary trends may even by considered as erroneous, the reviewing court must determine that the verdict is not supported by other evidence.[86] Thus, the Illinois Supreme Court, without reaching the propriety of the admission of evidence concerning inflation, held that there was other proper evidence sufficient to support the verdict.[87]

One other recent case representative of state court decisions finding error in admitting evidence of inflationary or productivity factors is *Havens v. Tonner.*[88] The plaintiff's expert in the lower court had computed the plaintiff's lost future earnings based on a 3.5% "productivity factor." In reversing the judgment the court stated:

> Steadily rising wage rates over the next twenty years, whatever the cause, are simply one face of the coin of inflation. It may be that inflation will become so much an established pattern of our economy that it should be recognized in estimating loss of future earnings. Certainly,

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[85]129 Ill. App. 2d 294, 263 N.E.2d 895 (1970), *rev'd*, 51 Ill. 2d 428, 283 N.E.2d 230 (1972).

[86]51 Ill. 2d 428, 283 N.E.2d 230, *cert. denied*, 409 U.S. 903 (1972).

[87]*See also* Kapeladi v. Alton & S. R.R., 36 Ill. App. 3d 37, 343 N.E.2d 207 (1976).

[88]243 Pa. Super. Ct. 371, 365 A.2d 1271 (1976).

> the erratic behavior of the economy over the past half dozen years, plagued by war and other unusual circumstances, is not a sufficient demonstration that inflation at any predictable rate will continue for another twenty years. Furthermore, even if inflation is a part of the pattern of the future, one certain consequence is that interest rates on money will reflect that fact. Consequently, a sum representing the present worth of future earnings will earn more in dollars in an inflationary period than would otherwise be the case. This may not wholly compensate for the effect of inflation but it is a closer and more certain approximation than any assumption of a certain rate of inflation over the next twenty years. We view the "productivity factor" as simply a substitute for inflation and equally speculative and inadmissible in a calculation of future earnings.[89]

Other recent state cases prohibiting testimony of future inflationary trends follow basically the same reasoning.[90]

*2. State Courts Allowing Consideration of Economic Trends.* — A somewhat novel approach among these states taking into consideration the effect of inflationary and productivity factors is *Beaulieu v. Elliott*[91] in which the Alaska Supreme Court held the rate of depreciation in the value of the dollar, attributable to ongoing inflation, approximately offsets the financial windfall otherwise attributable to a failure to discount to present value. The court suggested that such procedure was also justified by possible future wage increases.[92]

Federal courts and other state courts allowing evidence of future inflationary trends follow basically the same line of reasoning.[93] There have also been a number of state courts specifically ap-

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[89] *Id.* at 378, 365 A.2d at 1274.

[90] *See* Freeman v. Lanning Corp., 61 Mich. App. 527, 233 N.W.2d 68 (1975); Mississippi Power & Light Co. v. Shepard, 285 So. 2d 725 (Miss. 1973); Atwood v. Lever, 274 So. 2d 146 (Miss. 1973); Segebart v. Gregory, 160 Neb. 64, 69 N.W.2d 315 (1955). *But see* Hampton v. State Highway Comm'n, 209 Kan. 565, 498 P.2d 236 (1972); Washington v. American Community Stores Corp., 196 Neb. 624, 244 N.W.2d 286 (1976); Zaninovich v. American Airlines, Inc., 26 App. Div. 2d 155, 271 N.Y.S.2d 866 (1966).

[91] 434 P.2d 665 (Alaska 1967).

[92] *See also* State v. Guinn, 555 P.2d 530 (Alaska 1976).

[93] *See* Loetzerich v. Texas Pac.-Mo. Pac. Terminal R.R., 325 So. 2d 626 (La. Ct. App. 1976); Morgan v. Liberty Mutual Ins. Co., 323 So. 2d 855 (La. Ct. App. 1975); Lumber Terminals, Inc. v. Nowakowski, 36 Md. App. 82, 373 A.2d 282 (1977) (excellent discussion of recent state decisions); Rafferty v. Weimer 36 Md. App. 98, 373 A.2d 64 (1977); Tenore v. Nu Car Carriers, Inc., 67 N.J. 466, 341 A.2d 613 (1975); Williams v. General Motors Corp., 501 S.W.2d 930 (Tex. Ct. App. 1973); Hinzman v. Palmanteer, 81

proving the introduction of expert testimony on both increased future inflation and productivity.[94]

## II. Income Taxes

### *A. Introduction*

Awards received by settlement or verdict in death actions or personal injury actions are not taxable under the federal income tax laws.[95] This has led to controversy in almost every state and federal court as to the proper consideration to be given taxes in computing damage awards. Professors Harper and James have noted: "With anything as sure as 'death and taxes,' the courts are avoiding their responsibilities when they decline to make the best guess they can, once all the reasonably available evidence has been brought before them."[96] The majority of legal commentators clearly advocate that evidence of the amount of federal income tax that a plaintiff would pay on probable future earnings should be taken into account in computing the damage award.[97] However, the majority view of the courts has been that it is reversible error even to inform a jury that a plaintiff's award is not taxable. Consequently, very few courts have allowed the portion of the award representing compensation for loss of future earnings to be reduced by an amount the plaintiff would have been required to pay as income taxes had the plaintiff received that sum is income over the future years.

The propriety of instructing the jury that any awards made to the plaintiff will not be subject to federal income tax (based on the idea that such an instruction is to prevent a jury from adding to an award an amount it erroneously believes the plaintiff will be called upon to pay for income taxes) is a distinct and separate issue from that of whether evidence of the impact of such taxes may be shown to reduce the amount of the award. However, these two issues are often raised in the same case, and occassionally the courts will erroneously fail to distinguish them.[98] Therefore, these two issues will

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Wash. 2d 327, 501 P.2d 1228 (1972) (but see strong dissent against award of loss of value of future earnings capacity); Sadler v. Wagner, 5 Wash. App. 77, 486 P.2d 330 (1971).

[94]*See* Schnebly v. Baker, 217 N.W.2d 708 (Iowa 1974); Coco v. Winston Indus., Inc., 341 So. 2d 332 (La. 1976); Resner v. Northern Pac. Ry., 161 Mont. 177, 505 P.2d 86 (1973) (but see dissent); Turrietta v. Wyche, 54 N.M. 5, 212 P.2d 1041 (1949); Wilson v. Wylie, 86 N.M. 9, 518 P.2d 1213 (Ct. App. 1974); Ploud v. Southern Pac. Transp. Co., 266 Or. 666, 513 P.2d 1140 (1973), *aff'd on rehearing*, 272 Or. 35, 534 P.2d 965 (1975).

[95]I.R.C. § 104(a)(2).

[96]Harper & James, *supra* note 2, § 25.12 at 1327.

[97]*See, e.g.*, Harper & James, *supra* note 2, § 25.12 at 1326-27; Morris & Nordstrom, *Personal Injury Recovery and the Federal Income Taxes Law*, 46 ABA J. 274 (1960).

[98]*See, e.g.*, Highshew v. Kushto, 235 Ind. 505, 134 N.E.2d 555 (1956).

be treated together in this Note. Some cases have distinguished or limited the application of their opinions on the tax issues to wrongful death cases, while others have spoken in general terms that apply to both personal injury actions and wrongful death actions.

### *B. Indiana*

The law in Indiana on both issues dealing with the nontaxability of awards is as uncertain and confusing as it is on the questions of the use of inflationary and productivity factors. In *Highshew v. Kushto*,[99] the court of appeals reviewed a judgment for the plaintiff in a personal injury case in which the trial court had refused to give cautionary instruction concerning the non-taxability of the award:

> If given, the cautionary instruction would have informed the jury that in the event they found for the plaintiff any award made to him would not be subject to federal income taxes. *Such an instruction has been approved by the courts of Missouri, and we can find no reason for the disapproval of the one here involved.* It is obvious, however, that a refusal to give the instruction could only result in an excessive verdict due to the jury's desire to make the appellee whole after taxes. *The verdict in this case is not excessive and we are constrained to conclude that any error involved in the refusal to give instruction in question was harmless.*[100]

However, the Indiana Supreme Court, in denying a petition to transfer,[101] expressly disapproved the language emphasized in the above quotation. The court concluded that cautionary instructions such as those suggested by the court of appeals would raise collateral issues and require intricate instructions on tax and non-tax liabilities. As a result, no court would be able to properly instruct a jury without a tax expert at its side.[102]

The Indiana Supreme Court's decision in *Highshew* has been cited by a number of other courts as an example of an opinion that fails to recognize the distinction between the evidentiary issues concerning the consideration of the income tax impact on awards and the question of the propriety of a cautionary instruction concerning the non-taxability of the award.[103] A recent Indiana Court of Appeals

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[99]126 Ind. App. 584, 131 N.E.2d 652, *transfer denied*, 235 Ind. 505, 134 N.E.2d 555 (1956).

[100]134 Ind. App. at 596, 131 N.E.2d at 657 (citations omitted) (emphasis added).

[101]235 Ind. 505, 134 N.E.2d 555 (1956).

[102]*See also* Richmond Gas Corp. v. Reeves, 158 Ind. App. 338, 302 N.E.2d 795 (1973).

[103]*See, e.g.*, Domeracki v. Humble Oil Ref. Co., 443 F.2d 1245 (3d Cir. 1971).

decision diplomatically recognized this failure when it affirmed a lower court award where a cautionary instruction had been given. While recognizing that under the *Highshew* opinion it was improper to give such an instruction, the court stated:

> Clearly, an instruction regarding the income tax consequences of an award of damages can have two meanings. . . . They were not entitled to an inflated award based upon the jury's mistaken belief that a portion of the verdict would be used to pay taxes on the amount recovered. The instruction given, in conjunction with the other instructions, merely served to caution the jury to base its award on the evidence, and not on speculation about tax consequences.[104]

From the language of the above cases it would appear Indiana would hold that any evidence of the impact of income taxes on future earnings was inadmissible. However, such language is arguably dicta since it was raised in an opinion concerning the propriety of a cautionary instruction. Likewise, the opinion indicates no cautionary instruction would be allowed, although the recent court of appeals decision implies that such an instruction might be allowed if the court properly distinguishes the two issues.

### *C. Federal Courts*

*1. First Circuit.*—While the case law is not entirely clear, the First Circuit appears to permit the jury to consider the impact of taxes in those cases where future inflationary trends are considered. Furthermore, the First Circuit has held that it is not error to refuse to give a cautionary instruction on the non-taxability of the award, unless there is some indication in the record that the jury award was based on the assumption the award was taxable.

The question of whether evidence of future income taxes should be admitted first arose in *Boston & Maine Railroad v. Talbert.*[105] In the case, the court of appeals excluded the evidence, citing a Second Circuit decision[106] that had held such deductions to be too conjectural. However, in a recent decision under Rhode Island law, which expressly authorizes the consideration of inflation and other economic trends, the court concluded that whatever savings accrued to the plaintiff by excluding evidence on the "taxation bite" would be increased by the inflation multiplier.[107] As a result, the court of

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[104]Wickizer v. Medley, 348 N.E.2d 96, 99-100 (Ind. Ct. App. 1976).

[105]360 F.2d 286 (1st Cir. 1966).

[106]Stokes v. United States, 144 F.2d 82 (2d Cir. 1944). *See* discussion in text accompanying notes 117-18, *infra.*

[107]Turcotte v. Ford Motor Co., 494 F.2d 173 (1st Cir. 1974).

appeals reversed the trial court's decision that failed to make reductions in projected earnings for federal and state income taxes.[108] The court pointed out that the forecasting of future inflationary rates was clearly more speculative than the forecasting of future tax rates, and it would thus be logically inconsistent to require considerations of future inflation while at the same time disallowing evidence as to tax savings on the grounds that it was too speculative to compute future tax rates.[108]

In its most recent decision on the evidentiary issue, *Kennett v. Delta Airlines, Inc.*,[109] the First Circuit quoted extensively from both the majority and dissenting opinions in a leading Second Circuit decision.[110] The court indicated that it favored the dissenting opinion's argument that such evidence should be considered, but refused to apply that rule in the case under consideration because no evidence as to future taxes had been submitted at the trial court level.[111] In *Kennett*, the First Circuit also discussed the propriety of an instruction cautioning the jury that the award was not taxable and upheld the trial court's refusal to give such an instruction. The court recognized that this was a proper statement of the law, but argued it would inject an "irrelevant" factor in the jury's determination of damages. However, the court did note that it would be error not to give the instruction if it could be demonstrated from the record that the jury assumed the award was taxable.[112]

*2. Second Circuit.*—The Second Circuit has upheld a trial court's refusal to give a cautionary instruction where there was no evidence that this affected the jury's award and has suggested that in certain circumstances the jury may properly consider the tax consequences on future earnings. Both issues were raised in *McWeeney v. New York, New Haven & Hartford Railroad*,[113] one of the most frequently cited opinions in this area of the law. In *McWeeney*, the defendant requested both a cautionary instruction regarding the

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[108]*Id.* at 184-86. *But cf.* Caron v. United States, 410 F. Supp. 378 (D.R.I. 1976) (personal injury case decided under Michigan law in which the court held a recent Michigan decision foreclosed any argument as to the propriety of taking into consideration the impact of income taxes on a personal injury award).

[109]560 F.2d 456 (1st Cir. 1977).

[110]McWeeney v. New York, N.H. & H. R.R., 282 F.2d 34, 35-43 (2d Cir.), *cert. denied*, 364 U.S. 870 (1960).

[111]560 F.2d at 463-64.

[112]*Id.* at 461-62. Such a statement by the court seemed inconsistent with the record, which indicated a strong likelihood that the jury did assume the award was taxable, as the jury specifically asked the trial court whether they should consider income tax deductions in computing future lost earnings and the court informed them they should not consider them. The logical conclusion from such an exchange would appear to be that such an award is taxable. *But see id.* at 462 n.7.

[113]282 F.2d 34 (2d Cir.), *cert. denied*, 364 U.S. 870 (1960).

non-taxability of the award and an instruction directing the jury to calculate any future loss of earnings on the basis of the plaintiff's net income after deduction of income taxes. The court of appeals affirmed the denial of both requests by the trial court.

The court first discussed the instruction concerning the deduction of taxes and held that the impact of income tax liability should not be considered in computing the damage award because it would prove too difficult for the jury. "Practical difficulties," such as disputes over possible future exemptions resulting from marriage and newly born children, as well as tax shelters, would make any result merely speculative.[114]

The court also noted that if consideration of such a factor were allowed, there would be an additional problem resulting from the fact that lost future earnings awards are discounted to present value to account for the earning power of money. Since interest so computed would be taxable, another adjustment would have to be made in the award to add back in the taxes that would be paid on such interest.[115]

Arguing in support of the instruction, the defendant contended that regardless of how difficult the computation would be, the worst result from giving such an instruction would be better than the best result from not giving one. The court rejected the defendant's contention based on three justifications. First, it would be too conjectural to determine future tax liability in light of such factors as changes in the family status of the injured party in years to come, possible changes in the exemption and deduction provisions of the tax law, possible changes in the rates of taxation, and so forth. Second, the use of a net income theory would be too complex and confusing for the jury. And finally, other factors not considered in the computation, such as inflation and attorneys fees, would tend to counter-balance any resulting overcompensation.[116]

The court did, however, modify its position taken earlier in *Stokes v. United States*.[117] *Stokes* is often cited for the proposition that the amount of federal income taxes is too conjectural to be considered by a jury. In *Stokes*, the court made no analysis of the question, but was content to settle the problem by merely stating that "such deductions are too conjectural."[118] In *McWeeney*, the court noted that in cases involving computation of income in higher tax brackets, where added exemptions or deductions do not greatly af-

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[114]*Id.* at 36.
[115]*Id.* at 37.
[116]*Id.* at 38.
[117]144 F.2d 82 (2d Cir. 1944).
[118]*Id.* at 87.

fect the tax, 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. The court stated:

> In such cases . . . the criticism that the whole process of computation is unrealistic has a considerable measure of validity, the projection of future income at such levels being itself extremely conjectural, and the slope of the tax progression curve declines although only after having reached such a high plateau that earnings above it have relatively slight value.[119]

Concluding its discussion of the issue by acknowledging that the practice of refusing the instructions in some cases, but requiring adjustments in others, lacked precision and elegance, the court nevertheless left the decision to the trial judge.[120]

The *McWeeney* court then discussed the refusal of the trial court to caution the jury as to the non-taxability of the award. The court concluded there would be no error in giving such an instruction as it was a correct statement of the law that imposed no new burdens on the jury and did not require the jury to engage in speculation. Nevertheless, the court held it was not reversible error to refuse to give the instruction, stating: "Before an appellate court should hold that the failure to give such a cautionary instruction was reversible error, there ought to be evidence either that juries in general increase recoveries on this account or that the particular jury did so."[121]

Chief Judge Lumbard wrote an excellent dissent discussing both issues. Concerning the cautionary instruction, Lumbard argued it was the duty of the courts to "charge upon those matters regarding which misinformation by any one juror might lead the jury to give improper weight to a factor which should not be considered at all."[122] Taking judicial notice that media coverage of large sums won on television or in lotteries often pointed out that a large percentage of the winnings must be paid to the government as income tax, Lumbard reasoned that it would only be natural for the layman to conclude that the plaintiff's receipts from the judgment would be taxed.

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[119]282 F.2d at 38-39.

[120]*See also* Blake v. Delaware & H. Ry., 484 F.2d 204 (2d Cir. 1973). *But see* J. Lumbard's dissent, *id.* at 207-08, advocating a re-examination of *McWeeney*. *See also* Petition of Marina Mercante Nicaraguense, S.A., 364 F.2d 118 (2d Cir.), *cert. denied*, 385 U.S. 1005 (1966); Leroy v. Sabena Belgian World Airlines, 344 F.2d 266 (2d Cir.), *cert. denied*, 382 U.S. 878 (1965) (applying *McWeeney* exception to a geologist with an anticipated income of between $16,000 and $25,000).

[121]282 F.2d at 39.

[122]*Id.* at 40 (Lumbard, C.J., dissenting).

This danger, combined with the fact that such a request requires no calculation or computation and is simple and easily understood, led Lumbard to conclude that refusal to grant such a request was reversible error.

Lumbard further concluded that an instruction to consider tax savings should be granted if the defendant produces some evidence as to what the plaintiff actually paid in the past or as to what taxes would normally be paid by someone in the plaintiff's position. He claimed the majority greatly overestimated the difficulties that the jury would encounter in making such a computation. Furthermore, Lumbard rejected the majority's contention that such a factor was too speculative, pointing out that all items of damages listed by the majority (future normal earning power, expectancy and discount factor) were sheer speculation as to any plaintiff. Nevertheless, it would be unfair to omit any one of them merely because they were speculative. Lumbard noted that "on the facts of this case one thing is certain and that is that McWeeney never has escaped and never could expect to escape the payment of income taxes on any money which he has earned or would earn in the future" and that "[n]othing can be more certain than that there will be a federal income tax in the years to come and that it will be substantially what it is now and what it has been for many years."[123] Lumbard concluded that given the fact that a minimum of fifteen to twenty percent of an individual's gross income is generally paid on taxes it seemed unfair to deny an instruction as to future income taxes when such an instruction is requested and the record contains evidence as to taxes.[124]

*3. Third Circuit.*—The Third Circuit will allow a cautionary instruction when requested, but it will prohibit the introduction of evidence concerning possible future income taxes to reduce the award. The court of appeals in *Domeracki v. Humble Oil & Refining Co.*[125] noted that evidence of income taxation was to be excluded, but held that in personal injury actions the trial court must, upon request by counsel, give a proper cautionary instruction. The court stated that the purpose of personal injury compensation is neither to reward the plaintiff nor punish the defendant but to replace the plaintiff's losses resulting from the injury. An injured plaintiff loses

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[123]*Id.* at 41-42.

[124]For an earlier decision decided under Oklahoma law that supports Lumbard's dissent see O'Connor v. United States, 269 F.2d 578 (2d Cir. 1959). *See also* Perry v. Allegheny Airlines Inc., 489 F.2d 1349 (2d Cir. 1974); Feldman v. Allegheny Airlines, Inc., 382 F. Supp. 1271 (D. Conn. 1974), *aff'd in part, rev'd & remanded on other grounds*, 524 F.2d 384 (2d Cir. 1975).

[125]443 F.2d 1245 (3d Cir. 1971).

only his net or take-home pay and does not in fact "lose" his gross earnings. While acknowledging that legal commentators generally advocate the admissibility of such evidence, the court suggested that "shifting tax rates, together with other variables, could give rise to great conjecture, at least as to *en futuro* earnings. Indeed, the tax computation itself could completely overshadow the basic issues of liability and damages."[126] Thus, while realizing that such a practice may result in the plaintiff being overcompensated, the court chose to follow the majority of jurisdictions in allowing evidence only of gross earnings.[127]

In discussing the second issue concerning instructions on the taxability of the award, the court noted that while some courts have confused the evidentiary issue with the question of a cautionary instruction,[128] the issues are distinct. The court pointed out that the cautionary instruction did not require additional evidence or a tax expert and would not open the trial to matters irrelevant to traditional issues in personal injury litigation. Thus, it would in no way complicate the case or confuse the jury. The court concluded that the "tax conscious" American juror might well believe that the judgment would be taxable and would increase the verdict to compensate for the imaginary tax. Therefore, the court required the use of a cautionary instruction in the future if it is requested by counsel.[129]

A district court in a recent case, *Huddell v. Levin*,[130] discussed the evidentiary issue at length and considered many of the objections that have been raised regarding evidence offered on future taxes. The court rejected this evidence on several grounds. First, the court indicated that the majority of courts clearly prohibited this type of evidence.

> In all but one state, the gross earnings rule is followed. In twenty-eight states, the question has been specifically considered. In twenty-seven of those states, the courts have ruled either that income tax consequences cannot be considered, or have accepted the majority rule that cautionary instructions should not be given concerning the nontaxability of the award. Nor is there any case decided under

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[126]*Id.* at 1250.

[127]It should be noted that such language was dicta, as the issue before the court was the refusal of the trial court to grant the requested cautionary instruction.

[128]The court cited Highshew v. Kushto, 235 Ind. 505, 134 N.E.2d 555 (1966), as an example of a case confusing the two issues. *See* text accompanying notes 101-03 *supra*.

[129]*See also* Vizzini v. Ford Motor Co., 72 F.R.D. 132 (E.D. Pa. 1976), *remanded on other grounds*, 569 F.2d 754 (3d Cir. 1977).

[130]395 F. Supp. 64 (D.N.J. 1975), *rev'd on other grounds*, 537 F.2d 726 (3d Cir. 1976).

> "federal" law where the jury's consideration of income tax consequences has been permitted. In non-jury cases decided under "federal" law, there appears to be only two exceptions to the majority rule. The only area where authority is evenly divided is Federal Tort Claims Act cases, where the United States as defendant is also the benefactor of the exemption.[131]

Second, the *Huddell* court viewed the exemption for such awards found in the tax laws as an expression by Congress of a desire to give a benefit to victims of tortious conduct. The court recognized that such awards may have initially been excluded because of constitutional reservations as to their taxability, but subsequent cases have established that Congress can constitutionally tax any gain.[132] Since Congress re-enacted the exemption after these decisions, the court argued that this indicated that Congress "intended to relieve a taxpayer who has the misfortune to become ill or injured."[133]

The court's third rationale was that the "collateral source" doctrine found in the law of evidence[134] prohibited consideration of the intended benefit of the Congressional exemption, as "the incidence of federal taxation on personal injury awards is a matter solely between plaintiff and the Government."[135] The court therefore conclud-

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[131]*Id.* at 85-86 (footnotes omitted). It should be noted that this quote fails to include those cases that have allowed the consideration of taxes under the *McWeeney* Rule, nor does it note several decisions which state that the evidentiary issue of taxes is not affected by whether the case is before a jury or judge. *See* Mosley v. United States, 538 F.2d 555 (4th Cir. 1976); McWeeney v. New York, N.H. & H. R.R., 282 F.2d 34 (2d Cir. 1960) (Lumbard, C.J., dissenting).

[132]*See, e.g.*, Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955).

[133]395 F. Supp. at 87 (quoting Epmeier v. United States, 199 F.2d 508, 511 (7th Cir. 1952)). Professor Nordstrom has strongly attacked this argument, stating that the Congressional intent argument is merely an example of attributing a non-existent intent to a legislative act after the fact. In support of this view, he pointed out that such provision did not appear in our tax laws until 1918, and when it did so its purpose was not to benefit injured parties but rather it appeared because Congress thought it was doubtful that tort damages were income within the meaning of the Sixteenth Amendment. Nordstrom, *Income Taxes and Personal Injury Awards*, 19 OHIO ST. L.J. 212 (1958). Nordstrom does not meet the argument raised in *Huddell* that re-enactment of the exclusion after the rulings resolving the doubt as to whether tort damages were income indicates a Congressional intent to benefit the injured party; nor does *Huddell* show any indication of such an intent.

[134]Under the "collateral source rule," the defendant is not entitled to obtain the benefit of payments that have come from a collateral source, that is, a source that is collateral to, or independent of, the defendant. *See, e.g.*, Weiman v. Ippolito, 129 N.J. Super. 578, 324 A.2d 582 (1974).

[135]395 F. Supp. at 88. Professor Nordstrom likewise points out the fallacy of this argument and states that, while it is correct that what a plaintiff does with an award

ed that the jury should be concerned only with plaintiff's total losses and not with what might have happened to those earnings had he not been injured. The court thereafter merely reiterated the arguments raised in *McWeeney*.

In a recent personal injury action, *Varlack v. SWC Caribbean, Inc.*,[136] the Third Circuit rejected the argument that evidence of taxes on future earnings should be admitted, but failed to make any reference to the district court's argument in *Huddell*. Instead, the court relied on the rationale found in *McWeeney* that such evidence would be too complex and conjectural.

*4. Fourth Circuit.*—The Fourth Circuit has permitted the use of evidence on income taxes in computing damages in wrongful death cases but has not otherwise addressed the issues under consideration. However, the district courts of the circuit have applied the *McWeeney* Rule to the evidentiary issue in personal injury cases and have permitted cautionary instructions in both types of actions.

In *Mosley v. United States*,[137] a wrongful death action governed by North Carolina law, the court of appeals held that evidence of income taxes would be permitted. While noting that the issue had not been directly addressed by the North Carolina Supreme Court or by the court of appeals itself, the Fourth Circuit stated: "[W]e are of the opinion that income taxes are proper deductions in order to arrive at the 'pecuniary injury' retrievable by the estate."[138] This case is one of the few decisions which made a clear distinction between the admissibility of such evidence in wrongful death actions and its admissibility in personal injury cases. The court adopted the rationale previously expressed by the district court in *Brooks v. United States*,[139] which rejected the contention that evidence of future tax impact was too speculative in wrongful death cases. While acknowledging that changes in tax deductions (such as increases in dependents) may make it impossible to arrive at a fair calculation of future tax in personal injury cases, the court suggested that such arguments have little relevance in wrongful death actions. Both *Brooks* and *Mosley* were non-jury cases, but the courts

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after receipt is of no concern to the court, it is not correct to assume that the plaintiff's award is an accurate measure of his loss. His true loss is, rather, his net income. Nordstrom, *supra* note 133. The Second Circuit in Perry v. Allegheny Airlines, Inc., 489 F.2d 1349 (2d Cir. 1974), also rejected the argument that the collateral source rule barred such evidence, noting that the admissibility of evidence regarding income taxes does not present the general equitable considerations underlying the collateral source rule.

[136] 550 F.2d 171 (3d Cir. 1977).

[137] 538 F.2d 555 (4th Cir. 1976).

[138] *Id.* at 558-59 (footnote omitted).

[139] 273 F. Supp. 619 (D.S.C. 1967).

indicated that even a jury could deal with the complexities and confusion involved in admitting such evidence.

In *Plant v. Simmons Co.*,[140] decided before *Mosley*, the district court adopted the *McWeeney* Rule and prohibited the introduction of tax evidence. This approach has been modified by the Fourth Circuit's opinion in *Mosley* with respect to wrongful death actions. However, this will most likely be the rule in this circuit as to personal injury actions. *Plant* also recognized in dicta that a cautionary instruction should be given when requested by either side.[141]

*5. Fifth Circuit.*—The Fifth Circuit has also adopted the *McWeeney* Rule on the evidentiary issue but has chosen not to allow a cautionary instruction. There does appear to be, however, a substantial dissenting minority on both positions.

In *Blue v. Western Railway*,[142] the court of appeals addressed the evidentiary issue in some depth. In *Blue*, the plaintiff claimed the trial court had committed error by instructing the jury to consider and compute only the amount of net wages lost as a result of the injury. The court of appeals acknowledged that the rationale of those courts prohibiting the use of evidence of future taxation had been severely criticized by Harper and James.[143] Furthermore, the court indicated that such evidence was no more speculative than many of the other items that go into prophecies about future losses. Nevertheless, the court held that evidence of future taxes should not be allowed except under certain circumstances, quoting the *McWeeney* decision in its entirety for support. The court concluded that the rule enunciated in *McWeeney* was sound and in harmony with their prior decisions.[144]

On the related question of the propriety of a cautionary instruction, the court noted it had already held in prior decisions that it was proper for the trial court to refuse such an instruction.[145] However, none of the Fifth Circuit decisions discuss the rationale of these holdings.

The majority's position on both the evidentiary question and the cautionary instruction has provoked substantial disagreement. In its most recent decision, *Johnson v. Penrod Drilling Co.*,[146] the majority

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[140]321 F. Supp. 735 (D. Md. 1970).

[141]*Id.* at 740.

[142]469 F.2d 487 (5th Cir. 1972).

[143]*See* note 96 *supra* and accompanying text.

[144]The court in *Blue* also distinguished a prior decision, Hartz v. United States, 415 F.2d 259 (5th Cir. 1969), which had allowed future taxes to be considered on the grounds that *Hartz* was a non-jury death action brought under the FTCA. Therefore, *Hartz* was a suit between an individual and the government, which legislated the tax break, as opposed to a personal injury action between private parties.

[145]*See, e.g.*, Greco v. Seaboard Coast Line R.R., 464 F.2d 496 (5th Cir. 1972).

[146]510 F.2d 234 (5th Cir.), *cert. denied*, 423 U.S. 839 (1975).

of the Fifth Circuit, en banc, adhered to the *McWeeney* Rule. Three of the judges dissented on the income tax issue, noting that by following *McWeeney* the court would "open to [the jurors] the gates of fairyland and direct them to arrive at a take-home earnings figure . . . which never was and never would have been. This . . . is not logic and should not be law."[147] The dissent further criticized the majority's practice of not allowing an instruction to the jury concerning the non-taxability of the award, noting that such a practice could result in a double windfall for the plaintiff, first by allowing him to receive an award based on gross earnings, and second, by allowing a mistaken jury to add a factor which would never in fact have to be paid.

*6. Sixth Circuit.*—The Sixth Circuit has taken a position similar to the Fourth Circuit. It has adopted the *McWeeney* Rule on the evidentiary issue and requires that requested cautionary instructions be given. In *Petition of the United States Steel Corp.*,[148] a proceeding involving claims for the death of seamen and injuries to others under maritime law, the court of appeals rejected any consideration of the impact of income taxes on the computation of lost future earnings as too speculative, and stated: "[W]e therefore adopt the [*McWeeney* Rule] that no adjustment for income tax need be made 'at the lower or middle reach of the income scale.' "[149]

Later, in *Bach v. Penn Central Transportation Co.*,[150] the court addressed the propriety of a cautionary instruction. The court recognized that in a number of previous cases it had held it was not reversible error to refuse to give such an instruction.[151] However, the court held it was within the trial court's discretion whether to give such an instruction or not, since such an instruction does not involve speculation or complicated calculations and merely gives the jurors an accurate statement of the tax law.[152]

*7. Seventh Circuit.*—While the Seventh Circuit has not addressed the issue concerning the propriety of a cautionary instruction, it appears to have adopted the *McWeeney* Rule on the evidentiary issue. In *Wetherbee v. Elgin, Joliet, & Eastern Railway*,[153] a death action brought under FELA, the defendant had appealed the

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[147]*Id.* at 242 (Gee, J., dissenting).

[148]436 F.2d 1256 (6th Cir. 1970).

[149]*Id.* at 1274 (quoting *McWeeney*, 282 F.2d at 39).

[150]502 F.2d 1117, 1122-23 (6th Cir. 1974).

[151]*See, e.g.*, Hageman v. Signal L.P. Gas, Inc., 486 F.2d 479 (6th Cir. 1973); Payne v. Baltimore & O. R.R., 309 F.2d 546 (6th Cir.), *cert. denied*, 374 U.S. 827 (1962).

[152]502 F.2d at 1123. *Cf.* Johnson v. Husky Indus. Inc., 536 F.2d 645, 650 (6th Cir. 1976) (different result under Tennessee law).

[153]191 F.2d 302 (7th Cir. 1951), *rehearing denied*, 204 F.2d 755, *cert. denied*, 346 U.S. 867 (1953).

trial court's decision on grounds that the award was excessive. The defendant contended that the actuary's computation was based on the false premise that the descendants' loss of future benefits could be computed on the decendent's probable future gross earnings rather than his probable contribution for support. The court of appeals, after noting that the actuary's computations had in fact been based on the decedent's average past gross earnings rather than his "take-home" pay, concluded that it was error to receive this testimony over the defendant's objections. This implies that the tax factor should be taken into account in computing lost future earnings.

The court apparently modified its position somewhat in *Cox v. Northwest Airlines, Inc.*,[154] a non-jury action under the Death on High Seas Act. The trial court failed to reduce the decedent's projected future earnings by future income taxes. The Seventh Circuit remanded the decision with directions to modify the damages, adopting the rationale of the Second Circuit in *Petition of Marina Mercante Nicaraguense, S.A.*[155] In *Marina Mercante*, the Second Circuit stated that the *McWeeney* Rule should be followed in all cases where the question is one of federal law or the applicable state law is silent. Thus, even though *Cox* was a non-jury wrongful death action, its adoption of the rationale of the Second Circuit position indicates that the Seventh Circuit would apply the *McWeeney* Rule in both personal injury and wrongful death cases and in both a jury or non-jury setting.

*8. Eighth Circuit.*—The Eighth Circuit has indicated it would not permit evidence of income taxes but that the court might allow a cautionary instruction. However, none of the Eighth Circuit decisions discuss either issue in depth. *Chicago & Northwestern Railway v. Curl*,[156] a personal injury action brought under FELA, appears to be the only Eighth Circuit decision dealing with the evidentiary issue on taxes. The court of appeals in *Curl* held that the trial court was correct in refusing to receive appellant's offer of proof of appellee's average net earnings after deductions. In affirming the decision, the court merely cited to *Stokes v. United States*[157] for support of the proposition that such evidence is too conjectural.

In a more recent decision, *Raycraft v. Duluth, Missabe & Iron Range Railway*,[158] another personal injury action brought under the

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[154]379 F.2d 893 (7th Cir.), *cert. denied*, 389 U.S. 1044 (1967).

[155]364 F.2d 118 (2d Cir.), *cert. denied*, 385 U.S. 1008, *rehearing denied*, 386 U.S. 929 (1966).

[156]178 F.2d 497 (8th Cir. 1949).

[157]144 F.2d 82, 87 (2d Cir. 1944).

[158]472 F.2d 27 (8th Cir. 1973).

FELA, the appellant argued that the trial court had erred in refusing to give a requested cautionary instruction concerning the non-taxability of the award. The court noted that the Eighth Circuit had not previously expressed an opinion on the subject and that the law on the issue was unsettled. The court specifically refused to resolve the issue, stating: "Even if this panel were to adopt the instruction, this panel would do so only prospectively."[159] The court did indicate in a footnote that it viewed the *Curl* opinion as having held that the evidence of tax computation affecting gross income was improper.[160]

9. *Ninth Circuit.*—Although the Ninth Circuit has officially adopted the *McWeeney* Rule on the evidentiary issue, it is clear from its discussion in its most recent decisions that it favors the admissibility of such evidence.[161] It has also taken the position that cautionary instructions concerning the non-taxability of awards should be allowed. A recent opinion dealing with both issues, *Burlington Northern, Inc. v. Boxberger*,[162] is representative of the Ninth Circuit's position. In *Boxberger*, the trial court had refused to allow evidence of income taxes and rejected the defendant's request for a cautionary instruction. After reviewing the *McWeeney* decision at length, the court of appeals stated that under the compensatory theory of damages the windfall that the survivors would receive in tax-free dollars could not be justified either in fairness or logic.

The court noted several fallacies regarding the objections raised in *McWeeney* against the admission of evidence of future tax impact. First, the court rejected the primary objection that such evidence is too speculative and uncertain on the grounds it was no more speculative than other evidence submitted to the jury. Second, *McWeeney* had suggested that the calculation of future tax liability would be too confusing for the jury. The Ninth Circuit noted that jurors had experience in determining their own tax liability and the court was "confident that our juries and judges, with the aid of such competent expert testimony as may be received, are equal to the task and the responsibility."[163]

Finally *McWeeney* argued that any unfairness to the defendant resulting from the refusal to admit evidence of future tax consequences was counter-balanced by the unfairness to the plaintiff in not admitting evidence of inflation and not compensating the plaintiff for his attorney's fees. This rationale was not applicable to the Ninth Circuit, which had held that testimony as to future inflation

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[159] *Id.* at 33.

[160] *Id.*

[161] *See* Burlington N., Inc. v. Boxberger, 529 F.2d 284 (9th Cir. 1975).

[162] *Id.* The court also indicated that any problem with speculativeness could be reduced by careful court supervision of evidence admitted and instructions to the jury.

[163] *Id.* at 293.

was to be taken into consideration.[164] Furthermore, as to attorney's fees, the court indicated that the impact of these fees has no relation to the jury's task of estimating damages, unlike inflation and taxation, which clearly would have occurred had the decedent lived.[165] After indicating that fairness and logic would require a rule providing for the admissibility of, and corresponding deduction to account for, future income taxes in all cases, the court nevertheless concluded that the adoption of such a broad rule would go against the weight of authority. Therefore, the Ninth Circuit adopted the flexible *McWeeney* Rule.[166]

Subsequent to *Boxberger*, the Ninth Circuit decided *Felder v. United States*,[167] a death action brought under the FTCA and controlled by Arizona law, in which the court added a somewhat novel rationale for requiring the consideration of income taxes. The court argued that the failure to deduct income taxes in computing lost future earnings would result in an award of punitive damages that is impermissible under the FTCA.[168]

The Ninth Circuit has taken the position that a cautionary instruction should be allowed when requested. The court indicated that when all factors were considered the balance was overwhelmingly in favor of giving such an instruction. The court simply noted that the instruction could do no harm, and it could certainly help by preventing the jury from inflating the award on the erroneous assumption that the judgment would be taxable.[169]

*10. Tenth Circuit.*—The Tenth Circuit has not considered either issue in depth. However, it has ruled that both the consideration of tax savings in the computation of lost future earnings[170] and

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[164]*See* United States v. English, 521 F.2d 63 (9th Cir. 1975).

[165]529 F.2d at 294. The court also distinguished the question of attorney's fees as follows: "Attorneys' fees are related to private contracts between the litigants and the attorneys. They have no legitimate relevancy as to what amount of money is justly compensatory for the loss resulting from the defendant's tortious act." *Id.*

[166]The court did hold, however, that under the *McWeeney* Rule taxes should have been considered in this case, which involved an income span of $18,048 to $40,000 in annual earnings. *Id.*

[167]543 F.2d 657 (9th Cir. 1976).

[168]*Id.* at 669. The court distinguished two prior holdings, McCauley v. United States, 470 F.2d 137 (9th Cir. 1972), and United States v. Becker, 378 F.2d 319 (9th Cir. 1967), in which it had affirmed awards that had not deducted projected income taxes on the basis that in those cases the punitive damage issue had not been raised. *Id.* at 670.

[169]Burlington N., Inc. v. Boxberger, 529 F.2d at 297. In balancing the factors to be considered, the court held that the danger that the jury would assume the award was taxable and increase damage award to compensate for taxes combined with the fact that the instruction was neither time consuming nor confusing clearly led to the conclusion such instruction should be allowed. *Id.*

[170]*See* Sanchez v. Denver & R.G.W. R.R., 538 F.2d 304 (10th Cir. 1976), *cert. denied*, 429 U.S. 1042 (1977). *Sanchez* was a personal injury action brought under the

the giving of a cautionary instruction[171] are to be left to the trial judge's discretion.

*11. District of Columbia Circuit.*—The D. C. Circuit has no cases directly addressing either issue. However, in *Runyon v. District of Columbia*,[172] the court concluded that it was proper for the estate of the deceased to recover an amount based on probable net future earnings pursuant to the District of Columbia Survival Statute.[173] This net figure is computed by determining gross probable future earnings by use of actuarial tables, subtracting taxes and support, and then discounting the entire amount to present value. The court did not discuss the rationale for its decision at great length. In support of its conclusion, the court simply cited to several state decisions allowing such evidence and to Professors Harper and James' treatise on torts.[174]

### *D. State Courts*

*Floyd v. Fruit Industries*,[175] decided by the Connecticut Supreme Court, is the leading state court decision upholding the admission of evidence of the impact of future taxes. The court stated that it could not conceive of a more unrealistic, unjust, or unfair rule than one that would lead a jury to base their computations of future earnings capacity on the hypothesis that no income taxes would be paid on net earnings. The court also rejected the argument that such evidence was too uncertain or conjectural, raising again the counter argument that such evidence is no more speculative than many of the other factors that must be submitted to the jury for consideration.[176] Several other states have reached the same conclusion as

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FELA in which the court of appeals simply noted that in some cases it would be unconscionable not to take income tax liability into account, and that conversely a similar result could occur if too great a deduction were applied. Therefore, the admissibility of such evidence was best left to the discretion of the trial court. *See also* DeWeese v. United States, 419 F. Supp. 170 (D. Colo. 1976).

[171]*See* Nichols v. Marshall, 486 F.2d 791, 794 (10th Cir. 1973). The court in *Nichols* held it was not error to refuse to give a cautionary instruction but acknowledged that neither would it be error to give such a "precautionary" instruction.

[172]463 F.2d 1319 (D.C. Cir. 1972).

[173]D.C. CODE §§ 16-2701 to -02 (1973) (current version at *id.* §§ 16-2701 to -02 (Supp. 1978)).

[174]463 F.2d at 1322 (citing HARPER & JAMES, *supra* note 96).

[175]144 Conn. 659, 136 A.2d 918 (1957). *Floyd* was a wrongful death action in which the trial court had instructed the jury to consider the offsetting factor of probable income taxes on decedent's probable earnings. *But cf.* Gorham v. Farmington Motor Inn, Inc., 159 Conn. 576, 271 A.2d 94 (1970) (trial court did not err in refusing to charge the jury that the verdict in a personal injury action would not be subject to income tax).

[176]144 Conn. at 666, 136 A.2d at 925. The court also rejected the plaintiff's contention that tax considerations would be more proper in a case involving a fatality than in a case not involving a fatality. *Id.* at 667, 136 A.2d at 926.

Connecticut, using the rationale found in *Floyd* and the federal decisions allowing such evidence.[177]

The Missouri Supreme Court's opinion in *Dempsey v. Thompson*[178] is the state court decision most often cited for the proposition that a cautionary instruction should be given. The court rejected the defendant's contention that taxes should be considered in arriving at the amount of the award. However, the court held that the defendant was entitled to have the jury instructed that the award was not subject to taxation. The court reasoned that most jurors are not only conscious of, but acutely sensitive to, the impact of taxes, while few persons have knowledge of the exemption allowed under federal law. Therefore, the court concluded it was reasonable to assume the jury would believe the award was subject to taxation.[179]

The state court decision most representative of those standing for the proposition that the court should allow neither evidence of future tax liability nor a cautionary instruction is *Hall v. Chicago & Northwestern Railway*,[180] a personal injury action brought under the FELA. The Illinois Supreme Court reasoned that since it is a general principle of law that the status of the parties in a trial is immaterial, it follows that whether the plaintiff has to pay a tax on the award is a matter that concerns only the plaintiff and the government. The court also argued that Congress' intent in enacting the exemption was to give an injured party a tax benefit. This benefit would be nullified if the jury were to reduce the plaintiff's damages to compensate for the tax exemption.[181]

In upholding the refusal to give a cautionary instruction, the Illinois Supreme Court acknowledged that there was a possibility that a defendant might be harmed if the jury made some type of adjustment for this imaginary tax. Nevertheless, the court preferred to rely on the presumption that the jury will not take into consideration any factors that they are not instructed to consider by the trial court. The court also rejected the argument that a cautionary instruction is proper merely because it correctly states the

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[177]Adams v. Deur, 173 N.W.2d 100 (Iowa 1969); Tenore v. Nu Car Carriers, Inc., 67 N.J. 466, 341 A.2d 613 (1975); Turrietta v. Wyche, 54 N.M. 5, 212 P.2d 1041 (1949); Wilson v. Wylie, 86 N.M. 9, 518 P.2d 1213 (Ct. App. 1973); Geris v. Burlington N., Inc., 277 Or. 381, 561 P.2d 174 (1977).

[178]363 Mo. 339, 251 S.W.2d 42 (1952). *But see* McBee v. Schlupbach, 529 S.W.2d 435 (Mo. Ct. App. 1975); Senter v. Ferguson, 486 S.W.2d 644 (Mo. Ct. App. 1972).

[179]For other cases holding evidence of income tax liability inadmissible but requiring a cautionary instruction, *see* High v. State Highway Dep't, 307 A.2d 799 (Del. 1973); Abele v. Massi, 273 A.2d 260 (Del. 1970).

[180]5 Ill. 2d 135, 125 N.E.2d 77 (1955).

[181]*Id.* at 152, 125 N.E.2d at 86.

law.[182] There have been numerous other state decisions reaching the same result on both issues.[183]

Only one state court appears to have adopted the *McWeeney* Rule on the evidentiary issue,[184] and a number of cases have simply refused to allow any evidence of probable future tax liability with no real discussion of an underlying rationale.[185] There have also been a number of states that have held that while it would be proper to give a cautionary instruction concerning the non-taxability of an award, the decision to give such an instruction is totally within the trial court's discretion.[186] However, the majority of state cases dealing with the single issue of the propriety of a cautionary instruction have expressed disapproval of such an instruction.[187]

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[182]The court noted this argument could be adopted *ad infinitum*, to allow innumerable instructions—for example that the expense of trial is not provided for, that the cost of medical witnesses is not paid by the defendant, etc., all of which are correct statements of the law. *Id.*

[183]*See, e.g.*, Mitchell v. Emblade, 80 Ariz. 398, 298 P.2d 1034 (1956); St. Johns River Terminal Co. v. Vadeu, 190 So. 2d 40 (Fla. Dist. Ct. App. 1966); Seaboard Coast Line R.R. v. Thomas, 125 Ga. App. 716, 188 S.E.2d 89 (1972); Atlantic Coast Line R.R. v. Brown, 93 Ga. App. 805, 92 S.E.2d 874 (1956); Green v. Texeira, 54 Haw. 231, 505 P.2d 1169 (1973); Cereal Byproducts Co. v. Hall, 16 Ill. App. 2d 79, 147 N.E.2d 383 (1958) (income tax refund cannot be considered in mitigation of damages); Spencer v. Martin K. Eby Constr. Co., 186 Kan. 345, 350 P.2d 18 (1960) (confusing evidentiary issue and cautionary instruction question); Lumber Terminals Inc. v. Nowakowski, 36 Md. App. 82, 373 A.2d 282 (1977); Briggs v. Chicago Great Ry., 248 Minn. 418, 80 N.W.2d 625 (1957); Eriksen v. Boyer, 225 N.W.2d 66 (N.D. 1974); Bergfeld v. New York, C. & St. L. R.R., 103 Ohio App. 87, 144 N.E.2d 483 (1956).

[184]Morgan v. Liberty Mut. Ins. Co., 323 So. 2d 855 (La. Ct. of App. 1975).

[185]Beaulieu v. Elliot, 434 P.2d 665 (Alaska 1967); Reeves v. Louisiana & Ark. Ry., 304 So. 2d 370 (La. Ct. of App. 1974); Missouri-Kan.-Tex. R.R. v. Miller, 486 P.2d 630 (Okla. 1971); Girard Trust Corn Exch. Bank v. Philadelphia Transp. Co., 410 Pa. 530, 190 A.2d 293 (1963); Oddo v. Cardi, 100 R.I. 578, 218 A.2d 373 (1966); Hardware Mut. Cas. Co. v. Harry Crow & Son, 6 Wis. 2d 396, 94 N.W.2d 577 (1959).

[186]*See, e.g.*, Ahterley v. MacDonald, Young & Nelson, Inc., 142 Cal. App. 575, 298 P.2d 700 (1956); Ploud v. Southern Pac., 266 Or. 666, 513 P.2d 1140 (1973); Crum v. Ward, 146 W. Va. 421, 122 S.E.2d 18 (1961); Behringer v. State Farm Mut. Ins. Co., 6 Wis. 2d 595, 95 N.W.2d 249 (1959).

[187]These decisions have used basically the same rationale as those federal decisions refusing such instructions. *See, e.g.*, Polster v. Girff's of America, Inc., 82 Colo. App. 264, 514 P.2d 80 (1973), *rev'd on other grounds*, 184 Colo. 418, 520 P.2d 745 (1974); Davis v. Fortuno & Jackson Chevrolet Co., 32 Colo. App. 222, 510 P.2d 1376 (1973); Kawanato v. Yesutake, 49 Haw. 42, 410 P.2d 976 (1966); Louisville & Nash. R.R. v. Mattingly, 318 S.W.2d 844 (Ky. Ct. App. 1958), *modified on other grounds*, 339 S.W.2d 155 (Ky. Ct. App. 1960); Bracy v. Great N. Ry., 136 Mont. 65, 343 P.2d 848 (1959), *cert. denied*, 361 U.S. 949 (1960); Chicago, Rock I. & Pac. R.R. v. Kinsey, 372 P.2d 863 (Okla. 1962); Crecelius v. Gamble-Skozmo, 144 Neb. 394, 13 N.W.2d 627 (1944); Scalise v. Central R.R., 129 N.J. Super. 303, 323 A.2d 525 (1974); Stallcup v. Taylor, 62 Tenn. App. 407, 463 S.W.2d 416 (1971); Dixie Feed & Seed Co. v. Byrd, 52 Tenn. App. 619, 376 S.W.2d 745, *cert. denied*, 379 U.S. 878 (1964); Texas Consol. Trans. v. Eubanks, 340

## III. SUMMARY

### *A. Inflationary & Productivity Factors*

Unfortunately for attorneys practicing law in Indiana, neither jurisdiction they would be most concerned with, the Indiana Supreme Court nor the Seventh Circuit, has ever directly considered the admissibility of expert testimony on the effects of increased productivity and inflationary trends on the computation of lost future earnings. However, there are several Indiana cases indicating that such evidence is admissible. While most of the Federal Courts have addressed the issues, no general agreement has been reached. The First, Second and Fifth Circuits have taken the clearest stance against the use of such evidence, noting that it is far too speculative to be considered. Furthermore, the courts suggest that any undercompensation that might appear to result from the failure to consider the effects of inflation is offset by the concurrent increase in interest rates paid on investments and the refusal by most courts to allow a deduction of probable future income taxes from any award. However, even among these three circuits, there have been indications that the courts will allow evidence as to increased productivity to be admitted, provided a strict foundation is first laid to insure the reliability of such evidence.

Another approach, adopted by the Sixth and Eighth Circuits, rejects the notion that specific evidence as to inflationary trends should be received and considered but permits introduction of evidence on productivity increases, such as probable future raises in income or promotions. While holding evidence of future inflationary trends too speculative to be admissible, both circuits allow inflation to be taken into account by allowing the jury to consider diminished or increased purchasing power of the dollar. This approach appears to be an attempt by the circuits to avoid the use of expert witnesses to develop inflated awards.

A third approach is that followed by the Ninth and Tenth Circuits. These circuits allow evidence of both future inflationary trends and possible increases in productivity to be considered in determining lost future earnings based on the rationale that dealing with inflationary trends is the best way to insure a fairer and more accurate result. However, both circuits have added the caveat that they were not authorizing any arbitrary guesswork in determining inflationary effects and that a strict foundation should be laid before such evidence is permitted. While the Third Circuit originally re-

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S.W.2d 830 (Tex. Ct. App. 1960); John F. Buckner & Sons v. Allen, 289 S.W.2d 387 (Tex. Ct. App. 1956); Missouri-Kan.-Tex. R.R. v. McFerrin, 156 Tex. 69, 291 S.W.2d 931 (1956).

jected the introduction of such evidence as being too speculative, recent decisions have indicated a modification of its original position towards the approach taken by the Ninth and Tenth Circuits. Likewise, a district court of the Fourth Circuit has rendered a recent decision that if followed by the court of appeals in the Fourth Circuit would indicate the adoption of a position similar to that of the Ninth and Tenth Circuits.

The majority of the state courts that have addressed the issue have allowed such evidence. This would appear to be the current trend. The state courts, like the federal courts allowing such evidence, do so on the rationale that other factors equally speculative are already considered in determining damages, and that to ignore inflationary trends and evidence of increased productivity would lead to undercompensating the injured party. These courts also indicate that to exclude such evidence is to avoid economic reality and to indulge in the equally questionable presumption that inflation will not occur. However, decisions advocating the admission of such evidence require a strict foundation to insure the trustworthiness of the evidence.

The state courts excluding such testimony also follow basically the rationale of the federal courts, emphasizing the lack of consensus among economists and the basic unreliability of the science of economics in its efforts to accurately forecast economic conditions. State courts also express concern that allowing consideration of such factors will open the door to what they consider other collateral issues that would impair the proper functioning of the jury. Specifically, the courts note such additional evidence on factors such as taxes, deflation, and attorney fees would have to be allowed if evidence of inflation and productivity factors were to be considered. As a result, the jury would be caught in a quagmire of conflicting expert testimony and would lose sight of the main issues of the case. Finally, most courts also note that any apparent undercompensation is offset by the fact that a plaintiff receiving a large sum of money may invest the money in a manner that will give him some protection against inflation.

Thus, while there is an even split between federal courts allowing consideration of inflationary and productivity factors and courts not permitting evidence of such factors, the more recent federal decisions and the vast majority of state courts favor admissibility. However, even these courts have indicated reluctance to allow testimony that is based on unrealistically short time periods or uniquely inflationary periods. The courts have also been reticent to allow projections too far into the future because long term predictions of continued inflation lead to excessively high verdicts. In essence, such long term projections predict economic doom, since no

economy can function on a continued inflationary spiral. While the courts have reacted more favorably towards admission of evidence concerning increased productivity than evidence of inflationary trends, they still require a strict foundation to be laid, generally consisting of the particular individual's past wage increases. In the absence of such evidence, the courts require evidence of wage increases of an individual in as similar a position to the injured party as possible.

### *B. Income Taxes*

*1. Evidence of Tax Impact.*—Indiana is among the majority of states that have held that inquiries at trial into the incidents of taxation in damage suits would be too conjectural and confusing and would inject collateral issues into the trial. However, the issue has only been discussed where a party has merely requested a cautionary instruction to the effect that the award is non-taxable. The issue of the admissibility of evidence of the impact of income taxation on the award is entirely distinct from the question of the propriety of a cautionary instruction. Although the Indiana Supreme Court has failed to make this distinction, it has been acknowledged by the Indiana Court of Appeals. Only four states, Connecticut, New Jersey, Iowa and New Mexico, have held evidence of future tax impact should be considered, relying on the basic rationale that such evidence is no more speculative than other factors used to compute lost future earnings and that to do otherwise would lead to overcompensation of the plaintiff.

Only one state has adopted the *McWeeney* Rule permitting the jury to consider income taxes only in those cases where taxes will have a significant and substantial effect in the computation of probable future earnings. However, among the federal courts, the *McWeeney* Rule has clearly become the majority rule. It has been adopted by the Second, Fourth, Fifth, Sixth, Seventh and Ninth Circuits. While the Fourth Circuit and the D. C. Circuit require the impact of taxes to be considered in wrongful death actions, no federal court has even held that evidence of the projected effect of taxes on plaintiff's damages is always admissible, although there is dicta in a Ninth Circuit decision that evidence of the impact of taxation should be considered in all cases.

The *McWeeney* Court advanced the following propositions in support of its decision: (1) The determination of future tax liability would be too conjectural in light of factors such as changes in the family status of the injured party in years to come, possible changes in the exemption and deduction provisions of the tax law, possible changes in the rates of taxation, and so forth; (2) The use of a net income theory would be too complex and confusing for the jury; (3)

Other factors such as inflation and attorney fees tend to counterbalance any resulting overcompensation.

These propositions have come under sharp attack in dissenting opinions and legal commentaries. In response to the objection that such a determination would be too conjectural, it is generally noted that evidence of the impact of income taxes on future earnings is no more speculative than other factors used to compute damages. In fact, the existence of income tax in this country is less conjectural than the continuance of the plaintiff's salary during the same period. The argument for the first proposition loses much of its force when a court is willing to consider the equally if not more speculative factors of inflation and productivity. Even those federal circuits holding such evidence to be too speculative have acknowledged that when state law requires the effect of inflation to be considered one must in all fairness allow evidence of the impact of income taxes to be considered.

It is difficult to accept the second assertion made by the *McWeeney* Court that the tax issue is beyond the understanding of the layman when it is realized that the average American is exposed to tax computations and considerations in his everyday life and would thus appear to be qualified to assess such problems at trial. Finally, the argument that consideration of taxes would lead to the necessity of considering attorney's fees is discredited when one realizes that unlike taxation, which undoubtedly would have occurred whether or not the party had been injured, the impact of attorney's fees has no relation to the jury's task of estimating what the individual's future earnings would have been. Also, attorney's fees are the result of private contract between the litigant and attorneys and are thus irrelevant to the issue of just compensation.

Of the circuits not adopting the *McWeeney* Rule, the Tenth Circuit has taken the position that the admissibility of such evidence is totally within the trial court's discretion. Only the First, Third, and Eighth Circuits hold all evidence of income tax impact inadmissible, based on such various rationales as Congressional intent, collateral source doctrine or that such evidence is too speculative. However, even these courts acknowledge that when the plaintiff receives his gross earnings he is being overcompensated. One decision from the Ninth Circuit went so far as to hold in an FTCA case that failure to consider taxes was the equivalent of awarding punitive damages, which is impermissible under the FTCA.[188]

*2. Cautionary Instruction on Taxes.*—Many courts, especially the state courts, including Indiana, have refused to give a cautionary instruction because they have confused the problem of the

[188]Felder v. United States, 543 F.2d 657 (9th Cir. 1976).

cautionary instruction with the problem of whether the evidence of the incidence of taxation should be admitted during trial. Once these issues are confused, the court points out how "confused" the jury would be with this additional information. The fallacy of these arguments is that the requested instruction does not relate to the impact of taxation on plaintiff's future wages and requires no complex calculations. It concerns only the effect of the tax laws on plaintiff's award. The purpose of such a cautionary instruction is merely to dispel any misconceptions that the jurors might hold on this question. A recent Indiana Court of Appeals decision has recognized this distinction that eluded the Indiana Supreme Court.

In contrast to the clear majority following the *McWeeney* Rule on the evidentiary issue, the federal courts that have considered whether a form of a cautionary instruction should be given have not ruled uniformly. Three circuits, the Second, Sixth, and Tenth, have held that the decision to give such an instruction is within the trial court's discretion. Therefore, it will not be reversible error either to refuse such an instruction, or to give such an instruction. The First Circuit, while holding the refusal to give such an instruction was not error, indicated that if there was evidence that the jury was improperly considering taxes it would be error not to give the instruction. The Eighth Circuit has specifically refused to rule on the question. The Fifth Circuit flatly rejects the propriety of a cautionary instruction. The Third and Ninth Circuits have held that such an instruction must be given in future cases. The Third and Ninth Circuit holdings are also supported by the majority of commentators who have considered the question. However, the majority of states addressing the issue have held such an instruction should not be given.

The better rationale used in those federal and state cases that disapprove of the use of the instruction is that it cannot be assumed that the jury will not follow instructions when it has been correctly instructed on the measure of damages. Since there is a possibility of harming the plaintiff by allowing such an instruction, it is better to instruct the jury on the proper measure of damages and then rely on the presumption that it will follow the instruction. The counterargument is that, given the general tax awareness of the average citizen and the fact that few persons actually know of the special exclusion for personal injury awards, failure to give such an instruction could result in the plaintiff receiving an enhanced award based on the probable misconception that the amount awarded by the jury will be reduced up to fifty percent by taxes.

### *C. Conclusion*

The Indiana courts at the present apparently give the plaintiff's attorney the worst of both worlds, indicating indirectly that

economic trends may be considered but projections of future tax liability or cautionary instructions may not. Although many courts have done so, it is theoretically inconsistent to admit evidence of any one of the factors (that is inflationary/productivity evidence as opposed to tax impact evidence) without admitting evidence of the other. The objective of the basic system of damages in this country is to place the injured party in the same position, as nearly as can be done with a monetary award, as he or she would have been had the wrong not occurred. Since inflationary/productivity factors and taxes would both theoretically affect the injured party's position, it is inconsistent to admit evidence of one and not the other.

However, it may be more practical to admit evidence of tax impact evidence than inflationary/productivity evidence. Tax factors are less speculative than inflationary and productivity factors. It is more probable that taxes will continue at present rates than inflation, if only for the reason that no economy can continue to exist with constantly spiraling inflation. Furthermore, while taxes are generally a certainty of life that the plaintiff would have had to bear, the plaintiff and defendant must equally share the risk of inflationary and depressionary periods. Finally, any undercompensation due to inflation will be partially offset by realization of a higher interest rate than that used in discounting the award to present value. Nevertheless, the tendency of several courts in the past, including those in Indiana, has been to allow evidence of inflation and productivity and to exclude evidence of the impact of income taxes, a position which appears to be wholly untenable.

Perhaps the *McWeeney* Rule is the best approach to the tax issue, although the courts have been vague in setting out the rationale that underlies the rule. Some courts question the relevancy of such evidence. These courts are actually confusing relevancy with countervailing factors such as danger of confusion, collateral issues, or delay that may outweigh the probative value of such evidence. To say such evidence is not "relevant" or "pertinent" is to ignore the basic guide of tort law, which is to compensate the plaintiff for what he has lost. Although the *McWeeney* Rule has seldom been analyzed as such, it could be considered as an evidentiary rule, weighing probative value against probative danger. When admittedly relevant evidence has, on balance, a greater tendency to frustrate rather than to promote the ultimate end of just compensation, the trial court must exercise its discretion and refuse to admit it. Thus, at the lower and middle income levels, where the probative value of such evidence is less and the probative dangers greater, such evidence is often not allowed, while at the higher income brackets and consequently higher tax rates, the probative value increases sufficiently to outweigh any probative dangers.

Finally, as to the propriety of a cautionary instruction, the benefits of informing the jury of the actual consequences appear so obvious, and the burden in terms of confusion so minimal, that the argument for giving such an instruction is clearly the better position.

Inflation, productivity, and taxes do affect future earnings and should be considered if the injured party is to be adequately compensated. Furthermore, today's juror is likely to consider such factors regardless of whether evidence is presented on these issues and regardless of the lack of instructions. Therefore, it should be the court's duty to insure that the jury has competent evidence on which to base such predictions by requiring a strict foundation to be laid to assure the evidence is as reliable as possible.

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