

## Rules for Filing 1099 and W-2 Forms for Attorneys Fees as Part of an Employment Dispute Settlement

Steve Gerlach | September 9, 2009

Since the passage of the American Jobs Creation Act of 2004 (“AJCA”), there has been a lot of confusion about the proper filing of 1099 and W-2 forms when an employer has settled an employment dispute and as part of the settlement agrees to pay the employee’s attorney’s fees. In this client advisory, we attempt to clarify which forms need to be filed and when.

- o A W-2 must be issued to the employee for any back wages or other payments in lieu of compensation.
- o A 1099 must be issued to the employee for any non-W-2 proceeds. This 1099 must include the amount of any attorney’s fees paid on the employee’s behalf.
- o A 1099 must also be issued to the employee’s attorney in the amount of any payment made to that attorney, or in the amount of any co-payment made to both the attorney and the employee. The full amount of this payment must be reported without regard to how the payment is ultimately divided between the attorney and the employee.

Under this reporting regime, all amounts that are included in the gross income of the employee are reported on either a W-2 or a 1099, including the attorney’s fees. The employee is then entitled to take a deduction on his or her tax return in the amount of those attorney’s fees.

There are some minor exceptions to these reporting requirements, for example, for payments that are excluded (an exclusion is not the same as a deduction) from the employee’s gross income. These exceptions, however, are narrow and a misapplication of them could result in the assessment of penalties to the employer. We strongly recommend consulting with counsel before deciding not to issue a 1099 or W-2.

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