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(Original Signature of Member)

119TH CONGRESS
1ST SESSION

H. R. _____

To amend the Internal Revenue Code of 1986 to establish a tax on income from litigation which is received by third-party entities that provided financing for such litigation.

IN THE HOUSE OF REPRESENTATIVES

Mr. HERN of Oklahoma introduced the following bill; which was referred to the Committee on _____

A BILL

To amend the Internal Revenue Code of 1986 to establish a tax on income from litigation which is received by third-party entities that provided financing for such litigation.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Tackling Predatory
5 Litigation Funding Act”.

1 **SEC. 2. LITIGATION FINANCING.**

2 (a) IN GENERAL.—Subtitle D of the Internal Rev-
3 enue Code of 1986 is amended by adding at the end the
4 following new chapter:

5 **“CHAPTER 50B—LITIGATION FINANCING**

“Sec. 5000E–1. Tax imposed.

“Sec. 5000E–2. Definitions.

“Sec. 5000E–3. Special rules.

6 **“SEC. 5000E–1. TAX IMPOSED.**

7 “(a) IN GENERAL.—A tax is hereby imposed for each
8 taxable year in an amount equal to the applicable percent-
9 age of any qualified litigation proceeds received by a cov-
10 ered party.

11 “(b) APPLICABLE PERCENTAGE.—For purposes of
12 subsection (a), with respect to any taxable year, the appli-
13 cable percentage shall be the amount (expressed as a per-
14 centage) equal to the sum of—

15 “(1) the highest rate of tax imposed by section
16 1 for such taxable year, plus

17 “(2) 3.8 percentage points.

18 “(c) APPLICATION OF TAX FOR PASS-THRU ENTI-
19 TIES.—In the case of a covered party that is a partner-
20 ship, S corporation, or other pass-thru entity, the tax im-
21 posed under subsection (a) shall be applied at the entity
22 level.

23 **“SEC. 5000E–2. DEFINITIONS.**

24 “In this chapter—

1 “(1) CIVIL ACTION.—

2 “(A) IN GENERAL.—The term ‘civil action’
3 means any civil action, administrative pro-
4 ceeding, claim, or cause of action.

5 “(B) MULTIPLE ACTIONS.—The term ‘civil
6 action’ may, unless otherwise indicated, include
7 more than 1 civil action.

8 “(2) COVERED PARTY.—

9 “(A) IN GENERAL.—The term ‘covered
10 party’ means, with respect to any civil action,
11 any third party (including an individual, cor-
12 poration, partnership, or sovereign wealth fund)
13 to such action which—

14 “(i) receives funds pursuant to a liti-
15 gation financing agreement, and

16 “(ii) is not an attorney representing a
17 party to such civil action.

18 “(B) INCLUSION OF DOMESTIC AND FOR-
19 EIGN ENTITIES.—Subparagraph (A) shall apply
20 to any third party without regard to whether
21 such party is created or organized in the United
22 States or under the law of the United States or
23 of any State.

24 “(3) LITIGATION FINANCING AGREEMENT.—

1 “(A) IN GENERAL.—The term ‘litigation
2 financing agreement’ means, with respect to
3 any civil action, a written agreement—

4 “(i) whereby a third party agrees to
5 provide funds to one of the named parties
6 or any law firm affiliated with such civil
7 action, and

8 “(ii) which creates a direct or
9 collateralized interest in the proceeds of
10 such action (by settlement, verdict, judg-
11 ment or otherwise) which—

12 “(I) is based, in whole or part,
13 on a funding-based obligation to—

14 “(aa) such civil action,

15 “(bb) the appearing counsel,

16 “(cc) any contractual co-
17 counsel, or

18 “(dd) the law firm of such
19 counsel or co-counsel, and

20 “(II) is executed with—

21 “(aa) any attorney rep-
22 resenting a party to such civil ac-
23 tion,

24 “(bb) any co-counsel in the
25 litigation with a contingent fee

1 interest in the representation of
2 such party,

3 “(cc) any third party that
4 has a collateral-based interest in
5 the contingency fees of the coun-
6 sel or co-counsel firm which is re-
7 lated, in whole or part, to the
8 fees derived from representing
9 such party, or

10 “(dd) any named party in
11 such civil action.

12 “(B) SUBSTANTIALLY SIMILAR AGREE-
13 MENTS.—The term ‘litigation financing agree-
14 ment’ shall include any contract (including any
15 option, forward contract, futures contract, short
16 position, swap, or similar contract) or other
17 agreement which, as determined by the Sec-
18 retary, is substantially similar to an agreement
19 described in subparagraph (A).

20 “(C) EXCEPTIONS.—The term ‘litigation
21 financing agreement’ shall not include any
22 agreement—

23 “(i) under which the total amount of
24 funds described in subparagraph (A)(i)

1 with respect to an individual civil action is
2 less than \$10,000, or

3 “(ii) in which the third party de-
4 scribed in subparagraph (A)—

5 “(I) has a right to receive pro-
6 ceeds which are derived from, or pur-
7 suant to, such agreement that are lim-
8 ited to—

9 “(aa) repayment of the prin-
10 cipal of a loan,

11 “(bb) repayment of the prin-
12 cipal of a loan plus any interest
13 on such loan, provided that the
14 rate of interest does not exceed
15 the greater of—

16 “(AA) 7 percent, or

17 “(BB) a rate equal to
18 twice the average annual
19 yield on 30-year United
20 States Treasury securities
21 (as determined for the year
22 preceding the date on which
23 such agreement was exe-
24 cuted), or

1 “(cc) reimbursement of at-
2 torney’s fees, or

3 “(II) bears a relationship de-
4 scribed in section 267(b) to the
5 named party receiving the payment
6 described in subparagraph (A)(i).

7 “(4) QUALIFIED LITIGATION PROCEEDS.—

8 “(A) IN GENERAL.—The term ‘qualified
9 litigation proceeds’ means, with respect to any
10 taxable year, an amount equal to the realized
11 gains, net income, or other profit received by a
12 covered party during such taxable year which is
13 derived from, or pursuant to, any litigation fi-
14 nancing agreement.

15 “(B) ANTI-NETTING.—Any gains, income,
16 or profit described in subparagraph (A) shall
17 not be reduced or offset by any ordinary or cap-
18 ital loss in the taxable year.

19 “(C) PROHIBITION ON EXCLUSION OF CER-
20 TAIN AMOUNTS.—In determining the amount of
21 realized gain under subparagraph (A), amounts
22 described in section 104(a)(2) and 892(a)(1)
23 shall not be excluded.

1 **“SEC. 5000E-3. SPECIAL RULES.**

2 “(a) WITHHOLDING OF TAX ON LITIGATION PRO-
3 CEEDS.—Any applicable person having the control, re-
4 ceipt, or custody of any proceeds from a civil action (by
5 settlement, judgment, or otherwise) with respect to which
6 such person had entered into a litigation financing agree-
7 ment shall deduct and withhold from such proceeds a tax
8 equal to 50 percent of the applicable percentage (as deter-
9 mined under section 5000E-1(b)) of any payments which
10 are required to be made to a third party pursuant to such
11 agreement.

12 “(b) APPLICABLE PERSON.—For purposes of this
13 section, the term ‘applicable person’ means any person
14 which—

15 “(1) is a named party in a civil action or a law
16 firm affiliated with such civil action, and

17 “(2) has entered into a litigation financing
18 agreement with respect to such civil action.

19 “(c) APPLICATION OF WITHHOLDING PROVISIONS.—

20 “(1) LIABILITY FOR WITHHELD TAX.—Every
21 person required to deduct and withhold any tax
22 under this chapter is hereby made liable for such tax
23 and is hereby indemnified against the claims and de-
24 mands of any person for the amount of any pay-
25 ments made in accordance with the provisions of this
26 chapter.

1 “(2) WITHHELD TAX AS CREDIT TO RECIPIENT
2 OF QUALIFIED LITIGATION PROCEEDS.—Qualified
3 litigation proceeds on which any tax is required to
4 be withheld at the source under this chapter shall be
5 included in the return of the recipient of such pro-
6 ceeds, but any amount of tax so withheld shall be
7 credited against the amount of tax as computed in
8 such return.

9 “(3) TAX PAID BY RECIPIENT OF QUALIFIED
10 LITIGATION PROCEEDS.—If—

11 “(A) any person, in violation of the provi-
12 sions of this chapter, fails to deduct and with-
13 hold any tax under this chapter, and

14 “(B) thereafter the tax against which such
15 tax may be credited is paid,

16 the tax so required to be deducted and withheld
17 shall not be collected from such person, but this
18 paragraph shall in no case relieve such person from
19 liability for interest or any penalties or additions to
20 the tax otherwise applicable in respect of such fail-
21 ure to deduct and withhold.

22 “(4) REFUNDS AND CREDITS WITH RESPECT TO
23 WITHHELD TAX.—Where there has been an overpay-
24 ment of tax under this chapter, any refund or credit
25 made under chapter 65 shall be made to the with-

1 holding agent unless the amount of such tax was ac-
2 tually withheld by the withholding agent.”.

3 (b) EXCLUSION FROM DEFINITION OF CAPITAL
4 ASSET.—Section 1221(a) of the Internal Revenue Code
5 of 1986 is amended—

6 (1) in paragraph (7), by striking “or” at the
7 end,

8 (2) in paragraph (8), by striking the period at
9 the end and inserting “; or”, and

10 (3) by adding at the end the following new
11 paragraph:

12 “(9) any financial arrangement created by, or
13 any proceeds derived from, a litigation financing
14 agreement (as defined under section 5000E-2).”.

15 (c) REMOVAL FROM GROSS INCOME.—Part III of
16 subchapter B of chapter 1 of the Internal Revenue Code
17 of 1986 is amended by inserting after section 139I the
18 following new section:

19 **“SEC. 139J. QUALIFIED LITIGATION PROCEEDS.**

20 “Gross income shall not include any qualified litiga-
21 tion proceeds (as defined in section 5000E-2).”.

22 (d) CLERICAL AMENDMENTS.—

23 (1) Section 7701(a)(16) of the Internal Rev-
24 enue Code of 1986 is amended by inserting
25 “5000E-3(c)(1),” before “1441”.

1 (2) The table of chapters for subtitle D of the
2 Internal Revenue Code of 1986 is amended by in-
3 serting after the item relating to chapter 50A the
4 following new item:

“CHAPTER 50B—LITIGATION FINANCING”.

5 (3) The table of sections for part III of sub-
6 chapter B of chapter 1 of such Code is amended by
7 inserting after the item relating to section 139I the
8 following new item:

“Sec. 139J. Qualified litigation proceeds.”.

9 (e) EFFECTIVE DATE.—The amendments made by
10 this section shall apply to taxable years beginning after
11 December 31, 2025.