STATE OF TENNESSEE
OFFICE OF THE ATTORNEY GENERAL

June 29, 2018

Opinion No. 18-27

Payment of Professional Privilege Tax for State Judges

Question 1

May the judicial branch of the state government, as employer, remit the professional privilege tax, as permitted under Tenn. Code Ann. § 67-4-1709, on behalf of judges employed by the State?

Opinion 1

Yes.

ANALYSIS

The Tennessee Legislature has required that, in addition to meeting the qualifications specified in article VI, sections 3 and 4 of the Tennessee Constitution, judges of the Tennessee Supreme Court, Court of Appeals, Court of Criminal Appeals, chancery courts, circuit courts, and criminal courts be "learned in the law, which must be evidenced by the judge being authorized to practice law in the courts of this State." Tenn. Code Ann. § 17-1-106. This statutory requirement amounts to a requirement that all of the specified judges be licensed to practice law in Tennessee, since no one is permitted to "engage in the 'practice of law' or the 'law business'" without a license issued by the Supreme Court.[1] Tenn. S. Ct. Rule 7, Sec. 1.01.

But, while the Legislature requires these judges to hold a license to practice law, the Legislature at the same time prohibits them from actually practicing law. Tenn. Code Ann. § 17-1-105 ("No judge or chancellor shall practice law, or perform any of the functions of attorney or counsel, in any of the courts of this state."). In other words, although judges must be licensed as attorneys as a condition of employment as a judge, they may not actively practice law.

Tennessee levies a tax "on the privilege of engaging in" certain professions and occupations, and that professional privilege tax applies to "persons licensed as attorneys by the supreme court of Tennessee." Tenn. Code Ann. § 67-4-1702(5). The "tax levied . . . on "the privilege of engaging in certain occupations requiring registration or a license do [*sic*.] not apply to a person so registered or licensed, if the person is inactive or retired pursuant to the regulations of the appropriate licensing board." Tenn. Code Ann. § 67-4-1708(a).

[1] Authorization—i.e., admission—to practice law in Tennessee is controlled by the Tennessee Supreme Court. Tenn. S. Ct. Rule 7.

The Supreme Court has created the Board of Law Examiners for the State of Tennessee to determine initial eligibility for licensure for attorneys. Tenn. S. Ct. Rule 7. The Supreme Court has also created the Board of Professional Responsibility (the BPR) to oversee and administer a licensed attorney's continued fitness to be licensed to practice law. Tenn. S. Ct. Rule 9, sec. 1 and sec. 4. A licensed attorney who is not "engaged in the practice of law in Tennessee" as that term is defined in Rule 9, sec. 10.3(e), may apply to the BPR to assume inactive status. Tenn. S. Ct. Rule 9, sec. 10.7. A person who is granted inactive status remains licensed but may not actively engage in the practice of law in Tennessee. Reinstatement following inactive status is available provided certain conditions are met. *Id.*

Thus, to the extent that judges may qualify for inactive status pursuant to S. Ct. Rule 9 because they are prohibited by statute from practicing law in Tennessee while serving on the bench, the professional privilege tax would not apply to any judge who applies for and is granted inactive status by the BPR, the appropriate licensing authority. *See* Tenn. Code Ann. § 67-4-1708(a).

When the tax does apply to a person licensed to engage in one of the listed professions, that person is liable for payment of the professional privilege tax, but "[a]ny employer, including any governmental entity, may choose to remit the tax . . . on behalf of persons subject to the tax who are employed by such employer." Tenn. Code Ann. § 67-4-1709(a). Accordingly, the judicial branch, as employer of state court judges, is clearly authorized by the Legislature to remit the privilege tax on behalf of judges who are subject to the tax.

Even though the judicial branch is authorized to remit the professional privilege tax on behalf of the state court judges it employs, there is a question whether payment of the professional privilege tax by the employer on behalf of a judge would run afoul of the constitutional prohibition on increasing the "compensation" that the Legislature sets for elected judges during the time for which the judge is elected. The Tennessee Constitution provides that judges of the Tennessee Supreme Court and inferior courts

> shall, at stated times, receive a compensation for their services, to be ascertained by law, which shall not be increased or diminished during the time for which they are elected.

Tenn. Const. art. VI, § 7. Nor may these judges "be allowed any fees or perquisites of office." *Id.* The question is premised on the theory that "compensation" as used in article VI, section 7, is synonymous with "base salary," that payment by the employer of the privilege tax is a benefit paid in addition to the base salaries the Legislature establishes for judges,[2] and payment of the benefit in addition to the base salary is an "increase" in "compensation."

But "compensation" is not necessarily limited to "base salary." The words and terms in the Constitution should be given their plain, ordinary, and inherent meaning. *Hooker v. Haslam*, 437 S.W.3d 409, 426 (Tenn. 2014); *State ex rel. Sonnenburg v. Gaia*, 717 S.W.2d 883, 885 (Tenn.

[2] The "base salaries" of judges, justices, and chancellors as of 1990 are fixed by statute. Tenn. Code Ann. § 8-23-103(1). Those base salaries must be adjusted each year in accordance with a statutory scheme centered on changes in the average consumer price index. Tenn. Code Ann. § 8-23-103(2).

1986). The "compensation" delimited by the Constitution is "compensation" to judges "for their services" as "ascertained by law." Tenn. Const. art. VI, § 7. First, "compensation for services" is commonly understood to include more than base salary. For example, "compensation," according to *Black's Law Dictionary* 301 (8th ed. 1999), "consists of wages and benefits in return for services." (Citation omitted.) Thus, even if payment of the professional privilege tax on behalf of the judges is viewed as a benefit, it falls within the scope of "compensation" as that word is commonly understood.

Second, "compensation ascertained by law" means "that the compensation is either expressly set by statute or is capable of being computed pursuant to an objective statutory scheme." Tenn. Att'y Gen. Op. 93-30, at 2 (Apr. 2, 1993). Since the Legislature has expressly authorized payment of the tax by *any* government employer on behalf of its employee, that payment, which is capable of being computed pursuant to an objective statutory scheme—i.e., the professional privilege tax scheme—is within the scope of compensation as "ascertained by law." It follows, then, that the payment would not increase compensation for the judges, since it is included within the scope not only of the ordinary meaning of "compensation for services," but also within the scope of the meaning of "compensation ascertained by law."

Third, even if payment of the tax were deemed an "increase," that increase would not be unconstitutional as applied to any judge whose term began after 2002. The constitutional prohibition on the increase or diminution of the compensation of judges during the time for which they are elected has been held to mean that the compensation may not be altered by statute enacted *during that time*. *Barry v. Wilson County*, 610 S.W.2d 441, 444 (Tenn. Ct. App. 1980). The professional privilege tax statutory scheme was first enacted in 1992 and any amendments to the portions of that statutory scheme relevant here were last made in 2002, when the tax rate was increased from $200 to $400. In short, any alteration in compensation made by the provision in the professional privilege tax law that permits an employer to pay the tax for the employee was enacted before—not during—the time for which judges whose terms began after 2002 were elected. Payment of the tax by the judicial branch for those judges would, therefore, not be an increase to compensation within the meaning of article VI, section 7.

When previously asked for an opinion on this issue, this Office began with the proposition that "compensation" was not defined in the Constitution, and it looked to cases defining "compensation" for federal income tax purposes. Based on those cases, this Office previously opined that, because "generally" there is a strong presumption that payments from an employer in addition to an employee's agreed-upon salary are additional compensation for services rendered, payment of the professional privilege tax by the judicial branch on behalf of judges would constitute additional—i.e., increased—compensation to judges and would, therefore, be prohibited by article VI, section 7 of the Tennessee Constitution. Tenn. Att'y Gen. Op. 03-081 (June 25, 2003).

However, the previous opinion did not look beyond the "general" treatment of payments made in cash or in kind by employers on behalf of employees. It, therefore, did not consider other applicable principles used in determining whether and when such payments are "compensation." For example, it did not consider that the payment of a professional membership fee will not be considered taxable income if the employer is the primary beneficiary of the payment, and that the

employer is deemed the primary beneficiary whenever membership in the association is a requirement of employment. 26 CFR 1.132-5.

Importantly, the previous opinion did not factor into the analysis the "working conditions benefits" exclusion from income. If an employer provides an employee with a benefit, the cost of which would have been allowable as a business or depreciation deduction had the employee paid for it himself, that cost is not treated as income to the employee. This is known as the "working condition benefits" exclusion. *See* IRS Publication 15-B (2017), Employer's Tax Guide to Fringe Benefits. The "working condition benefits" exclusion applies to property and services and certain cash payments an employer provides to an employee so that the employee can perform his job. It applies to the extent the employee could deduct the cost of the property or services as a business expense or depreciation expense if he had paid for it.

In other words, "[g]ross income does not include the value of a working condition fringe [benefit]," and a "'working condition fringe [benefit]' is any property or service provided to an employee of an employer to the extent that, if the employee paid for the property or service, the amount paid would be allowable as a deduction under section 162 or 167." 26 CFR § 1.132-5(a)(1). And a cash payment made by an employer to an employee will qualify as a working condition fringe benefit as long as it is used for the payment of expenses in connection with a specific undertaking for which a section 162 or 167 deduction is allowed. 26 CFR § 1.132-5(a)(1)(v).

The IRS FRINGE BENEFIT GUIDE Jan. 2014, section 17, provides additional guidance specifically on the payment by the employer for an employee's professional license and for expenses necessary to maintain a license required for employment.

> Employer reimbursements to employees for the cost of their professional licenses and professional organization dues may be excludable [from gross income] if they are directly related to the employee's job. Once an employee has completed the education or experience required for a professional license, the expenses necessary to maintain a license or status are considered ordinary and necessary business expenses. **If paid or reimbursed by an employer for an employee**, the fees are a working condition fringe benefit. . . . **If paid by an individual**, with no employer reimbursement, the fees are deductible as a business expense on the individual's Federal income tax return. *IRC §162 Reg. §1.62-1T(e).*

(Emphasis in original.) And IRS Publication 529, *Unreimbursed Employee Expenses*, explains, in the specific context of the working conditions benefits exclusion, that an employee can deduct the amount he pays each year to state or local governments for professional licenses.

Because the analysis in Tenn. Att'y Gen. Op. 03-081 (June 25, 2003), is incomplete, the conclusion reached is not controlling. The payment by the employer of amounts necessary for an employee to maintain his professional license is not considered compensation to the employee for federal income tax purposes. It is, to the contrary, specifically excluded from gross income. Thus, even under the very broad IRS definition of gross income, payment by the judicial branch of the

professional privilege tax for its employee judges would not be deemed compensation to the judges and, accordingly, would not "increase" their compensation in violation of the Tennessee Constitution.

In sum, the judicial branch of the state government, as employer, may remit the professional privilege tax, as permitted under Tenn. Code Ann. § 67-4-1709, on behalf of judges employed by the State. That payment by the employer is not an "increase" in a judge's compensation within the meaning of article VI, section 7 of the Tennessee Constitution. First, since the Legislature has expressly authorized payment of the tax by a government employer on behalf of its employees, that payment is within the scope of—i.e., not in addition to—compensation for services as "ascertained by law." Second, even if payment of the tax were deemed an "increase," it would not be an increase for any judge whose term began after 2002 because the payment statute was enacted before their terms began. Third, payment of the professional privilege tax by the employer would not be treated as income to the employee—and therefore not an "increase" to the employee's salary—even under the very broad IRS definition of "gross income," because it would be excluded from income as a "working conditions [fringe] benefit."[3]

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[3] It is possible, of course, that the payment in a particular case may not qualify as a working conditions benefits exclusion, in which case this part of the analysis would not necessarily support the constitutionality of the payment. For example, it may be that an individual employee is not allowed to deduct the expense on his income tax return due to his particular circumstances, in which case the working conditions benefits exclusion would not apply.