BORROWING FROM THE TAXPAYER:

STATE AND LOCAL TAX CLAIMS IN BANKRUPTCY

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Bankruptcy affects virtually every sector of society, including state and local taxing authorities. Tax disputes lead many debtors to seek bankruptcy relief. As a result, state and local taxing authorities have become more aggressive in asserting their rights in the bankruptcy forum. FN1 Although in many cases the bankruptcy system has proven sympathetic to taxing bodies, FN2 there are some individual Bankruptcy Code FN3 sections which serve inconsistent policies or are poorly drafted.

The National Bankruptcy Review Commission (the "Commission") has been charged with making a thorough review of the Bankruptcy Code. FN4 This Article will highlight some of the important state and local tax issues which the Commission should consider. Some of the issues will apply generally to all taxing entities, including the federal government. Ad valorem, FN5 and sales FN6 and excise FN7 taxes, however, are uniquely state and local taxes and, therefore, present issues that arise only at the local level.

Part I of this Article examines the classification and treatment of tax claims in bankruptcy. Specifically, it examines the various classifications which tax claims may receive in bankruptcy and how this classification affects the treatment of such claims. The treatment of trust fund taxes, secured tax claims, administrative claims, and priority taxes, in particular, present interesting issues which should be considered by the Commission. The discussion explores whether the existing treatment of tax claims makes sense and whether the statutes setting forth this treatment should be simplified or clarified. Part II focuses on issues involving state and local tax claims which are most often litigated. These issues include sovereign immunity and the Eleventh Amendment, third party injunctions and section 505 issues.

I. CLASSIFICATION AND TREATMENT OF STATE AND LOCAL TAXES

The favorable treatment given to tax claims under state law, FN8 often is carried forward into bankruptcy. Proper classification, however, is necessary to determine the treatment of a tax claim in bankruptcy. For example, tax claims in bankruptcy may receive favorable treatment as trust fund, FN9 secured, FN10 administrative FN11 or priority FN12 claims. The following discussion examines these types of claims in detail and reveals that in some instances the favorable treatment of tax claims is undermined by conflicting Code provisions.

A. Trust Fund Taxes

Simply defined, a trust fund tax is one that is collected or withheld from third parties and temporarily held in trust for the state. FN13 Common law recognized the trust fund nature of some taxes, FN14 and many states have subsequently enacted statutory provisions designating certain taxes as trust fund taxes. FN15 Perhaps the most well known example of a trust fund tax is the sales tax that businesses collect from their customers. Depending on the particular state statute, however, many different kinds of taxes may be considered trust fund taxes. FN16

The Bankruptcy Code currently contains two references to trust fund taxes. First, a positive reference is found in section 507(a)(8)(C), which accords trust fund taxes priority over certain other priority and unsecured claims without any limit on the date the tax liability is incurred. FN17 Second, a negative reference is found in section 541, which defines property of the estate as property *in which the debtor has an interest*. FN18 Under this definition, trust fund taxes are excluded from property of the estate. Taxes collected by the debtor are at all times property of the estate, and the debtor never has an interest in them. FN19 Accordingly, a debtor with sufficient cash on hand as of the petition date to cover all or part of a prepetition trust fund tax debt should be required to turn over such funds as nonestate property, together with accrued interest. FN20

In order to exclude trust funds from the bankruptcy estate, however, bankruptcy courts currently require evidence that the trust fund retains its character. This can be shown either by evidence that funds were kept in a segregated account, or if the debtor commingled tax trust funds in accounts with other funds, the trust funds must be traced back to their source. The tracing process is an accounting inquiry that identifies trust funds and traces their progress through the debtor's bank accounts. FN21 This process can be a cumbersome undertaking, especially with respect to large debtors that utilize several different banking institutions and accounts. Many states have statutory authority to require taxpayers to deposit trust fund taxes into a segregated account, thereby avoiding the tracing requirement. FN22 If tax funds are maintained in a segregated account, tracing is unnecessary, because any funds in the account should be deemed nonestate property payable to the proper tax authority. Although segregation is not a prerequisite to establishing a trust fund claim, FN23 it simplifies the identification and recovery of such funds.

Aside from problems which may be presented by the tracing process discussed above, the Commission should be aware that the determination that a tax is a trust fund tax has implications with respect to at least two other more discrete, but very practical, issues. First, because they are not property of the estate under section 541, FN24 trust funds cannot be the cash collateral **FN25** of secured lenders. It follows that trust funds should not be included as such in any cash collateral orders FN26 entered at or near the inception of the case. Many practitioners incorrectly assume that by including the trust funds in a cash collateral order, the funds (nonestate property) can be turned into estate property subject to cash collateral orders. Given the time it takes for tax authorities to become aware of the bankruptcy filing FN27 and initiate tracing procedures, the determination that trust funds exist is often made well after an initial cash collateral order has been entered. A practical solution to this problem exists, but is underutilized: where counsel know of or anticipate trust fund claims, they should simply include state tax authorities in cash collateral negotiations to avoid subsequent litigation about the effect a cash collateral order may have on nonestate property. FN28 With increasing frequency, state tax authorities are participating in cash collateral negotiations and hearings in an attempt to protect possible trust fund claims. Trust fund claims and state tax authorities' right to seek recovery thereon may be protected under cash collateral orders by simply providing for such in the language of the order. Unfortunately, the distinction between estate and nonestate property does not appear to be observed in many cases because parties are either busy with other aspects of cash collateral negotiation or because they simply do not choose to recognize that trust fund taxes are at stake.

The Commission should also keep in mind that a "trust fund" designation may result in personal ("responsible person") liability for certain individuals. **FN29** Any person receiving trust funds from the debtor who fails to pay such funds over to the state could be considered to have converted state property to their own use since the trust funds are state property. FN30 This may be true even in states that have not enacted trust fund statutes. FN31 While a taxpayer/debtor's officers or directors may immediately come to mind as possible candidates for responsible person liability, the language of many statutes is sufficiently broad to impose liability on anyone who eventually receives the funds, given adequate tracing. FN32

Such broad language has proved to be a problem for banks and other creditors who use "lock−box" arrangements with delinquent taxpayer/debtors. A "lock−box" arrangement is one in which a bank or other lender requires payments on the debtor's accounts receivable to be paid or deposited directly into an account in the lender's name. FN33 Often, a portion of the payments taken in under the lock−box arrangement represents taxes. A difficult situation arises if the taxes go unpaid because many state statutes would impose liability on the bank or creditor which had received the tax, plus any accrued penalty and interest. **FN34**

Addressing the security of trust fund tax claims in a separate section of the Bankruptcy Code is an option the Commission may want to explore. From a drafting standpoint, it would seem sufficient to exclude from property of the estate, property in which the debtor does not have an interest, as section 541 provides. Current practice, however, suggests that such an exclusion may not be an effective way to preserve trust fund tax claims, and protect funds that are not property of the estate, against dissipation. Even if trust funds should not be defined in the Bankruptcy Code (and the authors are not at all certain that additional special interest clutter is what the Bankruptcy Code needs), the Commission cannot thoroughly consider the Bankruptcy Code and the practice that has grown out of it without considering the impact of Code provisions on trust fund tax claims and state tax revenues.

B. Secured Tax Claims Protection of Tax Liens in Bankruptcy

Both in and out of bankruptcy, a lien is always a good thing to have. Many state and local taxes enjoy secured status so that, generally, if the debtor does not pay, the taxing authority can foreclose its lien and be paid out of the proceeds. FN35 Although status as a secured creditor has a positive effect on the taxing authority's treatment in bankruptcy, an important concern for the taxing authority in a bankruptcy proceeding is whether it can keep the liens it had when the case was filed and whether future claims will be secured. The answers to these questions depend upon the interaction between the Bankruptcy Code and state law. As a general proposition, prepetition tax liens which are perfected and which are protected against bona fide purchasers for value under state law will also be protected in bankruptcy. FN36 Tax liens may, however, be subordinated in chapter 7. FN37 In addition, although postpetition ad valorem taxes will continue to be secured claims in bankruptcy, FN38 most other tax claims will not. The following discussion will address the aforementioned issues and examine whether the Bankruptcy Code does an adequate job of protecting state and local tax liens.

1. Subordination in Chapter 7 Section 724(b)

As previously stated, tax liens generally are protected if perfection occurs before bankruptcy. FN39 The rules relating to treatment of secured tax claims are dramatically altered in chapter 7. First, the Code automatically avoids liens for noncompensatory penalties and subordinates these claims below the level of general unsecured creditors. FN40 Second, and more dramatically, when property subject to secured tax liens is sold in chapter 7, section 724(b) provides that the amount which would have been paid to secured tax liens becomes a fund for payment of priority and administrative claims prior to the satisfaction of the lien. FN41 The secured tax claims are relegated to a level below the lowest priority claims. This is a peculiar provision which conflicts with the general rule that taxing authorities are protected in bankruptcy. FN42 Two examples will illustrate the working of section 724(b):

Example 1. The debtor owns a piece of property which sells for $250,000.00. There are tax liens of $25,000.00 against the property. Other priority claims total $15,000.00. There is a secured lien of $230,000.00 against the property which is junior to the tax lien.

In this case, the first $15,000.00 of the proceeds would go to the priority claims under section 507(a)(1)−(7). FN43 The next $10,000.00 would go to the holder of the tax lien, because this is the amount by which the tax lien exceeds the priority claims. FN44 The remaining $225,000.00 would go to pay the secured lender. FN45 The $15,000.00 remaining from the tax lien claim would not be paid out of the sale proceeds and would be an eighth priority unsecured claim if last payable without penalty one year prior to the filing of the petition, or would be a general unsecured claim if last payable without penalty more than one year prior to the filing of the petition. FN46

Example 2. The debtor owns a piece of property which sells for $250,000.00. There are tax liens of $25,000.00. There are priority claims under section 507(a)(1)−(7) of $50,000.00. The secured lender has a claim in the amount of $230,000.00.

In this situation, the entire $25,000.00 attributable to the tax lien would go to pay the other priority claimants, because the priority claims were greater than the amount of the tax lien. FN47 The remaining funds would go to pay the secured lender. No money from the sales proceeds would go to the tax lien. **FN48**

Cases applying section 724(b) confirm that it allows property subject to tax liens to be sold without payment of what would ordinarily be first lien tax claims. FN49 This is contrary to the general rule under section 363 which states that in order to sell property free and clear of liens, secured creditors must either receive payment of the value of their lien or consent to the sale. FN50 Section 363(f)(5) does, however, allow property to be sold free and clear of liens if "such entity could be compelled in a legal or equitable proceeding to accept a money satisfaction of such interest." FN51 Accordingly, courts have held that section 724(b) is a provision which would, in essence, compel a taxing authority to give up its security interest even if no funds are actually paid to the taxing authority. FN52

Some courts have been reluctant to apply this unique provision. In *In re Dowco Petroleum, Inc.*, FN53 the bankruptcy court refused to apply section 724(b) until all of the unencumbered funds in the estate had been used to pay administrative and priority claims. FN54 The court stated:

As a result of the statutory scheme envisioned in section 724(b), the chapter 7 trustee is required to exhaust all unencumbered funds of the estate in the payment of administrative expenses before resorting to the priming option of taxing administrative expenses against the proceeds encumbered by a taxing entity's lien. The court is of the opinion that this conclusion is self−evident. If the estate contains enough unencumbered funds to satisfy administrative claims, no justification exists for priming a taxing entity's otherwise valid lien. FN55

Section 724(b) occupies a strange place in the Bankruptcy Code. Although the Code generally protects taxing authorities, FN56 the legislative history to section 724(b) confirms that Congress intended to "subordinat[e] tax liens to administrative expense and wage claims." FN57 Other evidence that this was the intended result is found in section 67c of the Bankruptcy Act which contained a similar provision, applying to liens for personal property taxes but not secured tax claims in general. FN58

The Bankruptcy Review Commission should carefully examine whether section 724(b) belongs in the Bankruptcy Code. This section dictates that tax liens which are enforceable under state law and which must be respected in chapters 11, 12 and 13, may be displaced to pay priority and administrative claims in chapter 7 proceedings. This represents a questionable policy decision, especially where section 506(c) already allows expenses directly benefitting a secured creditor to be paid from the creditor's collateral. FN59 It seems that there is greater justification for subordinating penalties under section 726(a)(4). FN60 Where there are insufficient funds to pay all claims, basic fairness seems to dictate that creditors should be paid compensation before penalties.

2. Postpetition Liens

Taxing authorities are "entities" subject to the automatic stay FN61 under Bankruptcy Code section 362(a). Therefore, the filing of a bankruptcy petition stays most actions aimed at collecting tax debts or enforcing tax liens. FN62 Among other things, the automatic stay prohibits "any act to create, perfect, or enforce any lien against property of the [e]state." FN63 This provision reinforces section 545(2) in that unperfected liens may be avoided under section 545, FN64 while section 362(a)(4) provides that liens which have not been created or perfected prior to bankruptcy cannot improve their position. **FN65**

However, as with many statutory provisions, there are exceptions. Section 362(b)(3) taken together with section 546(b) allows liens created prior to bankruptcy to be perfected postpetition if the lien would have received priority over intervening liens under state law. FN66 In other words, statutory liens with a relation back feature may be perfected postpetition. This exception applies primarily to state real property taxes, FN67 purchase money security interests FN68 and mechanics' liens. FN69

For many years, there was a debate over the extent of this exception. Many cases held that a property tax lien created prepetition could be perfected postpetition. FN70 Most cases, however, limited the exception and held that if the lien was not created prior to bankruptcy, it could not be perfected postpetition. FN71 At least one bankruptcy court, however, held that the statutory sections created a continuing exception that allowed property tax liens to be created and perfected from year to year. FN72 Recently, Congress resolved the debate in favor of ad valorem taxing authorities by enacting section 362(b)(18), a new exception to the automatic stay which allows "the creation or perfection of a statutory lien for ad valorem property tax imposed by the District of Columbia, or a political subdivision of a State, if such tax comes due after the filing of the petition." FN73 While the amendment effectively resolves the issue of property tax liens after its effective date, it does not affect the creation or perfection of other tax liens, such as those for state sales and income taxes. Most state sales and income taxes do not take priority over intervening liens and are not protected by section 546(b).

Ultimately, whether postpetition liens which are not protected by sections 362(b)(3) and (b)(18) survive depends upon the nature of the automatic stay. If a violation of the stay is void, it may be asserted by any party without regard to time. FN74 On the other hand, if violations of the stay are merely voidable, they must be avoided pursuant to Bankruptcy Code section 549. FN75 Only the trustee or debtor−in−possession may bring an action under section 549, **FN76** and such an action must be brought within two years. FN77 There is a significant split among the circuits as to whether actions taken in violation of the automatic stay are void or voidable. FN78 This area raises two questions for the Bankruptcy Commission. First, should protection for postpetition tax liens be extended to sales and income taxes,

as well as ad valorem taxes? There is an argument that section 362(b)(18) is special interest legislation and that in all fairness its protection should be extended to all taxes. On the other hand, the property tax is a tax against property itself and since the ad valorem tax is essentially an *in rem* tax, there is an argument for granting special protection to property taxes.

The second issue is whether the Commission should resolve the split of authority respecting the "void" or "voidable" nature of violations of the stay. Clearly, the stay should have the same effect in all circuits. FN79 The "void" rule applied by most circuits appears to be overly harsh, while the "voidable" rule followed by the minority encourages gamesmanship. FN80 One possible solution would be to provide that violations of the stay are void unless validated by the bankruptcy court.

4. Postpetition Charges to Oversecured Tax Claims Section 506(b)

Although secured tax claims generally are treated the same as other secured claims, the Code distinguishes between statutory and contractual claims when awarding postpetition charges to oversecured claims. Section 506(b) governs interest and other charges on secured claims. Under section 506(b), claims must be oversecured in order to receive interest and other charges. FN81 This can present a problem for the taxing authority because although many ad valorem taxes will be oversecured due to their superpriority lien status, tax liens which rely on a "first in time" priority scheme may be undersecured. FN82 Section 506(b) allows "interest on such claim, and any reasonable fees, costs or charges provided for *under the agreement* under which such claim arose." FN83 This language has raised the question of whether a lien which arises by operation of law is entitled to fees and costs under section 506(b).

Interpreting section 506(b), the Supreme Court, in *United States v. Ron Pair Enterprises, Inc.*, FN84 held that postpetition interest is available on all oversecured claims regardless of whether they arise by contract or statute. FN85 In *Ron Pair*, the Court made clear that recovery of other charges, such as penalties and attorneys fees, depended upon the existence of a contract. Since tax claims arise by operation of law, rather than under a contract, it is clear that accrual of penalty and attorney's fees on tax claims ceases upon the filing of a bankruptcy petition. FN86

The Commission should consider whether such disparate treatment is justified. Currently, section 506(b) allows oversecured creditors with contractual claims to recover their collection expenses out of their collateral, while denying the same privilege to governmental creditors. Taxing authorities incur collection costs and the penalties they assess are used to defer costs of collection. While there is a legitimate reason to deny or subordinate true penalties, this should not prevent recovery of actual collection costs. The Commission should consider whether section 506(b) should be modified to allow all oversecured creditors to recover reasonable costs of collection.

C. Administrative Claims

1. Determination of Administrative Status

Administrative claims are those expenses *incurred* by the bankruptcy estate. FN87 In determining the administrative status of tax claims, the major issue that arises is exactly when the tax is incurred. FN88 Depending upon the type of tax involved, different dates may be used to determine when the tax was incurred. Many states provide that ad valorem tax liability attaches on a specific date even though the amount of the tax is determined later. FN89 In these states, the entire tax is incurred by the prepetition debtor even though the case is filed mid−year. FN90 On the other hand, in some instances taxes measured by income or sales may be pro−rated between the estate and the debtor. **FN91** The Bankruptcy Code, however, expressly provides that income earned by the estate in an individual case under chapters 7, 11 or 12 shall only be taxed to the estate, FN92 while income earned during an individual chapter 13 case shall only be taxed to the individual debtor. FN93

Determining whether a tax is incurred by the prepetition debtor or the estate has created some confusion in the case law. Some decisions erroneously classified a tax *incurred* by the prepetition debtor as an administrative tax based on when the tax was *assessed*. FN94 This confusion arose because the definition of priority ad valorem tax claims refers to taxes assessed before the petition date. FN95 The problem may be avoided by changing the definition in section 507(a)(8)(B) to refer to taxes incurred prior to bankruptcy, so that the two sections are consistent.

2. Treatment of Administrative Claims Penalties and Interest under Section 503(b)(1)(C)

Administrative claims receive favorable treatment in bankruptcy. FN96 In reorganization cases, they must be paid in full for a plan to be confirmed, **FN97** and in a liquidation case, they are paid prior to any other unsecured claims. FN98 If administrative tax claims are not paid on time, any penalties accruing on them are also administrative claims. FN99 Although the statute does not specifically list interest on postpetition taxes as an administrative claim, most courts have found the right to postpetition interest to be implied. **FN100** The Bankruptcy Commission may help to clarify this statute by recommending that Bankruptcy Code section 503(b)(1)(C) specifically allow recovery of interest. On the other hand, the Commission should consider whether penalties, which are expressly provided for, should be included. While federal law has a strong policy in favor of paying taxes incurred after bankruptcy, adding both penalties and interest onto late−paid administrative taxes tends to overcompensate the taxing authority and penalize unsecured creditors. FN101 The Commission should recommend that both oversecured taxes and administrative taxes receive uniform treatment in bankruptcy. In both cases, full compensation is justified, but the wisdom of allowing true penalties to be paid ahead of unsecured creditors is questionable.

D. Priority Taxes

Priority taxes are governed by some of the more difficult sections of the Bankruptcy Code. In particular, section 507(a)(8), which defines priority tax claims, FN102 is unusually complex, and section 1129(a)(9)(C), which governs treatment of priority tax claims in chapter 11, FN103 is difficult to apply. Both of these sections are discussed in detail below.

1. Classification of Priority Claims Section 507(a)(8)

Bankruptcy Code section 507(a)(8) defines seven categories of "unsecured claims of governmental units" FN104 as priority claims, including, among others, FN105 income taxes, excise taxes and claims to trust fund taxes. These three priority tax claims present interesting issues that arise with respect to their recovery in bankruptcy which are of particular concern to state and local taxing authorities.

a. Income Taxes Section 507(a)(8)(A)

Income taxes must meet one of the categories set forth in section 507(a)(8) in order to be entitled to priority status. FN106 The first category requires that if the debtor's income tax liability is based on a return, the return must have been due, regardless of when it was actually filed, no more than three years before the bankruptcy petition was filed. FN107 The second category grants priority to taxes "assessed" within 240 days before the filing of the petition. **FN108** This permits income taxes that are more than three years old to receive priority treatment if such taxes are assessed within 240 days before the petition is filed. FN109 Practitioners should be aware, however, that the term "assessed" has a different meaning among various taxing authorities. The definition of "assessed" is not found in the Bankruptcy Code, and the meaning of the term depends upon the state statute providing for the assessment. FN110 Practitioners also should be aware that there is a controversy over whether the three year and the 240 day time periods may be extended where there is a prior bankruptcy. FN111

The third and final category, section 507(a)(8)(A)(iii), allows priority treatment for income taxes assessable postpetition. FN112 Specifically, income taxes not assessed before the commencement of the bankruptcy case, but which become assessable "under applicable law" after the commencement of the case, are entitled to priority treatment. FN113 This has been interpreted by courts to mean that state law applies for purposes of determining when a tax is "assessable." FN114

Section 507(a)(8)(A)(iii), however, contains a curious exclusion. Specifically, it excludes claims "of a kind specified in sections 523(a)(1)(B) or 523(a)(1)(C)" of the Code. FN115 Sections 523(a)(1)(B) and 523(a)(1)(C) do not allow tax claims to be discharged if: (1) the tax return was not filed, **FN116** (2) the tax return was filed late and was filed within two years before bankruptcy, FN117 (3) the debtor filed a fraudulent return, FN118 or (4) the debtor willfully attempted in any manner to evade the tax. FN119 Read literally, these provisions provide that if a debtor engages in one of the specified types of misconduct, the tax claim will be excluded from priority treatment and will be treated as

a general unsecured claim, but will be nondischargeable. Courts applying this section confirm this result. FN120

Apparently, Congress sought to coordinate exceptions to discharge and priority provisions. By excluding late returns and willful evasion claims from priority treatment, Congress insured that nondischargeable taxes based upon unassessed liabilities would only fall under one of the grounds for nondischargeability. There was, however, no reason to do so because a tax claim may be nondischargeable for more than one reason. For example, if a tax return was due less than three years before bankruptcy, the debtor filed his return less than two years before bankruptcy and the return was fraudulent, the debt would be nondischargeable under all three subsections of section 523(a)(1). There is no conflict in finding that a claim is nondischargeable on multiple grounds. As a result, the Commission should recommend that Congress eliminate the exclusion from section 507(a)(8)(A)(iii). Even with this revision, section 507(a)(8)(A) would still be complicated. The remaining complexity, however, is necessary to grant priority in three distinct situations. It would be difficult to simplify the statute further without diminishing its coverage.

b. Claims to Trust Fund Taxes Section 507(a)(8)(C)

Section 507(a)(8)(C) gives priority to claims for taxes "required to be collected or withheld and for which the debtor is liable in whatever capacity." **FN121** These taxes are commonly known as "trust fund" taxes. FN122 Even though the statute includes *claims* for taxes required to be withheld, it does not include claims to the actual trust funds themselves. Trust funds are excluded from property of the estate, FN123 and therefore, a claim to recover trust funds still held by the debtor is a claim for recovery of a third party's property and is not subject to the rules governing priority tax claims. Furthermore, section 507(a)(8)(C) applies to amounts owed "in whatever capacity," which includes responsible party liability. FN124 If both a corporation and a responsible person file bankruptcy, the same taxes will be a priority claim in both bankruptcies. Thus, section 507(a)(8)(C) applies where the trust funds have been depleted prior to bankruptcy or where a third party, such as a corporate officer, is held liable for the failure to pay over trust funds.

Section 507(a)(8)(C) is distinguishable from several of the other types of priority tax claims because it does not contain a time limit: taxes required to be withheld are priority claims, regardless of when they arise. This apparently reflects a policy judgment that parties who breach a fiduciary duty to withhold trust fund taxes should not escape liability due to the mere passage of time. This, however, can have a harsh result in individual cases, since priority tax claims are not dischargeable in chapter 7 FN125 and, in other chapters, must be paid in full in order to confirm a plan of reorganization. FN126 Although it would be tempting to place a time limit on the priority status of trust fund tax claims so that they are structured similarly to the other subsections, this would be a marked shift in policy.

It is worthy to note that under the Bankruptcy Code there is no responsible person liability for unpaid unemployment taxes. As to the corporation, un−employment taxes are covered by section 507(a)(8)(D), FN127 which does not impose responsible person liability. Even if a corporate officer is held liable for the taxes, they should not be a priority claim in the officer's bankruptcy because the underlying taxes are not based on wages earned "from the debtor," as is required under section 507(a)(8)(D). Rather, the corporate officer's liability arises because of the respective statute imposing the corporate officer liability. FN128

c. Excise Taxes Section 507(a)(8)(E)

Taxes levied on transactions or for certain privileges are usually specified by statute as "excise taxes." FN129 Although the Bankruptcy Code does not define the term "excise tax," they include almost all taxes that are not income, sales or property taxes. Whether a tax is an "excise" tax does not depend on the label placed on it by the state. Rather, an independent determination of the nature of nonfederal excise taxes is made. FN130 The definition of "excise" tax has been interpreted to be broad enough to include many different types of taxes and assessments. FN131 At least one court, however, has held that section 507(a)(8)(E) is limited to excise taxes on transactions. FN132

In order to be granted priority under section 507(a)(8)(E) excise taxes on transactions must arise within three years prior to bankruptcy. FN133 Where the payment of the tax does not require the filing of a return, an excise tax is a priority tax if the event generating the tax occurs prepetition. FN134 This is important because if the tax is due postpetition, even though the taxable event occurs prepetition, the state taxing authority may argue that the tax is a

postpetition administrative expense entitled to the highest priority under section 507(a)(1). If a return is required, however, then the corresponding tax is classified under subparagraph (E) only where the due date for the return (whether the tax is paid before the due date or after) falls on a date within three years of filing of the bankruptcy petition. FN135

2. Treatment of Priority Tax Claims in Chapter 11

Treatment of priority tax claims is more complicated in chapter 11 than in other chapters of the Bankruptcy Code. FN136 In order to confirm a chapter 11 plan, except to the extent that a priority tax creditor agrees otherwise, the claim must receive "on account of such claim deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim." FN137 Chapter 11's requirements have raised various issues, such as whether priority tax claims are entitled to vote upon a plan, what it means to receive deferred cash payments, how long payments may be stretched out, and what interest rate must be paid. These issues are discussed below.

a. Voting Class Treatment

The role of voting by priority tax creditors under the Bankruptcy Code is not well understood. The Code provides that all creditors with allowed claims under section 502 may vote. FN138 However, because priority tax claimants may not be classified, FN139 they may not vote by class. This is consistent with the language of section 1129(a)(9) which states that "the holder of a particular claim" may agree to nonconforming treatment. FN140 Because priority tax claimants do not vote by class, they may not constitute an accepting impaired class under Bankruptcy Code section 1129(a)(10), and therefore, their rejection would not require the debtor to proceed to cramdown. FN141 Thus, voting by priority tax creditors serves only to indicate whether they consent to treatment other than provided in section 1129(a)(9)(C).

Priority tax claims, must be treated on an individual basis because the Code does not allow for their classification. This seems to allow a debtor to provide dissimilar treatment to similar claims, for example, by paying one tax claim in cash, paying a second out over twelve months, and paying a third over the maximum period allowed by the Code. In fact, different treatment may be mandated by the Code. There is nothing to stop the debtor from treating each creditor over a different time period because section 1129(a)(9)(C) only requires payment within six years from assessment. FN142

There does not appear to be any compelling logic in favor of this system. The present system excludes priority tax creditors from voting, except to require the minimum treatment required by statute. However, if priority tax creditors were allowed to vote as a class, the debtor might be motivated to negotiate for treatment which was better than the minimum standard in order to obtain a consenting class. Thus, priority tax claimants could well benefit from being enfranchised in chapter 11 proceedings.

In order to implement a system of class voting by priority tax claimants, it would be necessary to remove the prohibition against classifying priority tax creditors and place treatment of priority tax claims in the section on cramdown. In so doing, priority tax claimants would gain the protection of section 1129(b)(1), which prohibits unfair discrimination. FN143 It would also be necessary to amend section 1129(a)(9)(C) to allow for uniform treatment of priority tax claims. FN144

b. Deferred Cash Payments

The requirement of deferred cash payments imposed by section 1129(a)(9)(C) gives rise to several issues. For instance, what are deferred cash payments? How many must be made in order to qualify as "deferred"? Congress has established a six year period, beginning at the date of assessment, over which a tax claim must be satisfied. FN145 However, since the frequency of the cash payments remains unclear, and courts have done little to resolve the confusion, practitioners will continue to struggle with this phrase.

Courts take two approaches in defining "deferred cash payments." Some courts read the phrase restrictively and hold that unless the debtor faces circumstances that require another payment schedule, the debtor's plan must provide for equal monthly payments. FN146 This reasoning favors the taxing agency, which does not want to lose its priority status while financing the debtor's reorganization. FN147

Other courts take a more liberal approach and read the phrase broadly so as to give the debtor more flexibility. FN148 This reasoning is based, in part, on the courts' consideration of the basic objectives of reorganization, including "business preservation and creditor satisfaction." FN149 One court noted that a flexible reading of Bankruptcy Code section 1129(a)(9)(C) is consistent with its legislative history. FN150 While these rulings may help a debtor regain its financial strength, they also may defer payments which the debtor ultimately may fail to pay.

In reviewing section 1129(a)(9)(C), Congress should consider its objective in providing for payment of priority tax claims. Currently, the courts offer opposing views, leaving the debtor and the taxing authority to wrestle in court.

c. Length of the Payment Schedule

As was previously discussed, section 1129(a)(9)(C) prohibits a chapter 11 debtor from stretching payments on a priority tax claim over more than six years from the assessment date. FN151 Specifically, two problems with the language of this section have produced much litigation. First, the phrase "date of assessment" is not defined in the Code. The determination of this date is of great importance because the six year period is measured therefrom. **FN152** Second, due to the nature of the taxes, debtors often incorrectly compute the payment schedule and fail in efforts to adhere to the six−year payout requirement.

Assessment generally refers to the process of fixing liability for the tax. **FN153** The meaning of "assessment" turns on the type of tax at issue. For instance, the "date of assessment" for sales taxes and payroll taxes could be the date that the taxes are collected or withheld. FN154 This reasoning, however, can create an administrative nightmare for businesses trying to determine the due date for every sales tax collected and every income tax withheld, so as to comply with Bankruptcy Code section 1129(a)(9)(C).

Typically, businesses summarize monthly sales and payroll in a report submitted to the state by a specified date in the following month. FN155 As a result, the "date of assessment," may logically be the date on which the taxes (withheld or collected) are required to be paid over to the taxing authority. Therefore, in a bankruptcy setting, the "date of assessment" can be said to occur on the day taxes are due. Such reasoning is consistent with the flexible standards called for by the courts FN156 and is likely to address situations where additional taxes are assessed at a later date.

While the definition above may resolve some of the confusion, Congress can revise the Code to remove the ambiguity. Specifically, the Commission could suggest that the phrase "date of assessment" be replaced with "the date upon which the taxes are originally due to the taxing authority under applicable nonbankruptcy law." Even if the meaning of "assessment date" is clarified, however, the statute will remain unworkable because computing the expiration of the six year period following the date of assessment for each tax would be an accounting nightmare. Further, determining the monthly payments would be even more demanding as each payment must include a portion of the outstanding balances of the unpaid tax claims. FN157 Although not a panacea, one way to solve the computation problem is to use the median expiration date for all tax claims. First, the debtor must compute the number of months from the effective date of the plan to the expiration of the six−year period for each tax claim. Next, the debtor finds the median expiration period. Regardless of when the six−year period may expire for the various claims, the debtor can propose to satisfy the total liability over this median period. FN158 A far more workable solution, however, is to require that taxes be paid within a fixed period after the effective date. This is comparable to the requirement in chapters 12 and 13 that priority tax claims be paid over the life of the plan. FN159

d. Valuation and Interest rates

Like the other elements of Bankruptcy Code section 1129(a)(9)(C), the "present value" requirement is a source of much debate among practitioners and the courts. FN160 The various decisions addressing the "present value" requirements are uniform in two areas. First, the decisions agree that payments on chapter 11 priority tax claims must

include interest that will preserve the present value of the claims. FN161 Second, the decisions agree that the interest rate should be the prevailing market rate on the effective date, for a loan with similar payment terms, with due consideration of the quality of the security and the risk of subsequent default. FN162 Finding the applicable "market rate," however, remains a considerable source of debate. FN163 Some have argued that the rate is easily ascertained by turning to prescribed interest rates set forth in the applicable tax code. FN164 This position has some merit because, in essence, the government is being forced to finance the debtor's reorganization. Courts have been reluctant to adopt this stance, however, because the prescribed interest rates often have little to do with market conditions. FN165 Other examples of "market rates" are the prime rate and rates on treasury bills and bonds. FN166

Courts have considered several factors in selecting a market rate. The prevailing market rate must reflect the financial environment at the time of reorganization, FN167 and courts must weigh the quality of the security and the risk of default. FN168 Some courts add a "risk factor" to compensate for the unsettled financial condition of the reorganizing debtor and the lack of security. FN169 The market rate applied, however, should *not* take into account the "rehabilitation aspects" of the debtor's plan of reorganization. **FN170**

The uncertainty and disagreement regarding the "present value" language of section 1129(a)(9)(C) provide some temptation to alter that language. Much of the uncertainty would be removed by adopting a fixed standard such as the treasury bill rate for a similar period, or the rate applicable under nonbankruptcy law. However, any fixed rate ultimately would end up being higher or lower than a comparable market rate and would shift value from debtors to taxing authorities or vice versa. Any attempt to set specific variables in determining a market rate would probably only codify existing law and involve intangible factors. While the current standard may be imprecise, at least it is familiar. FN171

The Commission should address the problems with section 1129(a)(9)(C), which, in its current form, is overly complicated and generally unworkable. The simplicity of similar provisions in chapters 12 and 13 would provide a good model for amending chapter 11. FN172 A simpler statute will help to avoid lengthy confirmation battles which only add to the expense of chapter 11 proceedings.

II. LITIGATING WITH TAXING AUTHORITIES

In the past, debtors and trustees have paid little attention to state and local taxing authorities. However, with the abrogation of sovereign immunity, **FN173** the use of the section 105 injunction to prevent collection of taxes from responsible third parties, and the increasing use of Bankruptcy Code section 505, FN174 practitioners are more likely to find themselves in litigation with state and local taxing authorities.

A. Sovereign Immunity and the Eleventh Amendment

Prior to 1994, the availability of sovereign immunity as a defense to bankruptcy court action against state and federal governmental units was hotly debated. By including section 106 in the Bankruptcy Code, Congress intended to limit the availability of sovereign immunity under certain circumstances. FN175 However, the extent of that statutory limitation and the circumstances in which it was to be applied were unclear, giving rise to all manner of litigation. By 1992, it was clear that former section 106 was not the limitation on sovereign immunity that many people thought. FN176

In 1994, Congress amended section 106 to make the limitation of sovereign immunity and the circumstances in which it applies explicit. FN177 The new language leaves little room for argument about the abrogation of sovereign immunity with respect to the enumerated sections of the Bankruptcy Code. However, section 106 is effective only with respect to the sovereign immunity enjoyed by the federal government; it does not abrogate the immunity of the states, which is constitutionally guaranteed by the Eleventh Amendment to the United States Constitution. FN178 As state tax authorities become more active in bankruptcy cases, Eleventh Amendment issues will continue to arise more frequently. FN179

Although sovereign immunity and Eleventh Amendment immunity are often discussed interchangeably, FN180 the two doctrines are not identical. Sovereign immunity, which is enjoyed by the federal government, is a

judicially−created doctrine of governmental immunity. FN181 Because it is not constitutionally guaranteed, sovereign immunity may be waived *via* congressional action. FN182 Congressional waivers, which are narrowly construed, may not be implied and are only effective if "unequivocally expressed." FN183

Unlike sovereign immunity, the immunity granted the states under the Eleventh Amendment is constitutionally guaranteed. FN184 In order to abrogate a State's immunity from suit in federal court, Congress must make the abrogation "unmistakably clear in the language of the statute" FN185 and must act "pursuant to a valid exercise of power." FN186 Congressional abrogation in statutes enacted pursuant to the Fourteenth Amendment has been held constitutional, because the provisions of the Eleventh Amendment are necessarily limited by those of a later amendment. FN187

Congressional abrogation of States' immunity in statutes enacted pursuant to antecedent Constitutional provisions such as Article I, has been a more difficult issue for the Supreme Court. The Court held previously that Congress may abrogate Eleventh Amendment immunity when legislating pursuant to the Commerce Clause. FN188 The Court specifically left open the question of whether Congress could legislate pursuant to the Bankruptcy Clause, FN189 and the validity of the antecedent provision analysis itself was considered questionable. FN190 Thus, whether Congress could abrogate Eleventh Amendment immunity pursuant to the Bankruptcy Clause (*i.e.*, in section 106 of the Bankruptcy Code) remained an open question. FN191

On March 27, 1996, the Supreme Court answered that question in *Seminole Tribe of Florida v. Florida*, FN192 stating that "[t]he Eleventh Amendment restricts the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction." **FN193** Although the case at bar involved abrogation under the Indian Commerce Clause, FN194 the Court's holding is clearly applicable to the Bankruptcy Clause, as well as any other Congressional power contained in Article I of the Constitution. FN195 Under the reasoning of *Seminole Tribe*, section 106 of the Bankruptcy Code, which was enacted pursuant to an Article I grant of power, cannot be used to abrogate immunity guaranteed the States under the Eleventh Amendment. Accordingly, section 106 operates as a limitation on the assertion of sovereign immunity by the federal government, and does not affect the immunity of the several states.

The holding in *Seminole Tribe* merits serious consideration. FN196 The implications of the decision go far beyond the Seminole Tribe's inability to sue the State of Florida under the Indian Gaming Regulatory Act. Instead, the decision calls into question any federal statute enacted pursuant to an Article I grant of power which purports to create federal court jurisdiction over a State that has not consented to be sued. With respect to bankruptcy, the decision appears to eliminate the availability of sanctions against an unconsenting State for violations of the automatic stay. FN197 Because bankruptcy courts may not use contempt power to punish a statutory violation, **FN198** there may be no way to sanction an unconsenting State for stay violations. Instead debtors may be limited to filing an action to obtain injunctive relief with respect to future violations, FN199 or actions to subordinate State claims under section 510(c) of the Bankruptcy Code. FN200

The Commission should evaluate the impact of this dramatic Supreme Court decision on the entire bankruptcy system while undertaking its review of the Bankruptcy Code. As noted elsewhere in this Article, state tax authorities have just begun to see that there is a significant monetary recovery to be gained through the bankruptcy courts. It is highly unlikely that these entities will begin to violate the automatic stay as a matter of course and ignore the provisions of the Bankruptcy Code altogether, so the effect of *Seminole Tribe* on the bankruptcy practice may be limited. Even so, the Commission may have to examine those provisions of the Bankruptcy Code that most affect the States and determine if those provisions remain effective with respect to unconsenting states in light of the Court's decision. FN201

B. Third−Party Liability and the Section 105 Injunction

One aspect of state tax law frequently litigated in bankruptcy court is responsible person or third party liability for a debtor's unpaid taxes. FN202 Often, when a corporation or partnership fails to pay state taxes, state tax authorities affected by the default are faced with collecting the unpaid taxes from a business that is financially unsound at best, or, at worst, completely worthless.

It is logical that state legislators would look to these "responsible persons" as an alternative collection source because corporations can act only through corporate officers and directors, and partnerships only through partners. Most states FN203 have enacted provisions making these parties liable for unpaid taxes, either by creating a trust relationship with the state FN204 or by placing responsibility for such unpaid taxes on those parties under a duty to file and pay the taxes in the event they are not paid. FN205 Although some statutes are narrowly drawn, FN206 most provide that "any person" charged with the duty of collecting or receiving a tax who fails in that duty will be personally liable. FN207

States that seek collection from nondebtor "responsible parties" are sometimes faced with the threat of a bankruptcy court injunction against the collection of such liability from responsible persons considered vital to the reorganization effort. FN208 As a general rule, the Bankruptcy Code does not stay actions against third parties. FN209 Nonetheless, injunctions under section 105 are sometimes used for this purpose. The use of section 105 injunctions was pioneered in mass tort cases where the debtor's officers and directors faced thousands or even hundreds of thousands of suits. FN210 Section 105 also has been used to protect guarantors and other codebtors in nontort cases, FN211 as well as to protect "responsible parties" from taxing authorities. FN212

Mass tort cases provide a poor analogy for offering protection to nonbankrupt responsible parties because mass tort cases involve many thousands of individual claims, whereas generally there are only a limited number of taxing authorities seeking to collect from a limited number of responsible parties. Guarantor cases, on the other hand, provide a closer fit. In both cases, the primary obligor may be able to pay the debt if the reorganization succeeds. The reorganization may fail, however, if the creditor forces the guarantor/responsible party into his or her own bankruptcy. Thus, a section 105 injunction against enforcing responsible person liability may avoid a second bankruptcy filing while increasing the possibility that the primary obligor will pay the debt. FN213

Regardless of whether the courts should extend protection to nonbankrupt responsible parties, there are currently restrictions on the court's ability to do so. The Tax Injunction Act FN214 provides that "[t]he district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." FN215 Bankruptcy courts derive their jurisdiction from the district courts under 28 U.S.C. § 1334, and therefore, the Tax Injunction Act deprives the bankruptcy court of jurisdiction over the collection of the tax from nondebtors, assuming that the state involved provides a "plain, speedy and efficient" remedy to the taxpayer. FN216

The Bankruptcy Code also places limits on the use of section 105 to enjoin collection of responsible person penalties. FN217 Section 105 does not supersede the Anti−Injunction Act, FN218 nor does it create substantive rights and/or authorize activity that is otherwise unsupported or prohibited by law. **FN219** Thus, before section 105 may be invoked, there must be some showing that the relief requested is authorized by the Bankruptcy Code.

The Code generally does not support extending bankruptcy court jurisdiction over nondebtor tax liability, FN220 and many sections of the Bankruptcy Code specifically limit their reach *to the debtor*. FN221 Although early cases indicated otherwise, it has become clear that section 505 of the Bankruptcy Code generally does not authorize a bankruptcy court to determine the tax liability of nondebtor parties. FN222 Nor does the automatic stay of section 362 contain any protection for nondebtor third parties, as it is limited by its terms to acts against the debtor or the debtor's property. FN223 The Bankruptcy Code also limits any efforts to discharge nondebtor liability through section 524(e) which provides that, except under enumerated circumstances, FN224 the discharge of a debtor's debt does not affect the liability of any other entity on, or the property of any other entity for, such debt. FN225 Section 524(a)(2) provides that a discharge "operates as an injunction" against the collection of debts whether or not discharge of the debt has been waived. FN226 The effect of section 524 as a whole is to prohibit the issuance of a permanent injunction against the collection of a debt from a nondebtor third party. FN227 Section 524(a) describes the discharge as an injunction, and section 524(e) specifically limits the discharge to the debtor.

The law in this area appears to be clear that bankruptcy courts cannot, either through a plan of reorganization or an adversary proceeding, issue an injunction to prevent the assessment or collection of delinquent state taxes from nondebtor third parties in nonmass−tort cases. FN228 However, this continues to be an area of controversy, as shown by repeated attempts to gain protection for nonbankrupt third parties. The Commission should consider this issue, as well as the basic principles of federalism, when evaluating the effectiveness of the Bankruptcy Code. Allowing

protection of third parties is a departure from the general principles of the Code and such protection conflicts with the Anti−Injunction Act. The Commission should make a clear choice either to endorse these policies or amend them.

FN229

C. Section 505

Bankruptcy Code section 505 allows the bankruptcy court to "determine the amount or legality of *any* tax, any fine or penalty relating to a tax, or any addition to tax." FN230 This innocuous language was intended to allow expedited determination of tax claims. FN231 In practice, however, the statute promotes forum shopping and reopening of tax matters which are closed under nonbankruptcy law.

1. Scope of Section 505

Although the use of the word "any" in section 505 appears to suggest that an almost unlimited variety of tax disputes may be resolved in bankruptcy court, **FN232** there are three limits on the court's power under section 505: jurisdictional limits, FN233 limits on matters "contested and adjudicated," **FN234** and discretionary limits. FN235

Despite the use of the word "any" in section 505, bankruptcy courts still must have jurisdiction under 28 U.S.C. § 1334 before determining a tax issue. Section 1334 requires that a matter be a civil proceeding arising under title 11, or a civil proceeding arising in or related to a case under title 11. FN236 Generally, the bankruptcy court has jurisdiction over a proceeding if "`that proceeding could conceivably have any effect on the estate being administered in bankruptcy.'" FN237 As broad as this may seem, there are limits. First, the bankruptcy court generally may not determine the tax liability of nondebtors. FN238 Some courts have, however, exercised jurisdiction over third party tax claims where it will affect the bankruptcy estate or the ability to reorganize. FN239 The second limitation is that the tax liability must not have been "contested and adjudicated" before bankruptcy. **FN240** Tax issues which were never pursued prior to bankruptcy, FN241 claims lost due to default, FN242 and matters which are still pending when the case is filed FN243 are all subject to determination under section 505. Thus, some issues which are final under state law may be resurrected in bankruptcy court. On the other hand, where proceedings are pursued partway through the system and then dropped, redetermination is not allowed. FN244 Similarly, appeals or protests determined by an agreed order prior to bankruptcy remain final. **FN245**

Surprisingly, tax issues which are litigated and decided *postpetition* may still be subject to redetermination in the bankruptcy court. FN246 These matters still may be determined under section 505 because they were not adjudicated *before* the commencement of the case. Simply because the court may determine these issues, however, does not mean that it should.

The broad grant of jurisdiction in section 505 is balanced by one word in its text. The statute provides that the bankruptcy court "may" determine tax issues. FN247 This implies that in appropriate circumstances, the bankruptcy court may choose not to hear a case. FN248 Discretionary abstention under 28 U.S.C. § 1334(c)(1) may be appropriate where there is a prior pending state court action. FN249 Although the statutory text of section 505(a) would not prevent redetermination under these circumstances (because the adjudication would not be final), judicial economy may indicate that the pending action should go forward. Abstention also may be appropriate based upon difficult issues of state law FN250 or lack of benefit to the estate. **FN251**

Abstention may also be proper where postpetition taxes are concerned. Several courts have held that section 505 may be used to redetermine postpetition taxes. FN252 However, there are strong arguments to the contrary. Under 28 U.S.C. §§ 959 and 960, the debtor−in−possession or trustee is required to operate the property of the estate in compliance with valid state laws. FN253 Furthermore, under the Bankruptcy Act section 93(j), the trustee's acts of misfeasance or nonfeasance did not exempt the bankruptcy estate from state tax liability. FN254 In addition, the "contested and adjudicated" standard of section 505 is intended to insure that the debtor has at least one opportunity to litigate a tax claim on the merits. However, the cases allowing redetermination of postpetition taxes allow the debtor/trustee to litigate in one forum and then seek a different ruling in bankruptcy court. FN255 While the statutory language may permit this result, it is not a good way to run a court system.

2. Redetermination of Property Tax Values

There is a significant question as to whether section 505 should ever be used to redetermine property tax values. FN256 While section 505 allows the bankruptcy court to determine all facets of tax liability, FN257 the Supreme Court's decision in *Arkansas Corp. Commission v. Thompson* FN258 and a cryptic note in the legislative history appear to place limitations on valuation issues. FN259 *Arkansas Corp.* contained two major holdings. First, it held that the Court would not review a state court determination of ad valorem taxes which was not appealed. FN260 The second holding of *Arkansas Corp.* stated that where the state had established a specialized mechanism for valuing property for purposes of ad valorem taxation, the bankruptcy court should not interfere with the uniform state system. FN261 The Supreme Court stated:

Bankruptcy and reorganization proceedings today cover a wide area in the business field. But there is nothing in the history of bankruptcy or reorganization legislation to support the theory that Congress intended to set the federal courts up as super−assessment tribunals over state taxing agencies. The express legislative purpose of Arkansas to move towards a more nearly uniform and fairly distributed tax burden through relying on supervision by a single agency could be in large part frustrated by the construction of the Bankruptcy Act for which the trustee here contends. Section 64, sub. a, thus construed, would tend to obstruct, and not to facilitate, the enforcement of state tax laws. Nothing in the language of the Act requires such a construction. And the policy of revising and redetermining state tax valuations contended for by the trustee would be a complete reversal of our historic national policy of federal non−interference with the taxing powers of states. FN262

The legislative history to section 505 indicates that the second holding of *Arkansas Corp.* "remains as good law to permit abstention where uniformity of assessment is of significant importance." FN263

The question then becomes whether valuation of property for purposes of ad valorem taxation is a situation where uniformity of assessment is of "significant importance." Two courts which squarely addressed the issue ruled that because valuing property does not involve assessment, abstention is improper when a debtor requests redetermination of property tax values. FN264 In one of these cases, the court stated:

Today, abstention from deciding a tax adjudication question under [s]ection 505 is only appropriate upon a showing that uniformity of assessment is of significant importance. No such showing has been made here. If the tax rate were the subject of this motion, perhaps abstention might be appropriate. Because the trustee only challenges the excessiveness of the appraisal district's valuation of the estate's property, the taxes to be paid by other taxpayers will not be affected, nor will uniformity of assessment be placed in issue (*i.e.*, the overall valuation methodology used by the appraisal district is not being generally attacked). Because uniformity of assessment is not at issue, the taxing authorities' arguments on this point must be rejected. **FN265**

This court's reading of *Arkansas Corp.* and the definition of "assessment" may be open to criticism. FN266 The court read the term "assessment" narrowly. In the context of the state tax code under which that case was decided, assessment refers to setting tax rates, FN267 whereas *Arkansas Corp.* used the term in a broader sense. The specific facts in *Arkansas Corp.* refer to the use of a specialized tribunal to set property tax values. FN268 The Supreme Court stated that it was not Congress's intent to set up federal courts as "super assessment tribunals" FN269 over state agencies where the state had created a uniform administrative system. In many states, the term "assessment" refers to both setting values and tax rates. **FN270** One of the definitions of "assessment" in *Black's Law Dictionary* explains assessment as the "listing *and valuation of property* for the purpose of apportioning a tax upon it, either according to value alone or in proportion to benefit received." FN271

While there may be grounds to question redetermination of property tax values, **FN272** the cases are uniform in allowing this practice. FN273 This inconsistency may have resulted from the fact that pre−Code law, upon which Congress relied when drafting the Code, is inconsistent as well. While the *Arkansas Corp.* Court criticized federal interference in local valuation decisions, other cases applauded it. One circuit court decision hailed redetermination under the Bankruptcy Act (the "Act") as a means to protect creditors from incompetent or dishonest managers who might seek to artificially inflate their property tax values. FN274 This court found that,

[the Act] should be construed as a remedial effort, designed to alleviate an unfortunate situation in which bankrupts and their creditors are placed. This situation is well−described in *Collier on Bankruptcy*:

"Debtors financially involved are not always vigilant in the exercise of their rights to challenge tax claims or secure abatements; their managements may be inept, incompetent, uninterested, or dishonest; indeed, they may be under pressure to accept over−assessments which may aid in maintaining their credit standard or commercial rating."

The [Act], by authorizing redetermination in those instances where the tax claim was never appealed, serves to protect creditors of the bankrupt from the bankrupt's lack of diligence or interest. FN275

The Commission should reconsider which policy should be adopted in section 505. If the Commission agrees that redetermining property tax values constitutes "a complete reversal of our historic national policy of Federal noninterference with the taxing powers of the State," FN276 then it should prohibit the practice. However, if the Commission agrees with the bankruptcy courts which have allowed the practice, the Commission should consider whether property tax values should be removed from section 505 and codified as an avoiding power. The existing avoiding powers are either based upon state law rights or have strict time limits. FN277 Section 505 contains neither limitation. It is likely that section 505 can be used to avoid property tax values which are final under state law and may reach back as many years as the court's discretion will allow. FN278 Another possibility would be to allow redetermination of property values, but only as part of the claims allowance process. In other words, the court could determine the property valuations (and thus the amount of tax owed) on taxes which were still owing, but could not force a refund of taxes paid under prepetition valuations.

CONCLUSION

The Bankruptcy Review Commission will have its hands full as it seeks to review and overhaul the Bankruptcy Code. Many parties and interest groups will try to pull the Commission in one direction or another. However, in performing their task, the members of the Commission have an opportunity to bring greater consistency and clarity to bankruptcy tax policy.

The tax issues to be addressed by the Commission range from the major to the mundane. In the area of trust fund taxes, the Commission should consider whether the exclusionary language in section 541(d) is adequate to remove taxes held in trust from the reach of other creditors or whether specific language addressing trust funds should be added. Furthermore, secured tax creditors would benefit from the repeal of section 724(b), a perverse subsection which subordinates tax liens for no apparent reason. Tax creditors would also benefit from a redrafting of sections 503(b) and 506(b) to clarify that administrative tax creditors are entitled to interest on their claims and oversecured claimants may recover reasonable collection costs in addition to interest. With respect to priority tax claims, the Commission should address the issue of whether taxing authorities should be allowed to vote by class and should look for ways to simplify section 1129(a)(9)(C).

The Commission should also examine other areas that have caused considerable litigation such as whether the abrogation of sovereign immunity can or should negate the protection granted to the states under the Eleventh Amendment. Third party injunctions and the Anti−Tax Injunction Act provide another area for study. Finally, the Commission should consider whether to restrict the use of section 505.

Footnotes

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FN1 *See In re* Blackburn, 171 B.R. 292, 294 (Bankr. S.D. Ohio 1994) ("[I]t appears that the Internal Revenue Service has become more aware and aggressive with reference to collecting taxes in the bankruptcy context."); Colloquoy, *Congress's Role in Bankruptcy Tax Policy: A Roundtable Discussion*, 3 AM. BANKR. INST. L. REV. 257, 259 (1995) (quoting Judge Higdon, "the IRS and, . . . state taxing authorities are really becoming aggressive players in the system").

FN2 *See, e.g.*, 11 U.S.C. § 507(a)(8) (1994) (giving certain tax claims eighth priority in bankruptcy); *id.* § 523(a)(1) (preventing discharge of certain tax claims); *see also* Morgan D. King & Jonathan H. Moss, *Avoiding Tax Liens on Personal Property in Bankruptcy: A Look at the Interplay Between the Bona Fide Purchaser Provisions of the Tax and Bankruptcy Codes*, 31 CAL. W. L. REV. 1, 3−4 (1994) ("[T]axing authorities have enjoyed a history of special treatment in bankruptcy court that has continued to the present day.").

FN3 11 U.S.C. §§ 101−1330 (1994).

FN4 Bankruptcy Reform Act of 1994, Pub. L. No. 103−394, § 603, 108 Stat. 4106, 4147. It is the duty of the Commissioner "to investigate and study issues and problems relating to [the Bankruptcy Code]." *Id.*

FN5 An ad valorem tax is "[a] tax imposed on the value of property. The more common ad valorem tax is that imposed by the states, counties, and cities on real estate." BLACK'S LAW DICTIONARY 51 (6th ed. 1990). Such taxes have been described as "the worst taxes known in the civilized world." Edwin R.A. Seligman, *The General Property Tax, in* ESSAYS IN TAXATION 62 (9th ed. 1921).

FN6 A sales tax is "[a] state or local−level tax on the retail sale of specific property or services." BLACK'S LAW DICTIONARY 1339 (6th ed. 1990). Such taxes generally are paid by the purchaser, but are collected by the seller as an agent for the government. *Id.*

FN7 Excise taxes encompass levies on an activity, event, exercise of property rights, or privilege granted. JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, STATE & LOCAL TAXATION 29 (4th ed. 1978). Many states have enacted "use taxes" (excise taxes) in order to capture the revenue that would be lost because of purchases made by citizens from without the state. For examples of such statutes, see CONN. GEN. STAT. ANN. § 12−411 (West 1993 & Supp. 1995); VA. CODE ANN. § 58.1−609.7 (Michie 1995).

FN8 *See, e.g.*, N.Y. BANKING LAW § 625(1) (McKinney Supp. 1996) (providing that any claim "for taxes owed to any taxing authority shall be paid in full . . . prior to the payment of any other accepted claim"); N.Y. INS. LAW § 3410 (McKinney 1985) (requiring payment of any tax prior to payment of any claim resulting from damage to residence).

FN9 *See* 11 U.S.C. § 507(a)(8)(C) (1994) (granting priority to any "tax required to be collected or withheld and for which the debtor is liable in any capacity"); *id.* § 523(a)(1)(A) (excepting trust fund taxes from discharge).

FN10 *See id.* § 506.

FN11 *Id.* § 507(a)(1). Administrative claims are granted first priority. *Id.* Any taxes on income of the estate are granted first priority as an administrative expense. *Id.* § 728(b).

FN12 *See id.* § 507(a)(8).

FN13 *See, e.g.*, *In re* Al Copeland Enters., Inc., 133 B.R. 837, 839 (Bankr. W.D. Tex. 1991) (concluding sales taxes collected by debtor were collected in trust for state of Texas), *aff'd*, 991 F.2d 233 (5th Cir. 1993); *In re* Avant, 110 B.R. 264, 265 (Bankr. W.D. Tex. 1989) (finding Texas sales tax to be trust fund tax for which debtor is liable); *In re* Gulf Consol. Servs., Inc., 110 B.R. 267, 267 (Bankr. S.D. Tex. 1989) (concluding when debtor collects sales tax it is in form of trust fund).

FN15 *See, e.g.*, IND. CODE ANN. § 6−2.5−9−3 (Burns 1995) (providing that gross retail sales or use tax collected is held in trust for state); MD. CODE ANN., TAX−GEN. § 11−401 (1988) (defining vendor as trustee for state and imposing liability for "collection of sales tax for and on account of the state"); TEX. TAX CODE ANN. § 111.016(a) (West Supp. 1996) (requiring tax funds collected or withheld be held in trust for state).

FN16 *See, e.g.*, GA. CODE ANN. §§ 48−8−32, 48−8−33, 48−8−34 (Harrison 1994) (establishing Georgia sales tax); *id.* § 48−7−108(a), (b) (establishing employer liability for withholding tax); TEX. TAX CODE ANN. § 111.016(a) (West Supp. 1996) (covering any tax required to be collected, including sales/use tax and motor fuels tax); TEX. REV. CIV. STAT. ANN. art. 1.14−2, § 12(b) (West 1981) (establishing premium taxes on surplus lines insurance).

FN17 11 U.S.C. § 507(a)(8)(C) (1994).

FN18 *Id.* § 541(a).

FN19 *See* Begier v. IRS, 496 U.S. 53, 59 (1990) (finding debtor does not have equitable interest in property held in trust and therefore that interest is not property of estate); Al Copeland Enters., Inc. v. Texas (*In re* Al Copeland Enters., Inc.), 991 F.2d 233, 236−37 (5th Cir. 1993) (holding sales tax trust fund and interest thereon not part of estate). This, however, was not always the result. Interpreting the Bankruptcy Act, the United States Supreme Court held that the important bankruptcy policy of assuring payment of administrative expenses prevented tax authorities from tracing trust funds and removing them from the estate. *See* United States v. Randall, 401 U.S. 513, 517 (1971) (holding that because Bankruptcy Act subordinated tax claims to administrative claims it could not allow trust fund to "eat up an estate"). Congress intentionally changed this result in enacting the Bankruptcy Code, which declined to incorporate the rule in *Randall*. *Begier*, 496 U.S. at 63−65 ("The strict rule of *Randall* thus did not survive the adoption of the new Bankruptcy Code.").

FN20 *E.g.*, *In re* Al Copeland Enters., Inc., 133 B.R. 837, 840 (Bankr. W.D. Tex. 1991), *aff'd*, 991 F.2d 233 (5th Cir. 1993).

FN21 Tracing of a trust *res* that has been commingled with other funds is not a new idea. Salisbury Inv. Co. v. Irving Trust Co. (*In re* United Cigar Stores Co. of Am.), 70 F.2d 313, 316 (2d Cir. 1934) (allowing recovery of trust if it can be clearly traced in specific property); Majutama v. Drexel Burnham Lambert Group, Inc. (*In re* Drexel Burnham Lambert Group, Inc.), 142 B.R. 633, 637 (S.D.N.Y. 1992) (recognizing that rule of tracing with commingling of assets is well−established). It may even be appropriate to consider any funds remaining in the debtor's accounts on the petition date to be tax trust funds. *See* City of Farrell v. Sharon Steel Corp., 41 F.3d 92, 101 (3d Cir. 1994) (citing statements of Representative Edwards, 124 CONG. REC. at 11047). This process is generally referred to as the "lowest intermediate balance test." *See* Wasden v. Florida Dep't of Revenue (*In re* Wellington Foods, Inc.), 165 B.R. 719, 726 n.7 (Bankr. S.D. Ga. 1994) (describing lowest intermediate balance test). If the tax authority can show that the lowest balance in the account between the time of deposit and the petition date did not fall below the level of the claimed trust fund, the funds in the account will be impressed with a trust on behalf of the state. *Id.*; *Columbia Gas*, 997 F.2d at 1063 (stating "lowest intermediate balance in a commingled account represents trust funds that have never been dissipated and which are reasonably identifiable"); First Fed. v. Barrow, 878 F.2d 912, 916 (6th Cir. 1989) (stating that balance in account will be subject to equitable claim of trust); Connecticut Gen. Life Ins. Co. v. Universal Ins. Co., 838 F.2d 612, 619 (1st Cir. 1988) (same); *see* United States v. Banco Cafetero Pan., 797 F.2d 1154, 1159 (2d Cir. 1986) (allowing government to reach assets commingled with narcotics proceeds). In order for tracing to be successful, the state tax authority must demonstrate not only that the funds have been deposited into an account but also that the funds remain among the debtor's assets. *Drexel Burnham Lambert*, 142 B.R. at 638. The nature of the lowest intermediate balance test is such that once trust funds have been dissipated, they cannot be replenished by funds that come into the account after the lowest intermediate balance is reached. *Id.* (citing Schuyler v. Littlefield, 232 U.S. 707, 710 (1914)).

FN22 *See, e.g.*, N.Y. TAX LAW § 1137(e)(3) (McKinney 1987) (providing that tax commission may require person to deposit money in a separate account in order to protect tax revenues); TEX. TAX CODE ANN. § 111.012(a)(2) (West 1992) (providing that comptroller may require taxpayer to "establish a tax escrow account at a bank or other financial institution").

FN23 *See* Begier v. IRS, 496 U.S. 53, 60−61 (1990).

FN24 *See supra* note 19 and accompanying text.

FN25 "Cash collateral" is defined in part as "cash `in which the estate . . . [has] an interest.'" 11 U.S.C. § 363(a) (1994). Since the estate has no interest in the trust fund taxes, they cannot be cash collateral. *See* Stephen W. Sather, *Tax Issues in Bankruptcy*, 25 ST. MARY'S L.J. 1363, 1385 (1994).

FN26 A "cash collateral order" is an order authorizing the use of cash collateral. *See* FED. R. BANKR. P. 4001(b) (describing procedure for making motion to authorize use of cash collateral).

FN27 Taxing authorities face a time lag problem. For example, a corporation could fail to pay over its trust fund taxes, and by the time such delinquency was discovered and investigated, the corporation could be dissolved. *See* James Serven, *Taxation Survey*, 71 DENV. U. L. REV. 1063, 1076 (1994) (noting that taxing authority will lose out when employers go out of business).

FN28 This would make sense in light of the fact that Bankruptcy Rule 4001 requires that parties with an interest in the cash collateral be served. FED. R. BANKR. P. 4001(b).

FN29 "Responsible person" liability is imposed upon"[a]ny person required to collect, truthfully account for and pay over any tax imposed . . . who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof." I.R.C. § 6672(a) (1994). The term "person" includes officers or employees of a corporation, and members or employees of a partnership, "who as such officer, employee, or member is under a duty to perform the acts in respect of which the violation occurs." *Id.* § 6671(b). Section 6672 effectively "shift[s] the tax liability of a defaulting corporation to those responsible for the nonpayment." 1A COLLIER ON BANKRUPTCY [[paragraph]] 22.02[2][a] (Lawrence P. King ed., 15th ed. 1995). Indeed, many trust fund statutes were enacted to provide an alternative form of collection of state tax revenues. *E.g.*, State v. DeJesus, 642 So.2d 854, 856 (La. 1994).

FN30 *Cf.* I.R.C. § 6672 (1994). Liability under § 6672 attaches only upon a finding of a *willful* failure to collect, account for, or pay over taxes, *id.*, as opposed to a strict conversion theory which would include any "unauthorized act which deprives an owner of his property permanently or for an indefinite time," BLACK'S LAW DICTIONARY 332 (6th ed. 1990).

FN31 *See* Davis v. State, 904 S.W.2d 946, 953 (Tex. Ct. App. 1995) (finding taxpayer personally liable for spending sales tax funds even before statute was amended to include "trust fund" language).

FN32 *See, e.g.*, CAL. REV. & TAX. CODE § 6829 (West 1987 & Supp. 1996) (same); N.Y. TAX LAW § 1133(a) (McKinney 1987) (same); TEX. TAX CODE ANN. § 111.016(a) (West Supp. 1996) (making "any person" receiving tax liable).

FN33 *See* Bridgeport Co. v. United States Postal Serv., 39 B.R. 118, 121 (Bankr. E.D. Ark. 1984) (describing lock−box agreement).

FN34 CAL. REV. & TAX. CODE § 18670 (West 1994) (holding lender liable for unpaid taxes, penalty and interest under lock−box arrangement).

FN35 *See, e.g.*, TEX. TAX CODE ANN. § 33.41 (West 1992 & Supp. 1996) (providing for foreclosure of liens to satisfy payment of delinquent property taxes); *id.* § 34.01 (providing for sale of property following foreclosure on tax liens).

FN36 *See* 11 U.S.C. § 544(a)(3) (1994). Section 544 gives the trustee the power to avoid any interest in estate property which is voidable by a judicial lien creditor. *Id.* If, before bankruptcy, the government does not complete, the steps required to perfect under state law, see CAL. GOV'T CODE § 7170(b) (West 1995) (requiring recordation of

lien); CONN. GEN. STAT. ANN. § 12−35a(b) (West 1993) (stating lien is perfected when notice of such lien is filed); *cf.* TEX. TAX CODE ANN. § 32.01(c) (West Supp. 1996) (providing that lien is perfected upon attachment and requires no further action by taxing unit), the lien might be avoided, Abney v. Cox Enters. (*In re* Fulton Air Serv., Inc.), 777 F.2d 1521 (11th Cir. 1985) (allowing avoidance of lien not recorded according to Georgia statute). Sections 362(b)(3) and 546(b), however, allow some tax liens to be perfected postpetition. 11 U.S.C. §§ 362(b)(3), 546(b) (1994). Conversely, as a general rule, the lien is protected if perfection occurred before bankruptcy. Newport v. Tennessee (*In re* Boat Land Co.), 169 B.R. 47, 49 (Bankr. M.D. Tenn. 1994) (preventing avoidance of Tennessee personal property tax lien which was properly recorded and perfected); Riley v. Wisconsin Dep't of Revenue (*In re* Riley), 88 B.R. 906, 917 (Bankr. W.D. Wis. 1987) (forcing amendment of chapter 13 plan to provide for perfected tax liens of IRS and state taxing authority); Zoltanski v. Henderson (*In re* Putnam County Canning Co.), 35 B.R. 482, 485 (Bankr. N.D. Ohio 1983) (holding debtor could not avoid statutory tax liens properly perfected by taxing authorities prior to date of petition).

FN37 *See* 11 U.S.C. § 724(b) (1994).

FN38 *See id.* § 362(b)(18) (excepting from automatic stay, creation or perfection of "statutory lien for an ad valorem property tax"). For cases filed prior to October 22, 1994, however, there is still a substantial debate over whether postpetition ad valorem taxes may enjoy this exception from the automatic stay.

FN39 *See supra* note 36 and accompanying text (discussing perfection and its importance to secured status of tax claims in bankruptcy).

FN40 11 U.S.C. §§ 724(a), 726(a)(4) (1994).

FN41 *Id.* § 724(b). The operation of section 724(b) has been described as follows:

Section 724(b) governs the distribution of that property of the estate against which tax liens are asserted. The section in effect dictates that, where there are tax lien claims, those claimants, rather than other secured creditors, will pay for the cost of estate administration. . . .

When property is burdened by tax liens, as was the case at bar, that portion of the sale proceeds attributable to those tax liens becomes a fund into which the Trustee may dip in order to pay administrative expenses allowed under 507(a)(1)−(6), without affecting other secured claims.

In re Sherrill, 78 B.R. 804, 807 (Bankr. W.D. Tex. 1987).

Keep in mind, however, that the subordination provisions of § 724 apply only to property of the estate, and that, therefore, property of the debtor such as a homestead is not affected. Carlton v. IRS (*In re* Carlton), 19 B.R. 73, 75 (D.N.M. 1982).

FN42 *See supra* note 2.

FN43 *See* 11 U.S.C. § 724(b)(2) (1994) (stating that priority claims are second class of claims to receive proceeds of property on which there is a tax lien).

FN44 *Id.* § 724(b)(3).

FN45 *Id.* § 724(b)(4).

FN46 *Id.* § 507(a)(8)(B).

FN47 Section 724(b)(3) provides that once the priority claims are paid out of this property, only then will the claimant holding the tax lien get anything and that claimant can only take to the "extent that such holder's allowed tax claim that is secured by such tax lien exceeds any amount distributed [to priority claims]." *Id.* § 724(b)(3).

FN48 When the amount of the priority claims exceed the amount of the tax lien, the only way the tax lienholder could get paid at all is if there is still money left after satisfying any secured claims and any junior lienholders. *See* 11 U.S.C. § 724(b)(2)−(5) (1994).

FN49 *In re* Grand Slam U.S.A., Inc., 178 B.R. 460, 464 (E.D. Mich. 1995); King v. Board of Supervisors (*In re* A.G. Van Metre, Jr., Inc.), 155 B.R. 118, 123 (Bankr. E.D. Va. 1993).

FN50 11 U.S.C. § 363(f)(1)−(5) (1994).

FN51 *Id.* § 363(f)(5); *see Grand Slam*, 178 B.R. at 462 (noting cramdown provisions of § 1129 are legal proceedings within meaning of § 363(b)(5)).

FN52 *See* cases cited *supra* note 49.

FN53 137 B.R. 207 (Bankr. E.D. Tex. 1992).

FN54 *Id.* at 210.

FN55 *Id.* (citation omitted).

FN56 *See supra* note 2. This is further evidenced by the recent amendment to § 362(b)(18) which allows for perfection of postpetition ad valorem tax liens. *See* 11 U.S.C. § 362(b)(18) (1994).

FN57 H.R. REP. NO. 595, 95th Cong., 2d Sess. 382 (1978), *reprinted in* 1978 U.S.C.C.A.N 5763, 6338.

FN58 Bankruptcy Act of 1898, ch. 541, § 67c, 30 Stat. 544, 564, *repealed by* Bankruptcy Reform Act of 1978, Pub. L. No. 95−598, title IV, § 401(a), 92 Stat. 2682.

FN59 11 U.S.C. § 506(c) (1994).

FN60 *Id.* § 726(a)(4).

FN61 *Id.* § 101(15) (defining "entity" as including governmental units).

FN62 *Id.* § 362(a).

FN63 *Id.* § 362(a)(4).

FN64 11 U.S.C. § 545(2) (1994); *see supra* note 36 and accompanying text (discussing protection of perfected tax liens).

FN65 *Id.* § 362(a)(4).

FN66 *Id.* § 362(b)(3).

FN67 *See, e.g.*, Lincoln Sav. Bank v. Suffolk County Treasurer (*In re* Parr Meadows Racing Ass'n, Inc.), 880 F.2d 1540, 1548 (2d Cir. 1989) (applying exception to real property taxes), *cert. denied*, 493 U.S. 1058 (1990); Maryland Nat'l Bank v. Mayor of Baltimore, 723 F.2d 1138, 1143 (4th Cir. 1983) (finding city entitled to perfection and superpriority of lien with respect to real property).

FN68 *See, e.g.*, N.Y. U.C.C. § 9−312(4) (McKinney 1990).

FN69 *See, e.g.*, Butler Constr. Co. v. American Bluegrass Marble Co. (*In re* Butler Constr. Co.), 110 B.R. 281, 281 (Bankr. W.D. Ky. 1989) (holding mechanic's lien perfected postpetition entitled to share pro rata with other

mechanic's lien claimants); *In re* Brittian, 106 B.R. 665, 666 (Bankr. D. Mont. 1989) (holding construction lien related back to commencement of work which occurred prepetition).

FN70 *See Parr Meadows Racing*, 880 F.2d at 1546 (stating creditor with prepetition interest will not lose preferred standing where lien not perfected until after commencement of bankruptcy case); Equibank, N.A. v. Wheeling−Pittsburgh Steel Corp., 884 F.2d 80, 85 (3d Cir. 1989) (stating exception allows liens to become perfected after filing if created prior to bankruptcy); *In re* Summit Ventures, Inc., 135 B.R. 483, 487 (Bankr. D. Vt. 1991) (holding creditor with prepetition interest in property will not lose preferred standing where perfected after commencement of bankruptcy); Gline v. Horn & Co., P.C. (*In re* Isley), 104 B.R. 673, 677 (Bankr. D.N.J. 1989) (stating postpetition perfection allowed if there is prepetition interest in property).

FN71 Treasurer of Snohomish County v. Seattle−First Nat'l Bank (*In re* Glasply Marine Indus., Inc.), 971 F.2d 391, 394 (9th Cir. 1992); Makoroff v. City of Lockport, 916 F.2d 890, 894 (3d Cir. 1990), *cert. denied*, 499 U.S. 983 (1991).

FN72 Kocurek v. L.E. Arnold, M.D. (*In re* Thurman), 163 B.R. 95, 100 (Bankr. W.D. Tex. 1994) (stating §§ 362(b)(3) and 546(b) provide exception which allows annual postpetition tax liability to be incurred and perfected automatically rather than allowing one time exception for tax liability incurred prepetition and perfected postpetition).

FN73 Bankruptcy Reform Act of 1994, § 401, 11 U.S.C. § 362(b)(18) (1994).

FN74 *See* Richard v. City of Chicago, 80 B.R. 451, 454 (N.D. Ill. 1987) (stating because tax sale was void, § 549 time limits were inapplicable).

FN75 11 U.S.C. § 549 (1994).

FN76 *Id.* § 549(a).

FN77 *Id.* § 549(d).

FN78 Six circuits have concluded that actions taken in violation of the stay are void. Franklin Sav. Ass'n v. Office of Thrift Supervision, 31 F.3d 1020, 1022 (10th Cir. 1994); Schwartz v. United States (*In re* Schwartz), 954 F.2d 569, 571 (9th Cir. 1992); Maritime Elec. Co. v. United Jersey Bank, 959 F.2d 1194, 1207 (3d Cir. 1991); 48th St. Steakhouse, Inc. v. Rockefeller (*In re* 48th St. Steakhouse, Inc.), 835 F.2d 427, 431 (2d Cir. 1987), *cert. denied*, 485 U.S. 1035 (1988); Borg−Warner Acceptance Corp. v. Hall, 685 F.2d 1306, 1308 (11th Cir. 1982); *In re* Smith Corset Shops, Inc., 696 F.2d 971, 976 (1st Cir. 1982). Three circuits have held that violations of the stay are merely voidable. Bronson v. United States, 46 F.3d 1573, 1578 (Fed. Cir. 1995); Kendall County v. Boerne Hills Leasing Corp. (*In re* Boerne Hills Leasing Corp.), 15 F.3d 57, 59 (5th Cir. 1994); Easley v. Pettibone Mich. Corp., 990 F.2d 905, 910 (6th Cir. 1993).

FN79 *See supra* note 78 (showing split of authority).

FN80 *See* Garcia v. Phoenix Bond & Indem. Co. (*In re* Garcia), 109 B.R. 335, 337 (N.D. Ill. 1989). In *Garcia*, the bankruptcy court concluded that to find that acts in violation of the automatic stay were voidable would have the effect of encouraging disrespect for the stay by increasing the possibility that violators of the automatic stay may profit from their disregard of the law. *Id.*

FN81 Section 506(b) provides:

To the extent that an allowed secured claim is secured by property the value of which . . . is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose.

11 U.S.C. § 506(b) (1994).

FN82 *See* Tuggle v. IRS (*In re* Tuggle), 22 B.R. 439, 441 (Bankr. N.D. Ga. 1982) (finding that when liens for taxes other than ad valorem taxes attach to taxpayer's property, they are superior to all other liens filed thereafter, but not those recorded prior in time).

FN83 11 U.S.C. § 506(b) (1994); *In re* Schriock Constr., Inc., 176 B.R. 176, 178 (Bankr. D.N.D. 1994) (finding natural reading of § 506(b) entitles holder of oversecured claim to postpetition interest and, if secured claim created pursuant to agreement, the right to those reasonable fees, costs and charges provided for in agreement); *In re* A.J. Lane & Co., 113 B.R. 821, 823 (Bankr. D. Mass. 1990) (stating that holder of oversecured claim may be allowed any reasonable fees, costs or charges provided for under agreement from which claim arose).

FN84 489 U.S. 235 (1989).

FN85 *Id.* at 241. The Court found that,

[t]he relevant phrase § 506(b) is: "[T]here shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs or charges provided for under the agreement under which such claim arose." "Such claim" refers to an oversecured claim. The natural reading of the phrase entitles the holder of an oversecured claim to postpetition interest and, in addition, gives one having a secured claim created pursuant to an agreement the right to reasonable fees, costs and charges provided for in that agreement. Recovery of postpetition interest is unqualified. Recovery of fees, costs and charges, however, is allowed only if they are reasonable and provided for in the agreement under which the claim arose. Therefore, in the absence of an agreement, postpetition interest is the only added recovery available.

Id.

FN86 Bondholder Comm. v. Williamson County (*In re* Brentwood Outpatient, Ltd.), 43 F.3d 256, 260 (6th Cir. 1994), *cert. denied*, 115 S. Ct. 1824 (1995); Building Technologies Corp. v. City of Hannibal (*In re* Building Technologies Corp.), 167 B.R. 853, 859 (Bankr. S.D. Ohio 1994).

FN87 11 U.S.C. § 503(b)(1) (1994).

FN88 *See* Midland Cent. Appraisal Dist. v. Midland Indus. Serv. Corp. (*In re* Midland Indus. Serv. Corp.), 35 F.3d 164, 166−67 (5th Cir. 1994), *cert. denied*, 115 S. Ct. 1359 (1995). "The term `incur' is defined as `[t]o have liabilities cast upon one by act or operation of law [or to] become liable or subject to.'" *Id.* (quoting BLACK'S LAW DICTIONARY 691 (5th ed. 1979)).

FN89 *See, e.g.*, CAL. REV. & TAX. CODE § 2192 (West Supp. 1996) (all tax liens attach the first day of January); ILL. ANN. STAT. ch. 35, para. 200/9−175 (Smith−Hurd Supp. 1995) (owner of property liable for taxes as of January 1); TEX. TAX CODE ANN. § 32.07 (West 1992) (tax is personal obligation of owner as of January 1).

FN90 *Midland Indus.*, 35 F.3d at 167; *see In re* Firestone, 179 B.R. 148, 149 (Bankr. D. Neb. 1995) (finding tax refund for prepetition tax year to be prepetition debt for setoff purposes).

FN91 *See In re* O.P.M. Leasing Servs., Inc., 68 B.R. 979, 983 (Bankr. S.D.N.Y. 1987) (finding income earned prepetition to be distinct from postpetition earnings); *In re* Hillsborough Holdings Corp., 156 B.R. 318, 320 (Bankr. M.D. Fla. 1993) (denying administrative expense priority to tax on income earned prepetition).

FN92 11 U.S.C. § 346(b)(1) (1994).

FN93 *Id.* § 346(d).

FN94 *See In re* Pioneer Title Bldg., Ltd., 133 B.R. 822, 824 (Bankr. W.D. Tex. 1991) (granting ad valorem taxes assessed postpetition administrative expense priority); *In re* Fairchild Aircraft Corp., 124 B.R. 488, 494 (Bankr. W.D. Tex. 1991) (finding taxes assessed postpetition to be obligation of estate and therefore administrative claims).

FN95 11 U.S.C. § 507(a)(8)(B) (1994).

FN96 *See id.* § 507(a)(1) (establishing first priority of administrative claims).

FN97 *Id.* § 1129(a)(9).

FN98 *Id.* § 726(a)(1).

FN99 *Id.* § 503(b)(1)(C).

FN101 There is presently a significant controversy over whether § 510(c) allows bankruptcy courts to subordinate penalties on tax claims in the absence of wrongdoing by the taxing authority. The Supreme Court has granted certiorari in two cases dealing with this issue. *In re* CF&I Fabricators, Inc., 53 F.3d 1155 (10th Cir.), *cert. granted*, 116 S. Ct. 558 (1995); United States v. Noland (*In re* First Truck Lines, Inc.), 48 F.3d 210 (6th Cir.), *cert. granted*, 116 S. Ct. 558 (1995).

FN102 11 U.S.C. § 507(a)(8) (1994).

FN103 *Id.* § 1129(a)(9)(C).

FN104 *Id.* § 507(a)(8). It should be noted that the section does *not* apply to secured tax claims. Stanford v. Butler (*In re* Stanford), 826 F.2d 353, 356 (5th Cir. 1987) (viewing § 507 as addressed solely to priority of unsecured claims); *In re* Reichert, 138 B.R. 522, 526−27 (Bankr. W.D. Mich. 1992) (concluding that § 507 explicitly limits its application to unsecured claims).

FN105 *See* 11 U.S.C. § 507(a)(8)(A)−(G) (1994) (listing income tax, property tax, trust fund tax, social security tax, excise tax, customs duty and penalties on such claims).

FN106 *Id.* § 507(a)(8)(A).

FN107 *Id.* § 507(a)(8)(A)(i).

FN108 *Id.* § 507(a)(8)(A)(ii).

FN109 Thus, if the state taxing agency assesses a taxpayer on February 1, 1995, for 1991 income taxes, and the taxpayer files a bankruptcy petition on May 1, 1995, the claim for 1991 taxes would be entitled to priority even though the time for filing the return was more than three years prior to the filing of the bankruptcy petition.

FN110 *See* King v. Franchise Tax Bd. (*In re* King), 961 F.2d 1423, 1427 (9th Cir. 1992) (determining that precise date of assessment should be calculated in relation to specific tax code and procedures involved).

FN111 *See* 11 U.S.C. § 108(c) (1994) (providing for extension of time periods related to "applicable nonbankruptcy law"); *see also* West v. United States (*In re* West), 5 F.3d 423, 427 (9th Cir. 1993) (relying on § 108(c) to extend 240 day period due to prior bankruptcy proceeding), *cert. denied*, 114 S. Ct. 1830 (1994); *In re* Harris, 167 B.R. 680, 683 (Bankr. M.D. Fla. 1994) (relying on § 108 to extend three year period); *In re* Ross, 130 B.R. 312, 313 (Bankr. D. Neb. 1991) (same). Note, however, that because § 507(a)(8)(A) is part of the Bankruptcy Code, it is not "applicable nonbankruptcy law" as is required under § 108(c). Gore v. United States (*In re* Gore), 182 B.R. 293, 298 (Bankr. N.D. Ala. 1995).

FN112 11 U.S.C. § 507(a)(8)(A)(iii) (1994).

FN113 *Id.*

FN114 *See supra* note 110 and accompanying text; *see also* Haas v. IRS (*In re* Haas), 48 F.3d 1153, 1156 (11th Cir. 1995) ("Where Congress knows how to say something but chooses not to, its silence is controlling."); Florida Dep't of Revenue v. General Dev. Corp. (*In re* General Dev. Corp.), 165 B.R. 691, 694 (S.D. Fla. 1994) ("If Congress had intended federal law to determine the question of `assessment' under § 507(a)(8)(A)(iii), regardless of whether the tax at issue is a local, state or federal tax, it could have easily specified `federal law' rather than `applicable law.'").

FN115 11 U.S.C. § 507(a)(8)(iii) (1994).

FN116 *Id.* § 523(a)(1)(B)(i).

FN117 *Id.* § 523(a)(1)(B)(ii).

FN118 *Id.* § 523(a)(1)(C).

FN119 *Id.*

FN120 *See* Crawford v. United States (*In re* Crawford), 144 B.R. 346, 348 (Bankr. W.D. Tex. 1992) (treating debtors tax claim as nondischargeable); Longley v. United States (*In re* Longley), 66 B.R. 237, 244 (Bankr. N.D. Ohio 1986) (same).

FN121 11 U.S.C. § 507(a)(8)(C) (1994).

FN122 For an in depth discussion of trust fund tax liability in bankruptcy, see 1A COLLIER, *supra* note 29, [[paragraph]] 22.02 (discussing various trust fund tax issues).

FN123 11 U.S.C. § 541(a) (1994); *see* Begier v. IRS, 496 U.S. 53, 59 (1990) ("Because the debtor does not own an equitable interest in the property he holds in trust for another, that interest is not `property of the estate.'"); *see* discussion *supra* part I.A.

FN124 *See supra* notes 29−30 (discussing responsible person liability).

FN125 11 U.S.C. § 523(a)(1)(A) (1994).

FN126 *Id.* §§ 1129(a)(9)(C), 1225(a)(5), 1325(a)(5).

FN127 *Id.* § 507(a)(8)(D).

FN128 *See* Ndosi v. Minnesota, 950 F.2d 1376, 1378 (8th Cir. 1991) (discharging officer's personal liability for tax claim resulting from Minnesota state law).

FN129 *See supra* note 7 (defining "excise tax").

FN130 United States v. Mansfield Tire & Rubber Co. (*In re* Mansfield Tire & Rubber Co.), 942 F.2d 1055 (6th Cir. 1991), *cert. denied sub nom* 502 U.S. 1092 (1992). *Mansfield* held that when Congress defines a tax as an excise tax, it will automatically fall under § 507(a)(8)(E). However, less deference is given to state and local governments. *Mansfield* rejected two earlier decisions which held that federal "excise" taxes could be recharacterized as penalties under the Bankruptcy Code. *See* Mahon v. IRS (*In re* Unified Control Sys., Inc.), 586 F.2d 1036 (5th Cir. 1978); IRS v. Feinblatt (*In re* Kline), 403 F. Supp. 974 (D. Md. 1975), *aff'd*, 547 F.2d 823 (4th Cir. 1977).

FN131 *In re* Suburban Motor Freight, Inc., 998 F.2d 338 (6th Cir. 1993) (finding workers' compensation assessments to be excise taxes); United States v. Unsecured Creditors' Comm. (*In re* C−T of Virginia, Inc.), 977 F.2d 137 (4th Cir. 1992) (tax on pension assets reverting to an employer), *cert. denied*, 507 U.S. 1004 (1993); Williams v. Motley, 925 F.2d 741 (4th Cir. 1991) (uninsured motor vehicle assessments); *In re* Groetken, 843 F.2d 1007 (7th Cir. 1988) (retailer's occupation tax based upon percentage of gross receipts); *In re* Longo, 144 B.R. 305 (Bankr. D. Md. 1992)

(payments to fund designed to reimburse trade school students who lose their tuition when school closes); *In re* C.M. & C. Coal Co., 33 B.R. 358 (Bankr. N.D. Ala. 1983) (mine reclamation fees).

FN132 Templar v. Shamokin Area School District (*In re* Templar), 170 B.R. 562 (Bankr. M.D. Pa. 1994) (finding attorney occupation tax was an "excise" tax, but was not an excise tax on transactions and thus not within § 507(a)(8)(E)).

FN133 11 U.S.C. § 507(a)(8)(E)(i) (1994).

FN134 *See id.* § 507(a)(8)(E)(ii).

FN135 *Id.* § 507(a)(8)(E)(i).

FN136 Under chapter 7, the classification of a claim as a priority tax claim ensures that it will be nondischargeable. *Id.* § 523(a)(1)(A). Chapters 12 and 13, on the other hand, both require that a plan "provide for the full payment, in deferred cash payments, of all claims entitled to priority under § 507 of this title, unless the holder of a particular claim agrees to a different treatment of such claim." *Id.* §§ 1222(a)(2), 1322(a)(2). Priority claims do not receive postpetition interest under either chapters 12 or 13. *In re* Wakehill Farms, 123 B.R. 774, 775−76 (Bankr. N.D. Ohio 1990) (involving chapter 12); *In re* Hageman, 108 B.R. 1016, 1019 (Bankr. N.D. Iowa 1989) (involving chapter 13). Thus, chapters 12 and 13 require that the prepetition amount of the claim be paid over the life of the plan.

FN137 11 U.S.C. § 1129(a)(9)(C) (1994).

FN138 *Id.* § 1126(a).

FN139 *Id.* § 1123(a)(1).

FN140 *Id.* § 1129(a)(9).

FN141 *See id.* § 1129(a)(8) (requiring acceptance by classes of claims). Failure to comply with § 1129(a)(8) requires a debtor to resort to cramdown. *See id.* § 1129(b).

FN142 11 U.S.C. § 1129(a)(9)(C) (1994).

FN143 *Id.* § 1129(b)(1).

FN144 *See id.* § 1123(a)(4) (requiring that all members of class receive same treatment).

FN145 Section 1129(a)(9)(C) requires that the holder of priority tax claims receive "deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim." *Id.* § 1129(a)(9)(C); *see In re* Elm Creek Joint Venture, 93 B.R. 105, 110 (Bankr. W.D. Tex. 1988) (finding § 1129(a)(9) met by plan providing for payment of prepetition taxes within six years from effective date); *see supra* text accompanying note 137.

FN146 *See, e.g., In re* Inventive Packaging Corp., 81 B.R. 74, 79 (Bankr. D. Colo. 1987) (finding monthly installments provide priority tax creditor with "some degree of financial certitude that its claims will be paid promptly and in full under a plan of reorganization"); *In re* Mahoney, 80 B.R. 197, 200−01 (Bankr. S.D. Cal. 1987) (proposing to pay claims in lump sum during last month of five−year plan does not comply with § 1129(a)(9)(C)).

FN147 *See In re* Snowden's Landscaping Co., 110 B.R. 56, 61 (Bankr. S.D. Ala. 1990) (recognizing that loose construction of "deferred payments" leaves room for skillfully drafted plan to deprive creditor of priority status).

FN148 *See, e.g.*, United States v. Volle Elec., Inc. (*In re* Volle Elec., Inc.), 139 B.R. 451, 454−55 (Bankr. C.D. Ill. 1992) (allowing minimum monthly payments with large balloon payment at end of plan); *In re* Sanders Coal &

Trucking, Inc., 129 B.R. 516, 520 (Bankr. E.D. Tenn. 1991) (finding "deferred cash payments" requirement met by payments to begin three years after confirmation); *Snowden's Landscaping*, 110 B.R. at 61 (allowing payment of tax claims in graduated quarterly payments); *see also In re* Ferguson, 134 B.R. 689, 692 (Bankr. S.D. Fla. 1991) (applying same flexibility in interpreting "deferred cash payments" under § 1322(a)(2) as under § 1129(a)(9)(C))

FN149 *See, e.g., Volle Elec.*, 139 B.R. at 455.

FN150 *Snowden's Landscaping*, 110 B.R. at 60−61 n.7. The court noted that Congress did not intend that priority tax claimants be paid monthly. *Id.* (citing 124 CONG. REC. 34,006 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6542). Rather, according to the court, Congress was more concerned about affording the debtor a "breathing spell" while also ensuring that the priority tax claimants, whose claims are to be paid over the six−year period following assessment, receive the present value of their claims. *Id.*

FN151 *See supra* note 145 and accompanying text.

FN152 *See* 11 U.S.C. § 1129(a)(9)(C) (1994).

FN153 *See supra* note 110 and accompanying text (stating assessment determined under state law).

FN154 In the case of sales taxes, assessment occurs at the time of the taxable transaction, *i.e.*, when the consumer buys the merchandise. *See, e.g.*, Colonial Pipeline Co. v. Clayton, 275 N.C. 215, 223 (N.C. 1969) (stating sales tax is assessed and imposed at time of sale). The sales tax is computed and added to the sales price, and must be paid before the consumer can leave the store with his property. Similarly payroll taxes are paid by the taxpayer/employee on the date he is paid by his employer. I.R.C. §§ 3102(a), 3402(a) (1994) (requiring employers to collect income taxes from employees). In both cases, assessment occurs at a definite time, as the taxpayer has no right to the money collected on the sale or withheld by the employer. *See* Begier v. IRS, 496 U.S. 53, 58−59 (1990) (discussing "property of the debtor").

FN155 For instance, in Georgia, most businesses remit sales taxes on a monthly basis. Thus, sales taxes collected in a given month must be paid over to the State Department of Revenue by the 20th day of the following month. GA. CODE ANN. § 48−8−49(a) (Harrison 1994). Similarly, most businesses remit withheld income taxes on a monthly basis. Thus, employer withholding taxes accrued during a given month must be paid over to the Georgia Department of Revenue by the 15th day of the following month. *Id.* § 48−7−103(b).

FN156 *See* King v. Franchise Tax Board (*In re* King), 961 F.2d 1423, 1427 (9th Cir. 1992) (noting that specific date of assessment is function of applicable tax code and practices).

FN157 When a business is failing, several months may pass without payment of taxes even though they have been collected and/or withheld. When the bankruptcy petition is filed, the debtor could be in arrears for several monthly payments, each of which is a "claim" for taxes, having its own "date of assessment." So, a debtor that does not pay sales taxes over to the taxing authority for various months throughout a three−year period prior to filing for bankruptcy protection, may come into court owing different tax claims with different expiration dates. For example, the expiration of the six−year period following the date of the assessment for sales taxes for June 1995, is different from the expiration of the six−year period following the date of assessment for sales taxes for November 1995. The debtor may also have had additional taxes assessed at various times.

FN158 For example, a typical plan submitted for balloting will propose to pay the claims of the state taxing authority over a period of time not to exceed six years from the date of the assessment of the claims. The tax claims may have due dates ranging from 30 to 60 months from the effective date of the plan. Thus, the median time period is 45 months, and the plan should be amended to call for payments that satisfy the total tax claims over a period that does not exceed 45 months from the effective date.

FN159 *See* 11 U.S.C. §§ 1222(a)(2), 1322(a)(2) (1994).

FN160 *See* 5 COLLIER, *supra* note 29, [[paragraph]] 1129.03[4][f][i], at 1129−104. "Simply stated, `present value' is a term of art for an almost self evident proposition: a dollar in hand today is worth more than a dollar to be received a day, a month or a year hence." *Id.* The Code, however, does not define the appropriate market rate to be used in determining the present value of a particular claim. *Compare In re* Fi−Hi Pizza, Inc., 40 B.R. 258, 271 (Bankr. D. Mass. 1984) (finding § 6621 interest rate plus 2.5% appropriate rate to use in determining present value) *with In re* Connecticut Aerosols, Inc., 42 B.R. 706, 710−11 (D. Conn. 1984) (holding IRS entitled to T−Bill rate under § 1129(a)(9)(C)) *and In re* Bay Area Servs., 26 B.R. 811, 814 (Bankr. M.D. Fla. 1982) (finding IRS entitled to prime rate plus 10% adjustment for inflation under § 1129(a)(9)(C)).

FN161 The courts have determined that when a debtor chooses to defer payment under § 1129(a)(9)(C), the proper method for providing the creditor with an amount equal to the value of its claim as of the effective date, is to charge interest throughout the payment period. *See* Terex Corp. v. Metropolitan Life Ins. Co. (*In re* Terex Corp.), 984 F.2d 170, 174 (6th Cir. 1993) (holding award of interest was only means by which claim could be paid in manner consistent with § 1129); United States v. Southern States Motor Inns, Inc. (*In re* Southern States Motor Inns, Inc.), 709 F.2d 647, 650−51 (11th Cir. 1983) (holding proper method of providing creditor with present value of claim is to charge interest throughout payment period), *cert. denied*, 465 U.S. 1022 (1984).

FN162 *E.g.*, United States v. Camino Real Landscape Maintenance Contractors, Inc. (*In re* Camino Real Landscape Maintenance Contractors, Inc.), 818 F.2d 1503, 1505 (9th Cir. 1987); United States v. Neal Pharmacal Co., 789 F.2d 1283, 1285 (8th Cir. 1986); *Southern States*, 709 F.2d at 651.

FN163 *In re* Collins, 184 B.R. 151, 156 (Bankr. N.D. Fla. 1995) (noting that "[a]n absolute standard for determining market rates of interest has not been established"); *see infra* notes 167−70 (discussing factors in selecting market rate).

FN164 *See, e.g.*, *Camino Real*, 818 F.2d at 1505 (presenting IRS argument that I.R.C. § 6621 is appropriate interest rate under § 1129(a)(9)(C)).

FN165 In *Southern States*, the Eleventh Circuit cited two chief reasons why the I.R.C. § 6621 interest rate does not provide the "prevailing market rate." *Southern States*, 709 F.2d at 651−52. First, the court pointed out that the § 6621 rate is a static, rigid rate that often will differ from the rates prevailing at the time of a particular reorganization. *Id.* Citing *In re* Moore, 25 B.R. 131 (Bankr. N.D. Tex. 1982), the Eleventh Circuit noted that adoption of the method prescribed in § 6621 could lead to a windfall for the IRS. *Southern States*, 709 F.2d at 652. Second, the Eleventh Circuit reasoned that applying the § 6621 rate ignores differing lengths in the payout period, the quality of the security, and the risk of subsequent default. *Id.*

FN166 Farm Credit Bank v. Fowler (*In re* Fowler), 903 F.2d 694, 697−98 (9th Cir. 1990) (using prime rate); *In re* Connecticut Aerosols, Inc., 42 B.R. 706, 711 (D. Conn. 1984) (applying rate of treasury bills and bonds); *In re* Jordan, 130 B.R. 185, 191 (Bankr. D.N.J. 1991) (using prime rate).

FN167 *See In re* Birdneck Apartment Assocs., II, L.P., 156 B.R. 499, 508 n.15 (Bankr. E.D. Va. 1993). "Discount rates are largely a function of perceived risks. Risk is a function of general economic conditions. . . ." *Id.*

FN168 *In re* General Dev. Corp., 147 B.R. 610, 614 (Bankr. S.D. Fla. 1992); *Camino Real*, 818 F.2d at 1505.

FN169 *See Fowler*, 903 F.2d at 698 (reviewing lower court's addition of .75% risk factor); *Camino Real*, 818 F.2d at 1507 (allowing 2.0% risk factor); *In re* Moore, 81 B.R. 513, 516 (Bankr. S.D. Iowa 1988) (adding 2.5% risk factor).

FN170 United States v. Southern States Motor Inns, Inc. (*In re* Southern States Motor Inns, Inc.), 709 F.2d 647, 652−53 (11th Cir. 1983), *cert. denied*, 465 U.S. 1022 (1984).

FN171 The same standard is also present in 11 U.S.C. §§ 1129(b)(2)(A)(i)(II), 1225(a)(5)(B)(ii) and 1325(a)(5)(B)(ii) (1994).

FN172 *See supra* note 136 and accompanying text. One feature that the Commission would not want to borrow from chapters 12 and 13 is the lack of interest on priority tax claims. This would mark a major change in the balance of power between debtors and taxing authorities.

FN173 *See infra* note 175 and accompanying text (quoting text of § 106's sovereign immunity waiver provision).

FN174 11 U.S.C. § 505 (1994).

FN175 Prior to the recent amendment, § 106 provided as follows:

(a) A governmental unit is deemed to have waived sovereign immunity with respect to any claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which such governmental unit's claim arose.

(b) There shall be offset against an allowed claim or interest of a governmental unit any claim against such governmental unit that is property of the estate.

(c) Except as provided in subsections (a) and (b) of this section and notwithstanding any assertion of sovereign immunity−−

(1) a provision of this title that contains "creditor," "entity," or "governmental unit" applies to governmental units; and

(2) a determination by the courts of an issue arising under such a provision binds governmental units.

11 U.S.C. § 106 (1988).

FN176 *See* United States v. Nordic Village, 503 U.S. 30, 34 (1992) (finding congressional waiver of sovereign immunity insufficient to authorize monetary damages).

FN177 The new § 106 provides that "[n]otwithstanding an assertion of sovereign immunity, sovereign immunity is *abrogated* as to a governmental unit to the extent set forth in this section with respect to" enumerated sections of the Bankruptcy Code. 11 U.S.C. § 106(a)(1) (1994) (emphasis added). Subsections (a)(2)−(5) specifically provide that the courts may hear and determine such issues and award a monetary recovery (but not punitive damages) against governmental units. *Id.* § 106(a)(3). The new section also clarifies the waiver of sovereign immunity resulting from the filing of a proof of claim and retains the offset provision. *Id.* § 106(b),(c).

FN178 U.S. CONST. amend. XI; *see* Seminole Indian Tribe v. Florida, No. 94−12, 1996 WL 134309, at *15 (Sup. Ct. Mar. 27, 1996) (holding that State of Florida was protected from suit by Eleventh Amendment).

FN179 *See, e.g.*, York−Hannover Devs., Inc. v. Florida Dep't of Revenue (*In re* York−Hannover, Devs., Inc.), 181 B.R. 271, 272 (Bankr. E.D.N.C.) (finding abrogation of Eleventh Amendment immunity authorized under Bankruptcy Code and former § 106(a)), *aff'd* 190 B.R. 62 (E.D.N.C. 1995); Harden v. Texas Dep't of Transp. (*In re* Aer−Aerotron, Inc.), 181 B.R. 268, 268−69 (Bankr. E.D.N.C. 1995) (abrogation authorized under former § 106(c)); Field v. Montgomery County, M.D. (*In re* Anton Motors, Inc.), 177 B.R. 58, 62 (Bankr. D. Md. 1995) (abrogation authorized under amended § 106(a)); Mather v. Oklahoma Employment Sec. Comm'n (*In re* Southern Star Foods, Inc.), 190 B.R. 419, 422−26 (Bankr. E.D. Okla. 1995) (same); Solow v. Greater Orlando Aviation Auth. (*In re* Midway Airlines, Inc.), 175 B.R. 239, 243−44 (Bankr. N.D. Ill. 1994) (same). Although the holdings in each of these cases has been called into question by the Supreme Court's *Seminole Tribe* opinion (no doubt to the delight of the states), the sheer number of decisions reveals that the states have been more active in the bankruptcy arena.

FN180 Even the Supreme Court has had a difficult time keeping the two doctrines straight. *See* Pennsylvania v. Union Gas Co., 491 U.S. 1, 24−25 (1989) (Stevens, J., concurring) (noting Court's inability to develop coherent doctrine of Eleventh Amendment immunity) (citing Hans v. Louisiana, 134 U.S. 1, 10 (1890)). In *Seminole Tribe*, Chief Justice Rehnquist states that "[i]t was well established in 1989 when *Union Gas* was decided that the Eleventh

Amendment stood for the constitutional principle that state sovereign immunity limited the federal courts' jurisdiction under Article III." *Seminole Tribe*, 1996 WL 134309 at *12. Justices Stevens and Souter note in their respective dissents that the majority blurs the distinction between the ancient common law doctrine of sovereign immunity and the separate doctrine of immunity from suit in federal court embodied in the Eleventh Amendment. Justice Stevens has taken pains many times to distinguish the two separate doctrines. *Id.* at *27−29; *Union Gas*, 491 U.S. at 25 (Stevens, J., concurring) (finding doctrine of sovereign immunity "has absolutely nothing to do with the limit on judicial power contained in the Eleventh Amendment). In his dissent in *Seminole Tribe*, Justice Souter further suggests that the majority has "constitutionalized" the doctrine of sovereign immunity such that it has become unalterable by Congress. *Seminole Tribe*, 1996 WL 134309 at *33 n.7 (Souter, J., dissenting). Whether the Eleventh Amendment embodies the common law doctrine sovereign immunity or is a separate limitation on the jurisdiction of the federal courts as outlined in Article III is a question that is fundamental to our system of government and one that will resurface. *Id.* at *33. The "shocking character of the majority's affront to a coequal branch of government" prompted Justice Stevens to note that the issue confronted in *Seminole Tribe* has been confronted by thirteen Supreme Court Justices, eight of whom determined that Congress does have the authority to abrogate the Eleventh Amendment pursuant to its Article I powers. *Id.* at *26.

FN181 *Union Gas*, 491 U.S. at 23 (Stevens, J., concurring). The doctrine of sovereign immunity originally was derived from the premise that the monarch (or sovereign) could do no wrong. *See* United States v. Nordic Village, 503 U.S. 30, 42 (1992) (Stevens, J., dissenting). The doctrine also has a practical basis, recognizing that governments are often strapped for cash and that the judiciary has no method for enforcing a monetary judgment issued against such entities. *See* Karen Cordry, *Sovereign Immunity Time to Come in from the Cold!*, AM. BANKR. INST. J., Sept. 1994, at 19, 19 (noting that governments are always short on funds).

FN182 *See Union Gas*, 491 U.S. at 24 (Stevens, J., concurring) (noting that "Congress has plenary power to subject states to suit in federal court"); *Nordic Village*, 503 U.S. at 33 (same).

FN183 *Nordic Village*, 503 U.S. at 33−34. In *Nordic Village*, the Supreme Court addressed the validity of the waiver contained in § 106, and found that it did not unequivocally express a waiver with respect to monetary damages assessed against a governmental unit. *Id.* at 34. The amended version of § 106 appears to be the sort of unequivocal expression required by the Court. *See* 11 U.S.C. § 106 (1994).

FN184 The Eleventh Amendment provides that "[t]he judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by citizens of another State, or by citizens or subjects of any foreign state." U.S. CONST. amend. XI. In a sense, the Supreme Court paved the way for the Eleventh Amendment with the decision in Chisholm v. Georgia, 2 U.S. (2 Dall.) 419 (1793), which held that suits against unconsenting states could be heard in federal court. *Id.* at 468. The Eleventh Amendment was passed and ratified within two years of the *Chisholm* decision. Welch v. Texas Dep't of Highways & Pub. Transp., 483 U.S. 468, 484 (1987).

FN185 *Seminole Tribe*, 1996 WL 134309 at *7 (quoting Dellmuth v. Muth, 491 U.S. 223, 227−28 (1989)); Hoffman v. Connecticut Dep't of Income Maintenance, 492 U.S. 96, 101 (1989) (citing Atascadero State Hospital v. Scanlon, 473 U.S. 234, 242 (1985)).

FN186 *Seminole Tribe*, 1996 WL 134309 at *6 (quoting Green v. Mansour, 474 U.S. 64, 68 (1985)).

FN187 *See* Fitzpartick v. Bitzer, 427 U.S. 445, 456 (1976) ("[W]e think that the Eleventh Amendment, and the principle of state sovereignty which it embodies, are necessarily limited by the enforcement of § 5 of the Fourteenth Amendment.") (citations omitted). The substantive provisions of the Fourteenth Amendment were "by express terms directed at the States . . . [and] `were intended to be . . . limitations of the power of the States and enlargements of the power of Congress.'" *Bitzer*, 427 U.S. at 453−54 (quoting Ex Parte Virginia, 100 U.S. 339, 345 (1880)).

FN188 U.S. CONST. art. I, § 8, cl. 4. *See Union Gas*, 491 U.S. at 24 (Stevens, J., concurring) (holding Congress has authority under Commerce Clause to abrogate Eleventh Amendment immunity).

FN189 U.S. CONST. art. I, § 8, cl. 4. The Supreme Court specifically left the question open in *Hoffman*, 492 U.S. at 104. *See* Sparkman v. Florida Dep't of Revenue (*In re* York−Hannover Devs., Inc.), 181 B.R. 271, 278 (Bankr. E.D.N.C.), *aff'd*, 190 B.R. 62 (E.D.N.C. 1995).

FN190 The only decision to actually address the effect of legislation enacted pursuant to an antecedent provision prior to *Seminole Tribe* was Pennsylvania v. Union Gas Co., 491 U.S. 1 (1989), which was overruled by *Seminole Tribe*. The Court's decision in *Union Gas* was split 5 to 4, with Justices Brennan, Marshall, Blackmun, and Stevens holding that Congress could abrogate Eleventh Amendment immunity pursuant to the Commerce Clause, U.S. CONST. art. 1, § 8, cl. 3. Justice White, who disagreed with the much of the plurality's reasoning, provided the fifth vote for the result. Justices Brennan, Marshall, Blackmun, and White are no longer on the Court, and Justices Rehnquist, O'Connor, Kennedy, and Scalia, all of whom dissented in *Union Gas*, are in the majority in *Seminole Tribe*. Until *Seminole Tribe*, no other Supreme Court decisions specifically addressed the question of whether Congress may abrogate Eleventh Amendment immunity when legislating pursuant to an antecedent constitutional provision. *See, e.g.*, Welch v. Texas Dept. of Highways & Pub. Transp., 483 U.S. 468, 475 (1987) (refraining from deciding whether Congress has power to waive Eleventh Amendment when legislating pursuant to Commerce Clause); Oneida County v. Oneida Indian Nation, 470 U.S. 226, 252 (1985) ("[a]ssuming, without deciding" that Congress has authority to waive Eleventh Amendment when legislating under Commerce Clause); Green v. Mansour, 474 U.S. 64, 68 (1985) (finding congressional waiver actually made pursuant to Eleventh Amendment, rather than antecedent provision).

FN191 The Seventh Circuit addressed congressional ability to abrogate Eleventh Amendment immunity pursuant to the Bankruptcy Clause and concluded that the Bankruptcy Clause provides Congress with sufficient authority to enact such provisions. McVey Trucking, Inc. v. Secretary of State (*In re* McVey Trucking, Inc.), 812 F.2d 311, 328 (7th Cir.), *cert. denied*, 484 U.S. 895 (1987). The result reached in *McVey* was overruled in Hoffman v. Connecticut Dep't of Income Maintenance, 492 U.S. 96, 100 (1989), but the holding regarding congressional authority to abrogate the Eleventh Amendment was not. *Id.* The *McVey* court examined the grants of plenary power in the Constitution and the Fourteenth Amendment, determined that there is no difference between the grants of power, and determined that under the plenary power contained in the Bankruptcy Clause, U.S. CONST. art.I, § 8, cl. 4, Congress could abrogate Eleventh Amendment immunity. *McVey*, 812 F.2d at 319−28. The *McVey* analysis recently was followed in *York−Hannover*, 181 B.R. at 277−78 (holding that plenary power granted to Congress under Bankruptcy Clause authorized abrogation of Eleventh Amendment immunity).

FN192 No. 94−12, 1996 WL 134309 (Mar. 27, 1996). *Seminole Tribe*, like so many of the Court's sovereign immunity decisions, was also a 5−4 decision. Chief Justice Rehnquist delivered the opinion and was joined by Justices Scalia, O'Connor, Kennedy (the dissenters in *Union Gas*) as well as Justice Thomas. Justice Stevens dissented, as did Justice Souter, who was joined by Justice Ginsberg and Breyer.

FN193 *Seminole Tribe*, 1996 WL 134309, at *16 (involving Eleventh Amendment immunity and abrogation under Indian Commerce Clause).

FN194 U.S. CONST. art. I, § 8, cl. 3.

FN195 Justice Stevens recognizes in his dissent that the Court's holding "prevents Congress from providing a federal forum for a broad range of actions against States, from those sounding in copyright and patent law, to those concerning bankruptcy, environmental law, and the regulation of our national economy." *Seminole Tribe*, 1996 WL 134309, at *18 (Stevens, J. dissenting). A writ of certiorari has been filed with the Court in *In re* Merchants Grain, Inc., 59 F.3d 630 (7th Cir. 1995), *petition for cert. filed*, 64 U.S.L.W. 3287 (U.S. Sept. 28, 1995) (No. 95−561). The question raised in that case, which involves Eleventh Amendment immunity and abrogation under the Bankruptcy Clause, appears to have been answered in *Seminole Tribe*, which addressed Article I powers generally.

FN196 The determination of whether Congress may abrogate States' sovereign immunity pursuant to an exercise of Article I power is nothing less than the determination of the proper role of the federal courts in federal−state relations. *See Union Gas*, 491 U.S. at 241 (Stevens, J., concurring).

FN197 Section 362(h) of the Bankruptcy Code provides that "[a]n individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and in appropriate circumstances, punitive damages." 11 U.S.C. § 362(h) (1994).

FN198 *In re* Hunter, 190 B.R. 118, 119 (Bankr. D. Colo. 1995) (refusing to hold party in contempt for violation of stay).

FN199 *See Ex parte* Young, 209 U.S. 123 (1908) (allowing injunctive relief against state officials to prevent violations of federal law notwithstanding assertion of sovereign immunity). Chief Justice Rehnquist notes three alternative methods to force a State to comply with federal law in *Seminole Tribe*, 1996 WL 134309 at *16 n.4. The federal government may sue a state in federal court, *see, e.g.*, United States v. Texas, 143 U.S. 621, 644−45 (1892), an individual can sue a state officer to be sure that such officer complies with federal law, *see, e.g.*, *Young*, 209 U.S. at 157−58, and the Supreme Court may review questions of federal law arising from State court decisions in which a State has consented to be sued, *see, e.g.*, Cohens v. Virginia, 19 U.S. (6 Wheat.) 264 (1821).

FN200 Section 510(c) allows the bankruptcy courts to equitably subordinate claims if the creditor's actions warrant such a sanction. 11 U.S.C. § 510(c)(1994).

FN201 *See* 11 U.S.C. §§ 362(h), 505, 522(f), 542, 545, 547 (1994).

FN202 The same issue arises with respect to federal taxes. *See* I.R.C. § 6672 (1994) (imposing responsible person liability); *see supra* notes 29−32 and accompanying text (discussing responsible person liability).

FN203 Only Hawaii, Montana, Nevada, Vermont, and Wyoming have not enacted specific provisions imposing liability on responsible persons.

FN204 *See, e.g.*, IND. CODE ANN. § 6−2.5−9−3 (Burns 1995) (stating individuals with duty to remit tax, holds it in trust for state); TEX. TAX CODE ANN. § 111.016(a) (West Supp. 1996) (stating that any person who receives or collects a tax or money represented to be a tax from another person holds such amount in trust for state and is liable to state for full amount collected plus any accrued interest or penalty).

FN205 *See* CAL. REV. & TAX. CODE § 6829 (West 1987 & Supp. 1996) (holding personally liable any party responsible for filing or payment of tax); ILL. ANN. STAT. ch. 35, para. 5/1002(d) (Smith−Hurd 1993) (holding personally liable any person required to collect or account for tax); KAN. STAT. ANN. § 79−3643 (1989) (same); N.J. STAT. ANN. § 54:32B−14(a) (West 1986) (same).

FN206 *See, e.g.*, COLO. REV. STAT. § 39−21−116.5 (1994) (limiting liability to partners and corporate officers); IOWA ADMIN. CODE r. 701−12.15 (1994) (requiring ownership interest in corporation before liability imposed required); LA. REV. STAT. ANN. § 47:1561.1 (West 1990) (limiting liability to corporate officers and directors); MISS. CODE ANN. § 27−65−55 (1990 & Supp. 1995) (holding jointly and severally liable persons with 10% or more interest in corporation or persons with 10% or more interest in limited liability companies with 35 or fewer owners); S.D. CODIFIED LAWS ANN. §§ 10−45−55, 10−46A−13, 10−46B−11 (1989) (limiting liability to corporate officers).

FN207 "Any person" may be a defined term (either statutorily or judicially) with respect to a given statute. Accordingly, it is imperative that counsel determine whether the term is defined and if so, who is covered.

FN208 *See* 11 U.S.C. § 105 (1994) (authorizing court to issue any order or judgment necessary to carry out provisions of Bankruptcy Code).

FN209 The codebtor stay in chapter 13 is a limited exception. *Id.* § 1301. However, because this provision only applies to "consumer" debts, it does not prevent collection of taxes from nonbankrupt parties. *See, e.g.*, *In re* Goldsby, 135 B.R. 611, 613 (Bankr. E.D. Ark. 1992) (allowing tax levy against debtor's nonbankrupt wife); *In re* Gault, 136 B.R. 736, 738 (Bankr. E.D. Tenn. 1991) (finding no violation of codebtor stay when IRS mailed notice of lien to

nondebtor husband).

FN210 *See* A.H. Robins Co. v. Piccinin (*In re* A.H. Robins Co.), 788 F.2d 994, 999−1000 (4th Cir.) (staying actions against nondebtor codefendant due to "unusual circumstances"), *cert. denied*, 479 U.S. 876 (1986); Johns−Manville Corp. v. Asbestos Litig. Group (*In re* Johns−Manville Corp.), 33 B.R. 254, 263 (Bankr. S.D.N.Y. 1983) (staying actions against debtor's officers, directors or employees), *aff'd*, 40 B.R. 219 (S.D.N.Y. 1984). In *Robins* and *Johns−Manville*, the bankruptcy court enjoined an estimated 195,000 future, unidentified tort claimants from filing suit in order to allow the debtors to proceed to confirmation.

FN211 *See* Chase Manhattan Bank v. Third Eighty−Ninth Assocs. (*In re* Third Eighty−Ninth Assocs.), 138 B.R. 144, 149 (S.D.N.Y. 1992) (staying creditors from proceeding against guarantor of chapter 11 debtor); F.T.L., Inc. v. Crestar Bank (*In re* F.T.L., Inc.), 152 B.R. 61, 64 (Bankr. E.D. Va. 1993) (enjoining creditor from pursuing action against guarantor of debtor's obligation); Codfish Corp. v. FDIC (*In re* Codfish Corp.), 97 B.R. 132 (Bankr. D.P.R. 1988) (enjoining creditor from prosecuting action against guarantor and chief executive officer of debtor corporation).

F212 *See, e.g.*, *In re* Original Wild West Foods, Inc., 45 B.R. 202, 208 (Bankr. W.D. Tex. 1984) (enjoining IRS from collecting tax penalty from one of debtor's officers); Datair Sys. Corp. v. Starkey (*In re* Datair Sys. Corp.), 37 B.R. 690, 697 (Bankr. N.D. Ill. 1983) (finding injunction against IRS proper where debtor proves equity jurisdiction).

FN213 The converse is also true. If the injunction is improvidently granted, it may only delay the inevitable and ensure that neither party has sufficient resources to pay the debt. As a result, courts must exercise caution in considering such relief.

FN214 28 U.S.C. § 1341 (1994).

FN215 *Id.* The language of the Tax Injunction Act, which is applicable to state tax collections, is similar to that of the Anti−Injunction Act, I.R.C. § 7421 (1994), applicable to federal tax collections by the IRS. Although the language of the Tax Injunction Act is slightly broader than that of the Anti−Injunction Act, the body of case law that has been developed under the Anti−Injunction Act is directly relevant to the interpretation of the Tax Injunction Act. *Cf.* American Hardwoods, Inc. v. Deutsche Credit Corp. (*In re* American Hardwoods, Inc.), 885 F.2d 621, 625 (9th Cir. 1989) (finding § 105 supersedes neither Anti−Injunction Act, nor Tax Injunction Act).

FN216 *See* 28 U.S.C. § 1341 (1994).

FN217 *See* 11 U.S.C. § 105(a) (1994) (limiting power of court in issuing injunctions to situations necessary or appropriate to carry out provisions of Bankruptcy Code).

FN218 *See, e.g.*, American Bicycle Ass'n v. United States (*In re* American Bicycle Ass'n), 895 F.2d 1277, 1279 (9th Cir. 1990) (holding that nothing in Bankruptcy Code indicates Congress's intent to override Anti−Injunction Act); LaSalle Rolling Mills, Inc. v. United States (*In re* LaSalle Rolling Mills, Inc.), 832 F.2d 390, 394 (7th Cir. 1987) (finding § 505 provided no bankruptcy exception to Anti−Injunction Act); A to Z Welding & Mfg. Co. v. United States, 803 F.2d 932, 933 (8th Cir. 1986) (finding no congressional intent to override Anti−Injunction Act); *In re* John Renton Young, Ltd., 87 B.R. 635, 637 (Bankr. D. Nev. 1988) (holding Code did not authorize act in contravention of Anti−Injunction Act).

FN219 *See* Bear v. Coben (*In re* Golden Plan, Inc.), 829 F.2d 705, 713 (9th Cir. 1986) (stating equitable power must be strictly confined within prescribed limits of Code); United States v. Sutton, 786 F.2d 1305, 1308 (5th Cir. 1986) (stating § 105 does not authorize bankruptcy courts to create substantive rights or to act as a "roving commission to do equity"); Johnson v. First Nat'l Bank, 719 F.2d 270, 278 (8th Cir. 1983) (reasoning that bankruptcy courts' broad equitable powers must be exercised in manner consistent with Code), *cert. denied*, 465 U.S. 1012 (1984).

FN220 *See* 11 U.S.C. § 505 (1994); American Principals Leasing Corp. v. United States, 904 F.2d 477, 481 (9th Cir. 1990) (holding § 505 permits determination by bankruptcy court of debtor's liability but not nondebtor's liability); Brandt−Airflex, Corp. v. Long Island Trust Co. (*In re* Brandt−Airflex, Corp.), 843 F.2d 90, 96 (2d Cir. 1988) (finding

no bankruptcy court jurisdiction over nondebtor liability under § 505); United States v. Huckabee Auto Co., 783 F.2d 1546, 1549 (11th Cir. 1986) (same); *In re* Cadillac Recreation, Inc., 159 B.R. 244, 247 (Bankr. C.D. Ill. 1993) (same). *But see* Quattrone Accountants, Inc. v. IRS, 895 F.2d 921, 926 (3d Cir. 1990) (stating § 505 can extend jurisdiction to nondebtor liability if close nexus established with debtor estate).

FN221 *See, e.g.*, 11 U.S.C. § 524 (1994) (discussing effect of discharge on *debtor's* personal liability).

FN222 *See* cases cited *supra* note 220 and accompanying text.

FN223 11 U.S.C. § 362 (1994). *See* Teachers Ins. & Annuity Ass'n v. Butler, 803 F.2d 61, 65 (2d Cir. 1986) (finding automatic stay limited to debtors and do not encompass nonbankruptcy codefendants).

FN224 11 U.S.C. § 524(e) (1994). These special circumstances are enumerated in § 524(a)(3) and concern community property. *Id.* § 524(a)(3).

FN225 *Id.* § 524(e).

FN226 *Id.* § 524(a)(2).

FN227 *See* American Hardwoods, Inc. v. Deutsche Credit Corp. (*In re* American Hardwoods, Inc.), 885 F.2d 621, 626 (9th Cir. 1989) (concluding that § 524 limits court's equitable powers under § 105 to order discharge of liabilities of nondebtors).

FN228 Mass tort cases are in fact a different animal. Although § 105 injunctions might not be supported under current law even in those cases, the unusual circumstances encountered therein serve as some justification for such injunctions.

FN229 The authors represent more than one viewpoint on this issue. Ms. Barsalou, who prepared most of this section, believes that the Anti−Injunction Act reflects the correct policy and that the Commission should place limits on the use of § 105 to prevent its use against state taxing authorities. Mr. Sather believes that there is a legitimate use for § 105 in reorganization cases where the likelihood that the taxes will be paid in full by the corporate debtor exceeds the prejudice to the taxing authority in delaying collection from third parties. Mr. Sather acknowledges that this would be a departure from existing law and should not be lightly considered. All parties agree that it is bad policy to allow § 105 to be used as a de facto means of amending the Anti−Injunction Act.

FN230 11 U.S.C. § 505 (1994). The text of § 505(a) reads, in pertinent part, as follows:

(a) (1) Except as provided in paragraph (2) of this subsection, the court may determine the amount or legality of *any* tax, any fine or penalty relating to a tax, or any addition to tax, whether or not previously assessed, whether or not paid, and whether or not contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction.

(2) The court may not so determine

(A) the amount or legality of a tax, fine, penalty, or addition to tax if such amount or legality was contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction before the commencement of the case under this title.

Id. (emphasis added).

FN231 IRS v. Sulmeyer (*In re* Grand Chevrolet, Inc.), 153 B.R. 296, 300 (Bankr. C.D. Cal. 1993); *In re* Swan, 152 B.R. 28, 30 (Bankr. W.D.N.Y. 1992).

FN232 For decisions involving the use of section 505, see Kellogg v. United States (*In re* West Texas Marketing Corp.), 54 F.3d 1194, 1200 (5th Cir.) (finding nothing in § 505 to prevent successive requests for prompt determination of all relevant tax periods upon completion), *cert. denied*, 116 S. Ct. 523 (1995); Holywell Corp. v. Bank of N.Y. (*In re* Holywell Corp.), 177 B.R. 991, 998−99 (S.D. Fla. 1995) (holding that bankruptcy court had core jurisdiction over tort counterclaims asserted by chapter 11 debtor−defendants in tax liability suit); Tavormina v. United States (*In re* Seslowsky), 182 B.R. 612, 615 (Bankr. S.D. Fla. 1995) (deciding that chapter 7 trustee improperly sought determination of estate's unpaid tax liability for undisputed amount).

FN233 28 U.S.C. § 1334 (1994).

FN234 11 U.S.C. § 505(a)(A) (1994).

FN235 28 U.S.C. § 1334(c)(1) (1994).

FN236 *Id.* § 1334(b).

FN237 Wood v. Wood (*In re* Wood), 825 F.2d 90, 93 (5th Cir. 1987) (quoting Pacor, Inc. v. Higgins, 743 F.2d 984, 994 (3d Cir. 1984)).

FN238 *See* cases cited *supra* note 220.

FN239 Campbell Enters., Inc. v. United States (*In re* Campbell Enters., Inc.), 66 B.R. 200, 202−03 (Bankr. D.N.J. 1986); *In re* Original Wild West Foods, Inc., 45 B.R. 202, 206 (Bankr. W.D. Tex. 1984).

FN240 11 U.S.C. § 505(a)(2)(A) (1994).

FN241 *See In re* Ishpeming Hotel Co., 70 B.R. 629, 632 (Bankr. W.D. Mich. 1986) (determining court has jurisdiction to determine legality of tax claims absent prior contest and adjudication).

FN242 *See* Green v. Bruce W. Brooks Gen. Contractor, Inc. (*In re* Bruce W. Brooks Gen. Contractor, Inc.), 27 B.R. 9, 11 (Bankr. D. Ore. 1982) (holding no res judicata effect when debtor's status determined by default).

FN243 *See In re* Super Van, Inc., 161 B.R. 184, 192−93 (Bankr. W.D. Tex. 1993) (stating that only final adjudications can be barred by § 505(a)(2)(A)); *In re* B & B Marine Sales & Serv., 149 B.R. 465, 467 (Bankr. N.D. Ohio 1992) (finding jurisdiction where appeal pending prior to debtor filing); *In re* Electronic Theatre Restaurants, Inc., 85 B.R. 45, 47 (Bankr. N.D. Ohio 1988) (finding no full adjudication of matter and thus no impediment to court's jurisdiction).

FN244 *In re* Galvano, 116 B.R. 367, 374 (Bankr. E.D.N.Y. 1990) (disallowing redetermination of taxes owed where there were prior state adjudications); *Ishpeming Hotel*, 70 B.R. at 632 (hearing in front of municipality board prevented tax redetermination).

FN245 *See* IRS v. Teal (*In re* Teal), 16 F.3d 619, 622 (5th Cir. 1994) (stating that settlement agreement between IRS and taxpayer is considered final judgment on merits for purposes of res judicata); El Tropicano, Inc. v. Garza (*In re* El Tropicano, Inc.) 128 B.R. 153, 158 (Bankr. W.D. Tex. 1991) (finding that negotiated settlements count as adjudications within meaning of § 505(a)(2)(A)).

FN246 *See* Laptops Etc. Corp. v. District of Columbia (*In re* Laptops Etc. Corp.), 164 B.R. 506, 514 (Bankr. D. Md. 1993) (holding bankruptcy court has jurisdiction over tax issue when both initial assessment and subsequent hearing transpired postpetition); *In re* TMI Growth Properties, 109 B.R. 403, 404 (Bankr. N.D. Cal. 1990) (holding § 505(a)(2)(A) does not apply to postpetition litigation).

FN247 11 U.S.C. § 505(a)(1) (1994).

FN248 *El Tropicano*, 128 B.R. at 160−61 (discussing discretionary review under § 505).

FN249 *See In re* Chicago, Milwaukee, St. Paul & Pac. R.R., 6 F.3d 1184, 1189 (7th Cir. 1993) (discussing relevant factors courts may consider in support of discretionary abstention).

FN250 *See* Building Technologies Corp. v. City of Hannibal (*In re* Building Technologies Corp.), 167 B.R. 853, 858 (Bankr. S.D. Ohio 1994) (discussing complexity of state law as one factor in courts considering abstention).

FN251 *See* Smith v. United States (*In re* Smith), 122 B.R. 130, 133 (Bankr. M.D. Fla. 1990) (stating abstention would only be appropriate where interests of creditors and debtors not served).

FN252 *See, e.g.*, *In re* St. John's Nursing Home, Inc., 154 B.R. 117, 125 (Bankr. D. Mass. 1993) (finding that in order to determine postpetition liability, trustee must "properly request" refund from taxing authority under § 505(a)(2)(B)), *aff'd*, 169 B.R. 795 (D. Mass. 1994); Halpern v. Commissioner, 96 T.C. 895, 900 (1991) (citing *In re* Mirman, 98 B.R. 742, 745 (Bankr. E.D. Va. 1989)) ("[T]he bankruptcy court obtains jurisdiction over Federal tax liabilities otherwise properly characterized as postpetition liabilities.").

FN253 28 U.S.C. § 959 (1994), in pertinent part, reads:

[A] debtor in possession, shall manage and operate the property in his possession as such trustee, . . . according to the requirements of the valid laws of the state in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

Id.

FN254 United States v. New York Creditmen's Adjustment Bureau (*In re* Samuel Chapman, Inc.), 394 F.2d 340, 342 n.2 (2d Cir.) ("[The Act] does not purport to exempt the trustee from the operation of state laws, or to relieve the estate from liability for the trustee's delinquencies."), *cert. denied*, 393 U.S. 923 (1968).

FN255 *See In re* TMI Growth Properties, 109 B.R. 403, 405 (Bankr. N.D. Cal. 1990) (interpreting language of § 505 to permit "debtor two bites of the apple").

FN256 *See infra* notes 263−65 and accompanying text.

FN257 *See* 11 U.S.C. § 505 (1994).

FN258 313 U.S. 132 (1941).

FN259 S. REP. NO. 989, 95th Cong., 2d Sess. 11 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5853.

FN260 *Id.* at 144−45.

FN261 *Id.* at 145.

FN262 *Id.* (footnote omitted).

FN263 S. REP. NO. 989, *supra* note 259, at 11, *reprinted in* 1978 U.S.C.C.A.N. at 5853.

FN264 *In re* Quality Beverage Co. Inc., 170 B.R. 310, 312−13 (Bankr. S.D. Tex. 1994); *In re* Fairchild Aircraft Corp., 124 B.R. 488, 491−92 (Bankr. W.D. Tex. 1991).

FN265 *Fairchild*, 124 B.R. at 491−92 (citations omitted).

FN266 *See In re* Ishpeming Hotel Co. 70 B.R. 629, 632 (Bankr. W.D. Mich. 1986) (holding that because Board of Review was quasi−judicial or administrative body, bankruptcy court could not redetermine assessed tax valuations).

FN267 *See* TEX. TAX CODE ANN. § 1.04(9) (West 1992) (defining assessed value as "assessment of property for taxation").

FN268 Arkansas Corp. Comm'n v. Thompson, 313 U.S. 132, 139 (1941) (explaining that corporation commission has control over valuation and assessment of all property in administration of state tax laws).

FN269 *Id*. at 145.

FN270 *See, e.g.*, COL. REV. STAT. ANN. § 39−1−101 (West 1994) (legislative intent to determine "actual value at which . . . property shall be assessed for taxation"); FLA. STAT. ANN. § 192.001(1),(2) (West 1989 & Supp. 1996) (defining "property tax" as "a tax based upon the assessed value of the property" and "assessed value of property" as an "annual determination of the just or fair market value of . . . property"); N.J. STAT. ANN. § 54:4−66 (c) (West 1986 & Supp. 1995) ("[W]hen calculating taxes, . . . `assessed value' means the `net valuation taxable of each parcel of property'"); N.Y. REAL PROP. TAX LAW § 102(2) (McKinney 1984) (referring to "assessments" as "valuation of real property" and "whether or not real property is subject to taxation"); TEX. TAX CODE ANN. § 1.04(9) (West 1992) (defining "assessed value" as amount determined by multiplying appraised value by applicable assessment ratio).

FN271 BLACK'S LAW DICTIONARY 116 (6th ed. 1990) (emphasis added).

FN272 There are compelling reasons why *Arkansas Corp.* should continue to be good law. First, property taxes are uniquely local in nature and many states have created elaborate systems to uniformly appraise all of the property within a locality. Tax burdens are allocated based upon these appraisals and if federal courts intervene in issues of local valuation, the chances for nonuniform values increase. While bankruptcy courts have extensive experience valuing property, there is no guarantee that they will appraise property in the same manner as a state agency would have. Second, bankruptcy courts deal with financially distressed debtors. Given the benefits of hindsight, bankruptcy courts may be overly willing to lower values based on current circumstances. When bankruptcy courts lower appraised values, they shift the tax burden from the debtor to other taxpayers. Property taxes are qualitatively different from other taxes. A property tax divides a given tax burden among a group of taxpayers based upon a known level of total values. Sales and income taxes, on the other hand, seek to raise a projected level of income based upon taxable sales and taxable income which are forecasted to occur in the aggregate, but which are not known in advance with respect to any given taxpayer. When bankruptcy courts determine the amounts of sales or income taxes, they are merely calculating the amount due under state law. When they determine property tax values, however, they are reallocating the tax burden.

FN273 *See In re* Piper Aircraft Corp., 171 B.R. 415, 420 (Bankr. S.D. Fla. 1994) (holding debtor may challenge prior assessed tax liability in bankruptcy court); *In re* Quality Beverage Co., 170 B.R. 310, 312−13 (Bankr S.D. Tex. 1994) (finding removal of valuation adjudication to bankruptcy court is consistent with the intended function of § 505); *In re* AWB Assocs., G.P., 144 B.R. 270, 276 (Bankr. E.D. Pa. 1992) (holding court may redetermine tax assessments since abstention would result in significant prejudice to estate); *In re* Fairchild Corp., 124 B.R. 488, 491 (Bankr. W.D. Tex. 1991) (finding court has jurisdiction to redetermine debtor's tax liability); *In re* Fiedel Country Day Sch., 55 B.R. 229, 231 (Bankr. E.D.N.Y. 1985) (stating that § 505 allows bankruptcy court jurisdiction to redetermine postpetition taxes).

FN274 *See* City of Amarillo v. Eakens, 399 F.2d 541, 544 (5th Cir. 1968) (explaining that "by authorizing redeterminations . . . [the Act] serves to protect creditors of the bankruptcy from the bankrupt's lack of diligence or interest") (citation omitted), *cert. denied*, 393 U.S. 1051 (1969).

FN275 *Id*. (quoting 6A COLLIER ON BANKRUPTCY 183 (14th ed. 1965)).

FN276 Arkansas Corp. Comm'n v. Thompson, 313 U.S. 132, 145 (1941).

FN277 11 U.S.C. §§ 544, 545 (1994). Sections 544 and 545 are based upon rights available to creditors under state law or transactions which may be avoided under state law. Sections 547 and 548 are limited to transactions occurring within either 90 days or one year prior to bankruptcy. *Id.* §§ 547, 548.

FN278 In one case in which one of the authors was involved, the debtor sought to redetermine values going back ten years and sought a refund of taxes paid pursuant to those valuations.