No. _____

IN THE

Supreme Court of the United States

DONALD W. DAWES and PHYLLIS C. DAWES,
Petitioners,

v.

UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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Dated: August 17, 2011

QUESTION PRESENTED

As respondent has acknowledged previously in multiple filings, this case involves the same question presented in *Hall v. United States*, No. 10-875 (cert. granted June 13, 2011):

Whether 11 U.S.C. § 1222(a)(2)(A) authorizes the bankruptcy court, in a case brought under Chapter 12 of the Bankruptcy Code, to treat as a dischargeable non-priority claim a federal tax debt arising out of the debtor's post-petition sale of a farm asset.

PARTIES TO THE PROCEEDING

In addition to the parties to the proceeding, who are identified in the caption, Edward J. Nazar is also being served as a trustee.

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OPINIONS BELOW

The opinion of the United States Court of Appeals for the Tenth Circuit, Pet. App. 1a, is available at 2011 WL 2450930 (10th Cir. June 21, 2011). The opinion of the United States District Court for the District of Kansas, Pet. App. 21a, is reported at 415 B.R. 815 (D. Kan. 2009). The opinion of the United States Bankruptcy Court for the District of Kansas, Pet. App. 42a, is reported at 382 B.R. 509 (Bankr. D. Kan. 2008).

JURISDICTION

The Tenth Circuit issued its opinion on June 21, 2011. Pet. App. 1a. The Tenth Circuit denied rehearing on July 5, 2011. Pet. App. 72a. This Court's jurisdiction rests on 28 U.S.C. § 1254(1). The jurisdiction of the bankruptcy court and district court rested on 28 U.S.C. §§ 157, 158, and 1334.

RELEVANT STATUTORY PROVISIONS

The provisions of 11 U.S.C. §§ 503(b)(1)(B)(i), 507(a)(2), 507(a)(8), 541(a), 1207(a), 1222(a)(2)(A), 1305 and 26 U.S.C. §§ 1398, 1399 are reprinted at Pet. App. 74a-93a pursuant to Supreme Court Rule 14(f). U.S. CONST. art. I, § 8, cls. 1 and 4 are reprinted at Pet. App. 74a, also pursuant to that rule.

STATEMENT OF THE CASE

Chapter 12 of the Bankruptcy Code provides for the bankruptcy relief of family farmers and fishermen. 11 U.S.C. §§ 1201-1231. Part of that chapter, Section 1222(a)(2)(A) of the Code, permits family farmers to treat "a claim owed to a governmental unit that arises as a result of the sale . . . of any farm asset used in the debtor's farming operation" as a general unsecured claim that is not entitled to priority status and is dischargeable after less than full payment under the debtor's bankruptcy plan. *Id.* § 1222(a)(2)(A).

Petitioners here, like Petitioners in *Hall v. United States*, No. 10-875, 2011 WL 2297804 (U.S. June 13, 2011), owned and operated a family farm. On July 14, 2006, Petitioners in this case filed a *pro se* petition for bankruptcy relief under Chapter 7 of the Code in response to the collection efforts of the Internal Revenue Service ("IRS"). Pet. App. 44a. By operation of law, the filing of a Chapter 7 petition causes the creation of a bankruptcy estate consisting of the debtors' real and personal property. 11 U.S.C. § 541. Thus, when Petitioners filed their Chapter 7 case, ownership of their family farm passed to their bankruptcy estate.

Following retention of counsel, Petitioners' case was converted to a Chapter 12 proceeding.

Pet. App. 44a. At the time of this conversion, ownership of Petitioners' real and personal property continued to be vested in their bankruptcy estate. *See* 11 U.S.C. §§ 348, 1207. The IRS filed a stay relief motion to permit it to complete the marshal sale of eight parcels of property of the estate. Pet. App. 45a.

On November 13, 2006, Petitioners filed a Chapter 12 plan of reorganization. Petitioners' plan proposed to pay a portion of the IRS's claim against Petitioners by surrendering the eight parcels to the IRS. Pet. App. 45a. The plan further proposed that "pursuant to 11 U.S.C. § 1222(a)(2)(A), all claims of the IRS or Kansas Department of Revenue that arise post-petition as a result of the sale, transfer, exchange, or other disposition of the [eight parcels] shall be treated as a general unsecured claim not entitled to priority under § 507." Pet. App. 45a. The IRS objected to the proposed unsecured treatment of claims for taxes arising from the post-petition sale of the parcels. Pet. App. 45a-46a. The parcels were subsequently sold while they were property of Petitioners' bankruptcy estate, and the parties agreed that the sale would result in significant capital gains taxes incurred as a result. Pet. App. 46a.

On August 9, 2007, Petitioners sought partial summary judgment and requested the bankruptcy court to rule that "§ 1222(a)(2)(A) allows

[Petitioners] to provide in their Chapter 12 plan that the IRS' post-petition capital gains tax claim incurred as a result of the IRS' forced sale of the [Petitioners'] real estate is an unsecured claim." Pet. App. 46a. On September 24, 2007, the IRS filed its Reply and Cross Motion for Partial Summary Judgment, arguing that "§ 1222(a)(2)(A) does not apply to capital gains from postpetition sales." Pet. App. 46a.

The IRS argued that Section 1399 of the Internal Revenue Code prevents Section 1222(a)(2)(A) from affording unsecured status to its claim arising from post-petition disposition of estate property. Pet. App. 53a. Section 1399 provides that "[e]xcept in any case to which section 1398 applies, no separate taxable entity shall result from the commencement of a case under [the Bankruptcy Code]." 26 U.S.C. § 1399. Section 1398 applies, with certain exceptions that are not relevant here, to "any case under chapter 7 (relating to liquidations) or chapter 11 (relating to reorganizations) of [the Bankruptcy Code] in which the debtor is an individual." *Id.* § 1398(a).

Petitioners argued that a Chapter 12 debtor can treat post-petition income taxes as administrative expenses of the bankruptcy estate and that such expenses are subject to the protections of Section 1222(a)(2)(A), which affords the expenses unsecured non-priority status. Pet.

App. 51a. The bankruptcy court below agreed with Petitioners and held that "the capital gains taxes arising from the postpetition sale of Debtors' real property are not prohibited from administrative expense treatment because the filing of a Chapter 12 case does not create a new taxpaying entity." Pet. App. 70a. Accordingly, the bankruptcy court held that "the capital gains tax liability arising from the sale of Debtors' farm property is within the § 1222(a)(2)(A) exception to the requirement that all claims entitled to priority under § 507 be paid in full in deferred cash payments." Pet. App. 70a.

The district court affirmed, holding that the bankruptcy court "correctly granted the debtors' motion for summary judgment as to the construction of section 1222(a)(2)(A)." Pet. App. 40a-41a. The court noted that "the purpose of Chapter 12 bankruptcy . . . is to allow the debtors to pay their debts while they maintain control of their property and attempt to continue the farm business." Pet. App. 40a. According to the district court, "[t]reating capital gain taxes incurred post-petition as an administrative expense of the estate – and consequently as an unsecured claim – is consistent with the language of section 1222(a)(2)(A) and accomplishes the statute's clear remedial purpose." Pet. App. 40a.

Despite the well reasoned decisions of both the bankruptcy court and the district court, the

Tenth Circuit subsequently reversed the district court and held that "post-petition federal income taxes are not 'incurred' by a Chapter 12 'estate' for purposes of § 503(b)(1)(B)(i)." Pet. App. 20a. Instead, the court held that the taxes were incurred by Petitioners personally and outside the bankruptcy even though they were incurred post-petition and pre-confirmation. Pet. App. 20a. In light of that determination, the court held that the post-petition tax liabilities were "not eligible for treatment as unsecured claims under § 1222(a)(2)(A)" as proposed in Petitioners' reorganization plan. Pet. App. 20a.

REASONS FOR GRANTING THE WRIT

On June 13, 2011, this Court granted the petition for a writ of certiorari in *Hall v. United States*, No. 10-875, 2011 WL 2297804 (U.S. June 13, 2011), in order to consider the very same question presented in this case: "[w]hether 11 U.S.C. § 1222(a)(2)(A) authorizes the bankruptcy court, in a case brought under Chapter 12 of the Bankruptcy Code, to treat as a dischargeable non-priority claim a federal tax debt arising out of the debtor's post-petition sale of a farm asset." *Hall v. United States*, No. 10-875, 2011 WL 1837843 (U.S. May 13, 2011) ("U.S. *Hall* Cert. Br.").

The Court should hold this petition pending the Court's decision in *Hall v. United States*. Following this Court's decision in *Hall*, it should

(if appropriate) grant the petition, vacate the judgment below, and remand for further proceedings in light of its decision in *Hall*.

Like the Ninth Circuit's decision in *United States v. Hall*, 617 F.3d 1161, 1163 (9th Cir. 2010), the Tenth Circuit's decision below directly conflicts with the Eighth Circuit's opinion in *Knudsen v. IRS*, 581 F.3d 696 (8th Cir. 2009). Because of this circuit split, which can only be resolved by this Court, the courts below are inconsistently interpreting the Bankruptcy Code and the Internal Revenue Code on an issue of significant importance to the farming community.

A. This Case Presents the Same Question for Review This Court Has Agreed to Consider in *Hall v. United States*, No. 10-875.

In *Hall*, the Court granted certiorari to consider the identical question presented in this case, namely "[w]hether 11 U.S.C. § 1222(a)(2)(A) authorizes the bankruptcy court, in a case brought under Chapter 12 of the Bankruptcy Code, to treat as a dischargeable non-priority claim a federal tax debt arising out of the debtor's post-petition sale of a farm asset." U.S. *Hall* Cert. Br., 2011 WL 1837843, at *1.

In its response to the petition for a writ of certiorari in *Hall*, the United States agreed with the petitioners in *Hall* "that this Court should grant review to resolve the conflict between the Eighth and Ninth Circuits regarding the proper treatment in Chapter 12 bankruptcy proceedings of post-petition tax liabilities resulting from the sale of farm assets." *Id.* at *14. In its certiorari brief, the United States specifically cited this case and noted that "[a]lthough the Eighth and Ninth Circuits are the only two courts of appeals to have decided the question presented, the same question is presented in two cases pending in the Tenth Circuit," of which this case is one. *Id.* at *13 & n.7. In the proceedings below in this case, the United States filed two Rule 28(j) letters to inform the Tenth Circuit of the Ninth Circuit's decision in *Hall* and this Court's subsequent grant of the petition for writ of certiorari in that case. *United States v. Dawes (In re Dawes)*, No. 09-3129 (10th Cir. Aug. 23, 2010); *United States v. Dawes (In re Dawes)*, No. 09-3129 (10th Cir. June 13, 2011). Those letters took the same position that the issues to be decided in *Hall* and this case are one and the same.

Accordingly, this Court should hold this petition for writ of certiorari pending the Court's ruling in *Hall*. Once *Hall* has been decided, the Court should (if appropriate) grant the instant petition, vacate the judgment below, and remand for further proceedings consistent with *Hall*. *See*

Lawrence ex rel. Lawrence v. Chater, 516 U.S. 163, 166-67 (1996) (per curiam) (explaining circumstances in which a "GVR" is appropriate); *Stutson v. United States*, 516 U.S. 163, 181 (1996) (Scalia, J., dissenting) ("We regularly hold cases that involve the same issue as a case on which certiorari has been granted and plenary review is being conducted in order that (if appropriate) they may be 'GVR'd' when the case is decided.") (italics omitted).

B. Like *Hall*, This Case Presents a Circuit Split.

1. A Circuit Split Exists as to the Treatment of Post-petition Income Taxes in Chapter 12 Bankruptcy Cases.

The circuit split that animates this petition for writ of certiorari is now well established. The Eighth Circuit was the first of the three Courts of Appeals to consider the question presented (whether post-petition taxes incurred by the debtors should be considered administrative expenses) in *Knudsen v. IRS*, 581 F.3d 696 (8th Cir. 2009). As the Eighth Circuit summarized, "[a]s administrative expenses, the taxes would have priority status under 11 U.S.C. § 507(a)(2) via 11 U.S.C. § 503(b)(1)(B)(i), thereby allowing the Chapter 12 plan to treat such expenses as nonpriority unsecured claims under section 1222(a)(2)(A)." *Knudsen*, 581 F.3d at 708.

As it did in the proceedings below, the IRS argued in *Knudsen* that postpetition taxes are not administrative expenses under section 503(b)(1)(B)(i) because they are not "incurred by the estate," as that provision requires. 581 F.3d at 708. Rejecting this argument, the Eighth Circuit held that "incurred by the estate" means "incurred postpetition" based both on precedent and the plain language of section 1222(a)(2)(A), which does not restrict its application to pre-petition sales. *Id.* at 708-09. Moreover, the Eighth Circuit emphasized that it was only the Internal Revenue Code, "*not the Bankruptcy Code*," that creates a "separate taxable entity" in cases filed by petitioners under Chapters 7 and 11 but not in cases filed under Chapters 12 and 13. *Id.* at 709 (italics in original) (citing 26 U.S.C. §§ 1398, 1399). Finally, the Eighth Circuit noted that despite the lack of a "separate taxable entity" in a Chapter 12 case, an "estate" still exists. *Id.* (citing 11 U.S.C. § 1207(a)). Accordingly, it held that section 1222(a)(2)(A) applies to post-petition sales of farm assets. *Id.* at 710.

The next Court of Appeals to consider the question came to the opposite conclusion. In *Hall*, the Ninth Circuit held that the post-petition tax on the sale of the farm was not "incurred by the estate" because section 1399 of the Internal Revenue Code provides that a chapter 12 estate cannot incur taxes. 617 F.3d at 1163.

The Ninth Circuit decided that, because the chapter 12 estate is not a taxable entity, it could not "incur" a tax, and thus the post-petition tax did not qualify as an administrative expense under section 503(b)(1)(B)(i), was not entitled to priority under section 507, and could not get the benefit of section 1222(a)(2)(A). *Id.* at 1163-64.

The court rejected the debtors' argument that it did not matter whether the estate could incur a tax because the point was *when* the tax was incurred. *Id.* at 1165. Specifically, the Ninth Circuit held that "just because all apples are fruits does not mean all fruits are apples. Likewise, although all taxes 'incurred by the estate' are 'incurred post-petition,' not all taxes 'incurred postpetition' are 'incurred by the estate.'" *Id.* The court also rejected the Halls' argument that the Internal Revenue Code should not trump the Bankruptcy Code because Congress was "not aware of the relevance of the former when drafting the latter." *Id.* The Ninth Circuit instead "assume[d] that Congress [was] aware of existing law when it passe[d] [the] legislation" and treated the Internal Revenue Code as equally relevant to the dispute as the Bankruptcy Code. *Id.* at 1166.

In dissent, Judge Paez wrote that "Congress's intent was clear: it wanted to help family farmers keep their farms by allowing them to sell farm assets to pay off debts without being

liable for the full amount of any capital gains tax arising from the sale, regardless of whether they sold the assets before or after filing their Chapter 12 petition." *Id.* at 1168 (Paez, J., dissenting). He further stated that "[r]ather than follow the course proposed by the majority, I would follow the reasoning of the Eighth Circuit in *Knudsen v. IRS*, 581 F.3d 696 (8th Cir. 2009) . . . . This approach would honor Congress's clear intent and avoid an unwarranted circuit split." *Hall,* 617 F.3d at 1168 (Paez, J., dissenting).

The decision below deepened this circuit split. Siding with the majority in *Hall*, the Tenth Circuit held that post-petition federal income taxes are not incurred by a Chapter 12 estate for purposes of section 503(b)(1)(B)(i); rather, they are incurred by the debtors personally and outside the bankruptcy. Pet. App. 20a. Therefore, the court concluded such tax liabilities are "not eligible for treatment as unsecured claims under section 1222(a)(2)(A)." Pet. App. 20a.

After noting the circuit split on the issue, Pet. App. at 5a-6a, the Tenth Circuit reached this decision by analyzing the language of section 503(b). Pet. App. 7a. It determined that for an entity to "incur" a liability, it must be *liable* for it. Pet. App. 7a. To determine what entity is liable for post-petition taxes, the court held that it "must look to the relevant tax authority." Pet.

App. 7a. Based on section 1399 of the Internal Revenue Code, the Tenth Circuit held that "in Chapter 12 and 13 bankruptcies, the *debtor* – not the bankruptcy estate – bears the sole responsibility for filing and paying post-petition federal income taxes." Pet. App. 9a (citing 26 U.S.C. § 1399). Therefore, the court reasoned, the estate does not "incur" the post-petition taxes; indeed, "[t]hose taxes aren't in the bankruptcy at all but remain the personal obligation of the debtor during, after, and apart from the bankruptcy." Pet. App. 9a. According to the Tenth Circuit, "the markings of bankruptcy may be all over the transaction that produced the tax liability. The estate may have once possessed the farm assets in question. The bankruptcy court may have authorized their sale. And the estate might well have caused a tax liability to arise. But none of this means the estate incurs those taxes. Only the Daweses do." Pet. App. 9a.

The Tenth Circuit asserted that the basis for this allocation of tax liability is pragmatic: "[d]isregarding the temporary existence of a bankruptcy estate for purposes of tax liability tidies up the accounting somewhat, because there's only a single return – the debtor's – that needs to be filed and kept track of." Pet. App. 10a. The court further reasoned that the phrase "incurred by the estate" could not be equated with "incurred post-petition" – that "[b]eing incurred post-petition is a necessary – but not suf-

ficient – condition for a claim to be 'incurred by the estate.'" Pet. App. 11a-12a. The Tenth Circuit stressed that "who" (incurred the tax) and "when" (the tax was incurred) cannot mean the same thing in the context of the larger structure of the Bankruptcy Code. Pet. App. 11a. The court rejected the debtors' argument that the legislative purpose underlying the enactment of section 1222(a)(2)(A) was to provide "special solicitude to bankrupt farmers" and thus weighed in favor of their arguments, both because section 1222(a)(2)(A) applies to pre-petition disposition of certain farm assets and because Congress would then need to address "a number of thorny issues across the bankruptcy and tax codes." Pet. App. 16a-17a. In sum, the decision below sided with the Ninth Circuit's decision in *Hall* in its diametric opposition to the Eighth Circuit's decision in *Knudsen*.

2. The Decision Below, Like *Hall*, Conflicts with Other Bankruptcy Precedents Addressing Other Chapters of the Bankruptcy Code.

The far-reaching effect of the Tenth Circuit's decision cannot be overstated. Section 1398 of the Internal Revenue Code ("IRC") applies to "any case under chapter 7 (relating to liquidations) or chapter 11 (relating to reorganizations) of [the Bankruptcy Code] in which the debtor is an individual." 26 U.S.C. § 1398(a). Section 1399 of the IRC applies to any case *other*

than a "case to which section 1398 applies." *Id.* § 1399; *see also Knudsen*, 581 F.3d at 708 n.2 (noting that section 1399 of the IRC applies to Chapter 11 corporate cases). The decision below focused on administrative expenses in the context of section 1222(a)(2)(A) of the Bankruptcy Code, but that section governs only one form of administrative expense tax claim related to the sale of assets by a family farmer. Due to the broader applicability of section 1399 of the IRC, the reasoning of the Tenth Circuit further exacerbates circuit conflicts and will result in inconsistent treatment when applied to other kinds of tax claims, including tax claims incurred during corporate Chapter 11 bankruptcy cases. As the bankruptcy court below well understood, the conclusion adopted by the Tenth Circuit's decision will affect the treatment of tax claims in all cases other than individual Chapter 7 and 11 cases. Pet. App. 61a-62a.

Administrative expenses are granted priority over most other claims in bankruptcy. *See* 11 U.S.C. §§ 507(a)(2), 503(b). Administrative expenses include taxes "incurred by the estate . . . except a tax of a kind specified in section 507(a)(8)" of the Bankruptcy Code. *Id.* § 503(b)(1)(B)(i). Taxes of the kind specified in section 507(a)(8) are generally taxes that have been incurred pre-petition. *Id.* § 507(a)(8). This Court has previously explained that the concept of an administrative expense is very broad, en-

compassing even "damages resulting from the negligence of a receiver acting within the scope of his authority as receiver." *Reading Co. v. Brown*, 391 U.S. 471, 485 (1968). In fact, this Court has specifically held that taxes incurred during the period of bankruptcy administration are obligations of the bankruptcy estate entitled to administrative priority. *Nicholas v. United States*, 384 U.S. 678, 687-88 (1966) ("[T]axes incurred during the arrangement period are expenses of the Chapter XI proceedings and are therefore technically a part of the first priority under s 64a(1)."); *see also Varsity Carpet Servs., Inc. v. Richardson (In re Colortex Indus., Inc.)*, 19 F.3d 1371, 1381-82 (11th Cir. 1994) (confirming continued validity under Bankruptcy Code).

Various courts of appeals have held in the *non-individual* Chapter 11 context that administrative expense priority for taxes "incurred by the estate" applies to taxes incurred when the estate conducts post-petition business. *E.g., Towers v. United States (In re Pac.-Atl. Trading Co.)*, 64 F.3d 1292, 1301 (9th Cir. 1995) ("Because the estate was in existence [when the tax was incurred], we conclude that the corporate income taxes . . . were 'incurred by the estate.'"); *Mo. Dep't of Revenue v. L.J. O'Neill Shoe Co. (In re L.J. O'Neill Shoe Co.)*, 64 F.3d 1146, 1148 (8th Cir. 1995) (affording administrative expense priority to corporate income tax based on income earned post-petition); *W. Va. State Dep't of Tax*

& Revenue v. IRS (In re Columbia Gas Transmission Corp.), 37 F.3d 982, 986 (3d Cir. 1994) (declining to afford administrative expense priority where "the event giving rise to the property tax . . . occurred before the petition for bankruptcy had been filed"); *United States v. Friendship College, Inc. (In re Friendship College, Inc.)*, 737 F.2d 430, 432 (4th Cir. 1984) (affording administrative expense priority for income tax withheld from wages earned while conducting business in Chapter 11 reorganization). These cases demonstrate that a tax that has been "incurred by the estate" is a post-petition tax liability "since by definition there can be no bankruptcy estate until the petition in bankruptcy is filed." *E.g.*, *Friendship*, 737 F.2d at 431. As noted above, taken together with section 1398, section 1399 of the IRC provides that no separate taxable entity results from the commencement of a chapter 11 case where the debtor is not an individual. 26 U.S.C. §§ 1398, 1399. Accordingly, the non-individual Chapter 11 cases cited above directly conflict with the Tenth Circuit's decision because the Tenth Circuit essentially held that where section 1399 applies (*e.g.,* the non-individual Chapter 11 context and the Chapter 12 context), there are (nonsensically) no estates to incur taxes entitled to administrative expense priority. Pet. App. 8a-9a.

C. The Bankruptcy Taxation Issue Presented in This Case and in *Hall* Is Important, Particularly in the Farm Bankruptcy Context.

1. Uniform Application of the Internal Revenue Code and the Bankruptcy Code is of Critical Importance and Is Required by the Constitution.

The circuit split created by the decisions discussed above has resulted in a lack of uniformity as the lower courts divide along jurisdictional lines in their interpretations of relevant provisions of both the Bankruptcy Code and the Internal Revenue Code. Uniform interpretation is central to proper administration of both Codes. *See, e.g., New York v. Saper*, 336 U.S. 328, 329 (1949); *Dobson v. Comm'r*, 320 U.S. 489, 492 (1943). Indeed, the importance of uniformity in bankruptcy law led the framers of the United States Constitution to expressly grant Congress the power "to establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. CONST. art. I, § 8, cl. 4. Madison wrote that "[t]he power of establishing uniform laws of bankruptcy is so intimately connected with the regulation of commerce, and will prevent so many frauds where the parties or their property may lie or be removed into different States, that the expediency of it seems not likely to be drawn into question." THE FEDERALIST No. 42, at 308 (James Madison) (Benjamin Fletcher

Wright ed., 1961). Justice Story wrote that the reasons for conferring the bankruptcy power on the United States "result from the importance of preserving harmony, promoting justice, and securing equality of rights and remedies among the citizens of all the states. It is obvious, that if the power is exclusively vested in the states, each one will be at liberty to frame such a system of legislation upon the subject of bankruptcy and insolvency, as best suits its own local interests and pursuits. Under such circumstances no uniformity of system or operations can be expected. . . . There can be no other adequate remedy than giving a power to the general government to introduce and perpetuate a uniform system." 2 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1107 (2d ed. 1851).

The need for uniform interpretation of the Tax Code is no less pressing. The Constitution itself mandates uniform taxation throughout the United States. U.S. CONST. art. I, § 8, cl. 1 (taxes must be "uniform throughout the United States"); *Brushaber v. Union Pac. R.R. Co.*, 240 U.S. 1, 24 (1916); *see also United States v. Lee*, 455 U.S. 252, 261 (1982) (holding that taxes imposed "must be uniformly applicable to all, except as Congress provides explicitly otherwise"); *Burnet v. Harmel*, 287 U.S. 103, 110 (1932) ("Here we are concerned only with the meaning and application of a statute enacted by Congress,

in the exercise of its plenary power under the Constitution, to tax income. . . . It is the will of Congress which controls, and the expression of its will in legislation, in the absence of language evidencing a different purpose, is to be interpreted so as to give a uniform application to a nation-wide scheme of taxation.").

Until the Court resolves the question presented by this case and by *Hall*, the confusion among the lower courts and lack of predictability will continue to hurt family farmer debtors struggling to fashion a feasible reorganization plan. The constitutionally prohibited disparate treatment of family farmers who live in different states must be resolved by this Court.

2. Chapter 12 Bankruptcy Filings Are Increasing Rapidly.

Chapter 12 bankruptcy filings are on the rise. Although other bankruptcy filings slowed in calendar year 2010, statistics released by the Administrative Office of the U.S. Courts revealed a 33-percent increase in Chapter 12 bankruptcy filings in 2010 from calendar year 2009. *Growth in Bankruptcy Filings Slows in Calendar Year 2010*, http://www.uscourts.gov/News/NewsView/11-02-15/Growth_in_Bankruptcy_Filings_Slows_In_Calendar_Year_2010.aspx. The number of Chapter 12 family farm bankruptcy filings has more than doubled between 2008 and 2010. *Id.* (Total Bankruptcy Filings by Bankruptcy Chap-

ter and Calendar Years Chart) (reflecting total of 345 Chapter 12 bankruptcy filings in 2008 and total of 723 in 2010).

A comparison of Chapter 12 filings during the three-month period ending in March 2011 with Chapter 12 filings during the three-month period ending in March 2008 reveals a steady climb. *Compare* Table F-2, Business and Nonbusiness Bankruptcy Cases Commenced, by Chapter of the Bankruptcy Code from March 31, 2008 through December 31, 2010, http://www.uscourts.gov/Statistics/BankruptcyStatistics.aspx (Quarterly Filings: 3 month by Chapter and District Under Chapter 12 Heading) (March 2008 – 81, March 2009 – 102; March 2010 – 163; March 2011 – 181). This trend holds true also when comparing reports across those years for three-month periods ending in June, September, and December of 2008, 2009, and 2010. *Id.* (June – 85, 139, 194; September – 89, 155, 202; December – 90, 148, 164). Given the current state of the economy, one might expect this trend to continue, and increasing numbers of farmers will be forced to file Chapter 12 bankruptcy petitions. Accordingly, the issue presented by this appeal will repeatedly recur.

D. The Decision Below Was Wrongly Decided Because It Effectively Ignores the Purpose and Policy that Led to the Enactment of Bankruptcy Code Section 1222(a)(2)(A) and Is Demonstrably At Odds With the Intent of Congress.

Chapter 12 was "designed to give family farmers facing bankruptcy a fighting chance to reorganize their debts and keep their land." H.R. CONF. REP. NO. 99-958, at 48 (1986). When Congress added Chapter 12 to the Bankruptcy Code in 1986, it included a seven-year sunset provision because Chapter 12 was "a new chapter aimed at a specific class of debtors," and Congress wanted to "evaluate both whether the chapter [was] serving its purpose and whether there [was] a continuing need for a special chapter for the family farmer" before determining "whether or not to make th[e] chapter permanent." *Id.* Following its original enactment, Congress extended Chapter 12's expiration date numerous times and ultimately made the Chapter permanent in the 2005 amendment to the Bankruptcy Code known as the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA"). 147 CONG. REC. H4953 (daily ed. July 31, 2001) (statement of Rep. Baldwin); Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 1001(a), 119 Stat. 23, 185 (2005).

As part of its permanent addition of Chapter 12 to the Bankruptcy Code, Congress enacted section 1222(a)(2)(A) to help farmers "reorganize by keeping the tax collectors at bay." 145 CONG. REC. S764 (daily ed. Jan. 20, 1999) (statement of Sen. Grassley, sponsor of BAPCPA). Prior to the enactment of BAPCPA, tax claims by the IRS were afforded special priority, and former section 1222(a)(2) required that any Chapter 12 plan had to pay those claims in full pursuant to section 507 of the Bankruptcy Code. 11 U.S.C. § 1222(a)(2) (2004) ("The plan shall . . . provide for the full payment, in deferred cash payments, of all claims entitled to priority under section 507 of this title, unless the holder of a particular claim agrees to a different treatment of such claim."). As a result, the IRS would often have an effective veto over a Chapter 12 debtor's plan of reorganization. *See* Pet. App. 62a (noting that prior to BAPCPA, the IRS was perfectly content to agree that a claim for post-petition taxes was an administrative expense subject to section 1222(a)(2) given the special treatment that section afforded it) (citing *In re Ryan*, 228 B.R. 746, 747 (Bankr. D. Or. 1999)).

Senator Grassley, the original proponent of section 1222(a)(2)(A) and ultimately the primary sponsor of BAPCPA, sought to remedy that situation by amending section 1222(a)(2) to reduce the priority of claims owed to governmental entities as a result of the sale of certain assets in or-

der to "free up capital for investment in the farm, and help farmers stay in the business of farming." 145 CONG. REC. S764 (daily ed. Jan. 20, 1999) (statement of Sen. Grassley, sponsor of BAPCPA); *see also In re Knudsen*, 389 B.R. 643, 660 (N.D. Iowa 2008), *aff'd,* 581 F.3d 696 (8th Cir. 2009); Pet. App. 29a (noting that "Congress was concerned that if the debtor/farmer could not pay the I.R.S. in full, the I.R.S. was likely to veto the plan, and the farmer would likely lose the farm."); Pet. App. 65a ("The entire purpose of Chapter 12 is to allow a farmer to reorganize, and the specific purpose of the amendment to § 1222 was to remove a major impediment to reorganization."); 7 NORTON BANKRUPTCY LAW & PRACTICE § 133:6 n.2 (3d ed. 2010) (explaining that section 1222(a)(2) was amended by BAPCPA "in order to allow farm debtors to liquidate unprofitable portions of their family farm enterprise so that they could lower debt and improve profitability without regard to the capital gains tax or depreciation recapture which normally colors all sale decisions for family farmers."). As the primary sponsor of BAPCPA, it is not surprising that Senator Grassley was successful in having section 1222(a)(2)(A) enacted precisely as he had initially proposed it. *Compare* S. 260, 106th Cong. § 3 (1999), *available at* 1999 CONG US S 260; Pet. App. 93a *with* 11 U.S.C. § 1222(a)(2)(A); Pet. App. 81a-82a.

The legislative history of section 1222(a)(2)(A) demonstrates that Congress clearly intended to reduce the priority of tax claims of governmental entities for taxes incurred during the reorganization process to enable family farmers to successfully reorganize their affairs in a Chapter 12 bankruptcy. The decision below, like the decision in *Hall*, achieves precisely the opposite result, making capital gains tax claims in reorganization proceedings nondischargeable personal obligations of the debtor and frustrating the goal of successful reorganization. This makes no sense. Nothing in the text of the statute or the legislative history suggests that Congress intended to permit such potentially massive liability to escape the reorganization process, which often could doom to failure the best attempts of family farmer debtors to reorganize their affairs.

This Court has indicated that when an interpretation of a statute is "demonstrably at odds with the intentions of its drafters," courts should give effect to congressional intent. *United States v. Ron Pair Enters.*, 489 U.S. 235, 242 (1989) (citation omitted). In addition to the clear legislative intent of section 1222(a)(2)(A) to lead family farmers to a successful reorganization of their affairs in bankruptcy, the legislative history of section 503(b)(1)(B)(i) of the Bankruptcy Code further supports the result reached in the bankruptcy and district court decisions below and

contradicts the Tenth Circuit's opinion below. As the bankruptcy court explained, following its extensive review of the legislative history of section 503(b)(1)(B)(i), the Senate Reports discussing that section referred to administrative expenses under section 503(b)(2) as including taxes incurred "*in administering the debtor's estate*" or "*during the case*." Pet. App. 55a (quoting with emphases S. REP. NO. 95-989, at 66 (1978)); *see also Knudsen v. IRS*, 581 F.3d 696, 708-09 (8th Cir. 2009). These statements necessarily contemplate post-petition tax claims, just as Senator Grassley's comments did.

The erroneous nature of the result below, as well as that of *Hall* in the Ninth Circuit, is underscored by the reliance of those opinions on section 1399 of the IRC. Congress enacted section 1399 in 1980 and enacted section 1222(a)(2)(A) of the Bankruptcy Code in 2005. Bankruptcy Tax Act of 1980, Pub. L. No. 96-589, § 3, 94 Stat. 3389, 3400 (1980); Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 1003, 119 Stat. 23, 186 (2005). Utilization of section 1399 to thwart the intent of section 1222(a)(2)(A) makes no sense because section 1222(a)(2)(A) is more recent, more specific, and provides the exclusive method for treatment of claims owed to government entities relating to the sale of farm assets. As this Court has explained, "a specific policy embodied in a later federal statute should con-

trol [this Court's] construction of the [earlier] statute, even though it ha[s] not been expressly amended." *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 143 (2000) (quoting *United States v. Estate of Romani*, 523 U.S. 517, 530-31 (1998)). This is so because the "'classic judicial task of reconciling many laws enacted over time, and getting them to 'make sense' in combination, necessarily assumes that the implications of a statute may be altered by the implications of a later statute.'" *Id.* (quoting *United States v. Fausto*, 484 U.S. 439, 453 (1988)).

This rule is particularly appropriate here because when section 1399 was enacted, Chapter 12 *did not yet even exist*. Chapter 12 was not added to the Bankruptcy Code until 1986. Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, Pub. L. No. 99-554, § 255, 100 Stat. 3088, 3105 (1986). It is difficult to see how a provision of a statute can be held to unambiguously trump an entire area of law (Chapter 12) that was not even in existence when the provision was enacted.

Indeed, as the decision below concedes, such a result was never the intent of the drafters of sections 1399 and 1398. The Tenth Circuit explains that "[t]he rationale for allocating tax liability [in the manner sections 1399 and 1398 do] in Chapter 12 and 13 bankruptcies appears to be a pragmatic one." Pet. App. 10a. According

to the Tenth Circuit, because Chapter 12 and 13 estates often do not last long, "[d]isregarding the temporary existence of a bankruptcy estate for purposes of tax liabilities *tidies the accounting somewhat*, because there's only a single return – the debtor's – that needs to be filed and kept track of." Pet. App. 10a (emphasis added). This, however, is not a substantive policy rationale that could support the result below because the judicially-perceived administrative convenience associated with a prior statute cannot overcome the clear purpose of the subsequently enacted section 1222(a)(2)(A) designed to grant tax relief to family farmers.

The Tenth Circuit attempted to blunt the effect of its decision by claiming that "income taxes incurred as a result of the *pre-petition* disposition of certain farm assets *are* eligible for § 1222(a)(2)(A)'s generous rule allowing them to be treated as unsecured claims." Pet. App. 16a (emphasis in original). As the Tenth Circuit put it: "We *only* stop short of extending § 1222(a)(2)(A)'s treatment to income taxes incurred post-petition by the debtor rather than the estate." Pet. App. 16a (emphasis in original). But section 1222(a)(2)(A) was specifically enacted to address post-petition asset sales of family farmers as part of the reorganization process. As Senator Grassley explained, "[u]nder the bankruptcy code [prior to BAPCPA], the I.R.S. must be paid in full for any tax liabilities

generated *during a bankruptcy reorganization*. If the farmer can't pay the I.R.S. in full, then he can't keep his farm. This isn't sound policy. Why should the I.R.S. be allowed to veto a farmer's *reorganization plan*? 'Safety 2000' [which ultimately became section 1222(a)(2)(A)][1] takes this power away from the I.R.S. by reducing the priority of taxes *during proceedings*." 145 CONG. REC. S764 (daily ed. Jan. 20, 1999) (statement of Sen. Grassley, sponsor of BAPCPA) (emphases added).

Nothing in the language of section 1222(a)(2)(A) suggests Congress fashioned such a system or had any intention of doing so. *See Knudsen*, 581 F.3d at 709. Section 1222(a)(2)(A) is a remedial statute that reduces the tax burden carried by family farmers involved in Chapter 12 reorganizations to enhance their prospects of success. The decision below purports to "give[] respect to Congress's wish to provide a substantial form of special assistance targeted to farmers," but it incorrectly assumes that Congress intended the statute to apply only to farmers who had the foresight to sell their farms before their creditors and the Bankruptcy Court could supervise the sale, rendering section 1222(a)(2)(A) meaningless for most Chapter 12

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[1] *Compare* S. 260, 106th Cong. § 3 (1999), *available at* 1999 CONG US S 260; Pet. App. 93a *with* 11 U.S.C. § 1222(a)(2)(A); Pet. App. 81a-82a.

debtors. Pet. App. 16a. Promoting the pre-petition liquidation of the assets of family farmers does nothing to promote the congressional purpose of aiding farmers' reorganization efforts. Worse still, it is precisely the opposite result from that expressed by Congress. Congress sought to encourage the orderly reorganization of the affairs of beleaguered family farmers, and the special tax treatment related to the sale of assets during reorganization proceedings is essential to that goal.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be held pending the Court's ruling in *Hall*. Following the Court's decision in *Hall*, the Court should (if appropriate) grant the petition, vacate the judgment below, and remand for further proceedings in light of its decision in *Hall*.

Respectfully submitted,

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Dated: August 17, 2011

APPENDIX A – OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT DECIDED JUNE 21, 2011

FILED
United States Court of Appeals
Tenth Circuit

June 21, 2011

Elisabeth A. Shumaker
Clerk of Court

PUBLISH

UNITED STATES COURT OF APPEALS

TENTH CIRCUIT

In re: DONALD W. DAWES; PHYLLIS C. DAWES, Debtors, ---------- UNITED STATES OF AMERICA, Appellant, v. DONALD W. DAWES; PHYLLIS C. DAWES, Appellees, And EDWARD J. NAZAR, Trustee, Defendant.	No. 09-3129

Appendix A

Appeal from the United States District Court for the District of Kansas (D.C. No. 6:08-CV-01054-WEB)

Patrick J. Urda, Attorney, Tax Division (John A. DiCicco, Acting Assistant Attorney General; Bruce R. Ellisen, Attorney, Tax Division; and Lanny D. Welch, United States Attorney, with him on the briefs), United States Department of Justice, Washington, D.C., for Appellant.

Mark J. Lazzo, Mark J. Lazzo, P.A., Wichita, Kansas, for Debtors-Appellees.

Before **TYMKOVICH, McKAY** and **GORSUCH**, Circuit Judges.

GORSUCH, Circuit Judge.

Can a taxpayer avoid income taxes by selling farm assets after declaring Chapter 12 bankruptcy? In at least this respect, the tax collector bears resemblance to the grim reaper: always hovering, never avoidable. While the law provides some forms of tax relief, it stops short of

forgiving taxes incurred by a Chapter 12 debtor after filing a bankruptcy petition. And the taxes at issue here were incurred by the Daweses after they petitioned for bankruptcy. So it is that the Daweses must pay the tax collector his due and we must reverse.

The Daweses' struggle with the IRS has a lengthy provenance. Decades ago, and after repeated trips up and down the federal court system, the couple pleaded guilty for failing to file income tax returns in 1981 through 1983. All this is documented in no fewer than three of our published opinions. *See United States v. Dawes*, 951 F.2d 1189 (10th Cir. 1991); *United States v. Dawes*, 895 F.2d 1581 (10th Cir. 1990); *United States v. Dawes*, 874 F.2d 746 (10th Cir. 1989). But all this, as it turned out, was just the beginning. The Daweses *also* failed to pay all their taxes for still more years, including 1986–1988 and 1990. This led the IRS to seek — and ultimately obtain — a judgment declaring, first, that the Daweses had fraudulently conveyed certain assets in an effort to avoid their creditors; and, second, that those unlawful conveyances were null and void. Some six years ago we affirmed this result. *See United States v. Dawes*, 161 F. App'x 742 (10th Cir. 2005) (unpublished). After and in light of this ruling the government proceeded to execute its judgment, notifying the Daweses that it intended to take possession of

various pieces of their property. But before it could do so, the Daweses declared bankruptcy, seeking the protections of Chapter 12.

And that brings us to the latest installment of this epic. After declaring bankruptcy, the Daweses, with the permission of the bankruptcy court, sold several tracts of farm land. This sale, of course, created income tax liabilities. The Daweses proceeded to submit a bankruptcy reorganization plan in which they proposed to treat their newly incurred tax liabilities as general unsecured claims. As unsecured claims, the taxes would be entitled to no priority, paid only to the extent funds might be available after priority claims were satisfied, and any remaining unpaid portion would be eligible for discharge. Unsurprisingly, the IRS didn't take kindly to this proposal. It opposed the plan vigorously — but just as unsuccessfully — first before the bankruptcy court and then on appeal before the district court. The IRS now brings its complaint to this court, asking us to undo its earlier losses.

How is that the Daweses think they can defeat the IRS's tax claim? For the most part, of course, a bankruptcy filing offers scarce relief from the tax man. Other creditors may be neglected, but rarely the IRS. *See, e.g.*, 11 U.S.C. §§ 503(b), 507(a)(2), 507(a)(8) & 523(a)(1). Even so, the Daweses have their eye on a special provi-

sion of Chapter 12 that, they say, makes their situation special. Under § 1222(a)(2)(A), certain claims that are otherwise entitled to priority payment status under § 507, but that happen to be owed to the government as a result of the sale of farm assets, are downgraded, treated as mere unsecured claims, and made eligible for discharge. No one disputes that the taxes at issue here *are* owed to the government and *are* owed as a result of the sale of farm assets. So the only question is whether the taxes are entitled to priority under § 507. Moving to that provision, the Daweses point out that claims entitled to priority include "administrative expenses allowed under section 503(b)." 11 U.S.C. § 507(a)(2). And with this the Daweses take us next to § 503(b). That statute, they observe, speaks of "administrative expenses . . . including . . . any tax . . . incurred by the estate." 11 U.S.C. § 503(b)(1)(B)(i). Mapping their way through the thicket of the U.S. Code in this way, the Daweses argue that, because the federal income taxes at issue here are owed to the IRS as a result of a farm asset sale and were "incurred by the estate," they may be treated as general unsecured claims.

Whether this is so — whether income taxes flowing from the sale of a farm asset during a Chapter 12 bankruptcy are taxes "incurred by the estate" and so subject to downgrade and dis-

charge — is a question that has divided our sister circuits. The Eighth Circuit says yes; the Ninth says no. *See Knudsen v. I.R.S.*, 581 F.3d 696, 710 (8th Cir. 2009); *United States v. Hall*, 617 F.3d 1161, 1163 (9th Cir. 2010), *cert. granted*, 79 U.S.L.W. 3421 (June 13, 2011) (No. 10-875). The same disagreement has beset the bankruptcy courts as well. *Compare I.R.S. v. Ficken*, 430 B.R. 663, 672 (10th Cir. BAP 2010) *and In re Schilke*, 379 B.R. 899, 903 (Bankr. D. Neb. 2007) *with Smith v. I.R.S.*, 447 B.R. 435, 447 (Bankr. W.D. Pa. 2011).

Today, we must pick sides in this debate and we side with the Ninth. Whatever other problems may lurk in the Daweses' statutory analysis (and the IRS insists there are several), post-petition income taxes incurred during Chapter 12 proceedings are liabilities of the individual debtor and *not* the bankruptcy estate. As such, they are not within the purview of the bankruptcy proceedings or included in the reorganization plan. Instead, the taxes are due from the debtor personally, and the IRS's recourse remains exclusively with the individual debtor, separate and apart from the Chapter 12 estate and unaffected by the bankruptcy discharge. That this is so is suggested by an examination of the plain language of the statute before us, the larger statutory structure, and Congress's expressed purposes.

To begin, the plain language of § 503(b). The Daweses' argument hinges on the term "incurred by the estate" and the submission that the post-petition income tax at issue here *was* incurred by their bankruptcy estate rather than by them personally. But what does it mean for a tax to be *incurred* by the estate? Happily, that critical term has a definition that is as well-settled as it is precise. Black's Law Dictionary tells us that to "incur" means to "suffer or bring on oneself," as in a "liability or expense." Black's Law Dictionary 782 (8th ed. 2004). Webster's says the same thing, and adds the alternate definition "[to] become liable or subject to." Webster's Third New International Dictionary 1146 (2002) (unabridged); *see also* 7 Oxford English Dictionary 834-35 (2d ed. 1989) ("To run or fall into (some consequence, usually undesirable or injurious); to become through one's own action liable or subject to"). While at the margin there might be some distinctions between these definitions, they don't leave any room for debate on this proposition: one who has "incurred" an expense is *liable* for it.

To determine who has "incurred" a tax, then, we must ask *who* is liable for paying it. And to answer that question we must look to the relevant tax authority. Of course, Congress is free (and in some cases has chosen) to use the bankruptcy code to control certain aspects of how fed-

eral or state tax law operates during reorganizations. But, when the code hasn't told us otherwise, our attention is rightly turned to the underlying tax law to see who owes what. Indeed, bankruptcy law *often* relies on underlying income tax laws to assign priorities in bankruptcy. *See, e.g.*, § 507(a)(8)(A)(i) (treatment of prepetition tax turns on when the tax return was due); § 507(a)(8)(B) (treatment of property tax turns on when it was last payable without penalty); § 346 (commanding that state and local income taxes be allocated between debtor and bankruptcy estate in a way that generally follows their treatment under the federal Internal Revenue Code). When the bankruptcy code defers a question to existing tax law, our role is to apply that law, not to invent new rules of our liking.

This is one of those occasions, and the relevant tax authority is the federal government itself, so we need only flip forward a few titles in the U.S. Code to see how tax liability is allocated as between debtor and estate. And there, in Title 26, the answer is plain. In individual Chapter 7 and 11 bankruptcies, the trustee is charged with filing a separate return on behalf of the bankruptcy estate and paying from that estate any resulting taxes. *See* 26 U.S.C. §§ 1398(c), 6012(a)(8), (b)(3), (b)(4), & 6151(a). There's no escaping that *those* are "taxes incurred by the es-

tate" — the estate is obligated by federal law to pay them. But in Chapter 12 and 13 bankruptcies, the *debtor* — not the bankruptcy estate — bears the sole responsibility for filing and paying post-petition federal income taxes. *See* 26 U.S.C. § 1399; 26 U.S.C. § 6151(a); *Holywell Corp. v. Smith*, 503 U.S. 47, 52 (1992) ("The Internal Revenue Code ties the duty to pay federal income taxes to the duty to make an income tax return."). Only the debtor, not the estate, is *liable* for the payment of these taxes. And this, in turn, answers the question posed by § 503(b): because a Chapter 12 or Chapter 13 estate isn't liable for post-petition federal income taxes, the estate does not *incur* such taxes. Those taxes aren't in the bankruptcy at all but remain the personal obligation of the debtor during, after, and apart from the bankruptcy. It's little different than when a corporate officer executes a transaction that generates a tax bill for his employer: the officer may have *caused* the tax to arise, but it is the corporation that *incurred* and is *liable* for it. Here, the markings of bankruptcy may be all over the transaction that produced the tax liability. The estate may have once possessed the farm assets in question. The bankruptcy court may have authorized their sale. And the estate might well have caused a tax liability to arise. But none of this means the estate incurs those taxes. Only the Daweses do.

The rationale for allocating tax liability like this in Chapter 12 and 13 bankruptcies appears to be a pragmatic one. Upon confirmation of a plan under those chapters, the estate property, including any post-petition income, joins the post-petition income taxes back in the hands of the debtor. *See* 11 U.S.C. §§ 1227(b) & 1327(b). Disregarding the temporary existence of a bankruptcy estate for purposes of tax liability tidies the accounting somewhat, because there's only a single return — the debtor's — that needs to be filed and kept track of. And, because Chapter 12 and 13 cases are typically confirmed quickly (at least compared to bankruptcies under Chapters 7 and 11), the expectation is that the debtor's post-petition earnings and taxes will meet up in his hands soon enough. *See* 8 Collier on Bankruptcy ¶ 1200.01[4] (16th ed.) (noting that Chapter 12 debtor is required to file a plan within 90 days and court is required to confirm or deny that plan within 45 days); *cf.* H.R. Rep. No. 95-595, at 276 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6233 ("The administrative reality [is] that most Chapter 13 estates will only remain open for 1 or 2 months until confirmation of the plan.").

The Daweses reply to all this by urging us to follow the Eighth Circuit in reading "tax incurred by the estate" to mean "tax incurred during bankruptcy." The problem is, there's just no

way to root this reading in the text of the statute. It would be one thing if we faced a difference of opinion over the meaning of the word "incurred" — facing divergent definitions, one might reasonably move on to contextual clues to determine the term's meaning. But the Daweses neither cite some authority for an alternate definition of the word "incurred" nor urge one of their own creation. And once we accept that one must be *liable* for an expense in order to have *incurred* it, it's the phrase "by the estate" that poses the problem for the Daweses. That language focuses unavoidably on the question *who* did the incurring and there's just no way we can turn it into a question about *when* a liability was incurred. Trying to do so would be like saying that the phrase "debts incurred by my wife" (*who*) means "debts incurred by either of us while we were married" (*when*). The two statements simply mean different things. The Daweses' interpretation is thus irreconcilable with the plain language of § 503(b). *Who* does not mean *when*.

The Daweses insist that, because a bankruptcy estate can't incur taxes before it exists, the phrase "incurred by the estate" necessarily references taxes incurred post-petition. And with this much we have no objection. But the Daweses err when they take the further step of *equating* "incurred by the estate" with "incurred post-petition." The fact that a bankruptcy estate can't

incur liabilities until it comes into existence doesn't mean *every* liability that arises after a petition is filed is automatically incurred by the estate and becomes its liability. Being incurred post-petition is a necessary — but not sufficient — condition for a claim to be "incurred by the estate." And the Daweses don't address the requirement that is both necessary *and* sufficient under the text of the statute — that the *estate* be liable for payment of the taxes in question.

Beyond the narrow statutory provision before us, the larger structure of the bankruptcy code casts further doubt on the direction the Daweses urge us to take. If Congress had wanted to capture all post-petition taxes in § 503(b) — if it had wanted to focus on *when* the tax was incurred rather than *by* whom — it surely knew how to do so. And we don't need to look far to find some examples. Section 503 itself addresses many expenses with regard to *when* rather than *who* incurred them. *See* § 503 (b)(1)(A)(i) ("wages, salaries, and commissions for services *rendered after the commencement of the case*") (emphasis added); (b)(1)(B)(ii) (certain tax carryback adjustments "whether the [relevant] taxable year . . . ended *before or after the commencement of the case*") (emphasis added). For that matter, and in addition to taxes "incurred by the estate," § 503(b) categorizes a host of other charges based on *who* did the incurring. *See* § 503 (b)(3) ("the

[following] actual, necessary expenses . . . *incurred by* [] *a creditor*") (emphasis added). All this seems evidence that Congress was deliberately navigating the distinction between timing and identity when crafting § 503(b). To accept the Daweses' argument that *when* and *who* mean the same thing would require trampling these carefully delineated rules for administrative priority.

Other structural features confirm the Daweses' wrong turn. Their reading of § 503(b) would make nonsense of a central provision for paying post-petition taxes under Chapter 13. To accept that post-petition federal income taxes are "incurred" by the estate in Chapter 12 proceedings, we would seemingly need to say the same thing in the Chapter 13 context — after all, Chapter 12 is modeled on Chapter 13, and individual Chapter 12 and Chapter 13 estates are given the same treatment under the Internal Revenue Code. *See* 26 U.S.C. § 1399. But Chapter 13 explicitly allows the government the *option* of having post-petition taxes incurred by the debtor treated as part of the bankruptcy proceeding and dealt with in the reorganization plan. *See* 11 U.S.C. § 1305(a)(1). The Daweses' reading of § 503(b) forestalls that flexibility, forcing governmental claims into the bankruptcy proceedings whether the government wants them there or not. And, beyond thwarting the choice bestowed by § 1305,

the Daweses' handiwork raises an even more troubling question: what is § 1305(a)(1) doing on the books at all? If post-petition taxes are automatically included in the bankruptcy plan as taxes "incurred by the estate," then § 1305(a)(1)'s *optional* inclusion of these same claims is left loitering around the U.S. Code with no apparent purpose. So, to adopt the Daweses' reading of § 503(b), we would need to ignore "one of the most basic interpretive canons" — that a "statute should be construed so that effect is given to all its provisions, so that no part will be inoperative or superfluous, void or insignificant." *See Corley v. United States*, 129 S. Ct. 1558, 1566 (2009) (citation omitted); *see also Bilski v. Kappos*, 130 S. Ct. 3218, 3229 (2010) ("This principle . . . applies . . . even when Congress enacted the provisions at different times.").

Equally strange things would happen to state and local income taxes. Under the Daweses' reading of § 503(b), the bankruptcy estate would of course be responsible for paying *state* income taxes incurred during bankruptcy. But the bankruptcy code specifically *prohibits* state and local income taxes from being either "taxed to" or "claimed by" a Chapter 12 estate, instead directing that these state and local taxes be the liabilities of the *debtor*. *See* § 346(b) (requiring state and local income taxes to assign liability exclusively to the debtor whenever federal income tax

law does so). So, under the Daweses reading of § 503(b), the bankruptcy trustee would face conflicting instructions: § 503 would tell him to pay post-petition state income taxes while § 346(b) would tell him not to do just that. Either the trustee would have to reject the Daweses' understanding of § 503(b), or he would have to turn a blind eye to another provision of the bankruptcy code.

All of these riddles disappear if we apply the plain meaning of § 503(b). Post-petition federal income taxes are not ordinarily included in the Chapter 12 or Chapter 13 bankruptcy plan because they are not "taxes incurred by the estate." Section 1305 operates to give the government the *option* of having these taxes included — though only in Chapter 13. And otherwise mixed messages about the treatment of post-petition state and federal income taxes during Chapter 12 proceedings dissipate: none is treated as "taxes incurred by the estate" and so none is payable by the trustee during the bankruptcy proceedings — a result that comports with the plain language of § 346(b) and ensures the even-handed treatment of federal and state taxes Congress clearly sought to achieve.

The Daweses ask us to look beyond the statutory text and beyond even the larger statutory structure to the statute's underlying purpose,

stressing that § 1222(a)(2)(A) was enacted to provide special solicitude to bankrupt farmers. But spotting the Daweses the premise that in § 1222(a)(2)(A) Congress sought to provide tax relief to farmers does not mean their interpretation of § 503(b) ineluctably follows. Our interpretation as well gives effect and respect to the congressional purpose they identify. Ordinarily, of course, taxes are not dischargeable in bankruptcy; the tax man is rarely avoidable. Yet under our interpretation of § 503(b), income taxes incurred as a result of the *pre-petition* disposition of certain farm assets are eligible for § 1222(a)(2)(A)'s generous rule allowing them to be treated as unsecured claims, compromised, and discharged. *See Knudsen*, 581 F.3d at 699 (applying § 1222(a)(2)(A) to pre-petition sale of slaughter hogs). Clearly, then, our reading gives respect to Congress's wish to provide a substantial form of special assistance targeted to farmers. We *only* stop short of extending § 1222(a)(2)(A)'s treatment to income taxes incurred post-petition by the debtor rather than the estate.

Neither is there any indication that this particular result is at odds with Congress's purposes. If Congress had wished to grant farmers additional relief for *post*-petition income taxes it would have needed to attend to a number of thorny issues across the bankruptcy and tax codes. For example, to prevent § 1305 from be-

coming a nullity, Congress would have needed either to do away with it entirely — a tectonic shift in the treatment of taxes under Chapter 13 — or give "incurred by the estate" one meaning in Chapter 12 and a different one in Chapter 13. Congress also would have needed to revise § 346 to allow the Chapter 12 trustee to pay state and local income taxes. And, having accomplished all *that*, Congress still would have needed to measure the consequences — for debtors, governments, and other creditors — of including post-petition taxes in the many Chapter 12 bankruptcies where § 1222(a)(2)(A) doesn't even apply. It is entirely understandable that Congress, while intent on providing special tax relief to farmers, may not have seen fit to undertake such a large rewriting of the bankruptcy or tax codes in service of that mission — especially when *pre*-petition income tax relief could be provided surgically with the simple addition of § 1222(a)(2)(A). After all, "'[n]o legislation pursues its purposes at all costs' without consideration of competing goals and concerns." *Hydro Res., Inc. v. E.P.A.*, 608 F.3d 1131, 1158 (10th Cir. 2010) (en banc) (quoting *Pension Benefit Guar. Corp. v. LTV Corp.*, 496 U.S. 633, 646 (1990)); John F. Manning, *Textualism and the Equity of the Statute*, 101 Colum. L. Rev. 1, 18 (2001) ("Because statutory details may reflect only what competing groups could agree upon, legislation cannot be expected to pursue its purposes to their logical

ends; accordingly, departing from a precise statutory text may do no more than disturb a carefully wrought legislative compromise.").

The Daweses seek a final refuge in two pieces of legislative history. First, they point to a 1978 Senate Committee Report accompanying the Bankruptcy Act that created 11 U.S.C. § 503. That Report, the Daweses emphasize, explained that "[i]n general, administrative expenses include taxes which the trustee incurs in administering the debtor's estate, including taxes on capital gains from sales of property by the trustee and taxes on income earned by the estate during the case." S. Rep. No. 95-989, at 66 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5852. But as legislative history goes this is no smoking gun. The report speaks only of taxes *which the trustee incurs* in administering a debtor's estate. It doesn't state that the phrase "taxes incurred by the estate" turns on *when* the tax is incurred rather than *who* is responsible for paying it. It does not negate the possibility that the *debtor* may incur taxes during the bankruptcy. And it does not speak to the treatment of taxes that the debtor, rather than the trustee, incurs. Confirming the point, the mirror image committee report from the House of Representatives acknowledges that the bankruptcy estate sometimes may "not [be] a separate taxable entity," that there are cases when "any income . . . is to be taxed only to the

debtor," and that "[t]he duration of a chapter 13 case is so short that there is no reason to impose a duty to pay taxes on the trustee." H.R. Rep. No. 95-595, at 277.

On the back foot, the Daweses leap forward two decades and point to a senator's floor statement made in 1999 while he was introducing a never-enacted provision similar to § 1222(a)(2)(A). The senator described his unenacted provision as aimed at remedying situations in which "the I.R.S. must be paid in full for any tax liabilities generated during a bankruptcy reorganization." 145 Cong. Rec. S750-02, S764. The first problem with this argument, of course, is that Section 1222(a)(2)(A) wasn't adopted until six years later, in 2005 — so this floor statement might not tell us *anything* about what the Congress that *did* enact § 1222(a)(2)(A) had in mind. We suppose it's possible for a senator's remarks to linger in the hearts and minds of his colleagues and influence their work years later, but to assume as much would take us well beyond ordinary legislative history analysis and require us to engage in the sort of "psychoanalysis of Congress" the Supreme Court has repeatedly warned against. *United States v. Public Util. Comm'n of Cal.*, 345 U.S. 295, 319 (1953) (Jackson, J., concurring); *see also Massachusetts v. E.P.A.*, 549 U.S. 497, 529-30 (2007) (warning against attributing views of one Congress to

another); *Doe v. Chao*, 540 U.S. 614, 619-21 (2004) (warning against reading too much into unenacted bills). Notably, too, the remarks in question, like the Senate Report on which the Daweses rely, don't speak directly to the question whether post-petition income taxes qualify as administrative expenses under § 503(b). Neither could they have influenced or reflected the intent of the 1978 Congress that enacted § 503(b) many years *earlier*. And of course it's the language of *that* enacted statute we're tasked with construing in this case.

With the plain language and larger statutory structure pointing in the same direction, and without any convincing counter-indication in the legislative history, we hold that post-petition federal income taxes are not "incurred" by a Chapter 12 "estate" for purposes of § 503(b)(1)(B)(i). They are, instead, incurred by the Daweses personally and outside the bankruptcy. Accordingly, the Daweses' post-petition income tax liabilities at issue before us are not eligible for treatment as unsecured claims under § 1222(a)(2)(A) as currently proposed in their reorganization plan.

Reversed.

APPENDIX B – MEMORANDUM AND ORDER IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS DATED MARCH 12, 2009

IN THE UNITED STATES
DISTRICT COURT FOR
THE DISTRICT OF KANSAS

IN RE: DONALD W. DAWES and PHYLLIS C. DAWES,	)	
Debtors.	)	
UNITED STATES OF AMERICA,	)	
Appellant,	)	
v.	)	Case No. 08-1054-WEB Bankr. No. 06-11237-12
EDWARD J. NAZAR, *Trustee*; and DONALD W. DAWES, PHYLLIS C. DAWES,	)	
Appellees.	)	

Appendix B

Memorandum and Order

This is an interlocutory appeal by the United States from a ruling by the Bankruptcy Court. The ruling concerns a construction of 11 U.S.C. § 1222(a)(2)(A), which carves out an exception to the general rule that a Chapter 12 plan must provide for full payment of priority claims, including administrative expenses in the form of taxes incurred by the bankruptcy estate. Section 1222(a)(2)(A) provides that a claim owed to the Government "that arises as a result of the sale, transfer, exchange, or other disposition of any farm asset used in the debtor's farming operation" shall be treated as an unsecured claim that is not entitled to priority under § 507, provided the debtor obtains a discharge. The Bankruptcy Court found this section applied to capital gains taxes owed by the debtors arising from a post-petition sale of real property used by the debtors for farming. As a result, the Court denied the United States' objection to the debtors' Chapter 12 plan treating the capital gain taxes as a general unsecured claim.

I. Background.

The debtors first came to the attention of the United States in the 1980s, when they failed to file income tax returns. In 1988, they were convicted of willfully failing to file income tax returns for the tax years 1981, 1982, and 1983.

Doc. 2-6 at 91, United States v. Dawes, 88-10002 (D. Kan. 1989), aff. 874 F.2d 746 (10th Cir. 1989). Each of them spent seven months in federal prison. Doc. 3 at 2. Additionally, they failed to pay income taxes for 1982, 1983, 1984, 1986, 1988, and 1990. Doc. 2-6 at 91. They were assessed a tax liability of $142,007. Doc. 3 at 2. The Dawes did not pay the tax, and by 2006 the debt had grown to $1,747,841.53. Doc. 3 at 2.

In 2003, the United States filed suit against the Dawes to reduce their income tax liabilities to judgment, to set aside conveyances of real property, to obtain a determination that Plainsman Property Trust was a nominee of the Dawes, and to foreclose federal tax liens against nine real properties. United States v. Dawes, 03-1132-JTM (D.Kan. 2003), aff'd. 161 Fed.Appx. 742 (10th Cir. 2005). Judge Marten found that in 1985 and 1986, after the federal tax liens had been assessed, the Dawes began moving their property into three trusts in which close family members or the Dawes served as trustees or agents. The court found the Dawes created the Plainsman Property Company to avoid tax judgments. Judge Marten found that the Dawes' conveyance of nine parcels of land to the Plainsman Property Company must be set aside as fraudulent, and that the property was subject to the federal tax liens. Id., 03-1132-JTM (D.Kan. 2003), Doc. 33, filed Sept. 21, 2004. The District

Court approved an order for the sale of the nine parcels of property.

The Dawes filed for bankruptcy on July 14, 2006. On October 11, 2007, the IRS filed the Report of Sale for the nine parcels of property. The IRS sold all but 80 acres of the Dawes' real estate. (Doc. 3, p. 2).

II. Case History.

On July 14, 2006, Debtors filed for bankruptcy relief under Chapter 7. Doc. 2-2 at 2. The Chapter 7 case was dismissed on August 2, 2006, but was reopened, and on August 17, 2006, was converted to Chapter 12. Doc. 2-2 at 3-4. The IRS, which holds a judgment against the Debtors for $1,541,604.08, plus interest, is the principal creditor.

On October 23, 2006, the IRS obtained relief from the automatic stay to enforce its judgment as to eight parcels of real property titled in the name of Plainsman Trust. Doc. 2-2 at 7. On November 13, 2006, Debtors filed their Chapter 12 plan. Doc. 2-2 at 7, Doc. 2-3. The plan proposed to pay that portion of the IRS claim secured by the eight parcels by surrender of the property to the IRS. Doc. 2-3 at 4. The plan further provided that "pursuant to 11 U.S.C. § 1222(a)(2)(A), all claims of the IRS or the Kansas Department of Revenue that arise post-petition as a result of

the sale, transfer, exchange, or other disposition of the [nine parcels] shall be treated as a general unsecured claim not entitled to priority under § 507." Doc. 2-3 at 6. The United States objected to confirmation of the plan in numerous respects, including its treatment of taxes arising from the post-petition sale. Doc. 2-3 at 15. The parties did not immediately address this objection, proceeding instead with the sale of the property. The eight parcels were sold, and the sale proceeds exceeded $900,000. Both parties agree that the sale will result in the debtors owing a significant capital gains tax, although the exact amount was not specified in the pleadings.

On August 9, 2007, Debtors filed a motion for partial summary judgment, asking the court to find that "11 U.S.C. § 1222(a)(2)(A) allows the Debtors to provide in their Chapter 12 plan that the IRS' post-petition capital gains tax claim incurred as a result of the IRS' forced sale of Debtors' real estate is an unsecured claim." Doc. 2-2 at 17. On September 24, 2007, the United States filed a cross-Motion for Partial Summary Judgment asking the court to find that § 1222(a)(2)(A) does not apply to capital gains from post-petition sales. Doc. 2-2 at 20. The Bankruptcy Court granted the Debtors' Motion, noting that the purpose of Chapter 12 is to allow a farmer to reorganize and the purpose of § 1222 was to remove a major impediment to reorganization.

Doc. 1-2. The court found that the Chapter 12 post-petition capital gains taxes qualified as "administrative expenses" entitled to priority because they were incurred by the estate. As such, it found the tax liability was within the § 1222(a)(2)(A) exception. The court concluded that the Debtors may treat the claim as an unsecured claim not entitled to priority under § 507, limited by the condition that such treatment is allowed only if the Debtors receive a discharge. Doc. 1-2.

III. Standard of Review

"On appeal from the bankruptcy court, the district court sits as an appellate court." In re Barber, 191 B.R. 879, 882 (D.Kan. 1996). A district court reviews a bankruptcy court's factual findings for clear error, and reviews its conclusions of law de novo. Zions First Nat'l Bank, N.A. v. Christiansen Brother, Inc., 66 F.3d 1560, 1563 (10th Cir. 1995). The district court may affirm, modify, or reverse a bankruptcy judge's judgment, order, or decree or remand with instructions for further proceedings. Fed. R. Bankr. P. 8013.

IV. Summary of Arguments.

The United States contends that Section 1222(a) does not apply to any post-petition claims, including taxes. It argues that Chapter 12 plans deal only with the treatment of pre-

petition claims and are only binding upon creditors holding such claims. Appellant contends this view is confirmed by reading sections 1226(b)(1), 1222, and 1227(a) together. Moreover, it argues that the Bankruptcy Court erred in finding that the capital gain taxes were "incurred by the estate." Appellant contends that in a Chapter 12 proceeding, the estate is not a separate taxable entity and the debtor remains personally responsible for the tax. This is in contrast to Chapter 7 and 11 cases, appellant says, where the tax code provides that the bankruptcy estate shall be treated as a separate taxable entity. Only in the latter cases may the tax be said to be incurred by the estate, appellant contends, and only then may the taxes be treated as an administrative expense of the estate. *Citing* 26 U.S.C. §§ 1398, 1399. Appellant thus argues it was error to treat the taxes as administrative expenses, and error to find that they fell within the exception of section 1222(a)(2)(A).

The Debtors' response urges the court to follow several recent decisions finding that post-petition capital gain taxes fall under § 1222(a)(2)(A), including the only decision by a district court to address the issue. Debtors argue that In re Knudsen, 389 B.R. 643 (N.D.Iowa 2008), is instructive as it addresses the precise issue and relies extensively on Judge Somers' analysis. Debtors argue the plain language of

section 1222(a)(2)(A) does not restrict its applicability to pre-petition sales and that the legislative history behind the section supports the Bankruptcy Court's interpretation. They argue that appellant's interpretation, on the other hand, is flawed because it requires discriminatory treatment of similarly situated farmers, protecting only those who had the foresight to liquidate property before filing for bankruptcy protection. The debtors say post-petition tax claims have administrative priority status under section 503(b) – as the IRS has argued in other cases – and that such taxes are directly covered by § 1222(a)(2)(A). The Debtors have filed notice of supplemental authority, providing the court with two additional cases supporting their position.

V. Discussion

a. Chapter 12 Bankruptcy and 11 U.S.C. § 1222(a)(2)(A)

Chapter 12 Bankruptcy was created for family farmers with regular annual income. 11 U.S.C. § 101(19). Chapter 12 allows eligible farmer debtors to adjust their debts while they remain in control and possession of their property, and they maintain the ability to operate the farm. 8 Collier on Bankruptcy § 1200.01[2], p. 1200-4 (15th ed. Rev. 2006), 11 U.S.C. § 1227(b).

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The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was enacted on April 20, 2005. Pub. L. No. 109-8, 119 Stat. 23. The BAPCPA modified 11 U.S.C. § 1222(a)(2)(A) to read as follows: "The plan shall provide for the full payment, in deferred case payments, of all claims entitled to priority under section 507, unless the claim is a claim owed to a governmental unit that arises as a result of the sale, transfer, exchange, or other disposition of any farm asset used in the debtor's farming operation, in which case the claim shall be treated as an unsecured claim that is not entitled to priority under section 507, but the debt shall be treated in such manner only if the debtor receives a discharge." The new section 1222 created an exception by stripping priority from the claims of a "governmental unit" that "arise" from a transaction involving any farm asset used in the debtors farming operation, if the debtor receives a discharge. In re Hall, 393 B.R. 857, 862 (D.Ariz. 2008). In adopting this section, Congress was concerned that if the debtor/farmer could not pay the I.R.S. in full, the I.R.S. was likely to veto the plan, and the farmer would likely lose the farm. *See* 145 Cong. Rec. S750-02, S764, (statement of Sen. Grassley on S.260).[1] Clearly, section

[1] Senator Grassley's comments were regarding a previous amendment, "Safety 2000", which was considered in 1999.

1222(a)(2)(A) is a remedial measure designed to help family farmers reorganize and continue in operation by lessening the tax consequences of selling or transferring farm property.

Section 507 lists the expenses and claims that have priority in bankruptcy. Included are administrative expenses allowed under 11 U.S.C. § 503(b), including fees and charges assessed against the estate under chapter 123 of title 28. 11 U.S.C. § 507(a)(2). Administrative expenses are generally post-petition claims, and are assigned priority to "encourage[] the necessary par-

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The amendment did not pass at that time, but the exact language was adopted in the BAPCPA in 2005: "Safety 2000" also helps farmers to reorganize by keeping the tax collectors at bay. Under current law, farmers often face a crushing tax liability if they need to sell livestock or land in order to reorganize their business affairs. According to Joe Peiffer, a bankruptcy lawyer from Hiawatha, Iowa, who represents many family farmers, high taxes have caused farmers to lose their farms. Under the bankruptcy code, the I.R.S. must be paid in full for any tax liabilities generated during a bankruptcy reorganization. If the farmer can't pay the I.R.S. in full, then he can't keep his farm. This isn't sound policy. Why should the I.R.S. be allowed to veto a farmer's reorganization plan? " Safety 2000" takes this power away from the I.R.S. by reducing the priority of taxes during proceedings. This will free up capital for investment in the farm, and help farmers stay in the business of farming." 145 Cong. Rec. S750-02, S764, 1999 WL 20426 (Jan. 20, 1999).

ties to undertake the collection and distribution of the assets of the estate so as to generate proceeds to distribute to pre-existing creditors. 8 Collier on Bankruptcy § 507.02[1][b], p. 507-16 (15th ed. Rev. 2006). Administrative expenses are the costs of preserving the estate, and include taxes incurred by the estate, other than taxes entitled to priority under section 507(a)(8). Collier, 507- 28.

b. Application of 11 U.S.C. § 1222(a) to post-petition taxes.

The United States argues 11 U.S.C. § 1222(a) does not apply to claims for post-petition taxes. Section 1222 provides that a plan shall provide for the full payment of all claims entitled to priority under 11 U.S.C. § 507. Under section 507, there are two categories of taxes entitled to priority. Section 507(a)(8) gives priority status to certain pre-petition taxes. 11 U.S.C. § 507(a)(8); In re Schilke, 2008 WL 4224279 (D.Neb. 2008). The taxes at issue here are post-petition, therefore section 507(a)(8) is inapplicable. Section 507(a)(2) gives priority status to administrative expenses allowed under 11 U.S.C. 503(b). Section 503(b) contains an extensive list of allowed administrative expenses, including taxes incurred by the estate: "After notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this

title, including any tax incurred by the estate, whether secured or unsecured, including property taxes for which liability is in rem, in personam, or both, except a tax of a kind specified in section 507(a)(8) of this title." 11 U.S.C. § 503(b)(1)(B)(i).

The IRS argues that section 507 is limited to pre-petition claims of creditors. The IRS cites no authority for this assertion, and as discussed above, only section 507(a)(8) address pre-petition claims. Taxes that are incurred by the estate for the sale of property post-petition can clearly qualify as an administrative expense pursuant to section 503(b). Therefore, they are a priority claim pursuant to section 507(a)(2).

c. Creditor Status

The United States argues that Chapter 12 plans are only binding upon "creditors," not upon holders of post-petition claims, and it says "the binding effect of the plan can extend no further upon the United States." It points out that a "creditor" is defined as an "entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor; an entity that has a claim against the estate of a kind specified in section 348(d), 502(f), 502(g), 502(h) or 502(i) of this title; or an entity that has a community claim." 11 U.S.C. § 101(10).

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Section 1222(a)(2)(A) does not mention "creditors." Rather, the statute specifically applies to "claim[s] owed to a government unit...". 11 U.S. C. § 1222(a)(2)(A). The term "claim" is defined as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured. 11 U.S.C. § 101(5)(A). In the case at hand, the IRS, a government unit, has a right to payment for capital gain taxes arising from the sale of the Debtors' farm property. It thus has a claim against the debtors. Section 1222, by its terms, is not limited to "creditors." Moreover, the court notes that appellant's suggested construction of the statute is inconsistent with Congress's apparent intent in adopting that section: ""[C]ongress has chosen to recognize the uncollectibility of the majority of the income taxes occasioned by the sale of the farm debtor's assets used in the farming operation. The 2005 Amendments provide financially strapped family farmers the opportunity to downsize and restructure their farming operations without the necessity of paying the taxes in full as required under old Chapter 12." 7 *W. Norton, Bankr. L. & Prac.* 3d § 130:6 (2009). The statute by its terms is not limited to "creditors," and it therefore cannot be read to apply only to pre-petition claims. Section 1222 addresses claims owed to a government

unit, which includes the tax claim held by the IRS.

d. 11 U.S.C. § § 1226 and 1227

Appellant argues that post-petition claims in Chapter 12 cases are governed by 11 U.S.C. § 1226, and that when read with 11 U.S.C. § 1227 and 1222(a)(2)(A), the various sections confirm that holders of post-petition claims are not bound by Chapter 12 plans. Appellant further argues that these statutes show section that 1222(a)(2)(A) does not apply to taxes arising as a result of the sale of property of the estate.

The applicable sections of the statutes read as follows: "Before or at the time of each payment to creditors under the plan, there shall be paid any unpaid claim of the kind specified in section 507(a)(2) of this title." 11 U.S.C. § 1226(b)(1). "The provisions of a confirmed plan bind the debtor, each creditor, each equity security holder, and each general partner in the debtor, whether or not the claim of such creditor, such equity security holder, or such general partner in the debtor is provided for by the plan, and whether or not such creditor, such equity security holder, or such general partner in the debtor has objected to, has accepted, or has rejected the plan." 11 U.S.C. § 1227(a). In sum, then, the confirmed plan binds the debtor and all the creditors. Furthermore, confirmation obligates the trustee to

distribute all payments to creditors in accordance with the plan, and vests in the debtors all the rights in any post-petition acquired property. In re Plata, 958 F.2d 918, 922 (9th Cir. 1992).

As discussed above, section 507 lists the expenses and claims that have priority in bankruptcy. Administrative expenses allowed under section 503(b) and any fees and charges assessed against the estate have priority. 11 U.S.C. § 507(a)(2). Section 1226 sets out that the administrative expenses should be paid before payment to creditors of the confirmed plan. The court has already determined that post-petition taxes incurred by the estate qualify as administrative expenses pursuant to section 503(b), and are ordinarily a priority claim pursuant to section 507(a)(2).

The United States' argument that the foregoing sections necessarily preclude post petition claims fails to take into consideration the specific language of section 1222(a)(2)(A). This section specifically exempts from priority status a claim owed to a governmental unit that arises as a result of the sale of any farm asset, in which case the claim should be treated as unsecured. The claim of the IRS in this instance is a claim owed to a governmental unit, and it is the result of the sale of a farm asset, the farming property. The IRS' reliance on section 1226 and 1227 does not

overcome the straightforward and specific language of § 1222(a)(2)(A).

e. "Incurred by the estate."

The United States, relying on the "separate entity rules," argues that the post-petition income taxes are not administrative expenses because the taxes were not incurred by the Chapter 12 estate. It argues that the tax code does not consider a Chapter 12 bankruptcy estate to be a separately taxable entity, and therefore the debtors, not the estate, incurred the tax.

The Bankruptcy court referred to the legislative history of § 503(b)(1)(B)(i) in determining that the capital gains taxes are in fact administrative expenses. Specifically, the court referenced the Senate Report:

> In general, administrative expenses include taxes which the trustee *incurs in administering the debtor's estate*, including taxes on capital gains from sales of property by the trustee and taxes on income earned by the estate *during the case*. Interest on tax liabilities and certain tax penalties incurred by the trustee are also included in this first priority." S. Rep. No. 95-989, 95th Cong., 2d Sess. 66 (1978)(italics in original opinion).

Judge Somers also relied on the Report of the Recommendations of the Senate Finance Committee regarding administrative expenses: "Ad-

ministrative expenses - Taxes incurred *during the administration of the estate* share the first priority given to administrative expenses generally." S. Rep. No. 95-1106, 95th cong., 2d Sess. 13 (1978) as reported by the Senate Judiciary Committee and the Senate Finance Committee)(italics in original opinion).

The United States has raised the "separate entities" argument in other cases. In the Schilke case, the court rejected the argument, finding that a separate taxable estate was not required for post-petition taxes to be treated as administrative expenses subject to section 1222(a)(2)(A). In re Schilke, 2008 WL 4224279, at 4 (D.Neb. 2008). In doing so, the court considered the clear Congressional purpose of Chapter 12 and §1222(a)(2)(A), and found that treating post-petition taxes as administrative expenses meets the remedial purpose of providing relief to family farmers. Id.

The District Court in Arizona also considered this issue and recognized that Chapter 12 bankruptcy is treated differently than a Chapter 7 or Chapter 11. In re Hall, 393 B.R. 857, 861 (D.Ariz. 2008). It acknowledged that under the tax code, there is no separate taxable entity created when an individual commences a case under Chapter 12, as there may be in a Chapter 7 or Chapter 11. But the court said it would be

error to accept "the IRS's characterization of the pertinent provisions as federal income tax provisions found in the Bankruptcy Code, when they are properly understood as bankruptcy provisions to be construed in accordance with the Bankruptcy Code and bankruptcy policy to promote the effective reorganization of family farming operations." Id.. at 863 (quoting In re Knudson, 389 B.R. 643, 680-81 (N.D. Iowa 2008). The court examined the purpose of Chapter 12 and determined that the taxes generated from the sale of assets used in the farming operation must be considered administrative expenses to allow the debtor to receive the benefits of section 1222(a)(2)(A). Id at 863-864.

The District Court in In re Knudsen also found that taxes from sales of property after the filing of the petition may be treated as administrative expenses under 11 U.S.C. § 503(b)(1)(B)(i). 389 B.R. 643, 670 (N.D.Iowa, 2008). Knudsen relied in part on a Chapter 11 bankruptcy case where a tax claim against a corporation was split between pre-petition and post-petition taxes. In that case, the court rejected the separate entity argument, finding that a tax "incurred by the estate" referred to a tax that was incurred post-petition during the existence of the bankruptcy estate. In re L.J. O'Neill Shoe Co., 64 F.3d 1146, 1149 (8th Cir. 1995). The Eighth Circuit said in that case it was not treat-

ing the debtor and the estate as two separate entities. Rather, the tax was being imposed against a single corporate entity, but part of the tax was allocated as a claim against the estate and was treated as an administrative expense, in keeping with the bankruptcy laws determining priority of claims. Id. at 1152. The Knudson court likewise adopted this reasoning, saying that taxes may be "incurred by the estate" in a Chapter 12 because under the Bankruptcy Code that phrase refers to taxes incurred post-petition, during the existence of the bankruptcy estate, and the priority and treatment of such claims is determined under the policies in the Bankruptcy Code.

The Knudsen court went on to note that nothing in the plain language of § 1222(a)(2)(A) restricts its applicability to pre-petition sales. Id. at 675. The court examined the language of section 1222, recognizing that the "debtor's farming operation" refers to the farming operation under the reorganization plan. Id. Since reorganization occurs both before and after the filing of the Chapter 12 petition, it said, section 1222 must apply to transactions that occurred both before and after the filing of the petition. Id. The court stated that any ambiguity about a bankruptcy statute should be construed in favor of the debtor. Id. at 677. In doing so, the court should "give farmers a fighting chance" to reorganize their

debts based on farming and business factors, rather than on the potential adverse tax consequences. Id. In sum, Knudson reviewed the legislative history and case law and concluded that taxes "incurred by the estate" in § 503(b)(1)(B)(i) refers to when the tax liability is incurred rather than to the existence of the estate as a separate taxable entity. Id. at 680.

After reviewing the cases that have addressed this issue – including Schilke, Hall, and Knudson – the court finds that the decision by Judge Somers correctly applied the law and the prevailing view of section 1222(a)(2)(A). See also In re Gartner, 2008 WL 5401665 (Bkrtcy. D. Neb. 2008). In construing the provisions of the code, the court must consider the purpose of Chapter 12 bankruptcy, which is to allow the debtors to pay their debts while they maintain control of their property and attempt to continue the farm business. The Bankruptcy Court correctly observed that reorganization in a Chapter 12 applies to transactions that occur before and after the filing of the petition. Treating capital gain taxes incurred post-petition as an administrative expense of the estate – and consequently as an unsecured claim – is consistent with the language of section 1222(a)(2)(A) and accomplishes the statute's clear remedial purpose. The court concludes that the Bankruptcy Court correctly rejected the objection of the IRS, and correctly

granted the debtors' motion for summary judgment as to the construction of section 1222(a)(2)(A).

IV. Conclusion

The judgment of the Bankruptcy Court is AFFIRMED. IT IS SO ORDERED this 12th day of March, 2009, at Wichita, Ks.

s/Wesley E. Brown
Wesley E. Brown
United States District Judge

APPENDIX C — MEMORANDUM OPINION AND ORDER IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF KANSAS DATED FEBRUARY 11, 2008

SO ORDERED.

SIGNED this 11 day of February, 2008.

s/ Dale L. Somers
Dale L. Somers
UNITED STATES BANKRUPTCY JUDGE

FOR ONLINE USE AND PRINT PUBLICATION

IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF KANSAS

In re:	
DONALD W. DAWES and PHYLLIS C. DAWES, **DEBTORS.**	**CASE NO. 06-11237** **CHAPTER 12**

MEMORANDUM OPINION AND ORDER GRANTING DEBTORS' MOTION FOR SUMMARY JUDGMENT AND DENYING UNITED STATES' CROSS MOTION FOR

Appendix C

SUMMARY JUDGMENT ON WHETHER 11 U.S.C. § 1222(a)(2)(A) APPLIES TO CLAIMS ARISING FROM POST-PETITION SALES OF FARM ASSETS

Following oral argument, the Court took under advisement the Debtors' Motion for Partial Summary Judgment[1] and the United States' Cross Motion for Partial Summary Judgment.[2] One of the issues raised in Debtors' motion is whether "11 U.S.C. § 1222(a)(2)(A) allows the debtors to provide in their Chapter 12 plan that the IRS' post-petition capital gains tax claim incurred as a result of the IRS' forced sale of Debtors' real estate is an unsecured claim." Chapter 12 Debtors, Donald W. Dawes and Phyllis C. Dawes (hereinafter collectively "Debtors"), appear by their counsel, Mark J. Lazzo. Creditor, the United States of America, through the Internal Revenue Service (hereafter "IRS"), appears by Stephanie M. Page. There are no other appearances.[3] The Court has jurisdiction.[4] For the

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[1] Doc. 142.

[2] Doc. 166.

[3] The Chapter 12 Trustee, Edward J. Nazar, was present at oral argument, but has not filed a brief on any of the issues raised in the summary judgment motions.

[4] This Court has jurisdiction pursuant to 28 U.S.C. § 157(a) and §§ 1334(a) and (b) and the Standing Order of

reasons stated below, the Court grants the Debtors' motion for summary judgment, denies the IRS' cross motion for summary judgment, holds that § 1222(a)(2)(A) applies to postpetition sales, and enters judgment on this portion of the motions for partial summary judgment.

BACKGROUND AND FINDINGS OF UNCONTROVERTED FACTS.

On July 14, 2006, Debtors filed this case pro se under Chapter 7 of Title 11. The Chapter 7 case was dismissed by order filed on August 2, 2007, for failure to file form B22 and schedules. On August 4, 2006, counsel entered his appearance as counsel for Debtors. A motion to reopen case was granted, and by order entered August 17, 2006, the case was converted to Chapter 12. Edward J. Nazar was appointed Chapter 12 Trustee. The IRS, which holds a judgment against the Debtors for $1,541,604.08, plus in-

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the United States District Court for the District of Kansas that exercised authority conferred by § 157(a) to refer to the District's Bankruptcy judges all matters under the Bankruptcy Code and all proceedings arising under the Code or arising in or related to a case under the Code, effective July 10, 1984. A motion for construction of a portion of the Code relevant to confirmation of a plan is a core proceeding which this Court may hear and determine as provided in 28 U.S.C.§ 157(b)(2)(A) and (L). There is no objection to venue or jurisdiction over the parties.

terest from May 3, 2004 for 1982 through 1990 income taxes,[5] is the principal creditor.

On October 23, 2006, the IRS obtained an order of stay relief as to eight parcels of real property, titled in the name of Plainsman Trust, which was found to be Debtors' nominee in prepetition litigation between the IRS and Debtors.[6] On November 13, 2006, Debtors filed a Chapter 12 plan.[7] It proposed to pay that portion of the IRS claim secured by the eight parcels by surrender of the property to the IRS. The proposed plan further provided that "pursuant to 11 U.S.C. §1222(a)(2)(A), all claims of the IRS or Kansas Department of Revenue that arise postpetition as a result of the sale, transfer, exchange, or other disposition of the [nine parcels] shall be treated as a general unsecured claim not entitled to priority under § 507."[8] The IRS objected to the portion of the plan regarding the claims of governmental units for taxes arising

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[5] *United States v. Dawes*, 344 F. Supp. 2d 715 (D. Kan. 2004) aff'd 161 Fed. Appx. 742 (10th Cir. 2005).

[6] *United States v. Dawes*, 344 F. Supp. 2d at 715. The parties agree that the eight parcels were owned by Debtor on the date of filing.

[7] Doc. 50.

[8] *Id.*

from the postpetition sale.[9] The eight parcels of real estate were sold, and the sale proceeds exceeded $900,000.[10] Debtors assert the sale will result in a significant capital gains tax, and the IRS does not question this assertion.

On August 9, 2007, Debtors filed a motion for partial summary judgment,[11] requesting, in part, this Court to rule as follows: "§ 1222(a)(2)(A) allows the Debtors to provide in their Chapter 12 plan that the IRS' post-petition capital gains tax claim incurred as a result of the IRS' forced sale of Debtors' real estate is an unsecured claim." On September 24, 2007, the IRS filed its Reply and Cross Motion for Partial Summary Judgment,[12] moving for summary judgment on the issue that § 1222(a)(2)(A) does not apply to capital gains from postpetition sales.

There are no material facts in controversy. The question before the Court is an issue of law which has been fully briefed. Oral arguments have been heard. The Court is now ready to rule and, for the reasons stated below, grants the Debtors' motion and denies the IRS' motion, find-

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[9] Doc. 62.

[10] Doc. 142.

[11] Doc. 142.

[12] Doc. 166.

ing that capital gains taxes arising from postpetition sales of assets by a Chapter 12 debtor are governed by § 1222(a)(2)(A).

ANALYSIS AND CONCLUSIONS OF LAW.

Section 1222 addresses the requirements for confirmation of a Chapter 12 plan. Prior to the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), absent agreement otherwise, § 1222(a)(2) required full payment in deferred cash payments of all priority claims as defined by § 507. Subsection 1222(a)(2) provided:

> (a) The plan shall–
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> * * *
>
> (2) provide for the full payment, in deferred cash payments, of all claims entitled to priority under section 507 of this title, unless the holder of a particular claim agrees to a different treatment of such claim.

Effective for all cases filed after April 20, 2005, Congress amended § 1222(a)(2) by adding subsection (A), so the subsection now provides:

> (a) The plan shall–
>
> * * *
>
> (2) provide for the full payment, in deferred cash payments, of all claims entitled to priority under section 507, unless–
> (A) the claim is a claim owed to a governmental unit that rises as a result of the sale, transfer, ex-

> change, or other disposition of any farm asset used in the debtor's farming operation, in which case the claim shall be treated as an unsecured claim that is not entitled to priority under section 507, but the debt shall be treated in such manner only if the debtor receives a discharge;

Debtors contend the capital gains taxes arising from the postpetition sale of the farm real property come within the new provision and the plan need not provide for payment in full of this unsecured claim. The IRS contends the new provision is inapplicable to capital gains taxes arising from postpetition dispositions of farm assets in a Chapter 12 case because the tax is the personal liability of the debtor, not an administrative expense of the estate entitled to priority under § 507. Thus, the issue presented is whether the claim for capital gains taxes arising from the postpetition sale of real property is a priority claim under § 507, which pursuant to § 1222(a)(2)(A) shall be treated as an unsecured claim not entitled to priority.

Section 507 sets forth ten categories of claims that are entitled to priority status. Because holders of priority claims have special rights, "priorities . . . are narrowly construed [and a] party must fit clearly within the requirements of the priority statute to be accorded priority sta-

tus."[13] Of the ten categories, there is only one, administrative claims under § 507(a)(2), which the parties address as possibly applicable to postpetition capital gains taxes.

Second priority claims are defined by § 507(a)(2) as follows: "[A]dministrative expenses allowed under section 503(b) of this title, and any fees and charges assessed against the estate under chapter 123 of title 28." "[A]dministrative expenses are generally those that are incurred by the estate after the entry of the order for relief."[14] The relevant portion of § 503, allowance of administrative expenses, in subsection (b)(1), provides:

> (b) After notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including–
> (1)(A) the actual, necessary costs and expenses of preserving the estate including–
> * * *
> (B) any tax–
> (i) incurred by the estate, whether secured or unsecured, including property taxes for which liabili-

[13] *Collier on Bankruptcy* ¶ 507.01 (Alan N. Resnick & Henry J. Sommer eds.-in-chief, 15th ed. rev. 2007).

[14] 4 *Collier on Bankruptcy* ¶ 503.01.

> ty is in rem, in personam, or both, except a tax of a kind specified in section 507(a)(8) of this title; or
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> * * *
>
> (D) notwithstanding the requirements of subsection (a), a governmental unit shall not be required to file a request for the payment of an expense described in subparagraph (B) or (C), as a condition of its being an allowed administrative expense;

Taxes are therefore accorded administrative expenses priority if they are (1) "incurred by the estate" and (2) not "of a kind specified in section 507(a)(8)." "[T]he reference in section 503(a)(1)(B)(i) [sic] to section 507(a)(8) means that, to the extent that a debtor's prepetition liability becomes a tax claim after the petition, it is not for that reason alone to be given administrative expense status."[15] The IRS agrees that the capital gains taxes at issue in this case are not priority taxes under § 507(a)(8), such that the second requirement is satisfied.[16] Thus, the issue as to administrative claim status is whether the

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[15] 4 Collier on Bankruptcy ¶ 503.07[2].

[16] Doc. 166. Each of the three cases addressing whether capital gains taxes arising from the postpetition sale of assets in a Chapter 12 case have held that the taxes are not priority taxes under § 507(b)(1)(B). *In re Knudsen*, 356 B.R. 480, 490 (Bankr. N.D. Iowa 2006); *In re Hall*, 376 B.R.741, 744 (Bankr. D. Ariz. 2007); and *In re Schilke*, 379 B.R. 899, 901 (Bankr. D. Neb. 2007).

taxes were "incurred by the estate" within the meaning of § 503(b)(1)(B)(i). The IRS contends the taxes were not "incurred by the estate" because in a Chapter 12 case the filing of the petition does not create a new taxable entity so the taxes incurred postpetition are the liability of the debtor, not the estate.

Debtors rely on *Knudsen*,[17] the first case addressing whether § 1222, as amended by BAPCPA, permits debtors to treat an IRS claim for postpetition capital gains taxes as an unsecured claim. The court in *Knudsen* answered yes. It found capital gains taxes arising from the postpetition sale of debtors' farm assets were administrative expenses under § 503(b)(1)(B)[18] and such taxes can be treated as unsecured and dischargeable pursuant to § 1222(a)(2)(A). The court noted that "[p]revious to BAPCPA, it has

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[17] *In re Knudsen*, 356 B.R. at 480.

[18] The *Knudsen* court held that debtors' tax debt, which included both prepetition and postpetition components, could be "divided into separate components in accordance with the bankruptcy laws determining the priority of payment of those claims." *Id.*, 356 B.R. at 490, *quoting Missouri Dept. Of Rev. v. L.J. O'Neill Shoe Co. (In re L.J. O'Neill Shoe Co.)*, 64 F.3d 1146, 1152 (8th Cir. 1995). Section 1222(a)(2)(A) treatment based upon administrative claim status was litigated only for taxes arising from postpetition sales of farm assets.

been the priority status of an IRS claim arising from a debtor's sale of capital assets that often prevented chapter 12 debtors from reorganizing."[19] In amending § 1222, Congress removed this confirmation impediment. "By treating the portion of income tax resulting from the sale of capital assets as an unsecured claim, the farmer would no longer have to pay it in full to obtain confirmation."[20] *Knudsen* has been followed by *Schilke*,[21] which held that the Chapter 12 plan could treat the capital gains tax from the postpetition sale of assets as a general unsecured debt, even though acknowledging that debtors' Chapter 12 estate was not a separate taxable entity.[22] As to administrative expense characterization, the court stated:

> I do not believe that the language of § 503(b)(1)(B) regarding any tax "incurred by the estate" was intended to apply only to those situations where the estate itself is a separate taxable entity. In fact "incurred by the estate" has been interpreted to simply mean incurred post-petition.[23]

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[19] *In re Knudsen*, 356 B.R. at 488.

[20] *Id*.

[21] *In re Schilke*, 379 B.R. at 899.

[22] *Id*., 379 B.R. at 902.

[23] *Id*., citing *U.J. O'Neill Shoe Co.*, 64 F.3d at 1149.

Knudsen was rejected by *Hall*,[24] on which the IRS relies. *Hall* held that federal taxes on capital gains arising from the postpetition sale of farm assets in a Chapter 12 case are not entitled to administrative claim status under § 503(b)(1)(B)(i). The court read the definition of administrative claim in conjunction with the Internal Revenue Code (IRC) and concluded that because there is no separate taxable entity created by the filing of a Chapter 12 case, the capital gains tax arising from postpetition disposition of assets could not be "incurred by the estate."[25]

The IRS urges this Court to follow the reasoning of *Hall*. According to the IRS, in a Chapter 12 case, capital gains taxes arising from postpetition dispositions of the estate property are not administrative expenses because the tax liability is not "incurred by the estate," since in a Chapter 12 case the estate is not a separate taxpayer. The IRS relies upon the IRC §§ 1398 and 1399 which define the person liable for taxes on the income of a bankruptcy estate. IRC § 1398 applies to cases under Chapter 7 or Chapter 11 of Title 11 " in which the debtor is an individual" and provides the tax on the taxable income of the estate is computed in the same manner as for an

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[24] *In re Hall*, 376 B.R. at 741.

[25] *Id.*, 376 B.R. at 746.

individual and "shall be paid by the trustee."[26] IRC § 1399 provides, "Except in any case to which section 1398 applies, no separate taxable entity shall result from the commencement of a case under Title 11 of the United States Code."[27] Accordingly, the Court agrees with the IRS' position that the bankruptcy trustee has liability for income taxes in individual Chapter 7 and 11 cases, but not in corporate or other entity Chapter 7 and 11 cases or in any case under Chapter 12 or 13.

But this conclusion does not answer the question whether capital gains taxes arising from the postpetition sale of assets in a Chapter 12 case constitute administrative expenses under § 503(b)(1)(B)(i). The Court finds that the phrase "incurred by the estate" in § 503(b)(1)(B)(i) defining administrative expense for certain taxes is ambiguous. For all chapters, including Chapter 12, the filing of a petition under Title 11 creates an estate comprised of all of the property of the debtor, as defined by § 541.[28] "Incurred by the estate" could have reference to the time liability for a tax accrues - did the liability arise before or after the creation of the estate under § 541. Or,

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[26] 26 U.S.C. § 1398.

[27] 26 U.S.C. § 1399.

[28] 11 U.S.C. §§ 541 and 1207.

"incurred by the estate" could have reference to the entity liable for the tax - is the bankruptcy estate created under § 541 liable for the tax? Accordingly, the Court will consider legislative history to determine Congressional intent.[29]

The § 503(b)(1)(B)(i) definition of administrative expense, which applies to all chapters of the Code, was enacted as part of the 1978 Bankruptcy Code. The Senate report accompanying the proposed legislation does not address the identity of the taxpayer as a relevant consideration. It states, when discussing § 503(b)(2):

> In general, administrative expenses include taxes which the trustee *incurs in administering the debtor's estate*, including taxes on capital gains from sales of property by the trustee and taxes on income earned by the estate *during the case*. Interest on tax liabilities and certain tax penalties incurred by the trustee are also included in this first priority.[30]

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[29] *Blum v. Stenson*, 465 U.S. 886, 896 (1984) (stating where "resolution of a question of federal law turns on a statute and the intention of Congress, we look first to the statutory language and then to the legislative history if the statutory language is unclear") .

[30] S. Rep. No. 95-989, 95th Cong., 2d Sess. 66 (1978) (italics supplied), reprinted in D *Collier on Bankruptcy* App. Pt. 4-2008.

Appendix C

The Report of the Recommendations of the Senate Finance Committee, to which the tax-related provisions of the proposed Code had been referred, stated in part as follows concerning tax priorities: "Administrative expenses - Taxes *incurred during the administration of the estate* share the first priority given to administrative expenses generally."[31] Hence, the legislative history of § 503(b)(2)(B) evidences that Congress intended "incurred by the estate" to have reference to when the tax liability was incurred, not to the entity having liability for the tax.

This conclusion is strengthened by the history of the enactment of tax provisions related to the 1978 Bankruptcy Code. The phrase "incurred by the estate" in the definition of administrative expenses in § 503(b)(2)(B)(i) was adopted in 1978. Proposals in the 1978 bankruptcy bill concerning federal taxation were not enacted.[32] The

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[31] S. Rep. No. 95-1106, 95th Cong., 2d Sess. 13 (1978) (as reported by the Senate Judiciary Committee and the Senate Finance Committee) (italics supplied), reprinted in *D Collier on Bankruptcy* App. Pt. 4-2158.

[32] See *Id.*, 7 (stating, "Federal tax rules dealing with the subject matter of this section of title 11 [section 346] will be the subject of legislation expected early in the next Congress."); *see also Towers v. United States (In re Pacific-Atlantic Trading Co.)*, 64 F.3d 1292, 1298-1301 (9th Cir. 1995) (when determining that corporate Chapter 11

bankruptcy related tax proposals were enacted as separate legislation, the Bankruptcy Tax Act of 1980. The situation was described as follows:

> Prior to the enactment of the Bankruptcy Tax Act of 1980, there were no specific Internal Revenue Code provisions addressing the federal tax treatment of bankrupt individuals and their corresponding bankruptcy estates. The only guidance was provided by a few rulings issued by the IRS and judicial decisions, which were often conflicting. The legislative history underlying the codification of I.R.C. Section 1398 emphasized the obvious lack of guidance that created uncertainty for taxpayers and the courts.[33]

IRC §§ 1398 and 1399, relied upon by the IRS in this case, were enacted as part of that 1980 tax legislation.[34] That legislation amended the IRC and addressed matters of tax filing, reporting, and payment obligations, not the definition of administrative claim in the Bankruptcy Code.[35]

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debtor's tax liability to be an administrative expense, the court examined in detail the legislative history of interaction between the Bankruptcy Code, particularly § 346, and the tax law).

[33] 15 *Collier on Bankruptcy* ¶ TX2.02[3].

[34] Pub. L. 96-589 (1980), reprinted in E-1 *Collier on Bankruptcy* App. Pt. 5(a).

[35] See 15 *Collier on Bankruptcy* ¶ ¶TX3.01, TX 3.02 and TX 3.03.

Hence, the foregoing legislative history regarding the 1978 Code and the 1980 Bankruptcy Tax Act leads the Court to conclude that the use of the phrase "incurred by the estate" in the definition of administrative expenses in § 503(b)(1)(B)(i) has reference to the time when tax liability is incurred and not to whether the estate is a separate taxable entity.

This is the construction given to the phrase by courts and commentators since 1978. Other than the one recent case construing § 1222 as amended by BAPCPA,[36] the IRS has not cited and the Court has been unable to locate any Chapter 7, 11, or 12 case where taxpayer status was considered in determining whether tax claims were entitled to administrative claim status.[37] Commentators and cases, consistent with

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[36] *In re Hall*, 376 B.R. at 741.

[37] There are surprisingly few reported cases addressing whether capital gains taxes arising from postpetition sales are administrative expenses. The Court speculates that this is because the construction of § 503(b)(1)(B)(i) to include such taxes is so well accepted. The Court's research has revealed the following cases where capital gains taxes from postpetition sales in Chapter 7 and Chapter 11 cases have been held to be administrative expenses. *In re Goffena*, 175 B.R. 386, 391 (Bankr. D. Mont. 1994) (holding the tax liability incurred by the estate due

the legislative history, construe the phrase "incurred by the estate" in § 503(b)(1)(B)(i) to have reference to the time the "tax accrues and becomes a fixed obligation."[38] The distinction is whether the tax should be considered to have accrued to the postpetition estate as opposed to the debtor prepetition. Commentators do not identify the IRC provisions on which the IRS relies as relevant to the determination of administrative claim status for taxes accruing postpetition.[39]

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to the Chapter 7 Trustee's sale of real property is an administrative expense pursuant to § 503(b)(1)(B)); *In re Swann*, *149 B.R. 137, 144-45 (Bankr. D.S.D. 1993)* (holding capital gains taxes arising from Chapter 7 Trustee's § 363 sale of secured property is an administrative expense); and *In re Scott Cable Communications*, 227 B.R. 596, 600 (Bankr. D. Conn. 1998) (Chapter 11 Debtor conceded that capital gains tax that accrues during the administration of the case is an administrative expense under § 503(b)(1)(B)).

[38] 4 *Collier on Bankruptcy* ¶ 503.07[1]; *see United Mine Workers of Amer. 1992 Benefit Plan v. Rushton (In re Sunnyside Coal Co.)*, 146 F.3d 1273 (10th Cir. 1998) (holding that in a voluntary corporate Chapter 11 case, liability under the Coal Act arising postpetition constituted taxes incurred by the estate).

[39] See 3 *Norton Bankruptcy Law & Practice 3rd* § 49:21 (Norton, auth & ed.-in- chief 2008) (noting legislative history in support of the broad interpretation of which taxes are entitled to administrative status and citing cases holding capital gains taxes arising from sale of property

Appendix C

If administrative claim status were dependent upon the creation of a new taxpaying entity upon the filing of a petition, federal taxes incurred by Chapter 7 and Chapter 11 corporate debtors would be denied administrative claim status, as under the IRC sections cited by the IRS a corporation's filing of a petition under either Chapter 7 or Chapter 11 does not create a new taxpayer. Yet, it appears to this Court that in the past the IRS, when seeking to benefit from administrative claim priority, has disregarded the IRC Code sections on which it now relies. For example, in *United States v. Noland*,[40] the United States claimed administrative expense treatment for FUTA and FICA taxes, interest, and penalties that accrued after a corporate debtor filed for relief under Chapter 11 but before the case was converted to Chapter 7. The Chapter 7 Trustee opposed the IRS as to the penalty and interest. The bankruptcy court found the taxes to be administrative claims but held them categorically

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during administration of the estate are administrative expenses); and 4 *Collier on Bankruptcy* § 503.07[2][a] (stating it is clear that any taxes measured by the income earned postpetition will be administrative expenses of the debtor, but noting that some taxes on income earned prepetition may also be entitled to administrative expenses treatment depending upon when the tax year ends for a particular debtor under the various bankruptcy chapters).

[40] 517 U.S. 535 (1996).

subject to equitable subordination under § 510(c). The district court and Sixth Circuit affirmed. The United States Supreme Court held that the IRS' claims could not be categorically equitably subordinated in derogation of the Congressional scheme of administrative expense priority for penalties relating to priority taxes by § 503(b)(1)(B).

As to the administrative claim status of capital gains taxes, the general acceptance of the irrelevancy under the Code of whether or not a Chapter 7 or Chapter 11 debtor is an individual is illustrated by cases where such treatment was afforded without opposition. For example, in a corporate Chapter 11 case in litigation with the IRS, the debtor conceded that the capital gains tax arising from the postpetition sale of debtor's assets was an administrative expense if it accrued during the administration of the estate.[41] In another corporate Chapter 11 case, the court stated, "it is important to note at the outset that administrative expenses should include taxes

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[41] *In re Scott Cable Communications, Inc.*, 227 B.R. at 600, (sustaining IRS' objection to confirmation for the reason that the plan failed to provide for payment of the capital gains tax attributed to the sale of assets contemplated by the plan as an administrative expense and rejecting debtor's contention that such treatment was required when the sale occurred postconfirmation).

which the trustee, and, in Chapter 11 cases, the [corporate] Debtor-in-Possession, incurs in administering the estate, including taxes based upon capital gains from sales of property and taxes on income earned by the estate during the case post-petition."[42]

In the past, in a Chapter 12 case, the IRS has agreed that a claim arising from the debtor's failure to pay postpetition employment taxes as they became due was an administrative expense subject to § 1222(a)(2).[43] It therefore appears to the Court that the IRS has now changed its position because of the detrimental consequences if § 1222(a)(2), as amended by BAPCPA, applies to the capital gains taxes arising from the sale of Debtors' farm property. This view not only is inconsistent with the IRS' prior position but is also short sighted. If this Court were to adopt the rationale urged by the IRS, the holding would impact not only Chapter 12 cases, but also corporate Chapter 7 and 11 cases, and perhaps even tax claims of local and state authorities.

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[42] *In re Hillsborough Holdings Corp.*, 156 B.R. 318 (Bankr. M.D. Fla. 1993). *See also In re Pacific-Atlantic Trading Co.*, 64 F.3d at 1291 (holding that tax liability of corporate Chapter 7 debtor for taxes not assessed prepetition but assessable postpetition was entitled to allowance as an administrative expense).

[43] In re Ryan, 228 B.R. 746, 747 (Bankr. D. Or. 1999).

The Debtors' construction, is not only consistent with past understanding, but also promotes the purpose of § 1222(a)(2)(A). One respected commentator states the following:

> . . . The treatment now afforded certain priority claims is radically different than treatment afforded in Chapter 11 or Chapter 13. This treatment was included in the 2005 Amendments in order to allow farm debtors to liquidate unprofitable portions of their family farm enterprise so that they could lower debt and improve profitability without regard to the capital gains tax or depreciation recapture which normally colors all sale decisions for family farmers. Thus, the family farmer is allowed to make sound business decisions unfettered by the potential negative tax implications of the decisions.[44]

If, as contended by the IRS, only capital gains taxes arising from prepetition sales are covered by § 1222 (a)(2)(A), the provision would not apply to all "farm debtors," but only to farmers who had the foresight to liquidate assets before filing. The limited legislative history which is available contradicts this construction and strongly supports a construction urged by Debtors.[45] Senator Grassley, when introducing legislation in 1999

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[44] 7 *Norton Bankruptcy Law & Practice 3rd* § 133:6, n. 2.

[45] *See In re Knudsen*, 356 B.R. at 492.

containing identical tax benefits for family farmers, stated:

> "Safety 2000" also helps farmers to reorganize by keeping the tax collectors at bay. Under current law, farmers often face a crushing tax liability if they need to sell livestock or land in order to reorganize their business affairs. According to Joe Peiffer, a bankruptcy lawyer from Hiawatha, Iowa, who represents many family farmers, high taxes have caused farmers to lose their farms. Under the bankruptcy code, the I.R.S. must be paid in full for any tax liabilities generated during a bankruptcy reorganization. If the farmer can't pay the I.R.S. in full, then he can't keep his farm. This isn't sound policy. Why should the I.R.S. be allowed to veto a farmer's reorganization plan? "Safety 2000" takes this power away from the I.R.S. by reducing the priority of taxes during proceedings. This will free up capital for investment in the farm, and help farmers stay in the business of farming.[46]

Construing § 1222(a)(2)(A) to apply to postpetition sales provides debtors and their counsel when formulating a plan the flexibility intended by Congress to make decisions driven by farming and business factors, rather than potential adverse tax consequences.

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[46] 145 Cong. Rec. S750-02, (Jan. 20, 1999) (available at 1999 WL 20426).

Appendix C

The entire purpose of Chapter 12 is to allow a farmer to reorganize, and the specific purpose of the amendment to § 1222 was to remove a major impediment to reorganization. The IRS' interpretation of 1222(a)(2)(A) would require a farmer to develop a reorganization plan before filing, when few farmers have the benefit of legal counsel. Further, if that plan included selling assets, the farmer would be required to actually sell them prior to filing a Chapter 12. This alone would deprive a farmer of the benefit of the breathing space afforded by the automatic stay, which provides a period to develop a future plan for farming free from worrying about foreclosure and other creditor pressures. If Congress was primarily concerned with relieving the farmer of capital gains taxes incurred before filing bankruptcy, it would have made the amendment applicable to both Chapter 7 and Chapter 12 cases. It did not do so because the major goal was to assist reorganization and continuation of the debtor's farming operation. The IRS interpretation flies directly in the face of Congress' intent to amend Chapter 12 so that a farmer may develop a plan that includes selling property and not have capital gains taxes stand in the way of plan confirmation and a successful reorganization.

Appendix C

The IRS contends this Court should not follow *Knudsen* because it improperly relied upon *O'Neill Shoe Co.*[47] It points out that in *O'Neill Shoe* administrative claim status of the capital gains from postpetition dispositions of assets was not in dispute, that amendment to § 507 by the BAPCPA abrogated the ruling of *O'Neill Shoe*, and that *O'Neill Shoe* was a Chapter 11 rather than a Chapter 12 case. None of these matters cause the Court to reject the holding of *Knudsen*. The fact that administrative claim status was not litigated supports this Court's view that the allowance of such claims as entitled to administrative priority is so well established, even for Chapter 11 corporate debtors, that it is seldom litigated. Further, as thoroughly examined above, this Court concludes that Chapter 12 postpetition capital gains taxes are administrative expenses based upon Congressional intent without reliance on either *Knudsen* or *O'Neill Shoe*. Second, the amendment to § 507 after the *O'Neill Shoe* decision had to do with eighth priority claims, a matter not in issue in this case. Third, the fact that *O'Neill Shoe* is a Chapter 11 corporate debtor case means that in that case, as in this case, the filing of the petition did not create a separate taxable estate. This supports Debtors' argument that the fact that the filing of

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[47] *In re L.J. O'Neill Shoe Co.*, 64 F.3d at 1146.

a Chapter 12 case does not create a new taxpayer does not defeat administrative claim status for the taxes in issue.

The Court respectfully declines to follow *Hall*,[48] the § 1222(a)(2)(A) case which adopted the IRS' arguments. This Court questions the *Hall* court's reliance on the "maxim that the courts are to 'assume that Congress is aware of existing law when it passes legislation.'"[49] Although IRC §§ 1398 and 1399 were in place at the time of BAPCPA, this Court has been unable to find any Chapter 12, or even any Chapter 7 or Chapter 11 case, where those IRC provisions were held to be relevant to the construction of the definition of administrative claim in § 503(b)(2)B)(i). It is highly doubtful that Congress could have foreseen the impediment to the application of § 1222(a)(2)(A) relied upon by the IRS in this case.

The IRS also contends its position is supported by *Brown*,[50] a Chapter 13 case relied upon by *Hall*. In *Brown*, after confirmation of a Chapter 13 plan, the debtor sold rental property and

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[48] *In re Hall*, 376 B.R. at 741.

[49] *Id.*, 376 B.R. at 746.

[50] *In re Brown*, 2006 WL 3370867 (Bankr. D. Mass. Nov. 20, 2006).

sought to have the resulting income taxes treated as an administrative claim of the estate. The *Brown* court rejected administrative claim status because § 1305, rather than § 503(b)(1)(B)(i), controls postpetition tax claims in Chapter 13 cases, as well as because the Chapter 13 estate is not a separate taxable entity. This Court declines to follow *Brown*, which relied primarily upon § 1305. Section 1305 has been construed to eliminate a tax creditor from receiving administrative claim status under § 503(b)(1)(B)(i) for taxes accruing postpetition.[51] It has also been held that § 1305 grants to the tax creditor the "option whether it wishes to participate in a pending Chapter 13 bankruptcy because only the holder of the postpetition claim may file a claim under § 1305(a)."[52] Although in some respects patterned after Chapter 13, Chapter 12 has no provision similar to § 1305. Rather, as to administrative expenses, § 503(b)(1)(D), enacted by BAPCPA, provides that "a governmental unit shall not be required to file a re-

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[51] *In re Wright*, 66 B.R. 125 (Bankr. D. Kan. 1984); *In re Gyulafia*, 65 B.R. 913 (Bankr. D. Kan. 1986) (rejecting IRS position that it had a choice between filing a claim under § 1305 and filing a claim for administrative expense under § 503).

[52] *In re Brensing*, 337 B.R. 376, 382 (Bankr. D. Kan. 2006).

quest for the payment of an expense described in subparagraph (B) or (C), as a condition of its being an allowed administrative expense."[53]

The Court holds that administrative claim status for federal income taxes arising from the postpetition sales of farm assets is not determined by whether the tax is payable by the case trustee under §§ 1398 and 1399 of the IRC. If this were the case, all postpetition income taxes of Chapter 7 and 11 debtors other than individuals would not constitute administrative expenses. The legislative history of § 503(b)(1)(B)(i) and case law applying the subsection make no distinctions in Chapter 7 and 11 cases based upon the character of the debtor as an individual or whether the trustee has liability for postpetition taxes. The fact that in a Chapter 12 case a new taxpayer is not created is not relevant to the allowance of postpetition taxes as administrative claims. This construction promotes the Congressional purpose, identified by the *Knudsen* court, to remove the impediment to Chapter 12 plan confirmation imposed by the pre-BAPCPA requirement that capital gains taxes arising from the sale of farm assets be paid in full.

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[53] *See also* 3 *Norton Bankruptcy Law & Practice 3rd*. §49:16 (stating the proof of claim provisions of the Code do not apply to administrative expenses).

Appendix C

CONCLUSION.

For the foregoing reasons the Court rejects the objection of the IRS to the Debtors' Chapter 12 plan premised upon Debtors' construction of § 1222(a)(2)(A) and concludes that the capital gains taxes arising from the postpetition sale of Debtors' real property are not prohibited from administrative expense treatment because the filing of a Chapter 12 case does not create a new taxpaying entity. Having rejected the IRS' only objection to the Debtors' position that the capital gains taxes are not entitled to priority under § 507 as an administrative claim, the Court finds that the capital gains tax liability arising from the sale of Debtors' farm property is within the § 1222(a)(2)(A) exception to the requirement that all claims entitled to priority under § 507 be paid in full in deferred cash payments. Accordingly Debtors' plan may treat the claim as an unsecured claim not entitled to priority under § 507, limited by the condition that such treatment is allowed only if the Debtors receive a discharge. Debtors' motion for summary judgment on the construction of § 1222(a)(2)(A) is granted, and the IRS' cross motion for summary judgment on the same issue is denied.

The foregoing constitute Findings of Fact and Conclusions of Law under Rules 7052 and

9014(c) of the Federal Rules of Bankruptcy Procedure which make Rule 52(a) of the Federal Rules of Civil Procedure applicable to this matter. A judgment based upon this ruling will be entered on a separate document as required by Federal Rule of Bankruptcy Procedure 9021 and Federal Rule of Civil Procedure 58. Further, the Court determines pursuant to Federal Rule of Civil Procedure Civil 54(b), which is referenced in Federal Rules of Civil Procedure 58, there is no just reason for delay in the entry of judgment on this issue, even though this memorandum opinion adjudicates fewer than all of the objections to confirmation of Debtors' Chapter 12 plan and fewer than all rights and liabilities addressed by the Debtors' motion for partial summary judgment and the IRS' cross motion for summary judgment.

IT IS SO ORDERED.

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APPENDIX D – ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT DATED JULY 5, 2011

FILED
United States Court of Appeals
Tenth Circuit

July 5, 2011

Elisabeth A. Shumaker
Clerk of Court

UNITED STATES COURT OF APPEALS

FOR THE TENTH CIRCUIT

In re: DONALD W. DAWES; PHYLLIS C. DAWES, Debtors, ---------- UNITED STATES OF AMERICA, Appellant, v. DONALD W. DAWES, et al., Appellees, and EDWARD J. NAZAR, Trustee, Defendant.	No. 09-3129

Appendix D

ORDER

Before **TYMKOVICH, McKAY**, and **GORSUCH**, Circuit Judges.

Appellees' petition for rehearing is denied.

Entered for the Court,

s/ Elisabeth A. Shumaker

ELISABETH A. SHUMAKER, Clerk

APPENDIX E
STATUTORY APPENDIX

U.S. Const. art. I, § 8, cl. 1: Powers of Congress; Levy of Taxes for Common Defense and General Welfare; Uniformity of Taxation

The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States

U.S. Const. art. I, § 8, cl. 4: Naturalization and Bankruptcy

To establish an uniform Rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States;

11 U.S.C. § 503(b)(1)(B)(i): Allowance of administrative expenses

(b) After notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including--

(1) . . . (B) any tax--

(i) incurred by the estate, whether secured or unsecured, including property taxes for which liability is in rem, in personam, or both, except a tax of a kind specified in section 507(a)(8) of this title;

11 U.S.C. §§ 507(a)(2), 507(a)(8): Priorities

(a) The following expenses and claims have priority in the following order:

***

(2) Second, administrative expenses allowed under section 503(b) of this title, unsecured claims of any Federal reserve bank related to loans made through programs or facilities authorized under section 13(3) of the Federal Reserve Act (12 U.S.C. 343), and any fees and charges assessed against the estate under chapter 123 of title 28.

***

(8) Eighth, allowed unsecured claims of governmental units, only to the extent that such claims are for--

(A) a tax on or measured by income or gross receipts for a taxable year ending on or before the date of the filing of the petition--

(i) for which a return, if required, is last due, including extensions, after three years before the date of the filing of the petition;

(ii) assessed within 240 days before the date of the filing of the petition, exclusive of--

(I) any time during which an offer in compromise with respect to that tax was pending or in effect during that 240-day period, plus 30 days; and

(II) any time during which a stay of proceedings against collections was in effect in a prior case under this title during that 240-day period, plus 90 days; or

(iii) other than a tax of a kind specified in section 523(a)(1)(B) or 523(a)(1)(C) of this title, not assessed before, but assessable, under applicable law or by agreement, after, the commencement of the case;

(B) a property tax incurred before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition;

(C) a tax required to be collected or withheld and for which the debtor is liable in whatever capacity;

(D) an employment tax on a wage, salary, or commission of a kind specified in paragraph (4) of this subsection earned from the debtor before the date of the filing of the petition, whether or not actually paid before such date, for which a return is last due, under applicable law or under any extension, after three years before the date of the filing of the petition;

(E) an excise tax on--

(i) a transaction occurring before the date of the filing of the petition for which a return, if required, is last due, under applicable law or under any extension, after three years before the date of the filing of the petition; or

(ii) if a return is not required, a transaction occurring during the three years immediately preceding the date of the filing of the petition;

(F) a customs duty arising out of the importation of merchandise--

(i) entered for consumption within one year before the date of the filing of the petition;

(ii) covered by an entry liquidated or reliquidated within one year before the date of the filing of the petition; or

(iii) entered for consumption within four years before the date of the filing of the petition but unliquidated on such date, if the Secretary of the Treasury certifies that failure to liquidate such entry was due to an investigation pending on such date into assessment of antidumping or countervailing duties or fraud, or if information needed for the proper appraisement or classification of such merchandise was not available to the appropriate customs officer before such date; or

(G) a penalty related to a claim of a kind specified in this paragraph and in compensation for actual pecuniary loss.

An otherwise applicable time period specified in this paragraph shall be suspended for any period during which a governmental unit is prohibited under applicable nonbankruptcy law from collecting a tax as a result of a request by the debtor for a hearing and an appeal of any collection action taken or proposed against the debtor, plus 90 days; plus any time during which the stay of proceedings was in effect in a prior case under this title or during which collection was precluded by the existence of 1 or more confirmed plans under this title, plus 90 days.

Appendix E

11 U.S.C. § 541(a): Property of the estate

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is--

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date--

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

Appendix E

11 U.S.C. § 1207(a): Property of the estate

(a) Property of the estate includes, in addition to the property specified in section 541 of this title--

(1) all property of the kind specified in such section that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7 of this title, whichever occurs first; and

(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7 of this title, whichever occurs first.

11 U.S.C. § 1222(a)(2)(A): Contents of plan

(a) The plan shall--

***

(2) provide for the full payment, in deferred cash payments, of all claims entitled to priority under section 507, unless--

(A) the claim is a claim owed to a governmental unit that arises as a result of the sale, transfer, exchange, or other disposition of any farm asset used in the debtor's farming operation, in which case the claim shall be treated as an unsecured

claim that is not entitled to priority under section 507, but the debt shall be treated in such manner only if the debtor receives a discharge;

11 U.S.C. § 1305: Filing and allowance of postpetition claims

(a) A proof of claim may be filed by any entity that holds a claim against the debtor--

(1) for taxes that become payable to a governmental unit while the case is pending; or

(2) that is a consumer debt, that arises after the date of the order for relief under this chapter, and that is for property or services necessary for the debtor's performance under the plan.

(b) Except as provided in subsection (c) of this section, a claim filed under subsection (a) of this section shall be allowed or disallowed under section 502 of this title, but shall be determined as of the date such claim arises, and shall be allowed under section 502(a), 502(b), or 502(c) of this title, or disallowed under section 502(d) or 502(e) of this title, the same as if such claim had arisen before the date of the filing of the petition.

(c) A claim filed under subsection (a)(2) of this section shall be disallowed if the holder of such claim knew or should have known that prior ap-

proval by the trustee of the debtor's incurring the obligation was practicable and was not obtained.

26 U.S.C. § 1398: Rules relating to individuals' Title 11 cases

(a) Cases to which section applies.--Except as provided in subsection (b), this section shall apply to any case under chapter 7 (relating to liquidations) or chapter 11 (relating to reorganizations) of Title 11 of the United States Code in which the debtor is an individual.

(b) Exceptions where case is dismissed, etc.--

(1) Section does not apply where case is dismissed.--This section shall not apply if the case under chapter 7 or 11 of Title 11 of the United States Code is dismissed.

(2) Section does not apply at partnership level.--For purposes of subsection (a), a partnership shall not be treated as an individual, but the interest in a partnership of a debtor who is an individual shall be taken into account under this section in the same manner as any other interest of the debtor.

(c) Computation and payment of tax; basic standard deduction.--

Appendix E

(1) Computation and payment of tax.--Except as otherwise provided in this section, the taxable income of the estate shall be computed in the same manner as for an individual. The tax shall be computed on such taxable income and shall be paid by the trustee.

(2) Tax rates.--The tax on the taxable income of the estate shall be determined under subsection (d) of section 1.

(3) Basic standard deduction.--In the case of an estate which does not itemize deductions, the basic standard deduction for the estate for the taxable year shall be the same as for a married individual filing a separate return for such year.

(d) Taxable year of debtors.--

(1) General rule.--Except as provided in paragraph (2), the taxable year of the debtor shall be determined without regard to the case under Title 11 of the United States Code to which this section applies.

(2) Election to terminate debtor's year when case commences.--

(A) In general.--Notwithstanding section 442, the debtor may (without the approval of the Secre-

tary) elect to treat the debtor's taxable year which includes the commencement date as 2 taxable years--

(i) the first of which ends on the day before the commencement date, and

(ii) the second of which begins on the commencement date.

(B) Spouse may join in election.--In the case of a married individual (within the meaning of section 7703), the spouse may elect to have the debtor's election under subparagraph (A) also apply to the spouse, but only if the debtor and the spouse file a joint return for the taxable year referred to in subparagraph (A)(i).

(C) No election where debtor has no assets.--No election may be made under subparagraph (A) by a debtor who has no assets other than property which the debtor may treat as exempt property under section 522 of Title 11 of the United States Code.

(D) Time for making election.--An election under subparagraph (A) or (B) may be made only on or before the due date for filing the return for the taxable year referred to in subparagraph (A)(i). Any such election, once made, shall be irrevocable.

(E) Returns.--A return shall be made for each of the taxable years specified in subparagraph (A).

(F) Annualization.--For purposes of subsections (b), (c), and (d) of section 443, a return filed for either of the taxable years referred to in subparagraph (A) shall be treated as a return made under paragraph (1) of subsection (a) of section 443.

(3) Commencement date defined.--For purposes of this subsection, the term "commencement date" means the day on which the case under Title 11 of the United States Code to which this section applies commences.

(e) Treatment of income, deductions, and credits.--

(1) Estate's share of debtor's income.--The gross income of the estate for each taxable year shall include the gross income of the debtor to which the estate is entitled under Title 11 of the United States Code. The preceding sentence shall not apply to any amount received or accrued by the debtor before the commencement date (as defined in subsection (d)(3)).

(2) Debtor's share of debtor's income.--The gross income of the debtor for any taxable year shall

not include any item to the extent that such item is included in the gross income of the estate by reason of paragraph (1).

(3) Rule for making determinations with respect to deductions, credits, and employment taxes.--Except as otherwise provided in this section, the determination of whether or not any amount paid or incurred by the estate--

(A) is allowable as a deduction or credit under this chapter, or

(B) is wages for purposes of subtitle C,

shall be made as if the amount were paid or incurred by the debtor and as if the debtor were still engaged in the trades and businesses, and in the activities, the debtor was engaged in before the commencement of the case.

(f) Treatment of transfers between debtor and estate.--

(1) Transfer to estate not treated as disposition.--A transfer (other than by sale or exchange) of an asset from the debtor to the estate shall not be treated as a disposition for purposes of any provision of this title assigning tax consequences to a disposition, and the estate shall be treated as

the debtor would be treated with respect to such asset.

(2) Transfer from estate to debtor not treated as disposition.--In the case of a termination of the estate, a transfer (other than by sale or exchange) of an asset from the estate to the debtor shall not be treated as a disposition for purposes of any provision of this title assigning tax consequences to a disposition, and the debtor shall be treated as the estate would be treated with respect to such asset.

(g) Estate succeeds to tax attributes of debtor.--The estate shall succeed to and take into account the following items (determined as of the first day of the debtor's taxable year in which the case commences) of the debtor--

(1) Net operating loss carryovers.--The net operating loss carryovers determined under section 172.

(2) Charitable contributions carryovers.--The carryover of excess charitable contributions determined under section 170(d)(1).

(3) Recovery of tax benefit items.--Any amount to which section 111 (relating to recovery of tax benefit items) applies.

(4) Credit carryovers, etc.--The carryovers of any credit, and all other items which, but for the commencement of the case, would be required to be taken into account by the debtor with respect to any credit.

(5) Capital loss carryovers.--The capital loss carryover determined under section 1212.

(6) Basis, holding period, and character of assets.--In the case of any asset acquired (other than by sale or exchange) by the estate from the debtor, the basis, holding period, and character it had in the hands of the debtor.

(7) Method of accounting.--The method of accounting used by the debtor.

(8) Other attributes.--Other tax attributes of the debtor, to the extent provided in regulations prescribed by the Secretary as necessary or appropriate to carry out the purposes of this section.

(h) Administration, liquidation, and reorganization expenses; carryovers and carrybacks of certain excess expenses.--

(1) Administration, liquidation, and reorganization expenses.--Any administrative expense allowed under section 503 of Title 11 of the United States Code, and any fee or charge assessed

against the estate under chapter 123 of Title 28 of the United States Code, to the extent not disallowed under any other provision of this title, shall be allowed as a deduction.

(2) Carryback and carryover of excess administrative costs, etc., to estate taxable years.--

(A) Deduction allowed.--There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (i) the administrative expense carryovers to such year, plus (ii) the administrative expense carrybacks to such year.

(B) Administrative expense loss, etc.--If a net operating loss would be created or increased for any estate taxable year if section 172(c) were applied without the modification contained in paragraph (4) of section 172(d), then the amount of the net operating loss so created (or the amount of the increase in the net operating loss) shall be an administrative expense loss for such taxable year which shall be an administrative expense carryback to each of the 3 preceding taxable years and an administrative expense carryover to each of the 7 succeeding taxable years.

(C) Determination of amount carried to each taxable year.--The portion of any administrative expense loss which may be carried to any other taxable year shall be determined under section

172(b)(2), except that for each taxable year the computation under section 172(b)(2) with respect to the net operating loss shall be made before the computation under this paragraph.

(D) Administrative expense deductions allowed only to estate.--The deductions allowable under this chapter solely by reason of paragraph (1), and the deduction provided by subparagraph (A) of this paragraph, shall be allowable only to the estate.

(i) Debtor succeeds to tax attributes of estate.--In the case of a termination of an estate, the debtor shall succeed to and take into account the items referred to in paragraphs (1), (2), (3), (4), (5), and (6) of subsection (g) in a manner similar to that provided in such paragraphs (but taking into account that the transfer is from the estate to the debtor instead of from the debtor to the estate). In addition, the debtor shall succeed to and take into account the other tax attributes of the estate, to the extent provided in regulations prescribed by the Secretary as necessary or appropriate to carry out the purposes of this section.

(j) Other special rules.--

(1) Change of accounting period without approval.--Notwithstanding section 442, the estate may

change its annual accounting period one time without the approval of the Secretary.

(2) Treatment of certain carrybacks.--

(A) Carrybacks from estate.--If any carryback year of the estate is a taxable year before the estate's first taxable year, the carryback to such carryback year shall be taken into account for the debtor's taxable year corresponding to the carryback year.

(B) Carrybacks from debtor's activities.--The debtor may not carry back to a taxable year before the debtor's taxable year in which the case commences any carryback from a taxable year ending after the case commences.

(C) Carryback and carryback year defined.--For purposes of this paragraph--

(i) Carryback.--The term "carryback" means a net operating loss carryback under section 172 or a carryback of any credit provided by part IV of subchapter A.

(ii) Carryback year.--The term "carryback year" means the taxable year to which a carryback is carried.

Appendix E

26 U.S.C. § 1399: No separate taxable entities for partnerships, corporations, etc.

Except in any case to which section 1398 applies, no separate taxable entity shall result from the commencement of a case under Title 11 of the United States Code.

S. 260, 106th Cong. § 3 (1999): CONTENTS OF PLAN – AMEND

Section 1222(a)(2) of title 11, United States Code, is amended to read as follows:

'(2) provide for the full payment, in deferred cash payments, of all claims entitled to priority under section 507, unless –

'(A) the claim is a claim owed to a governmental unit that arises as a result of the sale, transfer, exchange, or other disposition of any farm asset used in the debtor's farming operation, in which case the claim shall be treated as an unsecured claim that is not entitled to priority under section 507, but the debt shall be treated in such manner only if the debtor receives a discharge;