

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF GEORGIA
ATHENS DIVISION

In the Matter of: : Chapter 7
: :
GEORGE LARRY HAMRICK :
LINDA HESTER HAMRICK, :
: :
Debtors : Case No. 98-31314 RFH
: :
: :
GEORGE LARRY HAMRICK :
LINDA HESTER HAMRICK, :
: :
Plaintiffs :
: :
: :
vs. :
: :
: :
STATE OF GEORGIA :
DEPARTMENT OF REVENUE, :
: :
Defendant : Adversary Proceeding
: No. 99-3005

BEFORE

ROBERT F. HERSHNER, JR.
CHIEF UNITED STATES BANKRUPTCY JUDGE

COUNSEL:

For Plaintiffs: ANNE M. BERNSTEIN
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MEMORANDUM OPINION

The State of Georgia, Department of Revenue, Defendant, filed on June 22, 2000, a motion for summary judgment. George Larry Hamrick and Linda Hester Hamrick, Plaintiffs, filed their response on July 19, 2000. The Court, having considered the record, Plaintiffs' depositions, Defendant's affidavit, Defendant's statement of uncontested facts, and the arguments of counsel, now publishes this memorandum opinion.

The following facts are not in dispute.¹ Plaintiffs have failed to pay in full their federal income tax obligations since the 1970s. Plaintiffs filed four bankruptcy petitions during the 1990s in response to collection actions by the Internal Revenue Service. Plaintiffs filed a petition under Chapter 7 of the Bankruptcy Code in 1991. Plaintiffs received a discharge in bankruptcy in July of 1991.

Plaintiffs also have failed to pay some of their state income tax obligations. Plaintiffs' 1993 state income tax return was due on April 15, 1994. Plaintiffs filed an accurate return, but failed to pay in full their tax obligation. Plaintiffs currently owe \$913.91 on their 1993 state tax obligation.

¹ Plaintiffs have presented no facts in opposition to Defendant's motion for summary judgment.

Plaintiffs' 1994 state income tax return was due on April 15, 1995. Plaintiffs filed an accurate return, but failed to pay in full their tax obligation. Plaintiffs currently owe \$7,274.17 on their 1994 state tax obligation.

Plaintiffs sought bankruptcy relief a second time by filing a petition under Chapter 13 of the Bankruptcy Code on June 26, 1996. Plaintiffs' Chapter 13 case was dismissed on April 22, 1997. Defendant was stayed from collecting Plaintiffs' tax obligations during the pendency of this Chapter 13 bankruptcy case.

Plaintiffs sought bankruptcy relief a third time by filing a petition under Chapter 13 of the Bankruptcy Code on August 14, 1997. Plaintiffs' Chapter 13 case was dismissed on June 26, 1998. Defendant was stayed from collecting Plaintiffs' tax obligations during the pendency of this Chapter 13 bankruptcy case.

Plaintiffs sought bankruptcy relief a fourth time by filing a petition under Chapter 7 of the Bankruptcy Code on October 8, 1998. This is Plaintiffs' pending bankruptcy case.

Plaintiffs filed on January 28, 1999, an amended complaint to determine the dischargeability of their state tax obligations for 1994 and prior years. Defendant filed a response on February 9, 1999.

Defendant concedes that Plaintiffs' state tax obligations for 1991 and prior years are dischargeable in

bankruptcy. Plaintiffs do not owe any state tax obligations for 1992.² Defendant's memorandum of law, p. 1 (filed June 22, 2000).

Plaintiffs and Defendant dispute the dischargeability of Plaintiffs' state tax obligations for 1993 and 1994. Section 523(a)(1)(A) and (7) of the Bankruptcy Code³ provides as follows:

§ 523. Exceptions to discharge

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt-

(1) for a tax or a customs duty-

(A) of the kind and for the periods specified in section 507(a)(2) or 507(a)(8) of this title, whether or not a claim for such tax was filed or allowed;

. . . .

(7) to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a tax penalty-

(A) relating to a tax of a kind not specified in paragraph (1) of this subsection; or

² Plaintiffs owe state tax obligations for 1987, 1988, 1989, and 1991. Defendant's Statement of Material Facts to Which There Exists No Issue, p. 2 (filed June 22, 2000).

³ 11 U.S.C.A. § 523(a)(1)(A), (7) (West 1993 & Supp. 2000).

(B) imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition;

11 U.S.C.A. § 523(a)(1)(A), (7) (West 1993 & Supp. 2000).

Section 507(a)(8)(A)(i) and (G) of the Bankruptcy Code⁴ provides as follows:

§ 507. Priorities

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

. . . .

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

(A) a tax on or measured by income or gross receipts-

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

. . . .

. . . .

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

11 U.S.C.A. § 507(a)(8)(A)(i), (G) (West Supp. 2000).

⁴ 11 U.S.C.A. § 507(a)(8)(A)(i), (G) (West Supp. 2000).

In Wood v. United States (In re Wood),⁵ the Eleventh Circuit Court of Appeals stated:

Sections 523(a)(1) and 507(a)[8](A) reflect a two-fold government interest. First, the Government has an interest in decreasing the number of delinquent income tax filers, and the sections encourage a prompt investigation of such filers. Presumably, the vigorous pursuit of delinquent filers, combined with substantial civil and criminal penalties, discourages the late filing of returns. Second, and perhaps more importantly, the Government has an interest in maximizing the period allowed for auditing returns and collecting taxes. In establishing the priority and discharge provisions of the Code, Congress recognized the IRS' status as an involuntary creditor and need to have a reasonable period of time within which to collect taxes. The three-year time period embodied in section 507(a)[8](A) reflects the "reasonable" period of time the IRS is allotted to audit the return and collect taxes.

866 F.2d at 1371.

Under section 523(a)(1), a claim for income taxes is entitled to priority and is nondischargeable if the due date, including extensions, of the tax return is less than three years prior to the date of the bankruptcy filing.

Prepetition interest is nondischargeable if the underlying tax is nondischargeable. Prepetition interest is entitled to the same priority as the underlying tax. Bates v. United States (In re Bates), 974 F.2d 1234, 1237 (10th Cir. 1992); Jones v. United States (In re Garcia), 955 F.2d 16 (5th

⁵ 866 F.2d 1367 (11th Cir. 1989).

Cir. 1992); In re Larson, 862 F.2d 112, 119 (7th Cir. 1988).

Plaintiffs filed their current Chapter 7 bankruptcy case on October 8, 1998. Plaintiffs' bankruptcy case was filed more than three years after the due dates for their state tax returns for 1993 and 1994. Plaintiffs filed two Chapter 13 bankruptcy cases during the three-year period. Defendant contends the three-year priority period of section 523(a)(1) should be tolled during the pendency of Plaintiffs' Chapter 13 bankruptcy cases. If the three-year priority period is tolled, Plaintiffs' 1993 and 1994 tax obligations are nondischargeable.

The Eleventh Circuit has held that the three-year priority period may be tolled, where appropriate.

In Morgan v. United States of America (In re Morgan),⁶ the Eleventh Circuit stated:

As a result, we conclude that 11 U.S.C. § 105(a) is broad enough to permit a bankruptcy court, exercising its equitable powers, to toll the three-year priority period, where appropriate, during the pendency of a debtor's prior bankruptcy proceeding.

"Interpreting [the Bankruptcy Code] literally would allow a debtor to create an 'impenetrable refuge' by filing a bankruptcy petition, waiting for [§ 507(a)(8)'s] priority periods to expire, and then dismissing the case and refile shortly thereafter." In re West, 5 F.3d 423, 426 (9th Cir. 1993) (citing In re Florence, 115 B.R. 109, 111 (Bankr. S.D. Ohio 1990)). Due to congressional intent, which

⁶ 182 F.3d 775 (11th Cir. 1999).

favors allowing the government sufficient time to collect taxes, and the fear that taxpayers may abuse the bankruptcy process in order to avoid paying taxes, we hold that the equities will generally favor the government in cases such as this. See In re Waugh, 109 F.3d at 492 ("Congress realized that '[a]n open-ended dischargeability policy would provide an opportunity for tax evasion through bankruptcy, by permitting discharge of tax debts before a taxing authority has an opportunity to collect any taxes due.'" (quoting H.R. Rep. No. 95-595, at 190 (1977), reprinted in 1978 U.S.C.C.A.N. 5787, 5963, 6150)). There may be factual scenarios, however, in which the equities favor the taxpayer.

182 F.3d at 779-80.

The circuit court also stated:

8. While the record has not been developed fully, there does not appear to be any evidence of dilatory conduct or bad faith on the part of the Morgans. We do not set forth the equitable considerations regarding § 105(a), but we reject the notion espoused in In re Gore, 182 B.R. 293, 316 (Bankr. S.D. Ala. 1995) that a finding of dilatory conduct or bad faith is necessary to find the equities in favor of the government.

Furthermore, we do not address the question of whether there may be a difference between the actual tax liability, penalties or interest for the purpose of considering the equities.

182 F.3d at 780 n.8.

Plaintiffs urge the Court not to apply equitable tolling to the three-year priority period. Plaintiffs argue that the bankruptcy court's equitable powers are quite limited and must only be exercised within the confines of the Bankruptcy Code. Plaintiffs argue that the plain language of

the Bankruptcy Code does not provide for equitable tolling of the three-year priority period. Plaintiffs essentially argue that the decision of the Eleventh Circuit in In re Morgan was erroneous. See Plaintiffs' Memorandum of Law In Opposition to Defendant's Motion for Summary Judgment (filed July 19, 2000).

This Court is bound by In re Morgan and will apply that case law to the facts in the case at bar.

Plaintiffs, in their depositions, testified that Defendant had not picked on Plaintiffs or treated Plaintiffs unfairly; Defendant had done nothing to contribute to Plaintiffs' tax problems; Defendant had not interfered with Plaintiffs' employment; and Defendant had not attempted to frustrate the confirmation of Plaintiffs' Chapter 13 plans or Plaintiffs' ability to carry out their Chapter 13 plans.

Plaintiffs further testified in their depositions that their state tax problems were not "Defendant's fault." Plaintiffs testified that they do not dispute the amount of their state tax obligations. Plaintiffs testified that their bankruptcy filings were in response to the collection actions of the IRS. Plaintiffs testified that they have had no disputes with Defendant's collection actions. Plaintiffs testified that Defendant worked with them when Plaintiffs attempted to repay their state tax obligations.

The Court is persuaded that the three-year priority period should be equitably tolled. Plaintiffs have presented

no facts in opposition to Defendant's motion for summary judgment or to support their position that equitable tolling should not apply. As noted in In re Morgan, the equities generally favor the government. Plaintiffs have not demonstrated facts sufficient to show that the equities favor them.

Plaintiffs argue that section 523(b) of the Bankruptcy Code⁷ requires that the three-year priority period be calculated by using the filing date of their most recent bankruptcy case. Under section 523(b), tax obligations that were nondischargeable in a prior bankruptcy case may be dischargeable in a subsequent bankruptcy case. The dischargeability of the tax obligations in the second

⁷ 11 U.S.C.A. § 523(b) (West Supp. 2000). This section provides as follows:

§ 523. Exceptions to discharge

. . . .

(b) Notwithstanding subsection (a) of this section, a debt that was excepted from discharge under subsection (a)(1), (a)(3), or (a)(8) of this section, under section 17a(1), 17a(3), or 17a(5) of the Bankruptcy Act, under section 439A of the Higher Education Act of 1965, or under section 733(g) of the Public Health Service Act in a prior case concerning the debtor under this title, or under the Bankruptcy Act, is dischargeable in a case under this title unless, by the terms of subsection (a) of this section, such debt is not dischargeable in the case under this title.

11 U.S.C.A. § 523(b) (West Supp. 2000).

bankruptcy case will depend upon whether they fall within any applicable exceptions of section 523(a). 4 Collier on Bankruptcy ¶ 523.25 (15th ed. rev. 2000).

In the case at bar, Plaintiffs' tax obligations for 1993 and 1994 are nondischargeable because the three-year priority period had not expired when Plaintiffs' current bankruptcy case was filed.⁸ The Court is not persuaded that section 523(b) makes these obligations dischargeable.

Finally, Plaintiffs argue that equitable tolling is inconsistent with section 349(a) of the Bankruptcy Code,⁹ which provides, in part, that dismissal of a case does not prejudice the debtor with regard to the filing of a subsequent bankruptcy case, except as provided in section 109(g) of the Bankruptcy Code.¹⁰

The Court is not persuaded by Plaintiffs' argument because the Court's decision is made by applying the applicable law to Plaintiffs' presently pending bankruptcy case. Plaintiffs' prior filings have in no way prejudiced their rights in the pending case.

An order in accordance with this memorandum opinion will be entered this date.

⁸ Equitable tolling being applicable to years 1993 and 1994.

⁹ 11 U.S.C.A. § 349(a) (West Supp. 2000).

¹⁰ 11 U.S.C.A. § 109(g) (West 1993).

DATED the 8th day of December, 2000.

ROBERT F. HERSHNER, JR.
Chief Judge
United States Bankruptcy Court