NATIONAL BANKRUPTCY CONFERENCE
A Voluntary Organization Composed of Persons Interested in the Improvement of the Bankruptcy Code and Its Administration

April 15, 2015

Ms. Susan Jensen
Committee on the Judiciary
House of Representatives
Washington, D.C. 20515

Re: Recommendation Concerning the ABA Section of Taxation Proposal for a Technical Correction to the Hanging Paragraph in 11 U.S. C. § 523(a)

Dear Susan:

The National Bankruptcy Conference (NBC) is a voluntary, non-partisan, not-for-profit organization composed of about 60 of the nation's leading bankruptcy judges, professors and practitioners. It has provided advice to Congress on bankruptcy legislation for over 75 years. I enclose a Fact Sheet, which provides further information about the NBC.

The NBC, on the recommendation of its Individual Debtor Committee, has reviewed the ABA Section of Taxation proposal for a technical correction to the hanging paragraph in 11 U.S.C. § 523(a). The NBC supports the proposal but suggests an additional technical correction to the hanging paragraph.

1. Overview of Case Law.

Before BAPCPA, the term "return" was not defined for § 523(a) purposes, and courts typically applied the four-part *Beard* test to determine whether a document qualifies as a tax return. *Beard v. Commissioner*, 82 T.C. 766, 777 (1984), *aff'd*, 793 F.2d 139 (6th Cir. 1986). To qualify as a return under this test, the document must: (1) purport to be a return; (2) be executed under penalty of perjury; (3) contain sufficient data to allow calculation of tax; and (4) represent an honest and reasonable attempt to satisfy the requirements of the tax law.

A definition of "return" was added to § 523(a) by BAPCPA in an unnumbered, hanging paragraph. It provides: "For purposes of this subsection, the term 'return' means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements)." The provision also specifies that a return filed by the IRS with the cooperation of the debtor under § 6020(a) of the Internal Revenue Code is a "return," but a return filed by the IRS without the debtor's cooperation under § 6020(b) is not.

Rejecting the continuing application of the *Beard* test, the Fifth Circuit in *In re McCoy*, 666 F.3d 924 (5th Cir. 2012), held that a filing deadline is an "applicable filing requirement," and, therefore, a late-filed return can never qualify as a "return" unless it falls under the § 6020(a) exception.

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The *McCoy* opinion was followed by the Tenth Circuit in *Mallo v. IRS (In re Mallo)*, 774 F.3d 1313 (10th Cir. 2014). The *Mallo* court rejected the arguments put forth by the debtors that: 1) there would be no reason for Congress to have specified that a return filed under 6020(b) is not a "return" for dischargeability purposes if no late-filed return falls under that definition; 2) the exception to discharge set forth in § 523(a)(1)(B)(ii), which applies to returns that were "filed or given after the date on which such return … was last due, … and after two years before the date of the filing of the petition," would be rendered meaningless by a finding that no late-filed return is dischargeable; 3) Congress could not have intended to place complete control in the hands of the IRS to determine whether a late-filed return is dischargeable by making its discretionary application of § 6020(a) decisive.

The First Circuit in *In re Fahey*, 779 F.3d 1 (1st Cir. 2015), found that the requirement under Massachusetts tax law that tax returns "shall be made on or before the fifteenth day of the fourth month," was mandatory. The court found that this time for filing requirement under state law was an "applicable filing requirement," thereby rendering a return filed outside that time nondischargeable unless filed under § 6020(a). Finding no ambiguity to justify going beyond the plain language of the hanging paragraph, the court rejected arguments of statutory construction raised by the debtors, their amici, and the dissenting opinion.

The dissenting opinion disputed the majority's dismissal of the significance of the pre-BAPCPA *Beard* test, noting that the hanging paragraph answered in the affirmative the previously debated question of whether a return filed under § 6020(a) was a "return." The opinion also identified the following flaws in the majority opinion:

- Massachusetts tax law contemplates tax assessments based on late-filed returns, therefore, it is inaccurate to say that under applicable state law late-filed returns are not "returns."
- The two-year rule set forth in § 523(a)(1)(B)(ii), which pre-dates BAPCPA, contemplates discharge of taxes based on late-filed returns and was not amended when the hanging paragraph was added.
- The majority's explanation that section 523(a)(1)(B)(ii) is still meaningful because it applies to returns filed under § 6020(a) is illogical because, a) the hanging paragraph permits late-filed returns "including," and therefore not limited to, those filed under § 6020(a), and, b) it renders the exclusion of those returns filed under § 6020(b) redundant.
- Permitting only late-filed returns under § 6020(a) absurdly rewards the tax debtor who sits on his hands and awaits IRS invitation to complete the return while punishing the debtor who voluntarily files his own return even one day late.

2. Position of the Internal Revenue Service.

The IRS filed an amicus brief in the First Circuit consolidated cases supporting the debtors' argument that the phrase "applicable filing requirements" applies to the substance of the return rather than the timing of the filing. As long as the debtor files a return that substantively conforms to state law requirements, it is a "return" for bankruptcy purposes. As noted in the IRS brief, this position adheres to the Eighth Circuit decision in *Colsen v. United States (In re Colsen)*, 446 F.3d 836 (8th Cir. 2006), where the court examined whether the purported return constituted an honest and reasonable attempt to comply with the tax laws as discerned from the face of the return, without regard to the timing of filing. The IRS has

consistently endorsed a middle view that tax liability based on returns filed prior to independent assessment by the tax authority under IRC section 6020(b) are dischargeable based on the pre-BAPCPA *Beard* test.

In its amicus brief, the IRS argued that "[t]he BAP's analysis appropriately conditions the dischargeability of a debt on whether debtors' tax forms are filed before or after the taxing authority has made its own assessment of the tax." With respect to the *McCoy* rule, the IRS states: "It produces overly harsh results, allows general statutory language to govern over more specific provisions, and renders other statutory language meaningless, contrary to the cardinal rule of statutory construction that no part of a statute should be rendered superfluous." The IRS maintains that to be a "return," the tax return must inform the assessment process and that, if it is filed after the IRS has does its own assessment without the cooperation of the debtor, the debtor's efforts are rendered essentially meaningless and the return is not a "return," even where the debtor's return states an amount different from that reached by the IRS.

The position of the IRS in its First Circuit amicus brief is consistent with the Memorandum from the IRS Office of Chief Legal Counsel, Litigating Position Regarding the Dischargeability in Bankruptcy of Tax Liabilities Reported on Late Filed Returns and Returns Filed After Assessment, Sept. 10. 2010, available at: http://www.irs.gov/pub/irs-ccdm/cc_2010_016.pdf.

3. Proposal of the ABA Section of Taxation.

The ABA Section of Taxation contends that the hanging paragraph appears to conflict with § 523(a)(l)(B)(ii), which allows for the discharge of taxes on late-filed returns as long as two years have passed between the tax-return-filing date and the bankruptcy-petition-filing date. If only timely returns are dischargeable based on the application of the hanging paragraph, then § 523 (a)(l)(B)(ii) is rendered meaningless. This is a reasonable construction of the statutory language. It is also consistent with the position taken by the Internal Revenue Service on this issue.

The report of the ABA Section of Taxation reviews the legislative history for the BAPCPA amendment and concludes that there was nothing in the legislative history that suggests Congress intended such a "dramatic change" in the application of § 523(a)(1)(B)(ii). The comprehensive review of the legislative history by the ABA Section of Taxation supports this conclusion. While the purpose of the amendment is not clear from the legislative history, it is likely that the hanging paragraph was added to address the previously unsettled question of whether a return filed under § 6020(a) is a return for purposes § 523(a)(l)(B)(ii), as suggested in the dissenting opinion in the First Circuit opinion.

The ABA Section of Taxation recommends that the first sentence of the hanging paragraph be amended to read as follows (new material in *italics*):

> For purposes of this subsection, the term "return" means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements *other than timeliness*).

By excluding timeliness from the applicable filing requirements, the proposed amendment would effectively overrule *McCoy* and its progeny.

In addition to supporting this proposal, the NBC recommends as an additional technical correction that the hanging paragraph should be designated as section 523(f), and that the opening phrase be changed to "For purposes of subsection (a) of this section" [instead of "For purposes of this subsection"].

With best regards.

Sincerely,

/s/ Richard Levin

Richard Levin
Chair

National Bankruptcy Conference

A non-profit, non-partisan, self-supporting organization of approximately sixty lawyers, law professors and bankruptcy judges who are leading scholars and practitioners in the field of bankruptcy law. Its primary purpose is to advise Congress on the operation of bankruptcy and related laws and any proposed changes to those laws.

History. The National Bankruptcy Conference (NBC) was formed from a nucleus of the nation's leading bankruptcy scholars and practitioners, who gathered informally in the 1930's at the request of Congress to assist in the drafting of major Depression-era bankruptcy law amendments, ultimately resulting in the Chandler Act of 1938. The NBC was formalized in the 1940's and has been a resource to Congress on every significant piece of bankruptcy legislation since that time. Members of the NBC formed the core of the Commission on the Bankruptcy Laws of the United States, which in 1973 proposed the overhaul of our bankruptcy laws that led to enactment of the Bankruptcy Code in 1978, and were heavily involved in the work of the National Bankruptcy Review Commission (NBRC), whose 1997 report initiated the process that led to significant amendments to the Bankruptcy Code in 2005.

Current Members. Membership in the NBC is by invitation only. Among the NBC's 60 active members are leading bankruptcy scholars at major law schools, as well as current and former judges from eleven different judicial districts and practitioners from leading law firms throughout the country who have been involved in most of the major corporate reorganization cases of the last three decades. The NBC includes leading consumer bankruptcy experts and experts on commercial, employment, pension, mass tort and tax related bankruptcy issues. It also includes former members of the congressional staff who participated in drafting the Bankruptcy Code as originally passed in 1978 and former members and staff of the NBRC. The current members of the NBC and their affiliations are set forth on the second page of this fact sheet.

Policy Positions. The Conference regularly takes substantive positions on issues implicating bankruptcy law and policy. It does not, however, take positions on behalf of any organization or interest group. Instead, the NBC seeks to reach a consensus of its members - who represent a broad spectrum of political and economic perspectives - based on their knowledge and experience as practitioners, judges and scholars. The Conference's positions are considered in light of the stated goals of our bankruptcy system: debtor rehabilitation, equal treatment of similarly situated creditors, preservation of jobs, prevention of fraud and abuse, and economical insolvency administration. Conferees are always mindful of their mutual pledge to "leave their clients at the door" when they participate in the deliberations of the Conference.

Technical and Advisory Services to Congress. To facilitate the work of Congress, the NBC offers members of Congress, Congressional Committees and their staffs the services of its Conferees as non-partisan technical advisors. These services are offered without regard to any substantive positions the NBC may take on matters of bankruptcy law and policy.

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