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In This Issue

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First Lien/Second Lien Issues in Bankruptcy

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(This article will be published in two parts in consecutive issues of the Adviser. This First Part discusses many of the common provisions in first lien/second lien agreements including the extent of the priority and the obligations entitled to priority, predefault payments, blockage and the noninterference principle, lien enforcement, covenants and a take out right. It then discusses the general impact of these provisions in bankruptcy cases and the conflict between the first lien/second lien provisions and some important bankruptcy policies. The Second Part will discuss the application of first lien/second lien provisions in various bankruptcy contexts and the relationship of those provisions to various bankruptcy issues such as DIP lending, adequate protection, claim and lien validity, plan support provisions, waivers of bankruptcy remedies, and enforcement of first lien remedies. There is an extended discussion of enforcement issues which concludes that the various enforcement remedies are not terribly well thought out and may not be effective.)

Second lien financing has become somewhat the rage with investors, hedge funds, distress investors, and bottom fishers. By definition, the alternative to a second lien is not a first lien because the borrower either already has first lien financing insufficient to its needs, or wants to borrow more than a first lien lender will risk. Instead, second lien financing contemplates a more highly leveraged capital structure, with higher interest rates as risk increases. An alternative to second lien financing is usually some version of unsecured lending with tight covenants and, possibly, a negative pledge and/or "equal and ratable" lien provision. What makes second lien lending attractive is

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113, 121 (Bankr. S.D.N.Y. 2007), aff'd, 386 B.R. 428 (S.D.N.Y. 2008), aff'd, 318 F. App'x 36 (2d Cir. 2009).

8. This is part of a larger issue of whether loan covenants (as opposed to the obligation to pay back the loan and perhaps the loan's financial terms), are enforceable in a bankruptcy case. A variant of that issue is whether intercreditor covenants (such as a "promise" by one group of lenders to get consent from another group before taking certain actions) are effective in bankruptcy; and what remedy if any the creditor group which must consent has if its consent is not obtained. A recent decision in the *Chrysler* case enforced provisions of loan agreements relating to deposition of collateral against dissenting members of the lending group. Ind. State Police Pension Trust v. Chrysler LLC (In re Chrysler LLC), 576 F.3d 108, 119-20 (2d Cir.), judgment vacated, 130 S. Ct. 1015, 175 L. Ed. 2d 614 (2009). Still another issue is whether, as part of a cramdown of first lien debt under section 1129(b)(2), the debtor will be required to perform covenants other than those relating to the pure cramdown issues of amount and timing of payments, and interest. These issues are beyond the scope of this article although analogous remedy issues are discussed below.

9. In cases where the value of the collateral is less than or equal to the first lien debt (or, perhaps, very slightly more), the second lien lenders are analytically unsecured creditors. Sometimes, provisions in first lien/second lien documents require the second lien lenders not to waive their second liens and thereby remain bound by the waivers in their agreements with the first lien lenders. However, unless carefully drafted, second lien lenders may still be bound by their agreements even if they waive their liens. And, the second lien lenders will be bound if there is also a debt subordination.

10. TCI 2 Holdings, 428 B.R. at 140-41. This case also reinforces the earlier discussion about the difficulties in drafting documents which will clearly protect first lien lenders in new and unexpected circumstances.

11. See Travelers Cas. & Sur. Co. of Am. v. Pac. Gas & Elec. Co., 549 U.S. 443, 127 S. Ct. 1199, 167 L. Ed. 2d 178 (2007); Official Comm. of Unsecured Creditors v. Dow Corning Corp. (In re Dow Corning Corp.), 456 F.3d 668 (6th Cir. 2006); In re Wright, 492 F.3d 829, 832 (7th Cir. 2007) (state law is the "default provision" for creditor claims).

12. In addition, second lien lenders usually do not serve on unsecured creditors' committees, even if their debt is largely under water. In some situations, this may effectively eliminate the largest unsecured creditors (*i.e.*, second lien lenders whose debt is wholly or largely unsecured) from the committee and leave the committee with members having a much smaller economic stake in the case.

13. See, e.g., In re Erickson Ret. Communities, LLC, 425 B.R. 309, 314 (Bankr. N.D. Tex. 2010) (enforcing waiver by subordinated creditors of the right to seek an examiner).

14. See, e.g., Official Comm. of Unsecured Creditors of Applied Theory Corp. v. Halifax Fund L.P. (In re Applied Theory Corp.), 493 F.3d 82, 87 (2d Cir. 2007) (committee cannot bring equitable subordination action without court authorization).

15. See, e.g., Guidelines for Financing Requests, General Order M-274 (Bankr. S.D.N.Y.); Local Rules of Bankruptcy Practice and Procedure of the United States Bankruptcy Court for the District of Delaware, Rule 4001-2. These attempts have, at best, had limited impact.

WHAT IS A TAX RETURN?

Morgan D. King*

BAPCPA added new language to the Bankruptcy Code in 2005 that clarifies an important issue in tax discharge cases, *or not*

Language added to the Bankruptcy Code by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA)[1] addresses the circumstances under which a debtor's tax return may fail to satisfy what is commonly referred to as the "two-year rule."[2] At the urging of the IRS, several bankruptcy courts recently carved an alarming path in interpretation of the new text. The decisions turned the two-year rule upside down. However, in an even more recent, surprising and unusual move, the IRS reversed itself on this issue in the middle of a case pending in the Northern District of Illinois. The new IRS position flipped the rule right-side up again. It appears the decisions in the three prior cases were incorrect.

The role of tax returns in bankruptcy

Tax returns play several roles in bankruptcy cases, particularly since BAPCPA became effective in 2005. Among other things, BAPCPA added some wrinkles to the fundamental question, what constitutes a tax return for bankruptcy purposes? We look carefully at that question here, because if the reasoning followed in several recent cases defining a "tax return" represents an emerging trend, there is a drastic limitation ahead on debtors' ability to discharge stale tax liabilities in bankruptcy. This article explores the reasons why those cases, and their definition of a "tax return," are in error

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and the possibility that the IRS has changed its position on the issue.

Prior to BAPCPA, the rules governing dischargeability of income taxes in Chapter 7 could be stated with a simple checklist of five rules. Income taxes were dischargeable if: 1) the taxpayer filed his or her return more than two years before the bankruptcy;[3] 2) the most recent due date for filing the return was over three years old;[4] 3) the tax was assessed more than 240 days prior to the bankruptcy;[5] 4) the tax return was not fraudulent;[6] and, 5) the taxpayer had not attempted to evade or defeat the tax.[7] You could simply go down the checklist and if all five were in the affirmative, the taxes were dischargeable.

Discharge in Chapter 13 was even simpler, due to the "super-discharge" of income taxes. To be treated as a general unsecured dischargeable tax in Chapter 13, only the three-year rule and the 240-day rule had to be satisfied.

Several of the wrinkles BAPCPA added are germane to whether a delinquent income tax may be discharged. For example, a major BAPCPA change eliminated much of the "super-discharge" for income taxes in Chapter 13 cases, making the rules for discharge in Chapter 13, for all practical purposes, virtually the same as for Chapter 7.[8] This nullified an opportunity for many delinquent taxpayers to come in out of the cold and become regular taxpayers again,[9] and eliminated an attractive remedy that bankruptcy attorneys could employ to help many of their desperate delinquent tax clients.

One of the rules BAPCPA changed was the two-year rule

Pre-BAPCPA, in Chapter 7 cases the rule was fairly simple: to discharge an income tax liability, the return had to have been a "1040" filed by the taxpayer,[10] more than two years before filing bankruptcy.[11] Even if the return was not timely filed, any related delinquent tax was not excepted from discharge merely because the return was untimely. If the return was filed more than two years before the bankruptcy petition, with a few exceptions, it satisfied the rule.[12] The notable exceptions were frivolous tax returns, or returns filed by the debtor after the IRS had both filed a substitute for return and assessed the tax.[13] Even returns filed after the IRS had filed a "dummy" or substitute for return for the taxpayer were typically deemed valid returns as long as they were filed before the IRS assessed the tax.[14]

Prior to BAPCPA, the two-year rule did not apply in Chapter 13. Failure to file a return prior to filing bankruptcy did not, by itself, disqualify a tax liability from discharge. However, part of the narrowing of the Chapter 13 super-discharge by BAPCPA made the rule equally applicable in Chapter 13 as well as Chapter 7.

However, what is a "tax return?"

Definitions of a tax return appear in legal literature. "'[T]ax return' is an 'income-tax form on which a person reports income, deductions, and exemptions, and on which tax liability is calculated.'"[15] Such definitions are not adequate to resolve the subtleties of what may be deemed a tax return for bankruptcy purposes.

Pre-BAPCPA, bankruptcy courts found various non-Form 1040 documents to be the equivalent of a Form 1040 for tax discharge purposes, including: IRS Form 870 Waiver of Restrictions on Assessment and Collection of Deficiency in Tax;[16] documents and information provided in a tax court proceeding;[17] IRS Form 4549 Income Tax Examination Changes;[18] and, IRS Form 1902-B Individual audit exam changes report.[19] These and similar documents could be called "constructive" tax returns. The IRS itself explicitly deemed at least the Forms 870 and 4549 to be acceptable equivalents of a Form 1040 tax return.[20]

In 2005, BAPCPA added language to the Bankruptcy Code that, at first glance, appears to broaden the definition of a tax return, which would in some cases permit delinquent taxpayers who had failed to file a regular Form 1040 to discharge overdue taxes in bankruptcy. Pre-BAPCPA, § 523(a)(1)(B) required that the taxpayer file a "tax return." New text added to that provision no longer restricts it to a tax return per se, but also includes an "equivalent report or notice."[21] This broadening language seems to embrace some of the documents that bankruptcy courts as well as the IRS have in the past deemed tax returns, such as the aforementioned Forms 870 and 4549.

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However, virtually at the same time as the effective date of BAPCPA, the IRS reversed its position on those Forms:

> A Form 870, although signed by both husband and wife, is not verified by a written declaration that it is made under the penalties of perjury. A Form 870 is not a return... because it does not purport to be a return and it is not signed under penalties of perjury as required by section 6065.[22]

Also, other new language added to § 523 appears to narrow, rather than to expand the definition of a tax return. That language is found in one of the famous "hanging paragraphs" that BAPCPA dropped into the middle of other text. This hanging paragraph appears immediately following § 523(a)(19). It provides that for purposes of that subsection a return means "a return that satisfies the requirements of applicable nonbankruptcy law (*including applicable filing requirements*)."[23]

Is a late-filed return a "return"?

From the debtor's point of view, the BAPCPA language seemed to have thrown in another monkey-wrench. The IRS successfully argued in recent cases that this language means a return failing to comply with the "applicable filing requirements"—for example, a return that is filed late[24]—is by definition not a return for purposes of the two-year filing rule.

This is the conclusion drawn by at least three recent bankruptcy court opinions. These courts have held that, because of the parenthetical language "(applicable filing requirements)," a late-filed return is, by definition, not a "tax return." In *McCoy v. Mississippi State Tax Comm'n (In re McCoy)*, the court stated: "The new definition of 'return' under § 523(a)(*) requires that a return meet the filing requirements of nonbankruptcy law[.]"[25]

The *McCoy* court dismissed the debtor's argument that since her returns were filed before the additional tax was assessed, they should be deemed valid returns. The weight of pre-BAPCPA authority was that such a return, though filed late, nevertheless constituted a valid return if filed prior to the assessment.

The Bankruptcy Court for the Northern District of Ohio, in *Links v. United States (In re Links)*,[26] noted that the IRS position was that a "tax 'return submitted after the relevant due date does not meet the definition of 'return' and is non-dischargeable under 11 U.S.C. § 523(a)(1)(B)(i).'"

The *Links* court cited a third case, *Creekmore v. IRS (In re Creekmore)*,[27] which supported the same Government argument. The *Links* court then writes, "[h]aving not been presented with any argument to the contrary, the Court finds the conclusion reached in *In re Creekmore* to be sound."[28]

The court in *Creekmore* cited this rule:

> The definition of 'return' in amended § 523(a) apparently means that a late filed income tax return, unless it was filed pursuant to § 6020(a) of the Internal Revenue Code, can never qualify as a return for dischargeability purposes because it does not comply with the 'applicable filing requirements' set forth in the Internal Revenue Code.[29]

The *Creekmore* opinion states boldly "Congress has now definitively addressed this issue."[30]

Not so fast

The language in the hanging paragraph upon which these courts base their conclusions immediately proceeds to excuse several kinds of returns from the timely filed rule, explicitly including a substitute for return filed under the Tax Code by the IRS in cases where the taxpayer has failed to file a Form 1040.[31] Section 6020(a) of the Tax Code provides that such a return, if signed by the taxpayer, may be treated as a return:

> If any person shall fail to make a return required by this title or by regulations prescribed thereunder,... the Secretary may prepare such return, which, being signed by such person, may be received by the Secretary as the return of such person.[32]

Also, the hanging paragraph text does not limit the definition of a return to those 1040s that are filed timely, or to Tax Code § 6020(a) returns. Immediately following the parenthetical words singled out by the above cases, the statute states: "*Such term includes*", then follows several kinds of documents that are included, such as the

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§ 6020(a) taxpayer-signed substitute for return as well as a "written stipulation to a judgment." Under accepted rules of statutory construction, the term "includes" is not restrictive, but is rather a recitation of examples.[33] The only kind of return explicitly excluded from the definition of return is a substitute tax return prepared by the IRS but unsigned by the taxpayer under 26 U.S.C.A. § 6020(b).[34]

The rule postulated by the three cases cited above has other problems. If it is congressional intent that an untimely filed return can never satisfy the two-year rule, then how do we explain the text under § 523(a)(1) that only excepts from discharge those taxes where either no tax return was filed at all, or the return was filed late and within two years before the bankruptcy? Nowhere in this short list of exclusions is found an untimely return filed more than two years before the bankruptcy.[35] This reading of the Bankruptcy Code is mirrored in IRS literature as recently as 2009. The rule adopted by the three cases overlooks this text. Had Congress intended to except from discharge any late-filed Form 1040 returns, it could have done so by simply replacing the text of § 523(a)(1)(B)(ii) with "(ii) was untimely filed" or similar words.

Also, trouble for the three cases does not stop there. As mentioned above, the language found in the hanging paragraph is not the only text regarding the tax return rule inserted by BAPCPA. The 2005 amendments also added to § 523(a)(1)(B) the words "an equivalent report or notice." So, the two-year rule may be satisfied even without a valid 1040 return being filed. Any equivalent report or notice, if filed more than two years prior to the bankruptcy, will do.

However, what is an "equivalent report or notice"?

The Bankruptcy Code does not define the phrase "equivalent report or notice." The argument might be raised under the hanging paragraph that, whatever an "equivalent report or notice" is, if offered to satisfy the rule it must also comply with "applicable filing requirements" (i.e., be filed timely).

However, where are the rules for "timely" filing an equivalent report or notice? Not surprisingly, there are no such rules in the Tax Code, in the Internal Revenue Manual, or in the Treasury regulations. All that is required to be filed "timely" is a tax return. Under the hanging paragraph, the only kind of documents that must satisfy applicable filing requirements are "returns." Not mentioned are equivalent reports or notices. Under ordinary rules of statutory construction, the addition of these two kinds of documents in the provision excepting a tax from discharge cannot be brushed off as merely alternative ways to describe a tax return. That BAPCPA inserted the words "report" and "notice" in § 523(a)(1)(B), but did not also insert them following the term "tax return" in the hanging paragraph, should be dispositive that Congress intended these terms to mean something different than a timely-filed Form 1040.[36]

Lending weight to the argument that a Form 1040 is not required to be filed at all, as long as an equivalent report or notice is provided more than two years before the bankruptcy, is yet other text added by BAPCPA. Pre-2005 language in § 523(a)(1)(B) restricted satisfaction of the rule to a return, however defined, that was "filed." BAPCPA added the disjunctive phrase "or given."

What does "given" mean?

What does "given" mean? The Bankruptcy Code does not define "given." However, again, under ordinary rules of statutory construction, "given" means something different than "filed."

This added term appears to be favorable to some delinquent taxpayers. It is not uncommon for a client to insist she "filed" her tax return with the taxing entity, when in fact what the taxpayer did was simply hand a copy of a return to an employee of the taxing entity. Some taxpayers do this during the course of an audit. In the client's mind, by giving a 1040 to an IRS person, she is "filing" the return. However, some bankruptcy cases have held that failing to mail the return to the applicable IRS service center fails to satisfy the requirement for filing the return, because the Tax Code is explicit that a return must be filed with the appropriate service center based on the taxpayer's residence.[37]

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Combining the addition of "report" or "notice" with "given," suggests that Congress intended the 2005 tax discharge language to provide an alternative way to satisfy the two-year rule: if the taxpayer has "given" an "equivalent report or notice" to the taxing entity more than two years before the bankruptcy, the rule is satisfied. Also, since, at least under existing statutes and regulations, there are no deadlines for giving a report or notice to the IRS, it clearly does not matter when the giving happened, as long as whatever was given, was given more than two years prior to the bankruptcy filing.

The IRS suddenly reverses itself!

It now appears that the Department of Justice was reexamining its position on this issue, at least along some of the lines of reasoning described above. In *In re Smart*,[38] a case that is pending at this writing in the Bankruptcy Court for the Northern District of Illinois, the IRS initially took the same position it had in the three cases discussed above—by definition a late-filed return is not a "return."

However, midway through this case the Department of Justice did something almost unheard of: it filed a memorandum with the bankruptcy court essentially falling on its sword, admitting that its position was wrong, and announcing it will no longer argue that a late-filed return, for that reason alone, is not a return within the meaning of § 523(a)(1)(B)(ii).

The principal basis for the new IRS position appears to be congressional intent. Here, from the IRS memorandum:

> [T]he United States has now determined that its initial position on this issue was incorrect and that it will no longer claim that taxes reported on and assessed in accordance with late-filed returns are excepted from discharge under section 523(a)(1)(B)(i). Although the foregoing authorities suggest that the plain language of the added definition of "return" at the end of amended section 523(a) unambiguously excludes any return that does not meet all "filing requirements," including timeliness of filing, the Internal Revenue Service has concluded that the definition is ambiguous and that the better view is that Congress did not intend to repeal the long-standing law that taxes assessed in accordance with a return filed late are governed primarily by section 523(a)(1)(B)(ii) rather than (i), so that the tax is dischargeable if more than two years elapse between the filing of the return and the bankruptcy petition.

The IRS memorandum in *Smart* goes on to identify other anomalies that would follow from its previous position, for example: "the exclusion of section 6020(b) returns [would be] wholly unnecessary if the first sentence in section 523(a)'s flush language were construed to eliminate late-filed returns generally."

So, what is a "return," really?

Presumably the new IRS position blocks the path cut by the three prior cases. However, what documents do satisfy the two-year rule? The BAPCPA text cited above may have been intended to clarify the definition of a tax return. Yet, it may have clouded, rather than clarified, what constitutes a return or perhaps a constructive return for purposes of the two-year rule.

However, there is more text added by BAPCPA that may point the way. The text BAPCPA included in the hanging paragraph says that to constitute a "return" it must satisfy "the requirements of applicable nonbankruptcy law."

On the one hand, it may be argued—for federal purposes, at least—that a return must be defined as a return by the IRS. At first blush, this might strengthen the argument that whatever it is, to constitute a "return" it must be timely filed. On the other hand, a stronger textual argument is that this text does not explicitly provide that a return is only whatever the IRS says it is. Reference to other authority, as long as it is "nonbankruptcy" law, should be considered to define what constitutes a valid return.

In 2005, the IRS adopted Revenue Ruling 2005-59[39] that dropped Forms 870 and 4549 from the kinds of documents the IRS deems a tax return. This ruling rested on prominent case law. The cited authority referenced a line of cases prescribing the elements required to constitute a tax return:

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> [A] document filed with the Service is treated as a return if the document: (1) contains sufficient data to calculate the tax liability; (2) purports to be a return; (3) represents an honest and reasonable attempt to satisfy the requirements of the tax law; and (4) is executed under penalties of perjury.[40]

Arguments about the meaning of the relevant Bankruptcy Code sections inevitably will include consideration of public policy and legislative intent. A search of the literature frequently finds a public policy statement:

> The drafters of the 1978 Bankruptcy Code recognized a tension between three constituencies: (1) taxing authorities, who must be given a reasonable time to collect taxes, (2) general unsecured creditors, who compete with the taxing authorities for distributions from the estate, and (3) the debtor, whose "fresh start" should not be burdened with an excessive accumulation of past-due taxes.[41]

Prior to BAPCPA, courts said this about the legislative purposes of the text: "Congress contemplated that late-filing of tax returns would not be sufficient in itself to bar dischargeability of tax debts. 11 U.S.C. § 523(a)(1)(B)(ii)."[42]

To be fair, courts have also embraced a policy of looking to tax law to identify tax return filing requirements. "Tax Code should be the primary source of guidance as to the requirements for a return under tax law and, thus, the meaning of the term under bankruptcy law."[43]

Yet, in reading the Tax Code tea leaves, courts have often concluded that untimely filing does not, by itself, make a return something other than a return: "A late-filed return becomes subject to penalties and interest. It does not, however, cease to be a return."[44] "The return may be frivolous. It may be false. It may be fraudulent. But it is a return nonetheless."[45] Reference to the Tax Code or regulations does not provide any more of an answer than does the Bankruptcy Code: "Surprisingly, neither the United States Tax Code… nor the regulations promulgated in connection therewith define the term 'return.'"[46]

When the two-year tax return filing rule is at issue today, the safest ground may be the four elements quoted above, frequently labeled as the "*Beard* test."[47] Cases relying on the *Beard* formula typically adjudicate the issue by focusing not on the timing of the filing, but rather on the fourth *Beard* prong, intent:[48]

> In *Moroney,* the court determined that the debtor should be permitted to demonstrate that the delayed filing was nonetheless an honest and reasonable attempt at self-assessment. The Fourth Circuit declined to apply a bright-line test because "[c]ircumstances not presented in this case might demonstrate that the debtor, despite his delinquency, had attempted in good faith to comply with the tax laws."[49]

In any event, the argument that an untimely tax return is by definition not a tax return is both inconsistent with the words added to the Bankruptcy Code by BAPCPA and quite possibly beside the point: any equivalent report or notice that was given to the taxing entity more than two years before bankruptcy now satisfies the rule. Tax liability is not excepted from discharge merely for failure to file a Form 1040 or equivalent document at or before the expiration of a filing deadline prescribed in tax regulations.

Research References: Norton Bankr. L. & Prac. 3d §§ 49:50, 57:6, 57:7

West's Key Number Digest, Bankruptcy ⚿2871, 2965, 3343.5

Notes

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1. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (2005).
2. The "two year rule" refers to the period of time prior to a debtor's bankruptcy filing that a tax return must have been filed if the debtor seeks to discharge the tax liabilities for that return. 11 U.S.C.A. § 523(a)(1)(B)(ii).
3. 11 U.S.C.A. § 523(a)(1)(B).
4. 11 U.S.C.A. § 507(a)(8)(A)(i).
5. 11 U.S.C.A. § 507(a)(8)(A)(ii).
6. 11 U.S.C.A. § 523(a)(1)(C).
7. 11 U.S.C.A. § 523(a)(1)(C).
8. Prior to BAPCPA an income tax falling into any of the exceptions to discharge under § 523(a)(1) could not be discharged in Chapter 7, but could be discharged in Chapter 13. Thus, failure to file a tax return rendered the tax nondischargeable in Chapter 7, but had no bearing on discharge under Chapter 13. Today, technically, in many cases personal income taxes remain dischargeable in Chapter 13, because income taxes, even if priority under § 507(a)(A), are not per se included in the exceptions to discharge found at § 1328(a). However, pursuant to BAPCPA, an income tax liability falling within the exceptions to discharge found at § 523(a)(1)(B) and (C) (e.g., failure to file the return) is now nondischargeable in Chapter 13 as well as Chapter 7.
9. To get the taxpayer back into "compliance" is ostensibly a goal of the IRS.
10. A Form 1040 filed on behalf of the taxpayer by the IRS ("substitute for return"), to which the taxpayer did not agree, did not, and still does not qualify for purposes of satisfying the tax return filing rule.
11. The rule was the flip-side of an exception to discharge found at § 523(a)(2)(B).
12. Any of several other exceptions may render the tax nondischargeable, to wit; the most recent due date for filing the return was within three years of the bankruptcy (§ 507(a)(8)(A)(i)); the tax liability was assessed within 240 days of filing (§ 507(a)(8)(A)(ii)); the tax return was fraudulent, or the taxpayer had engaged in a willful attempt to evade or defeat the tax (§ 523(a)(1)(C)). These, and the two-year filing rule constitute what are usually called the "5 Rules" that must be satisfied in order to be dischargeable. These are not addressed in this article. See King, Discharging Taxes Under the Bankruptcy Reform Act of 2005, ¶ 2.4 (BankruptcyBooks.com Release # 4, 2009).
13. "In point of fact, once the IRS has gone through the process of computing a derelict taxpayer's income tax from alternative information sources, preparing substitute returns, issuing notices of deficiency, and assessing taxes that then become an enforceable liability, the filing of voluntary returns by a taxpayer simply is no longer 'required.'... Once an involuntary government-made assessment is final, then, the taxpayer no longer can use the perfunctory expedient of filing belated voluntary returns to subject a now-stale tax claim to discharge in bankruptcy." Walsh v. United States (In re Walsh), 260 B.R. 142, 150-51 (Bankr. D. Minn. 2001). See also United States v. Hindenlang (In re Hindenlang), 164 F.3d 1029 (6th Cir. 1999). But contrary, "[t]his Court will not read into § 523(a)(1)(B)(i) the requirement that a debtor must have filed a return prior to an assessment by the IRS." Crawley v. United States (In re Crawley), 244 B.R. 121, 127 (Bankr. N.D. Ill. 2000).
14. Sullivan v. United States (In re Sullivan), 200 B.R. 327, 332 (Bankr. N.D. Ohio 1996) ("there is nothing in the tax law which supports the argument that the Debtor's 1040's were nullities and therefore would not qualify as returns").
15. Black's Law Dictionary (8th ed. 2004).
16. Carapella v. United States (In re Carapella), 84 B.R. 779 (Bankr. M.D. Fla. 1988).
17. Elmore v. United States (In re Elmore), 165 B.R. 35, (Bankr. S.D. Ind. 1994).
18. Berard v. United States (In re Berard), 181 B.R. 653 (Bankr. M.D. Fla. 1995).
19. Lowrie v. United States (In re Lowrie), 162 B.R. 864 (Bankr. D. Nev. 1994).
20. Rev. Rul. 74-203, 1974-1 C.B. 330 (revoked by Rev. Rul 2005-59, 2005-2 C.B. 505).
21. 11 U.S.C.A. § 523(a)(1)(B). Broadening the definition of a tax return would not be necessarily favorable to all debtors. Some states require that additional IRS tax assessments be "reported" to the state so they can do their "piggy-back" assessments. Many taxpayers fail to report the IRS audit adjustments to the state. If such reports are deemed tax returns, it would trigger a new two-year period before those state taxes could be dischargeable. Even when the IRS audit is timely reported, state taxing entities frequently take forever to get around to assessing the additional tax, sometimes drastically delaying the time when the debtor can discharge the piggy-back tax.
22. Rev. Rul. 2005-59, 2005-2 C.B. 505.
23. 11 U.S.C.A. § 523(a)(19)* (emphasis added).
24. "[R]eturns made on the basis of the calendar year shall be filed on or before the 15th day of April following the close of the calendar year." 26 U.S.C.A. § 6072(a).
25. McCoy v. Mississippi State Tax Comm'n (In re McCoy), Adv. No. 08-00175-EE, Case No. 07-02998-EE, 2009 WL 2835258 (Bankr. S.D. Miss. Aug. 31, 2009) (dealing with a state income tax liability). The "*" refers to the hanging paragraph under § 523(a)(19).

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26. Links v. United States (In re Links), Adv. No. 08-3178, Case No. 07-31728, 2009 WL 2966162 at *4 (Bankr. N.D. Ohio Aug. 21, 2009). It should be noted that the debtor in *Links* was in pro per, which may account for the apparently feeble argument on the debtor's side—"Having not been presented with any argument to the contrary, the Court finds."

27. Creekmore v. IRS (In re Creekmore), 401 B.R. 748 (Bankr. N.D. Miss. 2008) .

28. In re Links, 2009 WL 2966162 at *5.

29. In re Creekmore, 401 B.R. at 751.

30. In re Creekmore, 401 B.R. at 752.

31. 26 U.S.C.A. § 6020(a).

32. 26 U.S.C.A. § 6020(a). See also In re Creekmore, 401 B.R. at 750 ("[I]it appears that a return prepared by the 'Secretary' and signed by the taxpayer following a disclosure of all relevant information, constitutes a 'return' even if it is untimely filed.").

33. See 11 U.S.C.A. § 102(3); see also In re Krehl, 86 F.3d 737 (7th Cir. 1996); In re TBR USA, Inc., 429 B.R. 599 (Bankr. N.D. Ind. 2010); In re Walters, 113 B.R. 602 (Bankr. D.S.D. 1990); In re Hackney, 351 B.R. 179 (Bankr. N.D. Ala. 2006).

34. It is clear that a substitute for return filed by the IRS, by itself, does not satisfy the two-year rule. See Ehrig v. United States (In re Ehrig), 308 B.R. 542, 549-50 (Bankr. N.D. Okla. 2004) (citing Bergstrom v. United States (In re Bergstrom), 949 F.2d 341 (10th Cir. 1991)).

35. United States v. Klein, 312 B.R. 443, 449 (S.D. Fla. 2004) ("The plain language of the statute indicates that a late return may be an automatic bar to discharge only when the late return is filed within two years of the petition for bankruptcy.").

36. United States v. Nunez (In re Nunez), 232 B.R. 778 (B.A.P. 9th Cir. 1999) ("When Congress includes particular language in one section of the Code, but omits it in another, it is presumed to have acted intentionally and purposely.").

37. 26 U.S.C.A. § 6091(b)(1)(A)(ii); see also Savage v. IRS (In re Savage), 218 B.R. 126 (B.A.P. 10th Cir. 1998) (debtor hand-delivered the returns to an IRS official in Portland, Oregon, when based on his residency he should have filed them at the service center located in Ogden, Utah).

38. In re Smart, Case No. 08-27159 (Bankr. N.D. Ill.).

39. Rev. Rul. 2005-59, 2005-2 C.B. 505.

40. Rev. Rul. 2005-59, 2005-2 C.B. 505 (citing Beard v. Commissioner, 82 T.C. 766, 777 (1984), aff'd, 793 F.2d 139 (6th Cir. 1986) (citing Badaracco v. Commissioner, 464 U.S. 386, 104 S. Ct. 756, 78 L. Ed. 2d 549 (1984); Zellerbach Paper Co. v. Helvering, 293 U.S. 172, 55 S. Ct. 127, 79 L. Ed. 264 (1934); Florsheim Bros. Drygoods Co. v. United States, 280 U.S. 453, 50 S. Ct. 215, 74 L. Ed. 542 (1930)).

41. Waugh v. IRS (In re Waugh), 109 F.3d 489, 492 (8th Cir.1997) (citing S. Rep. No. 95-989, at 14 (1977), as reprinted in 1977 U.S.C.A.A.N.1978, 5787, 5800).

42. Colsen v. United States (In re Colsen), 311 B.R. 765 (Bankr. N.D. Iowa 2004), aff'd, 322 B.R. 118 (B.A.P. 8th Cir. 2005), aff'd, 446 F.3d 836 (8th Cir. 2006); In re Nunez, 232 B.R. at 781-82; In re Savage, 218 B.R. 126; In re Crawley, 244 B.R. at 126-27.

43. Mathis v. United States (In re Mathis), 249 B.R. 324, 327 (S.D. Fla. 2000); In re Colsen, 311 B.R. at 772.

44. 26 U.S.C.A. § 6651(a)(1); In re Colsen, 311 B.R. at 774 (citing Badaracco v. Commissioner, 464 U.S. 386, 104 S. Ct. 756, 78 L. Ed. 2d 549 (1984)).

45. Hess v. United States, 785 F. Supp. 137, 139 (E.D. Wash.1991).

46. In re Colsen, 446 F.3d 836 (8th Cir. 2006).

47. "The Bankruptcy Code does not define the term 'return' in section 523 or anywhere else. Most courts therefore apply a four-prong test, known as the '*Beard* test,' to determine whether a debtor's document qualifies as a return." United States v. Klein, 312 B.R. at 447.

48. "The IRS has the initial burden of proving by a preponderance of the evidence that the debt is an exception to discharge under § 523(a)(1)(B), which includes demonstrating that the "honest and reasonable attempt" prong is not satisfied." In re Henne, 359 B.R. 776, 779 (Bankr. D. Ariz. 2007) (debtor's returns failed the fourth prong because of his failure to follow up with the IRS and provide requested information).

49. United States v. Klein, 312 B.R. at 450.

From the Appellate Courts

RECENT DECISIONS FROM THE APPELLATE COURTS

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