Lesson 11

NON-TITLE 11 INSOLVENCIES

CONTENTS

I. OBJECTIVES

At the end of this lesson you will be able to determine in a given case:

- When the United States has priority under 31 U.S.C. § 3713;
- The types of proceedings in which the priority may be claimed;
- Whether a proof of claim should be filed in those proceedings; and
- When a fiduciary may be held personally liable for failure to honor a priority claim of the United States.

II. PROVISIONS OF THE FEDERAL PRIORITY STATUTE (31 U.S.C. § 3713)

31 U.S.C. § 3713 provides:

> (a)(1) A claim of the United States Government shall be paid first when
>
> (A) a person indebted to the Government is insolvent and
>
> (i) the debtor without enough property to pay all debts makes a voluntary assignment of property;
>
> (ii) property of the debtor, if absent, is attached; or
>
> (iii) an act of bankruptcy is committed; or
>
> (B) the estate of a deceased debtor, in the custody of the executor or administrator, is not enough to pay all debts of the debtor.
>
> (2) This subsection does not apply to a case under Title 11.
>
> (b) A representative of a person or an estate (except a trustee acting under title 11) paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of Government.

III. HISTORY OF THE FEDERAL PRIORITY STATUTE

The federal priority statute can be traced to the Acts of the First Congress, though its roots reach further back into the English common law. See United States v. Moore, 423 U.S. 77, 80 (1975). Subsequently, Congress re-enacted and expanded federal priority with varying degrees of modification. This early legislation, enacted before the federal bankruptcy law, expressed a canon first seen in the Magna Carta: "The king's debtor dying, the king shall first be paid." See United States v. Verlinsky, 459 F.2d 1085 (5th Cir. 1972).

In 1878, the federal priority statute was incorporated in Title 36 of the Revised Statutes, which comprised the first codification of U.S. law. R.S. § 3466 contained the federal priority, while R.S. § 3467 imposed personal liability upon a fiduciary that violated the priority scheme. Those sections were codified in 31 U.S.C. §§ 191 and 192, respectively. The federal priority statute continued in substantially the same form from 1797 until 1978, when Congress amended former 31 U.S.C. §§ 191 and 192 so that the provisions no longer applied in a case under Title 11. Pub. L. 95-598, § 322. Thereafter, 31 U.S.C. §§ 191 and 192 were revised by Public Law 97-258 (approved September 13, 1982) and were re-enacted as 31 U.S.C. § 3713(a) and (b), respectively. According to the legislative history, Congress did not intend to substantively change the existing law. Instead, the 1982 revision merely amended the language of the statute to reflect contemporary usage. See H. Rep. No. 97-651, 97th Cong., 2d Sess. 1, 130-35. Consequently, case law relating to the former Revised Statutes should be given precedential effect with respect to 31 U.S.C. § 3713. Accord State of Idaho ex rel. Soward v. U.S., 858 F.2d 445, 451 n.6 (9th Cir. 1988).

IV. SIGNIFICANCE OF THE FEDERAL PRIORITY STATUTE

The priority given to the United States pursuant to 31 U.S.C. § 3713 is vital to federal tax collection in nonbankruptcy cases. Generally, if a taxpayer is insolvent and is divested of control over the distribution of his property in a manner specified in 31 U.S.C. § 3713, the statute requires that the claims of the federal government, including taxes, be paid before the claims of other creditors. This priority is crucial in situations in which the government does not have a lien to rely on for collection. And, if the Service has a lien, section 3713 may provide a greater recovery than a federal tax lien in some situations. Straus v. United States, 196 F.3d 862 (7th Cir. 1999) (but for section 3713, state tax lien would have had priority over federal tax lien). The Supreme Court has often stated that the federal priority statute is to be construed liberally in favor of the government and has thus rejected a narrow or strict construction. U.S. v. Moore, 423 U.S. 77, 82 (1975).

V. REQUIREMENTS FOR FEDERAL PRIORITY

A. There Must Be Insolvency

1. For purposes of the statute, a debtor is insolvent under 31 U.S.C. § 3713 only if its liabilities exceed its assets, i.e., the "balance sheet" insolvency test. See Lakeshore Apartments, Inc. v. United States, 351 F.2d 349, 353 (9th Cir. 1965). Thus, the inability to pay debts as they mature in the ordinary course of business does not constitute "insolvency" for purposes of 31 U.S.C. § 3713. United States v. Oklahoma, 261 U.S. 253 (1923); U.S. v. Key, 397 U.S. 322, 328, 329 and n.7 (1970). In the latter instance, the debtor might have far more assets than liabilities, but due to the character of the assets, they cannot be readily liquidated.

2. Certain collection proceedings might constitute an act of bankruptcy, even though the debtor is not insolvent under either test (in the case of a general assignment) or is merely unable to pay debts as they mature (in the case of a receivership or trusteeship). Often such a proceeding may end with "balance sheet" insolvency even though it did not begin that way, and 31 U.S.C. § 3713 has been held applicable if such insolvency existed by the time of distribution. Hatch v. Morosco Holding Co., 61 F.2d 944 (2d Cir. 1932), cert. denied sub nom Irving Trust Co. v. U.S., 288 U.S. 613 (1933).

3. The relevant time for testing solvency is at distribution. In Hatch v. Morosco Holding, Co., 61 F.2d 944, 947 (2d Cir. 1932), cert. denied, 288 U.S. 613 (1933), a consent receivership was instituted for the purpose of conserving the debtor's assets, even though insolvency did not exist at inception of the proceeding. Insolvency was demonstrated at distribution some six years later. See also Schwartz v. Commissioner, 560 F.2d 311 (8th Cir. 1977) (when insolvency arises after death, the administrator may be held liable only as to payments made after insolvency arises); United States v. Estate of Young, 592 F. Supp. 1478, 1484 (E.D. Pa. 1984)(§ 3713 applied when decedent's estate became insolvent); but see Jonathan’s Landing v. Townsend, 960 F2d 1538 (11th Cir. 1992).

B. There Must Be a “Debt” Due the United States

1. Taxes are "debts" due to the United States. County of Spokane v. United States, 279 U.S. 80 (1929); Price v. United States, 269 U.S. 492 (1926).

2. The Government may exercise its priority even though taxes have not yet been assessed. The claim for taxes constitutes the "debt" required for purposes of 31 U.S.C. § 3713(a). Viles v. Commissioner, 233 F.2d 376 (6th Cir. 1956). This is consistent with the decision in United States v. Moore, 423 U.S. 77 (1975), which held that unliquidated claims of the United States should be accorded priority under former 31 U.S.C. § 191.

C. Divestiture of Property to a Fiduciary

Except in decedents’ estates cases, insolvency by itself is insufficient to trigger the application of the priority statute. The insolvency must be manifested in one of three prescribed ways.

1. The three ways are: (1) the debtor makes a "voluntary assignment" of property; (2) property of the debtor, if absent, is attached; or (3) an "act of bankruptcy" is committed. 31 U.S.C. § 3713(a)(1)(A).

2. In general, the priority statute applies "when the possession and control of the estate of the insolvent is given to any person charged with the duty of applying it to the payment of the debts of the insolvent, as the rights and priorities of creditors may be made to appear…." Bramwell v. United States Fidelity & Guar. Co., 269 U.S. 483, 490 (1926). Thus, in the typical case to which section 3713 applies there is a transfer of all (or substantially all) of the debtor’s assets to a receiver or other fiduciary charged with liquidating the

assets and satisfying the debtor's liabilities. Notwithstanding the quoted language, 31 U.S.C. § 3713 may also apply as indicated below in other cases not involving a transfer to a fiduciary when certain “acts of bankruptcy” as defined by the Bankruptcy Act are committed by the debtor.

3. The priority statute does not require that the insolvent debtor be “divested” or that the person who has the duty to pay the United States become “invested” with title to the debtor’s property. Bramwell v. United States Fidelity & Guar. Co., 269 U.S. 483, 489 (1926); United States v. Crocker, 313 F.2d 946, 948 (9th Cir. 1963).

4. Courts have applied the insolvency statute when certain acts of bankruptcy have been committed that do not involve or lead to collection proceedings administered by a fiduciary. For example, the priority statute has been used in cases of property fraudulently conveyed by the debtor and recovered by a judgment creditor. See United States v. Mr. Hamburg Bronx Corp., 228 F. Supp 115 (S.D.N.Y. 1964); cf. United States v. Fidelity & Deposit Co., 214 F.2d 565, 570 (5th Cir. 1954). It has also been held to apply to instances of preferential transfers not followed by bankruptcy. See Lakeshore Apartments, Inc. v. United States, 351 F.2d 349, 353 (9th Cir. 1965); United States v. Caldwell, 74 F. Supp. 114 (M.D. Tenn. 1947).

5. "Acts of bankruptcy," referred to in 31 U.S.C. § 3713(a)(1)(A)(iii), were listed in former 11 U.S.C. § 21, which was repealed in 1978. See Bankruptcy Reform Act of 1978, P.L. 95-598. Old section 21 defined an act as bankruptcy as (1) fraudulent conveyances or concealments of property, (2) transfers while insolvent, (3) permitting, while insolvent, a creditor's lien to attach to property through legal proceedings, (4) assignments for the benefit of creditors, (5) permitting or procuring, while insolvent in either the bankruptcy or equity sense, a receiver to be appointed to take charge of the bankrupt's property, and (6) admissions in writing of inability to pay debts and of willingness to be adjudged a bankrupt. In cases that arose under the Bankruptcy Act, the Department of Justice asserted priority under former section 191 merely when an "act of bankruptcy" had been committed by a debtor. See, e.g., W.T. Jones & Co. v. Foodco Realty, Inc., 318 F.2d 881 (4th Cir. 1963). There are no "acts of bankruptcy" under the Bankruptcy Code (effective for bankruptcy cases filed on or after October 1, 1979) but the concept of an act of bankruptcy remains.

VI. BURDEN OF PROOF

Parties who argue that a Government claim does not have priority have the burden of proving that such claim is not within the provisions of 31 U.S.C. § 3713. United States v. Cole, 733 F.2d 651, 654 (9th Cir. 1984). See Bramwell v. United States Fidelity & Guar. Co., 269 U.S. 483, 487 (1926).

VII. COMPARISON OF PRIORITIES UNDER 31 U.S.C. § 3713(a) AND THE BANKRUPTCY CODE

A. The priority afforded by 31 U.S.C. § 3713 is not available to the Government when it is a creditor in a bankruptcy proceeding. 31 U.S.C. § 3713(a)(2); In re Glinz, 46 B.R. 266 (D. N.D. 1984). Section 3713 does not apply to any litigation that involves assets of the bankrupt debtor. See NLT Computer Serv. v. Capital Computer Sys., 755 F.2d 1253 (6th Cir. 1985). Accordingly, the priority statute does not impose personal liability on a trustee acting under Title 11. 31 U.S.C. § 3713(b).

B. Section 3713(a) is more advantageous to the Government than Title 11 for several reasons:

1. Under 31 U.S.C. § 3713(a), federal tax claims have priority over other taxing authorities. In bankruptcy, all pre-petition eighth priority federal tax claims are on a par with similar state tax claims. See 11 U.S.C. § 507(a)(8).

2. Under 31 U.S.C. § 3713, all claims for federal taxes that are subject to collection are entitled to priority, no matter when the claim arose. In bankruptcy, a claim for taxes could lose priority. See 11 U.S.C. § 507(a)(8)(A)(i) (providing priority for a tax claim for which a return, if required, was last due after three years before the petition date).

C. On the other hand, in certain cases 31 U.S.C. § 3713 may be less advantageous to the Government.

1. Under 31 U.S.C. § 3713, claims are often made in state court, where favorable treatment to the Government is less certain.

2. A trustee in bankruptcy, as opposed to a receiver in other insolvency actions, usually has greater power to bring assets into the estate. For example, a trustee can avoid fraudulent or preferential transfers. 11 U.S.C. §§ 547, 548. A trustee can also assume or reject executory contracts and unexpired leases. 11 U.S.C. § 365.

VIII. EXTENT OF 31 U.S.C. § 3713 PRIORITY

A. **Time of Effectiveness:** If a debtor is insolvent, the right to priority of payment takes effect at the time the transfer of the property occurs.

1. In general assignments for the benefit of creditors, the priority accrues at the date of the execution of the assignment. Massachusetts v. United States, 333 U.S. 611 (1974).

2. In receivership proceedings the priority becomes effective on the date the receiver takes over by court order. United States v. Oklahoma, 261 U.S. 253 (1923).

3. In decedent's estate proceedings the priority of the United States arises at the date of death.

If a debtor only becomes insolvent after the transfer of property occurs, the right to priority could attach at such later time. See Hatch v. Morosco Holding Co., 61 F.2d 944 (2d Cir. 1932), cert. denied sub nom Irving Trust Co. v. U.S., 288 U.S. 613 (1933); see also Scwartz v. Commissioner, 560 F.2d 311 (8th Cir. 1977).

B. **Exceptions:** Although 31 U.S.C. § 3713 does not provide for any exceptions to the Government's priority, the courts have established several limited classes of claims that might be paid before satisfying the tax debt. See U.S. v. Texas, 314 U.S. 480 (1941). However, the Supreme Court has cautioned that "only the plainest inconsistency would warrant our finding an implied exception to the operation of so clear a command as that of [the federal priority statute]." United States v. Moore, 423 U.S. 77, 83-84 (1975);

1. The first exception is certain administrative expenses, such as court costs, reasonable compensation for the fiduciary and attorney, and expenses incurred in operating a business or liquidating assets made in the ordinary course of these operations. Generally, these expenses are incurred for the general welfare of creditors and in certain instances may enjoy priority over the Government's claim. See Abrams v. U.S., 274 F.2d 8 (8^{th} Cir. 1960) (cases cited). See also, Southern Railway Co. v. United States, 306 F.2d 119 (5^{th} Cir. 1962) (holding that the Service's administrative tax claim shared pro rata with other administrative claims); G.C.M. 37239, 1977 WL 46549 (August 31, 1977) (adopting Southern Railway). State law should be consulted because such expenses may be subject to a standard of reasonableness or specific dollar limitation. Distribution orders and accountings issued in insolvency proceedings should be

reviewed carefully to spot excessive attorney and fiduciary fees. Consideration should be given to filing a request for notice of proceedings in the case and for copies of pleadings.

2. The Supreme Court has also found a plain inconsistency between the federal priority statute and the Federal Tax Lien Act. In United States v. Estate of Romani, 523 U.S. 517 (1998), the Court held that a judgment lien creditor that recorded its liens on real property before the Service filed its Notices of Federal Tax Lien, prevailed over the Service's tax claims in an insolvent decedent's estate case. See I.R.C. § 6323.

   a. The general rule is that if the creditor would prevail against the Service under I.R.C. § 6323(a) outside of insolvency, it will also prevail against the Service in the insolvency.

   b. If the creditor's interest prevails over the federal tax lien under I.R.C. § 6323(a), then the Service cannot assert priority over that creditor under 31 U.S.C. § 3713. Pursuant to I.R.C. § 6323(a), purchasers, holders of security interests, mechanic's lienors, and judgment lien creditors prevail unless the Service has filed a Notice of Federal Tax Lien. A I.R.C. § 6323(a) creditor (including holders of mortgages and other consensual security interests) will generally have a higher priority claim than the Service if the creditor's interest is perfected prior to the filing of the Notice of Federal Tax Lien.

   c. If a competing interest is not specifically given priority over a tax claim by I.R.C. § 6323, the federal priority statute applies. For example, the priority of a Federal tax lien against a state tax lien is not governed by I.R.C. § 6323, so the Federal tax claim has priority over the state tax claim for distribution from an insolvent estate, even if outside of insolvency the state claim would prevail because it was choate before the federal lien arose. Straus v. United States, 196 F.3d 862 (7th Cir. 1999).

   d. Romani applies only where the Government is relying on its lien. In Law Offices of Jonathan A. Stein v. Cadle Company, 250 F.3d 716 (9th Cir. 2001), the Service issued a levy against the compensation of the president and CEO of an insolvent company. The company ignored the levy and continued to pay the president. The Service then sued the company to enforce the levy, and obtained judgment under I.R.C. § 6332(d). A third party also obtained a judgment against the company. The company then got a damages award, to which both the Service and the third party claimed priority. In the ensuing interpleader proceeding, the Government claimed priority under 31 U.S.C. § 3713. The third party claimed priority by virtue of a judgment lien under I.R.C. § 6323. The district court held for the Government under 31 U.S.C. § 3713, and the appellate court affirmed, finding that under Romani the judgment lien would have priority if the United States were relying on a tax lien created under I.R.C. § 6321. However, in this case, the Government claimed priority based on a judgment against the taxpayer's employer under I.R.C. § 6332(d)(1).

3. Another plain inconsistency was found between the federal priority statute and the McCarran-Ferguson Act (15 U.S.C. § 1011 et seq.) In United States v. Fabe, 508 U.S. 491 (1993), the Supreme Court held that the federal priority yields to state law subordinating Federal tax claims to insurance claims of policyholders in the liquidation of an insolvent insurance company, because the McCarran-Ferguson Act specifies that no federal law can supersede any state law regulating the insurance business. Ruthardt v. United States, 303 F.3d 375 (1st Cir. 2002), cert. denied sub. nom. Bowler v. U.S., 538 U.S. 1031 (2003), cert. denied sub. nom. Alabama Ins. Guar. Ass'n v. U.S., 538 U.S. 1031 (2003), relied on Fabe to conclude that the McCarran Ferguson Act preempted the federal priority statute in favor of a state law preference for claims of insurance guaranty funds. Ruthardt may be an unwarranted extension of Fabe as it involved a guaranty fund's claims, rather than policyholders' claims. The guaranty fund issue also arose in Greene v. U.S., 62 Fed. Cl. 418 (2004), appeal filed (Fed. Cir. 05-5032) (2004).

4. In the case of decedent's estates, 31 U.S.C. § 3713(a)(1)(B) provides a statutory basis excepting certain funeral expenses, because priority is afforded only when the estate is not enough to pay all debts of the debtor. Thus, funeral expenses and the cost of a headstone were not subordinated to the federal priority because they were held to be expenses of the estate, rather than debts of the decedent. See, e.g., Martin v. Dennett, 626 P.2d 473 (Utah 1981). See Rev. Rul. 80-112, 1980-1 C.B. 306. However, the expense of a decedent's last illness is a debt of the decedent and does not prime the government's priority under 31 U.S.C. § 3713. In re Shoptow's Estate, 54 Wash. 2d 602, 343 P.2d 740 (1959); In re Muldoon's Estate, 275 P.2d 597, 128 Cal.App.2d 284 (1954).

5. Similarly, homestead and family allowances are treated as debts of the estate, not the decedent. In addition, the Service should concede reasonable homestead and family allowances in insolvency

proceedings even where the IRS is asserting priority based on the tax lien rather than 31 U.S.C. § 3713. See Estate of Igoe v. IRS, 717 S.W. 2d 524 (Mo. 1986). While the argument can be made that the tax lien should prevail over homestead and family allowances, the decision has been made not to litigate this issue unless the allowances are excessive or unreasonable.

6. Though technically not an “exception,” the debts of the United States are to be satisfied from the debtor's estate only. If, therefore, before priority accrues to the Government, the debtor has made a bona fide conveyance of his/her estate to a third person, or if the property has been seized under a writ of execution of judgment, then the property is divested from the debtor and cannot be made liable to the United States. See In re Metzger*,* 709 F.2d 32 (9th Cir.1983) (attorney’s interest in fishing vessel, which was assigned as partial payment of legal services rendered before federal priority attached to debtor’s property, was superior to interest of United States).

7. A third party’s choate lien arising before insolvency may qualify as an exception, but the Supreme Court has not definitively addressed this issue. E.g., United States v. Romani, 523 U.S. 517, 529-30 (1998). For personal property, the Supreme Court has stated that choateness test requires that the creditor acquire either title or possession, in addition to establishing that the lien was choate, i.e., the lienor was identified, the amount of the lien was certain, and the property subject to the lien was definite. United States v. Vermont, 377 U.S. 351 (1964).

IX. PERSONAL LIABILITY OF FIDUCIARY UNDER 31 U.S.C. § 3713(b)

A. Except with respect to a trustee acting in accordance with the provisions of the Bankruptcy Code, 31 U.S.C. § 3713 makes the fiduciary personally liable for debts due to the United States if he pays, in whole or in part, any debt due by the person or estate for whom or for which he acts without first satisfying and paying the debts due the United States.

There can be no personal liability on a debtor's representative or an estate unless the federal priority of 31 U.S.C. § 3713(a) applies. See U.S. v. King, 322 F.2d 317 (1963) (holding that former 31 U.S.C. §§ 191 and 192 must be interpreted in *pari materi*, as part of a common statutory scheme); See also United States v. Butterworth Judson Corp., 269 U.S. 504 (1926) (regarding R.S. 3466 and 3467).

B. 31 U.S.C. § 3713(b) is the muscle behind subsection 3713(a).

C. Given 31 U.S.C. § 3713(b), the fiduciary must move with great care when advised of his or her potential liability:

1. Under 31 U.S.C. § 3713, a fiduciary must first pay known debts to the United States or stand personally liable if he or she fails to do so. United States v. Munroe, 65 F. Supp. 213 (W.D. Pa. 1946); Morris v. Commissioner, 36 B.T.A. 516 (1937); Forehand v. Commissioner, 66 T.C.M. (CCH) 1763 (1993).

2. The debts due the United States must have been determined or determinable at the time the other debts were paid. However, the taxes need not have been assessed as long as the fiduciary has been advised that taxes are owing. Viles v. Commissioner, 233 F.2d 376 (6th Cir. 1956).

3. Knowledge by the fiduciary of the tax debt, at a time when the estate had sufficient assets from which to pay the debt, must be proven. Bank of the West v. Commissioner, 93 T.C. 462 (1989); Want v. Commissioner, 280 F.2d 777 (2d Cir. 1960); Livingston v. Becker, 40 F.2d 673 (E.D. Mo. 1929). However, informal notice by a Government agent that taxes were owed, coupled with a suggestion that the fiduciary should not make distribution of the estate until the taxes were paid, was held to be sufficient notice to hold the fiduciary liable. Viles v. Commissioner, 233 F.2d 376 (6th Cir. 1956). If the Government has made a prima facie case showing knowledge, then the burden is on the fiduciary to establish a lack of knowledge. McCourt v. Commissioner, 15 T.C. 734, 737 (1950). Notice to apprise a fiduciary of a tax debt may be given by Letter 1005(DO).

4. The fiduciary is under no duty to inquire whether any taxes are due unless facts are presented that would put a reasonable person on notice. Irving Trust Co. v. Commissioner, 36 B.T.A. 146 (1937), acq., 1937-2 C.B. 15. Nonetheless, regulations pertaining to a decedent's income taxes require a fiduciary to exercise due diligence in ascertaining whether tax obligations exist. Treas. Reg. § 1.641(b)-2(a).

5. Payment of a bequest to a beneficiary is payment of a debt of the decedent. See Treas. Reg. § 20.2002-1.

6. The fiduciary's responsibility under 31 U.S.C. § 3713 may continue after the court proceedings have terminated if the fiduciary knew of the tax debt before the assets were distributed. Evans v. Commissioner, 12 B.T.A. 334 (1928). Even if the fiduciary had no knowledge of the taxes, he may be liable as a transferee if he was a recipient of property from the insolvent estate. Bell v.

Commissioner, 82 F.2d 499 (3d Cir. 1936). For a discussion of the differences between transferee and fiduciary liability, see Grieb v. Commissioner, 36 T.C. 156, 161-3, acq., 1961-2 C.B. 4.

7. If other elements are present, a fiduciary may be liable under 31 U.S.C. § 3713 even though payment of an inferior claim was pursuant to a court order. King v. United States, 379 U.S. 329 (1964), held that if a fiduciary properly raises the Government's priority, but the court orders payment to another over the fiduciary's objection, the fiduciary will not be liable. However, it is not clear to what extent the fiduciary must contest the court's order to avoid liability. See United States v. Burczyk, 389 F. Supp. 782 (E.D. Wis. 1975).

D. Fiduciary defenses to personal liability under 31 U.S.C. § 3713(b):

1. The fiduciary had no knowledge of a debt of the United States. Want v. Commissioner, 280 F.2d 777 (2d Cir. 1960). However, as noted above, informal notice may subject the fiduciary to liability. Viles v. Commissioner, 233 F.2d 376 (6th Cir. 1956).

2. The estate was solvent when each distribution was made.

3. The I.R.C. § 6502(a) collection period regarding the debt, as appropriately suspended, has expired.

4. The United States became a party to the proceeding by filing a proof of claim, and it received notices of distribution of assets or a final accounting, and did not object in a timely manner. See United States v. Muntzing, 69 F. Supp. 503 (N.D. W. Va. 1946); United States v. Pate, 47 F. Supp. 965 (W.D. Ark. 1942).

E. Fiduciary liability may be established through administrative procedures or through suit.

1. I.R.C. § 6901 provides the procedural method for the assessment and collection of a fiduciary's liability for income, estate and gift taxes in the same manner as the taxes themselves, i.e., through the deficiency notice procedures.

a. The statute of limitations for the assessment of a fiduciary's liability is: 1) one year after expiration of the statute of limitations for assessment against the taxpayer for liability; or 2) not later than the expiration of the period for collection of the tax in respect of which such liability arises, whichever is the later. I.R.C § 6901(a)(3). Issuance of a Notice of

Deficiency suspends the statute of limitations for the assessment of the fiduciary's liability for the period specified in I.R.C. § 6213(a).

2. A collection suit may be filed in court under I.R.C. § 7402(a). United States v. Motsinger, 123 F.2d 585 (4th Cir. 1941).

   a. Any suit filed to establish the liability must be instituted within the normal period for collection of the underlying tax.

3. In addition to the above remedies against a fiduciary, the United States may bring an action on the bond that is often required to be posted in an insolvency proceeding. The Government may also seek removal of the fiduciary for misconduct.

X. INSOLVENCY PROCEEDINGS

The insolvency proceedings most often encountered are receiverships, assignments for the benefit of creditors, corporate dissolutions, and insolvent decedents' estates.

A. Receiverships

1. A receivership usually has one of two purposes. It is either an ancillary proceeding designed to protect property until the principal proceeding is completed, or it is a proceeding for the liquidation of a debtor's assets for the payment of debts. Although the latter type is more common, the former is sometimes encountered in mortgage foreclosure proceedings in which the receiver operates a business as a going concern to preserve its value pending the foreclosure sale.

2. There are both general and limited receiverships. A general receivership is one in which the receiver takes control of all of the assets of the debtor. A limited receivership is one in which specific assets are in the custody of the receiver, or the proceeding is for the benefit of a specific creditor such as a foreclosing mortgagee.

3. A receivership is a type of proceeding which may come into operation for a number of reasons, and does not always involve insolvent debtors.

4. Receivership proceedings are encountered in both state and federal courts. The majority of the proceedings are brought in state courts

or informally under state law authorized proceedings. In those instances, state law should be examined closely for the authority of the court with respect to the debtor's property. Federal receiverships must be based on federal jurisdiction, such as:

a. Diversity of citizenship of the parties.

b. A debtor operating in several states.

c. A federal tax lien foreclosure filed under I.R.C. § 7403. Section 7403(d) provides that a court may appoint a receiver upon the request of the United States. The Government's suit letter in such a proceeding should request the appointment of a receiver where necessary for the collection, preservation, and orderly liquidation of the assets. See United States v. Florida, 178 F. Supp. 627 (E.D. Ark. 1959), aff'd, 285 F.2d 596 (8th Cir. 1961).

5. The I.R.C. § 6502(a) collection period is suspended for the period when all, or substantially all, of a taxpayer's assets are in the control or custody of the court, plus six months. I.R.C. § 6503(b). While assets are in custodia legis, levies are not effective, except on exempt or unclaimed assets. See United States v. Silverman, 859 F.2d 1352 (9th Cir. 1988), cert. denied, 493 U.S. 1036 (1990); Treas. Reg. § 301.6331-1(a)(3).

6. Claims for federal taxes in receivership proceedings are governed in part by the following procedures and rules:

a. I.R.C. § 6036 requires "every receiver, trustee in bankruptcy, assignee for the benefit of creditors, or other like fiduciary" designated by order of any court of the United States, or of any state or territory, in control of all or substantially all of the assets of a debtor or other party to the proceeding, to give notice to the Service within 10 days of the appointment.

b. In the case of income, estate and gift taxes, assessments are made as soon as possible after the receivership proceeding is initiated. I.R.C. § 6871(a). This is not a jeopardy assessment and the requirements pertaining to a jeopardy assessment, such as mailing a notice of deficiency, do not apply. However, the receiver is advised by Letter 1005(DO)(with a copy to the taxpayer) how the assessment was determined. Treas. Reg. § 301.6871(b)-1(c). Under this procedure the receiver has no access to the Tax Court.

c. As usual, a proof of claim may be filed in court. See Silverman, 859 F.2d at 1353. This filing of a claim is the basic method of collection during a general receivership because, where the assets of the taxpayer are under the jurisdiction of the court, the assets are not subject to levy. (Levy can be made on assets that are (1) not subject to receivership or (2) exempt from creditors under state law. Treas. Reg. § 301.6871(a)-2.) Bar dates are usually fixed by the state court or state law. However, the United States may not be bound by such state limitation, although it may be bound by state rules once it submits to jurisdiction by, for example, filing a claim. See United States v. Summerlin, 310 U.S. 414 (1940).

d. In a federal court receivership, the Government is to intervene and become a party to assert its claim. It is inadvisable to attempt to circumvent this requirement, because if the Government merely files a claim, it would probably not have standing to challenge what is done in the court proceeding, including the way money is distributed.

e. In a receivership action, a court does not have jurisdiction to make determinations of tax liability. In Sterling Consulting Corp. v. United States, 245 F.3d 1161 (10th Cir. 2001), cert. denied, 534 U.S. 1114 (2002), the Tenth Circuit held that the Declaratory Judgment Act, 28 U.S.C. § 2201(a), prohibits the district court from determining that the corporations in question owe no additional tax liabilities. Further, the court held that the Anti-Injunction Act, I.R.C. § 7421(a), bars the district court from enjoining the Service from assessing and collecting taxes for failure to evaluate tax returns by a court-imposed deadline.

f. Any portion of a claim for taxes allowed in a receivership proceeding that is not paid may be collected from the taxpayer after the proceeding. I.R.C. § 6873.

7. 28 U.S.C. § 959(a) states that receivers, trustees, or debtors in possession may be sued for any of their acts or transactions in carrying on the business or controlling the property of the debtor without leave of the court. 28 U.S.C. § 959(b) states that a receiver, trustee, or debtor in possession shall manage and operate the property in his/her possession in accordance with the laws of the state in which the property is located in the same manner that the owner

would be required to do if in possession. This section of the United States Code has had wide interpretation, and reference should be made to it in researching any specific receivership problem existing in the federal district courts.

8. Like a trustee in bankruptcy, a receiver stands in the place of the entities for which the receiver has been appointed and is only permitted to bring any claim in their place. Scholes v. Lehmann, 56 F.3d 750, 753-754 (7th Cir. 1995) (fraudulent transfer suit; receiver has power to sue on behalf of entities which participated in fraud once entity is no longer under spell of individual who ran fraud). See also SEC v. Holt, 2007 WL 2332584, at 2-3 (USDC D.Ariz. 2007); Stenger v. World Harvest Church, 2006 WL 870310, at 5-6 (N.D.Ga. 2006). Cf. Eberhard v. Marcu, 530 F.3d 122 (2d Cir. 2008).

9. Capacity to sue is related to but different than standing. Capacity has been defined as a party's personal right to come into court, and should not be confused with the question of whether a party has an enforceable right or interest or is the real party in interest. It concerns the personal qualifications of a party to litigate. Board of Educ. of City of Peoria, School Dist. No. 150 v. Illinois Bd. of Educ., 810 F.2d 707 (7th Cir. 1987). The capacity of a receiver appointed by a court of the United States to sue or be sued in a U.S. court is governed by 28 U.S.C. §§ 754 and 959(a). See Fed.R.Civ.P. 17(b).

10. Unfiled Pre-Receivership Tax Returns

a. The Service requests unfiled returns from receivers. See IRM 5.9.20.2(12). Receivers of all or substantially all of the assets of a debtor step into the shoes of the debtor and, after giving the required notice of fiduciary status, assume the powers, rights, duties, and privileges of the other person with respect to a tax imposed by the Code. See I.R.C. §§ 6036 and 6903(a); Treas. Reg. §§ 301.6036-1(a)(2) and 301.6903-1. Such receivers must file unfiled pre-receivership returns that the taxpayers themselves would have to file in the absence of the receiverships. See also I.R.C. § 6012(b)(2) and (3); Treas. Reg. §§ 1.6012-2, and -3.

b. The result is the same if the entity in receivership were a TEFRA or other partnership since a partnership is treated both as an aggregate of its partners who carry on their business in partnership form as well as a separate entity. See I.R.C. §§ 701 and 702. Because the partners are incapable of filing a partnership return, and the partnership return is deemed to be part of the partner's individual return, the receiver must file the partnership return for them. See Treas. Reg. § 1.702-1(c) (partners must compute gross income through reference to partnership return which is deemed to part of their own return).

11. Qualified Settlement Funds

a. Certain court-established receiverships should be treated as qualified settlement funds (QSFs) for purposes of I.R.C. § 468B and the underlying Treasury Regulations. QSFs are required to file an annual income tax return, Form 1120-SF, U.S. Income Tax Return for Settlement Funds. More information about QSFs may be found in Treasury Regulation §§ 1.468B-1 through -5.

b. Treas. Reg. § 1.468B-1(a) provides that a QSF is a fund, account, or trust that satisfies the requirements of Treas. Reg. § 1.468B-1(c). First, § 1.468B-1(c)(1) requires that the fund, account, or trust is established pursuant to an order of, or it is approved by, the United States, any state (including the District of Columbia), territory, possession, or political subdivision thereof, or any agency or instrumentality (including a court of law) of any of the foregoing and is subject to the continued jurisdiction of that governmental authority. Second, § 1.468B-1(c)(2) requires that the fund, account, or trust is established to resolve or satisfy one or more contested or uncontested claims that have resulted or may result from an event (or related series of events) that has occurred and that has given rise to at least one claim asserting liability (i) under the Comprehensive Environmental Response, Compensation and Liability Act of 1980; (ii) arising out of a tort, breach of contract, or violation of law; or (iii) designated by the Commissioner in a revenue ruling or revenue procedure. Third, § 1.468B-1(c)(3) provides that the fund, account, or trust must be a trust under applicable state law, or its assets must be otherwise segregated from other assets of the transferor (and related persons).

c. Section 1.468B-1(j)(1) provides that if a fund, account, or trust is established to resolve or satisfy claims described in § 1.468B-1(c)(2), the assets of the fund, account, or trust are treated as owned by the transferor of those assets until the fund, account, or trust also meets the requirements of § 1.468B-1(c)(1) and (c)(3). On the date the fund, account, or trust satisfies all the requirements of § 1.468B-1(c), the transferor is treated as transferring the assets to a qualified settlement fund.

d. Section 1.468B-2(k)(2) provides that a qualified settlement fund is in existence for the period that (i) begins on the first date on which the fund is treated as a qualified settlement fund under § 1.468B-1; and (ii) ends on the earlier of the date the fund (A) no longer satisfies the requirements of § 1.468B-1; or (B) no longer has any assets and will not receive any more transfers.

B. Assignments for the Benefit of Creditors

1. Assignments for the benefit of creditors are state law proceedings in which the debtor transfers his or her property to a person or trust to apply the property or the proceeds to the payment of debts. The statutory requirements for assignments for the benefit of creditors are created by state law. Generally, the assignments must be in writing. Such assignments usually are in the form of a document conveying title from the assignor to the assignee. As these assignments are essentially contracts, most states apply the requirements of contract law for a valid assignment. State law (particularly statutes) should be examined closely to determine also:

    a. Whether all assets must be assigned;

    b. Whether creditors must consent to the assignment; and

    c. What degree of court supervision is required. (There may be no requirement of court supervision.)

2. An assignment for creditors connotes liquidation of the property and distribution of the proceeds among the creditors. For example, if the assets were placed in trust for the benefit of creditors, but the debtor remained in possession in an effort to reorganize its affairs, then there is no assignment. United States v. Gargill, 218 F.2d 556 (1st Cir. 1955). But see Rev. Rul. 56-592, 1956-2 C.B. 945.

3. Under most state laws, a valid assignment for creditors vests the legal title in the assignee and places the property beyond the control of the assignor, or the reach of any of his/her creditors, beyond their rights under the assignment to share in the distribution of the assigned property. However, the rights of the Government are not necessarily governed by the effect of the state law. Normally under state law, the assignee takes title of the assigned property as a

trustee, and in general, his/her duties, powers and liabilities are those of a fiduciary.

4. 31 U.S.C. § 3713(a)(1)(A)(i) gives a federal claim first priority of payment when a debtor is insolvent and makes a voluntary assignment of property. This provision has been liberally interpreted in the interests of raising revenue. United States v. Moore, 423 U.S. 77, 81-82 (1975); United States v. Cole, 733 F.2d 651, 654 (9th Cir. 1984). Because federal taxes have first priority, an assignee for the benefit of creditors may be held personally liable for the taxes if he satisfies other creditors before paying them. Chambers v. United States, 71-1 U.S.T.C. par. 9412 (N.D. Cal. 1971).

5. If the court maintains supervision over the assignment, the proceeding resembles a receivership. In such a situation, the property is in custodia legis and the Government cannot take levy action without the permission of the court. Furthermore, the statute of limitations will be suspended during the period the taxpayer's assets are in the custody of the court. I.R.C. § 6503(b).

6. The following should be remembered concerning claims for federal taxes:

   a. Immediate assessments under I.R.C. § 6871(a) should be made in court-supervised proceedings in which the court can rule on the validity of claims. See Williams v. Commissioner, 44 T.C. 673 (1965), acq., 1966-2 C.B. 4, and acq., 1966-2 C.B. 7. See also the discussion of claims in receivership proceedings set forth above.

   b. If there is no court proceeding, the Government must give notice of the taxes and amounts to the assignee, reminding him of 31 U.S.C. § 3713. The Government can prove knowledge of the tax liability by showing it gave such notice.

7. As in the case of receiverships, not all tax claims are governed solely by 31 U.S.C. § 3713. If the Government has a lien claim, it can rely on the lien which takes priority over the title of the assignee. The assessment date of the tax is the key date in determining whether the Government has a lien effective against the assignee. See I.R.C. §§ 6321, 6322, 6303. If a general assignment for the benefit of creditors is made prior to the assessment of taxes, which assignment includes all property of the taxpayer, there would be no property to which the lien could attach, as all the taxpayer's property rights have passed to the transferee. Engleman v. Commodity Credit Corp.; 107 F. Supp. 930 (S.D. Calif. 1952); Sisk v. United

States, 61-1 U.S.T.C. ¶ 9476 (N.D. Okla. 1961). At this point, the Government must then rely upon 31 U.S.C. § 3713(a) and (b).

C. Decedents' Estates (Administrative Collection after Death of Taxpayer)

1. A lien perfected prior to the death of the taxpayer against property of the taxpayer continues after the taxpayer's death as the property passes encumbered with the lien. United States v. Bess, 357 U.S. 51, 57 (1958); United States v. Hoper, 242 F.2d 468 (7th Cir. 1957); United States v. Lawrence, 327 F. Supp. 650 (N.D. Tex. 1971).

2. Administrative collection can be pursued against the decedent's property if (i) the lien arose upon assessment of the tax prior to the time title to the property passed to heirs, devisees or legatees (which time is generally at the moment of death), and (ii) if the property is not in custodia legis (as where there is no probate proceeding or where administration of the estate is independent of a court, as is permitted in some states). See I.R.C. §§ 6321 and 6322; Treas. Reg. § 301.6331-1(a).

3. The decedent's heirs, devisees or legatees do not fall within any of the preferred categories of I.R.C. § 6323. Accordingly, assuming that estate assets are not within the custody of the court, the Government may levy upon such property in their hands whether or not a notice of tax lien has been filed. However, the filing of a tax lien may be necessary to perfect the tax lien against the claims of other creditors of the decedent or against purchasers of property sold to pay the decedent's debts.

4. An assessment made following the death of a taxpayer would attach to any property of the taxpayer’s estate. Thus, if all of the estate property has been distributed at the time of assessment, there would be nothing to which a lien could attach when it arose. In that case, the Government must pursue collection through probate proceedings or through transferee remedies.

5. All property in which the decedent had an interest prior to his death but in which his interest terminated at or prior to his death is not subject to probate administration and, therefore, not subject to the jurisdiction of the court. Examples of this type of property are jointly held property with the right of the survivor to take the entire property, proceeds from life insurance policies, and property held in trust for another.

6. Levying on assets to which the federal tax lien attached prior to

death requires permission of the court if the assets are in the custody of the court. However, federal estate taxes can be collected by levy and sale of "nonprobate" assets that were includable in the gross estate under I.R.C. §§ 2034-2042. I.R.C. § 6324(a).

7. In addition to federal law, state law requires the executor or administrator to pay liabilities. Taxes are usually high on the state law priority list. Note, however, that the priority of payment is determined by federal rather than state law. When part of the gross estate is used for the payment of the charges against the estate and the expenses of administration allowed by the court having jurisdiction over the estate, the estate tax lien is discharged or divested from the property so used. I.R.C. § 6324(a)(1). Administrative expenses are included within the scope of the divestment, as is the estate tax itself. For the estate tax lien to be discharged or divested for administration expenses or estate charges, however, I.R.C. § 6324(a)(1) requires that a court order be obtained approving estate expenses, regardless of whether the probate administration is subject to direct court supervision. Absent court approval, payment of estate expenses does not discharge the lien and estate fiduciaries therefore risk personal liability. See Kleine v. United States, 539 F.2d 427 (5th Cir. 1976).

8. The statute of limitations for collection is suspended under I.R.C. § 6503(b) while the decedent's assets are under the control or custody of a court. See United States v. Silverman, 859 F.2d 1352 (9th Cir. 1988), cert. denied, 493 U.S. 1036 (1990).

9. I.R.C. § 6871 is not applicable. If there is an estate tax deficiency, or if income or gift taxes have not been assessed prior to the decedent's death, the fiduciary for the estate receives a statutory notice of deficiency, which he can petition to the United States Tax Court. I.R.C. § 6212(b). Jeopardy provisions are available, when applicable.

10. For an estate, the priority statute of 31 U.S.C. § 3713 applies when the assets of the estate, "in the custody of the executor or administrator, is not enough to pay all debts of the debtor." Since property passing outside of probate (e.g., life insurance payable to someone other than the executor/decedent's estate, jointly held property, or property subject to a power of appointment) is not considered here, the estate for this purpose is the probate estate. (However, the estate does include any claims of the executor against holders of property to pay the tax liability. Under I.R.C. §§ 2206 and 2207, the executor has the right to compel contributions

toward the estate tax from life insurance recipients and property subject to a power of appointment, which are included in the gross estate.)

D Corporate Dissolutions and Insolvencies

1. Corporations, being artificial creations of the state, may be dissolved by several methods, such as by expiration of the charter, by merger and consolidation, or by surrender or forfeiture of the charter by either the stockholders or the state (usually for nonpayment of franchise taxes). Corporations may also be dissolved by dissolution proceedings. These proceedings may be judicial (conducted through a court-appointed receiver or other fiduciary), or nonjudicial (frequently conducted by corporate officials pursuant to statutes). In the latter situation, if the Government's interest is not being protected, a lien foreclosure suit under I.R.C. § 7403 should be filed, asking for a receiver if necessary.

2. Lien priorities and priority under 31 U.S.C. § 3713 are determined as in other insolvencies.

3. In judicial proceedings, the Government should intervene or file a proof of claim. In nonjudicial proceedings, the Government can levy upon the corporate assets if it has a lien claim.

4. In corporate dissolution cases, the Government can also collect taxes through assertion of transferee liabilities, through suits to set aside fraudulent conveyances, and through trust fund recovery penalty procedures.

5. Of growing interest is the application of personal liability to corporate officers, directors and shareholders who act to avoid the federal tax liability of a financially shaky corporation. Courts have extended personal liability to those in control of a corporation's affairs at a time when preferential payments are made and the corporation is insolvent. <u>See</u> <u>Lakeshore Apartments, Inc. v. United States</u>, 351 F.2d 349 (9th Cir. 1965); <u>United States v. Coyne</u>, 540 F. Supp. 175 (D. D.C. 1981); <u>In re Gottheiner</u>, 3 B.R. 404 (Bankr. N.D. Cal. 1980). In <u>United States v. Spitzer</u>, 261 F. Supp. 754 (S.D.N.Y. 1966), the Government broadened its argument to reach the officers, directors and stockholders who either directed or controlled wrongful payments, or knew of the payments from the corporation and failed to stop them. The court also stated that no statute of limitations applied to the claim brought under 31 U.S.C. § 3713(b).

XI. PROOFS OF CLAIM

A proof of claim (Form 4490) contains the following information:

1. The taxpayer's name and taxpayer identification number;

2. The kinds of taxes claimed, including class and taxable period;

3. The amounts of the taxes;

4. The date any liens arose or were perfected (assessment dates, lien notice filing dates);

5. Interest and penalties;

6. Notice to the fiduciary of liability under 31 U.S.C. § 3713 (formerly 31 U.S.C. §§ 191, 192).

A. Advantages

There are several advantages to the United States in the proof of claim procedure. The procedure--

1. Provides notice to the fiduciary of the Government's claim. Thus, one prerequisite for the assertion of liability against the fiduciary under 31 U.S.C. § 3713 is fulfilled.

2. May avoid unnecessary active litigation.

3. Avoids the necessity of tracing assets to collect taxes by levy or through transferee proceedings.

4. May, as Rev. Rul. 70-555, 1970-2 C.B. 296 holds, constitute the commencement of a "proceeding in court," thus tolling the statute of limitations, at least with regard to the assets in the proceeding. But see United States v. Silverman, 859 F.2d 1352 (9th Cir. 1998), cert. denied, 493 U.S. 1036 (1990). Also, note United States v. Saxe, 261 F.2d 316 (1st Cir. 1958), where, as to state probate court proceedings and based on the law of a particular state, it was held that the filing of a proof of claim did not constitute the commencement of a proceeding in court. In light of the adverse decisions, the Service should take care to protect the normal statute of limitations.

5. Generally results in the Internal Revenue Service getting notice of hearings, etc.

B. Disadvantages

There are also disadvantages to the Government in the proof of claim procedure.

The procedure:

1. Subjects the United States to the jurisdiction of the state court, probably for all purposes, see United States v. Pate, 47 F. Supp. 965 (W.D. Ark. 1942), although the Government does not necessarily agree with this view. A probate ruling on a formal Government claim has been held to be the final word in the disposition of that claim. United States v. Muntzing, 69 F. Supp. 503 (N.D.W.V. 1946); United States v. Pate, 47 F. Supp. 965 (W.D. Ark. 1942). The United States may attempt to withdraw the claim if already filed. This procedure is questionable because the court might find that the United States had already submitted itself to the jurisdiction of the court.

2. May result in the state court adjudicating the merits of the claim. But see P.C. Monday Tea Co., 29 Wis. 2d 372, 139 N.W.2d 26, 66-1 U.S.T.C. ¶ 9306 (Wis. 1966).

3. May delay collection due to an extended state court proceeding.

C. Alternatives

There are alternatives to filing a proof of claim which avoid a decision on the merits of the tax.

1. The Government can advise the fiduciary of the tax debt due the United States and rely on 31 U.S.C § 3713.

2. The Government can proceed to judgment in federal court before filing a claim (if time permits). I.R.C. § 7402(a). It should be noted that the statute of limitations on collection of the underlying tax is satisfied if the tax liability has been reduced to judgment prior to the collection statute expiration date. I.R.C. § 6502(a); United States v. Rose, 227 F. Supp. 259 (E.D. Pa. 1964), aff'd, 346 F.2d 985 (3d Cir. 1965).

3. The Government can assert transferee liability against the recipients of the assets.

D. Bar Dates

The United States is not bound by state statutes of limitations.

United States v. Summerlin, 310 U.S. 414 (1940). However, the Government should attempt to meet the state bar date if possible in order to avoid unnecessary litigation concerning the validity of its claim. Once the Government has filed a claim, it arguably has submitted to the jurisdiction of the state court so as to be subject to and bound by the state court rules and procedures.

E. Penalties And Interest

The rules for penalties and interest on proofs of claim are different in insolvencies and decedents' estates than in bankruptcy.

1. Interest and penalties are part of the absolute priority claim under 31 U.S.C. § 3713. See County of Spokane v. United States, 279 U.S. 80 (1929); Jobbers Credit Ass'n v. United States, 164 F. Supp. 22 (E.D.N.Y. 1958).

2. Generally, in state court insolvency proceedings, a creditor can claim interest to the commencement date of the proceedings and can claim all penalties. See Lapadula & Villani, Inc. v. United States, 563 F. Supp. 782 (S.D.N.Y. 1983). An exception to the general rule with respect to interest is that interest accruing after commencement of the proceedings can be claimed if the Service has a lien and its claim is oversecured, at least to the extent that the value of the property exceeds the underlying tax liability. See Rev. Rul. 87-99.

   In state court proceedings other than insolvencies (e.g., decedents' estates), penalties plus interest to date of payment are claimed. I.R.M. 5.5.4.6.1.1. But see United States v. Sullivan, 254 F. Supp. 254 (D. R.I. 1966), holding that in an insolvent decedent's estate, interest can only be claimed to the date of appointment of a fiduciary. The court viewed the insolvent estate as analogous to a bankruptcy estate or a receivership for which "[t]he general rule... is that interest ceases to accrue on the debtor's obligations at the beginning of the proceedings." Id. at 256. See also Atlantic Metal Prods., Inc. v. United States, 398 N.Y.S.2d 737 (N.Y. S. Ct. App. Div. 1977) (post-assignment interest on preassignment tax liability disallowed when assets were insufficient to pay all creditors; same rule applies to tax penalties accruing solely because of the delay in paying the tax liabilities incurred prior to the assignment); Pavone Textile Corp. v. Bloom, 97 N.E.2d 755 (N.Y. Ct. App. 1951), aff'd sub nom. United States v. Bloom, 342 U.S. 912 (1952) (interest accruing after assignment for benefit of creditors not afforded priority). Contra, In re T.J. Simpson, Inc., 258 A.D. 148, 15 N.Y.S.2d 1021 (N.Y.S. Ct. App. Div. 1939) (viewing Supreme Court decision in County of Spokane as holding that interest and penalties on taxes are "debts" afforded priority by priority statute).

3. The failure to pay penalty imposed by I.R.C. § 6651(a)(2) may be claimed in insolvency proceedings.