UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

In re

QUID ME BROADCASTING, INC.,

Debtor.

95-CV-0387E(M)
89-BK-12649K

MEMORANDUM
and
ORDER

In this bankruptcy appeal, the appellant ("the IRS") challenges an April 5, 1995 Order ("the Order"), signed by Chief Judge Michael J. Kaplan of the United States Bankruptcy Court for the Western District of New York. *In re Quid Me Broadcasting, Inc.,* 181 B.R. 715 (Bankr. W.D.N.Y. 1995). Before Judge Kaplan, the Chapter 7 trustee had objected to an administrative expense claim made by the IRS for $31,613.01, which represented interest on what was ultimately determined to be a "non-existent [tax] liability in a non-operating Chapter 7 case." The Order, at 10. This appeal presents an issue of first impression, which the appellant has dissected and phrased as follows:

> "A. Whether a Chapter 7 bankruptcy trustee has a statutory duty to pay administrative expense taxes when due, pursuant to 28

This Court has jurisdiction over this appeal pursuant to 28 U.S.C. §158(a). It will not set aside facts found below unless such are clearly erroneous; legal conclusions reached below are reviewed *de novo*.

The facts are not in dispute. The debtor-appellee ("Quid Me") had at one time operated a radio station in Buffalo, N.Y. under the call-letters WECK. In July 1989 Quid Me sold the station and its assets, the consideration for such sale including an unsecured promissory note ("the note") whereby $600,000 was to be paid over to Quid Me by the purchaser. On October 26, 1989 Quid Me filed a Chapter 7 bankruptcy petition. The trustee thereafter timely filed a tax return for the calendar year 1989 showing an income tax due in the amount of $88,394, with most of such liability arising from the capital gain realized from the pre-petition sale of the station. The trustee had at his disposal approximately $30,000 in Quid Me's account. Thus lacking sufficient assets and wanting to administer the entire estate at once, the trustee did not pay the taxes when he filed the return and requested prompt assessment thereof under 11 U.S.C. 505(b).[4] The return was accepted as filed. Pertinently, the IRS did

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[4] Subsection 505(b) states, in part:

> "A trustee may request a determination of any unpaid liability of the estate for any tax incurred during the administration of the case by submitting a tax return for such tax and a request for such a determination to the

(continued...)

Such would appear to have wiped the slate clean, but on November 27, 1994 the taxman requested the Bankruptcy Court to order payment of what it asserted was a Chapter 7 administrative expense, representing $31,613.01 in interest on this former-but-then-extinguished tax liability. *See* 11 U.S.C. §503.[5] The trustee objected to this claim, asserting that the underlying tax imposed upon the capital gain from the sale of the radio station had been incurred pre-petition and thus was *not* "any tax *** incurred by the estate." 11 U.S.C. §503 (*see* footnote 5 hereto). The IRS asserted in reply that, because the bankruptcy petition had been filed during the tax year in question and thus a return reflecting such would necessarily have been filed post-petition -- to wit, March 15, 1990 --, "all income tax liabilities for that year are considered post-

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[5] Section 503 was amended effective October 22, 1994. Such amendments are not applicable to bankruptcy cases commenced prior to the effective date of such amendments. 11 U.S.C. §503 (Supp. 1995)(Note). Section 503, prior to such amendments, stated, in part:

> "(a) An entity may file a request for payment of an administrative expense.
>
> "(b) After notice and a hearing, there shall be allowed, administrative expenses *** including--
>
> (1)(A) the actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case;
>
> (B) any tax--
>
> (I) incurred by the estate ***."

This issue was rephrased in the Order as:

> "whether a Chapter 7 trustee who is not an 'operating' trustee according to 11 U.S.C. § 721 is obligated to pay to the I.R.S. administrative expense taxes when they are due, or whether such tax payments must (in the absence of a court order) await complete administration of the bankruptcy estate and subsequent distribution under 11 U.S.C. § 726 and Bankruptcy Rule 3009."

The Court below continued, stating that it

> "need not address the question of whether administrative expense interest accrues on administrative tax liabilities, because in this case the Internal Revenue Service agrees with the amended tax returns which conclude that there is no underlying administrative tax liability in light of subsequent events. Put simply, the issue is whether it is the bankruptcy estate or the I.R.S. that was entitled to the use of the $88,394 while the trustee was performing his duty to 'collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest." The Order, at 2-3 (citing 11 U.S.C. §704(1) (duties of the trustee)).

Judge Kaplan also noted that, had the Trustee exhausted the bankruptcy estate's $30,000 coffer and immediately paid a portion of the $88,394 tax liability when the 1989 tax return was filed, the estate would still have had a large and looming tax deficiency as well as no funds to cover other administrative expenses (*e.g.*, "the wages of watchmen," insurance premiums,

> "**General rule.**--Except as otherwise provided in this subchapter, when a return of tax is required under this title or regulations, the person required to make such return shall, without assessment or notice or demand from the Secretary, pay such tax to the internal revenue officer with whom the return is filed, and shall pay such tax at the time and place fixed for filing the return ***."

There appears to be no dispute that the trustee would have had to pay any due taxes upon his administration of the estate in accordance with the Bankruptcy Code. The dispute herein -- being further focused and seemingly unique because of the extinguished tax liability and the extant claim for interest -- is whether the duty to remit arises upon the filing of the return or upon order of the Bankruptcy Court?

The Court below noted that the "[g]eneral rule" of 26 U.S.C. §6151(a) "does not specifically deal with trustees or fiduciaries and is inconsistent with provisions of the Bankruptcy Code that more specifically govern trustees' duties and responsibilities." The Order, at 7. The Bankruptcy Court correctly reasoned that, because the Bankruptcy Code specifically addresses the responsibilities of trustees and the process the IRS has to follow in order to claim an administrative expense, the more specific provisions of the Bankruptcy Code take precedence over the general rule stated in subsection 6151(a) of the

> "In the absence of express approval by the Bankruptcy Court of specific expenses, or general approval by the Court in the form of an order permitting operation of the Debtor or other similar blanket authority to pay expenses in the ordinary course of administration, there is no provision of the Bankruptcy Code or Rules that would permit, let alone require, the trustee to disburse funds of the estate as the I.R.S. demands." *Id.* at 9-10.

Because the IRS failed to seek an Order allowing the $88,394 tax liability when it arose, the duty to remit such could not have arisen prior to November 27, 1994 when the IRS did make such a claim. By that time, the tax liability was zero and, hence, so was the interest expense. Under the facts of this case, the "duty to remit" arises when the claim is allowed by the court.

The arguments posed by the IRS to this Court do not convince that a contrary result should attach on this appeal. The cases it cites are inapposite; they do not address the timing-of-payment issue. They also do not address the facts of this case -- a non-operating Chapter 7 trustee with insufficient funds in the estate. *In re I.J. Knight Realty Corp.*, 501 F.2d 62 (3d Cir. 1974), cited by the IRS, is a pre-Bankruptcy Code case that was not governed by the notice and hearing provisions of 11 U.S.C. §503. *Holywell Corporation* v. *Smith*, 503 U.S. 47 (1992), also cited by the IRS, addressed the duty of an "assignee" to file income tax returns and pay taxes due thereunder under Chapter 11 of the

Accordingly, it is hereby ***ORDERED*** that the decision of the Bankruptcy Court is affirmed.

DATED: Buffalo, N.Y.

May 15, 1996

John T. Elfvin

U.S.D.J.