

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:) CASE NO. BK02-81632-TJM
)
M & S GRADING, INC.,) CH. 7
)
Debtor(s).)

ORDER

This matter is before the court on Filing #909, Motion to Reconsider and for Findings of Fact and Conclusions of Law Under FRCP 52, filed by Contractors, Laborers, Teamsters and Engineers Health and Welfare Plan; Contractors, Laborers, Teamsters and Engineers Pension Plan; and Operating Engineers Local No. 571; Filing #924, Objection to Motion for Reconsideration and for Findings of Fact and Conclusion of Law Under FRCP 52, filed by Trustee James Killips. T. Randall Wright and Stacy Hines represent James Killips, the Chapter 7 Trustee of M & S Grading, Inc.; M. H. Weinberg represents Contractors, Laborers, Teamsters and Engineers Health and Welfare Plan, Contractors, Laborers, Teamsters and Engineers Pension Plan and Local 571 International Union of Operating Engineers.

The court recently entered an order at Filing #908 on a Motion to Compel filed by creditors Contractors, Laborers, Teamsters and Engineers Health and Welfare Plan; Contractors, Laborers, Teamsters and Engineers Pension Plan; and Local 571 International Union of Operating Engineers. That motion requested an order directing the Chapter 7 trustee to file a report concerning funds withheld from the employee wages but not turned over to the Internal Revenue Service. The court denied the motion, finding that the First National Bank of Omaha had a lien on all property of the bankruptcy estate and that lien had been determined by this court and the appellate court to have priority over any claims by the plans concerning mandatory contribution under ERISA to the plans.

A motion to reconsider has now been filed in which the plans and the local union clarify that the motion is not directed at recovering funds to contribute to the plans under ERISA, but is directed at the opportunity to attempt to proceed against third parties who received funds withheld from the checks of the men for taxes. The statutory provision for this motion is 29 U.S.C. § 185, et seq.

Apparently, the movants desire to attempt to trace the funds withheld from the checks of the men to attempt to recover the monies and use the recovered funds to pay the Internal Revenue Service and the Nebraska Department of Revenue for the unpaid taxes. Those two entities have filed claims in the case. Those claims have administrative priority equal to the administrative priority of the unpaid mandatory contributions and ancillary damages. Without recovery of the funds and payment of the taxes, the IRS claim reduces the recovery from estate assets for the plans.

The federal and state tax statutes and regulations provide that the men receive credit for the amounts withheld from their checks, even though the amount was not paid over to the IRS. See 26 U.S.C. § 31(a), Treasury Reg. § 1.31-1 (26 C.F.R. § 1.31-1) and Neb. Rev. Stat. §§ 77-2755 and 48-652(5). Because of that, neither the Internal Revenue Service nor the Nebraska Department of Revenue are looking to the men for additional funds.

The motion to reconsider is denied. The First National Bank of Omaha had a security interest in all of the accounts and other assets of the debtor. The monies in the accounts do not

become property of the employees simply because officials of the debtor made entries on the payroll records showing that tax withholding occurred. The men received checks representing the net amount of their earned wages and the receipt of those checks transferred the net amount of the wages from the ownership of the debtor to the ownership of the men. Until there was an actual transfer, by electronic means or otherwise, of the monies shown as withheld for tax purposes, the perfected security interest of the First National Bank of Omaha gave that bank a first priority lien on the money in the accounts. 26 U.S.C. § 6323(a); JP Morgan Chase Bank, N.A. v. Zwosta (In re Zwosta), 395 B.R. 378, 385-86 (B.A.P. 6th Cir. 2008) (the trust imposed on withheld funds dissipates when those funds are paid to other creditors, and the imposition of the trust in after-acquired funds is subject to the pre-existing interest of a secured creditor in those funds) (relying on Slodov v. United States, 436 U.S. 238 (1978)). The money did not become property of the men, or of the taxing authorities, while remaining commingled with other funds in the accounts. The failure of the officials of the debtor to deliver the funds represented as “withheld” to the IRS through the special tax account at the First National Bank of Omaha was a breach of fiduciary duty to the men, a breach of the post-petition contract among the debtor, the IRS and the First National Bank of Omaha, and, probably, a violation of the tax laws of the United States and the State of Nebraska. However, that failure to pay the IRS does not give rise to a claim by the debtor, the trustee, or the movants against the First National Bank of Omaha or any other recipients of funds paid by the debtor from its general accounts.

Since the ultimate aim of the movants is to go after such recipients, and since there is no legal basis for a claim against the recipients, there is no need for the trustee to spend time and estate funds attempting to reconstruct the books and records of the debtor to generate a report as requested by the movants.

IT IS ORDERED that the Motion to Reconsider, Filing #909, is denied.

DATED: August 17, 2009

BY THE COURT:

/s/ Timothy J. Mahoney
Bankruptcy Judge

Notice given by the Court to:
T. Randall Wright
Stacy Hines
*M. H. Weinberg

Movant (*) is responsible for giving notice to other parties if required by rule or statute.