IN THE UNITED STATES DISTRICT COURT FOR THE

DISTRICT OF NEBRASKA

IN THE MATTER OF:

THOMAS C. BROWN and
MARTHA T. BROWN,

Debtors.

UNITED STATES OF AMERICA on behalf of the Internal Revenue Service,

Appellant,

v.

THOMAS C. BROWN, et al.,

Appellees.

CV. 87-0-580

BK. 87-869

MEMORANDUM AND ORDER

This matter is before the Court on the United States' appeal of the Bankruptcy Court's order of July 22, 1987. The Bankruptcy Court overruled the objection of the United States to the Chapter 13 Plan of Thomas C. Brown and Martha T. Brown (hereinafter debtors). Debtors filed a voluntary petition and plan under Chapter 13 of the Bankruptcy Code on March 19, 1987. The plan directed that payment to the Internal Revenue Service (hereinafter IRS) be "applied first to interest." The United States, on behalf of the IRS, objected to this designation.

It is generally recognized, and the parties agree, that the taxpayer may designate how "voluntary" payments to the IRS are allocated, but not how "involuntary" payments are allocated. **In re Ribs-R-Us, Inc.**, 828 F.2d 199, 201 (3d Cir. 1987); **United States v. A & B Heating & Air Conditioning, Inc.**, 823 F.2d 462,

463 (11th Cir. 1987); **Muntwyler v. United States,** 703 F.2d 1030, 1032 (7th Cir. 1983). Therefore, the sole issue is whether payments made to the IRS under a Chapter 13 plan are to be considered voluntary or involuntary.

"An involuntary payment of Federal taxes means any payment received by agents of the United States as a result of distraint or levy or from a legal proceeding in which the government is seeking to collect its delinquent taxes or file a claim therefor." **Amos v. Commissioner,** 47 T.Ct. 65, 69 (1966). At least one court has used this definition to hold that a payment made to the IRS under a Chapter 13 plan is involuntary. **In re Frost,** 47 B.R. 961 (D.Kan. 1983). In **Frost,** the Court reasoned:

> The instant bankruptcy proceeding filed by the debtors is a legal action in which the IRS has filed a claim for delinquent taxes. The payments to be made by the debtors are under the Bankruptcy Court's jurisdiction and are made pursuant to a plan which must comply with the requirements of the Bankruptcy Code. Thus, we conclude that payments made by debtors to the IRS are not voluntary and the IRS has the right to allocate the payments as it sees it.

Id. at 65. This decision was based primarily on the decision in **Muntwyler v. United States,** 703 F.2d 1030 (7th Cir. 1983) (payments made under Chapter 11 plan held to be involuntary), where the court determined that an "involuntary payment [is] one made pursuant to a judicial action or some form of administrative seizure, like a levy." **Id.** at 1033.

While the reasoning in **Muntwyler** and **Frost** may appear to be sound, this Court respectfully declines to follow it. There is a recognized split by the courts on the issue of whether payments made under a bankruptcy plan are voluntary or involuntary. Some courts have adopted a **per se** rule that such payments are involuntary. **See, In re Technical Knockout Graphics, Inc.**, 833 F.2d 797 (9th Cir. 1987); **Matter of Ribs-R-Us, Inc.**, 828 F.2d 199 (3d Cir. 1987); **Muntwyler v. United States**, 703 F.2d 1030 (7th Cir. 1983); and **In re Frost**, 47 B.R. 961 (D.Kan. 1985). However, it is those cases which have decided this issue on a case-by-case basis which the Court finds more persuasive.

Court involvement should not be the sole determinate factor in deciding whether a payment is voluntary or involuntary. "[Each] debtor finds himself in his own unique set of circumstances which may often dictate the degree of court involvement required for that particular case. The pronouncement of a **per se** or inflexible rule would not permit the court to consider individual situations." **Hineline v. Household Finance Corp.**, 72 B.R. 642 (N.D.Ohio 1987)(payments made under Chapter 11 plan held to be voluntary). "[T]he allocation question should be left to judicial discretion to be decided on a case-by-case basis and analysis with the burden of proof being on the trustee or debtor-taxpayer to demonstrate exceptional or special circumstances or equitable reasons warranting such allocation." **In re B & P Enterprises, Inc.**, 67 B.R. 179, 183 (W.D.Tenn. 1986)(footnote omitted)(IRS allowed to designate the manner of

allocation of payments received in a Chapter 11 bankruptcy). "The question should be considered in light of, **inter alia**, the structure and general purposes of both the Internal Revenue and bankruptcy laws." **Id.** at 183-84. "Bankruptcy courts should look closely at the totality of the pre- and post-bankruptcy facts and circumstances before allowing (or disallowing) such allocation." **Id.** at 184.

In that context, the bankruptcy court should consider the history of the debtor, the absence or existence of pre-bankruptcy collection or "enforcement collection measures" of the I.R.S. against the corporation and responsible corporate officers; the nature and contents of the [plan] . . . the presence, extent and nature of administrative and/or court action; the presence of pre- or post-bankruptcy agreement between the debtor (or trustee) and the I.R.S.; and the existence of exceptional or special circumstances or equitable reasons warranting such allocation. **Id.** "Most importantly, the bankruptcy judge should consider whether the proposed plan is merely a stop gap scheme to hold the taxing authority at bay with little chance that the debtor will fulfill its obligation under the plan." **Matter of A & B Heating & Air Conditioning,** 823 F.2d 462, 466 (11th Cir. 1987)(case remanded to the district court with directions that the bankruptcy court weigh the impact of the proposed allocation upon the debtor, the IRS, and other creditors). "Should the bankruptcy court conclude that the

interest f all parties would be best served by allowing the debtor to allocate the payment of taxes, then that determination should stand in the absence of abuse of discretion." Id.

There has been no showing of abuse of discretion by the Bankruptcy Court. Whether a debtor may designate how payments to the IRS are allocated under a Chapter 13 plan should be decided on a case-by-case basis. In the present case, it is clear that the allocation by debtors was done in an attempt to take advantage of legally allowable interest deductions on future income tax returns. These deductions will be helpful to debtors in their attempt to fulfil their obligations, both under the plan and outside the plan. The United States does not dispute that the IRS will be paid in full no matter how the payments are allocated. Thus, it appears that the purposes of the Bankruptcy Code will be better served in this case if the debtors' planned allocation is adopted. Therefore, there are special circumstances and equitable reasons warranting the allocation made by debtors. Accordingly,

IT IS ORDERED that the Bankruptcy Court's order of July 22, 1987, is affirmed.

DATED this 11th day of February, 1988.

BY THE COURT:

LYLE E. STROM, Chief Judge
United States District Court