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Federal Tax Liens In Bankruptcy

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between a union and an employer providing for mandatory retirement with a pension be construed as not providing for pension payments while the employer is also liable for unemployment compensation. Of course an employer could probably provide effectively for this as a term of the employment contract.

Yet another solution would be a judicial ruling, whether or not pursuant to a statute, which would allow substitution of benefits already being received by the employee in lieu of payment of unemployment compensation. Possible substitutions are the pension and either the half of the social security paid by employers for the employee's benefits or the entire amount of social security receivable by the employee. The problem of the waiver section of the applicable unemployment compensation statute would have to be solved and might, as in *Marcum*, be accomplished by holding that the employee has no right to unemployment compensation.

The foregoing propositions are not ultimate answers; they are, however, an attempt to balance the equities of the situation and are submitted as a guide for jurisdictions considering the problem. But an answer should be sought, preferably by the legislatures, which would allow employers and the employees to know in advance how the provisions of employment contracts providing for mandatory retirement with a pension for a retiring employee will be construed. With such prior knowledge, employers could protect themselves from a double financial burden, and employees would know how their retirement would affect the assumed right to apply for unemployment compensation when there is inability to find immediate employment after mandatory retirement.

JAMES F. DOUTHAT

FEDERAL TAX LIENS IN BANKRUPTCY

An important policy of the Bankruptcy Act is to achieve pro rata distribution among all creditors of the bankrupt.¹ The general order of distribution of the bankrupt estate is:

I. Secured claims.² Claims of creditors who have security for their debts upon property of the bankrupt.³

¹See 3 Collier, Bankruptcy § 64.02, at 2058 (14th ed. 1964) [hereafter cited as Collier].

²The right of a secured creditor is technically a property right rather than a claim against the bankrupt estate. MacLachlan, Bankruptcy § 150 (1956) [hereafter cited as MacLachlan].

³Bankruptcy Act § 1 (28), 52 Stat. 840 (1938), 11 U.S.C. § 2 (28) (1964).

II. The General Bankrupt Estate.

A. Unsecured priority claims. Claims given priority by the Bankruptcy Act.⁴

These in order of priority are:

1. General expenses of administering the bankrupt estate.
2. Wages and commissions of employees of the bankrupt earned within 3 months before bankruptcy not to exceed \$600 per claimant.
3. Expenses of creditors incurred in the successful opposition to a discharge or in adducing evidence resulting in the conviction of any person of a bankruptcy offense.
4. *Unsecured* federal, state, and local tax claims.
5. Debts owing to any person including the United States, entitled to priority under any federal statute and rent within certain limitations entitled to priority under applicable state law.

B. Unsecured general claims. Dividends to general unsecured creditors.⁵ [Bracketed numerals and letters used hereafter refer to this outline.]

The Internal Revenue Code provides that the federal government acquires a lien for taxes on all property of any taxpayer liable for such taxes when it makes a demand for payment and the taxpayer neglects or refuses to pay.⁶ There is no practical way to discover the existence of this secret lien, but to alleviate some of its harshness Congress has provided in § 6323 of the Internal Revenue Code that the lien is not valid against a "mortgagee, pledgee, purchaser, or judgment creditor" until notice of the lien is recorded.⁷

⁴§ 64a, 52 Stat. 874 (1938), as amended, 11 U.S.C. § 104a (1964); See MacLachlan §§ 150-55.

⁵Bankruptcy Act § 65a, 52 Stat. 875 (1938), 11 U.S.C. § 105a (1964). See MacLachlan §§ 301-02.

⁶ If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person. Int. Rev. Code of 1954, § 6321.

⁷"[T]he lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate. . . ." Int. Rev. Code of 1954, § 6323(a). Notice must be filed in the office designated by the law of the state or territory in which the property subject to the lien is situated. When the state or territory has not designated such an office, notice is filed with the clerk of the United States

If the federal government acquires a tax lien by demand and refusal before a taxpayer goes into bankruptcy, the tax claim will ordinarily⁸ be paid as a secured claim [I] ahead of the claims of both priority [II A] and general unsecured creditors [II B], even though the lien is not recorded,⁹ unless the trustee in bankruptcy can be made to fall within one of the 4 classes—mortgagees, pledgees, purchasers, or judgment creditors—against whom the tax lien must be recorded to be valid.

The "strong arm clause" of the Bankruptcy Act, which is a part of § 70c, provides:

The trustee, as to *all* property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a *lien by legal or equitable proceedings* at the date of bankruptcy, shall be deemed vested as of such date with all the *rights, remedies, and powers of a creditor then holding a lien thereon by such proceedings*, whether or not such a creditor actually exists.¹⁰

This section has consistently been interpreted to give the trustee in bankruptcy all the powers of a "judgment creditor" to avoid liens when a judgment creditor would, under applicable state law, have better rights than such lienholder.¹¹ For example, the trustee is able to defeat the lien of a mortgagee who failed to record his mortgage before bankruptcy; the mortgagee then takes as a general unsecured creditor [II B] rather than as a secured claimant [I].¹²

The Courts of Appeals for the 2d, 3d, and 9th Circuits have not, however, held that the "strong-arm clause" vests the trustee with the

District Court in which the property is situated. Int. Rev. Code of 1954, § 6323(a) (1)-(2).

⁸Under certain circumstances the tax lien will not be paid until after payment of administration expenses and wages—the first two unsecured priority claims [II A 1, 2]. See text accompanying note 55, *infra*.

⁹See, e.g., cases cited at note 13, *infra*.

¹⁰52 Stat. 879 (1938), as amended, 11 U.S.C. § 110c (1964) [Emphasis added.]

¹¹See, e.g., *In re Sayre Manor, Inc.*, 120 F. Supp. 215 (D.N.J. 1954) (Unrecorded land purchase contracts void under New Jersey law against subsequent judgment creditors without notice void as to trustee); *McKay v. Trusco Finance Co.*, 198 F.2d 431, 433 (5th Cir. 1952) (Unrecorded conditional sales contract void as to judgment creditor with lien under Alabama law void as to trustee); *Sampbell v. Straub*, 194 F.2d 228, 231 (9th Cir. 1951), *cert. denied*, 343 U.S. 927 (1952) (Unrecorded homestead exemption void as to judgment lienholders under California law void as to trustee).

¹²E.g., *Hams v. Marshall*, 43 F.2d 703, 704 (2d Cir.) *cert. denied* 282 U.S. 882 (1930) (decided under bankruptcy Act § 47a, 30 Stat. 557 (1898), the predecessor to present § 70c). See 4 Collier § 70.55.

rights of a "judgment creditor" insofar as protection from the unrecorded federal tax lien is concerned.¹³ These decisions were based on the Supreme Court decision in *United States v. Gilbert Associates*¹⁴ involving a municipal tax assessment that the New Hampshire Supreme Court had held was "in the nature of a judgment."¹⁵ *Gilbert* sustained the validity of the unrecorded federal tax lien against the municipal tax claim, holding that a "judgment creditor," for purposes of defining the class protected from the unrecorded tax lien, is a creditor holding a judgment "in the usual, conventional sense of a judgment of a court of record."¹⁶ *Gilbert* stressed the necessity for a uniform interpretation of federal statutes and the confusion which would result from permitting state courts to make different interpretations of the phrase "judgment creditor."

When the 6th Circuit held that the "strong-arm clause" does give the trustee the rights of a judgment creditor as against the unrecorded federal tax lien,¹⁷ the Supreme Court granted certiorari¹⁸ to resolve the resulting inter-Circuit conflict and affirmed in *United States v. Speers*,¹⁹ thus settling the most common question involving the tax lien in bankruptcy proceedings.²⁰ In *Speers*, the federal government acquired a lien for more than \$14,000 in withholding taxes and interest on the property of the Kurtz Roofing Co. 17 days before bankruptcy. The lien arose by demand and refusal and was not recorded before bankruptcy. Sale of the assets of the Kurtz Roofing Co. after expenses of sale produced approximately \$14,000.²¹ The trustee successfully contended that "judgment creditors" are protected from the unrecorded federal tax lien by the Internal Revenue Code, and that under the "strong-arm clause" of the Bankruptcy Act the

¹³*Simonson v. Granquist*, 287 F.2d 489 (9th Cir. 1961), *rev'd on other grounds*, 369 U.S. 38 (1962); *In re Fidelity Tube Corp.*, 278 F.2d 776 (3d Cir.), *cert. denied sub nom. Borough of East Newark v. United States*, 364 U.S. 828 (1960); *Brust v. Sturr*, 237 F.2d 135 (2d Cir. 1956).

¹⁴345 U.S. 361 (1953) (decided under Int. Rev. Code of 1939, § 3672, the predecessor of § 6323).

¹⁵*Petition of Gilbert Associates, Inc.*, 97 N. H. 411, 414, 90 A.2d 499, 502 (1952).

¹⁶*United States v. Gilbert Associates*, *supra* note 14, at 364. A judgment creditor must also have a lien to be protected by § 6323 of the Int. Rev. Code, *Miller v. Bank of America*, 166 F.2d 415, 417 (9th Cir. 1948) (decided under Int. Rev. Code of 1939 § 3672, the predecessor of § 6323).

¹⁷*In re Kurtz Roofing Co.*, 335 F.2d 311 (6th Cir. 1964). See note, 1965 Duke L.J. 142; 53 Geo. L.J. 813 (1965).

¹⁸*United States v. Speers*, 379 U.S. 958 (1965).

¹⁹382 U.S. 266 (Black dissenting).

²⁰See *Levit, United States v. Speers—A Milestone*, 71 Com. L.J. 70 (1966).

²¹Notice of final meeting of creditors of Kurtz Roofing Co., No. 27743, (D. C. N. D. Ohio, W. Div., March 5, 1962).

trustee is *deemed* a "judgment creditor." Under the trustee's proposed plan of distribution, affirmed by *Speers*, the federal government received less than \$9,000 of the approximately \$14,000 realized from sale of the bankrupt's property;²² the Government's claim was reduced to the less favored status of a 4th priority unsecured tax claim [II A 4] sharing pro-rata with state and local taxes.

Speers permits for the first time an artificial judgment creditor, the bankruptcy trustee, to prevail against an unrecorded federal tax lien. The uniformity problem in *Gilbert* (the possibility of confusion resulting from permitting state courts to make different interpretations of the phrase "judgment creditor") is not present in *Speers* since interpretation of the Bankruptcy Act is a federal matter.²³

Speers felt that Congress intended to confer "judgment creditor" status on the trustee in bankruptcy. The predecessor of the "strong-arm clause" was enacted in 1910 and read in part:

Such trustees, as to all property in the custody or coming into the *custody of the bankruptcy court*, shall be deemed vested with all the rights, remedies, and powers of a creditor *holding a lien by equitable or legal proceedings* thereon; and also, as to all property *not in the custody of the bankruptcy court*, shall be deemed vested with all the rights, remedies, and powers of a judgment creditor holding an execution duly returned unsatisfied.²⁴

Prior to this amendment, the Bankruptcy Act provided that the trustee was to be vested with the title of the bankrupt to all property "which might have been levied upon and sold under judicial process against . . . [the bankrupt]." ²⁵ However, in 1906 the Supreme Court in *York Mfg. Co. v. Cassell*²⁶ had refused, despite the existing lan-

²²The federal government actually received only about \$1800 since costs of the appeal to the Supreme Court had to be paid as an administration expense [II A 1] before payment of its tax claim [II A 4]. Notice of Final Meeting of creditors of Kurtz Roofing Co., No. 27743, (D. C. N. D. Ohio, W. Div., Feb. 7, 1966).

²³The application of *Gilbert* as a basis for holding that the trustee was not to be deemed a judgment creditor in order to prevail against the unrecorded federal tax lien met with much disapproval. See, e.g., 4 Collier § 70.49 n.3c, at 1415; MacLachlan § 183, at 192; Loiseaux, *Federal Tax Liens in Bankruptcy*, 15 Vand. L. Rev. 137, 138-42 (1961); Seligson, *Creditors Rights*, 32 N.Y.U.L. Rev. 708-11 (1957).

²⁴Act of June 25, 1910, ch. 412, 36 Stat. 838, 840 (Emphasis added.)

²⁵Bankruptcy Act, § 70a (5), 30 Stat. 565 (1898) (now as amended, 66 Stat. 429 (1952), 11 U.S.C. § 110(a) (5) (1964).

²⁶201 U.S. 344 (1906). See 4 Collier § 70.47, at 1396; MacLachlan § 183, at 187.

guage of the Act, to give the trustee title to property in the possession of the bankrupt as a vendee under an unrecorded conditional sale contract. In *Cassell*, the Court found that under the controlling Ohio conditional sales law only creditors with liens could avoid an unrecorded conditional sale and that the conditional sale contract was still good between the parties even though not recorded. Since the trustee took the same title to property that the bankrupt had, the trustee simply stood in the shoes of the bankrupt in such circumstances and could not be given the benefit of the Ohio recording act. The 1910 amendment, therefore, expanded the trustee's powers to reach those cases where state law protected creditors with unrecorded liens.²⁷

The only substantial amendment²⁸ to the "strong-arm clause," adopted in 1950,²⁹ clearly simplified the definition of the status of the trustee.³⁰ The distinction between property coming into the custody of the bankruptcy court and property not coming into the custody of the bankruptcy court was eliminated, and the clause conferring the "rights, remedies, and powers of a judgment creditor then holding an execution returned unsatisfied" was deleted. Instead, the trustee was given the rights of a creditor who "could have obtained a *lien by legal or equitable proceedings*" as to *all* property of the bankrupt whether or not such property comes into the custody of the bankruptcy court. Since the rights of a creditor holding a lien by legal or equitable proceedings are ordinarily greater than those of a judgment creditor holding an execution returned unsatisfied,³¹ the elimination of the distinction as to possession by the 1950 amendment clearly put the trustee in the stronger of the 2 positions which had existed under the original enactment of the "strong-arm clause."³²

A creditor with a lien through legal or equitable proceedings does not necessarily have a judgment. For example, a creditor may acquire a lien by attachment prior to judgment.³³ A "judgment creditor" does not necessarily have a lien; in some jurisdictions a judgment does not become a lien until properly docketed.³⁴ It has generally been

²⁷See 4 Collier § 70.47, at 1388-91.

²⁸Other amendments occurred in 1938, ch. 575, § 1, 52 Stat. 879, and 1952, ch. 579, § 23, 66 Stat. 420.

²⁹Act of March 18, 1950, ch. 70, § 2, 64 Stat. 25.

³⁰See 4 Collier § 70.47, at 1393.

³¹See 4 Collier 70.47 n.18, at 1393; MacLachlan, § 70c of the *Bankruptcy Act*, 24 Ref. J. 107 (1950).

³²See MacLachlan § 183, at 192.

³³See 4 Collier § 70.49, at 1412, n.3a at 1413.

³⁴See 4 Collier § 67.08 and cases cited in n.7 at 96-97.

held, however, that the "strong-arm clause" gives the trustee the rights of a judgment creditor as against imperfect liens other than the unrecorded federal tax lien.³⁵ For example, the trustee's rights are better than those of a mortgagee who has failed to record his mortgage.³⁶ *Speers* said that the purpose of the 1950 amendment was to broaden rather than reduce the powers of the trustee³⁷ since "elsewhere in the same legislation it was recognized that the category of those holding judicial liens includes judgment creditors,³⁸ and a judicial lienholder generally has 'greater rights than a judgment creditor.'" ³⁹

Originally the federal tax lien statute did not protect any subsequent creditors from the secret tax lien.⁴⁰ In 1893 the Supreme Court held⁴¹ that the tax lien was valid against a bona fide purchaser for value, but to alleviate the harshness of this holding, Congress provided in 1913 that the federal tax lien would not be valid against a "mortgagee, purchaser, or judgment creditor" until the lien had been recorded.⁴² Pledges were added in 1939 to the classes protected.⁴³ During the period in which the term "judgment creditor" appeared in both the "strong-arm clause" of the Bankruptcy Act and the tax lien sections of the Internal Revenue Code, the 2d Circuit in 1949 said in dictum in *United States v. Sands*⁴⁴ that the trustee in bankruptcy was to be deemed a "judgment creditor" for purposes of avoiding the unrecorded tax lien.⁴⁵ After the 1950 deletion of the term "judgment creditor" from the "strong-arm clause," and after the *Gilbert* holding that a judgment creditor for purpose of protection from the unrecorded federal tax

³⁵See 4 Collier § 70.49, at 1412-13.

³⁶See e.g., *Hams v. Marshall*, *supra* note 12.

³⁷H.R. Rep. No. 1293, 81st Cong., 1st Sess. 7 (1949); See 4 Collier § 70.47, at 1393.

³⁸Act of March 18, 1950, ch. 70, 64 Stat. 24, 25 (1950), 11 U.S.C. § 96a(4). See 4 Collier § 70.49, n.3, at 1415; MacLachlan § 183, at 192 (1957); Loiseaux, *supra* note 23, at 139.

³⁹*United States v. Speers* *supra* note 19, at 273, quoting H.R. Rep. No. 745, 86th Cong., 1st Sess., to accompany H.R. 7242, p. 10. See Loiseaux, *supra* note 23, at 139.

⁴⁰Rev. Stat., § 318b (1875), as amended, ch. 125, 20 Stat. 327, 331 (1879).

⁴¹*United States v. Snyder*, 149 U.S. 210 (1893).

⁴²Act of March 4, 1913, ch. 166, 37 Stat. 1016.

⁴³Int. Rev. Code of 1939, § 401, ch. 247, 53 Stat. 862, 882.

⁴⁴174 F.2d 384, 385 (2d Cir. 1949).

⁴⁵*Speers* said that the 2d Circuit was "the only Court of Appeals [in *Sands*, *supra* note 44,] squarely to pass upon the question." *United States v. Speers*, *supra* note 19, at 272 (Emphasis added.) Although *Sands* unequivocally stated that the trustee in bankruptcy had the rights of a judgment creditor as against the unrecorded federal tax lien, since the collector had taken possession of the property before bankruptcy the court upheld the Government's unrecorded lien on the ground that it was a statutory lien by distraint.

lien meant a creditor with a judgment of a court of record, a Congressional effort was made expressly to exclude from the Internal Revenue Code "artificial" judgment creditors such as the trustee in bankruptcy from the classes protected against the unrecorded federal tax lien.⁴⁶ The Senate, however, deemed it "advisable to continue to rely upon judicial interpretation of existing law."⁴⁷ *Speers* felt that this existing law sought to be preserved was not *Gilbert* but the dictum in *Sands*, and cases holding that the trustee in bankruptcy was to have the rights which a judgment creditor would have under state law.⁴⁸ Although *Gilbert* held that for purposes of avoiding the unrecorded federal tax lien a judgment creditor must be a creditor with a judgment of a court of record, at the time the legislation was proposed, "*Gilbert* had not yet been applied by any court to displace the rights of the trustee in bankruptcy as against an unrecorded federal tax lien."⁴⁹

Speers also found that after the view began to spread that *Gilbert* compelled exclusion of the trustee in bankruptcy from the protection given judgment creditors against the unrecorded federal tax lien, legislation had been introduced "expressly to reiterate the trustee's power to upset unrecorded federal tax liens."⁵⁰ The proposed legislation⁵¹ on 1 occasion passed both Houses of Congress but was vetoed by President Eisenhower.⁵² *Speers* based its holding in part upon such "expressions of congressional discontent with recent decisions" denying the trustee the protection given judgment creditors against unrecorded tax liens.⁵³

Speers indicates that under an opposite result—upholding of the validity of the unrecorded federal tax lien against the trustee—the Government would have received "the full amount owing to it."⁵⁴ Even if this result had been reached, § 67c of the Bankruptcy Act⁵⁵

⁴⁶H.R. Rep. No. 1337, 83d Cong., 2d Sess., to accompany H.R. 8300, p. A407; 1954 U. S. Code Cong. & Ad. News 4554.

⁴⁷S. Rep. No. 1622, 83d Cong., 2d Sess., to accompany H.R. 8300, p. 575; 1954 U. S. Code Cong. & Ad. News 5224; H. Conf. Rep. No. 2543, 83d Cong. 2d Sess., to accompany H.R. 8300, p. 78.

⁴⁸E.g., *MacKay v. Trusco Finance Co., Sampsell v. Straub*, *supra* note 11.

⁴⁹*United States v. Speers*, *supra* note 19, at 274.

⁵⁰*Ibid.*

⁵¹H. R. 7242, 86th Cong., 1st Sess., § 6; H. R. 394, 88th Cong. 2d Sess., § 6; H. R. 136, 89th Cong., 1st Sess., § 6.

⁵²H.R. 7242, 86th Cong., 1st Sess., § 6, vetoed by President on Sept. 8, 1960, 106 Cong. Rec. 19168.

⁵³*United States v. Speers*, *supra* note 19, at 275.

⁵⁴*Id.* at 269.

⁵⁵66 Stat. 427 (1952), 11 U.S.C. § 107(c) (1964).

provides that payment of statutory liens, including liens for taxes owing to the United States, may be *postponed* until payment of the first two priority claims, administration expenses and wages up to \$600 [II A 1, 2]. This provision is applicable only if:

- (1) The bankrupt estate is insolvent.
- (2) The lien is on personal property.⁵⁶
- (3) The lien is not accompanied by possession.
- (4) The lien has not been enforced by sale prior to the filing of the petition in bankruptcy.

Although these requirements limit the instances to which the statutory lien postponement provisions of § 67c are applicable, the federal tax lien can under the proper circumstances be subordinated to the administration expense and wage priorities. This possibility existed before *Speers*.⁵⁷ Thus, in those cases where the trustee could already have applied the statutory lien postponement provision, the only benefit to unsecured creditors is to enhance the positions of the priority class 3 creditors [II A 3] and state and local tax claims [II A 4] to the extent the Government's position is made less favorable. The unrecorded federal tax lien still has priority over the claims of unsecured general creditors [II B].

The Government contended in its brief that to allow the trustee to invalidate the unrecorded federal tax lien would result in a "windfall" to secured creditors who are not mortgagees, pledgees, purchasers, or judgment creditors whose security was obtained *subsequent* to the unrecorded tax lien.⁵⁸ Under this contention, creditors who are not already protected by the recordation requirement of § 6323 of the Internal Revenue Code but whose liens are nevertheless valid in bankruptcy as secured claims [I], advance monetarily by the amount of the invalidated tax claim. To illustrate: Assume that before bankruptcy the Government acquires, but fails to record, a tax lien for \$10,000 and that subsequent to the tax lien but still before bankruptcy a creditor files, but does not reduce to judgment, a valid⁵⁹ attachment lien which will be paid as a secured claim [I] in bankruptcy. Assume that sale of the property produces no more than

⁵⁶"Personal property" has been interpreted to mean *tangible* personal property. *United States v. Eiland*, 223 F.2d 118, 123 (4th Cir. 1955).

⁵⁷See 4 *Collier* § 67.27.

⁵⁸Brief for Petitioner, *United States v. Speers*, *supra* note 19.

⁵⁹To be valid the attachment must not be followed by bankruptcy within 4 months of its acquisition if at the time the lien was obtained the debtor was insolvent. Bankruptcy Act § 67a, 52 Stat. 875 (1938), as amended, 11 U.S.C. § 107(a) (1964).

\$10,000. Unless the trustee can avoid the unrecorded tax lien, the Government takes the entire amount, because as against the federal tax lien the attachment lien is "inchoate" until judgment and therefore does not make the attachment holder a judgment creditor.⁶⁰ But, if the federal tax lien is invalid against the trustee for failure to record and thereby reduced from a secured claim [I] to an unsecured tax claim [II A 4], the attachment lien will be the first secured claim to be paid, thus producing an obvious windfall for the attaching creditor. *Speers* accepted this contention without argument:

It is true that the consequence of depriving the United States of claimed priority for its secret lien is to improve the relative positions of creditors—if there are any not already protected by § 6323—whose security was obtained subsequent to the Government's lien and who, once the federal lien is invalidated, have a prior claim to the secured assets.⁶¹

Such windfalls to junior lienors could be avoided if the trustees could assert the Government's invalidated rights for himself and obtain the amount the Government would have obtained had the federal tax lien been recorded for the benefit of the general estate [II]. Other sections of the Bankruptcy Act which enable the trustee to avoid or postpone certain transfers and security interests expressly provide for subrogation of the trustee to the invalidated interest, resulting in a larger distribution to the general estate [II]. § 67c, dealing with *postponement of statutory* liens, not only allows the trustee to postpone statutory liens, including federal tax liens, on personal property not in the lienholder's possession until payment of the administration and wage expense priorities; it also permits the trustees to step into the shoes of the creditor whose statutory lien has been postponed for the benefit of the general bankrupt estate.⁶² But, although *Speers* enables the trustee to avoid the unrecorded tax lien, it does not appear that he is in a position to use any preservation provision such as that contained in § 67c or other sections of the Bankruptcy Act to preserve the lien for the benefit of the general bankrupt estate and

⁶⁰United States v. Security Trust & Sav. Bank, 340 U.S. 47 (1950) (attachment lien inchoate until judgment, tax lien attaching prior to judgment entitled to priority). The "choate lien doctrine" requires that an antecedent lien must be specific and perfected to prevail against the government's lien. Choateness is always a matter of federal law. See Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905 (1954).

⁶¹United States v. *Speers*, *supra* note 19, at 275-76.

⁶²66 Stat. 427 (1952), 11 U.S.C. § 107(c) (1964).

prevent windfalls to competing lienholders. § 60⁶³ is the voidable preference section of the Bankruptcy Act. When a creditor of the bankrupt, having reasonable cause to believe the bankrupt insolvent, would receive a greater percentage of his debt than creditors of the same class, the trustee may avoid transfers made within 4 months before bankruptcy by the bankrupt debtor to such creditor-transferee. A transfer within the meaning of the Bankruptcy Act⁶⁴ includes securing an involuntary as well as voluntary lien.⁶⁵ A tax lien is an involuntary lien. § 60 further provides that where the preference is voidable, the court may

order such lien or title to be preserved for the benefit of the general bankrupt estate, in which event such lien or title shall pass to the trustee.

If these requirements are met, § 60 would apply to tax liens as involuntary transfers⁶⁶ were it not for § 67b which provides for a sweeping validation of statutory liens even though arising while the debtor is insolvent and within 4 months before bankruptcy.⁶⁷ § 67b allows statutory liens, including liens for federal taxes, to be perfected *after* bankruptcy if perfected within the time allowed by the applicable federal or state law creating or recognizing the lien.⁶⁸ As *Speers* pointed out:

§ 67, sub. b permits an otherwise inchoate federal tax claim to be "perfected" by assessment and demand within the four months prior to bankruptcy or afterwards. It does not nullify or purport to nullify the consequences which flow from the Government's failure to file its perfected lien prior to the date when the trustee's rights as a statutory judgment creditor attach—namely, on filing of the petition in bankruptcy.⁶⁹

Although it would now seem superfluous to be able to perfect the tax lien after bankruptcy since it must also be recorded to be valid against the trustee,⁷⁰ § 67b would always permit the lien to be per-

⁶³64 Stat. 24 (1950), as amended, 11 U.S.C. § 96 (1964).

⁶⁴Bankruptcy Act § 1 (30), 30 Stat. 544 (1898), as amended, 11 U.S.C. § 1 (30) (1964).

⁶⁵3 Collier § 60.07, 60.09 (14th ed. 1964).

⁶⁶3 Collier § 60.12.

⁶⁷66 Stat. 427 (1952), 11 U.S.C. § 107(b) (1964).

⁶⁸See 4 Collier § 67.20 at 183.

⁶⁹United States v. *Speers*, *supra* note 19, at 278.

⁷⁰The "strong-arm clause" may in other instances render impossible the perfection of statutory liens after bankruptcy under § 67b. See Oglebay, *Some Developments in Bankruptcy Law*, 24 Ref. J. 63 (1950).

fectured within the 4 months before bankruptcy thus taking it out of the § 60 voidable preference category.

§ 67a⁷¹ is another section that must be analyzed in connection with preventing windfalls to competing lienholders when the unrecorded federal tax lien is invalidated. It provides for invalidation of judicial liens and also contains an avoidance and preservation provision. Under § 67a every lien obtained by attachment, judgment, levy, "or other legal or equitable process or proceedings" within 4 months before filing of a petition in bankruptcy shall be void if the debtor was insolvent at the time the lien was obtained, and the bankruptcy court may order any such lien to be preserved for the trustee for the benefit of the general bankrupt estate. However, a federal tax lien is a statutory lien rather than a lien obtained by "legal or equitable process or proceedings," § 67a is therefore *inapplicable*.⁷²

§ 70e⁷³ provides that any transfer or obligation incurred by the bankrupt estate which is voidable under non-bankruptcy law by any creditor having a claim provable in bankruptcy shall be void against the trustee, and that the trustee may preserve such transfer or obligation for the benefit of the general bankrupt estate. But, to apply § 70e, it must be shown that at least 1 of the present creditors of the estate holding a provable claim was a creditor as against whom the transfer was fraudulent or voidable under the controlling state or federal law.⁷⁴

Although it appears no existing provision of the Bankruptcy Act can be used to preserve the invalidated tax lien for the trustee for the benefit of the general bankrupt estate [II] to prevent windfalls to competing lienholders,⁷⁵ the same result might be achieved by reference to the priorities contemplated by the Internal Revenue Code. It can be argued that the trustee's rights against the unrecorded federal tax lien in no way affect the federal government's rights against other lienholders against whom the unrecorded federal tax lien is valid. The Internal Revenue Code provides that to be valid against a "mortgagee,

⁷¹52 Stat. 874 (1938), as amended, 11 U.S.C. § 107(a) (1964).

⁷²"[L]iens created by statute to protect particular classes of persons are governed in bankruptcy by sub-divisions *b* and *c* of § 67, whatever the mode of perfection or enforcement." 4 Collier 67.12 [1] n.2a, at 120. See *e.g.*, *Davis v. City of New York*, 119 F.2d 559 (2d Cir. 1941) (city sales tax lien arising on docketing of a warrant in county clerk's office held statutory lien within § 67b rather than lien obtained by legal proceedings).

⁷³52 Stat. 882 (1938), as amended, 11 U.S.C. § 110(e) (1964).

⁷⁴4 Collier § 70.90, at 1729.

⁷⁵See Comment, *Avoiding Federal Tax Liens in Bankruptcy*, 39 Texas L. Rev. 616 (1961); Note, 35 Ind. L.J. 351, 353-57 (1960).

pledgee, purchaser, or judgment creditor" the federal tax lien must be recorded; if the lien is not recorded, a judgment creditor such as the trustee in bankruptcy has greater rights to the taxpayer's property than the Government. The Internal Revenue Code does not provide, however, that the existence of a judgment creditor will increase the rights of any other lienholder against whom the unrecorded tax lien is still valid. Rather, after the amount of the judgment creditor's lien has been paid, any balance remaining should be applied to the tax lien and *then* to the lien which is junior to the federal tax lien. Since the "strong-arm clause" of the Bankruptcy Act gives the trustee the power of a judgment creditor as to *all* property of the bankrupt taxpayer, as a practical matter there will never be anything left for a lienholder junior to the tax lien after the trustee has defeated the unrecorded tax lien. Thus, such junior lienholders who would receive windfalls under the assumption in *Speers* could only take as general creditors [II].

The *Speers* holding will never benefit more than a few claims, primarily unsecured state and local tax claims which, even then, will only share pro-rata with the federal tax claim. Third priority creditors' fraud expenses [II A 3] will also benefit, but such claims are rare.⁷⁶ Except in cases involving real property, administration expenses and wages [II A 1 & 2], the first 2 priorities, would by virtue of § 67c (the statutory lien postponement section) be paid before the federal tax lien anyway unless the Government takes possession of the property before bankruptcy,⁷⁷ the bankrupt estate is solvent, or the Government enforces its lien by sale prior to bankruptcy.⁷⁸ Furthermore, if the Court is correct in assuming the elevation of liens ordinarily behind the tax lien, the result is a windfall to junior lienholders simply because of the intervention of bankruptcy. It is obvious that this result is not contemplated by the Bankruptcy Act⁷⁹ inasmuch as all other sections permitting the trustee to invalidate liens and transfers provide that the trustee can preserve and assert the rights of the claimant whose interest has been invalidated for the benefit of the general bankrupt estate [II].⁸⁰

⁷⁶See Note, 39 Ref. J. 55, 56, n.21 (1965).

⁷⁷See *Goggin v. Division of Labor Law Enforcement*, 336 U.S. 118 (1949).

⁷⁸See text accompanying note 54, *supra*.

⁷⁹See Seligson, *Recent Developments in the Field of Federal Tax Claims*, 29 Ref. J. 7, 11 (1955).

⁸⁰Bankruptcy Act § 60, 64 Stat. 24 (1950), as amended, 11 U.S.C. § 96 (preferences) (1964); § 67a, 52 Stat. 875 (1938), as amended, 11 U.S.C. § 107(a) (1964) (judicial liens); § 67c, 66 Stat. 427 (1952), 11 U.S.C. § 107(c) (1964) (postponement of statutory liens); § 67d, 66 Stat. 428 (1952), 11 U.S.C. § 107(d)

The *Speers* holding does, however, conform to the general policy of the strong-arm clause and the entire Bankruptcy Act in giving the trustee broader control over the bankrupt's assets at the date of bankruptcy than would a holding that an unrecorded federal tax lien is valid in bankruptcy as a secured claim [I].⁸¹

While the Bankruptcy Act attempts to make distributions to the bankrupts' creditors as fair as possible, it also seeks to enable the bankrupt debtor to return to economic and social productiveness by discharging him from claims of his old creditors.⁸² Even though the amount the Government receives is altered by *Speers*, the bankrupt taxpayer is still liable for the excess amount not realized in bankruptcy, since no tax claim is dischargeable.⁸³ If avoidance of the unrecorded federal tax lien results in larger payments to junior lienholders and priority creditors, then to the extent of such payments the bankrupt is left with a greater amount of nondischargeable tax indebtedness.

The policy of insuring the collection of the Government's revenues is strong⁸⁴ as evidenced by the existence of the secret tax lien and the strict judicial definition of the classes against whom the unrecorded lien is invalid under § 6323 of the Internal Revenue Code.⁸⁵ Since allowing the trustee to invalidate the unrecorded tax lien primarily benefits unsecured state and local tax claims and, presumably, junior liens not protected by § 6323 of the Internal Revenue Code, as a result of *Speers* the policy of protecting the federal revenue is altered somewhat by the advent of bankruptcy. *Speers* permits a result in bankruptcy which nonbankruptcy cases such as *Gilbert* refused to reach.⁸⁶ While the unrecorded federal tax lien defeated the local assessment in *Gilbert*, *Speers* allowed the local tax to share pro-rata

(1964) (fraudulent transfers); § 70e, 52 Stat. 882 (1938), as amended, 11 U.S.C. § 110(e) (1964) (transfers voidable by any creditor of the bankrupt voidable by trustee).

⁸¹See 4 Collier § 70.45, at 1384.

⁸²See MacLachlan § 100.

⁸³Bankruptcy Act § 17 (9) (1), 30 Stat. 544 (1898), 11 U.S.C. § 35 (9) (1) (1964).

⁸⁴The purpose of the secret tax lien is to insure prompt and certain collection of taxes. See *United States v. Security Trust & Sav. Bank*, 340 U.S. 47, 51 (1950); *United States v. Bond*, 279 F.2d 837, 847 (4th Cir. 1960), *cert. denied*, 364 U.S. 895 (1960); "The Court today gives frail and inadequate support, I think, for its judicial destruction of the Government's congressionally created lien." *United States v. Speers*, *supra* note 19, at 280 (Black dissenting).

⁸⁵See *United States v. Security Trust & Sav. Bank*, 340 U.S. 47, 53 (1950) (concurring opinion); Walker, *What Protection Against the Secret Federal Tax Lien?* 9 J. Taxation 8 (1958).

⁸⁶*United States v. Gilbert Associates*, 345 U.S. 361 (1953).