

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF ALABAMA

IN RE:

HUGH L. BAYNES

Case No. 02-11237

Debtor

**ORDER TREATING THE UNITED STATES'S RESPONSE TO TRUSTEE'S MOTION  
AS A MOTION FOR SUMMARY JUDGMENT AND PARTIALLY GRANTING AND  
PARTIALLY DENYING SUCH MOTION**

Theodore L. Hall, Trustee, Mobile, AL  
Charles Baer, Assistant U.S. Attorney, Mobile, AL

This matter came before the Court on Theodore L. Hall's ("trustee") motion to determine whether or not the estate owes any tax penalties and interest to the IRS. At this Court's May 1, 2007, hearing, the trustee and the United States agreed to treat the United States's response to such motion as a motion for summary judgment. The Court grants this request and will treat the United States's response as a motion for summary judgment. The Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §§ 157 and 1334 and the Order of Reference of the District Court. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2), and the Court has authority to enter a final order. For the reasons indicated below, the Court is partially granting and partially denying the United States's motion for summary judgment.

**FACTS**

The debtor filed a voluntary chapter 7 case on March 5, 2002. After such filing, the trustee sold some of the debtor's real property in 2002 and 2003, thereby incurring tax liability for the estate. The trustee did not file estate income tax returns for those years until December 2006. On February 19, 2007, the IRS mailed the trustee two letters which informed him that the estate owed a penalty and interest of \$5,123.31 for the 2002 tax year and a penalty and interest of

\$163.61 for the 2003 tax year. On March 14, 2007, the IRS mailed the trustee another letter which informed him that the returns he filed in December 2006 had “been accepted as filed (“March 14th letter”) . . . ”

The trustee explained his delay in filing tax returns by contending that he was unable “to locate records of the debtor sufficient to ascertain the proper basis in the property . . . ” The trustee further explains that he thought the real property was rental property subject to depreciation deductions. At the Court’s May 1, 2007, hearing, the United States accepted both of the trustee’s explanations for purposes of the motion for summary judgment.

## LAW

Motions for summary judgment are controlled by Rule 56 of the Federal Rules of Civil Procedure, which has been adopted by Rule 7056 of the Federal Rules of Bankruptcy Procedure. A court shall grant summary judgment to a party when the movant shows that “there is no genuine issue as to any material fact and . . . the moving party is entitled to a judgment as a matter of law.” Fed. R. Civ. P. 56(c). “In assessing whether the movant has met this burden, the courts should view the evidence and all factual inferences therefrom in the light most favorable to the party opposing the motion.” *Clemons v. Dougherty County*, 684 F.2d 1365, 1368 (11th Cir. 1982). “All reasonable doubts about the facts should be resolved in favor of the non-movant.” *Id.* at 1369. A judge’s function is not to determine the truth of the matter asserted or the weight of the evidence presented; instead, a judge’s function is to determine whether or not the factual disputes raise genuine issues for trial. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248-49 (1986). “If the record presents factual issues, the court must not decide them; it must deny the motion and proceed to trial.” *Clemons*, 684 F.2d at 1369.

The 2002 and 2003 tax liability at issue consists of penalties for failure to file timely income tax returns (“late filing penalties”), failure to pay the penalties assessed in a timely manner, interest, and an estimated tax penalty for the 2002 tax liability. On May 1, 2007, the United States filed a post-hearing memorandum, wherein it concedes that no estimated tax penalty is applicable for the 2003 year. There appears to be no dispute regarding the amount of the underlying 2002 and 2003 tax liabilities. The dispute centers around whether the estate should be assessed any penalties and interest or whether they should be abated and/or waived.

The trustee argues that the estate should not be liable for the 2002 and 2003 tax penalties pursuant to the March 14th letter informing him that the December 2006 income tax return had been accepted as filed. The trustee contends that the Court has authority to review the applicability of these penalties and interest since the tax liability is not of a kind mentioned in 11 U.S.C. § 505(a)(2). Alternatively, the trustee argues that the tax penalties should be waived pursuant to 26 U.S.C. § 6654(e)(3)(A) since, at the time of the sales, he “had no way of knowing what, if any, income tax liability would be incurred by the bankruptcy estate.” If the penalties are waived, then no interest is due as well.

The United States counters that the Tax Code allows it to charge such penalties for late filed income tax returns. The trustee bears the burden of proof under applicable Tax Code provisions to prove that (1) the failure did not result from willful neglect, and (2) the failure was due to reasonable cause. *United States v. Boyle*, 469 U.S. 241, 245 (1985). The United States argues that the trustee’s explanation that he could not find the debtor’s records and estimate potential tax liability is not sufficient to meet such burden. Despite not being able to find the debtor’s records, the trustee could have nonetheless filed tax returns. In its motion for summary

judgment, the United States argues that the trustee could have estimated the potential tax liability in a timely filed tax return and later filed an amended tax return when he discovered the true amount of tax liability. Therefore, the United States requests summary judgment in its favor as to whether penalties and interest are due.

### 1. *Late Filing Penalties*

26 U.S.C. § 6651(a)(1) provides the IRS authority to assess a penalty against a taxpayer for his or her failure to timely file an income tax return. A taxpayer seeking to avoid such a penalty “bears the heavy burden of proving both (1) that the failure did not result from willful neglect, and (2) that the failure was due to reasonable cause.” *Boyle*, 469 U.S. at 245 (internal quotations omitted). Based upon the facts presented in the summary judgment motion, the fact that the trustee could not find the debtor’s records in order to file complete income tax returns for 2002 and 2003 does not justify his filing of a tax return more than 3 to 4 years later. The Court understands that the trustee would have had limited information. However, the trustee could have, as the United States asserts, filed timely tax returns and subsequently amended such tax returns at the time he found the applicable records. *See Craddock v. Craddock (In re Craddock)*, 149 F.3d 1249, 1257 (10th Cir. 1998) (“A tax return does not have to be completely accurate, but must be based on the best information available, . . . and may be amended later if necessary . . .”). To determine the proper basis in the property, the trustee could have used the transfer tax paid by the debtor upon purchase of the property and evidenced on the deed. *See ALA. CODE* 40-22-2 (2004). The Court finds that the United States has sustained its burden. There is no genuine issue of material fact for the Court to resolve at trial. Therefore, summary judgment is granted in the United States’s favor in this regard.

## 2. *Failure to Pay Penalties*

Pursuant to 26 U.S.C. § 6651(a)(3), the estate was also charged a penalty for failing to pay the assessed penalty in a timely fashion, specifically 21 calendar days from the date the trustee received such notice. Again, the burden of proof rests with the trustee to prove that the failure to timely pay is due to reasonable cause and not willful neglect. The trustee implies that he had reasonable cause to not pay this penalty in a timely fashion since the March 14th letter stated that the December 2006 tax return was accepted as filed. The trustee's argument fails unless he can prove at trial that the March 14th letter overrules or vacates the prior assessment. Otherwise, the only evidence the Court has leaves no genuine issue as to the fact that the return could have been timely filed.

## 3. *Interest*

26 U.S.C. § 6601 authorizes the imposition of interest on any unpaid taxes. The trustee requests that this interest be waived and/or abated. The United States argues in its summary judgment motion that the trustee has failed to present enough evidence to warrant an abatement of interest. The Eleventh Circuit has held that interest due on taxes is usually treated in the same manner as the underlying tax. *United States v. Cranshaw (In re Allied Mech. Servs., Inc.)*, 885 F.2d 837, 839 (11th Cir. 1989).

26 U.S.C. § 6404 allows the Secretary of the Treasury ("Secretary") to use his or her discretion to abate any portion of this interest. The trustee implies that this Court has authority to review the applicability of the interest imposed pursuant to 11 U.S.C. § 505(a)(1), which provides:

Except as provided in paragraph (2) of this subsection, the court may determine the amount or legality of any tax, any fine or

penalty relating to a tax, or any addition to tax, whether or not previously assessed, whether or not paid, and whether or not contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction.

The Fifth Circuit has agreed with the trustee's argument. *See Beall v. United States*, 336 F.3d 419 (5th Cir. 2003). The Federal Circuit, however, has reached the opposite result. *See Hinck v. United States*, 446 F.3d 1307 (Fed. Cir. 2006). Whether the Court has jurisdiction to abate interest or not pursuant to 11 U.S.C. § 505(a), the result is the same. The trustee may not obtain a rebate of interest under 26 U.S.C. § 6404 unless the interest owed was assessed due "to an unreasonable error or delay by an officer or employee of the Internal Revenue Service in performing a ministerial or managerial act." 26 U.S.C. § 6404(e). No such error was alleged or proven. Therefore, there is no genuine issue of material fact, and summary judgment is due to be granted as to the interest owed. The interest amount will be governed by the tax ultimately found to be due.

#### 4. *Estimated Tax Penalty*

Alternatively, the trustee contends that the penalties and interest should be waived under 26 U.S.C. § 6654(e)(3)(A). That section provides:

No addition to tax shall be imposed . . . with respect to any underpayment to the extent the Secretary determines that by reason of casualty, disaster, or other unusual circumstances the imposition of such addition to tax would be against equity and good conscience.

"Although a showing of 'reasonable cause' is not often accepted as an excuse for a § 6654(a) penalty, . . . it would be, at the least, a minimum requirement . . ." *Carlson v. United States (In re Carlson)*, 126 F.3d 915, 921 (7th Cir. 1997). "Reasonable cause" is clarified in the Treasury Regulations:

A failure to pay will be considered to be due to reasonable cause to the extent that the taxpayer has made a satisfactory showing that he exercised ordinary business care and prudence in providing for payment of his tax liability and was nevertheless either unable to pay the tax or would suffer an undue hardship . . . if he paid on the due date.

26 C.F.R. § 301.6651-1(c)(1).

The Eleventh Circuit has stated that bankruptcy courts do have the authority to allow or disallow 26 U.S.C. § 6654 penalties. *United States v. Sanford (In re Sanford)*, 979 F.2d 1511, 1514 (11th Cir. 1992). The Secretary is to waive the penalty only where there is a “casualty, disaster or other unusual circumstances.” 26 U.S.C. § 6654(e)(3)(A).

If this Court reviews the matter de novo<sup>1</sup> because there has been no appeal to the Secretary, the Court must conclude that the Secretary, acting on no information, acted properly. The trustee has apparently presented no evidence of his right to a waiver under the statute. The trustee’s evidence offers no proof of casualty or disaster. The unusual circumstances he asserts are inability to locate the debtor’s records. The U.S. asserts that 3 to 4 years of non-filing, without obtaining records or filing anyway, and a failure to check the Probate Court records is not enough to be “unusual circumstances.” The trustee could possibly prove that the unavailability of records was a result of unusual circumstances. There is at least an issue of material fact. The Court needs to hear the trustee’s testimony and judge his credibility and the credibility of his reasons for delay.

THEREFORE IT IS ORDERED AND ADJUDGED that the Court is granting summary

---

<sup>1</sup>The Court is using a de novo standard of review only for purposes of this motion for summary judgment. Such use by the Court in this opinion does not mean a different standard of review may not be applied at trial if the Court is presented with applicable authority requiring such.

judgment in favor of the U.S. on the following issues:

- (1) Barring evidence and/or legal authority that the underlying tax is not due because the IRS accepted the returns, the taxes as filed are due and owing;
- (2) Barring evidence and/or legal authority that the underlying tax is not due because the IRS accepted the returns, the late filing penalties are due and owing.
- (3) Barring evidence and/or legal authority that the underlying tax is not due because the IRS accepted the returns, the failure to file penalties are due and owing.
- (4) Barring evidence and/or legal authority that the underlying tax is not due because the IRS accepted the returns, and/or barring evidence that the failure to file was a result of “unusual circumstances” pursuant to 26 U.S.C. § 6654(e)(3)(A), the interest assessed is due and owing.

A hearing will be held on August 21, 2007, at 10 a.m. to determine the effect, if any, of the March 14, 2007, letter to the trustee from the IRS and to determine whether the trustee’s failure to file was a result of “unusual circumstances.”

Dated: May 17, 2007

  
MARGARET A. MAHONEY  
U.S. BANKRUPTCY JUDGE