

Federal Tax Rebate Credit
Property of Estate

Christopher and Katherine Lambert, Case No. 601-61015-fra7

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Debtors filed their bankruptcy petition under Chapter 7 of the Code on February 22, 2001. Subsequently, Congress passed legislation pursuant to which the Debtors received a check in the amount of \$600, which they delivered to the Trustee in response to his written demand for its surrender. Debtors thereafter filed a motion to compel the Trustee to abandon the funds on the grounds that the funds are not property of the estate.

The amount of the check was calculated based on the Debtors' 2000 income, but was payable in 2001. The Trustee argued that the entire \$600 was property of the estate because it was "sufficiently rooted in the prebankruptcy past," pursuant to Segal v. Rochelle. The court determined, however, that the check represented an advance refund of taxes paid in 2001 and must be prorated between the pre and post-petition part of the 2001 tax year.

However, since the amount of the advance refund was based on year 2000 income, it would be possible that the Debtors may have no refund owing for the year 2001. In that situation, Congress provided that recipients could keep the money without the need to return it. Based on recent Ninth Circuit caselaw, the \$600 would then represent a post-petition new benefit (because the legislation was enacted post-petition) which would not be property of the estate. The Trustee was ordered to return the check to the Debtors who would thereafter determine how much of the \$600 was property of the estate when they calculated their 2001 taxable income.

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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re:) Bankruptcy Case No.
) 601-61015-fra7
CHRISTOPHER T. LAMBERT and)
KATHERINE D. LAMBERT,)
) MEMORANDUM OPINION

Debtors.)

In this matter the Court must determine whether money received by the Debtors under newly enacted tax legislation is property of the Estate. I find that the funds are attributable to the tax year 2001, the year this case was filed, and that the funds must be prorated between the Estate and the Debtors.

I. BACKGROUND

The Debtors filed their Petition for Relief under Chapter 7 of the Bankruptcy Code on February 22, 2001. Subsequently, Congress enacted, and the President approved, the Economic Growth and Tax Relief Reconciliation Act of 2001 (hereinafter simply "the Act").¹

¹ The complete citation is Economic Growth and Tax Relief Reconciliation Act of 2001, Pub.L. No. 107-16, 115 Stat. 38. When codified the Act will be strewn throughout the Internal Revenue Code, U.S.C. Title 26.

1 Pursuant to the Act, Debtors received a check from the United States
2 Treasury, dated September 21, 2001, in the sum of \$600.00. On or
3 about November 14, 2001, Debtors delivered the check to the Trustee.
4 According to Debtors' motion, the check was delivered in response to
5 a written demand from the Trustee for surrender of the funds.

6 Debtors have now filed a motion to compel the Trustee to
7 abandon the funds, on the grounds that the funds are in fact not
8 property of the Estate.

9 The Trustee maintains that the money is a refund of taxes
10 paid in the year 2000, or otherwise attributable to 2000, and is
11 therefore property of the Estate. The Debtors disagree, claiming
12 that the funds constitute an entitlement newly created after the
13 Petition was filed and are not property of the Estate.

14 While the procedural posture may be ambiguous², the parties
15 agree on the nature of the controversy: What interest, if any, does
16 the Estate have in the \$600.00 tax relief check?

17 II. DISCUSSION The Act reduced the rate of tax imposed on the
18 first \$12,000 of income from 15% to 10%. In other words, the tax
19 paid on the first \$12,000 earned in 2001 and thereafter is reduced
20 from \$1,800 to \$1,200, or by \$600. Taxpayers who paid tax in 2000
21 are presumed to make the same payments in 2001. Moreover, taxpayers
22 who did not pay tax in 2000 are treated as if they had.

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24 ² Debtors demand that the Trustee abandon the Estate's interest in the funds
25 on the grounds that the Estate has no interest. As a practical matter what is
26 happening here is that the Debtors are resisting, after the fact, the Trustee's
demand that the funds be delivered. For all intents and purposes this is a
proceeding to compel the Debtors to deliver property to the Trustee, and will be
treated as such. See FRBP 7001(1) and FRBP 9014.

1 The Government is not giving away its money (but see below),
2 but rather undertaking to keep less of each taxpayer's 2001 income
3 than originally permitted by the pre-Act rates. This necessarily
4 requires a return of any money collected in excess of the amounts
5 now due, either in the form of a reduction of tax payed on higher
6 brackets (i.e., a tax credit taken on the 2001 return either
7 lowering the balance due, or applying it toward future tax
8 liability), or cash.

9 For political and economic reasons not important here
10 Congress has undertaken to accelerate the refund process by sending
11 \$600 to filers of joint returns who paid tax in the 2000 tax year.
12 To calculate the amount the statute assumes certain payments by
13 taxpayers in 2000, whether they were actually made or not.

14 When the time comes to file their 2001 tax returns, taxpayers
15 will be required to reconcile the amount their actual tax is reduced
16 and the money payment received in advance. The IRS describes the
17 process this way:

18 [Taxpayers will] complete a worksheet calculating the
19 amount of credit based on their 2001 tax return. They
20 would then subtract from the credit the amount of the
21 check they received. For many taxpayers, these two
22 amounts would be the same. If, however, the result is
23 a positive number (because, for example, the taxpayer
24 had no tax in 2000 but is paying tax in 2001), the
25 taxpayer may claim that amount as a credit against
26 2001 tax liability. If, however, the result is
negative (because, for example, taxpayer paid tax in
2000 but owes no tax for 2001) the taxpayer is not
required to repay that amount to the Treasury.
*Excerpt from explanation of Conference report, Pub.L.
No. 107-16, 115 Stat. 38 (5/26/01).*

1 There is little in the record establishing what the Debtors
2 paid in taxes for 2000, or what they will ultimately owe for 2001.³
3 If they owe no taxes for 2001, the \$600 will amount to a benefit not
4 unlike the Earned Income Credit (EIC) payable to low-income
5 taxpayers. 26 U.S.C. §32. Just as EIC payments are property of the
6 estate, In re Buchanan, 139 B.R. 721 (Bankr. D. Idaho 1992), so the
7 \$600 would have been to the extent attributable to pre-petition
8 2001, if the right had existed on the date of the petition. If the
9 debtor's tax credit and the check are equal, or they are entitled to
10 further credit, the check, for all intents and purposes, is a refund
11 of excess tax payments made in 2001, distinguishable from ordinary
12 refunds only by the date the check was mailed by the Treasury. Such
13 refunds are property of the estate to the extent the overpayment was
14 made with money that otherwise would have been property of the
15 estate. Segal v. Rochelle, 382 U.S. 375, 380 (1966) (Refunds
16 attributable to loss carryback provision of Internal Revenue Code
17 are property of the estate). The Segal Court laid down the oft-
18 cited proposition that after acquired property is part of the
19 bankruptcy estate if it is "sufficiently rooted in the prebankruptcy
20 past and so little entangled in the debtor's ability to make a fresh
21 start that it should not be excluded from property of the estate."

22 The Trustee argues that the payment "is based entirely upon
23 the return filed for 2000; and therefore, the amount of the credit
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25 ³Schedules E and F filed with Debtors' petition for relief disclose no
26 debts attributable to taxes. Schedule I shows income on the filing date of
roughly \$3,200/month, and the Statement of affairs reveals gross income in 2000
of \$32,000.

1 was identifiable by retroactive impact as of the commencement of
2 this bankruptcy case...The factors which give rise to this
3 entitlement are rooted in the pre-bankruptcy past and, thus, make
4 this estate property."

5 The payment is "based" on the 2000 tax year only in the sense
6 that 2000 tax payments (actual or imputed) are used as the basis for
7 calculating 2001 tax payments subject to refund. The pertinent
8 section of the Act (entitled "Advance Refunds of Credit Based on
9 Prior Year Data") states that

10 (1) IN GENERAL - Each individual who was an eligible
11 individual for such individual's first taxable year
12 beginning in 2000 shall be treated as having made a
13 payment against the tax imposed by chapter 1 for such
14 first taxable year in an amount equal to the advance
15 refund amount for such taxable year.

16 (2) ADVANCE REFUND AMOUNT - For purposes of paragraph
17 (1), the advance refund amount is the amount what
18 would have been allowed as a credit under this section
19 for such first taxable year if this section...had been
20 applied to such taxable year. P.L. 107-16, Sec.
21 6428(e). [Emphasis added]

22 The Trustee appears to construe the first paragraph as
23 creating an entitlement with respect to year 2000 tax payments. In
24 light of the additional language, it is clear that the debtor's 2000
25 tax year provides a template for calculating 2001 benefits, and
26 nothing more. The Act has no effect on liability for 2000, and does
not create an overpayment attributable to 2000.

The estate's right to tax refunds is not based on whether the
tax liability is based on pre-petition earnings, but whether the
money being refunded was placed in the government's hands before or
after the petition was filed. In re Christie, 223 B.R. 110 (10th

1 Cir. BAP 1999). In Christie, the debtors paid delinquent taxes owed
2 for a pre-petition tax year with money earned post-petition (and
3 thus excluded from the estate). As it turned out, the accountant's
4 estimate was high, and the amount paid was in excess of the debtors'
5 liability. The BAP rejected the trustee's claim that the resulting
6 refund was property of the estate, noting that, as of the date of
7 the petition, the debtors had no right to a refund of an
8 overpayment, since the overpayment had not yet occurred. Since the
9 refund was a return of post-petition assets excluded from the estate
10 under 11 U.S.C. §541, it was never part of the estate.

11 Debtors argue that the benefits of the Tax Relief Act did not
12 exist at the time Debtors filed for relief, and that no part of the
13 Act's benefits are included in the Estate. Two recent cases have
14 held that benefits created after a petition for relief is filed do
15 not become estate assets simply because the benefit is measured by
16 or granted because of pre-petition events. In In re Schmitz, 2001 WL
17 1222446 (9th Cir. 2001), the Court of Appeals held that fishing
18 quota rights promulgated after the debtor's petition was filed were
19 not an asset of the estate, because the right did not exist on the
20 date of the petition, and, while the rights were calculated on the
21 basis of the debtor's pre-filing fishing activities, they only
22 governed post-petition fishing. The Court noted with approval the
23 opinion of the 10th Circuit Bankruptcy Appellate Panel in In re
24 Vote, 261 B.R. 439 (10th Cir. BAP 2001). In Vote, the Panel held
25 that payments under crop disaster assistance programs created by
26 Congress post-petition were not property of the estate, even if the

1 disaster the payments were attributable to occurred pre-petition. In
2 a passage quoted by the Court of Appeals in Schmitz, the Panel says

3 As of the date the Debtor filed his bankruptcy
4 petition, he may have had, at most, an expectation
5 that Congress would enact legislation authorizing crop
6 disaster or assistance payments to farmers affected by
7 the weather conditions in 1999, but there was no
8 assurance that Congress would authorize such payments
9 or that the debtor would qualify for them if they were
10 authorized. It was equally likely that Congress would
11 not pass such relief legislation. Such an expectancy
12 (or "hope," if you will) does not rise to the level of
13 a 'legal or equitable interest' in property such that
14 it might be considered property of the estate under
15 11 U.S.C. § 541(a) (1).

16 261 B.R. 439, 444.

17 In light of Segal, Schmitz, and Vote, treatment of monies
18 paid this summer under the Act will depend on how much total tax is
19 payable with the Debtors' 2001 tax returns. Segal is still
20 applicable if the payments are early tax refunds. Money paid to or
21 withheld by the IRS pre-petition (or, more precisely, pre-petition
22 money paid to the IRS) is property of the estate if and when
23 refunded. The fact that the Relief Act alters the amount does not
24 change the fundamental character of the property. On the other
25 hand, if the money is proceeds of a new benefit, it is not included
26 in the estate under Schmitz and Vote.

27 Determination of the parties' interest in the funds cannot be
28 determined until Debtors' 2001 tax liability is determined. If the
29 payment is equal to or less than the total tax liability, the
30 September check is a refund, and a pro rata share - \$84.00 by my
31 calculation - will be payable to the Estate. If the September
32 payment is greater than the tax liability, the excess may be

1 retained nevertheless, and therefore is a newly created benefit that
2 is not part of the Estate.

3 III. CONCLUSION

4 The \$600.00 received by the Debtors under the Economic Growth
5 and Tax Relief Reconciliation Act of 2001 is property of the Estate
6 only to the extent of that portion attributable to that part of the
7 2001 tax year prior to February 22, the petition date. Moreover, if
8 the Debtors' 2001 tax liability is less than \$600, the amount of the
9 payment in excess of the liability is also excluded from the estate.

10 The Trustee should return the check to the Debtors. If the
11 Debtors' 2001 tax return discloses total tax liability of \$600.00 or
12 more they shall remit the sum of \$84.00 to the Trustee, plus any
13 additional refund payable to them and attributable to the pre-
14 petition part of the year. If the total tax liability is less than
15 \$516.00, then nothing needs to be paid to the Trustee. Anything
16 falling in between can be calculated by the parties.

17 This opinion constitutes the Court's findings of fact and
18 conclusions of law. Counsel for the Debtor shall submit a form of
19 order consistent with this opinion.

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22 FRANK R. ALLEY, III
23 Bankruptcy Judge
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