

11 U.S.C. § 362(a)(8)
TEFRA
FRCP 56(e)
partnership tax proceedings
tax

Durham Farms v. United States, Adversary No. 99-3291
W.J. Hoyt Sons Management Co., Case No. 397-31374

11/12/1999 ELP

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Trial court ruling regarding application of automatic stay under § 362(a)(8) to partnership proceedings in tax court, when partnership is in bankruptcy. Ruling discusses requirements for affidavits supporting or opposing a motion for summary judgment. The court struck portions of the affidavit because they were not based on personal knowledge or they constituted legal conclusions by a person not qualified as an expert.

The court ruled that § 362(a)(8) does not stay TEFRA (Tax Equity and Fiscal Responsibility Act) actions seeking a redetermination of debtor partnerships' tax liability. Section 362(a)(8) stays actions before the tax court "concerning the debtor." The TEFRA actions do not concern the debtor, because the tax court will not determine the tax liability of the debtor partnership, only of the individual partners. Further, any delay in administration of the estate while the tax proceedings are pending can be handled in bankruptcy court by estimating the partners' claims pursuant to Bankruptcy Code § 502(c).

The court declined to find unusual circumstances that would support extending the automatic stay to partnership tax proceedings. The court said that the partnerships, although named as the parties in the tax court proceedings, are not the real parties in interest because they can have no tax liability that can be affected by the tax court ruling.

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84 A.F.T.R.2d 99-7152, 99-2 USTC P 51,010, 43 Collier Bankr.Cas.2d 386,
Bankr. L. Rep. P 78,057
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<KeyCite History>

United States Bankruptcy Court, D. Oregon.

**W.J. HOYT SONS MANAGEMENT CO., LTD.,
Durham Farms, et al.**

v.

UNITED STATES.

No. 397-31374-ELP7.

Nov. 12, 1999.

Montgomery W. Cobb, Portland, Ore., for
plaintiffs.

Bernard J. Knight, Jr., Department of Justice,
Washington, D.C., for defendant.

FACTS

PERRIS, Bankruptcy J.

[Code Sec. 6871]

*1 Partnerships: Bankruptcy: Automatic stay: Tax Court proceedings: Effect on: Nondebtors: Real party in interest.-The automatic stay under Bankruptcy Code § 362(a)(8) did not apply to a partnership's tax redetermination proceedings that were taking place in the Tax Court because there was no showing that the proceedings would have the effect of liquidating claims when it was in bankruptcy. Since partnerships are not tax paying entities, the TEFRA proceedings were not Tax Court proceedings concerning the debtors. Moreover, the stay was not expanded to nondebtors. Although the debtor partnerships were named as parties in the Tax Court proceedings, they were not real parties in interest since they had no tax liability that could be affected by the Tax Court's ruling. Thus, there were no unusual circumstances requiring the expansion of the stay to nondebtors. Back reference: ¶ 40,630.0244.

[Code Sec. 6871]

Partnerships: Bankruptcy: Automatic stay: Tax Court proceedings: Bankruptcy court jurisdiction.-The determination of the Bankruptcy court's jurisdiction over a partnership's tax disputes was

unnecessary since the automatic stay under Bankruptcy Code § 362(a)(8) did not apply. Back reference: ¶ 40,630.0755.

On February 24, 1997, involuntary petitions under Chapter 7 were filed against W.J. Hoyt Sons Ranches, MLP and W.J. Hoyt Sons Management Co., Ltd. The court entered an order for relief and thereafter substantively consolidated the plaintiff partnerships with the bankruptcy cases of the original two debtors. Plaintiff partnerships are the subject of approximately 850 pending Tax Equity and Fiscal Responsibility Act (TEFRA) [FN1] proceedings in the United States Tax Court (TEFRA proceedings or partnership proceedings) in which a redetermination of partnership tax adjustments is sought. Cobb Affidavit ¶ 1. On July 27, 1999, plaintiff partnerships filed this complaint requesting that the court enforce the automatic stay against the partnership proceedings in the tax court and declare void any tax court ruling with respect to the partnerships since February 24, 1997.

FN1. For more on TEFRA procedures, see Willis, Pennell & Postlewaite, Partnership Taxation ¶ 20.01 et seq. (6th ed.1997).

DISCUSSION

Defendant moves the court for judgment on the pleadings and argues that plaintiffs' allegations fail to state a claim upon which relief can be granted because, under controlling law, 11 U.S.C. § 362(a)(8) does not automatically stay a partner's proceedings in the United States Tax Court when the partnership is in bankruptcy. In response, plaintiffs move the court for summary judgment and argue that as a matter of law § 362(a)(8) automatically stays the proceedings in the United States Tax Court. Under Fed.R.Civ.P. 12(c), made applicable to adversary proceedings by Fed. R. Bankr.P. 7012, "if matters outside the pleadings are presented to and not excluded by the court, a motion for judgment on the pleadings is treated as a motion for summary judgment." Because plaintiffs have filed a motion for summary judgment and presented matters outside the pleadings and the parties have been given "reasonable opportunity to present all material made pertinent" to such motion, defendant's motion for

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judgment on the pleadings shall be treated as a motion for summary judgment. Under Fed.R.Civ.P. 56(c), the court shall grant summary judgment when "there is no genuine issue as to any material fact and ... the moving party is entitled to a judgment as a matter of law."

1. Blackburn Affidavit and Exhibit 1

*2 Defendant moves to strike the affidavit of Gary L. Blackburn and attached Exhibit 1 on the grounds that the affiant presents facts of which he has no personal knowledge. Moreover, defendant argues that, if the affidavit is admissible as expert testimony under FRE 702, it should be excluded due to plaintiffs' failure to meet the requirements of Fed. R. Bankr.P. 7026 (incorporating Fed.R.Civ.P. 26).

Pursuant to Fed.R.Civ.P. 56(e), before an affidavit supporting or opposing summary judgment can be given weight, the affidavit "(1) shall be made on personal knowledge, (2) set forth such facts as would be admissible in evidence, and (3) show affirmatively that the affiant is competent to testify on the matters stated therein." *Coca-Cola Co. v. Overland, Inc.*, 692 F.2d 1250, 1255 (9th Cir.1982). An affidavit in support of summary judgment must be made on personal knowledge, not on information and belief. *Columbia Pictures v. Professional Real Estate Inv.*, 944 F.2d 1525 (9th Cir.1991) aff'd 113 S.Ct. 1920 (1993).

In his affidavit, Mr. Blackburn states (1) that he was a partner in at least one of the partnerships from 1984 through 1997, (2) that he worked on record organization, document retrieval and data processing for one of the Hoyt entities from 1994 through 1997, (3) that he is familiar with the partnerships' operation and history, (4) that he summarized in a spreadsheet the partners' unverified claims (attached as Exhibit 1), and (5) that 99 percent of the claims in these cases are subject to tax court proceedings. Blackburn Affidavit ¶ 1-6, 8. Blackburn's affidavit establishes his personal knowledge of these facts. Exhibit 1 attached to the affidavit contains Mr. Blackburn's summary of the unverified partners' claims in this case.

In paragraph 6, Mr. Blackburn states that the partners' claims against the bankruptcy estates are based on fraud. Defendant argues that the statement

is not based on personal knowledge and that it is a legal opinion by one not qualified as an expert. The affidavit is not clear whether the basis of the claims is apparent on the face of the claims, so that Blackburn could determine the basis simply by looking at the claims, or whether he had to reach a legal conclusion regarding the basis of the claims. As a result, I cannot tell that the statement is based on personal knowledge. I sustain the objection to this portion of paragraph 6. If the claims show on their face that they are based on fraud, the affidavit lacks a proper foundation to establish that Blackburn's statement is based on personal knowledge. If Blackburn had to draw some conclusions from the proofs of claim to determine the basis for the claims, the statement is an improper legal conclusion by a person not qualified as an expert. FRE 703. Therefore, the statement is inadmissible.

Paragraph 7 of the Blackburn affidavit contains predictions about the ultimate outcome of the tax court cases. Defendant's objection to paragraph 7 is sustained. Mr. Blackburn is a lay witness who is not qualified as an expert under FRE 702 to express such an opinion.

*3 In summary, the affidavit is admissible with the exception of portions of paragraphs 6 and 7. Defendant's motion to strike is granted with respect to Blackburn's opinion that the partners' claims against the bankruptcy estates are based on fraud in paragraph 6 and his prediction about the outcome of the tax court cases in paragraph 7.

2. Are the TEFRA proceedings tax court proceedings concerning the debtors?

(a) Overview

Section 362(a)(8) of the Bankruptcy Code provides that the filing of a bankruptcy petition stays "the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor." Any proceeding in violation of the automatic stay is void. *In re Schwartz* [92-1 USTC ¶ 50,069], 954 F.2d 569, 571 (9th Cir.1992). In addition to protecting the relative position of creditors, Congress designed the automatic stay to shield the debtor from financial pressure during the pendency of the bankruptcy proceeding. *Id.* To date, no controlling authority has

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decided whether § 362(a)(8) acts to automatically stay partnership proceedings in the Tax Court when the partnership is in bankruptcy. [FN2]

FN2. *Cheng v. Commissioner* [91-2 USTC ¶ 50,346], 938 F.2d 141 (9th Cir.1991) and *Delpit v. Commissioner* [94-1 USTC ¶ 50,127], 18 F.3d 768 (9th Cir.1994) dealt with whether § 362(a)(8) stayed appeals of tax court decisions.

The essence of the dispute is how the term "concerning" should be interpreted. Plaintiffs argue that the TEFRA proceedings concern the debtors for several legal and practical reasons. Plaintiffs point out that the plain language of § 362(a)(8) applies to all tax court proceedings concerning the debtor. This is in contrast to the other subsections of § 362(a), which are limited in their application only to actions "against" the debtor or "against" property of the estate. They assert that the bankruptcy case cannot be concluded until the tax liabilities of the partnerships and partners are resolved, because those liabilities are in effect the liabilities of the debtors. The tax court proceedings will take many years to complete, and may determine issues of fact and law that are important to the bankruptcy case, including ownership and value of partnership assets, validity of partnership indebtedness, the existence of the partnership entities, and potential estate liability for partners' tax liability based on tax manager or managing general partner fraud. According to plaintiffs, 99 percent of the claims filed in these consolidated cases relate to tax liability of partners or consequences flowing from that liability.

Defendants respond that Ninth Circuit case law rejects this broad interpretation of "concerning." Defendant argues that under applicable Ninth Circuit Court of Appeals authority a tax court proceeding does not concern the debtor unless it will possibly affect a tax liability of the debtor. Because partnerships are not tax-paying entities, a tax court proceeding involving a debtor partnership is not one "concerning" the debtor.

(b) Relevant Ninth Circuit case law

In *American Principals Leasing Corp. v. United States* [90-1 USTC ¶ 50,292], 904 F.2d 477 (9th Cir.1990), the court considered whether § 505 [FN3] of the Bankruptcy Code, which by its terms is not limited to debtors, authorized the bankruptcy

court to determine the tax liability of nondebtor partners of a debtor partnership. *Id.* at 480. After reviewing case law in other circuits and the legislative history of § 505, the court held that, although broad, the language of "section 505 was intended only to permit determination by the bankruptcy court of any unpaid tax liability of the debtor." *Id.* at 481 (citing *In re Brandt Airflex Corp.* [88-1 USTC ¶ 9258], 843 F.2d 90, 95 (2d Cir.1988) (citing legislative history)). Defendant argues that *American Principals* requires that the court similarly limit the scope of the stay under § 362(a)(8).

FN3. Section 505(a)(1) provides in pertinent part that "the court may determine the amount or legality of any tax[.]"

*4 As additional support, defendant looks to the Ninth Circuit's opinion in *Third Dividend/Dardanos v. Commissioner* [96-2 USTC ¶ 50,385], 88 F.3d 821, 823 (9th Cir.1996), and to language in that opinion that quotes a tax court decision holding that § 362(a)(8) does not operate to stay a partner's tax court proceedings when the partnership is in bankruptcy. The court in *Third Dividend* held, consistent with *American Principals*, that the tax court and not the bankruptcy court had jurisdiction to hear an indirect partner's tax redetermination petition when the general partner (an S-corporation) was in bankruptcy. In reaching its conclusion, the court explained that the term

"debtor" in bankruptcy statutes extends only to the debtor and does not include individuals who themselves have not filed for bankruptcy.... Thus, if a partnership declares bankruptcy, the bankruptcy court lacks jurisdiction over the non-debtor partners.

[96-2 USTC ¶ 50,385], 88 F.3d at 823.

Most significantly, in *Third Dividend* the court quoted with approval the tax court's decision in *Western Reserve Oil & Gas Co., Ltd. v. Commissioner* [CCH Dec. 46,717], 95 T.C. 51, 57 (1990), *aff'd* 995 F.2d 235 (9th Cir.1993) (table), which observed:

To argue that the partnership proceeding requires the Tax Court to make determinations with respect to the items of income, gain, loss, or credit of the partnership, rather than the individual partners, and that a partnership proceeding involving a bankrupt partner[ship] thus "concerns" the

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partnership, not the partner[s], is to exalt form over substance.

Id. [FN4]

FN4. Ninth Circuit panel misquoted words in brackets.

American Principals, Third Dividend and the Ninth Circuit's approval of the reasoning in *Western Reserve* raise doubt about whether § 362(a)(8) should be broadly construed to stay TEFRA proceedings involving partnerships that are debtors in bankruptcy.

In *Western Reserve*, the tax court faced essentially the same facts as those presented in this case. The tax court held that § 362(a)(8) does not stay a partner's petition of final partnership administrative adjustments when the partnership is in bankruptcy. [CCH Dec. 46,717], 95 T.C. at 51. As support for this decision, the tax court looked to two sources of authority. First, it looked at bankruptcy cases holding that (a) for bankruptcy purposes, a partnership is an entity separate and distinct from its partners; and (b) the filing of a bankruptcy petition does not ordinarily stay a proceeding against a partner in a bankrupt partnership. Second, the tax court read prior authority together with *American Principals* to require a narrow reading of § 362(a)(8). In essence, the tax court held that, because partnerships have no tax liability, the partners' tax proceedings never concern the partnership.

It is apparent that the Ninth Circuit, faced with broad language in § 505 authorizing the bankruptcy court to determine tax liability, has interpreted that language narrowly to apply only to a determination of tax liability of the debtor. In addition, it has quoted with approval a decision narrowly interpreting the language of § 362(a)(8) to apply only to tax court proceedings that concern a debtor's tax liability.

(c) Effect of tax court proceedings on administration of debtors' bankruptcy cases

*5 The tax court has decided and will decide the partners' ultimate tax liability, not that of the debtor partnerships. Essentially, the debtors' breathing spell is not impinged nor the orderly liquidation of

the estate affected. At most, plaintiffs have shown that not enforcing the stay would delay the administration of the bankruptcy case, because the partners' claims against the partnerships derive from their tax liability and those determinations will be made by the tax court.

Plaintiffs' concern about delays in the administration of the bankruptcy case can be handled by estimating the amount of the claims under § 502(c) of the Bankruptcy Code. Section 502(c) provides in pertinent part:

There shall be estimated for purpose of allowance under this section-

(1) any contingent or unliquidated claim, the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case. Thus, a delay in the tax court litigation will not necessarily unduly delay the administration of the bankruptcy estates.

Debtor also argues that the tax court proceedings could have an impact on the administration of the estate because they could in effect liquidate claims of the partners against the debtor partnerships. The theory is that the tax court could make findings in the proceedings involving the debtor partnerships, e.g., that the tax matters partner had committed fraud, which could be binding on the trustee in the bankruptcy cases, because the trustee is in privity with the partnership. If it were demonstrated that the proceedings in tax court would have the effect of liquidating claims against the bankruptcy estate, there would be a strong argument that § 362(a)(8) would stay that action. Liquidation of claims against the estate is a fundamental function of the bankruptcy court, and the liquidation of claims in the tax court would certainly concern the debtor.

In this case, however, there has not been a demonstration that the actions in tax court will have the effect of liquidating claims. Plaintiffs' arguments on this point were theoretical and speculative; counsel could not point to any specific effects in response to the court's request during argument for specifics. Therefore there is no basis in this case to interpret § 362(a)(8) to apply to the proceedings pending in tax court.

(d) Expanding the stay to nondebtors

Plaintiffs argue that, even if § 362(a)(8) does not

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usually apply to stay partnership proceedings in tax court, it should be applied to stay the actions in this case because they affect nondebtor parties and will have an adverse impact on the estate. Staying proceedings in which the debtor is not the real party in interest occurs only in unusual circumstances. See *A.H. Robins Co. v. Piccinin*, 788 F.2d 994, 999 (4th Cir.1986) (bankruptcy court may stay proceedings against nondebtor "when there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party defendant and that a judgment against the third-party defendant will in effect be a judgment or finding against the debtor.") That exception does not apply in this case. The debtor partnerships, although named as the parties in the tax court proceedings, are not real parties in interest, because they have no tax liability that can be affected by the tax court's rulings.

(e) Conclusion regarding interpretation of §
362(a)(8)

*6 In light of the circuit authority, I conclude that § 362(a)(8) should be read consistently with the holding in *Western Reserve*: the stay applies to proceedings that may affect the debtor's tax liability. Although I recognize that § 362(a)(8) could also apply to stay the proceedings if they would effectively result in liquidation of the partners' claims against the estates, there is no showing in this case that the tax court determinations will have that effect. Because a partner's tax court redetermination proceeding does not affect a partnership's tax liability and there is nothing before the court from which I could conclude that the redetermination may effectively determine claims against the estate, the stay does not apply.

3. Bankruptcy court jurisdiction to resolve the partnership tax disputes

Defendant asserts that plaintiffs' argument rests upon a faulty premise—that the bankruptcy court can decide the tax disputes involving the partnerships and the individual partners' tax liabilities arising from the partnerships. Although plaintiffs recognize that the Ninth Circuit's decision in *American Principals* precludes such a decision based on § 505, they argue that this court could assert jurisdiction over the partner's tax proceedings pursuant to 28 U.S.C. § 1334(b), Section 1334(b) gives bankruptcy

court jurisdiction over proceedings "related to" a bankruptcy case. Because I have concluded that the automatic stay does not apply, it is unnecessary in the context of this proceeding to determine whether this court would have jurisdiction over the tax matters under § 1334(b).

CONCLUSION

I conclude that the automatic stay does not apply to the tax redetermination proceedings that are taking place in tax court. Therefore, I will deny plaintiffs' motion for summary judgment and grant defendant's motion for judgment on the pleadings, which I have treated as a motion for summary judgment. Mr. Knight should submit an order disposing of the motions and a judgment dismissing the adversary proceeding.

END OF DOCUMENT