

BY ELIZABETH L. GUNN¹

A Day or a Decade

Failure to Meet Deadlines Makes Taxes Nondischargeable

“In this world, nothing is certain except death and taxes.”

— Benjamin Franklin, 1789

Benjamin Franklin’s famous words are especially prescient for debtors who fail to timely file pre-petition tax returns for income taxes that otherwise would be dischargeable. Section 523(a)(1)(A) excepts from discharge in cases under chapters 7, 11, 12 and 13 income taxes for which a return was “last due ... after three years before the date of the filing of the petition,” whether or not the return was actually filed or a claim is actually filed in the case.

For debtors who timely filed returns prior to that period, any unpaid income taxes prior to that period are eligible for discharge in individual cases. However, for the debtor with a history of failing to meet tax deadlines, § 523(a)(1)(B)(i) and the definition of a “return” added by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) under § 523(a)(*)² result in any tax obligations from such late-filed returns also being nondischargeable, regardless of whether the filing delay was a day, a year or a decade.

The case law discussing whether a tax obligation is nondischargeable pursuant to § 523(a)(1)(B)(i) hinges on the definition of a “return.” Prior to BAPCPA, the Bankruptcy Code did not define “return,” and a majority of circuits had adopted a form of a multi-factor test hinging primarily on a debtor’s intent to comply with the requirements of tax law. By adding a definition of “return,” BAPCPA requires that the return was not only filed but that it also satisfied the requirements of applicable nonbankruptcy law, including applicable filing requirements. The definition also specifically limits and defines the only safe harbors or exceptions to this rule for federal taxes, and neither of those requirements expand to a question of the debtor’s intent behind the delay in their filing. In addition, if a debtor complies with an applicable state law exception, such compliance might result in the dischargeability of the taxes.

Absent falling into a very narrow exception, with the addition of the definition of “return” in § 523(a)(*), Congress clearly intended to create a bankruptcy-specific consequence for individuals who fail to comply with tax-reporting requirements. In *McCoy v. Miss. State Tax Commission*, the Fifth Circuit determined that, absent qualifying under a safe harbor, a return that is filed late under applicable nonbankruptcy law is not a “return” for bankruptcy discharge purposes under § 523.³ This same standard was subsequently adopted by the First and Tenth Circuits, along with a number of lower courts interpreting both federal tax provisions and applicable state laws.⁴

Debtors with late-filed returns and their counsel frequently argue that the bright-line test established by *McCoy* and its progeny is unreasonably harsh, particularly to those debtors who made an “honest attempt” at filing or did not intend to disregard tax-filing deadlines. However, this view approaches the situation from the wrong direction: A debtor is entitled to a fresh start to the extent of the Bankruptcy Code, subject to the more than 19 exceptions to discharge enumerated by § 523(a).

Prior to BAPCPA, courts were left to the constructs of statutory interpretation to determine what qualified as a “return.” BAPCPA’s modification to § 523 clarified and specifically removed the “honest attempt” exception to the nondischargeability of late-filed taxes. By including only a few narrow exceptions, the language of § 523(a)(*) indicates that Congress determined that prompt compliance with tax laws is necessary for individuals to potentially be eligible to discharge such obligations. Although the impact of future dischargeability in bankruptcy of an obligation from a late-filed return might not be something of which an individual may be aware or have reason to know about, Congress’s exclusion from discharge for such taxes is one of a number of consequences of filing a late return.

Taxpayers who fail to file other returns are also subject to interest, penalties, fines and other consequences. The lack of the ability later to discharge such late-filed returns is merely another consequence of the failure to comply with tax deadlines.

Notwithstanding the arguments of debtors, this result is not abnormally harsh. The timeliness

¹ The opinions expressed herein are provided as a result of the author’s own experiences and not as a representative of the Attorney General or the Division of Child Support Enforcement, and some may have been adopted for the purposes of the debate in the Consumer Point/Counterpoint column.

² The definition of “return” is found in a hanging paragraph at the end of § 523(a) after § 523(a)(19), but was not provided with a subsection designation. Courts have uniformly adopted the designation of § 523(a)(*) as the citation for such paragraph.

³ 666 F.3d 924, 932 (5th Cir. 2012).

⁴ *Fahey v. Mass. Dep’t of Revenue*, 779 F.3d 1 (1st Cir. 2015); *Mallo v. IRS*, 431 F.3d 1313 (10th Cir. 2014).

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of a return is squarely within the ambit and control of an individual. In general, taxing authorities allow for a timely requested extension of deadlines, with such extensions being (essentially) automatically granted without the need for any specific justification. Returns filed within such extensions are treated as timely for purposes of § 523. The implications of nondischargeability are only set forth for those who chose not to comply with deadlines.

Just as a debtor who fails to comply with deadlines found in the Bankruptcy Code is subject to consequences, a debtor who has previously failed to comply with federal and state taxing deadlines should be subject to the loss of the potential to discharge any resulting obligations. This result further comports with the theory that

the Bankruptcy Code is intended to benefit the honest-but-unfortunate debtor.

Congress has clearly set forth that the debtor who elects, for whatever reason, not to comply with state and federal taxation guidelines, while otherwise perhaps honest and unfortunate, is not entitled to discharge such taxes. Whether a day or a decade late, and a day or a decade after such filing, the debtor's fate is determined when he/she fails to timely file returns. Bankruptcy courts cannot — and should not — override Congress's preference to require timely returns. *McCoy* and its progeny are correctly decided, follow Congress's intent for individuals to be held accountable for complying with taxation laws, and result in a straightforward analysis of what tax debts are dischargeable by a debtor. **abi**

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