

1                   IN THE SUPREME COURT OF THE UNITED STATES

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3   LYNWOOD D. HALL, ET UX.,                   :

4                   Petitioners                   :   No. 10-875

5                   v.                               :

6   UNITED STATES                               :

7   - - - - - x

8                               Washington, D.C.

9                               Tuesday, November 29, 2011

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11                   The above-entitled matter came on for oral  
12 argument before the Supreme Court of the United States  
13 at 10:03 a.m.

14 APPEARANCES:

15 SUSAN M. FREEMAN, ESQ., Phoenix, Arizona; on behalf of  
16 Petitioners.

17 PRATIK A. SHAH, ESQ., Assistant to the Solicitor

18 General, Department of Justice, Washington, D.C.; on  
19 behalf of Respondent.

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1 P R O C E E D I N G S

2 (10:03 a.m.)

3 CHIEF JUSTICE ROBERTS: We will hear  
4 argument first this morning in Case 10-875,  
5 Hall v. United States.

6 Ms. Freeman.

7 ORAL ARGUMENT OF SUSAN M. FREEMAN

8 ON BEHALF OF THE PETITIONERS

9 MS. FREEMAN: Mr. Chief Justice, and may it  
10 please the Court:

11 Bankruptcy estates incur taxes when they  
12 generate income. The government's attempt to limit the  
13 effect of the farm sale statute, section 1222(a)(2)(A),  
14 alters that fundamental principle in corporate Chapter  
15 11 cases and in all bankruptcy cases, as it requires  
16 this Court to construe the administrative section and  
17 the priority section of the Bankruptcy Code that do  
18 apply in all of those cases.

19 In a Chapter 12 case, the bankruptcy estate  
20 consists of more than just the assets that existed as of  
21 the date of filing. They also consist of all of the  
22 income that is earned thereafter, wages -- Mrs. Hall's  
23 wages as a convenience store clerk are part of the  
24 bankruptcy estate -- the proceeds from selling crops --

25 JUSTICE KENNEDY: Does it include debts

1 incurred after the filing?

2 MS. FREEMAN: From the period -- from the  
3 petition filing date until the confirmation of the plan,  
4 yes, it does. Those debts are incurred in the operation  
5 of the estate --

6 JUSTICE KENNEDY: Debts -- debts that were  
7 incurred after that date?

8 MS. FREEMAN: Yes, Your Honor. So that, for  
9 example, in operating an estate, you would incur a light  
10 bill as well as incurring taxes. All of the operating  
11 expenses are incurred by the bankruptcy estate, and are  
12 payable from the income and from the estate assets  
13 during that period from the petition filing date until  
14 the confirmation of the plan. That's the administrative  
15 period.

16 JUSTICE GINSBURG: Is that true of State --  
17 you said taxes. Is it true of State taxes?

18 MS. FREEMAN: Yes, Your Honor, it is true of  
19 State taxes as well as Federal taxes. County taxes, for  
20 example. Property taxes --

21 JUSTICE GINSBURG: We're dealing -- in  
22 this -- we're dealing with a capital gains tax on the  
23 sale of the farm. Suppose a State had a similar tax; it  
24 also taxed the gain on the sale.

25 MS. FREEMAN: Correct, Your Honor, and it

1 did in this particular case. So there would be State  
2 taxes on the capital gains, and those would also be  
3 administrative expense priorities, except for the farm  
4 sale provision here, which demotes that priority if the  
5 debtor is able to earn a discharge. And if so, then  
6 those farm sale taxes are demoted in priority and may be  
7 discharged under a plan of reorganization. They would  
8 share pro rata with the other prepetition claims of the  
9 bankruptcy estate.

10 JUSTICE ALITO: Who would file the State tax  
11 return? Would it be filed by the estate or would it be  
12 filed by the debtor?

13 MS. FREEMAN: The debtor and the estate are  
14 one in a -- in a reorganization case. And so the  
15 taxpayers, Lynwood and Brenda Hall, would file the tax  
16 return. The way that it would actually be administered,  
17 Your Honor, is shown by the Knudsen case. And  
18 basically, there would be a tax return that includes all  
19 of the income, the wages, the crop sale proceeds and so  
20 forth. And then it would compute it with the capital  
21 gains tax, and there would be a separate pro forma  
22 return that does not include the capital gains tax.

23 Those would be sent to the Special  
24 Procedures Unit of the IRS, so that somebody there would  
25 know how to deal with it and would be able to count the

1 difference.

2 JUSTICE SOTOMAYOR: Counsel, how do you deal  
3 with section 346?

4 MS. FREEMAN: Section 346, Your Honor,  
5 basically makes the State taxes consistent with the  
6 Federal taxes. When you have --

7 JUSTICE SOTOMAYOR: I read 346(b) to say  
8 that, unless the estate is a separate tax entity under  
9 the code, that the debtor, not the estate, pays State  
10 and local taxes. This is totally contrary to what  
11 you're saying, but the language of 346(b) basically  
12 answers the question against you with respect to State  
13 and local taxes.

14 MS. FREEMAN: Justice Sotomayor, I do not  
15 think it does, in the sense -- in this sense. The  
16 bankruptcy -- section 346(b) made the State and local  
17 taxes consistent with Federal taxes, and when you have a  
18 bankruptcy estate that consists only of assets on the  
19 petition filing date, then you have a separate taxable  
20 entity with a separate tax I.D. number that is set up.  
21 But under the Federal bankruptcy -- under the Federal  
22 tax code, under section 1399, whenever the bankruptcy  
23 estate had income during the course of the estate,  
24 during the administration period, as well as the assets  
25 on the petition filing date, then it's a single taxable

1     entity. And so that single taxpayer would pay it.

2                     Section 346 doesn't say what assets are used  
3     to pay the tax. That's a matter of bankruptcy law. The  
4     debtor, the individual taxpayer, is going to file the  
5     tax return under State and local and Federal law, but  
6     he's going to use the estate assets because that's all  
7     there is. He doesn't have any other assets.

8                     JUSTICE SOTOMAYOR: So the debtor is going  
9     to pay, and so when this --

10                    MS. FREEMAN: The debtor pays --

11                    JUSTICE SOTOMAYOR: -- says -- whenever the  
12     Internal Revenue Code of 1986 provides that no separate  
13     taxable estate shall be created in a case concerning a  
14     debtor under this title --

15                    MS. FREEMAN: Right.

16                    JUSTICE SOTOMAYOR: -- Chapter 12 doesn't  
17     create a separate taxable estate.

18                    MS. FREEMAN: Correct.

19                    JUSTICE SOTOMAYOR: And that the income,  
20     et cetera, shall be taxed to or claimed by the debtor  
21     under State or local law.

22                    MS. FREEMAN: That's correct, Your Honor.  
23     It's going to be on the debtor's tax return. The  
24     debtor's the one who will have the deductions and the  
25     deductions would include administrative expenses of the

1     bankruptcy estate.

2                   JUSTICE SOTOMAYOR:   This -- this is hard for  
3     me to understand, given the last line.   "The estate  
4     shall be liable for any tax imposed on such corporation  
5     or partnership, but not for any tax imposed on partners  
6     or members."

7                   By the logic of that last sentence, it seems  
8     to me that the preceding section is not looking to the  
9     estate, but to the debtor, to pay the taxes.

10                  MS. FREEMAN:   The debtor pays the taxes, but  
11     with estate assets, because those are the only assets  
12     that exist.

13                  JUSTICE SOTOMAYOR:   So why -- why would the  
14     last sentence be necessary?

15                  MS. FREEMAN:   The last sentence, I believe,  
16     Your Honor, deals with the partnership, and in a  
17     partnership case, just as outside a bankruptcy the  
18     partnership files the tax return and the partners  
19     individually are the ones who pay the taxes.   But they  
20     pay the taxes -- if a partner is in its own bankruptcy  
21     estate with the only assets that exist, all of his  
22     income, all of his wages, all of those are property of  
23     the bankruptcy estate, and he would use it to pay the  
24     taxes.   He's not individually liable any more than if a  
25     trustee were individually liable.   The trustee in a



1 bankruptcy case uses estate assets to pay taxes. And so  
2 with --

3 JUSTICE KENNEDY: But it says the estate --  
4 the estate's not liable for the tax imposed on the  
5 partners. So if it's not liable, how can it ask for a  
6 discharge?

7 MS. FREEMAN: The -- the debtor ultimately  
8 is the one who receives a discharge. Discharge  
9 provisions are separate than the -- than the tax payment  
10 issues. Tax payment deals with what monies are used to  
11 make the payments of taxes during the course of  
12 administration of a bankruptcy case. The debtor  
13 receives a discharge in a Chapter 12 case if it  
14 complies -- if he complies with all of the provisions of  
15 his plan of reorganization and then receives a  
16 discharge.

17 There are exceptions to the discharge.  
18 Certain prepetition taxes are excepted from a discharge  
19 and would carry through during the -- postpetition. But  
20 the farm sale statute provides that these particular  
21 administrative expenses would be subject to a discharge  
22 if he complies with the rest of the provisions of the --  
23 of his plan of reorganization.

24 JUSTICE BREYER: What happens in a 12 or 13  
25 case, just your typical case -- and this must arise

1 fairly often -- in year 1, on January 1 the farm or the  
2 ship or whatever is the subject goes into Chapter 12 or  
3 13. They have a lot of pre-1 debt. Then in year 2 and  
4 year 3, the proceedings are going on, but the farm is  
5 operating, so is the ship, or whatever. And they  
6 earn -- they run up debts during that time. People give  
7 them fertilizer -- you know, all kinds of things. So  
8 they have a lot of debts that they've run up in that  
9 time.

10 Now, it draws to a close at the end of  
11 year 3. Now, what about those debts that have been run  
12 up during that time? There isn't a separate bankruptcy  
13 estate for tax purposes, I understand. But if Joe Smith  
14 has loaned his farm some money during that time, and it  
15 comes time to look at the future income to subtract the  
16 prepetition debts, does his debt get wound up and get  
17 some priority in that process, or is he just at the end  
18 of the queue?

19 MS. FREEMAN: He does get priority in that  
20 process, Your Honor.

21 JUSTICE BREYER: All right. Well, if he  
22 gets priority, then why in heaven's name shouldn't a tax  
23 get priority?

24 That's your point.

25 MS. FREEMAN: Your Honor, it does have that

1 priority.

2 JUSTICE BREYER: And if it does, then, of  
3 course, the exception that Senator Grassley put in  
4 applies to that. So that's a question I should ask  
5 them, given your answer.

6 MS. FREEMAN: Yes, Your Honor.

7 And in fact, those taxes, along with the  
8 light bill and any other administrative expenses, would  
9 be paid when due over that 2- or 3-year period. And  
10 that's certainly what happens in the large Chapter 11  
11 bankruptcy case, like a Delphi bankruptcy case or a  
12 General Motors --

13 CHIEF JUSTICE ROBERTS: Well, but I mean,  
14 your -- it is a question for you, because these things  
15 don't go for 2 or 3 years, do they? I thought typically  
16 they were wrapped up very quickly, and that's to the  
17 advantage of the debtor. And your position with respect  
18 to postpetition taxes has the potential of extending  
19 them beyond the kind of quick turnaround that helps  
20 everybody.

21 MS. FREEMAN: Respectfully, Mr. Chief  
22 Justice, in Chapter 12 cases often the bankruptcy estate  
23 will drag on for 2 or 3 years, and certainly for longer  
24 than 1 year, and much longer than a Chapter 13 case,  
25 because you do have sales of assets. You have debts

1 that need to be restructured. You have leases that end  
2 up getting rejected. You have a -- new crop subsidies  
3 that are applied for and received. The chapter -- the  
4 amicus curiae brief of the professors has a study, and  
5 shows how long Chapter 12 cases generally last --

6 CHIEF JUSTICE ROBERTS: How long was this --  
7 this one?

8 MS. FREEMAN: This case, Your Honor, because  
9 of this appeal has lasted from 2005 through today, so a  
10 considerable period of time. And all of the taxes  
11 during that period of time and all of the operating  
12 expenses during that period of time are administrative  
13 expenses and are payable in the ordinary course. There  
14 is an administrative expense claim if in fact they  
15 haven't been paid.

16 And if -- if one of the creditors has not  
17 received payment or if a taxing authority has not  
18 received payment, it can move for payment as an  
19 administrative priority. It can ask that it be paid  
20 now, and it can ask that the case be dismissed if it  
21 hasn't been paid. So you -- you do have that highest  
22 priority, and this is consistent with the Court's  
23 Nicholas case, 1966, which preceded the Bankruptcy Code  
24 and which the Bankruptcy Code really incorporated and  
25 continued with.

1           In the Nicholas case the Court said that all  
2     taxes incurred by a debtor-in-possession and incurred  
3     during the administration period have administrative  
4     expense priority, and they are payable by the  
5     debtor-in-possession as an officer of the court, as the  
6     administrator of the estate under 28 U.S.C. section 960,  
7     which is still in effect today, and which requires that  
8     the person in control of the bankruptcy estate, whether  
9     it's a trustee or a debtor in possession, pay those  
10    taxes, but not pay them with his own money.

11           As the Court said in the Nicholas case, you  
12    pay them with the assets of the estate. The individual  
13    trustee is not responsible; the individual debtor in  
14    possession is not responsible. The responsibility of  
15    the debtor-in-possession really is a matter of the  
16    discharge provisions, whether he's going to be  
17    separately discharged or if he has responsible person  
18    liability because he's -- he's -- you're dealing with  
19    trust fund taxes, with wages from some other person.

20           JUSTICE KENNEDY: The -- what you say to me  
21    makes a great deal of sense, but I think one of their  
22    stronger arguments is, it may make sense, but  
23    unfortunately, even if Senator Grassley and the others  
24    wanted it, they didn't do it right technically. They  
25    didn't amend the right provision of the code, and

1     whoever's fault that is, is beside the point. So there  
2     is no way to get the words to get to the result that you  
3     want.

4                     I'll tell you the best I could do, and I see  
5     a problem with it. If you say that -- you go to  
6     1226(b)(1) and it says that any unpaid claim of the kind  
7     specified in 507(a)(2) -- and 507(a)(2) talks about  
8     administrative expenses and refers you to 503; and 503  
9     includes taxes and administrative expenses -- and then  
10    you say it's, at 1220 whatever it is, what did I just  
11    say?

12                    MS. FREEMAN: 1226?

13                    JUSTICE KENNEDY: 1226. .

14                    MS. FREEMAN: Uh-huh.

15                    JUSTICE KENNEDY: It's like an Abbott and  
16    Costello movie.

17                    (Laughter.)

18                    JUSTICE KENNEDY: The -- the -- you get to  
19    1226(b)(1) and it says that that that's -- shall be paid  
20    any unpaid payments of that kind, including  
21    administrative expenses, and -- and so then you have  
22    1222(a), which refers to that and then the amendment  
23    applies to that.

24                    But what I did was I sloughed over by  
25    talking too quickly -- it talked about "claim" -- of a

1 "claim," it says, any unpaid claim of the kind specified  
2 in 507(a)(2). And when you look to 507(a)(2), it talks  
3 about claims and expenses; and then in (2) there it  
4 refers to administrative expenses. And so I think the  
5 government says they left out what was key to you, the  
6 word "expense."

7 All right? Now, I don't know what I'm doing  
8 when I start tinkering with this Bankruptcy Code. And  
9 is that just true, what they say? It does leave out the  
10 word "expenses." Will -- will we cause untold harm if  
11 we were to read the word "claims" there to include  
12 expenses?

13 MS. FREEMAN: Your Honor; respectfully, you  
14 would cause untold harm because this provision applies  
15 in corporate Chapter 11's and in all bankruptcy cases.  
16 They all have the administrative expense provision, 503,  
17 and they all have section 507. So you would stop taxes  
18 from being payable in a big Delphi --

19 JUSTICE KENNEDY: No, but I was thinking, so  
20 if I do it by reading the word "claims" --

21 MS. FREEMAN: Right.

22 JUSTICE KENNEDY: -- in 5 -- in 1226, when  
23 it says "any unpaid claim" --

24 MS. FREEMAN: Right.

25 JUSTICE KENNEDY: Which is what you want to

1 have include taxes --

2 MS. FREEMAN: And claim --

3 JUSTICE KENNEDY: -- to read that word as  
4 including both the 507(a) claims, which are in (1)(a),  
5 (1)(b), and -- also administrative expenses in (2). Can  
6 I do that?

7 MS. FREEMAN: You can, Your Honor, because  
8 "claim" is defined in section 101 of the code as right  
9 to payment. "Creditor" is defined as someone who has a  
10 claim that arose prepetition, which necessarily means  
11 claim is broader and not just one that arose  
12 prepetition.

13 There are numerous provisions of the  
14 Bankruptcy Code that refer to administrative expenses as  
15 claims, including 1226. And so the Court can see that  
16 those are interpreted consistently.

17 This Court in the Hartford Underwriters case  
18 referred to administrative claims, calling them claims  
19 as well as administrative. And really what the  
20 government's argument here is that administrative  
21 expenses are outside of bankruptcy altogether, that they  
22 are not part of what get paid in a bankruptcy case. And  
23 that's simply untrue.

24 If the Court looks at the provisions with  
25 respect to requirements of a plan, including 1222(a),



1    which apart from the exception, it says that  
2    administrative expenses are required to be paid.  
3    Section 1228 says that a plan discharges all debts  
4    including debts provided for, allowed under section 503.  
5    Debt is a liability on a claim.

6                   JUSTICE BREYER:   But that's -- that's my  
7    first question.   What actually happens?   I mean, this  
8    isn't the first year of Chapter 12 and 13.

9                   MS. FREEMAN:   Right.

10                  JUSTICE BREYER:   And there must be instances  
11    where the -- where the debts run up postpetition are  
12    pretty big --

13                  MS. FREEMAN:   And --       .

14                  JUSTICE BREYER:   -- and there isn't enough  
15    money to go around and they are going to have to be paid  
16    out of future income along with the prepetition debts;  
17    and it can be done, but there is a question of  
18    priorities; and the government is saying there is no  
19    priority -- I think they are saying that -- for a  
20    postpetition debt, and -- and you're saying:   Oh, but of  
21    course there is.

22                  So what actually happens?   There have been  
23    perhaps thousands and thousands of cases, haven't there?

24                  MS. FREEMAN:   And administrative expenses do  
25    get paid in the ordinary course.   And if --

1 JUSTICE BREYER: Get paid, if necessary, by  
2 assigning priorities?

3 MS. FREEMAN: Yes. They have administrative  
4 priority and they do get paid.

5 JUSTICE BREYER: And so to look to a  
6 Hornbook on -- on bankruptcy law which just tells me  
7 what you've just said, I would look where?

8 MS. FREEMAN: We -- we've cited a number of  
9 hornbooks that have exactly that provision. What is  
10 particular interesting with respect to the government's  
11 position here is that, at the government's urging  
12 section 507(a)(8) of the Bankruptcy Code, that provided  
13 for prepetition priority, eighth priority, for  
14 prepetition taxes within a short period before the  
15 Bankruptcy Code, was amended; so that all of those  
16 eighth priority taxes during the year of the filing, the  
17 straddle year -- here the Halls filed their bankruptcy  
18 case in August, so during the entire period from  
19 January 1 through August when they filed -- are treated  
20 as administrative expenses. And yet now they say  
21 administrative expenses mean nothing and they don't get  
22 any payment as administrative expenses.

23 Why urge the change? Why make all of those  
24 year of filing taxes into administrative expenses and  
25 then say the administrative expenses have no meaning?

1 JUSTICE SOTOMAYOR: I'm going to ask the  
2 government this, but are you aware of any circuit split  
3 or any cases below that have accepted the government's  
4 arguments that Chapter 12 involves prepetition debts  
5 only and that don't pay administrative expenses  
6 postbankruptcy?

7 MS. FREEMAN: There are several cases that  
8 have interpreted section 1222(a)(2)(A). None of them  
9 have addressed the change in 507 or what that means.

10 JUSTICE SOTOMAYOR: That's a different  
11 question.

12 MS. FREEMAN: Okay.

13 JUSTICE SOTOMAYOR: The government's now  
14 saying that Chapter 12 involves only prepetition claims.

15 MS. FREEMAN: Right.

16 JUSTICE SOTOMAYOR: And it's basically by  
17 that argument saying it doesn't involve and can't  
18 involve administrative expenses. That's how I read  
19 their argument.

20 MS. FREEMAN: I think that's --

21 JUSTICE SOTOMAYOR: And so I'm asking is --  
22 are there any courts that you are aware of below who  
23 have been presented with this argument outside of the  
24 tax situation who have accepted it?

25 MS. FREEMAN: I --

1 JUSTICE SOTOMAYOR: Who have failed to give  
2 priority to administrative expenses?

3 MS. FREEMAN: None outside of this tax  
4 situation. And Your Honor, I don't believe that any of  
5 the cases that have followed the government's  
6 interpretation of this farm sale statute, 1222(a)(2)(A),  
7 have addressed the impact on other administrative  
8 expenses and other tax claims. The wages -- the taxes  
9 on wages that are incurred, the lottery winnings that an  
10 individual farmer may have, and the fact that those have  
11 administrative priority and that those would need to be  
12 paid off the top as administrative expenses -- none of  
13 the cases address those.

14 JUSTICE SOTOMAYOR: I'm not asking you to  
15 defend their position.

16 MS. FREEMAN: Okay.

17 JUSTICE SOTOMAYOR: It's just such a broad  
18 position that I'm trying to understand if there is a  
19 split out there that we are unaware of.

20 MS. FREEMAN: And the problem, Your Honor,  
21 is that it does have these broad impacts and none of the  
22 courts have really addressed it, and I don't believe  
23 that certainly the --

24 JUSTICE SOTOMAYOR: So can we go back to the  
25 issue that gives me trouble?

1 MS. FREEMAN: Yes, Your Honor.

2 JUSTICE SOTOMAYOR: How to read "incurred by  
3 the estate." If the estate doesn't pay taxes --

4 MS. FREEMAN: To incur --

5 JUSTICE SOTOMAYOR: -- how could it be  
6 incurred by the estate when Congress, if it intended  
7 what you're saying it intended, could have said  
8 "incurred during bankruptcy"?

9 MS. FREEMAN: Incurred -- to incur is to  
10 take on liability. So at the point in time that income  
11 is generated during a bankruptcy case, then liabilities  
12 are taken on at the same time, the operating expenses,  
13 the taxes. Here you had a clear estate asset, the Hall  
14 farm. It was sold. That generates an income tax  
15 liability, a capital gains liability, and so that is --  
16 it -- it's tied to the income which is here property of  
17 the estate. The -- the --

18 JUSTICE SCALIA: The -- the problem is that,  
19 with an exception that -- that is not applicable here,  
20 section 1399 of the Internal Revenue Code provides that  
21 no separate taxable entity shall result from the  
22 commencement of a case under Title XI of the United  
23 States Code.

24 How can you incur a tax when you are not a  
25 separate taxable entity?

1 MS. FREEMAN: Your Honor, because you are a  
2 single taxable entity instead of a separate taxable  
3 entity. The whole reason for the separate taxable  
4 entity section was when you had a bankruptcy estate that  
5 consisted only of the assets on the petition filing  
6 date, and the debtor earns income independently, so the  
7 debtor would independently have tax liability, and that  
8 would be separate from the estate.

9 But when you have a reorganization case, a  
10 corporate Chapter 11 or a Chapter 12, then the estate  
11 and the debtor are a single taxable entity and the  
12 debtor is the one that files the tax returns or the  
13 debtor-in-possession or the trustee, if there is  
14 a trustee in control --

15 JUSTICE SCALIA: But if that exception were  
16 intended, the provision I read contains an exception.  
17 It says "except in any case to which section 1398  
18 applies." 1398 applies to Chapter 7 and Chapter 11  
19 where the debtor is an individual.

20 MS. FREEMAN: That's --

21 JUSTICE SCALIA: Now, if there is an  
22 additional exception for Chapter 12 of the sort that you  
23 allege, why wasn't that put in there?

24 MS. FREEMAN: There is no exception and  
25 there shouldn't be an exception, Your Honor. They are

1 within section 1399, just like corporate Chapter 11  
2 debtors. The debtor is the one that files the tax  
3 return. The debtor and estate are one. All of that  
4 corporate earnings, all of the wages, the lottery  
5 winnings, the farm sale proceeds, all of those are part  
6 of the estate. And so --

7 JUSTICE SCALIA: What does it mean, then, to  
8 say that no taxable -- "no separate taxable entity shall  
9 result"? What does it mean, unless it means that it is  
10 not the estate which occurs the tax?

11 MS. FREEMAN: Your Honor, respectfully,  
12 there is a difference between taxable entity and estate.  
13 The estate is a collection of property, that is the  
14 collection of property that is operated by the  
15 debtor-in-possession or trustee in a reorganization  
16 case.

17 JUSTICE SCALIA: Well, but they -- but they  
18 would not have needed the exceptions for Chapter 7 and  
19 Chapter 11 where the debtor is an individual if what you  
20 say is true, if indeed a bankrupt estate is, as you say,  
21 not an entity at all.

22 MS. FREEMAN: You need that exception, Your  
23 Honor, in a Chapter 7 case for an individual because the  
24 individual earns income that is wholly independent from  
25 the estate, that is not part of the estate. So that the

1 bankruptcy estate consists of the assets that the  
2 individual owns on the petition filing date. The  
3 trustee administers those, sells the assets, may incur  
4 some liability for selling the assets for taxes, pays  
5 those and deals with those, while the individual  
6 continues to earn income postpetition that's his own  
7 income. And so you need to have a separate taxable  
8 estate in those instances.

9 But when the income that's earned during  
10 this whole period of administration, from the petition  
11 filing date to the confirmation date of the plan, is all  
12 property of the estate, then the debtor, the corporate  
13 Chapter 11 debtor or the corporate Chapter 12 debtor or  
14 the individual Chapter 12 debtor is incurring that  
15 income as part of the estate. It's all property of the  
16 estate in a Chapter 12 case. Section 1207 says that.  
17 And so the debtor is the one that files the tax returns  
18 and the debtor uses the estate assets to make the  
19 payments of the taxes and to make the payments on the  
20 light bill, and to make the payments on all of the other  
21 expenses of administration during this period of  
22 administration. That's what this Court held in Nicholas  
23 and that continues on in effect today.

24 JUSTICE KAGAN: But, Ms. Freeman, wouldn't  
25 it be fair to say then that the taxes are incurred by



1 the debtor and payable out of the estate. Why does it  
2 say "incurred by the estate"?

3 MS. FREEMAN: It uses the term "incurred by  
4 the estate" I think based upon the same kind of language  
5 that this Court used in Nicholas, as incurred by,  
6 incurred during the administration period, incurred by  
7 the debtor-in-possession. It's really a broad sense of  
8 all of the kinds of bankruptcy estates in a Chapter 7  
9 case. This refers to all bankruptcy cases. And so in a  
10 Chapter 7 case it's going to be just the assets that  
11 exist there on the petition filing date. If it's a  
12 corporate case it's going to be all of the assets that  
13 are generating the income during the course of the  
14 administration of the Chapter 12 or the Chapter 11 case  
15 or even the Chapter 13 case.

16 In Chapter 13 cases you have a specific  
17 additional provision, section 1305, that deals with  
18 taxes payable postpetition, and it also includes  
19 postconfirmation, so it gives the government a broader  
20 kind of right so that --

21 JUSTICE GINSBURG: The argument is made  
22 against your position that 1305 is one of the provisions  
23 that was featured I think both in the Ninth Circuit and  
24 the Tenth Circuit, and their position seems to be that  
25 1305 gives the government an election.

1 MS. FREEMAN: It does, Your Honor, provide  
2 for an election for the government. What's important is  
3 that in a 13 case, unlike a 12 or an 11, you have a very  
4 short period of administration. They have to file their  
5 plan within 15 days. It's confirmed within a month or  
6 2. And it's very unlikely that April 15th is going to  
7 fall within that short period of time and that's when  
8 the government says that your taxes are incurred. So  
9 you're going to have a -- it's unlikely you're going to  
10 have an administrative expense claim for your income  
11 taxes during the period of administration of a Chapter  
12 13. It's a very short period.

13 So the government has the option not only  
14 during the administration period, but also during the  
15 whole period of the plan, to elect to say: All right,  
16 there have been some big commissions earned here and I  
17 want to go ahead and collect from the estate rather than  
18 just wait and see what the debtor earns afterwards. And  
19 so it then can go ahead and file a claim and ask to have  
20 that claim paid out of the bankruptcy estate, and it  
21 really gives the government much broader rights than it  
22 does in a normal Chapter 11 or a Chapter 12 case or a 7.

23 If I may reserve the remainder of my time  
24 for rebuttal.

25 CHIEF JUSTICE ROBERTS: Thank you,

1 Ms. Freeman.

2 MS. FREEMAN: Thank you.

3 CHIEF JUSTICE ROBERTS: Mr. Shah.

4 ORAL ARGUMENT OF PRATIK A. SHAH

5 ON BEHALF OF THE RESPONDENT

6 MR. SHAH: Mr. Chief Justice, and may it  
7 please the Court:

8 The postpetition income tax liability at  
9 issue in this case is not subject to section 1222(a)(2)  
10 and thus cannot be treated as a dischargeable  
11 nonpriority debt for two reasons. First, consistent  
12 with the structure of Chapter 12, a Chapter 12 plan is  
13 limited to prepetition debts and does not cover  
14 postpetition debts, including administrative expenses.  
15 Rather, postpetition administrative expenses are paid  
16 separately through section 1226(b)(1), which contains no  
17 farm sale exception. Because section 1222(a)(2)(A)  
18 strips priority only from a subset of claims covered by  
19 a Chapter 12 plan and does not alter which debts fall  
20 within that plan, it cannot apply to the postpetition  
21 tax liability at issue.

22 JUSTICE GINSBURG: So what -- what farm  
23 sales would be included? What farm sales would get this  
24 benefit that Senator Grassley obviously wanted them to  
25 have?

1                   MR. SHAH: Your Honor, it would be  
2     prepetition sales. That is, any capital gains tax  
3     incurred from a prepetition sale, those would be  
4     priority expenses covered under a Chapter 12 plan under  
5     section 1222(a)(2), because they fall under -- they are  
6     an -- they are a priority claim under section 507(a).

7                   CHIEF JUSTICE ROBERTS: Does that make  
8     sense, though, in terms of if you are talking about  
9     farmers and fishermen and you are talking about the  
10    treatment of their central asset, whether it's the farm  
11    or typically the boat, and they either want to try --  
12    they want to try to save the farm or the boat, and they  
13    go into bankruptcy and the big issue is how that asset's  
14    going to be treated and your position is it's not in the  
15    bankruptcy at all, it's outside of it. That seems to me  
16    to be at least counterintuitive.

17                  MR. SHAH: Well, Your Honor, two points.  
18    One, as a practical matter Chapter 12 is a  
19    reorganization provision. It's not a provision just  
20    designed to allow farmers to get out of the business of  
21    farming. So often what will happen is that the farmers  
22    will try to reorganize some of their farm sale assets,  
23    sell some of their livestock, change their farming  
24    operation, to see if they can save it outside of  
25    bankruptcy first.

1 All of those sales -- an example of that is  
2 the Knudsen case. Knudsen is the only circuit case to  
3 go Petitioner's way. In Knudsen it not only involved  
4 the postpetition tax liability of the type at issue in  
5 this case. It also had a significant prepetition tax  
6 liability component in that case based upon just what I  
7 was explaining, the farmer trying to reorganize, trying  
8 to change the farming operation to save the farm without  
9 having to go into bankruptcy.

10 CHIEF JUSTICE ROBERTS: Yes, but also I  
11 gather it's a fairly typical situation where you have  
12 farmers that might want to sell part of the farm. You  
13 know, they have dairy and corn operations or something,  
14 and they sell one to try to preserve the other. And  
15 that's -- that's exactly the sort of thing that should  
16 be considered in the bankruptcy context, and yet your  
17 position says we're going to treat it outside the  
18 bankruptcy.

19 MR. SHAH: Well, Your Honor, it certainly  
20 happens within the bankruptcy, and I'm not disputing  
21 your point that that may -- that may arise in a  
22 bankruptcy case just like it arises in this case. And  
23 it will be dealt through the bankruptcy. That is, the  
24 sale will happen and it will be approved by the  
25 Bankruptcy Court. The question is how do you treat the

1 capital gains tax arising --

2 CHIEF JUSTICE ROBERTS: But that's a big  
3 deal if you're deciding how the plan's going to work.  
4 What the amount was here was big for the farmer and the  
5 idea of well, we are going to pretend that's not at  
6 issue here seems to me to be -- again, not to make a lot  
7 of sense.

8 MR. SHAH: Your Honor, we are not asking, to  
9 be clear, to pretend that that's not there. How the tax  
10 liability would be dealt with under the government's  
11 view is at the time the debtor moves to sell the farm  
12 asset during the case. Like in this case, that sale of  
13 the farm asset generated \$960,000. That was the sale  
14 price. The capital gain tax liability in this case is  
15 \$29,000. If they would have set aside from that  
16 \$960,000 sale price \$29,000 to pay the capital gains tax  
17 debt, that would resolve the issue. We are not  
18 saying that you ignore it.

19 JUSTICE KAGAN: But there's every reason to  
20 think, Mr. Shah, that what Congress was worried about  
21 here was cases in which the bankruptcy plan would not be  
22 approved at all because there were very high capital  
23 gains taxes that would result from a sale; and that that  
24 was the problem that everybody was focused on, was  
25 making sure that farmers could take advantage of section

1 12. So it's a little bit odd -- it's actually more than  
2 a little bit odd. It's a lot odd to read the statutes  
3 to apply not in that context, but only as to people who  
4 have somehow managed to sell their property, you know,  
5 18 months before going into bankruptcy.

6 MR. SHAH: Sure. Your Honor, when you say  
7 that everybody was focused on this problem, we have the  
8 evidence of exactly one person as to what one legislator  
9 thought that this bill would do. That's Senator  
10 Grassley. Now, admittedly, Senator Grassley's  
11 statements do indicate an intent on his part to reach  
12 postpetition taxes. But the preexisting statutory  
13 framework does not permit that result.

14 What section 1222(a)(2)(A) does is it allows  
15 the debtor to strip priority from a certain subset of  
16 governmental claims, such as prepetition taxes, and  
17 there is no doubt that Senator Grassley correctly  
18 understood that's how section 1222(a)(2) --

19 JUSTICE ALITO: It's not just Senator  
20 Grassley. Your interpretation makes this provision,  
21 1222(a)(2)(A), of very, very little practical value.  
22 You think that's what Congress intended? Not only would  
23 it -- would it mean that postpetition capital gains on  
24 the sale of part of the farm or the entire farm would be  
25 outside of the bankruptcy, outside of the bankruptcy,

1 but all of the prepetition capital gains would be  
2 outside of it too, unless they occurred in a previous  
3 taxable year.

4 MR. SHAH: A couple of responses, Your  
5 Honor. First of all, I don't think it's sort of a null  
6 set or a vanishingly small set. There is the Knudsen  
7 case which qualifies. In the professors' amicus brief,  
8 on page 10a of their amicus brief, they provide a chart  
9 of representative cases involving postpetition tax  
10 liabilities. They cite eight cases in their chart on  
11 page 10a. Three of those eight cases involve  
12 significant prepetition tax liabilities, even under the  
13 narrower definition of "prepetition."

14 But-- but to get to your larger point, even  
15 to the extent it might be narrower than what Congress  
16 intended, Congress certainly knew how section 1222  
17 operated in the sense that it would strip priority from  
18 certain claims that are already entitled to priority  
19 under a Chapter 12 plan, such as prepetition taxes. And  
20 both sides agree that that's how section 1220(a)(2)(A)  
21 works. There is no dispute about that. The dispute is  
22 about whether this postpetition tax liability comes  
23 within the Chapter 12 plan in the first place. That  
24 dispute turns on preexisting code provisions, part of  
25 the 1978 Act, part of the 1980 Act and the 1986 Act.



1    Whatever deference Senator Grassley is owed as to the  
2    operation of section 1220(a)(2)(A) itself, he is owed no  
3    deference whatsoever as to the proper interpretation of  
4    those preexisting code provisions.

5                   It's our position that these preexisting --  
6    preexisting code provisions, section 503(b), section 9  
7    -- 346 and section 1398 and 1399, all lead to the result  
8    that postpetition tax liabilities are not an  
9    administrative expense within the meaning of the code.

10                  JUSTICE GINSBURG:   How about employment tax?  
11    Employment taxes?

12                  MR. SHAH:   Your Honor, employment taxes  
13    arguably could be treated differently.  Now, as a matter  
14    of discretion IRS has chosen not to treat them  
15    differently.  That is, they don't try to seek those as  
16    administrative expenses.  I think there would be an  
17    argument and we set forth the argument in a footnote of  
18    our brief.  What the potential argument would be is that  
19    they could be deemed an administrative expense not  
20    because they are incurred by the estate, but under the  
21    other part of the definition of an administrative  
22    expense under 503(b)(1)(A).

23                  JUSTICE BREYER:   Just following up on  
24    that --

25                  MR. SHAH:   Yes.

1 JUSTICE BREYER: -- I'm looking for what I  
2 call past practice, where there must be a lot --

3 MR. SHAH: Yes.

4 JUSTICE BREYER: -- that would shed some  
5 light on this. So, I see -- your point that we cannot  
6 call these taxes administrative expenses is because when  
7 that's defined in 503 for the entire code.

8 MR. SHAH: Yes.

9 JUSTICE BREYER: It talks about  
10 administrative expenses incurred by the estate.

11 MR. SHAH: Yes, Your Honor.

12 JUSTICE BREYER: So you are saying here are  
13 three people who incurred their own taxes. One is  
14 Section 12, one is Section 13 and one is individuals in  
15 Section 11. Is that right?

16 MR. SHAH: Ah --

17 JUSTICE BREYER: At least that's my --

18 MR. SHAH: Yes. Yes, Your Honor.

19 JUSTICE BREYER: So we have three categories  
20 of people that -- where the taxes literally taken, they  
21 incur postpetition taxes. Now the bite would come up if  
22 it turned out when they were getting around to settle  
23 these things that there isn't enough money to pay fully  
24 the postpetition or let's -- no, to pay fully the  
25 domestic support obligations, wages, and also Federal

1 taxes.

2           Isn't that -- that's where it's going to  
3 show up, because the question will be, do you have to  
4 shave the Federal taxes because they are coming in to be  
5 paid as an administrative expense priority which is  
6 only -- there as number 2, I think, in light of number  
7 1. Or do you not shave them at all. If they were  
8 liable personally, there isn't any reduction in the  
9 amount of the Federal government, if they are allowed  
10 because it's one of the estate's expenses basically;  
11 using the estate very, very loosely then they would have  
12 to take a reduction, too. Am I right? Are you  
13 following it?

14           MR. SHAH: I think so. Let me try to say  
15 what I think what you're saying. Under Chapter 12 and  
16 13, if it is in fact a priority claim, whether it's a  
17 priority claim or an administrative expense, those have  
18 to be paid in full. There isn't an ability for the  
19 Court to shave those --

20           JUSTICE BREYER: No. The administrative  
21 expenses don't have to be paid in full if there isn't  
22 enough money for them to in unsecured claims for  
23 domestic support obligations, because the administrative  
24 expenses is the second priority, it isn't the first.

25           MR. SHAH: Okay. Well, Your Honor, there is

1 a misunderstanding I think in what you are saying. That  
2 is, in a Chapter 12 plan, the priorities matter more in  
3 terms of the relative priority between Category 1, 2, 3,  
4 4, 5, 6, 7 and 8. They matter more in a chapter 7  
5 liquidation where there is a finite set of assets being  
6 liquidated and those will be paid out in the priority  
7 that you are talking about. In a Chapter 12 or 13 case,  
8 there is going to be a plan proposed and that plan will  
9 be confirmed. Now under 1222(a)(2) any of those  
10 priority claims, whether it's first priority or eighth  
11 priority, has to be set out and to be paid in full in  
12 order for the plan to be confirmed.

13 JUSTICE BREYER: Okay.

14 MR. SHAH: So the plan won't be confirmed at  
15 all. There isn't a matter of ordering the priorities in  
16 a Chapter 12 or 13 case.

17 Now if I could turn back to Justice  
18 Sotomayor's question.

19 JUSTICE SOTOMAYOR: Could you turn back  
20 to -- before you answer my other question, could you  
21 finish your thought about what you are doing with wages?  
22 Are they given priority or aren't they? If you are  
23 saying they are not, if we accept your reading of this  
24 employee wage taxes are not administrative expenses.

25 MR. SHAH: Right. Well, Your Honor, they

1 are certainly not administrative expenses under the  
2 definition of incurred by the estate. That would be the  
3 relevant issue in this case. They may come under the  
4 other definition of administrative expense, that is the  
5 costs -- necessary costs of preserving the estate, like  
6 wages. If you consider the employment payroll tax that  
7 is paid simultaneously as the wage, that's part and  
8 parcel of the wages, you could get at it that way. But  
9 again that doesn't have anything to do with the  
10 "incurred by the estate" language. The incurred by the  
11 estate language, as you properly point out, is  
12 relevant -- the most relevant provision as to whether a  
13 tax is incurred by the estate are Sections 346b and 1398  
14 and 1399.

15 JUSTICE KAGAN: How does that work,  
16 Mr. Shah, because this is the part of your argument that  
17 I have to say sort of tripped me up.

18 MR. SHAH: Okay.

19 JUSTICE KAGAN: Because you define "incurred  
20 by the estate" by reference to those provisions, but  
21 those provisions were enacted 2 years and 4 years after  
22 the phrase that you are trying to define.

23 MR. SHAH: Sure.

24 JUSTICE KAGAN: So it must have been a very  
25 pressured Congress.

1                   MR. SHAH: Well, Your Honor it was a  
2     pressured Congress, because in the legislative history  
3     that we site, they say -- and it's not true that all of  
4     the accurate -- separate tax entity, these rules weren't  
5     implemented until afterwards. There -- Section 346  
6     which dealt admittedly only with state and local taxes,  
7     they set up rules, the same separate taxable entity  
8     rules that Congress later enacted 2 years later to apply  
9     to state and local entities. And that's the provision  
10    346 that is reprinted in our appendix at page 2.

11                   What Congress said when they passed 346 is,  
12    "we fully expect" -- we fully expect, and as they had  
13    originally drafted them in the 1978 Act to also apply to  
14    Federal taxes, but it decided to pull them out of the  
15    act so as not to step on the shoes of the jurisdiction  
16    of the Ways and Means Committee. That's the explanation  
17    that Congress provided and then 2 years --

18                   JUSTICE KAGAN: But you are saying that as  
19    of 1978 there was kind of an idea in people's heads  
20    about this separate tax entity or at least in some  
21    people's heads, but that idea had never been converted  
22    into any statutory language. And you are suggesting  
23    that we should take this phrase "incurred by the estate"  
24    and read it as if they were referring to something real  
25    that was in a statute.

1                   MR. SHAH: It's not simply taking out of  
2     their head, Your Honor, its Section 346 rules which are  
3     parallel and apply to state and local taxes, those  
4     didn't come out of nowhere. Those came out of prior IRS  
5     rulings as to when there is a separate taxable entity in  
6     a bankruptcy case.

7                   There were preexisting -- before the 1978  
8     act, in particular, there was a 1972 IRS revenue ruling  
9     which set forth the rules about when there is a separate  
10    taxable entity, whether the act should -- whether the  
11    tax should be taxed to the estate or to the debtor.  
12    Section 346 in the 1978 act codified those rules for  
13    State and local income taxes.

14                                 In the intervening 2 years  
15    between 1978 and 1980 when Congress consummated the step  
16    and extended those to Federal taxes, the IRS was still  
17    applying its preexisting practice based on its revenue  
18    ruling, so there wasn't a gap where there was no  
19    guidance as to whether -- how to determine whether these  
20    were incurred by the estate or not.

21                                 Courts may -- courts readily  
22    would have looked, I presume, to the 1972 Treasury  
23    ruling and the parallel 346 rulings in that gap time  
24    until the legislative guidance came along, and then  
25    codified that result with respect to federal taxes.

1 Now, I think to --

2 JUSTICE KAGAN: Can I ask another  
3 question --

4 MR. SHAH: Sure.

5 JUSTICE KAGAN: -- while we are on this,  
6 because the 1398, 1399 would suggest that we are looking  
7 to this separate taxable entity. But if I understand  
8 correctly, in the corporate context the IRS actually  
9 does not look to that. It looks to just the question of  
10 whose filing the tax return.

11 So if that's the case, aren't you, in that  
12 very large bankruptcy context, losing your textual  
13 anchor entirely?

14 MR. SHAH: No, Your Honor. There are two  
15 ways that a bankruptcy estate can incur a tax. One is  
16 if it's a separate taxable entity, then it -- then it's  
17 responsible for the taxes, all the taxes are taxed to  
18 the estate and it has to file the return and pay it.

19 The other way is if it has the duty to file  
20 the return. That's a different provision of the  
21 Internal Revenue Code, section 6012(b)(3). 6012(b)(3)  
22 also appears in the government's -- in the appendix to  
23 the government's brief. What 6012(b)(3) on page 14a  
24 says is that in a bankruptcy case the trustee of a  
25 corporate bankruptcy estate shall make the return for



1 income in a corporation.

2 What this Court held in Holywell, which both  
3 sides cite and both sides agree, is that when a  
4 corporate trustee has a duty to file a return under  
5 6012(b)(3), it also has a duty to pay the tax. That is,  
6 it incurs, it's liable for or incurs the tax.

7 So there are two ways to incur the tax: One  
8 is separate taxable entity; the other way is if the code  
9 imposes an obligation on the bankruptcy estate to -- to  
10 file and pay the tax return. That's the other way to  
11 interpret it, and that's why all the Chapter 7 and 11  
12 corporate cases that are cited by Petitioners are inapt.  
13 In those cases the postpetition tax liabilities are, in  
14 fact, incurred by the estate.

15 What is remarkable is that Petitioners do  
16 not cite a single Chapter 12 case in which a  
17 postpetition tax liability has been treated as an  
18 administrative expense. Chapter 12 has been around  
19 since 1986, and yet there is not -- if this was such a  
20 big problem that Congress was trying to get at it  
21 through this way, you would have expected at least a  
22 single case in which a postpetition tax liability had  
23 been treated as an administrative expense.

24 JUSTICE BREYER: How would it show up? I  
25 mean, what -- what -- what difference -- suppose --

1     suppose -- in 11 individual, 12, or 13, what's the  
2     difference whether you treated it as an administrative  
3     expense or not, as long as they all have to be paid  
4     anyway, you say?

5                 MR. SHAH:   Sure.   So the difference is in  
6     Chapter 12 and 13 they are treated outside of the  
7     bankruptcy plan itself, but they do need to be paid up  
8     front.   And in fact, they receive a special --

9                 JUSTICE BREYER:   No.   How would we know?  
10    How would we know --

11                MR. SHAH:   Oh, That they're treated  
12    differently?

13                JUSTICE BREYER:   Yes.   .

14                MR. SHAH:   Through the code.   In Chapters 12  
15    and 13, 1226(b)(1) and 1326(b)(1), the parallel  
16    provision in Chapter 13, they pull out administrative  
17    expenses.   They pull them out --

18                JUSTICE BREYER:   Let's imagine you are  
19    absolutely right.   They mean to treat them differently?

20                MR. SHAH:   Yes.

21                JUSTICE BREYER:   They mean to treat the  
22    postpetition tax obligation to the Federal Government  
23    not as an administrative expense.   But this is an  
24    instance where the business will continue, and  
25    therefore, you have said in order to continue you have

1 to pay all your tax liability and all your  
2 administrative expenses.

3 MR. SHAH: Yes.

4 JUSTICE BREYER: Therefore, what difference  
5 does it make whether you do or whether you don't treat  
6 them as administrative expenses? What is the  
7 operational difference?

8 MR. SHAH: Sure. Your Honor, it would be to  
9 the government's advantage if these were in the ordinary  
10 course -- at least before section 1222(a)(2)(A) was  
11 enacted that stripped priority, it would have been in  
12 the government's advantage to take the position that  
13 these were administrative expenses. And the reason why  
14 it's favorable to the government is, those have to be  
15 paid up front as part of the bankruptcy.

16 If you don't treat them as administrative  
17 expenses -- and the government took the self-denying  
18 position here in the years leading up to 2005,  
19 consistently taking the position these were not  
20 administrative expenses, even though it was to the  
21 government's disadvantage, because the code required  
22 that interpretation. And the disadvantage is you don't  
23 get -- the government didn't get them paid up front as  
24 administrative expenses. They would have to collect  
25 them outside of the bankruptcy. And when you go to

1 collect them outside of the bankruptcy, there is much  
2 more uncertainty. There may not be any --

3 CHIEF JUSTICE ROBERTS: Well, it's certainly  
4 not a self-denying position now, right? You are arguing  
5 that these are -- that the taxes of this sort are  
6 administrative expenses when that puts you at the head  
7 of the line. You are arguing that they are not  
8 administrative expenses, same type of taxes, when it  
9 puts you at the back of the line, even though the  
10 provision that puts you at the back of the line was  
11 designed to particularly help the fishermen and -- and  
12 farmers.

13 MR. SHAH: Your Honor, that -- that's just  
14 not true. Dating back to 1998 -- and these are cited in  
15 the government's brief at pages 16a to 18a -- dating  
16 back to 1998, the government had consistently taken the  
17 position that postpetition tax liabilities --

18 CHIEF JUSTICE ROBERTS: No, I'm talking  
19 about the position you are taking now. You argue for --

20 MR. SHAH: We have maintained our --

21 CHIEF JUSTICE ROBERTS: -- different  
22 treatment of these taxes as to whether or not they are  
23 administrative expenses -- not solely, but it leads to  
24 the result that you get the money first either way.

25 MR. SHAH: Because Congress -- the

1 government has stayed consistent in its position.  
2 Because Congress has changed the rules, it turns out  
3 that that same interpretation --

4 CHIEF JUSTICE ROBERTS: Well, but then  
5 you're saying that Congress changed the rules in a way  
6 that, as Justice Alito's question suggested, really  
7 doesn't do much at all, when what they wanted to do was  
8 provide some real protection for farmers and fishermen.

9 MR. SHAH: I can't speak to what Congress  
10 wanted to do. If in fact they wanted to do that, then  
11 they did it the wrong way. They could have --

12 JUSTICE GINSBURG: What would be -- what  
13 would be the right way?

14 MR. SHAH: You could easily enact a separate  
15 provision within 1222 that said -- something like -- use  
16 the language something like section 1305, that said "Any  
17 taxes that become payable after of the filing of the  
18 petition shall be treated as non-dischargeable,  
19 nonpriority debts and paid that way." But they didn't  
20 do that.

21 And I think section 1305 is critical here,  
22 and this goes to your question, Mr. Chief Justice, as  
23 well, that the government is trying to take advantage  
24 here. The -- adopting Petitioner's position would have  
25 a significant ripple effect in Chapter 13. This is not

1 simply a matter of trying to get to the result that  
2 Senator Grassley intended by narrowly interpreting  
3 1222(a)(2)(A) and it won't have any other affects in the  
4 code. It will have a significant effect in the intended  
5 operation of Chapter 13.

6 And -- and the reason why that's important  
7 is, is to put this in perspective, there are about 600  
8 to 700 total Chapter 12 filings each year. There is  
9 somewhere in the upwards of 400,000 Chapter 13 filings  
10 each year, and here's where it would throw a wrench into  
11 Chapter 13. If you look at section 1305 of Chapter 13,  
12 and that's reproduced on page 11a of the government's  
13 appendix.

14 What 1305(a)(1) does is it provides a  
15 special procedure for the government to file a claim for  
16 postpetition taxes, exactly the type of tax at issue in  
17 this case. It says: Government, you can go file a  
18 claim to have that included within the bankruptcy plan.  
19 If -- if you adopt Petitioner's position, there would  
20 never be a case in which the government would ever have  
21 any occasion to invoke 1305(a)(1), because they --

22 JUSTICE KAGAN: Why would that be a problem?  
23 You said that there would be a significant ripple effect  
24 and practical difficulties. And I understand your  
25 argument about 13 shows that you have to do this and why

1 would 13 be necessary if Petitioner were right, but you  
2 started out, I thought --

3 MR. SHAH: It -- yes.

4 JUSTICE KAGAN: -- by trying to show us that  
5 it would be a significant practical problem.

6 MR. SHAH: I said it would be a significant  
7 disruption to the intended operation of Chapter 13. In  
8 practice, it would actually mean that the government  
9 comes out better under Chapter 13 than in the  
10 government's current position, because what Petitioner's  
11 position would do, if you read --

12 JUSTICE KAGAN: So it just does  
13 automatically for the government what is now done by --  
14 by some kind of government filing?

15 MR. SHAH: Well -- well, not even that, Your  
16 Honor, because under 13 -- the reason why 1305(a)(1)  
17 would be dead letter -- you could just rip that page out  
18 of the code and throw it away if you accept Petitioner's  
19 reading. The reason why that's true is because under  
20 their reading it would get administrative expense  
21 priority, which are paid up front, super-priority, even  
22 before anything else; but under 1305 (a)(1) it doesn't  
23 get administrative expense priority, it may not even get  
24 any priority at all.

25 And so it's a significant change in the

1 operation of how the government would be seeking  
2 postpetition tax liabilities. Now, it would work to the  
3 detriment of the debtor in Chapter 13 cases, the upwards  
4 of 400,000 Chapter 13 cases that would occur --

5 CHIEF JUSTICE ROBERTS: But those are --  
6 those are small potatoes compared to the sale of a farm  
7 and a boat, right?

8 MR. SHAH: I would -- I would --

9 CHIEF JUSTICE ROBERTS: This particular  
10 issue of large capital gains from sale of significant  
11 assets doesn't typically arise in the Chapter 13 cases.

12 MR. SHAH: Sure, the capital gains tax  
13 wouldn't, but there's all sorts of postpetition income  
14 taxes that would arise in a Chapter 13 case. In a  
15 Chapter 13 case, those are wages that are being incurred  
16 after the filing of the petition. All of the taxes on  
17 those wages after the petition would be the -- the type  
18 of -- would be eligible for postpetition tax treatment.

19 CHIEF JUSTICE ROBERTS: Well, in Chapter --  
20 Chapter 13 cases are the ones that you -- that are  
21 typically resolved very quickly, right?

22 MR. SHAH: Your Honor, it is true that --  
23 from the statistics that I have seen on average, we are  
24 talking about 4 months in a Chapter 13 case. On average  
25 in -- in a Chapter 12 case, according to the professors'



1     amicus brief, median time is about 8 months.

2                     What's clear from the legislative history,  
3     the reason why Congress set up the Chapter 13 rules as  
4     to make the tax incurred by the debtor rather than by  
5     the estate is because Congress expressly said in the  
6     legislative history, which is cited in our brief, that  
7     they expected the confirmation time to be relatively  
8     quickly in a Chapter 13 case.

9                     We know that they made the same assumption  
10    in the Chapter 12 case because 1, they enacted the same  
11    separate taxable entity rules. And 2, they put in  
12    actual deadlines in the code for Chapter 13: 90 days to  
13    propose a plan, 45 days to confirm it. So roughly  
14    4 months is what Congress had extended. Now in  
15    practice, it's been the case that bankruptcy courts have  
16    extended that time beyond the statutory deadlines. So  
17    perhaps they are open a couple months longer than what  
18    Congress had expected. But that wasn't the intent that  
19    Congress had enacted this with, and if Congress wants to  
20    change that, it can go back and rewrite the rules to --  
21    to make that change.

22                    JUSTICE SOTOMAYOR: Counsel, before you  
23    finish, could you answer my question of what impact your  
24    broader reading -- your Chapter 12 affects only  
25    prepetition debts -- what else is that kind of holding

1 going to affect? Your narrow alternative holding  
2 affects just this issue. That broader reading -- I  
3 worry about a broader reading when I don't know its  
4 impact.

5 MR. SHAH: I -- I don't think it would have  
6 any adverse effects. And the reason is this: the  
7 administrative expenses, whether they are included in  
8 the plan or not --

9 JUSTICE SOTOMAYOR: Yes?

10 MR. SHAH: -- are still going to be paid up  
11 front. If you take Petitioner's reading that  
12 administrative expenses are really part of the plan  
13 under 1222(a)(2) rather than 1226(b)(1), you now have a  
14 conflict between 1226(b)(1), which is on page 10A, which  
15 expressly addresses and only addresses administrative  
16 expenses, and states that -- this is on page 10A -- it  
17 says "those will be paid before or at the time of each  
18 payment to creditors under the plan."

19 If you also said that they come under  
20 1222(a)(2), which is the only way that Petitioner's  
21 could win -- if they also came under 1222(a)(2),  
22 1222(a)(2) says that their -- they must be provided for  
23 full payment in deferred cash payment. So deferred  
24 interest-free payments over the life of a 3- to 5-year  
25 bankruptcy plan. That's very different than having them

1 get superpriority treatment under 1226(b)(1) and be paid  
2 in front -- upfront separate from the plan.

3 So that -- that is one significant piece of  
4 textual evidence that Congress thought that these should  
5 be paid outside of the plan.

6 The other piece of textual evidence is  
7 section 1227(a), which appears on page 10A as well, and  
8 what it says is that "the confirmed plan shall be  
9 binding on each creditor." That is the only potentially  
10 relevant category to the government.

11 But section 101 defines creditor -- and this  
12 is on page 1A of our appendix -- as entity that has a  
13 claim against a debtor that arose at the time of or  
14 before the order for relief concerning the debtor.

15 That is a holder of a prepetition claim.

16 If a confirmed Chapter 12 plan is only  
17 binding on the holder of a prepetition claim, it makes  
18 no sense to include postpetition claims within a  
19 Chapter 12 plan. I don't even know what it would mean  
20 to have a confirmed -- to have a plan included that and  
21 not have that plan binding on the government.

22 And so I think if you take those two pieces  
23 of textual evidence together, I think that strongly  
24 supports the interpretation of 1222(a)(2), that when it  
25 says a claim of the type specified in section 507, it

1 means "claim," and doesn't mean "claim and  
2 administrative expense."

3 Now admittedly, Congress has not been  
4 perfectly clear in using that term. It uses --  
5 sometimes it uses of the term "claim" to mean claim and  
6 administrative expense. Sometimes it means it to only  
7 mean claim. But we should give effect to the  
8 distinction between claim and administrative expense in  
9 light of 1226(b)(1), which specifically already  
10 addresses administrative expenses.

11 JUSTICE SOTOMAYOR: The problem with that  
12 argument is that the two are used interchangeably by  
13 everyone. Congress, the Court --

14 MR. SHAH: Yes, Your Honor.

15 JUSTICE SOTOMAYOR: The government in many  
16 situations, given the broad definition of "claims," the  
17 only logical conclusion is that it includes a subset, a  
18 liability created by administrative expenses.

19 MR. SHAH: Your Honor, and if you are only  
20 construing that language in isolation, if it only said  
21 claim in 507(a)(2) and 1226(b)(1) didn't exist, I would  
22 be in full agreement with you that you would read it to  
23 being claim and administrative expenses. Because we  
24 know that administrative expenses have to be paid in  
25 some way in a bankruptcy case.

1                   But 1226(b)(1) does exist in this code, and  
2     we need to give that provision effect.

3                   The last point I would make is Congress  
4     knows how to include administrative expenses within a  
5     bankruptcy plan when it wants to. If you look at the  
6     corresponding provision in Chapter 11 as opposed to the  
7     provisions in Chapter 12 and 13 -- this is section  
8     Section 1129(a)(9)(A) -- it expressly provides for the  
9     payment of administrative expenses within the context of  
10    the Chapter 11 plan. Chapter 12 and 13 take a different  
11    approach, and the Court should give effect to the choice  
12    that Congress made to treat administrative expenses  
13    outside of the bankruptcy plan.

14                  If there are no further questions?

15                  CHIEF JUSTICE ROBERTS: Thank you, Mr. Shah.

16                  Ms. Freeman, you have two minutes remaining.

17                  REBUTTAL ARGUMENT OF SUSAN M. FREEMAN

18                  ON BEHALF OF THE PETITIONERS

19                  MS. FREEMAN: Your Honor, one of the first  
20    things that Mr. Shah said was that the debtor should  
21    have set aside \$29,000 from the sale proceeds to pay the  
22    taxes. That's \$29,000 in sale proceeds of property of  
23    the estate. And yes, those are ordinarily set aside to  
24    pay the taxes. That's how bankruptcy cases work.

25                  Because you have 1222(a)(2)(A), that \$29,000

1 didn't need to be used to pay the taxes, and instead was  
2 set aside to be treated under the plan of  
3 reorganization, where that tax claim could be demoted in  
4 priority to a prepetition claim and discharged.

5 But the ordinary course is that the sale  
6 proceeds are used to pay the taxes, the administrative  
7 expenses. That's how bankruptcy works. And the  
8 government's argument here completely undercuts that.

9 With respect to section 1305, the language  
10 is different because it uses the word "payable." It  
11 includes all postpetition, postconfirmation, all the way  
12 through to the end of the bankruptcy case. Not just the  
13 short period of administration.

14 In Chapter 13 cases, you still have to pay  
15 administrative expenses. It's just that it's pretty  
16 rare that you have a tax that is incurred during that  
17 short period of administration. And so you have a  
18 separate statute that covers the whole period through  
19 the entirety of the plan of reorganization.

20 The Court -- Mr. Shah was asked about cases  
21 where -- and in fact an administrative expense claim was  
22 incurred for a capital gains tax in the Chapter 12 case.  
23 We would cite the Court to the Specht case. A copy of  
24 that is attached to the professors' amicus brief. And  
25 that shows where a plan was defeated because of the

1 large capital gains tax from the sale of the family  
2 farm. And that in fact is cited in some of the -- some  
3 of the legislative -- not the legislative history, but  
4 some of the commentary about one of the reasons why  
5 Senator Grassley supported section 1222(a)(2)(A) and  
6 drafted it in the first place.

7 This prevents a plan from being confirmed in  
8 so many Chapter 12 cases, family farmers are not able to  
9 go through with their plans. And that's why you have  
10 the demotion in priority.

11 It does have very little practical value if  
12 in fact it only applies to prepetition sales -- and not  
13 just prepetition but more than a year prepetition in  
14 most instances. The professors' amicus brief just  
15 refers to prepetition, and this little chart doesn't say  
16 that those are not within the scope of 507(a)(8) -- and  
17 those eighth priority -- I'm sorry, Your Honor.

18 CHIEF JUSTICE ROBERTS: Thank you, counsel.

19 The case is submitted.

20 MS. FREEMAN: Thank you.

21 (Whereupon, at 11:03 a.m., the case in the  
22 above-entitled matter was submitted.)

23

24

25

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