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In this article, the author considers the peculiarly preferred position of the tax lien under section 67 of the Bankruptcy Act. From his consideration of the position of the trustee and the claim of the government he concludes that the law as presently applied is inequitable. He advocates that the government's secret lien be held invalid against the trustee, that the inchoate lien doctrine should not be applied in bankruptcy, and that the doctrine of Moore v. Bay be modified.

I. Introduction

Congress and the courts have by their action in recent years singled out the federal tax lien for special treatment in bankruptcy proceedings. Tax liens cannot be treated in a general discussion of liens in bankruptcy because the assumption that they are treated in the same manner as other legal liens will lead to misunderstanding. This article is not concerned with federal claims for taxes which are unaccompanied with an asserted lien. The matters arising in the numerous cases on priorities under section 64 of the Bankruptcy Act are not considered; the only area here pertinent is that category of liens which are placed into the priority race by virtue of the subordination provisions of subdivisions (b) and (c) of section 67.[1] The subject matter discussed also excludes questions of federal priority outside of bankruptcy proceedings whether liened or unliened, except insofar as analogies are helpful or enlightening in understanding the development of the bankruptcy arguments.

Congress has long provided protection for federal revenues by giving the taxing authorities a lien upon the property of the delinquent taxpayer.[2] The present provision is found in Internal Revenue Code of 1954 as section 6321, which creates a lien for unpaid taxes in favor of the United States from the date of the assessment. The statute provides that the lien shall extend to all property and rights of property, whether real or personal, belonging to such person. Although section 6321 states that the lien arises upon refusal after demand, the next succeeding section states that the lien shall arise at the time of the assessment and will continue until satisfaction or until it becomes unenforceable by the lapse of time.[3] The above two sections which establish the lien and its time of existence make no mention of registration of any kind. This office is

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1. 11 U.S.C. §§ 107(b),(c) (1958).
2. Int. Rev. Code of 1939, ch. 2, § 3670, Rev. Stat. § 3186 (1875).
3. Int. Rev. Code of 1954, § 6322.

performed by section 6323 which says that the lien created shall not be good against mortgagees, pledgees, purchasers, or judgment creditors until notice has been filed by the tax authorities.[4] A further provision makes the lien invalid against mortgagees, pledgees, or purchasers of "securities" even though filed, absent actual notice.[5] Aside from the exceptions, the statute creates a floating lien upon all of the debtor's property. This floating lien is also a secret lien which cannot be discovered by third parties by any established procedure. Section 6323(d) does add the provision that "if a notice of lien has been filed" the tax authorities are authorized to provide rules allowing the disclosure of the amount of the outstanding obligation. This the Commissioner has done.[6] The pertinent provision provides that the district director may disclose the amount of the lien to "any person who has a right in the property or intends to obtain a right in the property by purchase or otherwise . . . ." It is assumed that the "or otherwise" would include creditors whether secured or unsecured.

The harm done by the secrecy of the unfiled tax lien could be held to a minimum by requiring the district director to file the notice of lien immediately upon receipt of the assessment lists. However, such a procedure would probably not be practical or desirable. Much of the room for adjustment before filing would be lost to the detriment of both the delinquent taxpayers and the Internal Revenue Service.

The regulations under section 6321 make one addition to the language of the Code; where the Code provides that the lien shall attach to the property and rights of property of the taxpayer, whether real or personal, the regulations add "tangible or intangible."[7]

II. VALIDITY AGAINST THE TRUSTEE

What is the effect of a petition in bankruptcy by or against the taxpayer after the date a tax lien arises under the above discussed sections? The first part of an answer to this question involves the determination of the validity of the lien against the trustee under the various provisions of the Bankruptcy Act. The so-called "strong arm" clause of section 70(c) states that "the trustee, as to all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt could have obtained a lien by legal or equitable proceedings at the date of bankruptcy, shall be deemed vested as of such date with all the rights,

4. INT. REV. CODE OF 1954, § 6323(a).
5. INT. REV. CODE OF 1954, § 6323(c).
6. Treas. Reg. § 301.6323-1(c) (1954).
7. Treas. Reg. § 301.6321-1 (1954). See United States v. Eiland, 223 F.2d 118 (4th Cir. 1955) (lien for taxes held to extend to debt owing from a third party to bankrupt). See United States v. Durham Lumber Co., 363 U.S. 522 (1960) where the court assumes that the surplus in hands of third party debtor of taxpayer-bankrupt after subcontractors are paid was subject to federal tax lien.

remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such creditor actually exists."[8] There can be no question that a tax lien which is filed before the date of the petition in bankruptcy is valid against the trustee under this provision.[9] Is an unfiled tax lien good against the trustee under the strong arm clause?

We have already seen above that the tax lien, even though unfiled, is good against all but mortgagees, pledgees, purchasers, and judgment creditors.[10] Therefore, if the trustee is to prevail, acting under the provisions of the Bankruptcy Act, he must fit himself into one of the excepted categories of the Internal Revenue Code. The language of section 70(c) does not state specifically that the trustee is a judgment creditor. The term "judgment creditor" was used from 1910[11] until 1950[12] and was found in the last clause of what is now section 70(c) in the following setting: "The trustee . . . shall be deemed vested as of the date of bankruptcy with all the rights, remedies, and powers of a judgment creditor then holding an execution duly returned unsatisfied, whether or not such creditor actually exists."[13] This clause was necessitated by the then existing distinction between property in possession and control of the bankruptcy court and other property. In 1950 the distinction in the relationship of the trustee to property in control and possession and property not so controlled and possessed was abolished. Absent that distinction, there was no longer any reason to give the trustee a slightly lesser status as to property not in possession and control of the court; consequently the language quoted was simply dropped. Furthermore, in light of the then existing cases it was proper to assume that the trustee's status as a legal lien holder at the date of bankruptcy was greater than and included the lesser status which he had occupied in relation to property not in possession and control of the court. To read this development as showing a positive intent to deprive the trustee of his status as a judgment creditor is to overlook the development of the subsection as a whole.[14]

Therefore, it is suggested that the trustee occupies the status of a judgment creditor and that an unfiled tax lien should not be good against the trustee. The cases are to the contrary. The most recent case, *In re Fidelity Tube Corp.*,[15] directly involved the question of the validity of an unfiled federal tax lien against the trustee in bankruptcy. The Third Circuit held that the trustee did not occupy the status of a judgment creditor. The referee making the initial determination in this litigation had found the

8. 11 U.S.C. § 110(c) (1958).
9. See Brust v. Sturr, 237 F.2d 135 (2d Cir. 1956).
10. INT. REV. CODE OF 1954, § 6323(a).
11. Act of June 25, 1910, ch. 412, 36 Stat. 838.
12. Act of March 18, 1950, ch. 70, § 2, 64 Stat. 26.
13. Act of June 22, 1938, ch. 575, § 70(c), 52 Stat. 881.
14. See the discussion in 4 COLLIER, BANKRUPTCY ¶ 70.02[4] (14th ed. 1959).
15. 278 F.2d 776 (3d Cir. 1960).

government's tax lien invalid against the trustee and District Judge Morrill had reversed.[16] The district judge relied on prior pronouncements of the various circuit courts and upon the Supreme Court decision in the case of *United States v. Gilbert Associates.*[17] In addition to the cases cited the district court's opinion referred to the Treasury Regulations[18] and to then pending legislation directed to clarifying the status of the trustee.[19] In the circuit court the trustee argued that to use the *Gilbert Associates* case as a precedent for holding that a bankruptcy trustee was not a judgment creditor within the meaning of the tax lien statute was to misunderstand the purpose of the Supreme Court when it held that the town of Walpole, New Hampshire, did not have a judgment. His contention was that the Supreme Court specifically and expressly intended to avoid the problem of a diversity of holdings in the different states because of the widely varying types of tax collection procedures; a bankruptcy trustee maintains his status under federal law and his status is not subject to different interpretation in different states. Chief Judge Biggs recites this argument in his opinion and refutes it by quoting the third sentence from a four-sentence paragraph written by Mr. Justice Minton. The sentence that Judge Biggs quoted is as follows: "In this instance, we think Congress used the words 'judgment creditor' in § 3672 [now 6323] in the usual, conventional sense of a judgment of a court of record since all states have such courts."[20] The Third Circuit opinion states that this language is decisive. However, if this language is put back into the paragraph it would seem very doubtful that it could be said to be decisive of the question of the status of the bankruptcy trustee. The entire paragraph from *Gilbert Associates* reads as follows:

> A cardinal principle of Congress in its tax scheme is uniformity, as far as may be. Therefore, a "judgment creditor" should have the same application in all the states. In this instance, we think Congress used the words "judgment creditor" in § 3672 in the usual, conventional sense of judgment of a court of record, since all states have such courts. We do not think Congress had in mind the action of taxing authorities who may be acting judicially as in New Hampshire and some other states, where the end result is something "in the nature of a judgment," while in other states the taxing authorities act quasi-judicially and are considered administrative bodies.[21]

It would seem clear that the Supreme Court did not have the problem of a bankruptcy trustee in mind in passing upon the propriety of the New

16. *In re* Fidelity Tube Corp., 167 F. Supp. 402 (D.N.J. 1958).
17. 345 U.S. 361 (1953).
18. § 301.6323-1(a)(2) (1954).
19. H.R. 5195, 85th Cong., 1st Sess. (1957).
20. 278 F.2d at 781.
21. 345 U.S. at 364.

Hampshire court's determination that the city was a judgment creditor.[22]

Under the argument that the government makes in these cases, it will not matter if an amendment is made to section 70(c) to make the trustee a judgment creditor again as before 1950. The government takes the position that the Supreme Court's language in *Gilbert Associates* precludes anyone as a judgment creditor except one who has *actually* obtained a judgment in a court of record in the usual and conventional way. Such an approach would preclude the trustee, even with express language re-added, from claiming that he has the status of a judgment creditor because his position is hypothetical and not the result of real litigation. If such an argument is accepted by the courts, Congress will be compelled to amend the Internal Revenue Code in order to add the trustee in bankruptcy to the list of persons unaffected by a tax lien that is not filed.

In the *Fidelity Tube* case Judge Kalodner writes an exhaustive dissenting opinion[23] in which he reviews a wide range of cases which have held that the trustee under the present language of section 70(c) enjoys the status of a judgment creditor. The dissenting opinion also traces the history of the section and demonstrates that the drafters of the present language of the strong arm clause did not expect or intend to weaken the position of the trustee by omitting the last clause which had specifically given the trustee the status of a judgment creditor with an execution returned unsatisfied. Judge Kalodner was joined in his dissent by Judge Hastie.

In the case of *United States v. Sands*[24] the Second Circuit quite clearly stated that the trustee was a judgment creditor so as to defeat an unfiled federal tax lien. The case was decided before the 1950 amendment to section 70(c), and the court relied upon the express language of the Bankruptcy Act. However, the government did prevail in that case because it had reduced the property allegedly subjected to the tax lien to possession. In the period following the deletion of the express reference to judgment creditor in the strong arm clause, only one district court case has held that the trustee is a judgment creditor.[25] On the other hand, since 1950 all the circuit courts of appeal which have passed upon the question of the trustee's status as a judgment creditor have taken the opposite view. Most of these cases rely directly upon the language of one sentence of the *Gilbert Associates* case as Chief Judge Biggs did in the *Fidelity Tube* case.[26]

22. Mr. Justice Frankfurter did state in his dissenting opinion: "Of course, the State courts cannot by the wand of a label waive away the requirement, which I agree is a matter of federal interpretation, that a creditor be a 'judgment creditor.' But federal law does not insist on anything more than that the creditor be in the same position as a creditor who holds a judgment 'in the usual, conventional sense.'" *Id.* at 367.

23. 278 F.2d at 782-92.

24. 174 F.2d 384 (2d Cir. 1949).

25. *In re* Sport Coal Co., 125 F. Supp. 517 (S.D.W. Va. 1954), *rev'd on other grounds sub. nom.* United States v. Eiland, 223 F.2d 118 (4th Cir. 1955).

26. Simonson v. Granquist, 287 F.2d 489 (9th Cir. 1961); Brust v. Sturr, 237 F.2d

In his opinion in the *Fidelity Tube* case, District Judge Morrill cited certain pending legislation directed toward excepting the trustee in bankruptcy from the operation of an unfiled tax lien.[27] He argued that this pending legislation showed that Congress was trying to exclude the trustee from the class of suitors affected by an unfiled lien; this, he felt, pointed up the fact that Congress did not consider a trustee as having the same rights at present as a judgment creditor. This may be so, but the reason for making an express exception for the trustee in bankruptcy may not be that Congress agreed that the trustee was not included in the term "judgment creditor"; it may be that Congress intended to encompass the trustee in the existing statutes but, being aware of the decisional interpretations to which Judge Morrill refers, decided that the intention was misinterpreted. The bill to which the judge referred was not passed by the Congress and as of this writing no other similar bill has become law.

In the past several sessions of Congress a bill called the "Federal Liens, Priorities, and Procedures Act" has been introduced.[28] The proposed bill does not expressly grant or deny a priority status to the trustee. In the proposed amendments to section 6323 of the Internal Revenue Code, subdivision (d) gives priority to a lien of judgment over an unfiled tax lien, but it refers to "a judgment in a judicial proceeding [which] has been rendered by any court . . . ." The definition of "lien" in subdivision p(4) of the amendment could include the trustee under the general statement that a lien is a lien under applicable law, whether at common law or in equity or by statute, and whether possessory or not. There are two exclusions, and neither would exclude the trustee if read literally. It is somewhat surprising that this over-all treatment of the subject of liens and enforcement thereof does not make specific reference to the trustee in bankruptcy.[29]

It is quite clear under the express terms of section 67(b) that the trustee cannot argue that a federal tax lien would constitute a preference within section 60 because the language states that "the provisions of section 60 of this Act to the contrary notwithstanding" these statutory liens will be valid even though they arise or are perfected during the four months immediately preceding bankruptcy.[30] For the purpose of this test it will not matter whether the lien is filed or unfiled. It might also be added that

135 (2d Cir. 1956); United States v. England, 226 F.2d 205 (9th Cir. 1955). See also In the Matter of Green, 124 F. Supp. 481 (N.D. Ala. 1954); *In re* Ann Arbor Brewing Co., 110 F. Supp. 111 (E.D. Mich. 1951).

27. *In re* Fidelity Tube Corp., 167 F. Supp. 402 (D.N.J. 1958), *aff'd*, 278 F.2d 776 (3d Cir. 1960).

28. H.R. 4319, H.R. 4320, 87th Cong., 1st Sess. (1961); S. 1193, 87th Cong., 1st Sess. (1961).

29. Other parts of the same bill expressly exclude either the trustee in bankruptcy or bankruptcy proceedings in general.

30. 11 U.S.C. § 107(b) (1958).

the federal tax lien will not be affected by the provisions of section 67(a) because it is a statutory lien and not a legal lien within the meaning of subdivision (a).[31]

For the purpose of determining the validity of a statutory tax lien under subdivision (b) of section 67 it is necessary to distinguish between the lien upon real and the lien upon personal property. Although subdivision (b) is a validating section, in that it makes certain liens good against the trustee that would not otherwise be valid, this same subdivision is followed by (c) which is an invalidating section and runs back over some of the same liens that are validated by the preceding section and knocks them out as to the trustee. Those liens within the scope of subdivision (c) which are not knocked out entirely are subordinated to the first two priorities of section 64,[32] unless accompanied by possession.[33] As subdivision (c) applies by its terms only to statutory liens upon personal property, the net result is that subdivision (b) validates tax liens against real estate and they are therefore to be treated as any other valid security whether contract, statutory, or legal.[34] This validation of tax liens against real property brings up two distinct and important problems.

The first result of validating a federal tax lien under section 67(b) is to raise the question of the validated federal tax lien's relationship to other valid liens. Suppose, for example, that in addition to a federal tax lien on Blackacre there is also an attachment lien which was levied upon the same land five months before the petition in the bankruptcy proceeding. Does it matter when the federal tax lien arose? So far the cases have applied the rule of first in time, first in right, and the two liens have been paid according to their respective dates, the earliest one being paid and then the later one.[35] This would be the result in most cases today, but the

31. See 4 COLLIER, BANKRUPTCY ¶ 67.20[2] (14th ed. 1954).

32. In United States v. Eiland, *supra* note 7, the court held that the lien for taxes under INT. REV. CODE OF 1954, § 6321 extended to intangibles; in that case a lien on a debt owing to the taxpayer-bankrupt was upheld, but this lien was not subordinated to administration and wage claims given priority under § 64 because the provisions of § 67(c) only apply to tangible personal property. It might be questionable whether "personal" as used in the Internal Revenue Code includes intangible property and "personal" in the Bankruptcy Act excludes intangibles. There does seem to be some concept of possession of intangibles under our law.

33. When the government does reduce personal property to possession prior to the time of the petition in bankruptcy it is not subject to the provisions of § 2(a)21 requiring delivery of possession or accounting to the trustee, as an agent to liquidate the debtor's property. *In re* Eden Equip. Corp., 177 F. Supp. 619 (S.D.N.Y. 1959). The possession required under § 67(c) is actual possession. *In re* George Shirt Co., 162 F. Supp. 749, 751 (D. Md. 1958) (the test was said to be, did director "'do all he could' to secure and retain possession"). See 4 REMINGTON, BANKRUPTCY § 1637.2 (6th ed. 1957).

34. See County of Clark v. United States, 284 F.2d 885 (9th Cir. 1960).

35. Adams v. O'Malley, 182 F.2d 925 (8th Cir. 1950); *In re* Freeze-in Mfg. Corp., 128 F. Supp. 259 (E.D. Mich. 1955); *In re* Ann Arbor Brewing Co., 110 F. Supp. 111 (E.D. Mich. 1951); see United States v. City of New Britain, 347 U.S. 81 (1954).

tax authorities take the position that because the Supreme Court of the United States has decided in non-bankruptcy cases that the attachment lien is inchoate and subject to a federal tax lien obtained anytime before judgment in the suit in which the attachment is pending, this same reasoning should be applied in the bankruptcy cases. The courts have resisted this argument on the basis that the non-bankruptcy cases involve a different problem; that is, in bankruptcy Congress has provided for a system of priorities and distribution and if it had intended such a doctrine to apply, it could easily have said so.[36] The principal difficulty with this argument is that the Bankruptcy Act does not make any rules or provisions as to valid security; in fact, the act does not state expressly that valid secured claims are to be paid out of the estate before priority creditors.[37] This argument applies to a valid federal tax lien upon real property. What is the result if we concern ourselves with a valid but subordinated lien against personal property?

Subdivision (c) of section 67 postpones statutory liens where not enforced by sale, expressly including tax liens not accompanied by possession, which are valid under the preceding subdivision to the first two priorities of section 64. Suppose a case in which an assessment is made against a taxpayer who owns an automobile. The Internal Revenue Code states that this assessment after notice shall be a lien upon the automobile. Thereafter, a creditor levies an attachment upon the taxpayer's automobile and five months later the debtor-taxpayer files a voluntary petition in bankruptcy. The tax lien is valid against the trustee but subordinated by 67(c) to claims for administration expenses and wages which are given priority under section 64. The attachment lien is good against the trustee but inferior to the tax lien because of later date (or inferior because of the inchoate lien doctrine, if that should eventually be applied to bankruptcy cases involving secured claims). There are several solutions to this circular priority problem and none is entirely satisfactory.[38] In the case of personal

36. The Federal Liens, Priorities, and Procedures Act would amend REV. STAT. § 3466 (1875) to modify substantially the inchoate lien doctrine but in the proposed subdivision (a) the phrase "otherwise than in bankruptcy" is used and in subdivision (c), the definitions section, part (6) states, "This section is a law of the United States entitling the United States to priority within the meaning of the Bankruptcy Act, and in proceedings under that Act claims of the United States shall have the degree of priority therein specified." H.R. 4319, H.R. 4320, S. 1193, 87th Cong., 1st Sess. (1961).

37. The express language preserving valid security was left out by the Chandler Act but it is clear that valid liens perfected before bankruptcy are recognized before other creditors. See Goggin v. Division of Labor Law Enforcement, 336 U.S. 118 (1949); Oppenheimer v. Oldham, 178 F.2d 386 (5th Cir. 1949); 4 COLLIER, BANKRUPTCY ¶ 67.02 (14th ed. 1954).

38. See the discussion in *In re* Meisel, 159 F. Supp. 879 (D. Md. 1958) where the shortage of assets saved the district judge from some very knotty problems. See *In re* Ann Arbor Brewing Co., 110 F. Supp. 111 (E.D. Mich. 1951) where a local tax on a possessory interest took the proceeds of personal property ahead of administration and wage claims and federal non-possessory interests took third. See also the solution to

property subject to tax liens there is a much stronger argument against application of the inchoate lien doctrine because in these cases the Congress has in fact made detailed provisions in regard to the disposition and order of payment from the estate, and in this particular they have specifically dealt with liens against personal property. This problem could be solved by saying that the liens falling under subdivision (c) of section 67 are invalidated and given a class 2(a) priority under section 64. The present language of 67(c) does not so read and it is doubtful if such was the intention of the drafters.

Another question concerns the relationship between the liens which are subordinated under section 67(c). What order of payment is appropriate as between federal tax liens and other valid liens when both are subordinated to the expenses of administration and priority wage claims? Once again, the courts lean to the first in time, first in right doctrine, but here the Commissioner can well argue that the inchoate lien doctrine should apply.[39]

III. Preservation Clauses of the Bankruptcy Act

Another set of problems can arise under those provisions of the Bankruptcy Act which allow the court to direct that an invalid security transaction may be preserved for the benefit of the estate. For example, an assessment is made against a taxpayer on January 1 and followed shortly thereafter by proper demand. On February 1 the taxpayer-debtor borrows money and executes a chattel mortgage on his recent model automobile. On March 1 the chattel mortgage is filed for record in the appropriate county record office. The creditor knew, or should have known, that the taxpayer-debtor was insolvent. On April 1 the government files its tax lien in the proper county. If a petition in bankruptcy is filed by or against the taxpayer-debtor anytime before July 2 it will raise the question of preservation of an invalid lien. Assuming that all other elements requisite to preference are present, this mortgage is invalid against the trustee under the provisions of section 60 as a security interest perfected within four months of bankruptcy. The tax lien is a valid lien against the automobile even though filed within the four months preceding bankruptcy; however, the lien is subordinated to the first two priorities under section 67(c). The chattel mortgage is valid against the tax lien because it was obtained and perfected before the tax lien was filed, mortgagees being one of the expressly labeled groups which are not affected by an unfiled tax lien. Can the court order the mortgage lien preserved for the benefit of the estate under that part of section 60(b) which states: "Where a preference by

circular priority in the proposed amendments to Int. Rev. Code of 1954, § 6323 (m), note 26 *supra*.

39. *See In re* Ann Arbor Brewing Co., 110 F. Supp. 111 (E.D. Mich. 1951).

way of lien or security title is voidable, the court may on due notice order such lien or title to be preserved for the benefit of the estate, in which event such lien or title shall pass to the trustee"? If the court does order the lien preserved can the trustee then take the automobile free of any interest of the government regardless of the size of the preserved lien? Assume that the loan for which the mortgage was given was in the amount of $200, and that the vehicle mortgaged has a market value at the time of bankruptcy of $2,500. The government's tax claim is for $1,000. Should the court apply *Moore v. Bay*[40] by analogy and let the trustee put the entire $2,500 into the estate as general funds? Should the court order the trustee to put $200 into general funds, pay the expenses of administration and wages given priority by section 64, and then order the balance, if any, paid to the government? Should the court order the *first* $200 be paid to the government because the trustee is not a mortgagee in the usual and conventional sense of the term and then order the payment of administration and wage priorities, with the balance to the government?[41] No case has been found dealing with this situation. It is suggested that the second question should be answered in the affirmative and the other two in the negative; such a result, however, seems unlikely in light of recent case law. Similar problems could arise under the preservation clauses of sections 67(a)3 and 70(e)2 whenever the situation presented a lien invalid against the trustee and valid against the tax lien.

IV. LIENED CLAIMS FOR PENALTIES AND POST-BANKRUPTCY INTEREST

It is probably safe to say that at the present time the courts will not allow post-bankruptcy interest on liened tax claims. It was early decided by the United States Supreme Court that post-bankruptcy interest should not be allowed on tax claims which were not accompanied by a lien.[42] Should it make any difference if the tax claim is secured by a lien? The courts have decided that it makes no difference and so far have not applied any exceptions.[43] It has been argued that there are several exceptions to the general rule that post-bankruptcy interest is not allowed. It is sometimes said that if the estate turns out to be solvent, then post-bankruptcy inter-

40. 284 U.S. 4 (1931).

41. *Cf. In re* Kobiela, 152 F. Supp. 489 (D. Neb. 1957) where the district judge held the state department of labor to be a "mortgagee" within the meaning of INT. REV. CODE OF 1954, § 6323, when the department filed notice of tax claims under provisions of Nebraska statute.

42. City of New York v. Saper, 336 U.S. 328 (1949); Bruning v. United States, 192 F. Supp. 826 (S.D. Cal. 1961).

43. *In re* Kerber Packing Co., 276 F.2d 245 (7th Cir. 1960); United States v. Bass, 271 F.2d 129 (9th Cir. 1959); United States v. Mighell, 273 F.2d 682 (10th Cir. 1959); United States v. Harrington, 269 F.2d 719 (4th Cir. 1959).

est should be allowed, but no case involving this rather infrequent situation has been found. It is also argued that in the case of contract liens if the proceeds from the property subject to the lien exceed the principal of the debt and the costs, then interest should be allowed to the date of the payment. In *United States v. Harrington*[44] the court recited that argument and stated that if there were such a rule, or rather exception to the general rule, it was confined to cases of contract liens where the creditor had extended funds in reliance upon specific assets. Such a rule would not be appropriate for the general lien of the federal government in tax claim situations. A third suggested argument was that where the security itself was income-producing, interest ought to be paid to the security holder; apparently this argument was not applicable in the *Harrington* case, but it would appear that even if it were applicable, the distinction between contract and legal liens would again be drawn. A collateral problem is whether discharge has the effect of barring collection of post-bankruptcy interest out of after-acquired assets of the discharged bankrupt. It would seem that if the post-bankruptcy interest is not provable, it is not dischargeable, but the cases tend to state that the post-bankruptcy interest is not allowable. If the claim is not provable, it should not be affected by a discharge. If there is a provable claim which is not allowable, then it should be barred by the discharge. Section 17(1) excepts from discharge obligations which are due as a tax. It can be argued that the interest on taxes is not a liability for taxes included within the exception.[45]

A parallel problem that has given the courts considerable difficulty is the question of the allowance of liened tax penalties. The question here is whether section 57(j) of the Bankruptcy Act, which states that debts owing to the United States as a penalty or forfeiture shall not be allowed except to the amount of actual loss, has application to such a claim when it is accompanied by a lien; the other position is that secured claims are not affected by bankruptcy proceedings. The question is really two questions: the first is whether the secured penalty should be allowed to share in the estate, and the second is whether the discharge bars collection of the liened penalty after bankruptcy. Typical of the cases disallowing liened tax penalties is *United States v. Harrington*[46] where the court took the position that it could look behind the lien to see what was secured, and in so doing they saw a penalty which was found to come within the terms of section 57(j). It should follow that if the penalties are not allowable or provable, they are not dischargeable, and it was so held in *In re Steckler*,[47] the court stating:

44. *Ibid.*

45. See United States v. Mighell, *supra* note 43.

46. Note 43 *supra*. See also United States v. Phillips, 267 F.2d 374 (5th Cir. 1959).

47. 195 F. Supp. 879 (S.D. Ind. 1961).

> The court therefore concludes that the penalties involved in this case were not allowable, even though secured by a lien, except to the extent provided in Section 57, sub. j, i.e., for pecuniary loss sustained by the transaction, with reasonable and actual costs occasioned thereby. Provability was likewise limited to that extent, and the obligation to pay the penalties was not affected by the discharge in bankruptcy.[48]

The cases on the other side of the question find the secured penalty allowable in full and thus dischargeable in full.[49] In *United States v. Mighell* the court reasoned that the lien which secures the penalty is validated by the provisions of section 67(b), and section 57(j) does not apply to the situation where the penalty is secured by the lien. The liened penalty is allowable in full and any part of it that is not paid out of the estate is discharged as a penalty and is not taxes within the meaning of section 17. It would seem apparent that, as stated in *Mighell*, "the conflict between the two lines of decision can only be resolved by the Supreme Court."[50]

V. Conclusions

The secret floating lien which the government obtains between the date of the assessment and the time of filing under appropriate state statutes should not be good against the trustee in bankruptcy. Courts in and out of bankruptcy have been diligent to avoid the secret lien whenever possible. However, this tax lien remains today as a potent and effective remedy unassailed by the courts. The justification for this situation may be in the need to protect the federal revenue; however, in this regard it should be considered that the total amounts involved in such situations are limited, and also that the result in the bankruptcy situation is actually that the creditors of the bankrupt are paying the tax claim. The present situation can be avoided in several ways. It would be possible to give the government a lien only from the date of filing notice of the lien. It would be possible to amend the Internal Revenue Code to include the trustee in the list of persons not subject to an unfiled tax lien. It might also be a solution to make the trustee an express judgment creditor under 70(c) of the Bankruptcy Act. The preferable solution would be to limit tax claims in bankruptcy to a specified period preceding bankruptcy whether liened or unliened, then provide that an unfiled tax lien is only good against the taxpayer and persons with actual notice thereof. With the tax claims thus limited, it would be advisable to take tax liens out of the subordination provisions of section 67(c).

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48. *Id.* at 887.

49. United States v. Mighell, *supra* note 43. And see Grimland v. United States, 206 F.2d 599 (10th Cir. 1953); Kentucky *ex rel.* Unemployment Compensation Comm'n v. Farmers Bank & Trust Co., 139 F.2d 266 (6th Cir. 1943).

50. 273 F.2d at 684.

The inchoate lien doctrine should not be applied in bankruptcy. The courts should continue to apply the rule of first in time, first in right to the cases where tax and other liens are competing in the same class in bankruptcy proceedings. The application of the inchoate lien doctrine has at best a dubious basis outside of the bankruptcy court and little, if any, basis within the court.[51]

Finally, in those cases where the trustee is put into the position of holder of a preserved lien, the doctrine of *Moore v. Bay* should not apply so as to enable the trustee to obtain any more than the amount the voidable lienholder could have received under state law absent the intervention of bankruptcy.

51. See the excellent analysis and discussion in Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905 (1954); Note, 108 U. PA. L. REV. 77 (1959).