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Bankruptcy

In April 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act (S. 256) was enacted, bringing significant changes to the treatment of state and local tax obligations in bankruptcy. In this article, the authors review the tax-related changes made under S. 256 and assess the potential impact of those changes on taxing authorities, debtors, and other creditors.

U.S. Bankruptcy Code's New State and Local Tax Provisions: Challenges and Opportunities for Debtors, Taxing Authorities

BY JIM SHEPARD AND KAREN CORDRY

INTRODUCTION

The genesis of the U.S. Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005 was the introduction in 1992 of bills to create a National Bankruptcy Review Commission (NBRC), charged with considering how well the U.S. Bankruptcy Code of 1978 was functioning after its first 15 years. That legislation was eventually enacted in 1994.

In considering the work to be done by the NBRC, taxing authorities had two main goals. First, they hoped that, as with the substantive provisions of the 1994 law, the review process might result in legislation that would clarify ambiguous provisions, with the added hope, of course, that the clarification would favor the government's position. Second, they wanted revisions that would reinforce the debtors' basic obligations with respect to taxes—*e.g.*, to file prepetition returns by the time they filed their petitions, to continue to file returns while they were in bankruptcy, and to pay their taxes while in bankruptcy without prompting by the government.

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The NBRC worked reasonably well in both regards with respect to tax issues. An advisory task force was appointed that included a number of representatives of state and federal taxing authorities, among others. The task force engaged in reasoned discussion of a variety of proposals and considered several iterations of its report; eventually its recommendations were adopted by the NBRC. And unlike the more controversial portions of the NBRC report, the tax recommendations were actually useful in framing the opening debate and discussions with the drafters in Congress, serving as the basis from which the first draft of the tax provisions was written.

In their discussions with Congress between 1998 and 2000, when the tax proposals were finalized, the taxing authorities argued that the proposals they were presenting were basically ''good government'' provisions. That is, they were not, in the main, efforts to significantly improve the position of taxes under the code, but rather were attempts to ensure that the taxes that the code assumed would be reported and paid were actually reported and paid.

One area, though, where substantive changes were sought was in the treatment of taxes typically owed to

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cities and counties; *i.e.* , revenues from secured and ad valorem property taxes. The concern was that the bankruptcy of a major employer would have a significantly greater effect on the budgets of a city or county than on an entire state, or on the nation as a whole. If a large local employer stopped paying taxes, or worse, demanded refunds for taxes that had been assessed years before, the results could be devastating for the municipality. Thus, several provisions of the 2005 act focused on protecting local property taxes in bankruptcy.

The discussion that follows addresses the various BAPCPA tax provisions grouped according to the several goals discussed above and envisions how these changes could play out for taxing authorities, debtors, and other creditors in future cases.

TAX-RELATED CHANGES

Making the System Work

A major aim of the 2005 legislation was to improve procedures in bankruptcy. In this section, we review those ''good governance'' provisions of the bill.

Sections 703 and 715

Section 703 of BAPCPA amends 11 U.S.C. §505(b) to clarify how a trustee is to request an expedited audit of an estate's liability for any tax. Under prior law, the trustee's return governed if the taxing authority did not challenge it within 60 days. The short deadline put a premium on ensuring that such requests went to the right address. The I.R.S. had directed that the requests be filed with the local district director, but some courts did not enforce that directive, and there was no mechanism for state or local tax authorities to designate an address where the request was to be sent.

Section 505(b) now provides:

- that a notice must be served in accordance with the procedures set by the tax authorities,
- that bankruptcy clerks maintain a list of addresses that the tax authorities designate as the proper location for filing such taxes, and
- that a default address be provided if none is listed by the tax authority.

The combination gives more certainty to debtors and tax authorities alike. Section 715 further amended §505(b) to provide that a determination of the tax liability under that expedited procedure protects the estate, as well as the trustee, the debtor, and any successor to the debtor.

Sections 712 and 716

Section 712 amends 28 U.S.C. §960 and imposes certain requirements to ensure that returns are prepared and filed and taxes paid as part of the trustee's or the debtor's routine operations and standard duties. Further, the amendment makes it clear that taxes incurred by a bankruptcy estate must actually be paid during the case, unless the trustee promptly and properly abandons property subject to a real estate tax or unless another code provision specifically excuses the payment of the taxes. In Chapter 7 cases, trustees are permitted to withhold payment of taxes until final distribution of estate funds after obtaining an order from the bankruptcy court finding that there will probably be an insufficiency of funds for such administrative expenses,[1] or that the taxes were incurred not by the Chapter 7 trustee but in another chapter prior to conversion to Chapter 7.

Section 712 also amends §503(b)(1) of the code to eliminate the need for the taxing authority to make a request for payment of administrative expense taxes and to make it clear that ad valorem property taxes that come due during the case are ''incurred'' by the estate as an administrative expense, whether they are in rem or in personam, or secured or unsecured. The amendment overrides bankruptcy court decisions and local rules that require tax authorities to file requests or motions in order to be paid these administrative expense taxes.[2]

Section 716 of the 2005 act deals with Chapter 13 cases. The code requires debtors to pay all priority taxes in full, but only if the taxing authority files a claim for those taxes. Before this amendment was enacted, if the debtor failed to file returns for prior years, taxing authorities had few practical means to judge the correct amount of their claims. Filing estimated claims for all years where the debtor had not filed a return would be a monumental task, given the volume of Chapter 13 filings. And even if the authorities tried to file such claims to preserve a right to receive payments under the plan, some courts sanctioned tax authorities for filing ''guesstimated'' claims where tax returns were not filed.[3]

Yet, in the absence of filed returns, taxing authorities had little other practical recourse. Where the taxing authority did go to the time and expense of seeking an order requiring the filing of returns, some courts did not necessarily find that they were required to issue such an order.[4]

The §716 amendments impose a number of added duties on Chapter 13 debtors to solve those problems. First, new code §1308 was enacted to require Chapter 13 debtors to file all returns that are due for the four taxable years ending before the petition was filed. The returns must normally be filed by the §341 meeting, but the meeting may be held open for a time to allow the returns to be filed. Section 502(b)(9) of the code was amended to provide that a governmental tax claim will be considered timely if filed within sixty days after a return is filed.[5] Section 1307 was amended to provide that

[1] This amendment incorporates the requirements of I.R.C. §6658(a)(1) under which penalties for failure to pay a tax can be avoided.

[2] *See, e.g., In re Glen Eden Hosp. Inc.*, 172 B.R. 538 (Bankr. E.D. Mich. 1994; *In re Quid Me Broadcasting Inc.*, 181 B.R. 715 (Bankr. W.D. N.Y. 1995).

[3] *See, e.g., In re McAllister*, 123 B.R. 393 (Bankr. D.Or. 1991); *In re Hamilton*, 104 B.R. 525 (Bankr. M.D. Ga. 1989).

[4] *See, e.g., Puerto Rico Dept. of Treas. v. Pagan*, 279 B.R. 43 (D. P.R. 2002).

[5] Some commentators think that, read literally, this section sets the 60-day period as an absolute time limit for tax claims that overrides the otherwise applicable 180-day minimum time period for filing government claims. While it is possible to read the section that way, another legitimate reading is that government claims are timely if filed within 180 days of the petition and are timely if filed within 60 days after a return is filed. Either provision or both can apply; *i.e.*, the government would have a minimum of 180 days, but, if the return was filed to-

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the failure to file such returns is cause for conversion of the case to Chapter 7 or dismissal; §1325 was amended by the addition of new subsection (a)(9), providing that all required returns must be filed to confirm a plan. Finally, §716 also includes a ''sense of Congress'' statement that the Rules Committee should propose rules providing that plan objections filed within 60 days after all required returns have been filed be timely and that no objection to tax claims be filed until the returns have been filed.

Section 442

Although tucked away in the small business chapter, this provision amends §1112 with respect to all Chapter 11 debtors and provides that a failure to timely pay postpetition taxes or to file postpetition tax returns constitutes ''cause'' for conversion or dismissal.

Section 718

Section 718 amends §362(b) of the U.S. Bankruptcy Code to permit taxing authorities to automatically set off a pre-petition income tax refund against pre-petition income tax liabilities. Prior law required stay relief for such setoffs, even though such motions were generally routine and uncontested. Debtors normally did not oppose such motions because nondischargeable interest and penalties continued to accrue until the setoff took place. Many courts had local rules that automatically allowed such setoffs, and the new section adopts that procedure.

Settling Questions (and Doing Better by Tax Authorities)

In addition to procedural changes, the 2005 bill also included provisions that settled areas of uncertainty for taxing authorities and in the process, gives states and localities greater advantage in securing their interests in bankruptcy.

Section 704

Section 704 of BAPCPA enacted new code §511, which provided for interest on tax claims to be paid at nonbankruptcy rates. This change met the taxing authorities' twin goals of obtaining certainty as to the rates to be paid and retaining the nonbankruptcy interest rates. Applying the statutory rates in bankruptcy is valuable both for fiscal reasons, so that debtors will not see bankruptcy as a way of receiving a low interest rate loan via their unpaid taxes, and for practical reasons, in that trying to force state computers to recognize and accept interest paid at nonstatutory rates was a difficult exercise at best.[6]

The need to avoid providing incentives for intentional noncompliance is particularly critical for taxes. Unlike trade debt, where one can usually avoid becoming a creditor at all, or can, at least, stop additional debt from piling up, taxing authorities have few protections. Most taxes are incurred as unsecured debt, and the government has little ability to avoid becoming a creditor or to limit its liability. Thus, interest rates on delinquent taxes are usually set at a relatively high level to discourage taxpayers from succumbing to the temptation to rely on tax avoidance as a source of financing. Bankruptcy filings that artificially reduced those rates could create a strong incentive for tax evasion tactics.

Section 705

Section 705 of the 2005 act addresses the tolling of time periods for discharging taxes where there has been a prior bankruptcy filing. The priority (and hence dischargeability) of most tax claims is determined by their accrual date in relationship to the date of the petition filing. Where the debtor filed successive petitions, barring collection efforts by taxing authorities during the pendency of each case, this provision potentially allowed the debtor to ''hide'' in bankruptcy while the time for priority/nondischargeability lapsed.

The case law was split as to whether the prior filing tolled those time periods with respect to later cases. Those issues were largely resolved during the long gestation of BAPCPA by the Supreme Court's decision in *Young v. United States*, 535 U.S. 43 (2002), which upheld the argument that time periods should be tolled while other bankruptcy cases are pending. This provision codifies the holding in that case.

In addition, §705 amended §507(a)(8)(A) of the U.S. Bankruptcy Code to clarify or correct several U.S. Courts of Appeal decisions that essentially provided for the bifurcation of the taxable year in which the petition was filed for purposes of deciding the priority status of taxes for the year.[7] Section 507(a)(8)(A)(ii) was also amended to extend the 240-day period for assessments while offers-in-compromise were pending and while a stay is in effect in a prior bankruptcy case and to provide generally that times for priority calculations are suspended for any time during which the tax authority is prohibited from pursuing a claim during a prior bankruptcy case, or while the debtor is performing under a confirmed plan in a prior case.

Section 707

Section 707 amends §1328(a)(2) of the code and does substantively improve the position of the taxing authorities by restricting the so-called ''superdischarge'' in Chapter 13, which discharged all taxes, even though the code required that a reorganization plan

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wards the end of that period, the government would still have a minimum of 60 days to file, even if that took the deadline past the 180-day mark. In light of the reason for including this provision, the latter reading seems to be far more logical.

[6] The use of nonbankruptcy interest rates is especially crucial to local governments where delinquent real estate taxes are routinely sold to a third party at public auction which fixes the interest rate to be paid with respect to each such sale.

[7] The amendment overruled *In re Pacific–Atlantic Trading Co.*, 64 F.3d 1292 (9th Cir. 1995), *In re L.J. O'Neill Shoe Co.*, 64 F.3d 1146 (8th Cir. 1995), and *In re Hillsborough Holdings Corp.*, 116 F.3d 1391 (11th Cir. 1997), which allocated income tax liability for a corporate debtor for the filing year between first and eighth priority. Those cases failed to clearly explain exactly how to calculate this allocation, since the tax liability would be based on transactions over the course of the year, both pre- and postpetition, that would normally produce a final net result for the entire year. The courts never explained how that final singular liability was to be allocated between pre- and postpetition liability, or how to avoid having it be manipulated by the debtor prepetition.

provide for payment in full of priority taxes.[8] The problem was that §507(a)(8)(A)(iii) gives priority to taxes that are still assessable on the petition date ''other than a tax of a kind specified in Section 523(a)(1)(B) or (C)'' of the code. Those two sections refer to taxes for which a return was not filed, was filed late, or where there was a fraudulent return or an attempt to evade or defeat the taxes. It was apparently thought that creditors should not be penalized for priority purposes by the debtor's prior failings, but outside of Chapter 13, those debts would still be nondischargeable and could be collected after the discharge. In Chapter 13, though, such nonpriority taxes would neither be paid in full nor excepted from discharge.

This led to the remarkable spectacle of Chapter 13 debtors affirmatively asserting that they had filed fraudulent tax returns in order to use these provisions to reduce or eliminate their obligation to pay these taxes. The amendments made by BAPCPA §707 eliminated this possibility by making these types of tax debts nondischargeable in Chapter 13 as well. In addition, debts for trust fund taxes, *i.e.*, those listed in §507(a)(8)(C), are also excepted from the discharge by the new provisions. Since such taxes represent monies that the debtor is holding for the government, which, if traceable, would be excluded from property of the estate, it makes sense to protect those debts from discharge.

Section 708

Section 708 adds a new §1141(d)(6) to bar corporate debtors from receiving a discharge of debts for fraudulent conduct, or for taxes arising from fraudulent returns or an attempt to evade taxes. This change is a significant break from prior law. Until now, only criminal debts owed to the United States were nondischargeable, pursuant to 18 U.S.C. §3613. Civil fraud and fraudulent tax returns might occur far more often than criminal conduct, so this may be a significant factor when debtors begin drafting plans in post-October 2005 cases.

Section 710

This section clarifies the proper treatment of tax claims in Chapter 11 plans. Prior to its amendment §1129(a)(9)(C) of the code gave debtors up to six years from the date the taxes were assessed to pay priority tax claims, with no other limitations on how or when the payments were to be made or how such payments should relate to payments to other classes of creditors. Similarly, while secured tax claims were to be paid in full with interest, there was no limitation on how long such payments could continue or when they had to be made. Yet at the same time, tax authorities were not allowed to vote on the plan's terms. The natural result of the combination of vague provisions and creditor disenfranchisement was plans that put tax claims at risk while preferentially paying the claims of favored trade creditors.

It was not uncommon to find proposals that backloaded payment of tax claims to the end of the six-year period, putting them at much greater risk if the debtor's plan failed, or that paid those tax claims only yearly, while other creditors received quarterly payments.[9] Similarly, if the tax claim were secured, debtors might stretch out payments for long periods, even if the tax claim would have priority status. Further, many plans treated the six-year period as automatically running from the date of confirmation, regardless of when the taxes had actually been assessed. And, finally, if the debtor did obey the law, the result could be an unwieldy hodge-podge of payment terms for taxes, since the assessments may have occurred on various dates.

Section 710 amended several sections to address these points. Section 1129(a)(9)(C)(ii) was added to change the payment period from six years from the assessment date to five years from the date of the order for relief. In some cases, this change will actually extend the time for payment of a tax[10]; in any event, it provides an easily identifiable outside date for the payments and encourages prompt confirmation to give the debtor the maximum time for payment of the taxes under the plan. Second, §1129(a)(9)(C) was further amended to require that plans provide for payment of tax claims in a manner no less favorable than that accorded to the most favored nonpriority unsecured claims, other than an ''administrative convenience'' class of claims which may be paid more quickly.

In addition, §1129(a)(9)(D) was added to provide that secured tax claims which, but for their secured status, would otherwise be payable as priority claims must be paid in a manner which is no less favorable than if the claims were merely priority. The combination of these provisions ensures that priority tax claims are not treated worse than general unsecured claims.

Section 714

Section 714 of BAPCPA resolves another issue which has occasioned much litigation over the last few years. Section 523(a)(1)(B) of the code excepts from discharge taxes where the debtor has failed to file a ''return,'' but does not define that term nor provide guidance as to whether returns that taxing authorities make on behalf of delinquent taxpayers should qualify for that treatment. Section 714 adds language to §523(a) to make it clear that the debtor must have filed a ''return'' that satisfies applicable nonbankruptcy law.[11] Moreover, substitute returns made by taxing authorities, with the cooperation of, and signed by, the debtor, are also included in this definition in order to encourage cooperation by the taxpayer. However, a return prepared by the taxing authority without the debtor's cooperation will not qualify.[12]

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[8] Making them dischargeable, though, had the effect of stopping the accrual of interest on the claims.

[9] The value of this extended payout period was, of course, enhanced by the debtor's ability to force the tax authorities to accept low interest rates during that time.

[10] If the tax claimed was assessed more than one year before the petition was filed, the new five-year period from filing date time would be longer than the six years under the prior rule. On the other hand, many courts approved plans imposing a uniform ''six years from the effective date'' period, which, whether correct or not, would be shortened by this provision.

[11] The amendment is intended to overrule *In re Elmore*, 165 B.R. 35 (Bankr. S.D. Ind. 1994), holding that returns submitted to Tax Court as evidence were ''filed'' for dischargeability purposes.

[12] This amendment is intended to codify the result of *In re Hindenlang*, 164 F.3d 1029 (6th Cir. 1999), which found that a

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The amendment also resolves another problem in §523(a)(1)(B) with respect to state taxes. Most state taxes "piggy-back" their income tax computation on federal tax returns, and state law normally requires taxpayers to provide some form of notice to the state if a federal audit results in changes in the income calculation on the return. In some states, this requirement is phrased in terms of an obligation to file a new "return"; in other states, the obligation may be to submit a "notice" or "report" to the state, which may then assess the liability. While there may be procedural differences among the states in how a change is to be reported, the laws generally all require the taxpayer-debtor to take some affirmative action. The problem is that, read literally, the code only treats violations of requirements to file "returns" as warranting a discharge exception[13] Yet, for the purposes of this requirement, there is no meaningful difference between a return, a notice, or a report. Thus, §714 further amends §523(a)(1)(B) to apply to both returns and "equivalent report[s] or notice[s]."

Section 716

A related provision deals with the definition of a "return" for purposes of the requirement in new code §1308 that a debtor must have filed all applicable returns in order to avoid dismissal of the case. Since even a return prepared by the government for collection purposes will provide a basis for filing a tax claim, the debtor may rely on those returns prepared under I.R.C. §6020(b) or similar state law to satisfy this return filing obligation. Any unpaid tax owed because of such a return, though, will remain nondischargeable under §523(a)(1)(B), as described above.

Section 719

Section 719 of BAPCPA substantially revises the Bankruptcy Code sections containing the "separate entity" rules, *i.e.*, special rules for determining the estate's state and local income taxes. Section 728 and subsections (a) and (b) of §§1146 and 1231 of the code were repealed, and §346 was substantially rewritten to conform those rules with the federal rules.[14] These amendments corrected several inconsistencies between the treatment of the estate's federal and state income taxes and resolved a number of anomalies. For instance, terminating the taxable year in which the case is filed on the petition date was an option for federal taxes, but was mandatory for state income taxes. These contradictions were particularly problematic because state income tax systems typically "piggy back" on federal taxes.

Impact on Localities

The 2005 bill also includes certain procedural changes in the treatment of tax liens that should be advantageous to local governments.

Section 701

Section 701 of BAPCPA substantially limits the provisions of prior-§724(b), which allowed for the subordination of secured tax claims in order to pay priority claims, including administrative claims incurred in failed Chapter 11 cases. Moreover, the prior law allowed subordination of the tax liens even when there might be other assets in the case from which those claims could be paid. Under §63(c)(3) of the pre-1978 Bankruptcy Act, tax liens could be subordinated only to pay the costs of administration of a Chapter 7 case and small wage claims, and then only with respect to liens on personal property, a relatively small component of all tax liens.

In the 1978 code, this provision was significantly expanded to allow subordination of liens on personal and real property to all first through (then) sixth priority claims.[15] This result was directly contrary to normal state law, under which, liens securing ad valorem property taxes "prime" all other liens, even those that predate the tax lien. That priming effect was, moreover, protected elsewhere by the code, as, for instance, in §362(b)(3), which allows certain priming liens to be perfected against the trustee. Conversely, subordinating the liens meant that professional fees from Chapter 11 were paid by diverting funds that would otherwise go for essential public services such as schools, police, and firefighters.

The new language in code §724(f) excepts liens for ad valorem taxes from subordination, except as necessary to pay priority claims for employee wages and benefit contributions. Thus, localities (and to a lesser degree, states) will continue to receive property tax revenues while rank and file employees are still protected. In addition, §724(e) requires the trustee to exhaust other unencumbered assets and surcharge other secured creditors for the costs of preserving their assets, prior to seeking a recovery from tax liens. Thus, tax liens will now be the last asset to be sacrificed, not the first.

Finally, §505(a)(2) of the code was amended to provide that challenges to the amount or legality of any amount for ad valorem taxes may only be made if the time in which to do so has not lapsed under applicable nonbankruptcy law. In this way, states and localities will not face refund requests and assessment challenges long after the applicable deadline, when it may be difficult or impossible to still marshal crucial evidence. More importantly, they will also be spared the need to make retroactive, unforeseen payments that could severely disrupt current budgeting, since the revenue at issue would have been budgeted and spent in a prior tax year.

Section 712

Section 712 amended §506(b) of the code to allow the recovery of attorneys' fees and costs by an oversecured statutory lien holder, including creditors holding claims for ad valorem and other secured taxes, and

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return filed after the taxing authority has prepared its return cannot constitute "an honest and reasonable attempt to satisfy the requirement of the tax law." See also the majority and dissenting opinions in *In re Payne*, 431 F.3d 1055 (7th Cir. 2005).

[13] *See, e.g., In re Jackson*, 184 F.3d 1046 (9th Cir. 1999).

[14] *See, e.g.*, I.R.C. §§1398 and 1399.

[15] Thereafter, in the 1994 amendments, domestic support obligations were created as a new seventh priority claim, moving down taxes to eighth priority. BAPCPA moved those domestic support obligations to first priority, but left taxes in eighth position.

amended §506(c) to allow applicable ad valorem taxes to be surcharged against a secured creditor's collateral.

Section 706

This section made a technical change in §507(a)(8)(B) of the code by replacing the term ''assessed'' with the term ''incurred,'' to eliminate the confusion that arose under varying state laws. ''Assessment'' has a specific meaning under federal law, dealing with the actual determination of the tax, but many state laws use that term for other stages of their tax collection process, particularly with respect to property taxes and the underlying ''assessment'' of the value of the property. The code is clearly geared to the federal meaning, and significant confusion arose when it was applied willy-nilly to the term ''assessed'' as used for other purposes in various state laws. ''Incurred'' on the other hand, while not a term of art in federal tax law, still has a relatively well settled meaning relating to the date when the tax becomes due Thus, by using that term, it is possible to better ensure that the code provisions apply when and how expected.

WHAT WILL RESULT FROM THE CHANGES?

An early, very small, and totally unscientific study among state tax counsel turns up the predictable—''it's too soon to tell'' how the changes to the bankruptcy law will affect the various players. More seriously, though, that reaction is exactly what one would expect with respect to many provisions. Most large corporate Chapter 11 cases, for instance, never did have problems filing income tax returns and paying taxes during the pendancy of the bankruptcy. And, as to the smaller Chapter 11 cases, the new small business proposals present a whole series of hurdles that such cases must navigate, with tax compliance being only one. To date, there appear to have been no reported decisions involving those provisions of BAPCPA.

Similarly, even with the efforts to speed up Chapter 11 cases, it is very early yet to see any such cases going to confirmation or having reported issues about interest rates, payment terms, or the like. It is certainly likely that such plans will put added burdens on debtors. Interest rates on taxes will almost certainly be higher than before, the time period for paying them may be considerably shorter, and the ability to manipulate the payment of taxes in order to shore up the debtor's operational cash flow in the immediate aftermath of bankruptcy will be curtailed. On the other hand, a debtor that abides by the code's terms will at least gain the advantage of knowing with some certainty what to do in the plan so as to avoid having to contend with numerous objections to confirmation by tax authorities.

The provisions for excepting certain debts for taxes and for fraud, on the other hand, may well lead to considerable controversy in the future. The rationale for not using discharge exceptions for corporations is that all of the value of the corporation is distributed in the case and the value of its future earnings are part of the value of the stock distributed to the lowest echelon of creditors. How then does one account for the result of excepting a debt from discharge? Should the plan do nothing special with respect to such debts and simply allow the tax creditors to sue the company and be paid from future earnings?

If so, this will diminish the value of the stock, and that must be accounted for in the calculus of payments. Or, if the new equity will have to bear the cost of the nondischargeable debt in any event, is it simpler to just provide for payment of that amount in full upon confirmation to get it over with? Will this raise similar issues to those in Chapter 13 where debtors seek to make preferential payments on debts that are excepted from discharge? The issues are endless in this brave new world BAPCPA ushers in

The one factor that has been noted by state tax counsel already is an increase in the numbers of Chapter 13 cases terminated quickly for failure to provide the required documents and tax returns. The code is relatively clear about the papers that must be produced, although it is likely to take some time for local practice, local rules, and case law to determine the exact protocol for who does what and when. Even the question of unfiled returns is not quite as simple as it seems—the McAllister case, cited above in footnote three , involved a debtor who had not filed returns because she was a nonresident.

In light of the median income of bankruptcy filers, it will certainly also be possible that a fair number will not have filed returns because their income was too low for them to have been obliged to do so. Thus, it will be important for the courts to set up a protocol to determine quickly whether the debtor has filed all recent returns and, if not, whether it is validly excused from doing so.

Further, the system will need to be clear about who is responsible for monitoring the status of the return filing, and for filing notices to the court and/or enforcement motions if returns are not filed. If thought is given to how to properly monitor and enforce these requirements, the result is likely to be a system that assists debtors and tax authorities alike to process the cases of those who are appropriately seeking relief and to quickly weed out the cases of those who are not.

The other interesting factor to watch will be the effect of the ''localities'' provisions discussed above. City and county taxing authorities were among the most active in supporting passage of BAPCPA (and all of its predecessors during the exactly eight-year odyssey between the introduction of the first bill on Oct. 17, 1997, and the effective date of BAPCPA on Oct. 17, 2005). At a minimum, the reduced number of challenges that can be brought to ad valorem taxes and the limits on subordination should limit the occasions on which small governmental entities find themselves being forced into litigation far across the country. At best, from their viewpoint, they will retain the same advantaged status for collecting their revenues that they hold outside of bankruptcy.

As to the rest of what may develop, in the words of Bette Davis in *All About Eve*, ''Fasten your seat belts. It's going to be a bumpy ride!''

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