
In the United States Bankruptcy Court
for the
Southern District of Georgia
Brunswick Division

In the matter of:)
) Chapter 13 Case
RALPH BENTON PERKERSON, JR.)
) Number 93-20327
)
Debtor)

MEMORANDUM AND ORDER
ON DEBTOR'S OBJECTION TO CLAIMS

On July 27, 1994, Debtor filed objections to claim number five of the Georgia Department of Revenue and claims number six, seven, and eight of the Internal Revenue Service. A hearing to consider these objections was held in Brunswick, Georgia, on September 14, 1994, after which the Court took the matter under advisement. Based upon the evidence and stipulations adduced at the hearing, the parties' briefs and applicable authorities, I make the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

Debtor filed a voluntary petition under Chapter 7 of the Bankruptcy Code on May 24, 1993. On April 4, 1994, in response to the U.S. Trustee's motion to dismiss

Debtor's Chapter 7 case for substantial abuse, this court entered an Order converting Debtor's Chapter 7 case to a case under Chapter 13 of the Bankruptcy Code. The Internal Revenue Service ("IRS" or "Service") and Georgia Department of Revenue ("Department of Revenue" or "State") thereafter filed proofs of claim in Debtor's Chapter 13 case. The IRS' proof asserts a secured claim of \$297,973.26, a priority unsecured claim in the amount of \$28,013.62 and a general unsecured claim of \$1,563.78. The Department of Revenue's proof asserts a secured claim of \$63,792.42 and a priority claim in an unknown amount.

The Service's secured claim of \$297,973.26 and the Department of Revenue's secured claim of \$63,792.42 stem from 1984 taxes that Debtor incurred when he left an Alabama partnership in which he practiced medicine. His departure from the partnership apparently triggered certain state and federal income tax recapture provisions, giving rise to a substantial tax liability. On August 28, 1987, Debtor filed a voluntary petition under Chapter 11 of the Code in the Northern District of Alabama to deal with the 1984 taxes and other obligations.

Debtor filed an objection to the Georgia Department of Revenue's claim in that case, and the Alabama bankruptcy court entered an order fixing the Department's claim at \$34,538.00. On February 27, 1989, the Alabama bankruptcy court confirmed Debtor's Chapter 11 Plan. Because the IRS had apparently filed a notice of tax lien against Debtor prior to his filing under Chapter 11, the Plan treated the IRS as a secured creditor, providing

that it would be paid \$206,333.51 over a ten-year period with interest at a rate of ten percent per annum. The State of Georgia, on the other hand, was treated as a priority unsecured creditor because its claim was entitled to priority treatment under section 507(a)(7) of the Code. Accordingly, the Plan provided that the State would receive \$34,538.00 over six years, without interest.¹

At some point in 1990, Debtor defaulted on his obligations under the Chapter 11 Plan. Prior to his default, Debtor had made payments totalling \$26,731.14 to the IRS and payments totalling \$4,295.52 to the Georgia Department of Revenue. The IRS also received an "involuntary" payment of \$7,739.00 after Debtor's default.

Debtor objects to the secured portion of both the Service's and the Department's claim.² His objection is based upon the contention that, because both claims were previously provided for in his confirmed Chapter 11 plan, they should be allowed in conformity with the terms of that plan. With respect to the IRS, Debtor contends that confirmation of his Chapter 11 plan affected a novation of his 1984 tax liability to it. That is, confirmation created a new obligation that replaced his original obligation to the IRS, and as a result, its claim in his present Chapter 13 case must be computed under the terms of the previously confirmed Chapter 11 plan. Thus, according to Debtor, the IRS should have a

¹ The parties are unable to explain why the Plan did not provide for interest in its provision for the State of Georgia's tax claim in conformity with section 1129(a)(9)(C).

² The Department claims to be secured in this case because it filed a notice of tax lien against Debtor after he defaulted under his Chapter 11 plan.

total secured claim in his Chapter 13 case of \$255,481.33, \$197,910.03 in principal and \$57,571.31 in interest. As to the claim of the State of Georgia, Debtor acknowledges that, because the State held a priority claim in his Chapter 11 case, its claim was not subject to discharge under sections 1141(d)(2) and 523(a)(1)(A) of the Code. Nevertheless, Debtor contends that the confirmation of his Chapter 11 Plan had a dual effect upon the State's claim. First, Debtor asserts that the amount of the State's claim was conclusively determined to be \$34,538.00 by the Alabama bankruptcy court when it ruled upon his objection to the claim. Second, Debtor contends that the manner in which the claim was to be paid in his Plan dictates, under the principle of *res judicata*, that the State is entitled to only an unsecured claim that must be paid in full without interest in his Chapter 13 plan.

The response of the State and the IRS to Debtor's objection is essentially the same. Both argue that, because Debtor's 1984 state and federal tax returns were last due within three years of Debtor filing his Chapter 11 petition in Alabama, these obligations became priority claims in the Chapter 11 case pursuant to section 507(a)(7)(A)(i). As a result, the claims were not, under sections 523(a)(1)(A) and 1141(d)(2), discharged upon confirmation of Debtor's Chapter 11 Plan. Thus, according to the State and the IRS, confirmation of Debtor's Chapter 11 Plan had no effect upon their tax claims against Debtor. The critical difference between the position of the IRS and that of the State is the fact that the IRS was treated as a secured creditor in the Chapter 11 Plan, while the State was treated as a priority creditor.

CONCLUSIONS OF LAW

Section 1141, in relevant part, provides:

(a) Except as provided in subsections (d)(2) and (d)(3) of this section, the provisions of a confirmed plan bind the debtor, . . . and any creditor, . . . whether or not the claim or interest of such creditor, . . . is impaired under the plan and whether or not such creditor, . . . has accepted the plan. . . .

(d)(1) Except as otherwise provided in this subsection, in the plan, or in the order confirming the plan, the confirmation of a plan--

(A) discharges the debtor from any debt that arose before the date of such confirmation, and any debt of a kind specified in section 502(g), 502(h), or 502(i) of this title . . .

(2) The confirmation of a plan *does not discharge* an *individual* debtor from any debt excepted from discharge under section 523 of this title.

11 U.S.C. Sections 1141(a), (d)(1) and (d)(2) (emphasis added). Thus, unless excepted from discharge under section 1141(d)(2), a pre-confirmation debt is discharged when a plan is confirmed. The confirmed plan replaces the pre-confirmation debt with a new obligation, the terms of which are dictated by the plan.³ However, where the debtor is an individual and a debt is of a kind specified in section 523, confirmation does not discharge the debtor from

³ See e.g., In re Benjamin Coal Co., 978 F.2d 823, 827 (3rd Cir. 1992); Paul v. Monts, 906 F.2d 1468, 1474-76 (10th Cir. 1990); In re Valley Park Group, Inc., 96 B.R. 16, 24 (Bankr. N.D.N.Y. 1989).

that debt.

Because Debtor filed his Chapter 11 case as an individual, the first issue in this case is whether the IRS and the State held a claim in that case that was excepted from discharge under section 523. As set forth above, both agencies contend that their claims were nondischargeable under section 523(a)(1)(A). Debtor concedes that the State held such a claim, but argues that the Service, as the holder of a secured claim, did not hold the sort of claim described in section 523(a)(1)(A). This section, in relevant part, provides:

(a) A discharge under section . . . 1141 . . . of this title does not discharge an individual debtor from any debt-

(1) for a tax or a customs duty--

(A) of the kind and for the periods specified in section[] . . . 507(a)(7) of this title, whether or not a claim for such tax was filed or allowed;

11 U.S.C. §523(a)(1)(A). Section 507(a)(7)(A)(i), in turn, provides:

(a) The following expenses and claims have priority in the following order:

(7) Seventh, allowed *unsecured* claims of governmental units, only to the extent that such claims are for--

(A) a tax on or measured by income or gross receipts--

(i) for a taxable year ending on or before the date of the filing of the petition for which a return, if required, is last due, including extensions, after three years before the date of the filing of the petition;

11 U.S.C. §507(a)(7)(A)(i) (emphasis added). The IRS takes the position that, even though it held a secured claim in Debtor's Chapter 11 case, its claim was nevertheless entitled to priority under section 507(a)(7)(A)(i) and was therefore non-dischargeable under section 523(a)(1)(A). This position is not, however, supported by the plain language of Section 507(a)(7)(A)(i) or the caselaw interpreting it. As more than one court has observed, section 507 applies exclusively to unsecured claims:

Each subsection of § 507 explicitly limits its application to unsecured claims. Over and over again section 507 clearly states that its provision for priority payment extends only to unsecured claims. There would be no need for anything else with secured creditors already directing their attention not toward the bankruptcy estate but to the property encumbered by their lien. Secured and priority claims are separate types of claims and deserve different treatment. The conclusion is inescapable that a claim cannot be both secured and deserving of priority status under §507 at the same time. Both are unique under the bankruptcy laws.⁴

I therefore conclude that, because the IRS held a secured claim in Debtor's

⁴ In re Reichert, 138 B.R. 522, 526-27 (Bankr. W.D.Mich. 1992). See also In re Darnell, 834 F.2d 1263, 1265-66, n.6 (6th Cir. 1987); In re Krump, 89 B.R. 821, 823 (Bankr. D.S.D. 1988); In re Healis, 49 B.R. 939, 940-41 (Bankr. M.D. Penn. 1985).

Chapter 11 case, confirmation of Debtor's Chapter 11 plan discharged Debtor from the pre-petition obligation and effected a novation of his 1984 tax obligations to the IRS. Accordingly, with respect to Debtor's 1984 tax obligations to the IRS, the terms of Debtor's confirmed Chapter 11 plan control the priority and amount that must now be repaid in Debtor's Chapter 13 plan.

As to the State's claim, even though Debtor concedes that the State's claim was excepted from discharge in his Chapter 11 case, he nevertheless contends that, under principles of *res judicata*, the State was bound by the terms of his confirmed plan at least with respect to the amount of its claim, \$34,538.00, and the manner in which the claim is to be repaid; that is, as an unsecured claim to be paid in full without interest. This contention essentially seeks to avoid the effect of nondischargeability.

In construing section 1141, as I must, in a manner that gives effect to all its provisions, I conclude that subsection (a), the "res judicata" provision, is plainly limited by the exception from discharge contained in section 1141(d)(2). Subsection (a) is effective, at most, to protect an individual debtor from the collection efforts of a creditor holding a non-dischargeable debt only for so long as the debtor adheres to the plan payment schedule. When an individual completes payments or defaults under a confirmed Chapter 11 plan, section 1141(a) ceases to protect the debtor, and the amount and priority of the remaining tax claim is, under section 1141(d)(2), unaffected by the terms of the prior plan, except of

course to the extent that payments were credited to the balance due.⁵ Accordingly, I hold that Debtor's previously confirmed Chapter 11 plan has no effect upon either the amount or priority of the Georgia Department of Revenue's claim for 1984 taxes.

ORDER

Pursuant to the foregoing Findings of Fact and Conclusions, IT IS THE ORDER OF THIS COURT that Debtor's Objection to the Claims of the Internal Revenue Service is hereby SUSTAINED.

FURTHER ORDER OF THIS COURT that Debtor's Objection to the Claim of the Georgia Department of Revenue is hereby OVERRULED.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia

This ____ day of November, 1994.

⁵ See In re Gurwitch, 794 F.2d 584, 585 (11th Cir. 1986). ("The Bankruptcy Code makes clear under 11 U.S.C. § 1141(d)(2) that the confirmation of a plan of reorganization does not fix tax liabilities made nondischargeable under 11 U.S.C. § 523. Moreover, the Code states that these taxes are nondischargeable 'whether or not a claim for such tax was filed or allowed.' Section 523(a)(1)(A).")