Indiana Law Journal

Volume 35 | Issue 3 Article 4

Spring 1960

The Rights of a Trustee in Bankruptcy as Against a Federal Tax Lien

THE RIGHTS OF A TRUSTEE IN BANKRUPTCY AS AGAINST A FEDERAL TAX LIEN

In the recent case of *In the Matter of Fidelity Tube Corp.*,[1] the Third Circuit Court of Appeals held that a trustee in bankruptcy was not a judgment creditor within the meaning of section 3672 of the 1939 Internal Revenue Code.[2] While this is not a shocking decision considering the Supreme Court's decision in the case of *United States* v. *Gilbert Associates, Inc.*,[3] it is noteworthy in that the Circuit Court successfully distinguished the *Gilbert* case from a case involving a trustee in bankruptcy[4] and still held the trustee was not a judgment creditor for purposes of section 3672 of the Code. When one considers the increasing frequency of bankruptcy in the United States[5] and the relatively small proportion of bankruptcies which are asset cases,[6] this decision can have devastating consequences for any of the first three priority claimants under section 64a[7] of the Bankruptcy Act. Unless the trustee can prevail over the federal tax lien, the chances of any of these claimants collecting their

1. 28 U.S.L. Week 2555 (3d Cir. 1959). Affirming on rehearing before the court en banc the case reported in 59-2 U.S.T.C. 9683.

2. Now Int. Rev. Code of 1954, § 6323.

3. 345 U.S. 361 (1953). In that case the Supreme Court said, "We think Congress used the words 'judgment creditor' in Section 3672 in the usual, conventional sense of a judgment of a court of record." *Id.* at 364.

4. The court said, "[T]he Supreme Court's decision in Gilbert was motivated by a desire to procure uniformity among the States in determining questions relating to priority of payment of lien claims and that the Supreme Court ruled as it did because it feared that if each State was left free to designate who was or who was not a 'judgment creditor' under their respective laws there would be lack of uniformity. . . . [U]nder Section 70c of the Bankruptcy Act there is no danger of heterogeneity since we are construing federal and not State law and that therefore the Gilbert decision is not apposite." In the Matter of Fidelity Tube Corporation, *supra* note 1.

5. Using 1945 (the all time low in the number of cases filed for bankruptcy in the United States since 1905) as the base point, the number of bankruptcies has risen at an almost fantastic rate until in 1958 there were approximately 92 thousand cases filed in the District Courts of the United States. (About 22 thousand cases more than in 1932 which was the worst year of the depression.) 32 Ref. J. 124 (1958).

6. A no asset case is one in which, after outstanding liens are paid, there is nothing to distribute to the general creditors. From the years 1946 to 1957, in cases where the bankrupt was given a discharge of his debts, slightly over 15% of the cases have been asset cases. Annual Reports of the Director of the Administrative Office of the United States Courts for years 1946-57.

7. 11 U.S.C. § 104. These priorities include many classes of expenses but they can be briefly summarized as: (1) Expenses for preserving and administering the estate, (2) Wages owed to certain classes of wage claimants, and (3) Expenses for successful opposition to an arrangement or discharge, or for adducing evidence leading to a conviction of a bankruptcy violation.

claims are greatly diminished. While neither the general creditor[8] (excepting the first three classes of priority claimants) nor the secured creditor[9] could have hoped to benefit from a contrary result in the *Fidelity Tube* case, these three classes of priority claimants could very well expect to prevail over the government in similar cases had the result been different,[10] and if other courts would accept the result in the light of the *Gilbert* case.

Section 6321 of the 1954 Internal Revenue Code[11] provides a lien for all taxes owing the United States, which will attach to any interest in property the taxpayer may have.[12] This lien arises at the time the assessment is made[13] and continues "until it is satisfied or becomes unenforceable by reason of lapse of time."[14] By its very nature and the method by which it arises,[15] the lien is secret as to persons dealing with the delinquent taxpayer, and these persons can do nothing to inform them-

8. The general creditor will take only after all valid liens and priorities have been satisfied. See 3 COLLIER, BANKRUPTCY §§ 60.01, 64.02, (14th ed. 1941) [hereinafter cited as COLLIER]; City of Richmond v. Bird, 249 U.S. 174 (1919). Since the Bankruptcy Act § 64a gives the government a fourth priority for taxes, the government would still take ahead of the general creditors under its priority.

9. As to secured creditors, ordinarily one would expect a junior lienor to advance when a senior lienor's lien has been defeated. However, due to the preservation clause of the Bankruptcy Act § 67a(3), the trustee is in effect subrogated into the shoes of the senior lienor as against junior lienors, and he preserves it for the benefit of the estate. White v. Steinman, 120 F.2d 799 (2d Cir.) *cert. denied* 314 U.S. 659 (1941).

10. If the court had held the trustee in bankruptcy to be a judgment creditor under INT. REV. CODE OF 1939, § 3672, he could claim protection from the government if the tax lien were not filed in the proper office.

11. Formerly INT. REV. CODE OF 1939, § 3670.

12. "If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount . . . shall be a lien in favor of the United States upon all property and rights to property, . . . belonging to such person." INT. REV. CODE OF 1954, § 6321. For an excellent discussion of this lien see Anderson, *Federal Tax Liens—Their Nature and Priority*, 41 CAL. L. REV. 241 (1953). See also 9 MERTENS, FEDERAL INCOME TAXATION §§ 54.38-54.46, (1956) [hereinafter cited as MERTENS].

13. INT. REV. CODE OF 1954, § 6322. Under the 1939 Code, the lien did not arise until the assessment lists were received by the collector. INT. REV. CODE OF 1939, § 3671. A tax assessment is a culmination of an administrative determination as to a particular person's liability to the government. This is very much like a judgment of a court, and the lien that arises under § 6321 can be favorably compared to a judgment lien. See 9 MERTENS § 54.38. See also Anderson, *supra* note 12.

14. INT. REV. CODE OF 1954, § 6323. Federal claims are not affected by state limitation periods. United States v. Summerlin, 310 U.S. 414 (1940). Thus unless there is fraud or failure to file a return for which there is no period of limitation, collection must be begun within six years after assessment of the tax liability. INT. REV. CODE OF 1954, § 6501. See also 9 MERTENS § 54.38 nn.20 & 21.

15. Although the date of the effectiveness of the lien is the date of assessment, the event which causes the lien to arise is demand. 9 MERTENS § 54.40. After demand, the effective date relates back to the date of assessment. 9 MERTENS § 54.38. Since the records of the assessment and demand cannot be inspected except on order of the President or under rules and regulations prescribed by the Secretary or his delegate and approved by the President, INT. REV. CODE OF 1954, § 6103, it is obvious that unless the lien is recorded, it is secret and effective as against everyone but those protected by § 6323. *In re* Litt, 128 F. Supp. 34 (E.D. Pa. 1955); 9 MERTENS § 54.40.

selves of the lien's existence.[16] To at least partially mitigate the harsh effect of such a lien, Congress, in 1913,[17] amended the provision so as to make it invalid as against a mortgagee,[18] purchaser,[19] or judgment creditor[20] unless notice of the lien was filed in the proper office.[21] In 1939, as a result of the *Rosenfield* case,[22] pledgees were added to the select group.

Another factor which has to a small degree mitigated the effect of the lien has been court construction of section 6321. Statutory liens for taxes are very strictly construed.[23] Consequently, if the government does not meet all the requirements of the statute, the lien will never arise,[24] and the first three priority classes under section 64a of the Bankruptcy Act will take ahead of the government.[25] Because of the liberal provisions in the Bankruptcy Act allowing for lien perfection, however, it would be rare indeed if the government would fail to perfect its lien in a bankruptcy situation.[26] Thus these three classes of claimants really have little hope apart from the trustee.

The trustee in a normal case is fairly well equipped to preserve a good portion of the bankrupt's estate for the general creditors, thanks to

16. See United States v. Snyder, 149 U.S. 210 (1893) where the Court held that federal tax liens were not subject to state recording statutes, and that the prior unrecorded tax lien would beat even a bona fide purchaser for valuable consideration.

17. 37 STAT. 1016 (1913).

18. It appears, however, that only mortgagees in the conventional sense are protected. See United States v. Ball Construction Co., 355 U.S. 587 (1958).

19. A purchaser within the meaning of § 6323 is one who acquires title for valuable consideration in the manner of vendor and vendee. United States v. Scovil, 348 U.S. 218 (1954).

20. A judgment creditor within the meaning of the INT. REV. CODE OF 1954, § 6323, is one who holds a judgment of a court of record in the usual and conventional sense. United States v. Gilbert Associates, *supra* note 3. When a person becomes a judgment creditor for purposes of § 6323 of the Code is not a matter of state law. United States v. Acri, 348 U.S. 211 (1955); United States v. Security Trust & Sav. Bank, 340 U.S. 47 (1950).

21. The proper office is a matter of state law, and notice of the lien must be filed in the office designated by that state in which the property subject to the lien is located. If the state has made no provision for filing of the lien, it must be filed with the clerk of the district court for the district in which the property is located. INT. REV. CODE OF 1954, § 6323.

22. United States v. Rosenfield, 26 F. Supp. 433 (E.D. Mich. 1938).

23. MacKenzie v. United States, 109 F.2d 540 (9th Cir. 1940); *In re* Crockett, 150 F. Supp. 352 (N.D. Cal. 1957); *In re* Holdsworth, 113 F. Supp. 878 (D.N.J. 1953).

24. However the courts sometimes fail to require strict compliance with the statute. Although the Code requires demand for the lien to be effective, this need not be a formal demand. *In re* Baltimore Pearl Hominy Co., 5 F.2d 553 (4th Cir. 1925).

25. The government would then be relegated to its priority status under the Bankruptcy Act § 64a(4), 11 U.S.C. § 104a.

26. Bankruptcy Act § 67b; 11 U.S.C. § 107b, provides that notwithstanding § 60 of the Act, certain statutory liens, including a lien for taxes, may be valid against the trustee even though arising or perfected while the debtor was insolvent and within four months of bankruptcy. Also if there is a filing of notice of the lien as required by local statute, the Act even permits perfection after the filing of the petition in bankruptcy.

Sections 60a, 67a, 67c, 70c, and 70e of the Bankruptcy Act. Section 60a deals with preferences. In many cases a federal tax lien would in theory fall under this provision, and the trustee could thereby avoid the lien as a preference.[27] However, Congress has effectively blocked the trustee from this avenue with the passage of section 67b, which provides a sweeping validation of statutory liens, including those for taxes, as against the trustee.[28] Thus the trustee must look elsewhere to attack the federal tax lien.

Section 67a has essentially the same effect as section 60a except that 67a is aimed at liens obtained by legal or equitable proceedings rather than preferences. This section is also aimed at fraudulent transfers, and a preference is not necessarily fraudulent.[29] The use of this section, however, is not relevant to federal tax liens because the federal lien is statutory and not obtained by legal or equitable proceedings.

Section 67c of the Bankruptcy Act provides some hope for the trustee even though it is very slight and very limited. The gist of this section is that when the statutory lien, including one for taxes, is on personal property not accompanied by possession; or where the lien has not been enforced by sale prior to the filing of the petition in bankruptcy, it will be postponed in payment to the first two classes of priorities defined in section 64a of the Bankruptcy Act.[30] By its very terms, this section is of limited value to the trustee because it applies only to personal property.[31] Since the tax lien applies to all the debtor's property,[32] section 67c

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27. In 3 COLLIER §§ 60.07, 60.09 it is stated that after 1938 involuntary as well as voluntary transfers were considered preferences if the other elements were present. § 60.12 says that statutory liens also should have been considered preferences, but never have been because of the Bankruptcy Act § 67b; 11 U.S.C. § 107b.

28. ". . . . statutory liens for taxes and debts owing to the United States or to any State or any subdivision thereof . . . . may be valid against the trustee, even though arising or perfected while the debtor was insolvent and within four months prior to the filing of the petition . . . ." Bankruptcy Act § 67b; 11 U.S.C. § 107b; See also 3 COLLIER § 60.12.

29. Van Iderstine v. Nat'l Discount Co., 227 U.S. 575, 582 (1913); 3 COLLIER § 60.03.

30. "Where not enforced by sale before the filing of a petition . . . (1) Though valid against the trustee under subdivision b of this section, statutory liens, including liens for taxes or debts owing to the United States . . . on personal property not accompanied by possession of such property . . . shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision a of section 64 of this Act . . . ." 11 U.S.C. § 107c.

Clause (1) of § 64a is a detailed list of expenses that can generally be classed as administration expenses.

Clause (2) of § 64a includes wages not to exceed $600 to each claimant which have been earned within three months of bankruptcy.

31. The provisions of § 67c of the Bankruptcy Act do not apply to real property. *In re* Pa. Central Brewing Co., 114 F.2d 1010 (3d Cir. 1940), *cert. denied sub. nom.* 312 U.S. 685 (1941). It also appears that the provision applies only to tangible personal property. United States v. Eiland, 223 F.2d 118 (4th Cir. 1955).

would probably be small consolation to the trustee when and if he ever got the chance to use it.[33]

Section 70c would initially appear to be the trustee's strongest line of attack against the federal tax lien. This section gives the trustee the status of a creditor holding a lien through legal or equitable proceedings.[34] In many cases, the trustee has been given all the rights of this hypothetical creditor, even in cases where equity would seem to demand a relaxation of such a stringent rule.[35] When dealing with federal tax liens, however, because the magic words "judgment creditor" were not used in section 70c,[36] the courts have done an abrupt about face with regard to the trustee's powers, and have generally held him not to be a judgment creditor for purposes of section 6323 of the Code.[37] While there was conflict on this point for a time,[38] it now appears that the *Gilbert* case[39] and the *Fidelity Tube* case[40] have settled the issue in favor of the contention that the trustee is not a judgment creditor within the meaning of section 6323.

The trustee's final line of attack lies in section 70e of the Bankruptcy Act. Under this section, it would appear at first glance, that the

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32. The lien attaches to after acquired property also. Glass City Bank v. United States, 326 U.S. 265 (1945).

33. The fact that the Bankruptcy Act, § 67c is not really an effective remedy is shown by the small number of cases where the tax lien was defeated. Freeman v. Mayer, 253 F.2d 295 (3d Cir. 1958); *In re* George Shirt Co., 162 F. Supp. 749 (D. Md. 1958).

34. ". . . . The trustee, as to all property, . . . 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, remedies, and powers of a creditor then holding a lien thereon by such proceedings, whether or not such a creditor actually exists." Bankruptcy Act § 70c; 11 U.S.C. § 110c.

35. *E.g.*, McKay v. Trusco Finance Co., 198 F.2d 431 (5th Cir. 1952); Hoffman v. Cream-O-Products, 180 F.2d 649 (2d Cir., 1950); Jubas v. Sampsell, 185 F.2d 333 (9th Cir. 1950); McGuire v. Gorbaty Brothers, 133 F.2d 675 (2d Cir. 1943); Guterman v. Rice, 121 F.2d 251 (1st Cir. 1941).

36. The Act says, "creditor then holding a lien thereon by such proceedings [referring to legal or equitable proceedings]. . . ." Bankruptcy Act § 70c; 11 U.S.C. § 110c. See note 34 *supra*.

37. In addition to the requirement that the creditor have a judgment of a court of record, United States v. Gilbert Associates, *supra* note 3, the courts have also required that the judgment creditor take steps under state law to reduce his judgment to a lien on specific property. If he does not, but merely relies on his judgment, he cannot prevail over the federal tax lien. Miller v. Bank of America, 166 F.2d 415 (9th Cir. 1948); United States v. Levin, 128 F. Supp. 465 (D. Md. 1955).

38. For cases holding the trustee to be a judgment creditor within the meaning of the INT. REV. CODE OF 1939, § 3672, see: Barish v. Cent. School Dist., 32 A.F.T.R. 1604 (S.D.N.Y. 1943); United States v. Sands, 174 F.2d 384 (2d Cir. 1949) (dictum). For cases *contra*, see: Burst v. Sturr, 237 F.2d 135 (2d Cir. 1956) which overruled the dictum in United States v. Sands, *supra;* United States v. England, 226 F.2d 205 (9th Cir. 1955); In the Matter of Green, 124 F. Supp. 481 (S.D. Ala. 1954); *In re* Taylorcraft Aviation Corp., 168 F.2d 808 (6th Cir. 1948); In the Matter of Fidelity Tube Corp., *supra* note 1.

39. See note 3 *supra*.

40. See note 1 *supra*.

trustee might have an excellent chance to prevail over the federal tax lien. Section 70e provides:

> A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this Act which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this Act, shall be null and void as against the trustee of such debtor.[41]

Thus it appears that all the trustee would have to do is find a creditor would could avoid the federal lien, and it would be void as to the trustee.[42] A brief look at the cases where other creditors have done battle with the federal tax lien (aside from the four classes of creditors protected from the secrecy of the federal lien),[43] however, reveals that the chances against the trustee finding such a creditor are very slim indeed.[44]

The government has had, since 1789,[45] a statutory priority which provides, in essence, that in any case of insolvency the debts due the United States shall be satisfied first.[46] This statute has always been construed liberally in favor of the government,[47] and in 1929,[48] the Supreme Court

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41. 11 U.S.C. § 110e.

42. In Moore v. Bay, 284 U.S. 4 (1931), the Court said, ". . . Claim for want of record or for other reasons [which] would not have been valid liens as against the claims of the creditors of the bankrupt shall not be liens against his estate . . . ." *Id.* at 4. While I have found no cases specifically holding that the doctrine of Moore v. Bay, would apply as to a federal tax lien, there is no good reason why it should not because the doctrine will invalidate all other types of specific and perfected liens if the trustee can find a single creditor who can avoid the competing lien. *E.g., In re* Central Metallic Casket Co., 170 F. Supp. 320 (E.D. Wisc. 1959); Exchange Bank of America v. Mo., 222 F.2d 567 (8th Cir. 1955). See also 4 COLLIER § 70.69. For a good article advocating the retention of the rule of Moore v. Bay, see Schwartz, *Moore v. Bay—Should Its Rule Be Abolished?*, 29 REF. J. 67 (1955).

43. These are mortgagees, pledgees, purchasers, and judgment creditors. INT. REV. CODE OF 1954, § 6323.

44. See Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L. J. 905 (1954); Cross, *Federal Tax Claims: Nature and Effect of the Government's Weapons for Collection*, 27 FORDHAM L. REV. 1 (1958). See also the Note, 30 IND. L.J. 476 (1955).

45. 1 STAT. 42 § 21 (1789). After three minor changes, the statutory priority was codified in the Revised Statutes. REV. STAT. § 3466 (1875), 31 U.S.C. § 191.

46. "Whenever any person indebted to the United States is insolvent, . . . the debts due to the United States shall be first satisfied. . . ." REV. STAT. § 3466, 31 U.S.C. § 191. This provision does not apply in a bankruptcy proceeding however. See, United States v. Gargill, 218 F.2d 556 (1st Cir. 1955). A real problem arises in this connection, however, if the government's tax claim is also a lien. See Note, 108 U. OF PA. L. REV. 77 (1959).

47. Beaston v. Farmers' Bank, 37 U.S. (12 Pet.) 102, 137 (1838). However the Court had always taken great pains to emphasize that the Act did not establish a lien. Thus the priority did not prevail over a bona fide transfer of property or over an established lien. United States v. Fisher, 6 U.S. (2 Cranch) 73 (1805); Brent v. Bank, 35 U.S. (10 Pet.) 596 (1836). For an excellent discussion of the history and character of REV. STAT. § 3466, see Kennedy, *supra* note 44.

embarked upon an even greater expansion of the priority by announcing the inchoate lien doctrine.[49] By reading the priority statute in *pari materia* with the lien provision of the Internal Revenue Code,[50] the Court has concluded that only a prior lien which is choate should prevail over the federal tax lien.[51] In the thirty years which have elapsed since this doctrine was promulgated, the Supreme Court has on only one occasion found the competing lien choate under federal standards.[52]

Thus we see that when the trustee is deprived of his status as a judgment creditor under section 6323 of the Code, his chances against the federal tax lien are meager indeed. He has a chance under section 70e of the Bankruptcy Act, but that depends on his finding a creditor who can prevail over the lien under section 6323 of the Code. He will prevail under section 67c of the Bankruptcy Act, but that depends on the fact that the lien is on personal property not in possession. As a practical matter most if not all of the trustee's weapons have been silenced either as a result of statutes or judicial interpretation.[53]

The reason the courts usually give for favoring the government is

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48. Spokane County v. United States, 279 U.S. 80 (1929).

49. The inchoate lien doctrine says in essence that a competing lien must have been specific and perfected before the federal priority attached or the priority will prevail. United States v. Texas, 314 U.S. 480 (1941); New York v. Maclay, 288 U.S. 290 (1933). Whether or not a lien is specific and perfected is always a federal question, United States v. Wadill, Holland & Flinn, Inc., 323 U.S. 353 (1945); United States v. Gilbert Associates, Inc., *supra* note 3. The Court finally set down definite standards for specificity and perfection in Ill. *ex rel.* Gordon v. Campbell, 329 U.S. 362 (1946), where it said, (1) the lienor must be identified, (2) the amount of the lien must be certain, and (3) the property to which the lien attaches must be definite. The Court implied that a transfer of title or possession might also be necessary. This implication was later made a condition of specificity in United States v. Gilbert Associates, Inc., *supra.*

50. United States v. Liverpool and London and Globe Ins. Co., 348 U.S. 214 (1955); United States v. Acri, *supra* note 20; United States v. Security Trust & Sav. Bank, *supra* note 20.

51. The Court said in the Security Trust case, *supra* note 20, "[W]e hold that the tax liens of the United States are superior to the *inchoate* attachment lien of Morrison . . . ." *Id.* at 51. (Emphasis added.)

52. United States v. City of New Britain, 347 U.S. 81 (1954). However, even in that case, the fact that the Court accepted the state court's characterization of the lien as specific and perfected did not allow the state's lien to prevail.

53. Section 67b of the Bankruptcy Act nullifies the use of Section 60a, because it provides for a sweeping validation of statutory liens. Section 67a of the Bankruptcy Act is not relevant because a federal tax lien is statutory rather than one obtained by legal or equitable proceedings. The interpretation placed on § 6323 of the Code effectively nullifies § 70c of the Bankruptcy Act as a useful weapon because unless the trustee is considered a judgment creditor for purposes of § 6323, the fact that he is a judgment creditor for other purposes is irrelevant. Finally the creation of the inchoate lien doctrine in construing § 3466 of the *Revised Statutes,* see notes 49-52 *supra,* removes a great deal of the effectiveness of § 70e because it will be almost impossible for the trustee to find a creditor who can avoid the federal lien under state law. If the trustee cannot find such a creditor, § 70e and the rule of Moore v. Bay, *supra* note 42, will not apply.

to protect the government revenues.[54] But this policy of protecting the government revenues has not always been so overriding as to outweigh all the equities on the other side. Both Congress and the Supreme Court have allowed the policy to fall by the wayside in actions brought under the Tort Claims Act.[55] The court has said that when the government is made to stand the loss, the resulting burden on each taxpayer is relatively slight; but when the entire burden falls on the injured party, it may leave him destitute.[56] As a policy matter, analogous reasoning could be applied in bankruptcy cases,[57] and the courts could allow the trustee his status as a judgment creditor even under section 6323 of the Code. In addition to being more just and equitable,[58] such a result would probably be more in harmony with the overall policy of the Code and the Bankruptcy Act.[59] If recording is an effective means for warning other credi-

54. See dicta in Glass City Bank v. United States, *supra* note 32; United States v. Phillips, 267 F.2d 374, 377 (5th Cir. 1959); United States v. Barndollar & Crosbie, 166 F.2d 793, 794 (10th Cir. 1948).

55. 28 U.S.C. § 1346(b).

56. Rayonier, Inc. v. United States, 352 U.S. 315, 320 (1957).

57. It could be argued that the government, by its negligence in not recording, lured unsuspecting creditors into a false sense of security, and thereby they consented to become unsecured creditors of the bankrupt. Such a loss resulting could be more easily spread over the whole country than to cause one creditor, or in the case of bankruptcy, all the creditors as represented by the trustee, to stand it and lose their whole claim.

58. Although this statement is essentially a value judgment, it is not one of personal bias alone. There has been growing discontent with the Supreme Court's position of constantly protecting the Government's claims at the expense of innocent businessmen. Many think this has disrupted commerce already and is potentially an even greater threat when businessmen begin to take account of the added risks due to this Court position. See MacLachlan, *Improving the Law of Federal Liens and Priorities,* 1 BOSTON COLLEGE IND. & COM. L. REV. 73 (1959). The Court's attitude has also incensed the practicing bar to the point that the American Bar Association has recommended new legislation to the present Congress in order to relax the stringent position the Court has taken. The Bar Association's Bill, H.R. 7915, along with three other identical Bills, H.R. 7914, H.R. 8406, and S. 2305, are in committee at the date of this writing. The gist of the 66 page bill is to expand the classes of security protected under § 6323; to give certain types of security and purchasers absolute protection against the government's lien; to mitigate the complete priority of the government under § 3466 of the *Revised Statutes* so that it is subject to five classes of expenses which are similar to the bankruptcy priorities in § 64a; and to have the government consent to be sued in actions affecting property in which it has a lien or interest.

59. The policy and fundamental principle of the Bankruptcy Act is equality of distribution. Sampsell v. Imperial Paper & Color Corp., 313 U.S. 215 (1941); *In re* Associated Gas & Electric Co., 149 F.2d 996, (2d Cir.), *cert. denied sub. nom.* 326 U.S. 736 (1945). The policy of the INT. REV. CODE seems to be to eliminate the harshness of the secret lien at least as to the four classes of creditors named in § 6323. In the Matter of Martin Woodcraft Corp., 130 F. Supp. 443, 444 (E.D.N.Y. 1955), *aff'd sub. nom.* 229 F.2d 895 (2d Cir. 1956). In that case the court said, "The sole function of the filing of the lien is giving notice." *Cf.* Pipola v. Chicco, 169 F. Supp. 229, 233 (S.D.N.Y. 1959), where the court said, "The very purpose of the lien-filing provision is to give notice to would-be purchasers of the government's right to collect taxes due from the owners of the property."

tors of secret liens, and Congress obviously has assumed recording is effective by enacting section 6323, the courts should not allow the government to continue luring other creditors into a trap by adhering to the policy of protecting government revenues when recording machinery has been provided whereby notice of the secret lien can be given to the world. The courts should simply interpret the language of both the Bankruptcy Act and the Internal Revenue Code according to their plain meaning and hold the trustee to be a judgment creditor[60] within the meaning of section 6323. Congress has provided protection for four classes of creditors, but court construction has unduly narrowed these classes.[61] If the government lien is secret, it is secret as to anybody dealing with the bankrupt, and since Congress has protected judgment creditors from secret liens, the trustee should be allowed his rights under the Bankruptcy Act in order to better accomplish the bankruptcy policy of equitable distribution. In addition to examining the general policy of the two acts, we must also look at the problem from the point of view of the policy of specific provisions of the Bankruptcy Act. The reason for the section 64a priorities is to encourage efficient administration.[62] The *Fidelity Tube* decision does just the opposite.

Also, the government's favored position can cause considerable hardship to others, *e.g.*, attorneys and employees. Congress has sought to insure active and efficient administration of bankrupt estates by allowing the attorney to collect his fee under the first priority of section 64a.[63] But as was shown earlier, many cases are no asset cases. The attorney is less likely to put forth his best efforts, if he accepts the case at all, when there are tax liens outstanding. He can usually be confident that the lien

60. 2 SUTHERLAND, STATUTES & STATUTORY CONSTRUCTION § 4702 (3d ed. 1943) says: "'There is no safer nor better settled canon of interpretation than that when language is clear and unambiguous it must be held to mean what it plainly expresses.'"

61. In the Fidelity Tube Case, it was not a question of Congress not providing protection for the class of creditor involved. It was a question of the courts construing the words "judgment creditor" as not to include a trustee in bankruptcy when § 70c of the Bankruptcy Act expressly provides that the trustee should have all the rights, remedies, and powers of a creditor holding a lien on the property through legal or equitable proceedings. See note 34 *supra*. This construction plus the requirement that the judgment creditor have a lien, see note 37 *supra*, has greatly narrowed the class of judgment creditors who are protected.

62. See Cohen v. United States, 115 F.2d 505 (1st Cir. 1940); In the Matter of John Horne Co., 124 F. Supp. 317 (N.D. Ill. 1954), *aff'd.* 220 F.2d 33 (7th Cir. 1955).

63. "The debts to have priority. . . . and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases and to the bankrupt in voluntary and involuntary cases, ..." Bankruptcy Act § 64a, 11 U.S.C. § 104a. For a good discussion of the subject of legal fees in bankruptcy see, Reich, *Let's Talk About Fees*, 59 COM. L.J. 108 (1954).

will prevail, and his chances of recovery for his services are diminished.[64] The plight of employees of the bankrupt is even sadder than that of attorneys. Generally, they will not quit their jobs before bankruptcy because of sociological and economic reasons.[65] Thus they are almost forced to sink or swim with the bankrupt. Congress has recognized this plight by granting them a second priority under section 64a.[66] The wage earner's needs are usually much more serious and much more immediate than those of the government.[67] The analogy to the Tort Claims Case is especially cogent in this area, and the courts could give relief by applying the plain meaning rule in interpreting the Bankruptcy Act and the Code.[68]

Thus we see that the results of the *Gilbert*[69] and *Fidelity Tube* cases[70] are unfortunate and probably unwise. That there is a great deal of discontent with these decisions and many others which give the government an almost impregnable position is obvious. The practicing bar has attempted to introduce legislation,[71] many writers have expressed dissatisfaction with the results,[72] and the state and lower federal court judges have actually attempted to change the judicially created laws only to be reversed by the Supreme Court on appeal.[73] This problem of com-

64. Since he probably would not prevail over the tax lien, *supra* note 53, and since less than twenty percent of the cases where the bankrupt is given a discharge are asset cases, *supra* note 6, the attorney's only alternative is to demand security for his services. See Reich, *supra* note 63.

65. REYNOLDS & SHISTER, JOB HORIZONS, 1949. "Out of his employment experience the worker develops a set of basic attitudes and beliefs about jobs: a definition of what constitutes a 'good job,' a feeling that job opportunities are scarce and valuable, a strong attachment to a particular plant and a particular community . . . ." *Id.* at 83-84. "[T]he worker who has located a 'good job' quickly develops a marked attachment to it and a strong aversion to change. . . ." *Id.* at 87.

66. Bankruptcy Act § 64a(2), 11 U.S.C. § 104a(2). See also 4 COLLIER § 67.27.

67. The government's total revenue for any one year is not adversely affected by the fact that in the single case of the trustee in bankruptcy, it does not prevail. Also the government has a ready source of credit when it needs money. The individual employee, on the other hand, generally does not have substantial savings to fall back on, and his avenues of credit are usually cut off abruptly when he becomes jobless.

68. Here the government could very easily spread this loss over the whole nation, and no one taxpayer would be adversely affected. If the wage earner, however, were made to bear the loss, it might be unduly burdensome.

69. See note 3 *supra*.

70. See note 1 *supra*.

71. See note 58 *supra*.

72. See MacLachlan, *supra* note 58; Kennedy, *supra* note 44; and Cross, *supra* note 44.

73. For cases where lower court opinions were reversed on appeal to the Supreme Court see, United States v. Scovil, *supra* note 19; United States v. Liverpool and London and Globe Ins. Co., 348 U.S. 215 (1955); United States v. Gilbert Associates, *supra* note 3; United States v. Security Trust & Sav. Bank; *supra* note 20; United States v. Acri, *supra* note 20; United States v. Waddill, Holland & Flinn Inc., 323 U.S. 353 (1945).

plete government supremacy is of judicial origin[74] and could have been avoided by never inventing the inchoate lien doctrine. As to the trustee in bankruptcy, the problem could have been avoided by applying the plain meaning rule to both the Bankruptcy Act and the Code. Allowing the trustee to be a judgment creditor under 6323 would not put the government at any serious disadvantage either. The only time the government could possibly be hurt would be when it engages in the practice of non-recording of its lien.[75]

LANDLORD AND TENANT: DEFECTS EXISTING AT THE TIME OF THE LEASE

In the bailment and sale of chattels the law of negligence has imposed on the bailor and seller a duty to exercise reasonable care in inspecting and preparing a chattel so that it will be safe for its intended use. Implied warranties have developed in the sale of chattels. But *caveat emptor* still prevails in the sale and leasing of real property; and the liability of the landlord for injuries caused the tenant by defects existing in the premises at the time of the demise continues to be the subject of much litigation although the courts treat the law as well settled. The general rule is stated to be that the landlord is not liable—*caveat* lessee—on the theory that the tenant assumes the risk of defective conditions existing at the time the lease is execued.[1] But the exception early developed that the landlord was liable if he knew of a defect and the tenant was unaware of it and could not have discovered it by a reasonable inspection.[2] Thus,

74. Before 1929, the inchoate lien doctrine was not used at all by the Supreme Court and before 1950 it was used only in cases arising under § 3466 of the *Revised Statutes*. See text accompanying notes 48-51. Thus the dilemma is of the Court's own making.

75. The federal tax lien is valid as against anybody except a mortgagee, pledgee, purchaser or judgment creditor without filing. United States v. Toys of the World Club, Inc., 170 F. Supp. 450 (S.D.N.Y. 1959); *In re* Litt, 128 F. Supp. 34 (E.D. Pa. 1955). It is valid as against a mortgagee, pledgee, purchaser, or judgment creditor provided it has been filed before the competing lien became specific and perfected. United States v. Security Trust & Sav. Bank, *supra* note 20; United States v. Kings County Iron Works, 224 F.2d 232 (2d Cir. 1955); United States v. Phillips, 198 F.2d 634 (5th Cir. 1952).

1. Valin v. Jewell, 88 Conn. 151, 90 Atl. 36 (1914); Whitman v. Oronor Pulp & Paper Co., 91 Me. 297, 39 Atl. 1032 (1892); Bowe v. Hunking, 135 Mass. 380 (1883); Marshman v. Stanley, 122 N.E.2d 482 (Ohio Ct. App. 1952); Stewart v. Raleigh County Bank, 121 W. Va. 181, 2 S.E.2d 274 (1939).

2. Wilson v. Lamberton, 102 F.2d 506 (3d Cir. 1924); Shotwell v. Bloom, 60 Cal. App. 2d 303, 140 P.2d 728 (1943); Wilensky v. Perell, 72 So. 2d 278 (Fla. Sup. Ct. 1954); Borggard v. Gale, 107 Ill. App. 128, *aff'd*, 205 Ill. 511, 68 N.E. 1063 (1903);