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The American Title Association is privileged to carry in this issue of "Title News" an address delivered by Mr. Harold L. Reeve, Senior Vice-President, Chicago Title and Trust Company, Chicago, Illinois, before the American Bar Association Section of Real Property, Probate and Trust Law, at Dallas, Texas, in August of this year.

Enthusiastically received by the American Bar, Mr. Reeve has numerous requests to repeat it again before various State Bar Associations, not to mention hundreds of requests he has received for copies of these remarks. Mr. Reeve presented a reduced version of this paper before the American Title Association Annual Convention in October, 1956.

Government and private liens and their relative priority are always of considerable concern to those engaged in title work. This learned treatment of a complex branch of the law deserves the attention and study of title men and women everywhere.

We extend our thanks to the Chicago Title and Trust Company and to Mr. Harold Reeve for use of this timely and comprehensive presentation.

We have printed an extra supply of this issue in anticipation of demand for additional copies. These are available at 50c each and requests may be made to The American Title Association, 3608 Guardian Building, Detroit 26, Michigan.

Those Troublesome Federal Tax Liens

By

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Those Troublesome Federal Tax Liens

By

HAROLD L. REEVE

My comments concerning the relative priority of Government and private liens will cover only two aspects of that large and important subject:

(1) The present status of the law, both as reflected in statutes and in judicial decisions, from the viewpoint of a practitioner in the real estate field; and

(2) The nature of today's problems under that law.

Such limited consideration necessarily will be confined to the more commonly encountered federal tax liens[1] and the more commonly encountered liens in the real property field. It will omit those facets of the tax-collecting problems which pertain to personal property, to transactions involving securities and similar commercial affairs.

PRESENT IMPORTANCE OF THE SUBJECT

Several circumstances make a discussion of the present state of the law concerning the relative priorities of Government liens and private liens of some importance.

One is that, by a series of recent United States Supreme Court decisions, the Government has been successful in establishing a new high point of federal supremacy for federal revenue liens upon real estate.

A second is that the 1954 Internal Revenue Code and the Treasury Regulations under that Code contain some important new provisions which heretofore have not been present.

A third is that as a result of the decisions of the Supreme Court, plus the enactment of the 1954 Code and issuance of the Treasury Regulations, the possibility of the existence of a prior, and frequently secret, federal revenue lien now has to be considered in relation to every real estate transaction, whether it involves a purchase, a mortgage, a mechanic's lien, a judgment, or some other interest in property, and in relation to every mortgage foreclosure or other suit in equity which involves real estate.

Still another is that at the request of Senator Byrd, Chairman of the Joint Committee on Internal Revenue Taxation, the present state of the law and the problems of public policy which it involves presently are being studied by the Joint Technical Staff, which serves both Houses of Congress in the drafting of federal tax legislation, and it is likely that in the next Congress consideration will be given to the question as to whether or not the law should be changed to promote fairness and to further facilitate normal property transactions without undue hazard to innocent persons.

RECENT TEST CASES IN THE UNITED STATES SUPREME COURT

Several recent Supreme Court decisions have emphasized the importance of the problem of priority of federal liens over private liens, both to those who must compete with the Federal Government for payment from the same fund or property, and to lawyers who represent purchasers of realty, or those who examine real estate titles.

In the last ten years, the Government has been before the United States Supreme Court in twelve cases which appear to have been carefully selected test cases aimed at strengthening its tax-collecting abilities. Seven of these cases have been decided in the last three years. The Government has won all twelve cases, a remarkable record. The cases involve a number of different aspects of the problem of establishing the supremacy of the federal lien for unpaid taxes over a number of kinds of liens which the federal statutes do not specifically deal with. In these cases, the United States has fared well in contests for priority as against attachment, garnishment, landlord's liens, mechanic's liens, municipal real estate tax liens, and city water rent liens. Because of their important holdings and even more important implications, the more recent cases, and the statutes which they involve, are hereinafter discussed, but, for purposes of perspective and emphasis, the recent cases have been arranged in the following table:

SCHEDU

Case	Property Involved
United States v. *White Bear Brewing Co.* (1956), 350 U. S. 1010, reversing 227 F. 2d 359 (7th Circuit); rehearing denied May 28, 1956, 351 U. S. 958, 76 S. Ct. 845.	Real estate
United States v. *Colotta* (1955), 350 U. S. 808, reversing 79 S. 2d 474 (Supreme Court of Mississippi).	Real estate
United States v. *Acri* (1955), 348 U. S. 211.	Cash and bonds in safety deposit box
United States v. *Liverpool & London Ins. Co.* (1955), 348 U. S. 215.	Payment due as fire loss by insurance company
United States v. *Scovil* (1955), 348 U. S. 218.	Sale proceeds of tenant's property
United States v. *New Britain* (1954), 347 U. S. 81.	Proceeds of real estate mortgage foreclosure sale
United States v. *Gilbert Associates* (1953), 345 U. S. 361.	Proceeds of receiver's sale of machinery
United States v. *Security Trust & Savings Bank* (1950), 340 U. S. 47.	Proceeds from sales of real estate
Goggin v. *California Labor Division* (1949), 336 U. S. 118.	Proceeds from bankruptcy trustee's sale of personal property
Massachusetts v. *United States* (1948), 333 U. S. 611.	Proceeds from assignee's sale
Illinois v. *Campbell* (1946), 329 U. S. 362.	Proceeds from receiver's sale
United States v. *Waddill, Holland & Fleming, Inc.* (1945), 323 U. S. 353.	Proceeds from trustee's sale

* Competing federal claims based on alleged

CASES

Type of Nonfederal Lien	Applicable Federal Statute	Priority Awarded to
Mechanic's lien	§ 3670	United States
Mechanic's lien	§ 3670	United States
Attachment	§ 3670	United States
Garnishment	§ 3670	United States
Landlord's lien	§ 3670	United States
Municipal water rents and real estate taxes	§ 3670	On Government appeal, case reversed and remanded to trial court for further proceedings
Municipal *ad valorem* tax	§ 3466	United States
Attachment	§ 3670	United States
*Wage claim	§ 64 and § 67 (c) of Bankruptcy Act	United States
*State unemployment tax	§ 3466	United States
State unemployment tax	§ 3466	United States
Landlord's lien and municipal tax	§ 3466	United States

y of payment rather than priority of lien.

THE IMPORTANCE OF PRIOR RIGHTS TO THE TAXPAYER'S PROPERTY

The Sixteenth Amendment went into effect in 1913. By 1950, the Treasury Department reported that its income tax and excess profits tax collections were slightly over twenty-eight billions of dollars. In the fiscal year ending 1955, the annual amount of income and excess profits taxes had increased to approximately fifty billions. An estimate of revenues from these sources for fiscal 1957 is expected to be just short of fifty-five and a half billions.[2] The Treasury further reports that the collection of employment taxes increased from less than three billions of dollars in the fiscal year ending in 1950, to over six billions in the fiscal year ending in 1955, with an estimate of over seven and a half billions to be collected by fiscal year 1957.[3] To assure the collection of this mounting revenue, the Government is accelerating its collection efforts by seeking increased operating efficiency and by enlarging the size of its staff devoted exclusively to audit and enforcement duties.

In an operation of such magnitude, there undoubtedly are and will continue to be substantial tax delinquencies. Tax delinquencies of substantial amount often result in the seizure of the taxpayer's property by the tax gatherers. Frequently, the property of a delinquent taxpayer is the only source from which competing lienors can hope for satisfaction, and often that property is insufficient in value to fully satisfy all of the liens which accrue against it. Consequently, in many of these cases, there is legal action to determine, as between the Government and private lienors, who has the first chance to collect his debt in full out of the property of the delinquent taxpayer. The right to be prior to other liens and so be the first to be paid in full is of more than academic interest.

Statistics covering the number of cases of seizure for delinquent taxes which have occurred throughout the country have not been found. An indication of some significance is furnished by Cook County, Illinois, which embraces a large part of the Chicago metropolitan area. There, according to the records of the County Recorder, the number of Notices of Federal Revenue Liens has averaged over twenty-five hundred in each of the last several years (2,854 in 1952; 2,401 in 1953; 2,705 in 1954; 2,414 in 1955; or a total of 10,374 in one county in four years). While these figures cover only one county, out of the 3,072 counties in the United States, it seems reasonable to assume that they give some indication of the scope of the Government's activities in asserting liens upon taxpayers' property throughout the country.

THE LITERATURE ON THE SUBJECT

The competition between the Federal Government, on the one hand, and its citizens, the several States and their political subdivisions, on the other, in seeking to collect taxes and debts from a common source, has attracted the attention of legal periodicals,[4] tax specialists,[5] real estate title companies,[6] and the American Bar Association.[7]

THE SOURCE OF THE POWER OF THE FEDERAL GOVERNMENT

The right of the United States to enforce the collection of taxes due it by asserting a lien upon property of a taxpayer necessarily has its origin in the constitutional provision that: "The Congress shall have power to lay and collect taxes, * * *."[8] The Sixteenth Amendment, which since 1913 has been the means of building up an incredibly powerful central government, grants the specific "power to lay and collect taxes on incomes * * * without apportion-

ment * * * and without regard to any census or enumeration." Pursuant to these constitutional grants, the Congress has passed the acts hereinafter referred to.

THE BASIC ATTITUDE OF THE COURTS CONCERNING UNTRAMMELED FEDERAL POWER

The United States Supreme Court never has been equivocal in supporting the federal power to tax and to do whatever is necessary to collect the taxes imposed upon its citizens. A century ago, the Court said:

> "The power to collect and disburse revenue, and to make all laws which shall be necessary and proper for carrying that power into effect, includes all known and appropriate means of effectually collecting and disbursing that revenue, unless some such means should be forbidden in some other part of the Constitution."[9]

Again, in 1893, when federal taxes were still relatively unimportant to the average citizen, the Court said:

> "A government that cannot, by self-administered methods, collect from its subjects the means necessary to support and maintain itself in the execution of its functions is a government merely in name."[10]

And, in 1950, when federal taxation had become the source of annual revenues measured in billions of dollars and had reached into every business and every home and every pay envelope, the Court adhered to the same principles and to a simple rule which is at the heart of the decisions and of the problem under consideration. That rule is that the effect of a private lien in relation to a provision of federal law for the collection of debts owing the United States is always a federal question.[11] The Court has been consistent in holding that state laws will not be permitted to interfere with the collection of federal taxes or the enforcement of revenue liens.[12]

THE PLAN OF THE FEDERAL STATUTES

In considering the legal aspects of federal revenue liens, a number of different statutes must be considered. There are three principal situations where federal statutes concern the priority of tax liens and competing liens. The statutes which are applicable to a given situation depend on the status of the delinquent taxpayer:

(1) The first typical situation covers the cases most frequently encountered by the real property practitioner. These are cases which do not involve the death or insolvency of the taxpayer, or extensions, reorganizations or similar proceedings under the Bankruptcy Act. The controlling statutes commonly are referred to as General Lien Provisions. They are found in the Internal Revenue Code of 1954[13] under §§ 6321 to 6323, inclusive. These sections replace §§ 3670 to 3672, inclusive, of the 1939 Code. The change in section numbers is important because even the recently decided cases involved the sections as found in the 1939 Code, not the 1954 Code.

(2) The second type of situation is one where (a) an insolvent taxpayer is involved, or (b) a deceased taxpayer is involved, or (c) an act of bankruptcy of the taxpayer is present but no bankruptcy proceeding is pending. The statute controlling such cases is not part of the Internal Revenue Code, but is found in the chapter of the Revised Statutes concerning "Debts due by, or to, the United States." The applicable section is § 3466 of the Revised Statutes.[14] This statute frequently is referred to in the decided cases and herein under the simple designation "§ 3466." Sometimes it is called the "priority statute."

(3) The third situation occurs when the taxpayer is involved in a pending proceeding under certain chapters of the Bankruptcy Act. The applicable statutes, of course, are found in the Bankruptcy Act.

Each of these factual situations is to be distinguished from the others, and therefore separate consideration is required as to each category. The text of the statutes as they exist in 1956 is set out in the appendix to this paper.

I

GENERAL LIEN PROVISIONS[15]

The statutory provisions which furnish the basis of governmental liens for unpaid taxes in situations of the first type are now §§ 6321, 6322 and 6323 of Subchapter C of Chapter 64 of the Internal Revenue Code.[16] These provisions have to be looked at in two connections, first, as to their effect on the taxpayer, and, second, as to their effect upon third parties who have interests in the taxpayer's property.

Creation of Lien

The section of the Code which gives the United States a lien for unpaid taxes is simply phrased and as between the Government and the taxpayer himself offers few problems. It is as follows:

> "§ 6321. *Lien for taxes*
>
> If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person."[17]

Property to Which the Lien Attaches

This section of the statute does not purport to give the Government's lien a priority over other liens.[18] It merely says that the amount of delinquent taxes "shall be a lien * * * upon all property and rights to property * * * belonging to such person." That concept seems simple and it is simply stated. Its application is clear as applied to the taxpayer in cases where (a) taxes are delinquent, (b) the taxpayer has property which the Government can subject to the payment of the delinquent taxes, and (c) the situation is not complicated by the existence of other liens for which third parties also seek satisfaction out of the same property. However, it is to be noted that the statute is silent as to whether the taxpayer's property rights are to be ascertained and measured by the local law of the place where the property is located or by some other criteria.

—Complications Arising Out of Equities and Existing Liens

Delinquent taxpayers frequently own equities in realty rather than unencumbered realty and those equities may be subject to a variety of other liens. In such cases, the practical questions arise as to (1) whether or not the federal lien is limited to the precise property interest or equity which was available to the taxpayer at the date when the federal lien came into existence; (2) by what rules of law the rights of private lienors and the rights of the Federal Government are to be ascertained and measured; and (3) whether the result of applying those rules is that under federal law the federal lien when it comes into existence will suddenly take precedence over other liens upon the property which under state law were validly in existence before the Government's lien was created.

It might seem at first blush that even where the situa-

tion is complicated by the existence of liens of third parties on the taxpayer's property, any particular case should respond to the principle that under the quoted statute the federal lien will attach only to the equity of the taxpayer, as of the date of the creation of the lien, whatever that equity may be under the laws of the state in which the realty is situated. Some cases decided by Courts of Appeals and other earlier cases have taken somewhat that view. Thus it has been said, when the lien attaches, "the property has in a sense two owners, the taxpayer and, to the extent of the lien, the United States"[19] and that "a federal tax lien has the effect of a judgment."[20] It has been held that the lien attaches to the equity of redemption which is subject to a mortgage,[21] but only to "the property of the person owing the tax"[22] and that the lien reaches no greater interest than the taxpayer possessed.[23]

The "Federal Question"

However, in cases involving the enforcement of federal revenue liens in judicial proceedings, the United States Supreme Court never has adopted or followed the simple concept that state law will determine the extent of the property interest of the delinquent taxpayer, to which the federal lien will attach, and the relative positions of federal and private liens. To protect the federal position, the Supreme Court has avoided the logical progression of: (a) the taxpayer owns certain "property and rights to property" under state law, when the federal lien arises, (b) the federal lien attaches to whatever property he then has, therefore, (c) the Federal Government will emerge from a lien foreclosure proceeding with the taxpayer's interest, whatever it may be, and, (d) in order to be the same interest which the taxpayer had, it obviously will have to remain subject to the private liens which lawfully encumbered it as against the taxpayer.

Instead, the Court has taken the position that:

> "The relative priority of the lien of the United States for unpaid taxes *is* * * * *always a federal question to be determined finally by the federal courts.* The state's characterization of its liens, while good for all state purposes, does not necessarily bind this court."[24] (Emphasis added.)

The net effect of viewing the priority problem as a federal question, instead of one to be determined under state rules of property, is that the extent of the property rights of the taxpayer becomes subordinated to the concept of federal supremacy. The courts seem to reason that: (a) the taxpayer owns certain "property and rights to property," (b) the federal lien attaches to that property, (c) no state law will be permitted to interfere with the federal right to assess and collect its taxes, so (d) to interfere with a federal lien, a competing private lien must have a federal basis rather than a state statutory basis for that competition[25] and must meet federal rather than state standards of being a complete and perfected lien upon the property affected.[26]

The result of reasoning of this kind is that, except as to the clearest of the cases hereinafter discussed, such as completed mortgages and judgments which have proceeded to execution, levy and sale, the federal courts achieve priority for federal liens over private liens, even though under state law the private liens are superior to the rights of the taxpayer[27] and would be superior to any other private lien arising as of the date when the federal lien arises.

Difficulties of Solution

When the Government follows the assertion of its lien by judicial action to enforce its lien as prior to pre-existing private liens, a lawyer in examining a title can at least ascertain the judicial results, whether or not he agrees

with the reasoning which produced those results. But, in a situation where there has been no judicial action to enforce the federal lien, an examining lawyer will not have the benefit of the Court's judgment as to what property the federal lien attached to and what its relative priority is as to other liens. For instance, the Internal Revenue Code contains provisions under which the Government may take the direct action of levy and sale of real estate without seeking judicial adjudication of its lien. Included is a section which provides that when a deed issues, as the result of governmental enforcement of the federal lien by levy and sale of a taxpayer's real property, "such deed shall be considered and operate as a conveyance of all the right, title and interest *the party delinquent had* in and to the real property thus sold *at the time the lien of the United States attached thereto.*"[28] (Emphasis added.)

If the property interest which has been subjected to the federal lien and the relative priority as between the federal lien and pre-existing private liens were to be ascertained under state law, the examining lawyer would be on familiar ground, but, when he has to ascertain under the federal law what that interest is and in what order the federal and other liens against the property are to be satisfied, he is in real difficulties. He must decide the relative priorities between federal and private liens as a federal question, controlled by the federal decisions upholding federal supremacy in an area where there is no clear statutory basis for the decisions, and where the federal courts are unhampered by state statutes and state decisions, although these in turn are applicable as between the property owner and private lienors and as between competing private lienors.

Duration of Lien

As to the duration of the lien, the statute provides:

> "§ 6322. *Period of lien*
>
> Unless another date is specifically fixed by law, the lien imposed by section 6321 *shall arise at the time the assessment is made* and shall continue until the liability for the amount so assessed is satisfied or becomes unenforceable by reason of lapse of time. * * *."[29] (Emphasis added.)

As enacted in the 1954 Code, § 6322 makes an important change from the provisions of its predecessor, § 3671 of the 1939 Code, with respect to the time when the federal lien arises. The 1939 Code provided that "the lien shall arise at the time the assessment list is received by the collector," whereas § 6322 of the 1954 Code states the lien "shall arise at the time the assessment is made."[30]

Secrecy of Lien

The significance of the change made by the 1954 Code concerning the commencement of the lien is especially important to competing lienors who are not protected as a mortgagee, pledgee, purchaser, or judgment creditor under § 6323, hereinafter discussed, because the lien arises from a mere administrative assessment of a tax by an office whose records are not open to public scrutiny. It is truly a secret lien.[31] As to others than the taxpayer, it remains secret from "the time the assessment is made" until a local District Collector removes the veil of secrecy by causing a Notice of Lien to be recorded. Under the 1954 Code, as contrasted with the 1939 Code, there necessarily will be a longer period of time during which many federal liens remain secret after the taxes are assessed and prior to the time the first warning of their existence appears in the public records. That period of secrecy is of great im-

portance to the practitioner who must act and advise his clients with regard to property rights which are subject to federal liens which he cannot find out about but which may be a threat to his client under many different circumstances.

Effect of the Lien as Against Others Than the Taxpayer

Many problems confront the real property lawyer who is called upon to evaluate the legal consequences of the existence of a federal lien for nonpayment of taxes and its effect upon competing private liens and other property interests of third parties which may exist in the delinquent taxpayer's realty. This is true both during the period the federal lien remains secret and the period after public notice is given by the usual method of recording notice.

—Present Statutory Protection to Third Parties

In its present form, the pertinent portion of the general lien statute[32] reads:

> "§ 6323.[33] *Validity against mortgagees, pledgees, purchasers, and judgment creditors*
>
> (a) Invalidity of lien without notice.—Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate—
>
> (1) Under state or territorial laws.—In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or
>
> (2) With clerk of district court.—In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has

not by law designated an office within the State or Territory for the filing of such notice; or

(3) With clerk of district court for District of Columbia.—In the office of the clerk of the United States District Court for the District of Columbia, if the property subject to the lien is situated in the District of Columbia.

(b) Form of notice.[34]—If the notice filed pursuant to subsection (a) (1) is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien. * * *''

—Need for Judicial Determination as to Application of the Statute

As to this statute, two things are obvious:

(1) Liens which compete with federal revenue liens fall into two categories: those which are mentioned in the federal statute and those which are not mentioned in that statute. The statute mentions only four classes of persons as to whom notice is required: mortgagee, pledgee, purchaser, and judgment creditor.[35] In 1950, Mr. Justice Jackson, after reviewing the history of the lien section of the statute, said:[36]

> ''My conclusion from this history is that the statute excludes from the provisions of this secret lien those types of interests which it specifically included in the statute *and no others.*'' (Emphasis added.)

(2) As to any one of the classes of persons the statute seeks to protect, viz., mortgagee, pledgee, purchaser, and judgment creditor, the statute makes no attempt at definition, nor does it contain any specification of the time when or the extent to which given facts fit into the generic terms which the statute uses. There is therefore left for Court

determination the circumstances under which the statute will actually protect one who claims to be a mortgagee, pledgee, purchaser, or judgment creditor.

Interests as to Which the Statute Requires Notice —Mortgages

While § 6323 purports to protect "any mortgagee" by requiring notice, a number of facets of the question as to who is a "mortgagee" and the circumstances under which he will be protected against federal revenue liens have not yet been the subject of Supreme Court consideration.

With respect to mortgages, § 6323 obviously covers only bona fide transactions. A mortgage, found to be fraudulent although valid as between the parties, is not entitled to priority over the United States.[37] However, a mortgagee's knowledge of a mortgagor's tax delinquency does not give the Federal Government a priority against an otherwise valid mortgage.[38] It has been held that a bona fide mortgage made by a wife holding title as grantee under her husband's fraudulent deed, of which the mortgagee had no notice, is entitled to priority over a federal lien which attached to the husband's property after his conveyance.[39]

It has been held that the federal lien will attach to after-acquired property of the taxpayer.[40] What will be its status as against a mortgage which was in existence prior to the federal lien and which by its terms purports to cover after-acquired property of the mortgagor-taxpayer?

—Open-End Mortgages

What is the effect of a revenue lien upon a prior recorded open-end mortgage, before additional advances are made?

It is basic that "a mortgage is security for a debt and without a debt it has no effect as a lien."[41] In the absence of an agreement binding the lender to advance additional moneys, a mortgage to secure future advances can take

effect as a lien only from the time some debt or liability secured by it is created, and the lien is measured by the extent of the debt and the amount which at a given time has been advanced.[42]

On February 6, 1956, the Internal Revenue Service issued a ruling which takes the position that § 6323 affords no protection to lenders under recorded open-end mortgages who make future advances subsequent to the time a notice of a federal lien against the mortgagor is recorded.[43] Analogy is made to the holding in the *Security Trust* case that a state-recognized lien for indebtedness to be determined in the future will not prevail, under the doctrine of relation back, over a subsequently arising federal lien.

Some state statutes purport to protect the continuity of the lien of a mortgage provided the mortgage is recorded and the loan proceeds are disbursed within a given period thereafter.[44] Statutes of this type would seem to offer little protection in the case of the typical open-end mortgage, where notice of a federal lien is recorded after the original mortgage transaction has been concluded and before the making of new advances which are authorized but not required to be made, for (1) they would seem to depend upon the doctrine of relation back, a doctrine so far rejected by the Supreme Court in the tax lien cases, and (2) in any event the Court has consistently held that state statutes cannot interfere with the collection and enforcement of federal taxes.

—Advances Under Construction Loans and Other Recorded Mortgages

Priority has been awarded to a federal revenue lien recorded after a real estate mortgage loan was made but before the deed in trust securing the loan was recorded.[45] But what of the situation where notice of a federal lien is recorded after the security instrument has been executed and before the mortgage loan has been disbursed?

Or what are the relative rights of Government and mortgagee under a building or construction loan where the security instrument has been placed of record but the proceeds of the loan are wholly or partially undisbursed when notice of a federal revenue lien against the mortgagor is recorded?

The theory of the Internal Revenue Service ruling concerning advancements under open-end mortgages may be equally applicable to these cases. That theory may also be applied to any disbursements of the original loan which are made after notice of a federal lien is recorded against the mortgagor. Likewise, the same view may be taken as to advances authorized to be made under a conventional mortgage for the mortgagee's protection in the discharge of subsequent real estate taxes which the mortgagor may fail to pay, or for the making of necessary repairs to the mortgaged premises, or for other obligations of the mortgagor, as well as expenses and fees agreed to be paid in defending litigation affecting the mortgagee's interest, or in foreclosing the mortgage itself.

—Powers of Sale Under Mortgages

The Supreme Court has not passed upon the situation where there is a mortgage which is to be foreclosed under a power of sale rather than by judicial proceedings and a federal lien arises subsequent to the mortgage, but prior to the exercise of the mortgagee's power of sale. Under such circumstances, will the federal lien be cut out by such a sale without notice to the Government? The Sixth Circuit Court of Appeals has held that under these circumstances the federal lien is not cut out.[46] Several decisions have followed that case. A contrary view has been taken by District Courts in Minnesota[47] and Texas.[48] Until the Supreme Court decides the question, it cannot be known whether a real estate mortgage which depends for enforce-

ment upon a power of sale is in the same class with a mechanic's lien, the precarious position of which is hereinafter discussed.

—Purchaser

In its earlier form the predecessor to the present statute failed to include a specific provision as to the effect of a federal lien as against a purchaser for value. Under that statute the Government took the extreme position that an innocent purchaser for value of the realty affected by such a lien had no protection from it even though he had no knowledge or notice of the lien and even though the lien was so secret that it could not be found out about. This contention was upheld by the Supreme Court in *United States* v. *Snyder,* decided in 1893.[49]

After the harsh result of the *Snyder* case,[50] the predecessors of § 6323 were twice amended to grant protection to classes of innocent persons who normally are protected in commercial transactions[51] and a "purchaser" was included as one of the protected categories.

As to who is a purchaser, the Supreme Court lately has said that:

> "A purchaser within the meaning of §3672 usually means one who acquires title for a valuable consideration in the manner of vendor and vendee."[52]

The Court's statement would seem to be limited to cases where (1) the title has been conveyed, and (2) the entire purchase price has been paid. However, that statement leaves untouched many typical situations in which the real estate lawyer may be involved. The simplest of these is the ordinary case of a real estate deal in which the parties enter into a commitment to buy and sell and the purchaser makes a down payment and agrees to pay the remainder of the purchase price within a stipulated time after the title has been demonstrated to be acceptable. If, be-

tween the date as of which the seller's title is examined and the date of the closing of the deal, notice of a federal lien against the seller is recorded, will the contract purchaser at that point be a "purchaser" who has acquired title for a valuable consideration, or will the federal lien prevail as against the property in his hands even though in ignorance and good faith he subsequently paid the full purchase price?

A similar question arises where a person is purchasing realty under an installment contract, with title to be conveyed after a specified number of installment payments had been made, and during the payment period a federal lien is recorded against the property of the seller who is still in title and who has received only part of the purchase installments.

Counsel who represents a purchaser of realty is confronted by a dilemma. Shall he fashion and put into all his title opinions a stock objection by which he excuses himself from liability should a federal lien against the seller, not disclosed by his original examination of the record title, be recorded before his client secures the statutory protection accorded a purchaser, thus leaving his client to take the risk which is involved; shall he demand some protection by requiring proof of payment of the seller's known income taxes and all other ascertained tax liabilities which could result in a lien, in the hope that the deal will be safely closed before notice of some other unpaid tax is recorded; shall he insist that all real estate deals be closed in escrow with the purchase price to be held by the escrowee until after (a) the deed to the purchaser has been recorded and (b) no recorded notice of lien has intervened; or shall he just take a chance and hope that neither he nor his purchasing client will meet disaster?

—Judgment Creditor

One of the classes sought to be protected by § 6323 is "judgment creditor." The answer as to what is meant by the term "judgment creditor" seems deceptively simple. It would seem that a judgment creditor is a creditor who has pursued the ordinary processes of judicial procedure in a court of competent jurisdiction to the point where the court has entered a judgment. Indeed the Supreme Court recently said:

> " * * * we think Congress used the words 'judgment creditor' in § 3672 in the usual conventional sense of a judgment of a court of record."[53]

However, the Treasury Regulation under § 6323 seems to take a different view. It sets up two criteria which must be met by one who claims to be a judgment creditor. He must (1) be "a judgment creditor in a court of record and of competent jurisdiction for the recovery of specifically designated property or for a certain sum of money," and (2) in the case of a judgment for the recovery of a certain sum of money, he also must be one *"who has a perfected lien under such judgment on the property involved."*[54] (Emphasis added.) The Supreme Court has not yet been called upon to decide whether or not the Regulation's requirement of "a perfected lien under such judgment on the property involved" is in accord with a proper construction of § 6323, or is administrative legislation imposing a condition over and above what the Congress intended when it used the term "judgment creditor," and indeed one which it had refused to enact.[55] The language of the Regulation probably is an indication that the Government will contend that as a matter of federal law a judgment creditor, even "in the usual, conventional sense," cannot rely upon a general statutory lien afforded judgments under state statutes, but must have "perfected" that

lien by seizing specific property by execution and levy and possibly by sale before the revenue lien arose.[56]

Leaving aside the necessity of levy and sale to perfect a judgment lien, so far no case before the Supreme Court has involved the problem of the point in time when a judgment becomes final as against a federal revenue lien. Does this occur when the judgment is entered by the trial court? Or does it occur when the trial court subsequently has lost jurisdiction to alter or amend the judgment? Or does it occur when either time for appellate review has expired or final disposition has been made of a pending appeal? Or does it occur at the point of time when under state law the judgment lien arises? Or does it not arise until the judgment lien has been perfected by execution, levy, and sale of the realty which also is affected by the federal lien?

Liens Not Mentioned in the Statute

Purchasers, mortgagees, pledgees, and judgment creditors have such protection as flows from their having been specifically mentioned in § 6323 of the statute. There are a number of other classes of persons who may have liens which compete with federal revenue liens who have not been mentioned in that section and therefore do not have whatever degree of statutory protection is afforded to those who can qualify under § 6323 as a mortgagee, purchaser, or judgment creditor. In this category are mechanic's lien claimants, those claiming vendor's or vendee's liens, or landlord's liens, those having attachment or garnishment liens, and municipalities which have water liens or other liens. Also not specifically mentioned in the statute are states which claim general tax liens under state statutes. Some of these seek to make real estate taxes a lien on realty as of a specified calendar date even though the

amount of the tax, or the elements of the formula for computing the tax, such as tax rate and assessed value, may not be ascertainable until long after the date specified by the state statute.

In a contest solely between a state and the United States, it would appear that the federal lien will prevail.[57]

In a mortgage foreclosure case, taxes due the State of Ohio were secured by liens which were not entitled to priority as against federal revenue liens alone. However, they were given such priority indirectly, by ordering their payment out of the share of sale proceeds allocated to a mortgagee and a judgment creditor, both of whom were entitled to priority over the federal liens under § 3672.[58] This formula recognizes federal law as to the priority of mortgages and judgments over a federal lien and state law as to the priority of state taxes over mortgages and judgments.

In viewing the legal situation of liens which are not mentioned in § 6323, it must be remembered that the United States Supreme Court consistently has given a strict construction to the predecessors of §§ 6321 to 6323. As late as the 1955 term of Court, it has indicated its adherence to the theory of *United States* v. *Snyder* (1893), 149 U. S. 210, and stated that a secret unrecorded federal lien is prior to a competing lien unless the competing claimant clearly comes within one of the preferred classes now designated in § 6323.[59]

—Mechanic's Liens

The attitude of the United States Supreme Court on the question of the effect of federal tax liens upon mechanic's liens may come as a shock to the real estate lawyer who has been brought up on the doctrine that a mechanic or materialman, who contributes labor or materials which

enter into and enhance or create the value of realty, is protected because of his contribution to the extent of the enhancement, against the owner and even as against a prior mortgage on the property. By terse *per curiam* orders in two very recent cases, the Supreme Court has ignored this doctrine and the established philosophy which supports it. In one, the *Colotta* case, the federal lien arose after the work was completed but prior to the recording of the mechanic's lien.[60] In the other, the *White Bear* case, the federal tax lien arose after the mechanic's lien had come into existence, after it had been recorded according to state law, and after a suit to enforce it had been instituted in a state equity court, and that court had acquired jurisdiction of the parties and of the property.[61] Under these circumstances, both the District Court and the Court of Appeals had held that the subsequently arising federal lien was subordinate to the mechanic's lien. Without writing a majority opinion, the Supreme Court, in a single brief order, both granted certiorari and reversed. The Supreme Court apparently saw no need to go further than to find that, as a matter of federal law, so long as a mechanic's lien claim is still in process of litigation to enforce it, so that its existence, validity and amount had not been determined by final decree, it is not choate and perfected to the point where it will have priority over a subsequent federal lien. The only opinion in the case is a dissenting opinion by Justices Douglas and Harlan.[62] It contains a serious warning to the real estate lawyer who represents a mechanic's lien claimant or who is called upon to judge a real estate title which has been affected by a federal tax lien or by a pending equity suit. The dissenting opinion said:

> "The Court apparently holds that under 26 U. S. C. § 3670 a lien that is specific and choate under state

> law, no matter how diligently enforced, can never prevail against a subsequent tax lien, short of reducing the lien to final judgment."

Therefore, under the present statute and these holdings, it must be assumed that at least until final judgment a subsequently arising federal tax lien attaching to the realty is prior to an existing mechanic's lien even though that lien has attained the status of a perfected lien under state law.

Before the Supreme Court spoke on the subject, four federal courts and one state court had refused to uphold the contention that a federal revenue lien takes precedence over a mechanic's lien recorded before the federal lien attached.[63] These cases were decided on the basic theory that priority was controlled by the time of recording a notice of a mechanic's lien in accordance with the state law under which the lien was created, as compared with the time when the federal lien arose. One federal court and two state courts had held that a mechanic's lien is inchoate and not perfected as to a federal lien attaching before the mechanic's lien is recorded.[64] The recent case of *Fleming* v. *Brownfield*[65] in the State of Washington, decided before the *White Bear* case, presents the only full written opinion of any court upholding the Government's contentions of priority over a previously recorded mechanic's lien which was not reduced to judgment before the federal lien attached. The Washington Court noted that the foreclosure decree found due a lesser amount than that stated in the recorded lien claim. It held that, in view of the *Acri, Liverpool,* and *Scovil* cases, the amount of the lien was not certain prior to entry of a decree and, therefore, the mechanic's lien was not choate or perfected in the "federal sense" when the federal lien arose.

This position, of course, disregards any differences between a mechanic's lien, which is a contractual lien under a

state statute,[66] and pure remedial liens, such as attachment and garnishment, which are available in aid of collecting a debt. It also avoids application of "the first in time is the first in right" principle of the *New Britain* case.[67]

Such a result obviously is inequitable to a laborer or materialman who has contributed his services in good faith and enhanced the value of the taxpayer's property only to find that the labor and material he contributed has been confiscated by the Federal Government to satisfy the tax debt due it from the one to whom the labor and materials had been furnished and that the very property the mechanic's lien claimant has created or improved goes to satisfy a tax liability of another, for which the unpaid mechanic's lien claimant had no possible liability. But under the present holdings of the Supreme Court only a change in the federal statute will avoid such a result.[68]

—The Equitable Doctrine of Lis Pendens

The *White Bear* case, which is the last case decided by the Supreme Court, involved another principle of importance to the real estate lawyer, namely, the effect of a federal lien which arises after a state equity court has acquired jurisdiction of the realty to which the lien will attach and of the necessary parties to the litigation.

If the United States acquires a secret lien against any party to the suit either before or after its commencement and is not made a party, what effect, if any, has the final decree on the federal lien? In an equity suit involving title to real estate, including a mortgage or mechanic's lien foreclosure case, "the necessities of mankind" have long been recognized as requiring that *all interests acquired during the pendency of the suit* be bound by the decision of the court in that suit under the familiar rule of *lis pendens*.[69] This principle, which is applicable to all equity suits affecting title to real estate, was not involved in *United States* v.

Security Trust & Savings Bank, where the Court stated that an attachment lien was merely "a *lis pendens* notice that a right to perfect a lien exists."[70] It is regrettable that the Court by refusing to write an opinion in the *White Bear* case failed to give its reasoning as to why the Government was not in the position of anyone else who acquired an interest in the taxpayer's realty during the pendency of the suit. The proposition was urged by counsel, but it was ignored by the Court's order and also by the dissenting opinion.

No federal court of review has yet passed on the application of this well-recognized rule of *lis pendens* to the United States, which acquires a revenue lien after the commencement of an equity suit affecting real estate. Unless the doctrine does apply, federal supremacy may be held to extend to any situation where a state court has jurisdiction of realty in a pending equity proceeding, the federal lien thereafter arises, the Government ignores the state court case, allows it to go to decree, sale and deed without intervention, and then collaterally attacks the decree by seeking to reach the property after it has passed into or through the hands of the purchaser at the judicial sale. Indeed, that was the factual situation in the *White Bear* case.[71]

It is entirely possible that at no time after the commencement of a case will the parties learn of a prior existing secret lien or a subsequently arising federal lien. If the doctrine of *lis pendens* does not apply in such cases, lawyers may be forced to adopt the general procedure of making the United States a party defendant to every equity suit involving the title to real estate, including mortgage foreclosures and mechanic's lien foreclosures, under an allegation that the United States has a secret lien against the premises involved for nonpayment of taxes which have been assessed. Under adverse economic conditions, the

course of making the United States a party defendant to a great number of mortgage foreclosure suits or other equity suits might place an intolerable burden upon the federal officials charged with the collection of taxes and upon the Department of Justice.[72]

In addition, what effect will be had on an equity proceeding affecting title to real estate pending before the recording of a notice of lien, when the suit does not result in any sale or in any person becoming a judgment creditor? In this classification would fall partition suits, the numerous types of proceedings to quiet title or to remove clouds, and suits to construe, cancel or modify a contract, lease, deed, option, will or trust agreement.

—Municipal Liens

In *United States* v. *New Britain*,[73] municipal real estate tax and water rent liens were before the Court. The fund in which both federal tax liens and these competing liens sought prior rights arose from a foreclosure sale under a real estate mortgage. Some of the municipal liens arose before the revenue liens, and some arose after. The Supreme Court of Connecticut had sustained the City of New Britain's claim of complete priority under a Connecticut statute. On the other hand, the Government contended for complete priority over the earlier municipal liens because they were not specific, choate or perfected prior to the time the federal liens arose.[74] It also contended for an application of § 3466 requirements to that case, although the taxpayer was not insolvent. In reversing and remanding the case, the Supreme Court found that the earlier municipal liens were specific in that "they attached to specific pieces of real estate" and that they were "perfected in the sense that there is nothing more to be done to have a choate lien—when the identity of the lienor, the

property subject to the lien, and the amount of the lien are established." It further held that § 3670 (now § 6321) does not confer any priority upon federal liens.

The Government relied heavily on prior decisions in the *Gilbert Associates* case under § 3466[75] and the *Security Trust* case.[76] However, the Court stated, "We do not think they are inconsistent with our decision in this case." Further distinguishing the *Gilbert Associates* case, the Court stated (page 87):

> "* * * But the question we have here did not arise there because that was a case involving personal property and insolvency of the taxpayer. * * *
>
> * * * * *
>
> "Here the contest is between two groups of statutory liens, one specific and one general, attached to the same real estate, with no question of insolvency involved; therefore, 'the first in time is the first in right.'"

—Attachment

Two cases have involved the supremacy of federal tax liens over earlier attachment liens. In *United States* v. *Security Trust & Savings Bank,*[77] Morrison filed a suit against Styliano on an unsecured note and procured an attachment lien on four parcels of the latter's real estate. Subsequently, federal revenue liens arose against Styliano and were recorded; thereafter, Morrison recovered a judgment. Under applicable California law, the rights of the judgment creditor related back to the date of the attachment lien. However, the federal lien was given priority. The Supreme Court found that, prior to judgment, the attachment lien was "contingent or inchoate—merely a *lis pendens* notice that a right to perfect a lien exists" and that the state rule of "relation back" could not "operate to destroy the realities of the situation." The opinion states that under § 3466, "it has never been held sufficient

to defeat the federal priority merely to show a lien effective to protect the lienor against others than the Government, but contingent upon taking subsequent steps for enforcing it." From this, the Court concluded that "to insure prompt and certain collection of taxes," it was necessary that a similar rule must prevail under § 3670.

The *Security Trust* case was adhered to in 1955, under a like chronology of events in *United States* v. *Acri*.[78] The *Acri* case involved an attachment lien on personal property ancillary to a suit for wrongful death.

—Garnishment

The same result was reached in *United States* v. *Liverpool & London Insurance Co.*,[79] which involved a garnishment lien on personal property ancillary to a suit on an open account. In this case also, the priority of the federal lien was sustained on the ground that the competing lien was inchoate at the time the federal lien attached, in that the precise amount of the garnishment lien was dependent on the outcome of the principal suit.[80]

—Landlord's Lien

In *United States* v. *Scovil*,[81] a landlord's lien on personal property, filed April 7, 1952, was held not perfected in the "federal sense" to be entitled to priority over federal liens which attached before that date although notice of the federal liens was not recorded until after that date. Again, the Court relied on § 3466 cases, but specifically found "it unnecessary to pass on the effect of that section." The decisions leave unsolved the question of priority when a distraint and attachment is levied prior to the existence of a federal lien, but the landlord has not reduced his claim to judgment.

The General Principles Applicable to Competing Private Liens

From the statute and the decisions of the United States Supreme Court in the cases hereinbefore mentioned, it seems clear that the general practitioner must assume that:

(1) Nonpayment of federal taxes will result in a federal revenue lien upon all of the property of a delinquent taxpayer.

(2) The federal lien now takes effect from the date of assessment of the tax.

(3) At first, the lien is a secret lien. For some time, the facts concerning assessment, amount of tax, and nonpayment are not readily available to any third person.

(4) A recorded notice of the existence of a federal lien is not required to establish priority for the federal lien, except as to the four categories of persons specifically mentioned in § 6323, viz., purchaser, mortgagee, pledgee, and judgment creditor.

(5) If the federal lien antedates a competing private lien, the federal lien will prevail, absent the protection to a purchaser, mortgagee, pledgee, or judgment creditor given by § 6323 (§ 3672 of the 1939 Code).

(6) Even when a competing lien antedates the federal lien, nevertheless the federal lien will prevail, unless the competing lien meets federal standards of being "choate," "specific" and "perfected."

(7) A competing private lien of a type which is not mentioned in the federal statute, but which is specific and choate under state law, while it is in process of judicial enforcement, cannot prevail as against a *subsequently arising* federal tax lien, unless the competing prior lien has at least reached the stage of a final judgment by a

court of competent jurisdiction before the tax lien came into existence.

(8) It is not safe to assume that the well-established doctrine of *lis pendens* will bind the United States to a decree entered in an equity suit which was pending when the Government's lien came into existence.

How Did the Law Get That Way?

The present state of the law has been achieved in part, not by legislation, but by the Government's success in persuading the Supreme Court to apply and extend one or more of the following principles:

(1) The question of the relative priority between competing liens always is a federal question.

(2) To be entitled to priority over the federal lien, a competing lien must be specific, choate and perfected at the time a federal lien arises. This concept originated in § 3466 cases in which a state or county tax was (1) either not even a lien under state law or (2) the lien arose at a specified date prior to the federal lien, but *no amount* of such tax had been assessed, ascertained or put in collection before the federal lien arose. This concept has been extended to situations where a private lien of record states a definite amount before the federal lien arose.

(3) The doctrine of relation back, recognized under state law, will not apply to defeat the priority of a federal lien. This concept originated in the same factual situations as the immediately preceding item.

(4) A state law cannot interfere with the enforcement of a federal revenue lien. This concept is based primarily on the *Snyder* case, which involved the single question of the effect of a state recording statute on a federal lien. It would seem to be one thing to apply the doctrine that a state law cannot interfere with the collection of federal

taxes to a situation where a state statute is invoked to prevent the federal lien from reaching property in which the delinquent taxpayer retains the ownership and enjoyment, such as a limitation law, a homestead law, a recording law, or the protection afforded the beneficiary of a spendthrift trust. It is quite another thing to extend the application of that doctrine to give the Government an interest in the taxpayer's property greater than the taxpayer himself possessed.

II

§ 3466 OF THE REVISED STATUTES

The Priority Statute

The United States enjoys a special statutory priority in situations where the delinquent taxpayer is insolvent,[82] is deceased, or an act of bankruptcy exists with respect to his property. This statutory provision is necessary to give the federal revenues priority because the common law priority of debts due a sovereign is not applicable to the United States, there being no federal common law, and the Federal Government being one of delegated powers.[83]

Such statutory grant of priority has existed in one form or another since 1797.[84] Presently, the effective provision is found in § 3466 of the Revised Statutes, which, like its predecessors, does not purport to create a lien, but merely to provide a federal priority in the proceeds on the liquidation of a taxpayer's property. It reads as follows:

> "Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor, not having

> sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed."[85]

Federal taxes are included within the wording "debts due to the United States"[86] used in § 3466, although a distinction between "taxes" and "debts" due the United States is made in § 64 (a) of the Bankruptcy Act.[87] § 3466 has been held inapplicable to bankruptcy proceedings.[88] The earlier cases held that this priority did not displace an antecedent lien.[89]

Requirement That Competing Lien Be Specific and Perfected

In 1929, the Supreme Court injected into the law the doctrine that the antecedent lien must be specific and perfected before it is in a position to contest the federal priority under § 3466.[90] This doctrine has been followed to the present time. The Supreme Court never has found that a competing lien in fact met the federal requirements of a specific and perfected lien so as to require a decision of whether such a lien actually defeats the federal priority. However, one Court of Appeals has met the issue squarely and sustained the priority of a county tax lien certificate over a subsequent federal lien.[91]

Requirements as to Title and Possession

The Federal Government has been eminently successful in maintaining its priority under § 3466. *United States* v. *Gilbert Associates*[92] reiterated the rule that, notwithstanding the absence of any such statutory requirement, a lien to be entitled to priority over a federal lien must not only meet the usual tests of specificity and perfection, but also

the lienor must reduce the property to possession and divest the taxpayer of title as well.

That case involved a conflict concerning the priority of tax liens of a town in New Hampshire and the United States. The fund was the proceeds of a receiver's sale of machinery formerly owned by an insolvent corporation. Under New Hampshire law, machinery is considered real estate for tax purposes, although generally understood to be personal property.[93] The town had bid the property in at two prior tax sales, but had never taken possession of the machinery. Both tax sales were held after notice of the federal lien had been recorded. The federal lien prevailed because the town tax was only a general unperfected lien and "the taxpayer had not been divested by the Town of either title or possession."[94]

In a law review article, it has been aptly stated:

> "To speak of a lienor with title is of course to utter a legal solecism; but the incongruities of the doctrine of the inchoate and general lien have never been a handicap to its development."[95]

While the requirements of title and possession are to be found in cases dealing with personal property, language appearing in *United States* v. *Texas*[96] should serve as a warning that it may not be so limited in a future case involving real property. In the *Texas* case, the Court stated that § 3466 created no exceptions to the Government's absolute priority. Conceding that early cases read an exception into the section in case of previously executed mortgages, the Court followed by saying (pages 484 and 485):

> "This doctrine seems to have been based on the theory that mortgaged property passes to the mortgagee. The question of whether the priority of the United States under § 3466 would also be defeated by a specific and perfected lien upon property whose title re-

> mained in the debtor was reserved in those cases * * * a general judgment lien on the lands of an insolvent debtor does not take precedence over claims of the United States unless execution of the judgment has proceeded far enough to take the land out of the possession of the debtor."

A similar warning to lawyers in states whose mortgage laws declare the mortgagee's interest is a lien and not title to real estate is given in *New York* v. *Maclay*,[97] where it is stated:

> "We do not now determine whether the holding in the mortgage cases is to be applied in jurisdictions where a mortgage upon real estate is a lien and nothing more * * *."

A landlord's lien, under a 1937 lease, was held subordinate to federal liens when the landlord levied a distress warrant and attachment on the lessee's personal property on July 1, 1941, twelve days after the lessee executed a general deed of assignment to a trustee for the benefit of creditors.[98] The assignment gave an immediate priority to the United States under § 3466, at which time the landlord had no specific lien for a definitely ascertained amount, and "the tenant was divested of neither title nor possession" of the property.

State Taxes

States, seeking to collect their own revenues, have felt the might of the Federal Government with claims against the same delinquent and insolvent taxpayer.[99] In each instance, the general lien of the United States was given priority over the state's lien because the latter was a general lien and not a specific lien against particular property, or because the precise amount of the state lien had not been determined judicially before the federal lien at-

tached. Collection of revenue is equally important to the continued existence of a state government, yet both equality and priority are denied the state on the ground of federal supremacy.

While sustaining the supremacy of a federal claim as against a state claim, the Supreme Court has conceded, "Nor would the Federal Treasury have been rendered bankrupt by a contrary result."[100]

III

BANKRUPTCY ACT PROVISIONS

Nonfederal liens fare much better under the Bankruptcy Act than they do under § 3466. In a bankruptcy case, the contest over priority does not necessarily result in favor of the Federal Government, for, when regular bankruptcy proceedings are involved, the United States does not enjoy an absolute statutory priority as is provided in § 3466. This is true even though the actual financial status of the delinquent taxpayer is the same, the presence or absence of a pending bankruptcy proceeding being the determinative factor as to which statutory provision controls. There has been considerable discussion to the effect that the true congressional intent is expressed in the Bankruptcy Act, not as the Supreme Court has interpreted § 3466 by engrafting additional requirements on nonfederal liens before they can prevail over a federal lien.[101]

Ordinary Bankrupts

§ 64 (a) of the Bankruptcy Act[102] gives the United States a priority over certain unsecured claims, but does not give it priority over valid liens. However, if the § 3466 priority has attached previously, it is not lost by the subsequent bankruptcy of the taxpayer.[103]

In *United States Fidelity and Guaranty Co.* v. *Sweeney*,[104] the Court awarded priority to an equitable lien and held:

> "The government must look to the Bankruptcy Act * * * and not to section [3466] * * * Taxes due the government are, of course, entitled to priority of payment in the administration of the estate of a bankrupt, but the priority which the Bankruptcy Act creates is in the assets of the bankrupt's estate, and it does not give priority over valid liens. *Richmond* v. *Bird*, 249 U. S. 174, 39 S. Ct. 186, 63 L. Ed. 543; *City of Tampa* v. *Commercial Bldg. Co.* (CCA 5), 54 F. (2) 1057."

In addition to recognizing valid pre-existing liens, § 67 (b) of the Bankruptcy Act permits the perfection of liens after the debtor becomes insolvent and during the bankruptcy proceedings.[105] Furthermore, bona fide lienors are protected even though the lien is fraudulent as to other creditors of the debtor, and such lienor is protected to the extent of his debt, which may be less than a fair consideration for the property subject to the lien.[106]

When a sale free and clear of liens is had in bankruptcy proceedings, existing liens attach to the sale proceeds. Such sale cannot prejudice a lienor or impair any substantive right.[107]

Mortgage liens are not displaced by federal liens when the controversy over relative priority of liens takes place in an ordinary bankruptcy proceeding.[108] A mortgage lien was found prior under the following chronological order of events: (a) federal lien arose, (b) mortgage executed and recorded, (c) federal lien recorded, and (d) involuntary petition in bankruptcy filed.[109] More clearly a mortgage, executed and recorded before a federal lien arose, is entitled to priority,[110] yet the Government litigated that issue to the Court of Appeals.

A mechanic's lien was protected against the Government's assertion of priority by application of the doctrine

of relation back, the statutory right to perfect a lien after bankruptcy and by recognizing the enhancement of value of the property.[111] There the lien claimant filed his affidavit of claim on November 20, 1946, thus perfecting his lien after performing his contract. Federal tax liens arose on and subsequent to August 14, 1946. On November 8, 1946, the Government recorded notice of its tax claims a few hours before the filing of a proceeding in a bankruptcy court. On the contrary, if a mechanic's lien claimant does not have a perfected lien, the federal lien will prevail.[112]

A judgment lien was held entitled to priority over a subsequent federal tax lien even though the levy under it was not made until within four months of bankruptcy.[113]

Claims of the United States have been held subordinate to state tax liens which attached under state law before the bankruptcy proceedings, but the exact amount of the state claim was not ascertained until afterwards.[114]

Special Bankruptcy Proceedings

As to other types of proceedings in bankruptcy, separate statutory provisions are to be considered on the question of relative priorities. While existing liens are said not to be disturbed, provision for payment of federal taxes must be made before the confirmation of any plan for composition, extension, arrangement or reorganization. Under Chapter 8, a farmer's composition or extension proposal may not "reduce the amount of or impair the lien of any secured creditor below the fair and reasonable market value of the property securing any such lien."[115] Yet any such proposal to be confirmed must accord priority of payment to debts having priority under § 64 (a) of the Bankruptcy Act,[116] such as federal taxes. Priority of payment favors the United States in Wage Earners' Plans

under Chapter 13, although the chapter purports to preserve creditor's rights as in ordinary bankruptcy.[117]

In Arrangements under Chapter 11 to affect unsecured debts, the rights of all claimants are said to be generally the same as if an ordinary bankruptcy proceeding were involved.[118] However, before a proposed arrangement can be confirmed, deposits must have been made to pay all debts which have priority unless the priority claimants have waived such rights.[119] Thus a federal revenue lien may be subordinate to another lien but be in a position to require payment before a taxpayer's arrangement can be confirmed.

Many tax delinquencies may arise out of the difficulties of financially embarrassed corporations or large property owners. Litigation as to priority of liens does not develop when such parties adjust their affairs in a bankruptcy court to permit continuation of their operations. Whenever such a delinquent taxpayer seeks the aid of a bankruptcy court to effect a Railroad Reorganization under Chapter 8, a Corporate Reorganization under Chapter 10, or a Real Property Arrangement under Chapter 12, in each instance full payment to the United States or its consent to accept a lesser sum is a statutory prerequisite to a confirmation of the plan.[120]

FOOTNOTES

[1] The more commonly encountered federal taxes, nonpayment of which may result in a federal tax lien, include the following: income taxes, withholding taxes on wages, estate and gift taxes, employment taxes under the Federal Insurance Contributions Act, the Railroad Retirement Tax Act and the Federal Unemployment Tax Act, retailers' excise taxes, manufacturers' excise taxes, a wide variety of miscellaneous excise taxes, taxes on alcohol, tobacco and other items.

[2] Treasury Bulletin, January 1956, United States Treasury Department, p. 2, "Table 1—Receipts by Principal Sources."

[3] *Ibid.*

[4] "Federal Liens" (April 1927), 33 W. Va. L. Q. 240.
"The Tax Lien of the United States" (October 1927), 13 Am. Bar Assn. Journal 576.
"The Differences in the Priority of the United States in Bankruptcy and in Equity Receiverships" (1929), 43 Harv. L. R. 251.
"Federal Tax Liens" (1936), 105 A. L. R. 1244 and (1948), 174 A. L. R. 1373.
"Federal Liens" (January 1940), 14 Univ. of Cinn. L. R. 1.
"Federal Tax Liens and Their Enforcement" (January 1947), 33 Va. L. R. 13.
"Correlation of Priority and Lien Rights in the Collection of Federal Taxes" (June 1947), 95 Univ. of Pa. L. R. 739.
"Federal Claims Priority Statute Versus the Specific and Perfected Lien" (March 1951), 20 Univ. of Cinn. L. R. 274.
"Statutory Liens Under Sec. 67c of the Bankruptcy Act" (June 1953), 62 Yale L. J. 1131.
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"The Relative Priority of the Federal Government" etc. (May 1954), 63 Yale L. J. 905.
"The Correlation of Liens and Priorities" (July 1954), 28 Referee's Journal 104.
"Recent Developments in the Field of Federal Tax Claims" (January 1955), 29 Referee's Journal 7.
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"The Unsolved Problems in Priority for Federal Tax Claims" (Summer 1955), 30 Ind. L. J. 476.
"Effect of Federal Tax Liens on Ohio Real Property" (Winter 1955), 16 Ohio St. L. J. 92.
"Priority of a Subsequent Federal Tax Lien Over an Antecedent Inchoate Lien" (April 1956), 54 Mich. L. R. 829.
"Priority as Between the Federal Tax Lien and the Mechanic's Lien" (Spring 1956), 25 Fordham L. R. 100.
"Priority of Advances Under Open-End Mortgages," 24 George Washington Law Review 725 (June 1956).

[5] "Federal Tax Liens and Their Enforcement" (1947), Institute on Federal Taxation, Fifth Annual, New York University, 185.
"Tax Liens, Their Operation and Effect" (1951), Institute on Federal Taxation, Ninth Annual, New York University, 563.
9 Mertens, Law of Federal Income Taxation, §§ 54.10, *et seq.*
2 Prentice-Hall Federal Tax Service (1956), Pars. 19,909 and 19,910.
4 C. C. H. Standard Federal Tax Reporter (1956), Pars. 5362, *et seq.*

[6] "Status of Liens on Real Estate in Bankruptcy" (June 1955), 34 Title News 7.
"Federal Tax Liens" (November 1955), 34 Title News 62.

[7] 64 Am. Bar Assn. Report 474 and 1939 Proceedings, Section of Real Property, Probate and Trust Law, 95 (for paper presented see "Federal Liens," 14 Univ. of Cinn. L. R. 1, footnote 8).

The Association's prolonged effort secured the enactment in 1913 of the ancestor of present § 6323 protecting purchasers, mortgagees and judgment creditors from an unrecorded revenue lien (1898), 21 Am. Bar Assn. Report 108, 261; (1899) 22 Am. Bar Assn. Report 487; (1900) 23 Am. Bar Assn. Report 411; (1902) 25 Am. Bar Assn. Report 497; (1905) 28 Am. Bar Assn. Report 525; (1906) 29 Am. Bar Assn. Report 598; (1912) 37 Am. Bar Assn. Report 569; (1913) 38 Am. Bar Assn. Report 618. Later the Association was active in securing the enactment of the statute (28 U. S. C. A. § 2410) permitting the United States to be made a defendant in a suit seeking to remove its liens from real estate (1930), 55 Am. Bar Assn. Report 519.

Report of Am. Bar Assn. Section of Real Property, Probate and Trust Law, Committee on Relative Priority of Government and Private Liens, Section Proceedings 1956.

[8] Constitution of the United States, Article I, Section 8.

[9] *Murray's Lessee* v. *Hoboken Land Co.* (1855), 18 How. (59 U. S.) 272, 281 (quoted in *United States* v. *Snyder* (1893), 149 U. S. 210, 215). The Court also said, p. 282:

> "* * * probably there are few governments which do or can permit their claims for public taxes, either on the citizen or the officer employed for their collection or disbursement, to become subjects of judicial controversy according to the course of the law of the land. Imperative necessity has forced a distinction between such claims and all others, which has sometimes been carried out by summary methods of proceeding, and sometimes by systems of fines and penalties, but always in some way observed and yielded to."

[10] *United States* v. *Snyder* (1893), 149 U. S. 210, 214.

[11] *United States* v. *Acri* (1955), 348 U. S. 211, 213; *United States* v. *Gilbert Associates* (1953), 345 U. S. 361, 363; *United States* v. *Security Trust & Savings Bank* (1950), 340 U. S. 47, 49.

[12] "The federal priority is not destroyed by state recording acts * * *." *Illinois* v. *Campbell* (1946), 329 U. S. 362, 375; *United States* v. *New Britain* (1954), 347 U. S. 81, 84; *United States* v. *Snyder* (1893), 149 U. S. 210.

[13] 26 U. S. C. A., Chapter 64, Collection, Subchapter C—Lien for Taxes, §§ 6321-6323.

[14] 31 U. S. C. A. § 191.

[15] The special liens for distilled spirits taxes (26 U. S. C. A. §§ 5004, 5177 (b) (1 to 4) and 5194 (f)) and for estate and gift taxes (26 U. S. C. A. § 6324) are not considered in this report.

[16] In the 1939 Internal Revenue Code, the predecessor of § 6321 was § 3670, of § 6322 was § 3671, and of § 6323 was § 3672. It is reiterated that it is under those numbers that the applicable sections have been discussed in the cases reported before the 1954 Code became effective.

[17] Provisions similar to those now found in § 6321 have been included in federal revenue acts since 1866. See Historical Note, 26 U. S. C. A. § 6321 at page 437.

[18] In *United States* v. *New Britain* (1954), 347 U. S. 81, 84-85, the Court said:

> "* * * the federal statutes do not attempt to give priority in all cases to liens created under the paramount authority of the United States. The statute creating the federal liens here involved, I. R. C., § 3670, does not in terms confer priority upon them."

[19] *United States* v. *City of Greenville* (C. A. 4th—1941), 118 F. 2d 963, 965; *Welsh* v. *United States* (C. A. Dist. of Col.—1955), 220 F. 2d 200, 203.

[20] *Citizens National Trust & Savings Bank* v. *United States* (9th—1943), 135 F. 2d 527, 528.

[21] *Metropolitan Life Ins. Co.* v. *United States* (6th—1939), 107 F. 2d 311, cert. denied 310 U. S. 630.

[22] *United States* v. *Kaufman* (1925), 267 U. S. 408, 414. A revenue lien arising after a taxpayer's death does not attach to his wife's dower interest in real estate. *United States* v. *Ettelson* (Wisc.—1946), 67 F. Supp. 257, reversed on other grounds (7th—1947), 159 F. 2d 193.

[23] *Mansfield* v. *Excelsior Refining Co.* (1890), 135 U. S. 326; *United States* v. *Hutcherson* (8th—1951), 188 F. 2d 326; *United States* v. *Winnett* (9th—1947), 165 F. 2d 149; *Citizen's State Bank* v. *Vidal* (10th—1940), 114 F. 2d 380.

[24] *United States* v. *Acri* (1955), 348 U. S. 211, 213. However in the earlier case of *Tyler* v. *United States* (1930), 281 U. S. 497, 501, the Supreme Court said with reference to state decisions as to tenancies by the entirety, "These decisions establish a state rule of property, by which, of course, this court is bound."

In *United States* v. *Snyder* (1893), 149 U. S. 210, 213, the Court said:

> "The single question thus presented for our consideration is whether the tax system of the United States is subject to the recording laws of the States."

In holding that the taxing power of the Federal Government could not be limited or circumscribed by state law, the Court said (page 214):

> "* * * If the United States, proceeding in one of their own courts, in the collection of a tax admitted to be legitimate, can be thwarted by the plea of a state statute prescribing that such a tax must be assessed and recorded under state regulation, and limiting the time within which such tax shall be a lien, it would follow that the potential existence of the government of the United States is at the mercy of state legislation."

[25] See § 6323, *post*, as to mortgagee, pledgee, purchaser, and judgment creditor.

[26] *United States* v. *Scovil* (1955), 348 U. S. 218.

[27] *United States* v. *White Bear Brewing Co.* (1956), 350 U. S. 1010, reversing 227 F. 2d 359 (7th Cir.); rehearing denied May 28, 1956, 351 U. S. 958, 76 S. Ct. 845.

[28] § 6339 (b) (2) of the 1954 Code, formerly § 3704 (c) (2) of the 1939 Code.

[29] See Reg. § 301.6321-1 (T. D. 6119); the "lapse of time" mentioned in § 6322 is referable to six years after assessment, in the absence of a waiver, as provided in § 6502. Federal claims are not barred by a state's statute of limitation. *United States* v. *Summerlin* (1940), 310 U. S. 414, 416.

[30] For mechanics of assessment see 26 U. S. C. A., Chapter 63, Assessment, §§ 6201-6206; Reg. § 301.6203-1.

[31] See 26 U. S. C. A. § 6103, as to "Publicity of returns and lists of taxpayers (a) Public records and inspection." Also see 26 U. S. C. A. § 7213, which makes unauthorized disclosure a misdemeanor. See also 165 A. L. R. 1302, 1355 and 1358.

[32] Subsection (c) dealing with "securities" and subsection (d) of § 6323 are omitted as not pertinent to this report.

[33] Internal Revenue Code of 1954 (26 U. S. C. A.) § 6323. See Reg. § 301.6323-1 (T. D. 6119).

[34] Subsection (b) is new in that it overcomes any state recording law requirements that the Notice must contain a legal description of property sought to be affected.

[35] Of interest are two of the proposals to strengthen the hand of the tax collector which were made for inclusion in the Revenue Code of 1954. Each would have overcome existing decisions adverse to the Government. Both proposals were in H. R. 8300 (83rd Congress, 2d Session), introduced in the House of Representatives, but were omitted from the Revenue Code of 1954, as finally enacted. One was to include a taxpayer's interest as tenant by the entirety as property to which the federal lien would attach. The second would have nullified the protection afforded a mortgagee, pledgee, purchaser, or judgment creditor against unrecorded tax liens by § 3672 of the 1939 Code if such party had notice or knowledge that tax delinquencies existed against the person with whom he was dealing. Apparently the fatal notice could have been either actual or constructive, thus placing a tremendous burden on anyone claiming adverse to the Government. The second proposal also would have required that the lien of a judgment be "perfected" previously against specific property. The provisions as to notice and perfection of judgment liens were to take the form of a new subsection to be added to existing § 3672 and to read as follows:

> "(c) LIEN VALID WITHOUT NOTICE IN CERTAIN CASES.—The lien imposed by section 6321 shall be valid, without the filing of notice thereof, as against any mortgagee, pledgee, purchaser, or judgment creditor, if—
>
> (1) in the case of a mortgage, pledge, or purchase, such mortgagee, pledgee, or purchaser had notice or knowledge of the existence of such lien at the time the mortgage, pledge, or purchase, was made, or
>
> (2) in the case of a judgment creditor, the creditor has not obtained a valid judgment in a court of record and of competent jurisdiction for the recovery of specifically designated property or for a certain sum of money, or
>
> (3) in the case of a judgment creditor who has a valid judgment of a court of record and of competent jurisdiction for the recovery of a certain sum of money, no lien with respect to the property involved has been perfected under such judgment."

[36] Concurring opinion in *United States v. Security Trust & Savings Bank* (1950), 340 U. S. 47, 53.

[37] *Hart* v. *United States* (8th—1953), 207 F. 2d 813, cert. denied 347 U. S. 919.

[38] *United States* v. *Beaver Run Coal Co.* (3rd—1938), 99 F. 2d 610.

[39] *United States* v. *Fidelity & Deposit Co.* (5th—1954), 214 F. 2d 565.

[40] *Glass City Bank* v. *United States* (1945), 326 U. S. 265.

[41] *Freutel* v. *Schmitz* (1921), 299 Ill. 320, 323, 132 N. E. 534.

[42] *Ibid.*

[43] Revenue Ruling 56-41; Internal Revenue Bulletin, 1956-6, 15. See 24 Geo. Washington Law Review 725 (June, 1956).

This refusal to recognize future advances may affect the guarantee liability of the Federal Housing Administration on guaranteed mortgages. See 12 U. S. C. A. § 1709 d, § 1710(a), § 1713(a)(1) and § 1715(p). As to Military Housing Insurance Fund see 12 U. S. C. A. § 1748 b(a) and § 1748 b (d), as to the War Housing Insurance Fund see 12 U. S. C. A. § 1738, 1739(a), 1743(c) and 1746(b)(2), and as to the National Defense Housing Insurance Fund see 12 U. S. C. A. § 1750 c(a).

[44] For example, Ill. Rev. Stat., Chap. 30, Par. 37a.

[45] *Underwood* v. *United States* (5th—1941), 118 F. 2d 760.

[46] *Metropolitan Life Ins. Co.* v. *United States* (6th—1939), 107 F. 2d 311, cert. denied 310 U. S. 630. As between private persons, an exercise of

a power of sale cuts out a subsequent attaching creditor (*Jackson* v. *Lawrence* [1886], 117 U. S. 679) and a subsequent purchaser from the mortgagor who received no notice of the sale (*Scott* v. *Paisley* [1926], 271 U. S. 632).

47 *United States* v. *Ryan* (D. C. Minn.—1954), 124 F. Supp. 1, 33 Texas L. R. 761 (May 1955).

48 *Trust Co. of Texas* v. *United States* (D. C. Tex.—1933), 3 F. Supp. 683.

49 *United States* v. *Snyder* (1893), 149 U. S. 210. In *United States* v. *Security Trust & Savings Bank* (1950), 340 U. S. 47, 52, Mr. Justice Jackson, in a concurring opinion, said:

> "*United States* v. *Snyder*, 149 U. S. 210 (1893), was decided at a time when the forerunner of the present statute, § 3186 of the Revised Statutes as amended by § 3 of the Act of March 1, 1879, provided:
>
> " '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 from the time when the assessment-list was received by the collector, except when otherwise provided, until paid, with the interest, penalties, and costs that may accrue in addition thereto, upon all property and rights to property belonging to such person.' 20 Stat. 327, 331.
>
> "The *Snyder* case held, in interpreting the above statute along with Art. I, § 8 of the Constitution, that the lien created by that statute was a valid binding lien even against a bona fide purchaser for value without knowledge or notice of the existence of such a lien."

50 So termed in *United States* v. *Gilbert Associates* (1953), 345 U. S. 361, where the Court said, page 364:

> "Congress enacted § 3672 to meet the harsh condition created by the holding in *United States* v. *Snyder*, 149 U. S. 210, when federal liens were few, that a secret federal tax lien was good against a purchaser for value without notice."

See also *Blacklock* v. *United States* (1908), 208 U. S. 75, as to a subsequent mortgagee.

51 The concurring opinion of Mr. Justice Jackson in the *Security Trust & Savings Bank* case, note 49, *ante*, says concerning these amendments:

> "Thereafter the statute was amended and a proviso added which said: '. . . That such lien shall not be valid as against any mortgagee, purchaser, or judgment creditor until notice of such lien shall be filed by the collector . . .' in the appropriate place for filing. 37 Stat. 1016. The House Report accompanying the proposed amendment, H. R. Rep. No. 1018, 62 Cong., 2d Sess. 2 (1912), said in part, after citing the above case:
>
> "'. . . the lien is so comprehensive that it covers all the property and rights to property of the delinquent situated anywhere in the United States, and any person taking title to real estate is subjected to the impossible task of ascertaining whether any person, who has at any time owned the real estate in question, has been delinquent in the payment of the taxes referred to while the owner of the real estate in question. The business carried on under the internal-revenue law may be at a great distance from the property affected by this secret lien, but this will not relieve the property from the lien.'
>
> "In 1938, *United States* v. *Rosenfield*, 26 F. Supp. 433 (D. C. E. D. Mich., S. D.), held that a bona fide purchaser for value of shares of stock from a seller against whom notice of lien for federal income taxes had been duly filed prior to the sale, took subject to the lien even though the purchaser did not have notice or knowledge of such lien. As a direct result of this decision, the statute was again amended, this time to include *pledgees* and the exception in case of securities as now found in 26 U. S. C. § 3672 (b)(1). The reason for this amendment is disclosed in the Committee Report accompanying the Revenue Bill of 1939. H. R. Rep. No. 855, 76th Cong., 1st Sess. 26 (1939). This report says, in part:
>
> "'. . . While it is true that the filing of the notice of the tax lien

may constitute notice in the case of real property, it is inequitable for the statute to provide that it constitutes notice as regards securities. . . . An attempt to enforce such liens on recorded notice would in many cases impair the negotiability of securities and seriously interfere with business transactions. . . .'"

52 *United States* v. *Scovil* (1955), 348 U. S. 218, 221. See also *National Refining Co.* v. *United States* (8th—1947), 160 F. 2d 951, 955.

53 *United States* v. *Gilbert Associates* (1953), 345 U. S. 361, 364. A more liberal interpretation is found in the dissenting opinion (p. 367) and *In re Northwest Products Co.* (7th—1948), 168 F. 2d 639.

54 Reg. § 301.6323-1 (T. D. 6119). See *Miller* v. *Bank of America, N. T. & S. A.* (9th—1948), 166 F. 2d 415, which holds that to compete with a federal tax lien, the mere entry of a judgment is insufficient. The judgment must be a lien on the property involved.

55 It is to be noted that the language of the Regulation is the same as the language of proposed § 3672 (c)(3) of H. R. 8300, shown at note 35, *ante*, which the Congress failed to enact as part of the Internal Revenue Code of 1954.

56 In *United States* v. *Texas* (1941), 314 U. S. 480, 486, 487, it was said: A state statute giving a general lien does not "by its own force create[s] a specific and perfected lien" in that the debtor's property "is neither specific nor constant." And in *Illinois* v. *Campbell* (1946), 329 U. S. 362, 374, the Court held that to perfect a lien there must be "a final assertion or attachment of rights to specific property, as is, for example, the enforcement of a judgment by execution and levy. *Conard* v. *Atlantic Ins. Co.*, 1 Pet. 386, 443-444." See also note 97, *post*.

57 *New York* v. *Maclay* (1933), 288 U. S. 290, 292-293.

58 *Southern Ohio Savings Bank & Trust Co.* v. *Bolce* (May 1956), 165 Ohio St. 201, 135 N. E. 2d 382. The formula (previously applied as to a mortgage, mechanic's lien and federal lien in *Samms* v. *Chicago Title and Trust Co.*, mentioned in footnote 64) penalizes the mortgagee and judgment creditor who are the very ones § 6323 seeks to protect. The share of proceeds allocated to their prior interests would never exceed the full amount due them. Therefore, they cannot receive full payment if given a subordinate position as to that share. It will be interesting to see how a court will apply the formula in a situation where the property or its proceeds is sufficient to pay in full the mortgage and a judgment creditor but only a portion of such a state tax or mechanic's lien. In any event, "the United States is not interested in whether the State receives its taxes * * * prior to the mortgagees and judgment creditors." *United States* v. *New Britain* (1954), 347 U. S. 81, 88.

59 *United States* v. *Scovil* (1955), 348 U. S. 218, 221; *United States* v. *Gilbert Associates* (1953), 345 U. S. 361, 364.

60 *United States* v. *Colotta* (1955), 350 U. S. 808, a *per curiam* decision, reversing 79 S. 2d 474 (Supreme Court of Mississippi).

61 *United States* v. *White Bear Brewing Co.* (1956), 350 U. S. 1010, decided by *per curiam* order, April 9, 1956, reversing 227 F. 2d 359 (7th Circuit), rehearing denied May 28, 1956, 76 S. Ct. 845, 351 U. S. 958.

62 Dissenting opinion of Justices Douglas and Harlan in *United States* v. *White Bear Brewing Co.*, 350 U. S. 1010.

63 *United States* v. *White Bear Brewing Co.* (7th—1955), 227 F. 2d 359; *United States* v. *Holman Lumber Co.* (5th—1953), 206 F. 2d 685, 208 F. 2d 113; *Great Indemnity Co.* v. *United States* (1954), 120 F. Supp. 445; *In re Caswell Construction Co.* (1926), 13 F. 2d 667; *United States* v. *Griffin-Moore Lumber Co.* (Florida—1953), 62 S. 2d 589.

64 *United States* v. *King County Iron Works* (2nd—1955), 224 F. 2d 232; *United States* v. *Eisinger Mill & Lumber Co.* (Maryland—1953), 98 A. 2d 81; *Republic Natl. L. I. Co.* v. *Hedstrom* (Ill. App.—1952), 105 N. E. 2d 782. However, if in a foreclosure case a mortgage is entitled to priority

over a federal lien, a mechanic's lien subordinate to the federal lien may be paid out of the share of sale proceeds which is allocated to the mortgage. *Samms v. Chicago Title and Trust Co.* (Ill. App.—1953), 111 N. E. 2d 172.

65 *Fleming* v. *Brownfield* (Washington—1955), 290 P. 2d 993.

66 In *Van Stone* v. *Stillwell & Bierce Mfg. Co.* (1891), 142 U. S. 128, 136, the Court said, concerning a mechanic's lien:

> "The lien is brought into operation by virtue of the statute, and the contract for building is entered into presumably in view of, or with reference to, the statute."

67 *United States* v. *New Britain* (1954), 347 U. S. 81. In that case, the Court said, page 84:

> "We believe that priority of these statutory liens is determined by another principle of law, namely, *'the first in time is the first in right.'* * * * This principle is widely accepted and applied, in the absence of legislation to the contrary. 33 Am. Jur., Liens, § 33; 53 C. J. S., Liens, § 10b. We think that Congress had this cardinal rule in mind when it enacted § 3670, a schedule of priority not being set forth therein. Thus, *the priority of each statutory lien contested here must depend on the time it attached to the property in question and became choate.*" (Emphasis added.)

68 Shortly after the decision in *Colotta*, a bill was introduced in the 2d Session of the 84th Congress which reads:

"84TH CONGRESS
2D SESSION H. R. 7967

"IN THE HOUSE OF REPRESENTATIVES
JANUARY 3, 1956

MR. SMITH of Mississippi introduced the following bill; which was referred to the Committee on Ways and Means

---

"A BILL

To amend the Internal Revenue Code of 1954 with respect to the validity of a lien for taxes as against a mechanic's lien.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled. That (a) section 6323 of the Internal Revenue Code of 1954 is hereby amended as follows:

(1) By inserting 'MECHANIC'S LIENORS,' after 'PURCHASERS,' in the heading.

(2) By inserting 'mechanic's lienor,' after 'purchaser,' in subsection (a).

(3) By adding at the end thereof the following new subsection:

'(e) DEFINITION OF MECHANIC'S LIENOR—For purposes of subsection (a), the term "mechanic's lienor" means any contractor, subcontractor, materialman, or any person who has rendered services or performed labor on real property and who has acquired a lien in the nature of a mechanic's or materialman's lien on such real property under the law of the State in which the real property is located. Such lien shall be deemed effective as of the date of the commencement of the work of improvement of the property by the lienor.'

(b) The table of sections for subchapter C of chapter 64 is hereby amended by inserting 'mechanic's lienors,' after 'purchasers,'.

SEC. 2. The amendments made by subsection (a) (2) and (3) of the first section of this Act shall apply with respect to any mechanic's lien which was recorded on or after January 1, 1953."

[69] Pomeroy's Equity Jurisprudence (5th Ed. 1941), Sec. 632, 635; *Secombe* v. *Steele* (1857), 20 How. (61 U. S.) 94, 105; *Eyster* v. *Gaff* (1875), 91 U. S. 521, 524.

[70] *United States* v. *Security Trust & Savings Bank* (1950), 340 U. S. 47, 50.

[71] This *lis pendens—collateral attack* principle has not yet been discussed by the Supreme Court. Facts of this kind are involved in the *White Bear* case, reversed by *per curiam* order, April 9, 1956, 350 U. S. 1010. In non-tax cases the United States, as a *pendente lite* purchaser has been held bound by the doctrine of *lis pendens* (*Ward* v. *Congress Construction Co.* (7th—1900), 99 F. 598; *United States* v. *Mayse*, 5 F. 2d 885, 886-887, cert. den. 269 U. S. 580; *United States* v. *Calcasieu Timber Co.* (5th—1916), 236 F. 196, 198-199; *United States* v. *Chicago M. & St. Paul Ry.* (D. Minn.—1909), 172 F. 271, 275).

[72] 28 U. S. C. A. § 2410 and also § 7424 of the Revenue Code of 1954. During depression years, mortgage foreclosures throughout the United States numbered several million. In the single field of small home loans in the two-year period beginning in June 1933, Home Owners' Loan Corporation received 1,886,491 applications for $6.2 billion of home mortgage refinancing. Harris, *History and Policies of HOLC*, p. 1. See Lawyers Service Letter, No. 193, circulated to New York State Bar Association members, which says:

> "1954 INTERNAL REVENUE CODE—DISCHARGE OF PROPERTY FROM FEDERAL TAX LIEN. United States Attorneys have been requested by the Department of Justice to call the attention of the legal profession to § 6325 (b) (2), of the 1954 Internal Revenue Code, which expressly authorizes the Revenue Service to discharge property from a worthless tax lien through administrative process, thus eliminating the necessity of joining the United States as a party defendant in a mortgage foreclosure action.
>
> "Under the 1939 Revenue Code it was not clear whether a mortgagee could secure an administrative discharge of the property from a federal tax lien without some payment being made. As a consequence there has been a steadily increasing number of mortgage foreclosure suits in which the United States is named as a party defendant pursuant to 28 U. S. C. A. 2410, because of the existence of such a lien. In a large percentage of those cases the tax lien is of no value because the market value of the property is such that no surplus can exist after satisfaction of the mortgage, which takes priority. The Department has been flooded with litigation in which the United States has no valuable interest. In the hope of eliminating such litigation it procured the enactment of the provision noted.
>
> "It should be remarked that an administrative discharge has the advantage of eliminating the one year period of redemption which the United States has under 28 U. S. C. A. 2410 (c), where it is joined as a party defendant."

[73] *United States* v. *New Britain* (1954), 347 U. S. 81.

[74] *Dicta* appearing in *United States* v. *Sampsell* (9th—1946), 153 F. 2d 731, 735, states there is nothing in § 3670 "providing for government priority over inchoate liens which antedate its own liens."

[75] *United States* v. *Gilbert Associates* (1953), 345 U. S. 361.

[76] *United States* v. *Security Trust & Savings Bank* (1950), 340 U. S. 47.

[77] *Ibid.*

[78] *United States* v. *Acri* (1955), 348 U. S. 211.

[79] *United States* v. *Liverpool & London Ins. Co.* (1955), 348 U. S. 215.

[80] While in these cases the Court made no comment on the *New Britain* case (which was cited to it), it did rely on § 3466 cases which the Court in the earlier *New Britain* case had found not to control in a non-§ 3466 case. This may be an indication that the Supreme Court will apply the *New Britain* case in a limited way only and will not extend it to private liens. In fact, *New Britain* may have been rendered obsolete by the *White Bear* case cited at footnotes 61 and 62, *supra*. However, the future applicability of § 3466 cases to noninsolvency factual situations is not clear as a result of these decisions.

[81] *United States* v. *Scovil* (1955), 348 U. S. 218.

[82] Insolvency defined. *United States* v. *Oklahoma* (1923), 261 U. S. 253, 260, and 169 A. L. R. 626.

[83] *United States* v. *The State Bank of North Carolina* (1832), 6 Pet. 29, 35.

[84] *United States* v. *Emory* (1941), 314 U. S. 423, 428.

[85] 31 U. S. C. A. § 191.

[86] *Illinois* v. *United States* (1946), 328 U. S. 8, 9.

[87] 11 U. S. C. A. § 104.

[88] *United States* v. *Gargill* (1st—1955), 218 F. 2d 556; *Adams* v. *O'Malley* (8th—1950), 182 F. 2d 925; *United States* v. *Sampsell* (9th—1946), 153 F. 2d 731. Also held inapplicable to a Chapter XI proceeding. *United States* v. *Press Wireless, Inc.* (2nd—1951), 187 F. 2d 294. Wage claims given priority under § 64 (a) of the Bankruptcy Act are not entitled to priority under § 3466 (*United States* v. *Division of Labor Law Enforcement* [9th—1953], 201 F. 2d 856, 36 A. L. R. 2d 1203).

[89] *Brent* v. *Bank of Washington* (1836), 10 Pet. 596, 615.

[90] *Spokane County* v. *United States* (1929), 279 U. S. 80. See *New York* v. *Maclay* (1933), 288 U. S. 290, 292. However, in *United States* v. *Gilbert Associates* (1953), 345 U. S. 361, it is said at page 365:

> "* * * the Town asserts that its lien is a perfected and specific lien which is impliedly excepted from this statute. *This Court has never actually held that there is such an exception.* Once again, we find it unnecessary to meet this issue because the lien asserted here does not raise the question." (Emphasis added.)

[91] *United States* v. *Atlantic Municipal Corp.* (5th—1954), 212 F. 2d 709.

[92] *United States* v. *Gilbert Associates* (1953), 345 U. S. 361. The Court relied on *United States* v. *Waddill Co.* (1945), 323 U. S. 353, wherein it was said, pages 356-357 and 360:

> "Only after the lien was actually asserted and an attachment or distraint levied * * * could it be argued that such goods severed themselves from the general and free assets of the tenant from which the claims of the United States were entitled to priority of payment. * * * At least until actual distraint, therefore, there was no certainty as to the property subject to the lien, and no transfer of title or possession relative to any property."

[93] *United States* v. *Gilbert Associates* (New Hampshire—1953), 90 A. 2d 499, 501.

[94] *United States* v. *Gilbert Associates* (1953), 345 U. S. 361, 366.

[95] (May 1954), 63 Yale L. J. 905, 918, footnote 88.

[96] *United States* v. *Texas* (1941), 314 U. S. 480. Compare *Savings and Loan Society* v. *Multnomah County* (1898), 169 U. S. 421, wherein the Court said at page 428:

> "This court has always held that a mortgage of real estate, made in good faith by a debtor to secure a private debt, is a conveyance of such an interest in the land, as will defeat the priority given to the United States by act of Congress in the distribution of the debtor's estate. *United States* v. *Hooe*, 3 Cranch. 73: *Thelusson* v. *Smith*, 2 Wheat. 396, 426; *Conard* v. *Atlantic Ins. Co.*, 1 Pet. 386, 441."

[97] *New York* v. *Maclay* (1933), 288 U. S. 290, 294. However, with reference to the priority of a sovereign, the Court said in *Marshall* v. *New York* (1920), 254 U. S. 380, at page 382:

> "The priority could be defeated or postponed only through the passing of title to the debtor's property, absolutely *or by way of lien*, before the sovereign sought to enforce his right." (Emphasis added.)

[98] *United States* v. *Waddill Co.* (1945), 323 U. S. 353.

[99] *Massachusetts* v. *United States* (1948), 333 U. S. 611; *Illinois* v. *Campbell* (1946), 329 U. S. 362; *Michigan* v. *United States* (1943), 317 U. S. 338; *United States* v. *Texas* (1941), 314 U. S. 480; *New York* v. *Maclay* (1933), 288 U. S. 290; *Florida* v. *Mellon* (1927), 273 U. S. 12. Purchase of real estate by United States is subject to existing state tax liens which are not enforcible against the United States without its consent, but will become enforcible against a subsequent owner of the property (*United States* v. *Alabama* (1941), 313 U. S. 274).

[100] *Massachusetts* v. *United States* (1948), 333 U. S. 611, 635.

[101] "Bankruptcy Act: Congressional Signpost on the Priority Road" (April 1955), 29 Referee's Journal 63; "Correlation of Priority and Lien Rights in the Collection of Federal Taxes" (June 1947), 95 Univ. of Pa. L. R. 739; "The Differences in the Priority of the United States in Bankruptcy and in Equity Receiverships" (1929), 43 Harv. L. R. 251. But see *United States* v. *Emory* (1941), 314 U. S. 423, wherein the Court finds no congressional intent from § 64 (a) of the Bankruptcy Act to modify the federal priority under § 3466 in nonbankruptcy proceedings.

[102] 11 U. S. C. A. § 104. See text in appendix, *post.*

[103] *Massachusetts* v. *United States* (1948), 333 U. S. 611.

[104] *United States Fidelity & Guaranty Co.* v. *Sweeney* (8th—1935), 80 F. 2d 235, 240, 241. *In re Taylorcraft Corp.* (6th—1948), 168 F. 2d 808, 810; *Claude D. Reese, Inc.* v. *United States* (5th—1935), 75 F. 2d 9, 10. See *Goggin* v. *California Labor Division* (1949), 336 U. S. 118, and cases at footnote 88, *supra. Contra: United States* v. *Reese* (7th—1942), 131 F. 2d 466.

[105] 11 U. S. C. A. § 107. See text in appendix, *post.*

[106] 11 U. S. C. A. § 107 (b) and § 107 (d)(6). See text in appendix, *post.*

[107] *Louisville Joint Stock Land Bank* v. *Radford* (1935), 295 U. S. 555, 583-5; *VanHuffel* v. *Harkelrode* (1931), 284 U. S. 225, 227.

[108] *Miners Savings Bank of Pittston* v. *Joyce* (1938), 97 F. 2d 973, 978.

[109] *United States* v. *Gargill* (1st—1955), 218 F. 2d 556.

[110] *United States* v. *Sampsell* (9th—1946), 153 F. 2d 731; *In re MacKinnon Mfg. Co.* (7th—1928), 24 F. 2d 156.

[111] *In re Taylorcraft Aviation Corp.* (6th—1948), 168 F. 2d 808, wherein the Court relied on language in *Henderson* v. *Mayer* (1912), 225 U. S. 631, 637.

[112] *Phoenix Indemnity Co.* v. *Earle* (9th—1955), 218 F. 2d 645.

[113] *Claude D. Reese, Inc.* v. *United States* (5th—1935), 75 F. 2d 9, 10; and see *In re Weil* (1942), 40 F. Supp. 14.

[114] *In re Knox-Powell Stockton Co.* (9th—1939), 100 F. 2d 979.

[115] 11 U. S. C. A. § 203 (k).

[116] 11 U. S. C. A. § 203(l). See text in appendix, *post.*

[117] 11 U. S. C. A. §§ 1059 (6) and 1041. Special provisions for governmental approval of any plan are found in §§ 1078 and 1080.

[118] 11 U. S. C. A. § 752 and see §§ 712 and 713; *Lockhart* v. *Garden City Bank & Trust Co.* (2nd—1940), 116 F. 2d 658.

[119] 11 U. S. C. A. §§ 737 (2) and 761. See text in appendix, *post.*

[120] 11 U. S. C. A. §§ 205 (e), 599 and 855. See text in appendix, *post.*

APPENDIX

For convenience, the text of the statutes discussed in this report is here set out.

GENERAL LIEN

26 U. S. C. A. § 6321, *et seq.*
(Internal Revenue Code of 1954)

"§ 6321. Lien for taxes

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal belonging to such person.

"§ 6322. Period of lien

Unless another date is specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed is satisfied or becomes unenforceable by reason of lapse of time.

"§ 6323. Validity against mortgagees, pledgees, purchasers, and judgment creditors

(a) Invalidity of lien without notice.—Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate—

(1) Under state or territorial laws.—In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

(2) With clerk of district court.—In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law designated an office within the State or Territory for the filing of such notice; or

(3) With clerk of district court for District of Columbia. —In the office of the clerk of the United States District Court for the District of Columbia, if the property subject to the lien is situated in the District of Columbia.

(b) Form of notice.—If the notice filed pursuant to subsection (a) (1) is in such form as would be valid if filed with the clerk of the United States district court pursuant to subsection (a) (2), such notice shall be valid notwithstanding any law of the State or Territory regarding the form or content of a notice of lien.

(c) * * * [Deals with securities] } [Not pertinent]
(d) * * *"

TREASURY REGULATION

Excerpt from Treasury Regulation Applicable to § 6323: Regulation (T.D. 6119) § 301.6323-1 (a) (2).

[2 P-H Federal Taxes, Par. 19,891.5 (1956)]

"Meaning of Terms.—(i) As used in section 6323 and this section—

(a) The term 'purchaser' means a person who, for a valuable present consideration, acquires property or an interest in property.

(b) The term 'judgment creditor' means a person who has obtained a valid judgment in a court of record and of competent jurisdiction for the recovery of specifically designated property or for a certain sum of money and, in the case of a judgment for the recovery of a certain sum of money, who has a perfected lien under such judgment on the property involved. The term 'judgment' does not include an inchoate lien, such as an attachment lien, unless and until such lien has ripened into a judgment. *United States* v. *Security Trust and Savings Bank* (1950) 340 U. S. 47. Nor does the term 'judgment' include the determination of a

quasi-judicial body or of an individual acting in a quasi-judicial capacity, such as, for example, the action of State taxing authorities. *United States* v. *Gilbert Associates* (1953) 345 U. S. 361; and *United States* v. *City of New Britain* (1954) 347 U. S. 81.

(ii) The determination whether a person is a mortgagee, pledgee, purchaser or judgment creditor, entitled to the protection of section 6323 (a), shall be made by reference to the realities and the facts in a given case rather than to the technical form or terminology used to designate such person. Thus, a person who is in fact and in law a mortgagee, pledgee, or purchaser will be entitled as such to the protection of section 6323 (a) even though such person is otherwise designated under the law of a State, such as the Uniform Commercial Code."

PRIORITY STATUTE

31 U.S.C.A. § 191, DEBTS DUE BY, OR TO, THE UNITED STATES.

"§ 191. Priority established

Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed. R.S. § 3466."

ORDINARY BANKRUPTS

11 U.S.C.A.

"§ 104. Debts which have priority

(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be

(1) * * *; (2) wages not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) * * *; (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: *Provided,* That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: *And provided further,* That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States in[1] entitled to priority, and rent owing to a landlord who is entitled to priority by applicable State Law: *Provided, however,* That such priority for rent to a landlord shall be restricted to the rent which is legally due and owing for the actual use and occupancy of the premises affected, and which accrued within three months before the date of bankruptcy.

[Omitted items (1) and (3) are long. They cover fees, costs and expenses of the proceeding.]

"§ 107. Liens and fraudulent transfers

(a) (1) Every lien against the property of a person obtained by attachment, judgment, levy or other legal or equitable process or proceedings within four months before the filing of a petition initiating a proceeding under this title by or against such person shall be deemed null and void (a) if at the time when such lien was obtained such person was insolvent or (b) if such lien was sought and permitted in fraud of the provisions of this title: *Provided, however,* That if such person is not finally adjudged a bankrupt in any proceeding under this title and if no arrangement or plan is proposed and confirmed, such lien shall be deemed reinstated with the same effect as if it had not been nullified and voided.

* * * * *

[1] So in original. Probably should read 'is.'"

(b) The provisions of section 96 [section 96 covers voidable preferences] of this title to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or to any State or any subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition initiating a proceeding under this title by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court.

* * * * *

(d) (6) A transfer made or an obligation incurred by a debtor adjudged a bankrupt under this title, which is fraudulent under this subdivision against creditors of such debtor having claims provable under this title, shall be null and void against the trustee, except as to a bona fide purchaser, lienor, or obligee for a present fair equivalent value: *Provided, however,* That the court may, on due notice, order such transfer or obligation to be preserved for the benefit of the estate and, in such event, the trustee shall succeed to and may enforce the rights of such transferee or obligee: *And provided further,* That such purchaser, lienor, or obligee, who without actual fraudulent intent has given a consideration less than fair, as defined in this subdivision, for such transfer, lien, or obligation, may retain the property, lien, or obligation as security for repayment."

SPECIAL BANKRUPTCY PROCEEDINGS

11 U. S. C. A.

Chapter 8—Agricultural compositions and extensions

§ 203

"(1) Upon the confirmation of a composition the consideration shall be distributed under the supervision of the conciliation commissioner as the court shall direct, and the case dismissed: *Provided,* That the debts having priority of payment under section 104 of this title, for bankrupt estates, shall have priority of payment in the same order as set forth in said section 104 under the provisions of this section in any distribution, assignment, composition or settlement herein provided for."

Chapter 8—Reorganization of railroads engaged in interstate commerce

§ 205 (e)

A plan of reorganization may be confirmed under certain conditions, and "*Provided further,* That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance, certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of the preceding paragraph hereof: *Provided further,* That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed."

Chapter 10—Corporate reorganizations

"§ 599. United States as creditor

If the United States is a secured or unsecured creditor or stockholder of a debtor, the claims or stock thereof shall be deemed to be affected by a plan under this chapter, and the Secretary of the Treasury is hereby authorized to accept or reject a plan in respect of the claims or stock of the United States. If, in any proceeding under this chapter, the United States is a secured or unsecured creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against the debtor, as secured or unsecured creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance of a lesser amount by the Secretary of the Treasury certified to the court: *Provided,* That if the Secretary of the Treasury shall fail to accept or reject a plan for more than ninety days after receipt of written notice so to do from the court to which the plan has been proposed, accompanied by a certified copy of the plan, his consent shall be conclusively presumed. July 1, 1898, c. 541, § 199, as added June 22, 1938, c. 575, § 1, 52 Stat. 893."

Chapter 11—Arrangements [No specific requirement]

§ 737.

"* * * the judge or referee shall, after the acceptance of the arrangement * * *

(2) fix a time within which the debtor shall deposit, in such place as shall be designated by and subject to the order of the court, the consideration, if any, to be distributed to the creditors, the money necessary to pay all debts which have priority, unless such priority creditors shall have waived their claims or such deposit, or consented in writing to any provision of the arrangement for otherwise dealing with such claims, and the money necessary to pay the costs and expenses of the proceedings and the actual and necessary expenses incurred in connection with the proceedings and the arrangment by the committee of creditors and the attorneys or agents of such committee, in such amount as the court may allow; and

* * * * *

"§ 752. Rights, duties, and liabilities of creditors, etc.

Where not inconsistent with the provisions of this chapter, the rights, duties, and liabilities of creditors and of all other persons with respect to the property of the debtor shall be the same, where a petition is filed under section 721 of this title and a decree of adjudication has not been entered in the pending bankruptcy proceeding, as if a decree of adjudication had been entered in such bankruptcy proceeding at the time the petition under this chapter was filed, or, where a petition is filed under section 722 of this title, as if a voluntary petition for adjudication in bankruptcy had been filed and a decree of adjudication had been entered at the time the petition under this chapter was filed. July 1, 1898, c. 541, § 352, as added June 22, 1938, c. 575, § 1, 52 Stat. 909.

* * * * *

"§ 761. Unanimously accepted arrangement; confirmation upon deposit by debtor.

An arrangement which at the meeting of creditors, as provided in section 736 of this title, has been accepted in writing by all creditors affected thereby, whether or not their claims have been proved, shall be confirmed by the court when the debtor shall have made the deposit required under this chapter and under the arrangement, and if the court is satisfied that the arrangement, and its acceptance are in good faith and have not been made or procured by any means, promises or acts forbidden by this title. July 1, 1898, c. 541, § 361, as added June 22, 1938, c. 575, § 1, 52 Stat. 911.

* * * * *

"§ 762. Majority accepted arrangement; application for confirmation.

If an arrangement has not been so accepted, an application for the confirmation of the arrangement may be filed with the court within such time as the court shall have fixed in the notice of such meeting, or at or after such meeting and after, but not before—

* * * * *

(2) the debtor has made the deposit required under this chapter and under the arrangement. July 1, 1898, c. 541, § 362, as added June 22, 1938, c. 575, § 1, 52 Stat. 911."

Chapter 12—Real property arrangements

"§ 855. United States as creditor

If the United States is a secured or unsecured creditor of a debtor, the claim thereof shall be deemed to be affected by an arrangement under this chapter, and the Secretary of the Treasury is hereby authorized to accept or reject an arrangement in respect of the claims of the United States. If, in any proceeding under this chapter, the United States is a secured or unsecured creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against the debtor, as a secured or unsecured creditor), no arrangement which does not provide for the payment thereof shall be confirmed by the court except upon the acceptance of a lesser amount by the Secretary of the Treasury certified to the court: *Provided,* That if the Secretary of the Treasury shall fail to accept or reject an arrangement for more than sixty days after receipt of written notice so to do from the court to which the arrangement has been proposed, accompanied by a certified copy of the arrangement, his consent shall be conclusively presumed. July 1, 1898, c. 541, § 455, as added June 22, 1938, c. 575, § 1, 52 Stat. 920."

Chapter 13—Wage earners' plans

"§ 1059. Priority of payment

In advance of distribution to creditors, there shall first be paid in full, out of the moneys paid in by or for the debtor, and the order of payment shall be—

* * * * *

(6) the debts entitled to priority, in the order of priority, as provided by subdivision (a) of section 104 of this title. July 1, 1898, c. 541, § 659, as added June 22, 1938, c. 575, § 1, 52 Stat. 935."

SUITS TO CLEAR FEDERAL LIENS

From the Judicial Code, 28 U. S. C. A. § 2410

"§ 2410. Actions affecting property on which United States has lien

(a) Under the conditions prescribed in this section and section 1444 of this title for the protection of the United States, the United States may be named a party in any civil action or suit in any district court, including the District Court for the Territory of Alaska, or in any State court having jurisdiction of the subject matter, to quiet title to or for the foreclosure of a mortgage or other lien upon real or personal property on which the United States has or claims a mortgage or other lien.

(b) The complaint shall set forth with particularity the nature of the interest or lien of the United States. In actions in the State courts service upon the United States shall be made by serving the process of the court with a copy of the complaint upon the United States attorney for the district in which the action is brought or upon an assistant United States attorney or clerical employee designated by the United States attorney in writing filed with the clerk of the court in which the action is brought and by sending copies of the process and complaint, by registered mail, to the Attorney General of the United States at Washington, District of Columbia. In such actions the United States may appear and answer, plead or demur within sixty days after such service or such further time as the court may allow.

(c) A judicial sale in such action or suit shall have the same effect respecting the discharge of the property from liens and encumbrances held by the United States as may be provided with respect to such matters by the local law of the place where the property is situated. A sale to satisfy a lien inferior to one of the United States, shall be made subject to and without disturbing the lien of the United States, unless the United States consents that the property may be sold free of its lien and the proceeds divided as the parties may be entitled. Where a sale of real estate is made to satisfy a lien prior to that of the United

States, the United States shall have one year from the date of sale within which to redeem. In any case where the debt owing the United States is due, the United States may ask, by way of affirmative relief, for the foreclosure of its own lien and where property is sold to satisfy a first lien held by the United States, the United States may bid at the sale such sum, not exceeding the amount of its claim with expenses of sale, as may be directed by the head of the department or agency of the United States which has charge of the administration of the laws in respect of which the claim of the United States arises.

(d) Whenever any person has a lien upon any real or personal property, duly recorded in the jurisdiction in which the property is located, and a junior lien, other than a tax lien, in favor of the United States attaches to such property, such person may make a written request to the officer charged with the administration of the laws in respect of which the lien of the United States arises, to have the same extinguished. If after appropriate investigation, it appears to such officer that the proceeds from the sale of the property would be insufficient to wholly or partly satisfy the lien of the United States, or that the claim of the United States has been satisfied or by lapse of time or otherwise has become unenforceable, such officer shall so report to the Comptroller General who may issue a certificate releasing the property from such lien. June 25, 1948, c. 646, § 1, 62 Stat. 972, amended May 24, 1949, c. 139, § 119, 63 Stat. 105."

From the Internal Revenue Code of 1954, 26 U. S. C. A. § 7424

"§ 7424. Civil action to clear title to property

(a) Obtaining leave to file.—

(1) Request for institution of proceedings by United States. Any person having a lien upon or any interest in the property referred to in section 7403 [section 7403 covers suits by United States to enforce its liens against property of taxpayer], notice of which has been duly filed of record in the jurisdiction in which the property is located, prior to the filing of notice of the lien of the United States

as provided in section 6323, or any person purchasing the property at a sale to satisfy such prior lien or interest, may make written request to the Secretary or his delegate to authorize the filing of a civil action as provided in section 7403.

(2) Petition to court.—If the Secretary or his delegate fails to authorize the filing of such civil action within 6 months after receipt of such written request, such person or purchaser may, after giving notice to the Secretary or his delegate, file a petition in the district court of the United States for the district in which the property is located, praying leave to file a civil action for a final determination of all claims to or liens upon the property in question.

(3) Court order.—After a full hearing in open court, the district court may in its discretion enter an order granting leave to file such civil action, in which the United States and all persons having liens upon or claiming any interest in the property shall be made parties.

(b) Adjudication.—Upon the filing of such civil action, the district court shall proceed to adjudicate the matters involved therein, in the same manner as in the case of civil actions filed under section 7403. For the purpose of such adjudication, the assessment of the tax upon which the lien of the United States is based shall be conclusively presumed to be valid.

(c) Costs.—All costs of the proceedings on the petition and the civil action shall be borne by the person filing the civil action."

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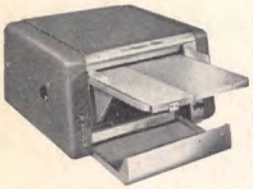

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