UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF FLORIDA
OCALA DIVISION

In re:

JOHN ROBERT SHEK,

Debtor.

MASSACHUSETTS DEPARTMENT OF REVENUE,

Appellant,

v. Case No: 5:18-cv-341-JSM

JOHN ROBERT SHEK,

Appellee.

ORDER

The Massachusetts Department of Revenue brings this timely appeal from a final judgment entered by the Bankruptcy Court on stipulated facts. This Court has jurisdiction pursuant to 28 U.S.C. § 158(a).

The issue, a question of law, is whether a state income tax debt from a late-filed return is dischargeable in bankruptcy. Its resolution turns on the interpretation of the dischargeability statute. A literal reading gives one result while reading it to give the statute a common sense meaning as a whole (as did the Bankruptcy Court) gives another. The Court agrees with the Bankruptcy Court that the statute should be read as a whole and will affirm.

FACTS

In 2008, John Robert Shek was a resident of Massachusetts required to file a state income tax return. Shek, who was undergoing a divorce at the time and says he was trying to

get information from his wife about deductions she may have claimed, did not file his tax return by the date it was due. He filed his return about seven months late on November 25, 2009, showing a tax due of $11,489.

Almost six years later, on October 8, 2015, Shek filed a voluntary Chapter 7 bankruptcy petition in the Bankruptcy Court for the Middle District of Florida. On January 26, 2016, the Bankruptcy Court entered a discharge pursuant to 11 U.S.C. § 727. Subsequently, a dispute arose about whether that order discharged the 2008 Massachusetts income tax obligation.

On June 24, 2016, Shek filed a motion to reopen the case seeking a determination that his state income tax liability was discharged. The State of Massachusetts took the position that the tax debt was not discharged because Shek's return was not a "return" as defined in the statute because it was filed after the due date. The parties stipulated to the facts and submitted a motion for entry of an agreed final order. Shek agreed to forego his claims that Massachusetts had violated the automatic stay by seeking to collect a discharged debt. Massachusetts agreed that if the *Beard* test[1] to determine what is a "return" is still applicable nonbankruptcy law, Shek satisfied all four prongs of the test, and the debt was dischargeable. But Massachusetts reserved its right to appeal whether *Beard* was the applicable nonbankruptcy law rather than Massachusetts tax law. On June 21, 2018, the Bankruptcy Court granted the joint motion and entered a final judgment holding the tax debt was dischargeable.

[1] *Beard v. Comm'r of Internal Revenue,* 82 T.C. 766 (1984), *aff'd*, 793 F.2d 139 (6th Cir. 1986) ("*Beard*"). Under the *Beard* test, a document submitted to the IRS by a taxpayer qualifies as a return if it (1) purports to be a return; (2) is executed under penalty of perjury; (3) contains sufficient data to calculate the tax liability; and (4) represents an honest and reasonable attempt to satisfy the requirements of the tax law. *Id.* at 777-78.

DISCUSSION

Section 727 of the Bankruptcy Code dictates whether a debtor is entitled to a discharge from his debts in a Chapter 7 proceeding. 11 U.S.C. § 727. It is a rule of nondischargeability but is subject to several exceptions. Whether unpaid taxes are dischargeable is specified in 11 U.S.C. § 523(a)(1) which states, in relevant part:

> (a) A discharge under section 727…of this title does not discharge an individual debtor from any debt—
> (1) for a tax or a customs duty—
> …
> (B) with respect to which a return, or equivalent report or notice, if required—
> (i) was not filed or given; or
> (ii) was filed or given after the date on which such return, report, or notice was last due, under applicable law or under any extension, and after two years before the date of the filing of the petition[.]

In sum, the statute provides that a tax debt is not dischargeable if a return (1) was not filed, or (2) was filed after the date on which the return was due and the filing was within two years before the filing of the bankruptcy petition.

Prior to 2005, the statute did not contain a definition of what constituted a "return." Was any paper filed, regardless of the information contained, a "return," even one filed in bad faith? Courts were called upon to weigh in on that issue and adopted what is now called the "*Beard* test." *See In re Fahey*, 779 F.3d 1, 10 (1st Cir. 2015) (discussing the "*Beard* test"). The tax court in *Beard* set forth a four-part standard for determining when a document was a federal tax return. It was a tax return if:

> (1) it reported to be a return;
>
> (2) was signed under penalty of perjury;
>
> (3) contained information sufficient to determine tax liability; and

(4) was a honest and reasonable attempt to satisfy the tax law requirements.

Beard, 82 T.C. at 777-78.

In 2005, Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act adding a definition of "return" to section 523 of the Bankruptcy Code. This definition has been termed a "hanging paragraph"[2] because it was merely stuck at the end of section 523(a). The added definition states:

> For purposes of this subsection, the term "return" means a return that satisfies the requirements of applicable nonbankruptcy law *(including applicable filing requirements)*. Such term includes a return prepared pursuant to section 6020(a) of the Internal Revenue Code of 1986, or similar State or local law, or a written stipulation to a judgment or a final order entered by a nonbankruptcy tribunal, but does not include a return made pursuant to section 6020(b) of the Internal Revenue Code of 1986, or similar State or local law. (Emphasis supplied.)

11 U.S.C. 523(a)(*).

The new definition, while obviously intended to clarify the situation, only served to create additional consternation among the courts. Now even judges from the same court disagree on what constitutes a "return" for purposes of dischargeability. *See Wendt v. U.S.* (*In re Wendt*), 512 B.R. 716 (Bankr. S.D. Fla. 2013) (concluding a late filed return is not a "return" under the statute); c.f. *Coyle v. U.S.* (*In re Coyle)* 524 B.R. 863 (Bankr. S.D. Fla 2015) (finding a late filed return is still a "return" under the statute).

The culprit lies in the parenthetical phrase in the new definition: "including applicable filing requirements." Courts disagree whether this parenthetical phrase includes applicable filing deadlines. That is, is a return filed after its due date still a "return" as now defined by the statute?

[2] The "hanging paragraph" is denoted as section 523(a)(*).

This question has been addressed by many courts. One directly on point, and involving Massachusetts state income tax, is *In re Fahey*, 779 F.3d 1 (1st Circ. 2015). *Fahey,* in a divided opinion, does an excellent job of exploring both sides of the issue. In the interest of brevity, the Court will not repeat the arguments here, but rather commends a reading of the *Fahey* opinion. While saying *Fahey* does an excellent job of setting forth both sides of the argument, this Court agrees with the dissent rather than the majority.

The *Fahey* majority concludes that a return filed after its due date is not a "return" except in the limited circumstance where a taxpayer does not file a return at all, but later cooperates with the IRS in preparing a return under 6020(a) of the Internal Revenue Code. That interpretation is based on a literal reading of the hanging paragraph and glosses over that it renders superfluous the reference to section 6020(b) (if all late-filed returns, except those under 6020(a) are not "returns," there is no need to mention 6020(b)). 779 F.3d at 5-10.

A first reading of the statute points to the conclusion that a filing deadline would be an "applicable filing requirement." If Congress intended this result, a return filed after the due date no longer would be a "return" meeting the exception entitling the tax debt to dischargeability. But reading the statute as a whole, as we must do, reveals that a literal reading, in addition to rendering the reference to section 6020(b) superfluous, creates an internal conflict.

First, note that in section 523(a)(1)(B)(ii) Congress still refers to a document filed after the due date as a "return." And, just as the new congressional definition appears clear upon first reading, so too is this section's reading clear that a return filed after a due date but before the two years immediately proceeding the filing of the bankruptcy petition is entitled to have its tax debt discharged.

Second, not only does Congress still refer to late-filed documents as "returns," it makes a commonsense distinction between the types of "returns." A section 6020(a) return is one prepared by the IRS with the cooperation of the taxpayer. A section 6020(b) return is one prepared by the IRS without the cooperation of the taxpayer. Obviously, both are late-filed returns because the IRS would not be trying to prepare a return for a taxpayer before it was due. This distinction focuses on the *information* that was filed, not *when* it was filed. That is, Congress does not seem to be treating a filing deadline as an "applicable filing requirement." In fact, including filing deadlines in that phrase leads to an absurd result as pointed out by the dissent in *Fahey*:

> Second, allowing § 6020(a) returns, but not other late-filed returns, to be dischargeable leads to another preposterous result. Section 6020(a) returns result from a taxpayer's failure to file a federal tax return. Under the majority's formulation, then, the scofflaw who sits on his hands at tax time, doesn't bother to file a return, and then, after getting caught, cooperates with the authorities and lets the government filed the substitute return for him, would be the *only* late filer who would be allowed to discharge his tax debt. The person who files his return one day late—which the state then accepts—would not be permitted to discharge, regardless of the reason for the tardiness.

In re Fahey, 779 F.3d at 15.

Because we must read the statute as a whole, avoiding internal conflicts and absurd results where possible, it appears Congress did not intend to include filing deadlines as an "applicable filing requirement." And, notably, the IRS agrees with this interpretation and has stipulated that a late filed tax return can be discharged if it complies with section 523(a)(1)(B)(ii). *In re Coyle*, 524 B.R. at 867.

Having discussed the background of the law and this Court's conclusions about it, the Court turns to the case before it.

THE CASE BEFORE THE COURT

Shek takes the position that this Court is bound by Eleventh Circuit precedent to rule that the *Beard* test still applies as the "applicable nonbankruptcy law" after the 2005 amendment. For support, Shek points to *In re Justice*, 817 F.3d 738 (11th Cir. 2016). The State of Massachusetts disagrees and argues that *Justice* in not on point because it dealt with a federal income tax debt, not a State of Massachusetts income tax debt.

The Court agrees with Appellant that it is not bound by Eleventh Circuit precedent. First, *Justice* concerned a federal income tax "return," not a state income tax "return." And, the Eleventh Circuit did not specifically hold that the *Beard* test still applied, it only assumed so *arguendo*:

> We assume, without deciding, that Congress did not intend to include filing deadlines when it required, in the hanging paragraph, that tax returns comply with "applicable filing requirements." Even making that assumption, however, we hold that Justice's late-filed Forms 1040 do not qualify as tax returns under the *Beard* test because they do not evince an honest and reasonable effort to comply with the tax law.

In re Justice, 817 F.3d at 746.

Having said that *Justice* is not binding precedent, this Court, like the Bankruptcy Court, concludes that the reasoning in *Justice* applies and will rule consistently with it. Appellant's argument that this case concerns a state income tax rather than a federal income tax is a distinction without a difference. Both the State of Massachusetts and the Federal Government have filing deadlines. So, the phrase "applicable filing requirements" applies as well to state tax returns as it does to federal tax returns. The main issue in this case is whether the *Beard* test still applies—after the 2005 addition of the "hanging paragraph"—

to determine whether a late-filed return is still a "return" under the statute. For the reasons explained, I conclude that it does.

The States of Massachusetts stipulated in the Bankruptcy Court that if the *Beard* test still applied as the "applicable nonbankruptcy law" referred to in the "hanging paragraph," the debt would be dischargeable. That is how the Bankruptcy Court ruled and this Court agrees.

Therefore, the final judgment of the Bankruptcy Court is hereby affirmed. The Clerk is directed to close this case.

DONE and **ORDERED** in Tampa, Florida, this 13th day of November, 2018.

JAMES S. MOODY, JR.
UNITED STATES DISTRICT JUDGE