

## Assigned Ad Valorem Tax Claims in Chapter 13

Chapter 13 debtors whose taxes are not escrowed will occasionally resort to one of the property tax payment services which pay the taxes and take an assignment of the taxing entity's claim. The upside for the taxing authority: they get their money faster without incurring collection costs. The upside for the debtor: they get to pay the taxes over a longer period of time without incurring collection costs. The downside for the debtor: taxing authorities can only charge 12% interest while tax assignees can charge 18%. If the debtor pays the claim over a longer period of time at 18% interest, they end up paying far more interest. (Actually, the best case for the debtor is for the mortgage company to pay the taxes. That way, the debtor can pay back the mortgage company at no interest.)

BAPCPA added new Section 511 which provides: "If any provision of this title requires the payment of interest on a tax claim... the rate of interest shall be the rate determined under applicable bankruptcy law." It is significant that Section 511 does not define "tax claim."

There have been a recent spate of opinions on this issue starting with Judge Lynn in In re Davis, 352 B.R. 651 (Bankr.N.D.Tex.2006). Judge Lynn held that the claim of a creditor which paid the ad valorem tax claim prior to filing of the Chapter 13 and held a transfer of the tax lien was a "tax claim" under Section 511 and so was entitled to receive its contractual rate of interest in a Chapter 13. The important point here is the anti-modification provision of Section 1322(b)(2) which provides that a debtor may modify the rights of holders of secured claims "other than a claim secured only by a security interest in real property that is the debtor's principal residence."

In In re Sheffield, 390 B.R. 302 (Bankr.S.D.Tex.2008), Judge Isgur went into a more detailed analysis and concluded that although the private company assignee of a taxing authority held a "tax lien", it did not hold a "tax claim", disagreeing with Judge Lynn.

Section 101(51) defines a security interest as a "lien created by an agreement." Ad valorem tax liens are created by state law, not by any agreement. In most of these cases, the tax assignee takes a transfer of the taxing authority's lien, but they also have the debtor execute a note and deed of trust. As Judge Isgur explains, the lien is not created by the agreement, but arises by operation of state law. In order to obtain an assignment of the tax lien, the taxes must be paid by the assignee. When the taxes are paid, there is no longer any "tax claim." A new claim arose under the promissory note executed by the debtor. That claim may have resulted from payment of taxes, but it was not a "tax claim." Judge Isgur makes the further point that the tax assignee did not purchase the taxing authority's claim - it paid the claim. Judge Isgur concludes: "A state taxing authority may assign its tax claims if state law so provides. Hypothetically, a state could authorize the sale of its tax receivables to a third party. That third-party assignee would presumably be protected by Sec. 511, But, that is not the structure that this State has chosen for the private collection of its property taxes."

Approximately one month later, Judge Bohm followed Sheffield in In re Prevo, 393 B.R. 464 (Bankr.S.D.Tex.2008). Judge Bohm provides some discussion of the Kentucky and Pennsylvania tax statutes to contrast them with the language of the Texas statute and clarify the issue.

Judge Isgur revisited the issue in January 2009 in In re Kizzee-Jordan, 399 B.R. 817 (Bankr.S.D.Tex.2009). In Kizzee-Jordan, the tax assignee took another approach arguing that Sheffield was inconsistent with the Supreme Court's opinion in Johnson v. Home State Bank, 501 U.S. 78 (1991) and the Sixth Circuit's opinion in Glance v. Carroll, 487 F.3r 317 (6<sup>th</sup> Cir.2007). Neither of those opinions have any relevance to the disposition of this issue and Judge Isgur so concluded. (In short order.) [Judge Isgur confirmed this conclusion again a month later in In re Sotto, 2009 WL 260957 (Bankr.S.D.Tex.2009).]

I have not found any opinions in the Eastern or Western Districts or by any other judges in the Northern or Southern Districts.

Assuming that 511 does not apply to "tax liens" as opposed to "tax claims", the appropriate rate of interest for tax assignees in Chapter 13 would be the Till "prime plus" approach. FYI, the interest rates confirmed in Sheffiled, Prevo, Kizzee-Jordan and Sotto were 12%, 8.25%, 8.5%, and 7%, respectively. (As a debtor's attorney, I like the downward trend in rates.)

I would guess that we will see the tax assignee lobby try to get the legislature to "fix" this "defect" in the tax statutes, but until then, your Chapter 13 plans should pay Till interest, not the contract rate of 15% or 18%.