

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
Central Division

In re:)	
)	Bankr. Case No. 87-30128
DESMOND V. VAN ZEE)	
Social Security No. 504-34-0300)	Chapter 12
)	
and)	MEMORANDUM OF DECISION RE:
)	HAND COUNTY'S MOTION TO DISMISS
PATRICIA E. VAN ZEE)	FOR FAILURE TO PAY REAL ESTATE
Social Security No. 503-64-9154)	TAXES AND MOTION TO LIFT
)	AUTOMATIC STAY
Debtors.)	

The matter before the Court is the Motion to Dismiss for Failure to Pay Real Estate Taxes and Motion to Lift Automatic Stay filed by Hand County and the response thereto filed by Debtors. This is a core proceeding under 28 U.S.C. § 157(b)(2). This Memorandum and accompanying Order shall constitute findings and conclusions as required by F.R.Bankr.P. 7052.

I.

Debtors filed a Chapter 12 petition on September 3, 1987. In their schedules, Debtor's acknowledged that Hand County had a priority claim for \$6,800.75 for real estate taxes. Hand County filed a proof of claim on September 23, 1987 for \$18,225.27 for pre-petition real estate taxes and special assessments.¹ The proof

¹ These taxes included:

Year	Tax	Interest	Total
1981	\$ 359.94	\$ 297.01	\$ 656.95
1982	390.59	241.19	631.78
1983	417.09	195.00	612.09
1984	3,061.82	1,012.13	4,073.95
1985	3,954.55	681.39	4,635.94
1986	<u>3,820.27</u>	<u>105.05</u>	<u>3,925.32</u>
	\$12,004.26	\$2,531.77	14,536.03
<i>Assessments</i>	<u>209.11</u>	<u>21.66</u>	<u>579.18</u>
Total	<u><u>\$12,213.37</u></u>	<u><u>\$2,553.43</u></u>	<u><u>\$15,115.21</u></u>

Based on the Court's calculations, the total on Hand County's proof of claim was apparently incorrect.

of claim did not identify the claim as a secured claim or a priority claim.

Debtors' debt adjustment plan was confirmed on August 30, 1988. The plan as confirmed, which was filed on August 30, 1988, stated Hand County had a *priority* claim of \$6,800.75 that would be paid over ten years with ten percent interest (annual payments of \$1,106.83). The plan further stated that Farmers Home Administration's (FmHA) undersecured claim was subordinate to Federal Land Bank's (now Farm Credit Bank of Omaha [FCBO]) secured claim for \$46,885.48 and to Hand County for taxes of \$16,617.77. Hand County never filed any objections to Debtors' proposed plan.

Debtors' pre-petition real estate taxes were the subject of litigation twice after confirmation. The first time was when Debtors filed an adversary complaint against Hand County and its Treasurer on November 6, 1990. Debtors stated Hand County was trying to take tax deeds on some of Debtors' property for back taxes. Debtors stated those pre-petition taxes were covered by Debtors' plan and that Debtors had made all plan payments. Therefore, Debtors asked the Court to enjoin the tax sale as a violation of the automatic stay. The Defendants did not answer. On December 24, 1990, Debtors' attorney filed an application and affidavit for a default judgment. Attached to the affidavit were copies of the County's Statement of Taxes that showed Debtors owed \$6,069.95 in certain real estate taxes and special assessments for 1981 through 1989. A default judgment and permanent injunction

were entered January 17, 1991. The injunction prohibited the Defendants from "commencing, pursuing or completing any of such tax sale procedures and such procedures as have transpired or taken place to date [were] declared to be null and void as having been conducted in violation of the automatic stay." A copy of the County's Notice to Take Tax Deeds by County and the Statements of Taxes were attached to the permanent injunction order.

Debtors' post-petition real estate taxes were addressed a second time after confirmation when counsel for FCBO filed an affidavit of default on February 4, 1992. He stated Debtors had defaulted on their January 1, 1992 payment to FCBO and had also failed to pay back real estate taxes as required by the plan. Counsel for FCBO filed a supplemental affidavit on March 5, 1992 that stated Debtors had not cured the default timely. Pursuant to the default provision in Debtors' confirmed plan, the Court granted FCBO relief from the automatic stay by Order entered March 6, 1992.

Debtors filed a motion to vacate the relief from stay order on March 12, 1992. FCBO filed a resistance on March 27, 1992 that acknowledged Debtors' argument that they had paid all real estate taxes due but that Hand County had failed to apply them properly. FCBO argued, however, that application of the funds was Debtors' problem and that its mortgage position should not be weakened by the misapplication of the taxes. An attachment to FCBO's resistance from the Hand County Treasurer indicated Debtors owed \$12,534.98 for 1984, 1985, 1986, 1987, and 1991 real property taxes.

A hearing on Debtors' motion to vacate the relief from stay order was held April 14, 1992. Appearances included James E. Carlon for Debtors and Timothy M. Engel for FCBO. LaDonna Kindle, the Hand County Treasurer, testified that Debtors had made three plan payments of \$1,106.83 to date. She said the taxes were being held in a trust account until enough was accumulated to pay all back taxes or until she was directed by someone to apply them to certain taxes. Ms. Kindle also testified that Debtors' taxes on their farm property were paid in full for the years 1988, 1989, and 1990. She said Debtors also owed 1987 taxes on some in-town property. Finally, she stated FmHA had paid \$15,420.07² in back taxes in 1987 and that the amount was deducted before the County filed its proof of claim for \$18,225.27. Upon finding that Debtors had failed to pay timely the plan payment to FCBO due to Mr. Van Zee's illness and that Debtors had made all tax payments required by the Plan, the Court granted Debtors' motion to vacate the relief from stay order. The Court directed counsel to work with the Treasurer to insure that the plan payments were properly applied to back taxes.

Debtors filed their final report and account on September 2, 1993. Therein, Debtors stated they had made \$3,320.49 in plan payments to the Hand County Treasurer. They also acknowledged that

² In an affidavit attached to Hand County's post-hearing brief, Ms. Kindle stated that on December 31, 1984 FmHA paid \$18,625.46 in taxes on Debtors' farmland for years 1979 (½), 1980, 1981, 1982, and 1983.

they had not yet paid \$6,000.00 in 1993³ real estate taxes that were due. Several parties filed objections to Debtors' discharge.⁴

FCBO objected to Debtors' discharge on September 9, 1993. It argued Debtors are in default on their plan because they have failed to pay past due real estate taxes on FCBO's collateral.

FmHA filed an objection to Debtors' discharge on September 30, 1993. It argued Debtors had not made all plan payments because real estate taxes of \$25,451.33 remain unpaid. FmHA also stated a disposable income evaluation was needed.

On October 21, 1993, Hand County filed a motion to dismiss Debtors' case because Debtors had failed to pay the real estate taxes on which Hand County had filed a proof of claim and because Debtors had failed to pay \$43,237.54 in real estate taxes that

³ The Court assumes Debtors were referring to 1992 taxes that had to be paid in 1993.

⁴ Two objections did not relate to Debtors' unpaid real estate taxes. Chapter 12 Trustee John S. Lovald objected to Debtors' discharge on September 3, 1993. He stated that the plan provided for payments to unsecured claim holders for ten years with a lien on cattle. He wanted to insure that the discharge order "clearly define[d] and establish[ed] the procedure for the continuation of the security interest granted by Debtors, and the continuation of the stream of payments to unsecured creditors." The Trustee also stated that Debtors had dissipated the collateral given to the unsecured creditors and that post-petition administrative expenses should be paid before a discharge is entered. Finally, Trustee Lovald argued there may be disposable income available for unsecured claim holders.

The Small Business Administration objected to Debtors' discharge on September 28, 1993. It stated it had not received its pro rata unsecured payment for 1992 as provided by Article VII of Debtors' confirmed plan.

accrued during the term of the plan.

Debtors filed a resistance to Hand County's motion on October 26, 1993. They argued Hand County is bound by the terms of the confirmed plan and may collect no more taxes than are provided in the plan. Debtors further argued that the amount of taxes owed to Hand County was previously litigated before this Court.

FCBO filed a response to Debtors' resistance on October 29, 1993. It stated that the plan is not *res judicata* on the issue of taxes and that tax liens survive confirmation under this Court's decision in *In re Ralph A. Timmerman*, Bankr. No. 88-30016, slip op. (Bankr. D.S.D. July 22, 1993). FCBO also argued that the adversary proceeding between Debtors and Hand County did not address the tax lien issue but merely said the County's proposed sale for taxes was in violation of the automatic stay. Finally, FCBO stated the Court's prior ruling that vacated the order giving FCBO relief from the automatic stay also did not address the issues presented by the objections to Debtors' discharge and Hand County's motion to dismiss.

A hearing was held November 16, 1993. Appearances included Bradley G. Zell for Hand County, James E. Carlon for Debtors, Assistant U.S. Attorney Thomas A. Lloyd for FmHA, Timothy M. Engel for FCBO, and Chapter 12 Trustee John S. Lovald. At the hearing, the key issues were whether Hand County could collect delinquent taxes for which the plan did not provide and whether Hand County's tax liens would survive discharge. Counsel for Hand County stated another \$8,000.00 in 1992 taxes had accrued November 15, 1993 for

an approximate total of \$43,500.00 in taxes due.

By letter filed November 17, 1993, counsel for Hand County informed all parties that Debtors had paid their 1992 taxes in full on November 8, 1993. In its post-hearing brief, Hand County further stated that as of November 24, 1993, Debtors owed \$39,826.37 in real estate taxes, mostly for 1981 through 1987, plus some 1989 taxes and various special assessments. Most taxes for 1988 through 1992 are paid.

Upon receipt of all briefs, the tax issues raised by Hand County's motion to dismiss were taken under advisement.

II.

Real property owners in South Dakota are assessed taxes annually. S.D.C.L. § 10-6-2. Based on the value of the property on November 1 of the preceding year, *id.*, all taxes become due on the first day of January of each year following the assessment. S.D.C.L. § 10-21-4. One-half of the annual tax becomes delinquent on May first if not paid. S.D.C.L. § 10-21-23. The other half is due October thirty-first. *Id.* Interest attaches to all delinquent taxes. *Id.* Taxes imposed on real property and any interest and penalty⁵ thereon becomes a perpetual lien on the property.

⁵ South Dakota law distinguishes between interest on taxes and penalties on taxes. *See, e.g.*, S.D.C.L. § 10-22-60. South Dakota law currently does not provide for any penalty on late-paid real estate taxes.

S.D.C.L. § 10-21-33.⁶ If real property taxes are not paid timely, the county may sell the property and issue a tax certificate. S.D.C.L. Ch. 10-23. The county may hold the certificate if no buyer is found. *Id.* The county's lien is extinguished when a tax certificate is issued to a purchaser other than the county. See *Broadhurst v. American Colloid Co.*, 177 N.W.2d 261, 264 (S.D. 1970), and *Read v. Jerauld County*, 17 N.W.2d 269, 271 (S.D. 1945). If property sold for taxes is not redeemed timely, the county, after proper notice, may issue a tax deed and deliver it to the tax certificate holder. See S.D.C.L. Ch. 10-25.

In bankruptcy, *unsecured*, pre-petition real property taxes are a priority claim if they were "assessed before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition." 11 U.S.C. § 507(a)(7)(B). Such priority claim taxes must be paid in full over time with interest. 11 U.S.C. §§ 1222(a)(2) and 1225(a)(1).

A Chapter 12 plan may provide for claims for taxes secured by a lien on property under §§ 1222(b)(2) and 1225(a)(5). The plan may modify the rights of the holder of the secured claim. 11 U.S.C. § 1222(b)(2). However, a Chapter 12 plan must be accepted⁷

⁶ S.D.C.L. § 10-21-33 was adopted in 1992. Before then, the same perpetual lien provision was codified at S.D.C.L. § 10-19-2.

⁷ At the time Debtors' plan was confirmed, F.R.Bankr.P. 3018(c) stated an acceptance or rejection of a plan shall be in writing and signed by the creditor. The Rule did not differentiate clearly among Chapters 11, 12, or 13. In 1993, Rule 3018 was amended to state that it governs only Chapter 9 and Chapter 11 cases. Federal Rule of Bankruptcy Procedure 3015 was also amended to include provisions for objections to Chapter 12 and 13 plans.

by the secured claim holder, the secured claim holder must retain his lien and receive deferred cash payments, or the property securing the claim must be surrendered to the claim holder. 11 U.S.C. § 1225(a)(5).

A confirmed plan binds the debtor and the claim holders, even if the plan does not provide for a particular claim and even if the claim holder did not accept⁸ the plan. 11 U.S.C. § 1227(a). Upon completion of all plan payments, the debtor is entitled to a discharge. 11 U.S.C. § 1228(a). All debts "provided for by the plan" may be discharged. *Id.* However, a tax lien on real property may survive a Chapter 12 discharge, see, e.g., *In re Kuebler*, 156 B.R. 1012, 1017 (Bankr. E.D. Ark. 1993); *In re Honaker*, 4 B.R. 415 (Bankr. E.D. Mich 1980), especially if the plan does not treat the secured claim adequately. See *Sun Finance Co., Inc. v. Howard (In re Howard)*, 972 F.2d 639 (5th Cir. 1992); compare *In re Pence*, 905 F.2d 1107 (7th Cir. 1990).

III.

When Debtors filed their petition on September 3, 1987, Hand County had a secured claim for all real estate taxes through 1986 since a statutory tax lien attached on January 1 of each year for the prior year's taxes. However, both Hand County and Debtor failed to classify Hand County's claim properly. In essence, it is

Amended Rule 3015 does not define "accepted" as that term is used in 11 U.S.C. §§ 1225(a)(5)(A) and 1227(a).

⁸ See *supra* note 7.

safe to say that very little has gone right with Hand County's claim in this case. Hand County filed a proof of claim but stated an incorrect amount and failed to identify the claim as a secured claim. Hand County did not participate in the confirmation process. Debtors proposed a plan that stated two different amounts for Hand County's claim and they misclassified Hand County's claim as a priority claim rather than a secured claim. Further, while the plan recognized Hand County had a lien on real property for \$16,617.77 superior to FmHA's lien, the plan did not provide treatment for Hand County's statutory lien. Moreover, Debtors may not have paid timely all annual payments to Hand County due under the plan.⁹ Finally, the Court erred by confirming a plan with these deficiencies.

Now that Debtors are seeking a discharge and the case is ready to be closed, the key question is whether Hand County's lien for pre-petition taxes survives discharge or did Hand County waive the liens by not objecting to Debtors' offer in their plan of ten annual payments of \$1,106.83. Upon consideration of applicable law and all the enigmatic provisions in Debtors' confirmed plan, the Court concludes Hand County's tax liens will survive Debtor's discharge.

Debtors recognized Hand County had a lien when their plan stated FmHA's lien was subordinate to Hand County's taxes and to

⁹ Under the plan, Debtors are required to make annual payments of \$1,106.83 for ten years. The plan was confirmed August 30, 1988 but Debtors have made only four payments through November 24, 1993. See *infra* note 11.

FCBO's mortgage. The paragraph that sets forth the treatment of Hand County's claim did not state that the lien would be extinguished. Moreover, while property of the estate vested in Debtors at confirmation, there is no provision in the plan on which the Court could conclude that Debtors took the property free of any liens to which the bankruptcy estate was subject. In sum, the plan acknowledged Hand County's lien but did not provide any treatment for it. Thus, Hand County could rely on Debtors' recognition of its tax liens in the plan and look to the liens for satisfaction of the remainder of its claim.

The Code supports this conclusion. As provided in § 1227(c), property of the estate reverts in the debtor at confirmation "free and clear of any claim or interest of any creditor *provided for by the plan.*" Assuming that "claim or interest" as used in § 1227(c) includes "liens,"¹⁰ Debtors' plan did not provide for the treatment of Hand County's lien other than recognizing that it exists. Finally, Debtors may receive a discharge only for debts provided for in the plan. Again, Hand County's lien was not "provided for" in the plan. While a discharge may relieve Debtors of any personal liability for the tax claims so that Hand County cannot seek payment of pre-petition taxes from Debtors in excess of the annual payments provided in the plan,¹¹ the County nonetheless may look to

¹⁰ See *Johnson v. Home State Bank*, 111 S.Ct. 2150, 2153-54 (1991) (The definition of "claim" encompasses "liens.")

¹¹ Debtors' plan does not clearly state when Debtors will make the annual payments to Hand County or when those payments were to commence. If the parties cannot agree on whether Debtors have made

its liens for satisfaction of its tax claims after discharge. Had Debtors litigated Hand County's claim in a § 506(a) action or had the plan not recognized that Hand County had a lien on real property, a different conclusion may have been reached. See *In re Martin*, 130 B.R. 951, 956-61 (Bankr. N.D. Iowa 1991).

Contrary to Debtors' argument, this lien survival issue was not addressed in the two earlier tax related hearings. In the adversary between Debtors and Hand County, the Court held that the automatic stay prevented Hand County from issuing a tax deed for Debtors' land for back taxes. In the default hearing between Debtors and FCBO, the Court equitably ruled that its earlier Order granting FCBO relief from the automatic stay should be vacated because the default on the plan payments was the result of Mr. Van Zee's illness and because the default had been cured. In neither proceeding did the Court address the post-discharge status of Hand County's lien.

This decision is similar to the conclusion reached in *Timmerman*. In *Timmerman*, the debtor's plan did not provide any treatment for the county's tax claim. Thus, it was not discharged. Here, Debtors failed to provide any treatment of Hand County's tax liens and the liens will survive discharge.

Hand County's Motion to Dismiss for Failure to Pay Real Estate Taxes and Motion to Lift Automatic Stay will be denied. Cause for lifting the automatic stay or for dismissing the case has not been

all plan payments to Hand County required to date, that issue may be heard in conjunction with any disposable income hearing.

shown. Hand County's *in rem* remedies against Debtors' property will not be impaired while the discharge process in this case is completed.

Dated this ____ day of February, 1994.

BY THE COURT:

Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:

PATRICIA MERRITT, CLERK

By _____
Deputy Clerk

(SEAL)

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
Central Division

In re:)
) Bankr. Case No. 87-30128
DESMOND V. VAN ZEE)
Social Security No. 504-34-0300) Chapter 12
)
and) ORDER DENYING HAND COUNTY'S
) MOTION TO DISMISS FOR FAILURE
PATRICIA E. VAN ZEE) TO PAY REAL ESTATE TAXES AND
Social Security No. 503-64-9154) MOTION TO LIFT AUTOMATIC STAY
)
Debtors.)

In compliance with and recognition of the Memorandum of Decision Re: Hand County's Motion to Dismiss for Failure to Pay Real Estate Taxes and Motion to Lift Automatic Stay entered this day,

IT IS HEREBY ORDERED that Hand County's Motion to Dismiss for Failure to Pay Real Estate Taxes and Motion to Lift Automatic Stay is DENIED.

So ordered this ____ day of February, 1994.

BY THE COURT:

Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:

PATRICIA MERRITT, CLERK

By _____
Deputy Clerk
(SEAL)