WASHINGTON – Senators Chuck Grassley and Al Franken have introduced legislation that would reverse a Supreme Court ruling (Hall v. United States) that is leaving family farmers in Chapter 12 bankruptcy proceedings vulnerable to the IRS.

In May 2012 the Supreme Court ruled that despite Congress's express goal of helping family farmers, the language inserted into the Bankruptcy Code in 2005 conflicted with the Tax Code.

Grassley and Franken's *Family Farmer Bankruptcy Tax Clarification Act of 2012* remedies this conflict and clarifies that bankrupt family farmers reorganizing their debts are able to treat capital gains taxes owed to a governmental unit, arising from the sale of farm assets during a bankruptcy, as general unsecured claims. This bill removes the Internal Revenue Service's veto power over a bankruptcy reorganization plan's confirmation, giving the family farmer a chance to reorganize successfully.

"Chapter 12 is a proven success for farmers and their lenders. It helps the farmer and the banker sit down and work out alternatives for debt repayment so a farmer can keep his land," Grassley said. "There's no question as to congressional intent in the 2005 law. We simply need to ensure the plain language of the law says and does what we intended."

"The federal government should be doing everything it can to help family farmers keep their land, and that's what Congress meant to do in 2005," said Franken. "This legislation would fix the 2005 law and help more farmers pay their creditors, keep their land, and stay in business."

Grassley and Franken said that while they understand the legislative agenda is very full between now and the end of the year, they would like the bill to be considered yet this year, but they will press for full consideration in the new Congress should the bill not be taken up.

Chapter 12 recognizes the unique situation that family farmers face when reorganizing through bankruptcy proceedings. It was made permanent in 2005 after nearly 10 years of congressional debate to fine-tune the bankruptcy laws. Chapter 12 allows family farmers to sell portions of their farms to reorganize without capital gains taxes jeopardizing the reorganization. Before 2005, the IRS was able to collect any tax liabilities generated during a family farmer bankruptcy reorganization. Too often, when the IRS took its cut through the capital gains taxes, there was no money to pay the other creditors, like the local feed store or the local bank. So, the farmer had to sell the rest of his land and still lost the family farm.

Congress' intent in the 2005 bankruptcy reform law was to create a narrow exception through Chapter 12 that if a family farmer sold land that resulted in a capital gains liability, then the IRS's claim would not receive priority status.

Specifically, the *Family Farmer Bankruptcy Tax Clarification Act of 2012*:

- strikes the current unworkable language in the Bankruptcy Code 11 U.S.C. § 1222(a)(2)(A) and inserts a new 11 U.S.C. § 1222(a)(5);
- transforms all government claims arising as a result of the sale or transfer of post-petition farm assets into unsecured, non-priority claims, notwithstanding any language in the Internal Revenue Code to the contrary;
- provides new sections for treatment of these claims during the bankruptcy process;
- recognizes that some asset sales may occur post-confirmation;
- provides a mechanism for plan modification as a result of these sales, if used for the specified purpose of reorganization, to assist in reorganization;
- makes a technical change to 11 U.S.C. § 1228(a), which practitioners and commentators have long argued is needed.

Here is the text of Grassley's statement for the Congressional Record upon introduction of the Family Farmer Bankruptcy Tax Clarification Act.

I rise today to introduce, along with Senator Franken, the Family Farmer Bankruptcy Tax Clarification Act of 2012. This bill addresses the recent United States Supreme Court case Hall v. United States
. In a 5-4 decision, the Supreme Court ruled the provision I inserted into the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act did not accomplish what we intended. The Family Farmer Bankruptcy Tax Clarification Act of 2012 corrects this and clarifies that bankrupt family farmers reorganizing their debts are able to treat capital gains taxes owed to a governmental unit, arising from the sale of farm assets during a bankruptcy, as general unsecured claims. This bill will remove the Internal Revenue Service's veto power over a bankruptcy reorganization plan's confirmation, giving the family farmer a chance to reorganize successfully.

In 1986 Congress enacted Chapter 12 of the Bankruptcy Code to provide a specialized bankruptcy process for family farmers. In 2005 Chapter 12 was made permanent. Between 1986 and 2005 we learned what aspects worked and did not work for family farmers reorganizing in bankruptcy. One problematic area was where a family farmer needed to sell assets in order to generate cash for the reorganization. Specifically, a family farmer would have to sell portions of the farm to generate cash to fund a reorganization plan so that the creditors could receive payment. Unfortunately, in situations like this, the family farmer is selling land that has been owned for a very long time, with a very low cost basis. Thus, when the land is sold, the family farmer is hit with a substantial capital gains tax, which is owed to the Internal Revenue Service.

Under the Bankruptcy Code, taxes owed to the Internal Revenue Service receive priority treatment. Holders of priority claims must receive payment in full, unless the claim holder agrees to be treated differently. This creates problems for the family farmer who needs the cash to pay creditors to reorganize. However, since the Internal Revenue Service has the ability to require full payment, they hold veto power over a plan's confirmation, which means in many instances the plan will not be confirmed. This does not make sense if the goal is to give the family farmer a fresh start. Thus, in 2005 Congress said that in these limited situations, the taxes owed to the Internal Revenue Service could be treated as general, unsecured debt. This removed the government's veto power over plan confirmation and paved the way for family farmers to reorganize successfully.

However, in Hall v. United States, the Supreme Court ruled that despite Congress's express goal of helping family farmers, the language inserted into the Bankruptcy Code in 2005 conflicted with the Tax Code. The Hall case was one of statutory interpretation. There is no question what Congress was trying to do; rather, did Congress use the correct language? My goal, along with others at the time, was to relieve family farmers from having their reorganization plans fail because of huge tax liabilities to the federal government. Justice Breyer noted this in the dissent: "Congress was concerned about the effect on the farmer of collecting capital gains tax debts that arose during (and were connected with) the Chapter 12 proceedings themselves. . . . The majority does not deny the importance of Congress' objective. Rather, it feels compelled to hold that Congress put the Amendment in the wrong place."
Hall v. United States
, 132 S.Ct. 1882, 1897 (2012) (Breyer, J., dissenting) (internal citations and quotations omitted).

As a result of the Hall case, family farmers facing bankruptcy now find themselves caught in an unfortunate situation. The rules have changed and must be corrected in order to provide certainty and clarity in the law. The Family Farmer Bankruptcy Tax Clarification Act of 2012 will provide the clarity needed to help family farmers reorganize in bankruptcy.

This bill strikes the current language in the Bankruptcy Code, which the Supreme Court said does not work, 11 U.S.C. § 1222(a)(2)(A) and inserts a new 11 U.S.C. § 1222(a)(5). The new provision transforms all government claims arising as a result of the sale or transfer of post-petition farm assets into unsecured, non-priority claims, notwithstanding any language in the Internal Revenue Code to the contrary. The bill also provides new sections for treatment of these claims during the bankruptcy process. The bill recognizes that some asset sales may occur post-confirmation. As a result, we also provide a mechanism for plan modification as a result of these sales, if used for the specified purpose of reorganization, to assist in reorganization. Finally, we make a technical change to 11 U.S.C. § 1228(a), which practitioners and commentators have long argued is needed. This technical change is within the limited scope of this clarification bill, as it provides greater certainty and clarity that has troubled courts and practitioners alike.

We recognize the end of this session of Congress is near and the time to do something is short. However, we have been fine tuning this legislation to ensure it properly corrects the Hall case. We will seek to do what we can during the remaining Congressional calendar to fix the problem this year. Should we run out of time, then we will maintain our focus on this problem into the next year. The Family Farmer Bankruptcy Tax Clarification Act of 2012 ensures that what Congress sought to do in 2005 actually occurs. In the wake of the

Hall
decision, clarification is needed to help ensure family farmers facing bankruptcy will have a chance to reorganize successfully.

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