

1979

State of Utah et al v. I. M. C. Mint Corporation et al : Brief of Respondent

Utah Supreme Court

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IN THE SUPREME COURT OF THE STATE OF UTAH

STATE OF UTAH, and STATE OF
UTAH, by and through JOHN
KOLLY, Director, Utah State
Trade Commission,

Plaintiffs,

I.M.C. MINT CORPORATION,
HOWERT GRABAR, GEORGE E.
TWIBEY, et al.,

Defendants.

BRIEF OF RESPONDENT, RAY THOMPSON

I.M.C. MINT CORPORATION

APPEAL FROM THE ORDER OF THE DISTRICT COURT

THIRD JUDICIAL DISTRICT, SALT LAKE COUNTY

Honorable James S. Sawaya, District Judge

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FILED

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IN THE SUPREME COURT OF THE STATE OF UTAH

STATE OF UTAH, and STATE OF :
UTAH, by and through JOHN W. :
ROLLY, Director, Utah State :
Trade Commission, :
 :
Plaintiff, :
 : Case No. 16555
-vs- :
 :
I.M.C. MINT CORPORATION, :
ROBERT GRABAR, GEORGE E. :
TWIBEY, et al., :
 :
Defendants. :

BRIEF OF RESPONDENT, RAY TWELVES, RECEIVER OF
I.M.C. MINT CORPORATION

APPEAL FROM THE ORDER OF THE DISTRICT COURT OF THE
THIRD JUDICIAL DISTRICT, SALT LAKE COUNTY
Honorable James S. Sawaya, District Judge

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IN THE SUPREME COURT OF THE STATE OF UTAH

STATE OF UTAH, and STATE OF	:	
UTAH, by and through JOHN W.	:	
ROLLY, Director, Utah State	:	
Trade Commission,	:	
	:	
Plaintiff,	:	
	:	Case No. 16555
-vs-	:	
	:	
I.M.C. MINT CORPORATION,	:	
ROBERT GRABAR, GEORGE E.	:	
TWIBEY, et al.,	:	
	:	
Defendants.	:	

STATEMENT OF THE NATURE OF THE CASE

This is an appeal from a decision of the Third District Court wherein the court denied Appellant State Tax Commission's claim for priority payment of the sales and withholding tax debts of the defendant, I.M.C. Mint Corporation from the assets marshalled by the Receiver of the estate and property of said defendant. The Receiver is the Respondent on this appeal.

DISPOSITION IN LOWER COURT

On March 15, 1979, a hearing was held before the Honorable James S. Sawaya upon the Receiver's objections to the priority claims of the Utah State Tax Commission for certain sales and withholding taxes and penalties in connection therewith. Memoranda of law were filed by counsel for

the Receiver and the State Tax Commission. After due consideration, the district court issued an order sustaining the Receiver's objections to these priority claims, from which order the Tax Commission now appeals.

RELIEF SOUGHT ON APPEAL

Appellant seeks a reversal of the Third District Court's determination and a ruling that the state's claims for sales and withholding taxes be declared superior to those claims of general, unsecured creditors. Respondent seeks an affirmance of the order below.

STATEMENT OF THE FACTS

On June 21, 1974, a receivership was instituted at the instance of the Consumer Fraud Division of the Utah Attorney General's office and a Receiver appointed of the estate and property of I.M.C. Mint Corporation. (R. 12-13). Subsequently, the Tax Commission of the State of Utah filed claims of preferred debt with the Receiver in the amounts of \$12,380.79 for unpaid sales tax (R. 440) and \$7,538.22 for unpaid withholding of income tax (R. 441).

The Receiver filed objections to those claims on the following basis:

1. The claims had no priority over claims of general creditors except to the extent that lien status was conferred by statute upon the tax debts.

2. There was no lien in favor of the Tax Commission for either unpaid sales taxes or unpaid withholding taxes as of the date the receivership was instituted, there having been no warrant for either sales or withholding taxes filed by the Tax Commission pursuant to Sections 59-15-11 and 59-14-16, U.C.A. 1953, as amended.

3. The claim for withholding tax included penalties in the amount of \$1,620.20 and the claim for sales tax included penalties in the amount of \$60.00, neither of which were properly allowable. (R. 438-41).

A hearing on the objections of the Receiver was held before the Honorable James S. Sawaya on March 15, 1979. (R. 485-6). Arguments were heard and the Judge granted the request of the tax commission's counsel for leave to file a written memorandum of law on the issues involved with the state's claim for priority over general, unsecured creditors. Memoranda were filed by both parties. (R. 455-484). An order was issued sustaining the Receiver's objections. (R. 485).

ARGUMENT

POINT I

THE EXISTENCE OF A LIEN IS THE ONLY BASIS
UPON WHICH THE TAX CLAIMS ASSERTED HEREIN
CAN BE GIVEN PRIORITY OVER THE CLAIMS OF
OTHER CREDITORS.

The central issue on this appeal is whether or not a lien existed in favor of the Tax Commission for unpaid sales taxes or unpaid withholding taxes and penalties in connection

therewith on the date the receivership was instituted even though warrants had not as yet been filed. Such a lien must arise, if at all, pursuant to the statutory provisions conferring lien status on certain tax debts.

In its brief, the Commission argues that tax claims are inherently superior to other claims, yet the Commission cites no authority either in the Utah case law or in the Utah statutes which would suggest that tax claims have some inherent priority over other claims irrespective of any priority status specifically conferred by statute upon such claims.

In support of its inherent superiority claim, the Commission cites two decisions of the United States Supreme Court, Marshall v. New York, 254 U.S. 380 (1920), and Michigan v. Michigan Trust Co., 286 U.S. 334 (1932). In each of these cases the Supreme Court specifically identified the issues involved as issues of local law and therefore, deferred to the local statutory provisions and case law.

Whether the priority enjoyed by the state of New York is a prerogative right or merely a rule of administration is a matter of local law. Being such, the decisions of the highest court of the state as to the existence of the right and its incidents will be accepted by this court as conclusive. Marshall v. New York, 254 U.S. 380 at 384-85 (1920).

We are not required to choose from these diversities the construction that

would appeal to us as the most consonant with reason if choice were wholly free. Choice, as it happens, is not free, for our task is to ascertain the meaning of a Michigan statute, and as to that the courts of the State, if they have spoken, pronounce the final word. Michigan v. Michigan Trust Co., 286 U.S. 334 at 342 (1932).

The local law to which Appellant refers, however, lends no support to Appellant's argument and provides no guidance to this Court in determining the issues at hand. The cases of Hanson v. Burris, 86 Utah 424, 46 P.2d 400 (1935), affirmed in Ingraham v. Hanson, 297 U.S. 378 (1936), Robinson v. Hanson, 75 Utah 30, 282 P. 782 (1929), and Union Cent. Life Ins. Co. v. Black, 67 Utah 268, 247 P. 486 (1926) cited in Appellant's brief do not address the issue of when a lien based upon unpaid taxes arises, which is the central issue of this appeal, but rather address the priority among admittedly existing liens.

The only decision of the Utah Supreme Court cited by Appellant which addresses the issue herein is Phillips Petroleum Co. v. Wagstaff, 22 Utah 2d 177, 450 P.2d 100 (1969), which decision Appellant argues should be overruled. (Brief of Appellant p.21).

It should be noted that the case of Michigan v. Michigan Trust Co., supra, cited on pages 5 and 18 of Appellant's

brief addressed an issue which is different and distinct from the issue under discussion herein. In Michigan a receivership was established to continue the corporate business rather than to aid in the dissolution of the corporation and the liquidation of its business, which is the purpose of the I.M.C. Mint Corporation's receivership. In that context, the Court found that franchise taxes accruing for the most part during the pendency of the receivership, constituted a necessary cost of continuing the business and thus was an expense of the receivership having priority over other debts.

Distinctions have been drawn between receivers appointed to carry on the business of a corporation with a view to the continuance of its corporate life, and receivers appointed in aid of the dissolution of the corporation or the liquidation of its business.

* * * *

Viewing the receivership in its true light as one, not to wind up the corporation, but to foster the assets, we think the annual taxes accruing while the receiver was in charge must be deemed expenses of administration and therefore charges to be satisfied in preference to the claims of general creditors. They are so treated in the order by which the receiver was appointed. By the order the receiver is directed in continuing the business to pay taxes and rentals and any other expenses necessary to enable the business to go on, and to give such payments priority over other debts and obligations. These privilege fees were charges of the nature there described. Michigan v. Michigan Trust Co., 286 U.S. 334 at 341-44 (1932).

Similarly in Coy v. Title Guarantee & Trust Co., 212 F. 520 (D.Ct. Oregon 1914) aff'd 220 F. 90 (9th Cir. 1915), which is relied on and cited by the court in Michigan, the court addressed the issue of the receiver's obligation to pay personal property taxes assessed and accrued during the pendency of the receivership. In holding that the receiver had a duty to pay such taxes prior to the payment of other claims the Ninth Circuit in Coy relied on various treatises on receivers, one of which stated:

Taxes levied upon personal property in the hands of a receiver become a charge upon the estate, and are properly payable by the receiver as a part of the costs and expenses of the administration of the trust. High on Receivers, §881a (4th Ed.) as quoted in Coy v. Title Guarantee & Trust Co., 220 F. 90, 92 (9th Cir. 1915).

It is a well established rule that costs and expenses of a receivership constitute a first charge against the property or funds in receivership. 66 Am. Jur. 2d, Receivers §280 at 98. The payment of taxes accruing during the pendency of the receivership and other costs or expenses of administration of the receivership is a separate and distinct issue from that of the priority of taxes such as those at issue herein which accrued prior to the institution of receivership proceedings and which cannot be categorized as an administration expense.

Thus, the cases cited by the Appellant in its first point of argument are inapplicable and afford the court no assistance or guidance in the determination of the issue at hand.

POINT II.

THE ACCRUAL OF SALES AND WITHHOLDING TAXES ALONE IS INSUFFICIENT TO ESTABLISH A LIEN AGAINST THE PERSONAL PROPERTY OF I.M.C. MINT CORPORATION WITHOUT THE FILING OF A WARRANT.

As conceded by the Commission, the sales and withholding taxes upon which this controversy are based, accrued prior to the appointment of the Receiver, but no warrant based thereon was filed or docketed prior to the institution of the receivership.

Rule 66(f) of the Utah Rules of Civil Procedure requires a receiver to discharge all taxes constituting a lien on personal property held by the receiver before such property can be sold or transferred:

Payment of Taxes Before Sale or Hypothecation of Personal Property. Before any personal property coming into the hands of a receiver may be sold, transferred or hypothecated, such receiver shall pay and discharge any and all taxes constituting a lien thereon, legally levied by any taxing unit of the state, and shall file with the court having jurisdiction of such receivership, receipts or other competent evidence showing the full payment and discharge of any and all such taxes, provided, that in a case where no sufficient liquid assets are at the time of the proposed sale, transfer or hypothecation, in the hands of such receiver, the court having jurisdiction of such receivership may authorize such sale, transfer or hypothecation to be made prior to the payment and discharge of such taxes, but immediately

upon receipt of the consideration for such sale, transfer or hypothecation such receiver shall pay and discharge all such liens, taxes, and within 10 days thereafter shall file with the court receipts of other competent evidence showing the full payment and discharge of all such taxes. (Emphasis added).

The pivotal issue is obviously whether or not the tax claims asserted herein by the commission constitute a lien on the personal property held in receivership.

The Commission argues that the mere accrual of the tax constitutes a lien irrespective of whether or not a warrant has been filed, citing Section 59-14A-44(e) as establishing a lien to secure the payment of withholding taxes and Section 59-15-10 as establishing a lien for sales tax. ^{1/} Although these sections appear on their face to establish liens for sales and withholding taxes, they must be read in the light of subsequent sections in the sales and withholding tax chapters which provide for the issuance of warrants.

^{1/} It should be noted that §59-15-10 only applies to a "... proprietor who shall sell out his business or stock of goods or shall quit business." Whether or not an involuntary receivership constitutes a selling out or a quitting of business is highly questionable. It is, however, an issue which is not specifically addressed because no lien exists, in any event, without the filing of a warrant.

Section 59-14A-79(c-e) of the Utah Code Annotated
provides as follows:

(c) If any person liable under this act for the payment of any tax, addition to tax, penalty or interest neglects or refuses to pay the same within ten days after notice and demand for payment has been given to such person under subsection (b) of this section, the tax commission may issue a warrant in duplicate under its official seal directed to the sheriff of any county of the state commanding him to levy upon and sell such person's real and personal property for the payment of the amount assessed, plus the cost of executing the warrant, and to return such warrant to the tax commission and pay to it the money collected by virtue thereof within sixty days after the receipt of the warrant. If the tax commission finds that the collection of the tax or other amount is in jeopardy, notice and demand for immediate payment of such tax may be made by the tax commission and upon failure or refusal to pay such tax or other amount the tax commission may issue a warrant without regard to the ten-day period provided in this subsection. See section 59-14A-91 for provisions relating to jeopardy assessment procedure.

(d) Any sheriff who receives a warrant under subsection (c) of this section shall within five days thereafter file the duplicate copy with the clerk of the district court of the appropriate county. The clerk of such court shall thereupon enter in the judgment docket, in the column for judgment debtors, the name of the taxpayer mentioned in the warrant and, in appropriate columns, the tax or other amounts for which the warrant is issued and the date when such copy is filed; and such amount shall thereupon be a binding lien upon the real, personal and other property of the taxpayer to the same extent as other judgments duly docketed in the office of such clerk.

(e) When a warrant has been filed with the county clerk, the tax commission shall, in the right of the people of the State of Utah, be deemed to have obtained judgment against the taxpayer for the tax or other amounts.

Nearly identical language is found in Section 59-15-11 of the Utah Code Annotated in relation to sales tax.

In Phillips Petroleum Co. v. Wagstaff, 22 Utah 2d 177, 450 P.2d 100 (1969) the Utah Supreme Court interpreted language identical to the withholding tax provisions cited above and held:

. . . that the lien of a state for delinquent withholding taxes begins to run at the time notice thereof is given by filing the warrant. 450 P.2d at 102.

The Receiver submits that the Phillips case mandates the conclusion that the tax claims asserted herein did not constitute liens until warrants were filed. Inasmuch as the warrants were not filed at the institution of the receivership, no lien existed and therefore the tax claims have no priority.

The Commission attempts to avoid the effect of the clear holding in the Phillips case by arguing first that other jurisdictions have arrived at different interpretations of similar statutory language; second, that the interpretation in Phillips is somehow discredited by the legislative reenactment of language identical to the language interpreted in Phillips;

third, that Phillips is distinguishable from the present case; and fourth, that Phillips should be overruled.

Generally, reference to the decisions of other jurisdictions is only justified where there is no controlling authority in the court's own jurisdiction. Even assuming that such reference is justified in this case despite the Phillips opinion, the interpretations of statutory provisions relating to the creation of tax liens by courts in other jurisdictions are only relevant to the extent that the statutory provisions of those jurisdictions resemble the Utah statutes.

The Commission cites District of Columbia v. Hechinger Properties Co., 197 A. 2d 157 (D. C. Ct. App. 1964) for the proposition that the existence of a tax lien for delinquent taxes does not depend upon the filing of a warrant. The Commission points out the similarities between the Utah Statutes and the statutes of the District of Columbia but fails to note the differences. These differences are in fact determinative of the question whether or not tax claims have priority as to property in the hands of a receiver. There was no receivership pending in the Hechinger case and therefore, the case is factually dissimilar to the present case. If a receivership had been pending in that case as is pending in the present case, the

statutes of the District of Columbia specifically provide that all taxes due and payable shall be paid by the receiver before any payment is made to other claimants.

The District of Columbia statute reads as follows:

Whenever the business or property of any person subject to tax under the terms of this chapter, shall be placed in receivership or bankruptcy, or assignment is made for the benefit of creditors, or if said property is seized under distraint for property taxes, all taxes, penalties, and interest imposed by this chapter for which said person is in any way liable shall be a prior and preferred claim. Neither the United States marshal, nor a receiver, assignee, or any other officer shall sell the property of any person subject to tax under the terms of this chapter under process or order of any court without first determining from the Collector the amount of any such taxes due and payable by said person, and if there be any such taxes due, owing, or unpaid under this chapter, it shall be the duty of such officer to first pay to the Collector the amount of said sale before making any payment of any moneys to any judgment creditor or other claimants of whatsoever kind or nature. * * * (Emphasis added). D. C. Code §74-2609 as cited in District of Columbia v. Hechinger Properties Co., 197 A.2d 157, 159 fn. 5 (D.C. Ct. App. 1964).

Under the District of Columbia statute, tax claims would have priority under the circumstances existing in the

present case irrespective of whether or not they constitute liens. These statutes should be contrasted with the Utah Rule 66(f) which requires the receiver to discharge only those taxes which constitute a lien on the property held by the receiver before paying other claims.

Utah has no provisions similar to those of the District of Columbia, dealing with the priority tax claims in receivership. The only Utah statutes which confer any priority status on tax claims are those cited above which have been interpreted by the Utah Supreme Court as conferring a lien only after the filing of a warrant.

Also, the District of Columbia statutes specifically provide that the lien for unpaid withholding taxes ". . . shall accrue on the date that the amounts were withheld." D.C. Code 1961, §47-15869(f)(2). In contrast, Utah Code Annotated, Section 59-14A-44(e) which establishes a lien for withheld taxes, does not specify an accrual date.

The Commission argues on page 15 of its brief that the enactment in 1973 of Sections in Chapter 14A using the same language as the parallel provisions on tax liens and warrants in Chapter 14 somehow discredits the Phillips decision as a correct interpretation of the legislative intent. Actually, the fact that the legislature did not change the language in light of t

Phillips decision would indicate that the legislature acquiesced in the interpretation of that language by the Utah Supreme Court.

A further indication of the legislative acquiescence in this Court's interpretation of the language of the statute as then constituted, is the apparent recognition by the legislature, subsequent to the Phillips decision, of the need for a specific provision indicating the date a tax lien accrues or arises. In the 1979 General Session, the Utah Legislature adopted and the Governor has subsequently signed House Bill No. 308 which added the following provision to Section 59-10-22 of the Utah Code Annotated:

2. If any person liable to pay the Utah sales and withholding 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 State of Utah upon all property and rights to property, whether real or personal, belonging to such person.

3. Unless another date is specifically fixed by law, the lien imposed for state taxes shall arise at the time the assessment is made and shall continue until the liability for the amount so

assessed (or a judgment against the taxpayer arising out of such liability) is satisfied or becomes unenforceable by reason of lapse of time.

This amendment resolves controversies such as this one as to the accrual date of a tax lien in the future and thus the dire consequences of Phillips decision forecast by the Commission on page 20 of its Brief will not come to pass. However, the Phillips decision still controls controversies such as the present one arising under the prior statutes which do not specify an accrual date other than the date of the filing of a warrant.

Similarly unpersuasive, is the Commission's assertion that the Phillips case is distinguishable from the present case and therefore the Phillips opinion is inapplicable. The Commission attempts to distinguish the Phillips case on the basis that a mortgagee relies on the public record to indicate clear title, whereas general creditors do not rely on public records in extending credit. The assumption that general creditors extend credit without checking public records is not a reasonable assumption. It is not reasonable to assume that a general creditor of I.M.C. Mint Corporation would extend as much as \$385,000, as one creditor has done, without thoroughly investigating that company's financial responsibility through the public records in the Secretary of State's office and the

County Clerk's office. General creditors are entitled to rely on these records to the same extent as secured creditors.

If liens are permitted to arise and exist without any reflection thereof in the public record, it would impair the practice of extending credit by general creditors just as seriously as it would impair the extension of credit by secured creditors.

In Phillips, this Court based its holding that a lien arises only upon the filing of a warrant on the following consideration:

. . . the only record as to delinquent withholding taxes rests wholly within the knowledge of the employer until such time as the Tax Commission makes its determination as to the amount due and delinquent and files its warrant with the appropriate county clerk. 450 P.2d at 102.

The concern evidenced by this Court over the existence of secret liens is applicable to all forms of extension of credit. This concern is reflected in the legislative policy embraced by the filing provisions of Article Nine of the Utah Uniform Commercial Code.

The argument that the Phillips case should be overruled requires little comment. The Commission asserts that this Court ignored the plain language of the statute. In fact, this Court, faced with a split of opinion among district courts, gave

careful consideration to the interrelation of the statutory provisions relating to liens and warrants. This Court interpreted that statutory language to provide that a lien does not arise without the filing of a warrant. The legislature has apparently acquiesced in that interpretation and found it necessary to amend the statutes in order to provide for the accrual of a lien prior to the filing of a warrant. If the legislature intended under the prior statute to provide for the accrual of a lien prior to the filing of a warrant, the legislature did not accomplish that purpose. In Phillips, this Court was bound to interpret the statute as it then read.

POINT III.

THE TRIAL COURT'S DENIAL OF CLAIMS BY THE TAX COMMISSION FOR PENALTIES AND EXCESS INTEREST SHOULD BE UPHELD.

The Tax Commission asserted in the court below that interest, penalties and costs for a receiver's nonpayment of taxes accruing during the receivership constitute a lien on the property and are payable by the Receiver. (R. 468-9). This assertion and the citations thereto, apply only to penalties and interest relating to taxes which accrued during the receivership and are inapplicable to penalties and interest on taxes accruing prior to the receivership. This distinction has been discussed previously in Point I of this Brief. The Commission has cited no authority which imposes a duty on the

Receiver to pay penalties and interest on taxes which accrued prior to the appointment of a receiver.

A receivership proceeding, like a bankruptcy proceeding is equitable in nature, and thus the court has considerable discretion in determining the equities of various charges and claims. In bankruptcy, no penalties or excessive interest for the nonpayment of taxes are allowed as against the funds held by the trustee ^{2/} nor is interest allowed after the date the petition in bankruptcy is filed. ^{3/} In the context of a receivership, as in the context of bankruptcy, the assessment of penalties and excess interest against funds held by the receiver has no impact on the entity which failed to pay the taxes but rather has the effect of penalizing the creditors of that entity. Thus, the punitive effect of such penalties is lost. Accordingly, the trial court exercised its equitable discretion and denied penalties and excessive interest. This Court should uphold that exercise of discretion.

^{2/}

11 U.S.C.A. §93(j); 3 Collier on Bankruptcy, ¶57.22 [2.1] at p. 391-2.

^{3/}

3A Collier on Bankruptcy, ¶63.16 [2] at p. 1864-70.

The case of Ralph Child Construction Co. v. State Tax Commission, 12 Utah 2d 53, 362 P.2d 422 (1961) illustrates in another context this policy that penalties should not be assessed against persons other than the wrongdoer. Not only are pre-receivership penalties inappropriate and inequitable, but post-receivership penalties attributable to pre-filing taxes are particularly inappropriate. It would be intolerable for a court-appointed officer to scrutinize, challenge and disallow a tax claim at the peril of paying penalties if he is in error or if there should be inadequate funds in the receivership to pay the claim if uncontested. This is dramatized even more in this case where the tax claims have no priority over other claims and could not be paid until such time as the Tax Commission's proportionate interest in the subject funds could be determined and satisfied.

CONCLUSION

The existence of a lien is the only basis upon which the tax claims asserted herein can be given priority over the claims of other creditors. The Utah statutes imposing liens for tax claims have been interpreted by this Court as requiring the filing of a warrant before such liens arise. No warrants were filed with respect to those claims asserted

herein by the Tax Commission prior to the appointment of the Receiver. Thus, no liens as to those tax claims existed and therefore, those tax claims have no priority.


Therefore, the determination of the District Court that these tax claims have no priority was a correct application of the relevant statutes and case law, as was its denial of the Tax Commission's claim for penalties, and for interest accruing subsequent to the institution of the receivership and such determination should be upheld.

Respectfully submitted this 15th day of October, 1979.

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