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# *In re J.J. Re–Bar Corp.*: The Application of the Anti-Injunction Act

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## Introduction

The Anti–Injunction Act[1] is a provision of the U.S Code that prohibits any court from impeding the Internal Revenue Service from collecting an assessed tax. The Circuits have applied the Anti–Injunction Act to bankruptcy proceedings in two different ways. When the IRS seeks to assess a tax against a corporate fiduciary of a bankrupt corporation, as when the IRS tries to collect a penalty associated with unpaid payroll taxes, the Circuits have held that the Anti–Injunction Act allows the IRS to collect the funds it is entitled to without any interference. However, when the IRS attempts to collect unpaid income taxes from debtors without allowing the Bankruptcy Court the opportunity to directly assess the validity of the debt, the Circuits have found that the Anti–Injunction Act does not prohibit a court from enjoining the IRS's collection efforts. Two cases illustrate these different applications of the Anti–Injunction Act: *J.J. Re–Bar Corp. v. United States*, 644 F.3d 952 (9th Cir. 2011) and *Bostwick* v. *United States*, 521 F.2d 741 (8th Cir. 1975).

[1] 26 U.S.C. § 7421(a) (2006) (stating "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed.")

In *J.J. Re–Bar Corp. v. United States* (*In re* J.J. Re–Bar Corp.)[2] the Ninth Circuit held that the Anti–Injunction Act precludes a court from barring the post-confirmation collection of a trust fund recovery penalty ("TFRP")[3] from the responsible officers of a debtor corporation by the IRS.[4] The Appellant in *J.J. Re–Bar Corp.* raised two novel and ultimately unsuccessful arguments to overcome the effect of the Anti–Injunction Act. First, the appellant argued that the specific terms of a confirmed Chapter 11 plan can be used to overcome the Anti–Injunction Act.[5] Second, the appellant argued that a TFRP penalty could not exist without an underlying payroll tax deficiency, and therefore, J.J. Re–Bar Corp. was the "primary obligator" of the debt and thus protected by the debtor's reorganization plan.[6]

The Ninth Circuit, relying on a line of cases, including *Davis v. United States*[7] and *American Bicycle Ass'n v. United States,*[8] determined that because TFRP liability arose from the officers' willful conduct, the penalties were the obligations of the officers themselves and not the debtor corporation.[9] In reaching its decision, the Ninth Circuit relied on a line of reasoning adopted by the Fourth[10], Seventh[11], and Third[12] Circuits, which have concluded that the

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[2] 644 F.3d 952 (9th Cir. 2011).
[3] 26 U.S.C. § 6672 (2006) (providing any responsible person required to collect and pay payroll taxes who fails to do so may be assessed a penalty equal to the total amount of payroll tax evaded).
[4] *In re* J.J. Re–Bar Corp., 644 F.3d 952, 956–57.
[5] *In re* J.J. Re–Bar Corp., 644 F.3d 952, 956 n. 3 (reading plan to provide clear, specific, and unambiguous discharge of § 6672 liability).
[6] *Id* at 956.
[7] 961 F.2d 867 (9th Cir. 1992).
[8] 895 F.2d 1277 (9th Cir. 1990).
[9] *In re* J.J. Re–Bar Corp., 644 F.3d 952, 957.
[10] Clark v. Baker (*In re* Heritage Village Church & Missionary Fellowship), 851 F.2d 104, 105 (4th Cir. 1988) (finding "no express provision in the Bankruptcy Code indicating congressional intent that the Code supersede the Anti-Injunction Act.").
[11] LaSalle Rolling Mills v. U.S. Dep't of Treasury (*In re* La Salle Rolling Mills), 832 F.2d 390, 392 (7th Cir. 1987) (holding Anti-Injunction Act prevents issuance of injunction in Bankruptcy proceedings).

Bankruptcy Code does not provide a specific provision that overrides the Anti–Injunction Act and the fiduciaries of a bankrupt corporation cannot use the protections afforded their failed company to insulate themselves from liability.[13]

On the other hand, in *Bostwick v. United States*, the Eighth Circuit concluded that "the Bankruptcy Court must have the power to enjoin the assessment and/or collection of taxes in order to . . . fulfill the ultimate policy of the Bankruptcy Act."[14] The Eighth Circuit relied heavily on the general grant of authority provided to bankruptcy courts in 11 U.S.C § 35[15] to prevent the collection of unpaid taxes even in the face of the Anti–Injunction Act.[16] This sentiment was picked up by the concurring opinion of a Third Circuit Judge who concluded:

> Sections 2(a)(2A), 2(a)(15), and 17(c) of the old Bankruptcy Act gave the bankruptcy court jurisdiction to adjudicate the dischargeability of a tax debt and to make all necessary orders in exercise of this jurisdiction. I agree with the opinion of the United States Court of Appeals for the Eight Circuit in Bostwick v. United States [citation omitted] that these sections evidence congressional intent that the comprehensive statutory scheme governing bankruptcy overrides the general policy represented by the anti-injunction statute [citation omitted] and that section 7421(a) does not prohibit the bankruptcy court from granting injunctive relief in exercising its power to determine questions of dischargeability.[17]

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[12] Becker's Motor Transp. Inc., v. U.S. Dep't of Treasury (*In re* Becker's Motor Transp.), 632 F.2d 242, 247 (3rd Cir. 1980) (finding absent express authorization Bankruptcy Courts cannot issue declaratory relief to prevent collection of taxes by IRS).

[13] *See In re* Szwyd, 408 B.R. 547, 552 (Bankr. D. Mass. 2009) (outlining reasoning of the circuits).

[14] Bostwick v. U.S. 521 F.2d 741, 744 (8th Cir. 1975).

[15] 11 U.S.C. § 35(c) (1976). This section of the bankruptcy code was repealed and replaced by 11 U.S.C. § 105 (2006).

[16] Bostwick, 521 F.2d 741 at 744. ("[W]e do not believe that the 'anti-injunction statute' is relevant . . . inasmuch as Congress has evidenced an intention to enact a complete scheme governing bankruptcy which overrides the general policy represented by the 'anti-injunction' act.").

[17] Becker's Motor Transp. v. Dep't of Treasury, 632 F.2d 242, 251 (3rd Cir. 1980) (Chief Judge Seitz concurring). As indicated *supra* at note 11 the majority of the same court concluded that since there was no express provision of the bankruptcy code that authorized the courts to override the anti-injunction the courts were without authority to issue an injunction.

Overall, the Circuits appear to be concerned with providing debtors with the maximum protections provided by the Bankruptcy Code while prohibiting those protections to extend to individuals other than the debtor before the court. When corporate fiduciaries seek to extend the debtor corporation's protections to themselves, the Circuits appear to be hesitant to step on the IRS's toes by enjoining its collection efforts. However, when the IRS does not abide by the due process procedures of the Bankruptcy Court and attempts to collect unpaid taxes from a debtor directly, the Circuits are more willing to ignore the strict wording of the Anti–Injunction Act and prevent the IRS from assessing any taxes against the debtors before the court.

**Applicable Statutes**

The Anti–Injunction Act provides that, "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed."[18] Generally this provision of the United States Code has been interpreted to mean that bankruptcy courts are prohibited from enjoining the IRS from collecting taxes.[19] It appears that the majority of discourse surrounding the interpretation of I.R.C. § 7421 occurred in the late 1980s after the repeal of 11 U.S.C. § 35 and its replacement with 11 U.S.C § 105.[20] Section 35 provided Bankruptcy Courts with their general grant of authority to decide matters placed before them, including a specific provision

[18] 26 U.S.C. § 7421(a) (2006).
[19] *See* American Bicycle Ass'n v. U.S. (*In re* American Bicycle Ass'n.), 895 F.2d 1277 (9th Cir. 1990); Becker's Motor Transp. Inc., v. U.S. Dep't of Treasury (*In re* Becker's Motor Transp.), 632 F.2d 242, (3rd Cir. 1980); LaSalle Rolling Mills v. U.S. Dep't of Treasury (*In re* La Salle Rolling Mills), 832 F.2d 390, 392 (7th Cir. 1987).
[20] *In re* H & R Ice Inc., 24 B.R. 28, (Bankr. W.D. Mo. 1982) (holding that bankruptcy court could enjoin the assessment of a tax penalty). The district court reversed its opinion in *In re* Booth Two Services, Inc., 53 B.R. 1014, 1014 (W.D. Mo. 1985).

dealing with tax debts.[21] While section 105 provides the court with the authority to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title," it does not provide the specific authority to discharge tax debt that was present in section 35.[22]

The tax at issue in *In re J.J. Re–Bar Corp*. arises from I.R.C §§ 3102, 3402 which require employers to withhold income and social security taxes from employees' wages.[23] These wages must be held "in a special fund in trust for the United States."[24] An employer is required to deposit the funds held in trust for the United States monthly into a federally approved bank and remit those funds to the IRS in full by the end of each fiscal quarter.[25] Employers are entitled to a tax credit for the withheld funds even if those funds are never turned over to the government.[26] To facilitate payment of trust fund taxes, I.R.C. § 6672 permits the IRS to impose a trust fund recovery penalty or TFRP equal to the unpaid portion of the trust fund taxes on the individual responsible for their payment.[27]

In order for a person[28] to be held liable under I.R.C. § 6672, the IRS must demonstrate that he or she (1) was a responsible person; and (2) acted willfully in failing to remit withheld payroll taxes.[29] Under I.R.C. § 6671, the assessment of any penalty will be treated as a tax.[30]

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[21] 11 U.S.C. § 35 (1976). This was the last version of the US Code that section 35 appeared in.
[22] *Compare* 11 U.S.C. §35 (1976) *with* 11 U.S.C. §105 (2006).
[23] 26 U.S.C. §§ 3102, 3402 (2006).
[24] 26 U.S.C. § 7501(a) (2006).
[25] *See* 26 U.S.C. §§ 3102, 3402, 6151, 6302, 7501 (2006). *See also* Matter of Hanshaw, 94 B.R. 753, 755 (Bankr. M.D. Fl. 1988)
[26] American Bicycle Assoc. v. U.S. (*In re* American Bicycle Assoc.), 895 F.2d 1277, 1278 n.2 (9th Cir. 1990) (citing Slodov v. U.S., 436 U.S. 238, 243 (1978)).
[27] *See* 26 U.S.C §6672 (2006).
[28] 26 U.S.C. §6671(b) (2006) ("[t]he term 'person', as used in this subchapter, includes an officer or employee of a corporation . . . who as such officer [or] employee is under a duty to perform the act in respect of which the violation occurs.").
[29] 26 U.S.C. §6672 (2006). *See* Purcell v. U.S.. 1F.3d 932, 936 (9th Cir. 1993).

Therefore, liability under section 6672 creates an obligation "separate and distinct" from the underlying trust fund taxes that is in the nature of an independently assessed tax against the responsible officers of the corporation.[31]

**When the IRS Assesses a Tax Against a Corporate Fiduciary**

In the recent case of *In re* J.J. Re–Bar Corp. a common scenario unfolded. In 1974, Joseph and Joanne Skokan founded J.J. Re–Bar Corp.[32] The husband and wife team became the sole shareholders of the company, which was engaged in re-bar fabrication in the construction business.[33] J.J. Re–Bar Corp. failed to pay federal employment taxes from 1995 to 1997 and filed a Chapter 11 petition for reorganization in 1998.[34] The IRS filed a claim of $833,269.00 against J.J. Re–Bar Corp. for its unpaid payroll taxes, which was subject to change upon completion of an audit.[35] A final plan of reorganization was confirmed by the bankruptcy court, which provided that the debtor, J.J. Re–Bar Corp., would be completely discharged from all its obligations upon the confirmation of the plan of reorganization.[36]

The IRS's audit resulted in a final assessment of liability against J.J. Re–Bar Corp. of $3,111,035.44.[37] In 2007 the IRS began investigating the possibility of assessing a TFRP against Joseph and Joanne Skokan, and the Skokans responded by filing a motion in the United States Bankruptcy Court for the Eastern District of California, on behalf of J.J. Re–Bar Corp., seeking

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[30] 26 U.S.C. §6671(a) (2006) ("The penalties and liabilities provided by this subchapter shall be . . . assessed and collected in the same manner as taxes.").
[31] *See* Duncan v. Comm'r, 68 F.3d 315, 318 (9th Cir. 1995). *See also* SEC v. Sec. Nw., Inc., 573 F.2d 622, 626 (9th Cir. 1978) (holding obligation from section 6672 " is 'a totally independent liability from that of the corporation.'" (quoting Teel v. U.S., 529 F.2d 903, 906 (9th Cir. 1976)).
[32] *In re* J.J. Re–Bar Corp., 644 F.3d 952 at 953.
[33] *Id*.
[34] *In re* J.J. Re–Bar Corp., 644 F.3d 952 at 953.
[35] *Id*.
[36] *Id.* at 954.
[37] *See Id.*

to enforce the plan of reorganization and hold the IRS in contempt.[38] Both the bankruptcy court and the Bankruptcy Appellate Panel of the Ninth Circuit (the "BAP") denied J.J. Re–Bar's motion and concluded that the Anti–Injunction Act prevented the Bankruptcy Court from exercising its jurisdiction in the matter.[39]

J.J. Re–Bar Corp. offered two main arguments. First, the appellant argued that the specific terms of a confirmed Chapter 11 plan can be used to overcome the Anti–Injunction Act.[40] Second, the appellant argued that a TFRP penalty could not exist without an underlying payroll tax deficiency, and therefore, J.J. Re–Bar Corp. was the "primary obligator" of the debt and thus protected by the debtor's reorganization plan.[41] The Ninth Circuit concluded that the plain meaning of J.J. Re–Bar Corp.'s plan of reorganization did not provide for the discharge of any potential TFRP liability and even if the plan had done so, such a provision would be found invalid as against public policy.[42] The Ninth Circuit also held that section 6672 "operates as a penalty by creating an obligation, *separate and distinct* from the underlying tax obligation."[43] Therefore TFRP liability is distinct from the original tax debt, precluding any argument that the

[38] *Id.*
[39] *Id.* at 955.
[40] *Id at* 956 n. 3 (reading plan to provide clear, specific, and unambiguous discharge of § 6672 liability).
[41] *Id* at 956.
[42] *In re* J.J. Re–Bar Corp., 644 F.3d 952 at 956 ("[A] debtor corporation '[can] not be permitted to do indirectly what it cannot by law accomplish directly. Allowing a debtor to avoid or forestall the tax liabilities of its officers by use of a Plan would violate the policy of the Anti–Injunction Act as readily as allowing the debtor to avoid such liability by filing a suit for injunctive relief.'") (quoting U.S. v. Condel, Inc. (*In re* Condel, Inc.), 91 B.R. 79, 82 (B.A.P. 9th Cir. 1988)).
[43] *In re* J.J. Re–Bar Corp., 644 F.3d 952, 957. (quoting Duncan v. Comm'r, 68 F.3d 315, 318 (9th Cir. 1995).

tax debt of J.J. Re–Bar Corp. and the section 6672 penalty assessed against the Skokans "are one and the same."[44]

Overall, it appears that the Skokans fought the assessment of a TFRP so hard because of the $3.1 million price tag associated with it. The legal arguments advanced by counsel for J.J. Re–Bar Corp. were not only novel but flew in the face of nearly thirty years of established legal precedent in the Ninth Circuit.

**When the IRS Assesses a Tax Against a Debtor**

In 1975, the Eight Circuit concluded that, "the 'anti–injunction statute' is [ir]relevant . . . inasmuch as Congress has evidenced an intention to enact a complete scheme governing bankruptcy which overrides the general policy represented by the 'anti–injunction' act."[45] The facts surrounding the Eight Circuit's decision are rather simple. The Bostwicks filed petitions in bankruptcy in February of 1973.[46] The United States was listed as a creditor for unpaid Federal income taxes for the years 1963–67.[47] The United States did not participate in the bankruptcy proceeding and the referee ordered a discharge of the Bostwicks' tax debt.[48] The United States filed a motion in June of 1973 seeking to dismiss the discharge for lack of jurisdiction.[49] In July of 1973 the Bostwicks sought an injunction to prevent the United States from instituting collection methods until dischargeability was determined by the bankruptcy court.[50] The bankruptcy court decided that it had jurisdiction to determine the discharge of tax debts and

[44] *In re* J.J. Re–Bar Corp., 644 F.3d 952, 957.
[45] Bostwick v. U.S., 521 F.2d 741, 744.
[46] *Id.* at 742.
[47] *Id.*
[48] *Id.*
[49] Bostwick v. U.S., 521 F.2d 741, 742.
[50] *Id.*

enjoined the United States from pursuing any collection proceedings against the Bostwicks until the question of discharge was determined by the bankruptcy court.[51]

The Eight Circuit determined that 11 U.S.C. §35(c)[52] granted the bankruptcy court the authority to "determine the 'dischargeability of any debt'; 'make such orders as are necessary to protect or effectuate a determination that any debt is dischargeable'; [and] enjoin actions in other courts pending its determination."[53] These authorities when viewed as a whole, "evidences a complete scheme of regulation and procedures to be followed in determining the dischargeability of debts."[54] As outlined above section 35 was repealed and superseded by section 105 in the 1980s.[55] While much of the language of section 35 was omitted by section 105 its spirit remained.[56] The guiding provisions of section 35 continue to be used as a keystone by Bankruptcy Courts when deciding larger issues related to the overarching purpose of Bankruptcy generally.[57] The scheme first outlined in section 35 grants authority to bankruptcy courts to enjoin the "enforcement and/or collection of taxes."[58] Overall the Eighth Circuit seemed particularly concerned with providing a means to assure debtors that they could move forward with their lives.[59]

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[51] *Id.*
[52] *See* note 21 *supra.*
[53] Bostwick v. U.S., 521 F.2d 741, 745.
[54] *Id.*
[55] *See* note 21 *supra*.
[56] Becker's Motor Transp. v. Dep't of Treasury, 632 F.2d 242, 251.
[57] Bostwick v. U.S., 521 F.2d 741, 745.
[58] *Id.*
[59] Bostwick v. U.S., 521 F.2d 741, 746 ("We think that Congress intended that the bankrupt have the opportunity for a full and final determination of the dischargeability of his tax debts in order that he might avoid having a sword of Domocles hanging over his head. The purpose of the Bankruptcy Act is to rehabilitate the debtor in order that the debtor might be motivated to lead a full and productive economic life.")

**Putting It Together**

If we look at the factual circumstances surrounding the final determinations of the Ninth and Eight Circuits, a clear difference begins to emerge. In *In re* J.J. Re–Bar Corp., the responsible officers of the debtor, not the debtor itself, sought injunctive relief against the IRS for the collection of a separate and distinct tax debt. In *Bostwick v. U.S.* the debtors themselves sought to have the dischargeability of their tax debt decided by a bankruptcy court. "It is not hard to see how reviewing courts might be much more concerned about Bankruptcy orders that might interfere with IRS actions against third parties."[60]

The sentiments expressed by the Eighth Circuit in *Bostwick* were completely proper and correct. An individual that finds himself confronted with the prospect of bankruptcy should not be confronted with the possibility that once he believes his ordeal is over the IRS will come knocking for its cut. The entire bankruptcy process is meant to insure that individuals can take up the broken pieces of their lives and reassemble them in a way that allows them to be productive members of society. Granting the US government a free pass to assert whatever claim it wishes against the individual debtor is not only a travesty of the bankruptcy system but a black eye on the principles of individual liberty that this country was founded upon. The Eight Circuit's application of the limitations of the Anti–Injunction Act is totally appropriate with respect to the dischargeability of tax debts within the bankruptcy system.

By the same token, *In re J.J. Re–Bar Corp.* stands for the proposition that unscrupulous individuals who engage in willful tax evasion may not use the protections afforded their failed companies in bankruptcy to insulate themselves from liability. In this era of economic uncertainty it is imperative that every individual stands up and does his part to ensure the future

[60] *In re* Szwyd, 408 B.R. 547, 552 (Bankr. D. Mass. 2009).

success of this noble country. While sophistic arguments may be made to hack away at the clear intentions of Congress, at the end of the day those who circumvent the law must pay the penalty due.

Each of these interpretations of the Anti–Injunction Act is reasonable and each can exist with the other in harmony. While two applications of the same provision of the United States Code may lead to some confusion, that confusion is more than outweighed by the benefit created by the different interpretations. On the one hand, debtors are afforded the protections and certainty of the bankruptcy courts with respect to all of their debts, including federal taxes. On the other hand, those who would use the bankruptcy courts to further their own ill deeds are prevented from doing so.

**Conclusion**

The law has developed along two different but complementary paths. Often the same legal provision must be applied to widely different factual circumstances leading to dynamic interpretations. Such is the case with the Anti–Injunction Act. The Circuits have consistently held that if individuals attempt to use the protections provided by the Bankruptcy Court to further their own deception they will be provided no refuge and the Anti–Injunction Act will be applied to allow the IRS to collet its due. However, the Circuits have also held that the Anti–Injunction Act will be given no effect when the IRS attempts to collect a tax from a debtor without going through the due process protections provided by the Code.