IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF IOWA

In the Matter of

FRANK E. DUNCAN,
LUPE DUNCAN,

Debtors.

Case No. 91-1857-C J

Chapter 7

FRANK E. DUNCAN,
LUPE DUNCAN,

Plaintiffs,

Adv. Pro. No. 92-92020

V.

UNITED STATES OF AMERICA AND
IOWA DEPARTMENT OF REVENUE,

Defendants.

MEMORANDUM AND ORDER GRANTING MOTION FOR SUMMARY JUDGMENT

On July 14, 1992 the court conducted a telephonic hearing on the motion for summary judgment filed by the Chapter 7 debtors, Frank and Lupe Duncan. Walter T. Hart appeared on behalf of the debtors. Dale T. Baker appeared on behalf of the Iowa Department of Revenue and Finance (DOR). The matter was considered fully submitted at the conclusion of the arguments.

BACKGROUND

On January 15, 1992 the debtors filed an adversary complaint against the United States of America (USA) and the DOR seeking a determination that their 1983 and 1984 federal and state income tax obligations were dischargeable. On March 17, 1992 the debtors and the USA filed a stipulation agreeing that the tax obligations to the Internal Revenue Service (IRS) were dischargeable. The court approved the stipulation.

With regard to their state tax obligations, the debtors allege in paragraph four of the complaint that the DOR determined their income tax for the taxable years ending December 31, 1983 and 1984 was in the aggregate amount of $4,389.79, including late payment penalty and interest to December 29, 1988, plus statutory additions thereafter. In paragraph six of the complaint, the debtors contend returns for tax years 1983 and 1984 were due and filed more than three years prior to the filing of their bankruptcy petition and were filed neither fraudulently nor in a willful attempt to evade the income tax for those years.

In its answer filed April 10, 1992, the DOR admits paragraph 4 but denies paragraph 6 of the complaint. The DOR affirmatively states the assessment of Iowa income taxes for 1983 and 1984 "was based on Iowa taxable income which the Duncans falsely and fraudulently failed to report on returns or amended returns" as required by the Iowa Code. The DOR asserts the tax obligations are nondischargeable pursuant to 11 U.*S.* C. sections 523(a)(1)(B)(i) and 523(a)(1)(C).

In the stipulated scheduling order signed by both counsel of record and filed April 27, 1992, the parties agree the debtors timely filed Iowa individual income tax returns for the years ending December 31, 1983 and 1984 and the deficiencies were timely assessed by the State of Iowa based on a federal audit. The stipulated scheduling order indicates the only fact in dispute is whether the debtors 1983 and 1984 returns were false and fraudulent, and the issue to be determined is whether deficiencies for income not shown on those returns are dischargeable or excepted from discharge pursuant to section 523(a)(1).

On May 19, 1992 the debtors filed a motion for summary judgment seeking a determination that their state tax obligations are dischargeable. The debtors assert the IRS conducted an audit of their 1983 and 1984 income taxes and determined there was a deficiency but did not impose any penalty for fraud in connection with the assessed deficiency. They point out the DOR assessed the 1983 and 1984 state taxes based on the results of the federal audit. Attached to the motion is a copy of IRS Form 870-AD reflecting the debtors' waiver with regard to restrictions on assessment and collection of the tax deficiency. Also attached to the motion is a copy of the joint stipulation the debtors and the IRS reached with regard to the dischargeability of their 1983 and 1984 federal tax obligations.

On June 8, 1992 the DOR filed an objection to the motion for summary judgment. The DOR alleges “[t]here exist genuine issues of material fact as would preclude summary judgment pursuant to rule 56 F.R.C.P., as indicated by the separate Statement in Support of objection to Motion for Summary Judgment filed herewith.". In the statement of material facts, the DOR admits the debtors' allegations about the federal audit, the DOR's use of the audit information, and the stipulated dischargeability of the federal income taxes. The DOR then alleges “(t]he assessment of Iowa income tax for those periods was based on Iowa taxable income which the Duncans falsely and fraudulently failed to report on returns or amended returns for those periods as required by Iowa Code §§ 422.13 and 413.21.”.

The DOR did not attach supporting documentation or affidavits to its motion or statement. Late in the afternoon on July 13, 1992, the DOR filed with the court and faxed to debtors' counsel the affidavit of Kent Taylor, an auditor and revenue examiner for the DOR. In his affidavit, Mr. Taylor states the debtors timely filed tax returns for 1983 and 1984 but did not file amended returns or otherwise notify the DOR of the final disposition of the federal audit. (He acknowledges the DOR did issue an assessment based on the debtors' original returns and the federal audit adjustment information the DOR received from the IRS in September of 1988.) Mr. Taylor further alleges the debtors failed to report income, interest, dividends and loans attributable to their interest in two business entities. He contends Frank Duncan "knew or should have known that the financial condition of [one of the business entities] created an obvious likelihood that it would not be able to repay any 'loan', which should have been reported as income along with the interest and dividends from [the other business entity]". He asserts Frank Duncan was "convicted of crimes in connection with the submission of false and fraudulent claims to underwriters by [one of the two business entities]". The DOR did not provide any documentary evidence in support of the allegations in the affidavit.[1] Parenthetically the court notes Mr.

[1] Rule 56(c) Fed. R. Civ. P., made applicable to adversary proceedings by operation of Rule 7056 Fed. R. Bankr. P., does permit the nonmoving party to serve opposing affidavits one day prior to the hearing; waiting, however, until 4:00 p.m. of the day before the hearing when that hearing is scheduled for 9:00 a.m. abuses the already generous provision in the federal rules. Moreover, the local rules of this court emphasize timely and complete presentation of the factual basis and legal theory in support of a party's position on an issue. Local Rule 14(f)(3)

Taylor was not identified as a possible witness on the stipulated scheduling order.

During the July 14, 1992 hearing, debtors' counsel argued the debtors timely filed their 1983 and 1984 tax returns, the IRS audit did not conclude the returns were filed fraudulently, and the IRS assessed only a 5% negligence penalty. He strongly objected to Mr. Taylor's mention of the criminal conviction because the mail fraud crime had nothing to do with the controversy pending in this matter. He contended the allegation Frank Duncan knew or should have known the tax consequences related to the arrangments of the two business entities was too speculative to support a civil fraud theory.

The DOR counsel argued the debtors had a continuing duty to report all income and, therefore, the court should conclude they did not file returns as contemplated by section 523 (a) (1) (B) (i) because the debtors did not amend the returns or otherwise advise the DOR of the results of the IRS audit. Both accordingly and

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requires that supporting documentary evidence and affidavits be attached to an objection filed in opposition to a motion.

Failure to submit supporting documentation or affidavits in a timely manner hinders preparation for argument and can delay, as it did in this case, disposition by the court. Case law supports the requirement that parties document timely and fully their objections to motions for summary judgment. "Where a party has filed a motion for summary judgment, the opposing party is under an obligation to respond to that motion in a timely fashion and to place before the court all materials it wishes to have considered when the court rules on the motion." Cowgill v. Ravmark Industries, Inc., 780 F.2d 324, 329 (3rd Cir. 1985). "A party may not defeat a summary judgment motion by reference to 'phantom' documents not supplied to the court." Connick v. Teachers Ins. and Annuity, Ass'n, 784 F.2d 1018, 1020 (9th Cir. 1986), cert. denied 479 U.S. 822 (1986).

alternatively, DOR counsel maintained the debtors' failure to provide the DOR with that information was indicative of fraudulent action and willful intent to avoid taxes as contemplated by section 523(a)(1)(C). He contended the settlement between the debtors and the USA did not bind the DOR.

Debtors' counsel pointed out that Iowa law did not require the filing of amended returns. Based on his years as a tax practitioner in this state, debtors' counsel professionally stated that Iowa tax practitioners rely on the common knowledge there is an exchange of information between the IRS and the DOR.

DISCUSSION

A party is entitled to summary judgment only if there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Bankr. P. 7056. The federal rules do not require the movant to support its motion with affidavits or other similar materials negating the opponent's claim. Hartnagel v. Norman, 953 F.2d 394, 395 (8th Cir. 1992). A court must view all inferences to be drawn from the facts in a light most favorable to the party opposing the motion.

Parties opposing summary judgment may not rest upon the allegations in their pleadings. The nonmovant must resist a motion by setting forth specific facts showing there is a genuine issue of fact for trial. Buford v. Tremayne, 747 F.2d 445, 447 (8th Cir. 1984). Once the moving party has carried its burden, its "opponent must do more than simply show there is some metaphysical doubt as to the material facts." Hartnagel, 953 F.2d at 395.

To preclude the entry of summary judgment, the nonmovant must make a sufficient showing on every essential element of its case for which it has the burden of proof at trial. United States v. McIntyre, 779 F.Supp. 119, 120 (S.D. Iowa 1991). The quantum of proof the nonmoving party must produce is not precisely measurable, but there must be enough evidence so that a reasonable jury could return a verdict for the nonmovant. Id. at 121. The nonmoving party must establish significant probative evidence to prevent summary judgment. Johnson v. Enron Corp.., 906 F.2d 1234, 1237 (8th Cir. 1990).

Summary judgment is designed to remove factually unsubstantial cases from crowded district court dockets. Smith v. Marcantonio, 910 F.2d 500, 502-03 (8th Cir. 1990). Summary judgment is properly regarded not as a disfavored procedural shortcut but rather as an integral part of the federal rules designed to secure the just, speedy and inexpensive determination of every action. Postscript Enterprises v. City of Bridgeton, 905 F.2d 223, 225 (8th Cir. 1990).

The relevant portions of section 523(a)(1) provide:

> (a) A discharge under section 727 ... of this title does not discharge an individual debtor from any debt--
>
> (1) for a tax...—
>
> ...
>
> (B) with respect to which a return, if required--
>
> (i) was not filed; or ...
>
> (C) with respect to which the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat such tax.

The DOR concedes the debtors filed their original tax returns for 1983 and 1984 in a timely fashion. It argues, however, that tax obligations for income not reported on those returns are nondischargeable under section 523(a)(1)(B)(i). This argument is contrary to the statutory language denying a discharge of a tax obligation for which a required return was not filed.

The DOR cites two Illinois bankruptcy decisions in support of its argument. In re Cohn, 96 B.R. 827, 828 (Bankr. N.D. Ill. 1988); In re Haywood, 62 B.R. 482, 485 (Bankr. N.D. Ill. 1986). The failure to file amended returns in those cases rendered the related taxes nondischargeable under section 523(a)(1)(B)(i). Those opinions relied on an Illinois statute that required taxpayers to amend their returns to reflect any adjustments made in the amount of their previously reported federal taxable income.

Even if this court otherwise adopted the reasoning in the above cited decisions, the Iowa Code does not appear to contain any comparable statute, and the record does not indicate the Director of the DOR ever ordered the filing of supplementary returns. See Iowa Code § 422.22. At least one other court has rejected the Cohn and Haywood reasoning because its state tax statutes could not be read to require the debtors to file amended returns. See In re Blackwell, 115 B.R. 86 (Bankr. W.D. Va. 1990). To the extent the DOR relies on Matter of Kempf, Adv. No. 86-0154, slip op. at 9-10 (Bankr. S.D. Iowa Sept. 23, 1988), the undersigned notes Judge Russell J. Hill made only a general reference to the Haywood case, and the facts before him did not require an interpretation of tax provisions in the Iowa Code.

As a matter of law the court rejects the DORI s assertion that the debtors' tax obligations stemming from unreported income are nondischargeable under section 523(a)(1)(B)(i). Congress specifi- ically addressed the dischargeability of tax obligations stemming from a fraudulent or willful failure to report taxable income in section 523(a)(1)(C). This court will not read those elements into the provisions of section 523(a)(1)(B)(i). But see In re Blackwell, 115 B.R. 86, 89 (Bankr. W.D. Va. 1990) ("the purpose of 523(a)(1)(B)(i) is to except from discharge taxes to which a debtor willfully attempted to evade or defeat by not filing a return").

With respect to the DOR's argument the debtors filed a fraudulent return or willfully attempted to evade or to defeat the tax, the court observes that issues of fraud or willfulness typically involve an assessment of intent and usually entail a material question of fact. The DOR, however, has failed to demonstrate there is a genuine issue for trial. The DOR's sole documentation in support of its objection is the affidavit of Kent Taylor. The affidavit does not identify what amounts of income the debtors allegedly failed to report to the DOR and it presents no real factual basis for the court to conclude there is any genuine issue of material fact as to the section 523(a)(1)(C) argument. Mr. Taylor's allegation regarding the "submission of false and fraudulent claims to underwriters" provides no relevant basis for considering further whether the debtors filed fraudulent tax returns in this pending matter. Likewise, the affiant’s conclusory allegation that the debtors "knew or should have known" a loan could not be repaid and should have been reported as income is not alone sufficient to defeat the motion for summary judgment.

Viewing all inferences which can be drawn from the record in a light most favorable to the DOR, the court concludes the DOR failed to make a sufficient showing there is a genuine issue of material fact as to the alleged filing of fraudulent returns or the willful evasion of taxes.

ORDER

THEREFORE, IT IS HEREBY ORDERED that the plaintiffs' motion for summary judgment is granted.

Dated this 5th day of August, 1992.

LEE M. JACKWIG
CHIEF U.S. BANKRUPTCY JUDGE