



OFFICE OF THE ATTORNEY GENERAL
STATE OF ILLINOIS

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September 5, 1995

FILE NO. 95-016

REVENUE:
Discharge of Tax Liability
in Bankruptcy

The Honorable George H. Ryan
Secretary of State
100 West Randolph Street, Suite 5-400
Chicago, Illinois 60601

Dear Secretary Ryan:

I have your letter wherein you inquire whether, under section 523 of the Bankruptcy Code (11 U.S.C. § 523), an exception to discharge is provided for past due franchise taxes owed to the Secretary of State upon confirmation of a reorganization plan for a corporation under section 1141 of the Bankruptcy Code (11 U.S.C. § 1141). For the reasons hereinafter stated, it is my opinion that the exceptions set forth in section 523 do not apply upon a corporate reorganization under section 1141.

You have stated that Britt Airways, Inc., a foreign corporation authorized to transact business in Illinois, was a party to a merger in 1990, and had also incurred an increase in paid-in capital due to an issuance of shares or contribution in

1986. Neither event was reported to the Secretary of State, and subsequent annual reports filed by the corporation allegedly misrepresented the amount of paid-in capital, resulting in underpayment of franchise taxes. Britt Airways, along with Continental Airlines, Inc., filed a voluntary petition under chapter 11 of the Bankruptcy Code (11 U.S.C. § 1101 et seq.) on December 3, 1990, and the Bankruptcy Court set a bar date of September 27, 1991, as the last day for filing a proof of claim against the corporation. Because the Secretary of State had no notice that the corporation's paid-in capital had been underreported, no claim for additional franchise taxes was filed. Under the chapter 11 reorganization plan, Britt Airways merged into Continental Airlines. Continental has refused to pay additional franchise taxes for the years 1986 through 1989 based upon the bankruptcy court action.

Section 1141 of the Bankruptcy Code provides; in pertinent part:

"(a) Except as provided in subsections (d)(2) and (d)(3) of this section, the provisions of a confirmed plan bind the debtor, any entity issuing securities under the plan, any entity acquiring property under the plan, and any creditor, equity security holder, or general partner in the debtor, whether or not the claim or interest of such creditor, equity security holder, or general partner is impaired under the plan and whether or not such creditor, equity security holder, or general partner has accepted the plan.

* * *

(c) Except as provided in subsections (d) (2) and (d) (3) of this section and except as otherwise provided in the plan or in the order confirming the plan, after confirmation of a plan, the property dealt with by the plan is free and clear of all claims and interests of creditors, equity security holders, and of general partners in the debtor.

(d) (1) Except as otherwise provided in this subsection, in the plan, or in the order confirming the plan, the confirmation of a plan--

(A) discharges the debtor from any debt that arose before the date of such confirmation * * * whether or not--

(i) a proof of the claim based on such debt is filed or deemed filed under section 501 of this title
* * *;

(2) The confirmation of a plan does not discharge an individual debtor from any debt excepted from discharge under section 523 of this title * * *.

* * *

"

(Emphasis added.)

Section 523 of the Code provides that a discharge under section 1141 does not discharge an individual debtor from any debt for a tax with respect to which the debtor made a fraudulent return or willfully attempted to evade payment. (11 U.S.C. § 523(a) (1)

(C).)

Both section 1141 and section 523 of the Code refer to non-discharge of an individual debtor in the described circumstances. The legislative history and reported case law support

the plain reading of these provisions as excluding corporate debtors from their operation. Thus, the Bankruptcy Court, in In re Kuempel Company (1981), 14 B.R. 324, specifically held that the quoted exception from discharge for individual debtors did not apply to a corporate debtor. In In re A.H. Robins Co., Inc. (1986), 59 B.R. 99, the court held that the broader discharge for corporate debtors does not violate due process or equal protection guarantees in the Constitution.

During Congressional consideration of the Bankruptcy Code, different versions were developed in the House and the Senate. The Senate version provided that corporate, as well as individual, debtors under section 1141 would not have been discharged from tax debts excepted from discharge under section 523. (S. Rep. No. 989, 95th Cong., 2d Sess. 129-30 (1978), reprinted in 1978 USCCAN 5787, 5915-16.) Congress, however, rejected the Senate version of section 1141 and the House version was ultimately adopted. The difference in the versions was explained by Senator DeConcini and Congressman Edwards:

"Congressional Record

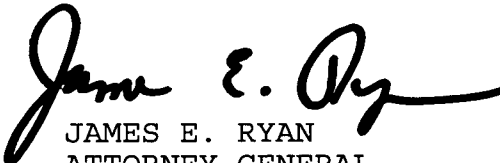
* * * section 1141(d) (2) of the House amendment is derived from the House bill as preferable to the Senate amendment. It is necessary for a corporation or partnership undergoing reorganization to be able to present its creditors with a fixed list of liabilities upon which the creditors or third parties can make intelligent decisions. Retaining an exception for discharge with respect to nondischargeable taxes would leave an

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undesirable uncertainty surrounding reorganizations that is unacceptable. Section 1141(d)(3) is derived from the Senate amendment. Section 1141(d)(4) is likewise derived from the Senate amendment." (Remarks of Sen. DeConcini, 124 Cong. rec. S17, 422, daily ed., Oct. 6, 1978; Remarks of Rep. Edwards, 124 Cong. Rec. H11, 105, daily ed. Sept. 28, 1978.)

Based upon these authorities, it is clear that confirmation of a plan under section 1141 of the Bankruptcy Code discharges a corporate debtor from liability for taxes imposed prior to the date of confirmation. Therefore, it is my opinion that the franchise taxes owed by Britt Airways for the years 1986 through 1989 were discharged upon the entry of the order of the bankruptcy court confirming the reorganization plan for Britt and Continental Airlines, even if the underpayment of such taxes resulted from misrepresentations of Britt's paid-in capital.

Sincerely,


JAMES E. RYAN
ATTORNEY GENERAL