

FIDUCIARY LIABILITY UNDER THE FEDERAL PRIORITY STATUTES

ROBERT N. DAVIES*

Myriad aspects of commercial interaction between the federal government and individuals may be affected by the near-ancient sections 3466 and 3467 of the Revised Statutes which subject a fiduciary of an insolvent estate to personal liability for failure to grant priority to specified governmental claims. In an attempt to guide the practitioner through the maze of contingencies presented by these provisions, the author outlines considerations relevant to an assessment of the applicability and effect of the statutory priorities.

JUDGES and legislators have not been hesitant in placing extraordinary duties upon those individuals deemed worthy of the title "fiduciary." One of the greatest, yet least familiar, of these duties is that imposed by sections 3466 and 3467 of the Revised Statutes.¹ Under section 3467, "every executor, administrator, . . . assignee, or other person" who pays any debts of the estate or person represented by him without first satisfying all debts owing the United States, as required by section 3466,² is personally liable to the United States "to the extent of such payments . . . or for so much thereof as may remain due and unpaid."³ Enacted in the latter portion of the

* B.A. 1958, DePauw University; LL.B. 1961, Duke University; Member Indiana Bar.

¹ 31 U.S.C. §§ 191-92 (1964).

² This section provides: "Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed." This statute, giving the federal government priority in its claims, is principally derived from the Act of March 3, 1797, ch. 20, § 5, 1 Stat. 515. The language comes in large part from the Act of March 2, 1799, ch. 22, § 65, 1 Stat. 676.

³ Section 3467 provides: "Every executor, administrator, or assignee, or other person, who pays, in whole or in part, any debt due by the person or estate for whom or for which he acts before he satisfies and pays the debts due to the United States from such person or estate, shall become answerable in his own person and estate to the extent of such payments for the debts so due to the United States, or for so much thereof as may remain due and unpaid." Congress first imposed personal liability on fiduciaries who

Eighteenth Century to ensure adequate revenues to sustain the financial burdens of government and to discharge the public debt,⁴ these sections, liberally construed,⁵ combine to render fiduciaries responsible for administering the estates of deceased or insolvent debtors personally liable for failing to accord requisite priority to debts due the United States Government.

In order to avoid personal liability under section 3467, it is essential that fiduciaries be totally familiar with the applicability of the federal priority statutes. The purpose of this article is to assess the burden that personal representatives and assignees must assume in determining the types of representatives, debts, debtors, and competing claims to which sections 3466 and 3467 apply. In addition, particular emphasis will be given to an extremely unsettled and controversial issue under these sections—the degree of notice or knowledge of an outstanding government claim to which a fiduciary is entitled before he can be held personally liable under the priority statutes.

FIDUCIARIES COVERED BY THE FEDERAL PRIORITY STATUTES

Perhaps the first question that any fiduciary should ask is whether he is the type of representative subject to the personal liability provisions of the priority statutes. Because section 3467 expressly includes “every executor, administrator [and] . . . assignee,” few problems have arisen in ascertaining those fiduciaries covered by the statute.⁶ Most of the difficulties in determining coverage under

did not make provision for the federal government's priority claims in the Act of March 2, 1799, ch. 22, § 65, 1 Stat. 676. The history of §§ 3466 and 3467 is discussed in *King v. United States*, 379 U.S. 329, 334-45 (1964).

⁴ See *Nathanson v. NLRB*, 344 U.S. 25 (1952); *United States v. State Bank*, 31 U.S. (6 Pet.) 29 (1832).

⁵ In order to effectuate the purpose of the priority statutes of securing public revenues, the courts have generally construed sections 3466 and 3467 liberally in favor of the United States. See, e.g., *Price v. United States*, 269 U.S. 492, 500 (1926); *United States v. Crocker*, 313 F.2d 946 (9th Cir. 1963). However, the statutory purpose of these sections may also limit the imposition of priority under some circumstances. *United States v. Marxen*, 307 U.S. 200, 206 (1939). For an example of this approach see *Nathanson v. NLRB*, 344 U.S. 25 (1952), where the Court refused to allow priority for the NLRB's claim for back pay of a bankrupt's employees because the beneficiaries of the claim were *private* parties and, consequently, no public revenue was involved. Because of their close relationship, the statutes are normally construed together in determining questions of priority and fiduciary liability. See *King v. United States*, 379 U.S. 329, 334-36 (1964).

⁶ The statute has generally been held applicable to trustees, see *Delaware v. Irving*

section 3467 have concerned the definition to be afforded the catch-all category "other persons." In 1953, for example, the Fifth Circuit in *United States v. Stephens*⁷ held that a court-appointed receiver was not embraced within the definition of "other person," since in the court's view this category was intended to include only *personal* representatives of the debtor, and not persons acting at the direction of a court.⁸ Ten years later, however, the Ninth Circuit in *United States v. Crocker*⁹ held that the controlling factor in determining who is an "other person" within the meaning of the statute was not whether a fiduciary was court-appointed or the debtor's personal representative, but whether he had been given possession and control of the debtor's assets and charged with the payment of the debtor's obligations.¹⁰ The resulting split in the circuit courts was resolved by the Supreme Court in 1964 in *King v. United States*.¹¹ In *King* the Court adopted the reasoning of the Ninth Circuit and held that the purpose of section 3467 was clearly "to make those into whose hands control and possession of the debtor's assets are placed, responsible for seeing that the Government's priority is paid."¹² If this is the purpose of the statute, the title of a fiduciary's position, the mode of his appointment, and the fact that he is not the personal representative of the debtor are irrelevant considerations. Under the *King* test, the only significant question to be answered in determining whether a fiduciary qualifies as an "other person" under section 3467 is whether he has possession and control of the assets of a deceased or insolvent debtor for the purpose of satisfying the debtor's outstanding obligations.¹³

Trust Co., 92 F.2d 17 (2d Cir.), *cert. denied*, 302 U.S. 754 (1937), and to assignees for the benefit of creditors, *see Massachusetts v. United States*, 333 U.S. 611 (1948); *Livingston v. Becker*, 40 F.2d 673, 674 (E.D. Mo. 1929).

⁷ 208 F.2d 105 (5th Cir. 1953).

⁸ *Id.* at 108-09.

⁹ 313 F.2d 946 (9th Cir. 1963).

¹⁰ *Id.* at 949.

¹¹ 379 U.S. 329 (1964).

¹² *Id.* at 337.

¹³ The control and possession test has been used to impose liability upon stockholders in complete control of an insolvent corporate debtor's assets, *Lakeshore Apartments, Inc. v. United States*, 351 F.2d 349 (9th Cir. 1965), and a defendant who was president, director, and virtually the sole shareholder in two insolvent corporations, *United States v. Lutz*, 295 F.2d 736 (5th Cir. 1961).

DEBTS TO WHICH FEDERAL PRIORITY ATTACHES

After a fiduciary has determined that he is subject to the personal liability provisions of section 3467, a second problem confronting him is whether a particular claim asserted by the United States is entitled to priority under section 3466. While it may be reasonably accurate to conclude that section 3466 priority applies to virtually *any* class of indebtedness due the United States,¹⁴ and that neither the form of the debt nor the mode in which it is incurred are material to priority status,¹⁵ the fiduciary should be aware of at least four limitations which are often utilized by the courts to defeat the attachment of federal priority:

1. *The Government must acquire its claim prior to the debtor's insolvency.*

Although the attachment of priority does not depend upon *how* the United States acquires its claims against a debtor's estate, it may be contingent upon *when* the claim was procured. As a general rule, the courts have required that the Government obtain its claim before the manifestation of the debtor's insolvency in order to claim priority under section 3466.¹⁶ A debt transferred to the United States after the filing of the debtor's bankruptcy petition, for example, is not entitled to priority, since the rights of all his creditors are fixed at the date of filing by the Bankruptcy Act.¹⁷ The courts have reasoned that to hold otherwise would permit the Government to purchase general claims after bankruptcy and collect in full to the detriment of other creditors by invoking the priority statute.¹⁸ For similar reasons, a claim acquired by the United States after an assignment for the benefit of creditors has been held unworthy of priority status.¹⁹

It is important to recognize, however, that the requirement that a government claim must be acquired before insolvency does not

¹⁴ See *In re Wilson*, 23 F. Supp. 236, 239 (N.D. Tex. 1938); *United States v. Barnes*, 31 F. 705, 707 (C.C.S.D.N.Y. 1887).

¹⁵ See *Bayne v. United States*, 93 U.S. 642, 643 (1876).

¹⁶ See *United States v. Marxen*, 307 U.S. 200 (1939); *Korman v. Federal Housing Adm'r*, 113 F.2d 743, 744 (D.C. Cir. 1940).

¹⁷ See *United States v. Marxen*, 307 U.S. 200 (1939); *In re Hansen Bakeries, Inc.*, 103 F.2d 665 (3d Cir. 1939); *In re Wissmeir*, 26 F. Supp. 806 (E.D.N.Y. 1939); *In re Stamford Auto Supply Co.*, 25 F. Supp. 530 (N.D. Tex. 1938); *In re Miller*, 25 F. Supp. 337 (S.D.N.Y. 1938).

¹⁸ See *In re Miller*, 25 F. Supp. 337 (S.D.N.Y. 1938).

¹⁹ See *Engleman v. Commodity Credit Corp.*, 107 F. Supp. 930 (S.D. Cal. 1952).

mean that a claim must mature in advance of insolvency. Reasoning that the same policy of securing revenues to relieve the financial burdens of government applies equally to debts presently payable and those maturing in the future,²⁰ the courts have consistently defined the word "due" in the statute as synonymous with "owing" rather than "payable."²¹ Thus, a debt owing to the United States at the date of a debtor's insolvency is entitled to priority under the statute even if it will not mature until after insolvency has taken place.

2. *The government agency holding the claim must have acquired it purely as an agent of the federal government and not as an independent entity with a separate corporate personality.*²²

Most federal agencies have little difficulty in qualifying their claims for priority under section 3466. Past decisions, for example, have upheld the priority status of claims asserted by such diverse agencies as the Farm Credit,²³ Federal Housing,²⁴ and Small Business Administrations.²⁵ On the other hand, the courts are hesitant to permit agencies with separate and distinct corporate personalities, like the Reconstruction Finance Corporation, to attain priority status for claims arising out of their individual endeavors.²⁶ It is possible, however, even for agencies with separate corporate identities to have claims entitled to priority status when they act solely as federal agents with funds from the federal treasury rather than their own coffers.²⁷

3. *The Government must be the beneficiary of the proceeds of the claim.*

Where the beneficiaries of a claim asserted by the Government are private parties, the statutory purpose of securing public revenue does not require that the claim be accorded priority over competing

²⁰ See *United States v. State Bank*, 31 U.S. (6 Pet.) 29, 36-37 (1832).

²¹ *Id.*; *Engleman v. Commodity Credit Corp.*, 107 F. Supp. 930, 932 (S.D. Cal. 1952). See also *Bernhard, Government Priority for Repayment of Monies Advanced to Contractors*, 33 GEO. L.J. 279, 281-87 (1945).

²² See *Korman v. Federal Housing Adm'r*, 113 F.2d 743, 746 (D.C. Cir. 1940).

²³ See *United States Dep't of Agriculture v. Remund*, 330 U.S. 539 (1947); *In re Wilson*, 23 F. Supp. 236 (N.D. Tex. 1938).

²⁴ See *Korman v. Federal Housing Adm'r*, 113 F.2d 743, 746 (D.C. Cir. 1940); *Wagner v. McDonald*, 96 F.2d 273, 276 (8th Cir. 1938).

²⁵ See *Small Business Administration v. McClellan*, 364 U.S. 446 (1960); *W.T. Jones & Co. v. Foodco Realty, Inc.*, 318 F.2d 881, 885 (4th Cir. 1963).

²⁶ See *In re Peoria Consol. Mfrs., Inc.*, 286 F.2d 642, 645 (7th Cir. 1961) (dictum); *West Va. Rail Co. v. Jewett Bigelow & Brooks Coal Co.*, 26 F.2d 503, 504-05 (E.D. Ky. 1928) (dictum).

²⁷ See *In re Peoria Consol. Mfrs., Inc.*, 286 F.2d 642, 645 (7th Cir. 1961).

obligations. For this reason, the courts have generally refused to permit the United States to utilize its statutory priority for the benefit of private persons.²⁸ A National Labor Relations Board order for back pay for the employees of an insolvent debtor, for example, is not considered worthy of section 3466 priority.²⁹ Similarly, a claim for money distributed by the Indian Agency to a guardian of minor Indian children who deposited the money in a bank which later became insolvent was held not entitled to priority status, since the United States was not a party to the purely private guardian-bank transaction.³⁰ However, where funds are deposited in a bank by an agent or officer of the United States, and it is clear that the Government is the actual beneficiary of the claim, priority attaches.³¹ Thus, it is probably safe to generalize that, in order for a claim asserted by the United States to be entitled to priority under section 3466, its collection must benefit the public revenue, and not private individuals.

4. *According priority to the claim must not conflict with another congressional policy.*

In those cases in which the Supreme Court has refused to uphold the priority status of a government claim, it has usually been because the application of section 3466 priority would, in a particular case, conflict with other congressional policies.³² In *United States v. Guaranty Trust Company*,³³ for example, the Court declined to apply the priority statutes on the ground that to do so, under the circumstances, would tend to thwart the purpose of the Transportation Act of 1920. For similar reasons, the Court, in *Cook County National Bank v. United States*,³⁴ denied priority to a federal deposit claim against an insolvent national bank, since priority was, in its view, inconsistent with the congressional act which created the national banking system.

²⁸ See *Nathanson v. NLRB*, 344 U.S. 25 (1952); *United States v. Johnson*, 87 F.2d 155 (10th Cir. 1936).

²⁹ See *Nathanson v. NLRB*, 344 U.S. 25 (1952).

³⁰ *United States v. Johnson*, 87 F.2d 155, 161 (10th Cir. 1936); see *Spicer v. Smith*, 288 U.S. 430 (1933).

³¹ See *Barnett v. American Surety Co.*, 77 F.2d 225 (10th Cir. 1935). *But cf.* *Cook County Nat'l Bank v. United States*, 107 U.S. 445 (1882) (deposit of federal funds in national bank held not entitled to priority).

³² See notes 33-34 *infra* and accompanying text.

³³ 280 U.S. 478 (1930).

³⁴ 107 U.S. 445 (1882).

What constitutes sufficient inconsistency to preclude the application of the priority statutes has never been clearly defined by the Supreme Court. The only guidance offered by the Court which even approaches a meaningful test is its holding in *United States v. Emory*³⁵ that "only the plainest inconsistency would warrant our finding an implied exception to the operation of so clear a command as that of § 3466."³⁶ Since *Emory*, the Court has affirmed its "plainest inconsistency" criterion in *United States Department of Agriculture v. Remund*,³⁷ holding that congressional legislation authorizing emergency crop and feed loans is not inconsistent with federal priority. With varying results the lower federal courts have attempted to follow the *Emory* approach in assessing the consistency of section 3466 with other federal legislation.³⁸ An examination of these cases, however, reveals that so long as the "plainest inconsistency" test prevails, the priority status of government claims will face little danger from other congressional legislation.³⁹

TYPES OF DEBTORS TO WHICH THE FEDERAL PRIORITY STATUTES APPLY

A fiduciary must also ask whether the debtor whose assets or estate he is responsible for administering is within the coverage of the priority statutes. It is clear that section 3466 includes two basic types of debtors within its provisions: (1) a debtor who dies leaving an estate insufficient to discharge all his outstanding obligations; and (2) a debtor who becomes insolvent while still alive.⁴⁰ The first type of debtor covered by the statute is self-explanatory, and few obstacles, if any, exist in discovering those who qualify under this

³⁵ 314 U.S. 423 (1941).

³⁶ *Id.* at 433.

³⁷ 330 U.S. 539 (1947).

³⁸ See, e.g., *Korman v. Federal Housing Adm'r*, 113 F.2d 743, 746 (D.C. Cir. 1940) (giving F.H.A. loan claims priority actually furthers the objectives of the National Housing Act); *In re J.F. Mulkey Co.*, 189 F. Supp. 716 (E.D. Mich. 1960) (priority is not incompatible with the goals of the Defense Production Act of 1950).

³⁹ See cases cited notes 35-38 *supra*. In *Massachusetts v. United States*, 333 U.S. 611 (1948), the Court held that a federal claim for unemployment compensation taxes under Title 9 of the Social Security Act should not be diminished by a state claim for ninety percent of that amount, which is allowed as a credit under the Act. Justice Jackson, in a vigorous dissent joined by three others, said that § 3466 "should not lightly be construed to frustrate a specific policy embodied in a later federal statute." *Id.* at 635.

⁴⁰ 31 U.S.C. § 191 (1964); see *Conard v. Atlantic Ins. Co.*, 26 U.S. (1 Pet.) 386, 438-39 (1828); *United States v. Belkin*, 358 F.2d 378, 381-82 (6th Cir. 1966); *United States v. Crocker*, 313 F.2d 946, 947-48 (9th Cir. 1963).

provision. However, living debtors who are included under section 3466 are not so easily ascertained. The statute provides that in order for priority to attach to government claims against a living debtor he must be insolvent, and his insolvency must be manifested in one of three ways: (1) by voluntary assignment for the benefit of creditors; (2) by attachment of his estate as an absconding, concealed, or absent debtor; or (3) by the commission of an act of bankruptcy.⁴¹ Under any of these tests the courts have held that the controlling consideration is whether the debtor has actually transferred title and possession of all his assets to a fiduciary.⁴² As long as a debtor retains title to or possession of his property, section 3466 will not apply,⁴³ regardless of the insufficiency of his assets to meet his obligations.⁴⁴ Moreover, a debtor must surrender all of his property to a fiduciary, since a partial divestment is not enough to invoke the priority statutes.⁴⁵ While it is possible under section 3466 for a debtor's insolvency to be manifested by the attachment of his estate as an absconding, concealed, or absent debtor,⁴⁶ the two most frequently recognized indications are the voluntary assignment and the act of bankruptcy:

1. *Voluntary assignment for the benefit of creditors.*

An assignment for the benefit of creditors has been defined as a "transfer without compulsion of law by a debtor of his property to an assignee in trust to apply the same or the proceeds thereof to the payment of his debts"⁴⁷ In applying this definition, the courts have generally demanded three requirements: (1) the purpose of the assignment must be to pay creditors of the assignor;⁴⁸ (2) the

⁴¹ See *United States v. Emory*, 314 U.S. 423, 426 (1941); authorities cited note 40 *supra*.

⁴² See *Bramwell v. United States Fidelity & Guar. Co.*, 269 U.S. 483, 488 (1926); *Beaton v. Farmers' Bank*, 37 U.S. (12 Pet.) 102, 133-34 (1838).

⁴³ See authorities cited note 42 *supra*.

⁴⁴ Federal priority will not attach merely because a debtor is insolvent. See *United States v. Oklahoma*, 261 U.S. 253, 260 (1923); *United States v. Hooe*, 7 U.S. (3 Cranch) 73, 90-91 (1805); *W.T. Jones & Co. v. Foodco Realty, Inc.*, 318 F.2d 881 (4th Cir. 1963); Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 *YALE L.J.* 228, 237 (1967).

⁴⁵ See *Conard v. Atlantic Ins. Co.*, 26 U.S. (1 Pet.) 386, 438-39 (1828); *United States v. Fabricated Air Prods. Co.*, 206 F. Supp. 228, 231 (E.D. Tex. 1962).

⁴⁶ See note 41 *supra* and accompanying text.

⁴⁷ *United States v. Fabricated Air Prods. Co.*, 206 F. Supp. 228, 231 (E.D. Tex. 1962).

⁴⁸ *Id.*

assignment must be made to a fiduciary;⁴⁰ and (3) the assignment must transfer all the assets of the debtor to the fiduciary.⁵⁰ While some courts have also indicated that the debtor must take some affirmative action in initiating the assignment,⁵¹ the majority require only that he acquiesce in the transfer of his assets.⁵² A fiduciary, therefore, may assume that any consensual transfer of a debtor's assets to him for the purpose of satisfying creditors will be a sufficient manifestation of insolvency to invoke the priority statutes regardless of who initiated the assignment.

2. Act of bankruptcy.

Because the Bankruptcy Act classifies a general assignment for the benefit of creditors as an act of bankruptcy, many courts have characterized a voluntary assignment as an act of bankruptcy.⁵³ Aside from the general assignment, however, the most frequently occurring act of bankruptcy affecting the priority statutes is the procurement or appointment of a receiver to administer a debtor's estate.⁵⁴ While a contrary rule existed prior to the 1926 amendments to the Bankruptcy Act,⁵⁵ subsequent Supreme Court decisions have

⁴⁰ See *United States v. Sullivan*, 19 F. Supp. 695, 699 (W.D.N.Y. 1937), *aff'd*, 95 F.2d 1021 (2d Cir. 1938) (per curiam).

⁵⁰ See note 45 *supra* and accompanying text.

⁵¹ See *Motherhead v. United States Fidelity & Guar. Co.*, 22 F.2d 644, 652-53 (8th Cir. 1927), *cert. denied*, 276 U.S. 637 (1928).

⁵² The following actions have been held to be voluntary assignments by the courts: a debtor's consent to a court order giving a receiver exclusive control of the debtor's assets for the benefit of creditors, *United States v. Butterworth-Judson Corp.*, 269 U.S. 504, 513-14 (1926); *Hatch v. Morosco Holding Co.*, 56 F.2d 640 (S.D.N.Y.), *aff'd*, 61 F.2d 944 (2d Cir. 1932), *cert. denied*, 288 U.S. 613 (1933); a debtor's filing of an answer in an involuntary bankruptcy proceeding consenting to adjudication as a bankrupt, *In re Waxaid Co.*, 55 F. Supp. 289, 290 (D. Md. 1943); and a debtor's acquiescence in the taking of his property by an authorized state official in order to administer it for the benefit of creditors, *United States ex rel. Ray v. Porter*, 19 F.2d 541, 544 (D. Idaho 1927).

⁵³ *E.g.*, *In re Waxaid Co.*, 55 F. Supp. 289 (D. Md. 1943); *In re Berthoud*, 231 F. 529 (S.D.N.Y.), *appeal dismissed*, 238 F. 797 (2d Cir. 1916); see Bankruptcy Act § 3 (a) (5), 11 U.S.C. § 21 (a) (5) (1964). Sections 3 (a) (1) through 3 (a) (6) of the Act, 11 U.S.C. §§ 21 (a) (1)-(6) (1964), classify six activities as acts of bankruptcy.

⁵⁴ See Bankruptcy Act § 3 (a) (6), 11 U.S.C. § 21 (a) (6) (1964).

⁵⁵ Prior to 1926, the Supreme Court held that the appointment of a receiver was not necessarily an act of bankruptcy, because the Bankruptcy Act then required that the reason for the appointment must have been the insolvency of the debtor if the appointment was to qualify as an act of bankruptcy. See *United States v. Oklahoma*, 261 U.S. 253 (1923). Since receivers are often appointed for reasons other than insolvency (*e.g.*, to act as a state agent to protect the depositors of an insolvent bank), appointment was not an automatic act of bankruptcy under such a rule. However, the 1926 amendments to the Bankruptcy Act solved this problem by removing the necessity for showing an exclusive causal relationship between insolvency and appoint-

uniformly held that the appointment of a general equity receiver is an act of bankruptcy sufficient to accord priority status to claims owed to the United States by the debtor.⁵⁶

The requirements for an act of bankruptcy for the purposes of determining section 3466 priority closely parallel those for a voluntary assignment. Thus, priority may attach even though the debtor did not initiate the appointment of the receiver.⁵⁷ Similarly, the statutes will not apply unless the receiver is given title and possession of all the debtor's assets.⁵⁸ The appointment of a receiver in a Bankruptcy Act Chapter XI proceeding, for example, is not an act of bankruptcy for section 3466 purposes, since under this arrangement the debtor remains in possession of his property and continues to operate his business with court supervision.⁵⁹ A receiver, however, who has complete control of a debtor's assets may be reasonably certain that government claims are entitled to priority under section 3466.

CLASSES OF COMPETING CREDITORS TO WHICH FEDERAL PRIORITY APPLIES

As a general rule, a fiduciary faced with competing claims asserted by federal and non-federal or private claimants can be fairly confident that, as between the two, the federal claim will be entitled to priority under section 3466.⁶⁰ There are several exceptions to this generalization, however, and in examining them it is necessary for analytical purposes to separate non-bankruptcy and bankruptcy proceedings.

1. *Non-bankruptcy proceedings.*

While creditors holding prior state statutory or common law liens have often competed with the United States for preference in the distribution of the assets of a deceased or insolvent debtor, the

ment. Act of May 27, 1926, ch. 406, § 3, 404 Stat. 662; see *United States v. Bliss*, 40 F.2d 935, 936 (D. Neb.), *aff'd*, 44 F.2d 909 (8th Cir. 1930).

⁵⁶ See *Illinois ex rel. Gordon v. Campbell*, 329 U.S. 362, 367-70 (1946); *United States v. Emory*, 314 U.S. 423, 426 (1941); *United States v. Texas*, 314 U.S. 480, 483 (1941).

⁵⁷ See *Adams v. United States*, 24 F.2d 907, 908 (9th Cir. 1928), *aff'g* 9 F.2d 624 (W.D. Wash. 1925); *Mothersead v. United States Fidelity & Guar. Co.*, 22 F.2d 644, 652-53 (8th Cir. 1927), *cert. denied*, 276 U.S. 637 (1928).

⁵⁸ See *United States v. National Furniture Co.*, 348 F.2d 390 (8th Cir. 1965).

⁵⁹ *Id.*

⁶⁰ See Meaders, *Priority of Federal Tax Claims in Nonbankruptcy Proceedings*, 50 A.B.A.J. 288, 289 (1964).

Supreme Court has consistently found federal claims entitled to priority under section 3466.⁶¹ In doing so the Court's methodology has been to subordinate earlier competing liens by characterizing them as "general and inchoate" rather than "specific and perfected."⁶² The Court first held that a general and inchoate lien must yield to subsequently acquired federal claims in 1929 in *County of Spokane v. United States*.⁶³ For a decade thereafter, the Court continued to hold competing liens inferior to United States claims, making little effort to clarify its standards for determining under what circumstances a lien was to be considered specific and perfected.⁶⁴ However, in *United States v. Waddill, Holland, & Flinn, Incorporated*,⁶⁵ and *Illinois ex rel. Gordon v. Campbell*,⁶⁶ decided in 1945 and 1946 respectively, the Court attempted to clarify its previous decisions. It began by holding that the effect of a competing lien upon United States priority is always a federal question to be decided by the federal courts, regardless of the characterization of the lien under state law.⁶⁷ Next, and most importantly, the Court enunciated three requirements which must be met before a lien may be considered specific and perfected. It must be explicit as to: (1) the identity of the lienor; (2) the amount of the lien; and (3) the particular property to which the lien is attached.⁶⁸ Sub-

⁶¹ See notes 63-70 *infra* and accompanying text.

⁶² For an attack on the origin and retention of the inchoate and general lien doctrine see Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien*, 63 YALE L.J. 905 (1954). Kennedy argues that in enacting the priority statutes Congress had no intention of overriding valid liens arising prior to federal claims. *Id.* at 907. See also Plumb, *supra* note 44, at 229-33.

⁶³ 279 U.S. 80 (1929). The case involved state taxes which were assessed prior to the federal tax assessment, but because state statutory procedure for acquiring a tax lien had not been followed, the Court held that the state lien was not "specific." *Id.* at 94.

⁶⁴ See *United States v. Texas*, 314 U.S. 480, 486-88 (1941) (unsecured federal tax claim held superior to unsecured state tax lien on grounds that property to which the lien was to attach and the amount of the lien were uncertain); *United States v. Knott*, 298 U.S. 544 (1936); *New York v. Maclay*, 288 U.S. 290 (1933).

⁶⁵ 323 U.S. 353 (1945).

⁶⁶ 329 U.S. 362 (1946).

⁶⁷ 323 U.S. at 356-57; 329 U.S. at 371. If state law describes the lien in question as inchoate, however, the Court will take this determination as "practically conclusive." *Id.* at 371.

⁶⁸ 329 U.S. at 375. In applying its criteria for a specific and perfected lien, the Court, in *United States v. Waddill, Holland & Flinn, Inc.*, 323 U.S. 353, 357-60 (1945), found that neither a landlord's lien nor a municipal tax lien were specific, since the amount of the liens and the property they covered were not definite. In *Illinois ex rel. Gordon v. Campbell*, 329 U.S. 362, 375 (1946), the uncertainty of the property to which the lien attached caused its subordination to a federal claim, even though record

sequent decisions have left these requirements relatively undefined, with one exception. In 1953, in *United States v. Gilbert Associates, Incorporated*,⁶⁹ the Court added content to its third requirement by holding that a lien is sufficiently definite as to particular property only when the lienholder has acquired title or possession of the property subject to his lien. Interestingly enough, the Court has not had the occasion actually to decide that a specific and perfected lien will be entitled to priority over a later federal claim, since in applying the foregoing criteria it has successfully managed in every case since *County of Spokane* to characterize competing liens as general and inchoate rather than specific and perfected.⁷⁰

Although the lower federal courts have generally attempted to apply the tests suggested by the Supreme Court in assessing the character of competing liens,⁷¹ at least one circuit has taken the additional step, avoided thus far by the Supreme Court, of actually holding that a specific and perfected lien will prevail over a later

notice of the competing lien had specified the identity of the lienor and the amount of the lien.

⁶⁹ 345 U.S. 361, 366 (1953). It seems somewhat peculiar that the Supreme Court should suggest that acquiring *title* may be a prerequisite to perfecting a lien. Such an acquisition, prior to the existence of a federal claim, would mean that the "lienor" was the property owner anyway. The divested debtor's subsequent federal obligation would be irrelevant.

The thrust of this decision is that "'specificity' requires that the lien be attached to certain property by reducing it to *possession*, on the theory that the United States has no claim against property no longer *in the possession* of the debtor." *Id.* (emphasis added). There is apparently some confusion in this area as to whether the possession requirement applies to liens on real estate. See *Plumb, supra* note 44, at 234-35.

⁷⁰ See *Meaders, supra* note 60, at 289. But Kennedy asserts that the Court settled the issue as early as 1828 by holding a mere equitable lien superior to United States priority in *Conard v. Atlantic Ins. Co.*, 26 U.S. (1 Pet.) 386 (1828). See *Kennedy, supra* note 62, at 909. The Court did find a specific lien based on its three criteria in *United States v. New Britain*, 347 U.S. 81 (1954). However, the Government's claim in *New Britain* was not based on the federal priority statutes. Perhaps the most explicit dictum that a specific lien will prevail over federal priority is Justice Brandeis' statement in *United States v. Knott*, 298 U.S. 544, 551 (1936), that a general and inchoate lien "lacks the characteristics of a specific perfected lien which alone bars the priority of the United States."

⁷¹ The Fourth Circuit has held a mechanic's lien arising under state law inferior to a competing federal claim on the ground that, although the lien had been filed and recorded, the lienholder had not secured a final judgment and enforced his claim against specific property of the debtor. *W.T. Jones & Co. v. Foodco Realty, Inc.*, 318 F.2d 881, 887 (4th Cir. 1963). Similarly, the Sixth Circuit recently granted preference to a federal claim over a municipal tax lien because the municipality had taken no action to attach its lien to specific property. *United States v. County of Wayne*, 378 F.2d 671, 672 (6th Cir. 1967) (per curiam), *cert. denied*, 389 U.S. 972 (1967).

federal claim;⁷² and there are dicta in the opinions of several other lower federal courts supporting this view.⁷³ The reluctance of most federal courts to find that a lien is specific and perfected under the Court's criteria, however, greatly reduces the significance of these opinions. Indeed, the current trend seems to be toward holding almost all prior competing liens inferior to United States claims by simply labeling them general and inchoate, and thus side-stepping the more troublesome issue of the status to be accorded a specific and perfected lien. One commentator became so exasperated with this approach that he concluded that the category of general and inchoate liens as defined by the courts must "embrace practically every lien to be found in modern American law."⁷⁴ While such a statement may be somewhat over-inclusive, it would seem that little short of a judgment and execution on specific property of a debtor, thus divesting him of title and possession, is likely to satisfy the courts in their quest for specificity and perfection.⁷⁵

Apparently the only lien to escape the judicial conundrum of the "general and inchoate" vs. "specific and perfected" distinction is the ordinary mortgage lien. The original rationale for according a mortgage lien priority over a subsequently acquired federal claim was based on the common law theory that a mortgagee received title to the mortgaged property.⁷⁶ Thus, the debtor who mortgaged his property before he became indebted to the United States had no title or interest in the property to which federal priority could attach.⁷⁷ Although most states have abandoned the title theory and now view a mortgage as merely giving the mortgagee a lien on the mortgagor's property,⁷⁸ the Supreme Court has not yet had occasion to reverse its earlier holdings that a prior mortgage is entitled to priority over competing federal claims.⁷⁹ However, in view of the prevailing rule

⁷² See *United States v. Atlantic Municipal Corp.*, 212 F.2d 709, 711 (5th Cir. 1954).

⁷³ See *United States v. Saidman*, 231 F.2d 503, 505 (D.C. Cir. 1956); *United States v. Department of Indus. Relations*, 201 F.2d 857, 859 (9th Cir. 1953); *United States v. Haddix & Sons*, 252 F. Supp. 634, 636 (E.D. Mich. 1966).

⁷⁴ Kennedy, *supra* note 62, at 918.

⁷⁵ See note 71 *supra* and cases cited therein.

⁷⁶ See, e.g., *Thelusson v. Smith*, 15 U.S. (2 Wheat.) 396, 426 (1817); *United States v. Guaranty Trust Co.*, 33 F.2d 533, 537 (8th Cir. 1929), *aff'd on other grounds*, 280 U.S. 478 (1930); Meaders, *supra* note 60, at 290.

⁷⁷ See authorities cited note 76 *supra*.

⁷⁸ See Meaders, *supra* note 60, at 290.

⁷⁹ See Kennedy, *supra* note 62, at 918-19. Lower federal courts have continued to find that mortgages negate United States priority. See *United States v. Boston &*

that a mortgagee has only a lien, and the Court's current criteria for determining whether a lien is specific and perfected, it is possible that, if confronted with the issue today, the Court might be inclined to find at least some mortgage liens subordinate to subsequently acquired federal claims.⁸⁰ It would seem, therefore, that a fiduciary may reasonably anticipate that in a non-bankruptcy proceeding a federal claim will almost invariably be entitled to priority over an earlier lien, unless the competing lien has been enforced by judgment and execution on particular property of the deceased or insolvent debtor.⁸¹

2. *Bankruptcy proceedings.*

Because the Bankruptcy Act establishes its own system of priorities,⁸² section 3466 does not grant an absolute preference to federal claims in bankruptcy proceedings. Under the Bankruptcy Act four categories of competing claims are entitled to priority over debts due the United States: (1) costs and expenses of administering the assets of the insolvent debtor; (2) wages owed the employees of the insolvent debtor which were earned within three months of the commencement of the bankruptcy proceedings; (3) reasonable costs and expenses of creditors in securing the refusal or revocation of a confirmation of a discharge in bankruptcy, wage-earner plan, or other arrangement; and (4) taxes owed to any state or subdivision thereof.⁸³ While a thorough discussion of priorities in bankruptcy proceedings is beyond the scope of this article, it is clear that these four categories do not embrace the entire spectrum of competing obligations. Within the fifth priority afforded claims of the United States, section 3466 is applicable in the same manner as in a non-bankruptcy proceeding.⁸⁴

Berlin Transp. Co., 237 F. Supp. 1004, 1009 (D.N.H. 1964); *United States v. Anthony*, 231 F. Supp. 414, 421 (S.D. Iowa 1964); *Bank of Wrangell v. Alaska Asiatic Lumber Mills, Inc.*, 84 F. Supp. 1, 5 (D. Alas. 1949).

⁸⁰ See Meaders, *supra* note 60, at 290. In *Bank of Wrangell v. Alaska Asiatic Lumber Mills, Inc.*, 84 F. Supp. 1 (D. Alas. 1949), the court analyzed a mortgage lien in terms of the three federal tests of specificity and found it insufficient to be declared specific. However, the court deferred to the weight of precedent in allowing the mortgage lien to destroy federal priority. *Id.* at 5.

⁸¹ One exception to this observation is that expenses of administering the insolvent's assets take priority over federal claims. See, e.g., *Abrams v. United States*, 274 F.2d 8, 12-13 (8th Cir. 1960).

⁸² See Bankruptcy Act § 64 (a), 11 U.S.C. § 104 (a) (1964).

⁸³ *Id.*

⁸⁴ See *Small Business Administration v. McClellan*, 364 U.S. 446, 447 n.5 (1960); *United States v. Belkin*, 358 F.2d 378, 382 (6th Cir. 1966).

NOTICE REQUIRED TO IMPOSE PERSONAL LIABILITY UNDER
THE FEDERAL PRIORITY STATUTES

The foregoing sections of this article have all assumed that the fiduciary was fully apprised of an outstanding government claim against the estate of the decedent or insolvent prior to the distribution of assets. However, since the courts have held that a person may be subject to personal liability under section 3467 even though the United States has made no effort to assert its claim in probate or bankruptcy proceedings as other creditors are required to do,⁸⁶ every fiduciary needs to be thoroughly familiar with the requirements for adequate "notice" under the priority statute.

As early as 1804, in *United States v. Fisher*,⁸⁶ Chief Justice Marshall recognized that the imposition of personal liability under section 3467 should be limited to those cases in which the fiduciary has notice or knowledge of the existence of a United States claim.⁸⁷ While subsequent decisions have engrafted upon the statute a general requirement that a fiduciary have some knowledge of the Government's claim,⁸⁸ they have at best succeeded only in establishing the outer limits of what constitutes adequate notice. At the threshold the rules are clear. It is firmly established, for example, that a fiduciary will be personally liable if he fails to accord priority to United States claims after the Government has notified him, either

⁸⁶ See, e.g., *Viles v. Commissioner*, 233 F.2d 376 (6th Cir. 1956) (state probate proceeding); *United States v. Barnes*, 31 F. 705 (C.C.S.D.N.Y. 1887) (bankruptcy proceeding). In *United States v. Murphy*, 15 F. 589 (C.C.D. Ind. 1883), however, the court refused to impose personal liability upon a trustee in bankruptcy who distributed the assets in his possession knowing of an outstanding judgment of the United States against the debtor because the Government had knowledge of the bankruptcy proceeding and did not submit its claim therein.

If the United States does submit its claim in a probate proceeding, it is bound by the decision of the supervising court. See *United States v. Muntzing*, 69 F. Supp. 503 (N.D.W. Va. 1946); *United States v. Pate*, 47 F. Supp. 965 (W.D. Ark. 1942). If the Government submits a claim in a bankruptcy proceeding, its priority is governed by §64(a) of the Bankruptcy Act, 11 U.S.C. §104(a) (1964), and not by the priorities statutes exclusively. See *United States v. Gargill*, 218 F.2d 556 (1st Cir. 1955); *In re Silver*, 109 F. Supp. 200 (E.D. Ill.), *aff'd*, 204 F.2d 259 (7th Cir. 1953); *cf. District of Columbia v. Greenbaum*, 223 F.2d 633 (D.C. Cir. 1955). See notes 82-84 *supra* and accompanying text.

⁸⁶ 6 U.S. (2 Cranch) 358 (1805).

⁸⁷ Chief Justice Marshall stated: "I only say for myself, as the point has not been submitted to the court, that it [the priority statute] does not appear to me to create a *devastavit* in the administration of effects, and would require notice, in order to bind the executor, or administrator or assignee." *Id.* at 390 n.a.

⁸⁸ See, e.g., *United States v. Ricketts*, 27 F. Cas. 806 (No. 16,159) (C.C.D.C. 1825). See generally Annot., 41 A.L.R.2d 446, 450-52 (1955).

formally or informally, through its agent or representative, that it believes it has a claim against the assets he is responsible for administering, though the claim may not be perfected or even established as to amount.⁸⁹ Conversely, it is equally well settled that a fiduciary will not be personally liable under the statute unless he had some "knowledge" or "notice" of the United States claim before he undertook to distribute the assets of the decedent or insolvent.⁹⁰ Unfortunately, these general rules do not answer any of the questions of adequate notice that fall between the extremes they represent. Nor are the answers easily found by merely reciting the statements in many of the older cases that a fiduciary subject to the provisions of section 3467 is a trustee for the United States with the duties of a fiduciary acting for the United States.⁹¹ It is additionally unfortunate, moreover, that the recent case law has done little to fill this void. Two recent cases, for example, draw entirely different conclusions as to what constitutes adequate notice under the priority statutes. In 1966, in *United States v. Vibradamp Corporation*,⁹² the Government had contended that an "executor acts at his peril if he distributes the estate without first making certain that no branch of the Federal Government is holding a claim against the estate"⁹³ The district court, however, rejected this contention and held that the notice required under section 3467 "is *actual knowledge* of such facts as would put a prudent person on inquiry as to the existence of the claim of the United States."⁹⁴ Although this holding alone was sufficient to dismiss the action, the court continued in significant dictum to express its opinion of the obligation of a fiduciary under the priority statutes by asking:

⁸⁹ See *Viles v. Commissioner*, 233 F.2d 376 (6th Cir. 1956); *United States v. Kaplan*, 74 F.2d 664 (2d Cir. 1935); *United States v. Munroe*, 65 F. Supp. 213 (W.D. Pa. 1946); *United States v. Weisburn*, 48 F. Supp. 393 (E.D. Pa. 1943).

⁹⁰ See *Livington v. Becker*, 40 F.2d 673 (E.D. Mo. 1929); *Giovaninni Terranova*, 12 P-H Tax Ct. Mem. 1186 (1943); *Irving Trust Co.*, 36 B.T.A. 146 (1937); Rev. Rul. 66-43, 1966-1 CUM. BULL. 291. In *United States v. Eyges*, 286 F. 683, 684 (D. Mass. 1923), for example, the court said: "Where the tax is not brought to the trustee's or the court's attention, and he does not know of it, and no order is made for the payment of it, and he distributes the assets in accordance with the orders of the bankruptcy court, it would be plainly unjust and would be going beyond what the statute contemplated to hold that he is personally liable."

⁹¹ In *United States v. Barnes*, 31 F. 705, 707 (C.C.S.D.N.Y. 1887), for example, the court stated: "The assignee becomes a trustee for the United States, and is bound to pay their debt first out of the proceeds of the debtor's property."

⁹² 257 F. Supp. 931 (S.D. Cal. 1966).

⁹³ *Id.* at 935.

⁹⁴ *Id.* (emphasis in original).

Even if [the executor] . . . did recognize the existence of [a potential government claim] . . . , was he obliged to arouse this 'long sleeping dog' and suggest to the Government that it might assert a claim? Such conduct would hardly be in harmony with the interests of the beneficiaries under the will, to whom the executor has a fiduciary duty. But does the executor nonetheless fail at his peril to remind the Government of all the potential claims that it might have against the estate and suggest that they be prosecuted?⁹⁵

The court thought not. In its view of the statutory language "debts due the United States" could only have been intended to mean "those debts concerning which the Government has asserted a claim before the distribution is made."⁹⁶ For fiduciaries, such a rule was just too good to be true. One year later it was firmly rejected by the Tax Court in *Leroy K. New*,⁹⁷ the court holding that adequate notice under section 3467 required only that a fiduciary be "chargeable with knowledge of the debt to the United States."⁹⁸ Under the test adopted by the Tax Court, a fiduciary has sufficient notice of a United States claim when he is "in possession of such facts as that a faithful and fair discharge of his duty would put him on inquiry."⁹⁹ Moreover, once "on inquiry," his investigation must not only be thorough, it must include an inquiry to the federal government itself, since according to the court, a fiduciary "pursues a unilateral inquiry at his peril."¹⁰⁰ Any other conclusion, in the court's view, would make the fiduciary the sole arbiter of what the estate owed the Government, thus entirely nullifying the effect of section 3467.¹⁰¹

As *Vibradamp* and *New* reveal, as of 1967 the requirements of adequate notice under section 3467 are yet to be agreed upon by the courts. A fiduciary, however, should be aware of at least three

⁹⁵ *Id.* at 936.

⁹⁶ *Id.* In support of its view the court cited *Field v. United States*, 34 U.S. (9 Pet.) 182 (1835); *United States v. Crocker*, 313 F.2d 946 (9th Cir. 1963); and *Want v. Commissioner*, 280 F.2d 777 (2d Cir. 1960). Of these cases, only the language of *Want* directly supports the proposition that the federal government must have actually asserted a claim prior to distribution. See 280 F.2d at 783.

⁹⁷ P-H TAX CT. REP. ¶ 48.65 (Aug. 9, 1967).

⁹⁸ *Id.* at 482.

⁹⁹ *Id.* Paradoxically, the notice to the fiduciary consisted of opinions that the decedent owed income taxes from persons who did not appear to have knowledge of any facts which could cause the imposition of a tax. In fact, the tax was due because of income which was unknown to the persons who put the fiduciary "on inquiry."

¹⁰⁰ *Id.* at 483.

¹⁰¹ *Id.*

vital notice issues which may be determinative of his liability under the priority statutes:

1. *Must the fiduciary be informed of the Government's claim by an officer or agent of the United States?*

The cases which have considered this question have for the most part answered it in the negative. In 1826, for example, it was decided in *United States v. Clark*¹⁰² that notice of a government claim adequate for the imposition of personal liability under section 3467 does not have to emanate from an officer or agent of the United States. Over a century later, this view was reaffirmed by the Board of Tax Appeals in *Irving Trust Company*¹⁰³ when it stated:

If the [fiduciary] . . . has knowledge of the debt, it matters not how that knowledge was obtained. The [fiduciary] . . . cannot disregard or ignore the debt, and if he does, his breach of duty renders him liable personally.¹⁰⁴

While the court in *Vibradamp* did not reach the source of notice issue,¹⁰⁵ the holding of the Tax Court in *New* clearly supports the rule that a fiduciary need not acquire his notice of the government claim from a federal agent to be personally liable under section 3467.

The only reason, in good policy, for adopting a different rule, and imposing a requirement that adequate notice must be given by an officer or agent of the United States, is that without such a requirement the fiduciary must carry the often heavy burden of proving that he was without sufficient knowledge of the government claim to accord it the requisite priority under the statute.¹⁰⁶ Poten-

¹⁰² 25 F. Cas. 447 (No. 14,807) (C.C.N.Y. 1826).

¹⁰³ 36 B.T.A. 146 (1937).

¹⁰⁴ *Id.* at 148 (dictum). The Board of Tax Appeals held, however, that the fiduciary was not personally liable under § 3467 because it was unable to "discover anything in the record . . . which might have put a reasonably prudent trustee upon inquiry as to whether or not there was any debt due the United States." *Id.*

¹⁰⁵ However, the court's statement that there was no indication of how the fiduciary knew "or should have known" of the existence of the potential government claim, 257 F. Supp. at 936, appears to have left the door open to such proof had it been offered.

¹⁰⁶ The fiduciary undoubtedly has this burden of proof in assertions of tax liability pursuant to § 6901 (a) (1) (B) of the Internal Revenue Code. INT. REV. CODE OF 1954 § 6901 (a) (1) (B). It is not altogether clear whether he has this burden in other cases. The Government could well argue that it has proved a prima facie case of liability without any evidence of notice, which it would claim was a matter of defense. *Cf.* L.T. McCourt, 15 T.C. 734 (1950). In fact, the Government normally includes an allegation that the defendant had notice of the United States claim in its complaint. *See, e.g.,* *King v. United States*, 379 U.S. 329 (1964).

tial injustice may exist in placing the burden of proof of lack of knowledge of United States claims upon the person against whom personal liability under section 3467 is sought to be imposed. It is submitted, therefore, that the Government be required by rule or statute to prove that the fiduciary had knowledge of a United States claim at the time he satisfied other claimants before liability under section 3467 may be imposed.

2. *Must the Government actually assert its claim against the estate of the deceased or insolvent debtor prior to the distribution of assets by the fiduciary?*

Although the *Vibradamp* court stated unequivocally that the United States should be required to assert its claim prior to the distribution of assets as a condition precedent to the imposition of personal liability under section 3467,¹⁰⁷ few cases lend direct support to this view. On the other hand, both *New* and *Clark* clearly hold that adequate notice under the statute does not require that the Government actually assert its claim.¹⁰⁸ The latter rule will probably prevail, since under the *Vibradamp* approach the fiduciary is in a position, if he has indirect knowledge or notice of a potential claim not yet asserted by the Government, to thwart the effectiveness of the priority statutes by hastily distributing the assets of a deceased or insolvent debtor before federal preference can attach. It would seem, however, that this objection to requiring the Government actually to assert its claim before distribution of assets could be alleviated, if not overcome, by holding that fiduciaries may be personally liable for any distribution of assets made to hinder the collection of a United States claim.

3. *What actions should a fiduciary take to avoid personal liability if he knows of an actual or potential United States claim?*

It is clear that the actual assertion of a claim by the United States is sufficient notice to impose upon a fiduciary the duty of according priority to debts owing the United States.¹⁰⁹ Once the Government has asserted its claim and the fiduciary has knowledge of it, his duty under the priority statute demands that he make every effort to satisfy the federal claim before distributing assets to other claimants, which might deplete the estate of the decedent or in-

¹⁰⁷ 257 F. Supp. at 936. See notes 92-96 *supra* and accompanying text.

¹⁰⁸ See notes 98, 102 *supra* and accompanying text.

¹⁰⁹ See note 89 *supra* and accompanying text.

solvent below the amount due the United States.¹¹⁰ While it is arguable that such a duty may require, under some circumstances, that a fiduciary seek the aid of administrative or judicial determinations,¹¹¹ a fiduciary should not be made to retain, at his peril, assets in excess of the claim actually asserted by the United States, even though the Government may be permitted to increase the amount of its claim and demand that this increase be entitled to priority in a suit directed against either the estate or the transferees of the proceeds thereof.¹¹²

The more difficult issue, however, concerns the duty of a fiduciary after he has received information which indicates that the Government might have a potential, but unasserted, claim against the assets of the estate which he is responsible for administering. An executor, for example, may be aware that the decedent had taken substantial deductions or exclusions on his income tax returns, which may be contested by the Government if the returns are audited. If, after a thorough investigation of the basis of the decedent's tax reporting, the executor concludes that the treatment of these items was proper, albeit disputable, can he safely distribute the assets of the estate? This is basically the question posed by the court in *Vibradamp* when it asked whether a fiduciary should be required, at his peril, to "arouse this 'long sleeping dog' and suggest to the Government that it might assert a claim."¹¹³ Although the district court in *Vibradamp* concluded, in dictum, that such conduct would not be in harmony with the interests of the beneficiaries under the will, and, thus, not a proper action of executors,¹¹⁴ both *Clark* and *New* espouse a contrary conclusion. In *Clark* the district court held un-

¹¹⁰ See *United States v. Hurst*, 2 F.2d 73 (D. Wyo. 1924). In that case the court stated that a fiduciary could not rely on government inactivity after the issue of a potential claim was raised, "but should have reasonably pursued his activities to securing [sic] an adjustment of the matter before making distribution of the estate." *Id.* at 80; cf. *United States v. Kaplan*, 74 F.2d 664 (2d Cir. 1935).

¹¹¹ See notes 113-17 *infra* and accompanying text.

¹¹² In *United States v. Barnes*, 31 F. 705, 709 (C.C.S.D.N.Y. 1887), the court stated: "The assignee can ascertain, if he uses reasonable diligence, what part of the estate should be reserved to meet the claim of the government, and the rest of the estate can be distributed to the other creditors . . ."

¹¹³ 257 F. Supp. at 936. In *Irving Trust Co.*, 36 B.T.A. 146, 149 (1937), the court reached a similar conclusion: "The Commissioner says that the petitioner should have inquired of the collector whether or not any taxes were due. But the petitioner was under no duty to seek out unknown creditors of the bankrupt under the circumstances."

¹¹⁴ *Id.*

equivocally that after a fiduciary has been put on notice of a potential government claim, he is under a duty to accord that claim priority under section 3467.¹¹⁵ According to the court, a fiduciary must, if necessary, go so far as to "make inquiry at the proper [government] office" to ascertain if the potential claim actually exists.¹¹⁶ Similarly, in *New* the Tax Court held that a fiduciary, who is chargeable with knowledge of a possible federal tax liability, must inquire of the Internal Revenue Service whether they wish to assert a claim, or pursue "a unilateral inquiry at his peril."¹¹⁷

Important considerations may have been overlooked, however, in the *Clark* and *New* decisions. Both courts seemingly ignored the strong policy favoring the expeditious disposition of the estates of deceased and insolvent debtors. Such a policy is obviously thwarted by requiring every fiduciary to work his way through the maze of administrative procedures necessary to obtain a binding decision from any federal agency that it has no claim against the estate.¹¹⁸ In addition, the reasoning of the Tax Court in *New* that a different rule "would make the fiduciary the final arbiter of what the estate owed in tax, a result entirely nullifying all effect of [the priority statute] . . .,"¹¹⁹ does not distinguish adequately between the priority afforded federal claims by section 3466 and the duty imposed upon a fiduciary under section 3467. Section 3466 provides that United States claims have priority over all competing obligations,¹²⁰ and, under this section, the Government is entitled, despite a wrongful distribution of assets by the fiduciary, to trace the assets of the decedent or insolvent into the hands of all *gratuitous* trans-

¹¹⁵ 25 F. Cas. at 451.

¹¹⁶ *Id.*

¹¹⁷ P-H TAX CT. REP. ¶ 48.65, at 483 (Aug. 9, 1967).

¹¹⁸ Even the Internal Revenue Service recognizes that after a personal representative has requested prompt assessment of taxes due from a decedent under § 6501 (d) of the Code, and has had no response after eighteen months, he may distribute the assets in his hands without risk of liability under § 3467, albeit the Government may assert taxes due against the transferees if the decedent had submitted false or fraudulent returns. See Rev. Rul. 66-43, 1966-1 CUM. BULL. 291. Most states, however, impose a limit of six months for the filing of estate claims. Even if prompt assessment is requested, the estate may have to be open eighteen months waiting for IRS action. This is an unreasonably long period for many smaller estates to be open. For a good example of how §§ 3466 and 3467 may be utilized to frustrate the orderly administration of a receivership see *Pennsylvania Cement Co. v. Bradley Contracting Co.*, 274 F. 1003 (S.D.N.Y. 1920).

¹¹⁹ P-H TAX CT. REP. ¶ 48.65, at 483 (Aug. 9, 1967).

¹²⁰ See 31 U.S.C. § 191 (1964).

ferences for the satisfaction of its superior claim.¹²¹ Thus, to permit a unilateral inquiry by a fiduciary would not, as the Tax Court contended, "entirely nullify" the effect of the priority statutes, although it would, of course, seriously affect the ability of the United States to collect its debts, since it is unquestionably more difficult and costly for the Government to pursue its claims against many persons rather than one. However, a sound analysis of the problem should balance this practical hardship on the United States against the harsh result of imposing personal liability upon a fiduciary who may not have "acted dishonestly in any way [nor] . . . positively intended to thwart the Government's claim."¹²² A fiduciary with knowledge of a potential but unasserted government claim should not be subject to personal liability under the priority statute unless it can be shown that he acted unreasonably under the circumstances. Assuming *arguendo* that a fiduciary has an obligation under section 3467 with regard to unasserted claims,¹²³ he should be required, under a reasonableness test, to check the records of the decedent or insolvent to determine whether there is any substance to the potential government claim. If a fiduciary encounters a legal question in ascertaining if the facts indicate a valid federal claim, he should be entitled to rely on the advice of competent counsel. Once he has made a reasonable investigation of the relevant records, and, if necessary, consulted legal counsel, a fiduciary should not be required to ask the Government whether it intends to assert the potential claim in the future.

CONCLUSION

When the federal priority statutes were first enacted and earliest interpreted, individuals had few direct relations with the Government and, hence, little opportunity to become indebted to it. However, with the increasing proliferation of federal agencies which have contractual and statutory relations with many individuals and

¹²¹ See INT. REV. CODE OF 1954, §§ 6901 (a) (1) (A), 6322, 6323. See generally Annot., 94 A.L.R.2d 748 (1964). There is some question whether the Government can trace the proceeds of a wrongful distribution into the hands of innocent distributees in cases not involving taxes on a constructive trust fund theory. Compare *United States v. Anderson*, 66 F. Supp. 870 (D. Minn. 1946), and *United States v. Fisher*, 57 F. Supp. 410 (E.D. Mich. 1944), with *United States v. Vibradamp Corp.*, 257 F. Supp. 931, 937-38 (S.D. Cal. 1966).

¹²² *King v. United States*, 379 U.S. 329, 339 (1964).

¹²³ See notes 107-08 *supra* and accompanying text.

corporations, and with the imposition of a pervasive and far-reaching federal tax structure, a fiduciary must act with extreme care and clear direction, if he is to avoid unexpected personal liability under the priority statutes. The courts have generally provided the fiduciary with adequate guidance for determining most of the issues that may confront him, such as the types of representatives, claims, debtors, and competing obligations to which the statutes apply. Nevertheless, because the United States is not required to submit a formal claim against the assets of a decedent, as are other creditors in probate and bankruptcy proceedings, the potential for injustice exists under the personal liability provisions of section 3467.¹²⁴ This is especially true, if as some courts have held,¹²⁵ a fiduciary merely chargeable with knowledge of a potential and unasserted government claim is required to pursue a unilateral inquiry as to the actual existence of such a claim at his peril. In order to eliminate the possibility for injustice, and to facilitate the expeditious disposition of decedents' and debtors' estates, it is suggested that Congress clarify the degree of notice required for the imposition of personal liability under section 3467 of the federal priority statutes. If notice of unasserted claims is made sufficient, the fiduciary should only be required to act in a reasonable manner in ascertaining the merits of the claim and should not be required to seek a federal determination of the claim.

¹²⁴ Several courts have indicated that they recognize the potential for injustice inherent in such a rule. *See, e.g.,* *Massachusetts v. United States*, 333 U.S. 611, 635 (1948) (dissenting opinion); *United States v. Barnes*, 31 F. 705, 709 (C.C.S.D.N.Y. 1887).

¹²⁵ See notes 115-17 *supra* and accompanying text.