UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In re	:	Chapter 11
PLYMOUTH HOUSE HEALTH CARE CENTER, INC., et al.	:	
Debtor	:	Bankruptcy No. 03-19135F

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MEMORANDUM

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The above-captioned debtor—which now is a number of nursing home operating entities that have been consolidated as part of a confirmed chapter 11 plan of reorganization—has filed a motion seeking a determination of its real estate tax liability pursuant to 11 U.S.C. § 505(a). The Colonial School District, the Montgomery County Board of Assessment Appeals, the Montgomery County Tax Claim Bureau, Plymouth Township, and Montgomery County (hereinafter, the "Taxing Authorities") have filed a response to this motion. In this response, the Taxing Authorities seek to dismiss the motion by asserting that this bankruptcy court has no subject matter jurisdiction to determine the debtor's motion. Response, ¶ 5. They also seek dismissal contending that the debtor utilized an incorrect procedure in seeking a determination under section 505(a). Finally, they maintain that this motion is prohibited by the Tax Injunction Act and so must be dismissed.

After the Taxing Authorities' response was filed, the parties submitted a stipulation requesting that respondents' jurisdictional and procedural challenges be resolved prior to any evidentiary hearing on the underlying merits of the motion. I approved that stipulation. The movant and respondents have filed memoranda in support of

their respective positions; oral argument has also taken place. The issues posed by the Taxing Authorities are now ripe for adjudication.

I.

For purposes of the jurisdictional challenge, the following facts shall be considered true.

At the time of its bankruptcy filing, the debtor operated a senior care nursing facility in Plymouth Meeting, Pennsylvania. Motion and Answer, ¶ 1. This facility operated at 845 Germantown Pike, Plymouth Meeting, Pennsylvania. On August 1, 2001, the debtor leased the realty from its owner, Morris Manor Associates, for a fifteen-year period. Motion and Answer, ¶ 2, Ex. A. Paragraph 5.1 of the Lease provides in relevant part:

> Tenant at its sole cost and expense, shall pay when due all real estate taxes and assessments becoming due and payable against the Premises beginning on the Effective Date [of the lease] and all taxes, and assessments thereafter becoming due and payable during the Term of this Lease. . . .. Tenant shall have the right at its sole cost and expense and in good faith, to contest the validity of any such tax or assessment payable by Tenant under the terms of this Lease . . . .

Montgomery County, Plymouth Township, and the Colonial School District claim to have assessed and liened real estate taxes against this real estate in the amount of $216,249.22. Answer, ¶ 5. The debtor asserts that the total tax liability is $234,118.49. Motion, ¶ 17.

On June 1, 2004, the debtor and Morris Manor sold the facility and real estate to a third-party for $1,150,000. Motion and Answer, ¶¶ 25-26. The debtor contends

that this sale price represents the proper value of the real estate for tax purposes, and that the Taxing Authorities improperly used a much higher valuation when computing the taxes due on the realty. The debtor further asserts that a portion of the sale proceeds have been set aside to pay the challenged tax liability, pending a determination of the instant motion under section 505(a) of the Bankruptcy Code. If the debtor's motion is granted and the tax liability is reduced, the debtor avers that the portion of the sale proceeds equal to the tax reduction will be turned over to the debtor for distribution to creditors under the terms of its confirmed plan. If the motion is denied, these funds will be paid to the Taxing Authorities.

II.

A.

I turn first to the assertion by the Taxing Authorities that the debtor's motion for a determination of tax liability pursuant to section 505(a) is barred by the Tax Injunction Act (TIA), 28 U.S.C. § 1341. The TIA states:

> The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State.

If this statutory provision applies, a federal court is divested of jurisdiction over the state tax dispute. See, e.g., Gass v. County of Allegheny, 371 F.3d 134 (3d Cir. 2004); see generally In re Hechinger Inv. Co. of Delaware, Inc., 335 F.3d 243, 247 n.1 (3d Cir. 2003).

In considering the applicability of the TIA in a bankruptcy context, the Third Circuit Court of Appeals has explained: "It is well established, however, that the Tax Injunction Act does not prevent a Bankruptcy Court from enforcing the provisions of the Bankruptcy Code that affect the collection of state taxes." In re Hechinger, 335 F.3d at 247 n.1. More specifically, in considering a dispute involving section 505 of the Bankruptcy Code, my colleague, Bankruptcy Judge Stephen Raslavich, noted:

> To the extent that a bankruptcy court must determine a debtor's tax liability in an area where such a determination may otherwise be barred by the Tax Injunction Act, the overwhelming majority view is that Congress expressly conferred jurisdiction on bankruptcy courts to do so in § 505 of the Code.

In re Daniels, 304 B.R. 695, 700 (Bankr. E.D. Pa. 2003); see, e.g., In re Pontes, 310 F. Supp. 2d 447, 453 (D.R.I. 2004) ("[W]hile the jurisdictional bar of the TIA is indeed broad, § 505 appears to allow a federal court to exercise jurisdiction if the amount or legality of any tax, fine, or penalty relating to the tax needs to be determined in order to finalize the estate and move the bankruptcy case to closure.").

Similarly, the Seventh Circuit Court of Appeals has held:

> The district court thought itself and the bankruptcy court barred by the Tax Injunction Act, 28 U.S.C. § 1341, from reexamining Chandler's liability for use tax. The Act forbids federal courts to enjoin the assessment or collection of state taxes unless the taxpayer has no adequate remedy in the state courts. But Illinois is not trying to extract taxes from Chandler. It is trying to get a penalty in lieu of taxes from Stoecker's estate in bankruptcy. Its right to do so depends on whether Chandler owed use tax, and the district judge thought that a federal court cannot decide an issue of state tax law. That is incorrect. The Bankruptcy Code expressly authorizes bankruptcy courts to decide tax issues, 11 U.S.C. § 505(a)(1), and although state taxes are not specified, the courts have interpreted the statute to cover them . . . . The Act is anyway addressed only to injunctive remedies (or a declaratory judgment viewed as a

> preliminary to an injunction . . . , and no one is seeking an injunction against the state's going after Chandler for the taxes that the state believes Chandler owes it. If federal courts could not determine the debtor's liability for state taxes--if they had to abstain pending a determination of that liability in state court--bankruptcy proceedings would be even more protracted than they are.

In re Stoecker, 179 F.3d 546, 549 (7th Cir. 1999) (citations omitted), aff'd sub nom. Raleigh v. Illinois Dep't of Revenue, 530 U.S. 15 (2000); see also Adams v. Indiana, 795 F.2d 27, 29 (7th Cir. 1986).

Thus, numerous courts have held, and I agree, that bankruptcy court subject matter jurisdiction under section 505(a) is not affected by the provisions of the Tax Injunction Act. Therefore, I must deny the Taxing Authorities request to dismiss the debtor's section 505(a) motion on this basis.

B.

Next, the Taxing Authorities contend that the relief sought by the debtor can only be obtained by filing an adversary proceeding—i.e., a complaint accompanied by a summons—rather than by motion under Fed. R. Bankr. P. 9014. This procedural issue has been addressed by the Fifth Circuit Court of Appeals:

> Second, the normal procedure to determine the amount of a tax debt is for the debtor (or the IRS) to file a motion requesting that the bankruptcy court make the determination under 11 U.S.C. § 505. . . . Section 505 authorizes the court to determine "the amount or legality of any tax . . . whether or not previously assessed." 11 U.S.C. § 505(a)(1). This determination should be made under Rule 9014, which governs contested matters, because it does not fall within adversary proceedings as delineated by Rule 7001. . . . Under Rule 9014, "relief shall be requested by motion, and reasonable notice and

> opportunity for hearing shall be afforded the party against whom relief is sought." Fed. R. Bankr. P. 9014. The motion should state with particularity the grounds and the relief desired. Fed. R. Bankr. P. 9013.

Matter of Taylor, 132 F.3d 256, 262 (5th Cir. 1998) (citations omitted); accord, e.g., In re Carson, 227 B.R. 148 (S.D. Ind. 1998); In re Whelan, 213 B.R. 310 (Bankr. W.D. La. 1997).

To the extent that the Taxing Authorities need pretrial discovery to defend against this motion, Rule 9014—which governs contested matters—incorporates all of the discovery rules applicable to adversary proceedings. Thus, deciding a section 505(a) dispute by motion, rather than by complaint, will not prejudice their ability to prepare for an evidentiary hearing. See generally In re Orfa Corp., 170 B.R. 257, 275 (E.D. Pa. 1994).

Accordingly, I must reject respondents' request to dismiss this motion for lack of proper procedure.

III.

Finally, and most strenuously, the Taxing Authorities contend that there is no jurisdiction to determine this motion under section 505(a) because the debtor is actually seeking a determination of the real estate tax liability of Morris Manor Associates, and not its own liability. In so contending, the Taxing Authorities rely upon the Third Circuit's decision, Quattrone Accountants, Inc. v. Internal Revenue Service, 895 F.2d 921 (3d Cir. 1990), for the proposition that a bankruptcy court has no jurisdiction to determine the tax

liability of a non-debtor.[1] For the following reasons, I conclude that the respondents have misapplied the reasoning of Quattrone to this contested matter.

Section 505(a)(1) provides: "Except as provided in paragraph (2) of this subsection, the court may determine the amount or legality of any tax, any fine or penalty relating to a tax, or any addition to tax, whether or not previously assessed, whether or not paid, and whether or not contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction." Section 505(a)(2) identifies certain exceptions to this

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[1]Fed. R. Bankr. P. 9014(c) provides:

> Unless the court directs otherwise, the following rules shall apply: 7009, 7017, 7021, 7025, 7026, 7028-7037, 7041, 7042, 7052, 7054-7056, 7064, 7069, and 7071. An entity that desires to perpetuate testimony may proceed in the same manner as provided in Rule 7027 for the taking of a deposition before an adversary proceeding. The court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply. The court shall give the parties notice of any order issued under this paragraph to afford them a reasonable opportunity to comply with the procedures prescribed by the order.

(emphasis added). Thus, a bankruptcy court may direct that any of the adversary procedural rules will apply to a contested matter under Rule 9014. See Matter of Stavriotis, 977 F.2d 1202, 1204 (7th Cir. 1992).

Accordingly, while Fed. R. Bankr. P. 7012—which incorporates, inter alia, Fed. R. Civ. P. 12(b)(1)—is generally not applicable in contested matters, I hereby direct that Rule 7012 shall apply to this dispute. See In re Takeout Taxi Holdings, Inc., 307 B.R. 525, 533 n.7 (Bankr. E.D. Va. 2004); In re Kmart Corp., 290 B.R. 601, 604 n.1 (Bankr. N.D. Ill. 2002); see also In re LTV Steel Co., Inc., 307 B.R. 37, 48 (Bankr. N.D. Ohio 2004) (applying Rule 7016); In re MK Lombard Group I, Ltd., 301 B.R. 812 (Bankr. E.D. Pa. 2003) (applying Rule 7015). The stipulation of the parties requesting that I first determine the Taxing Authorities jurisdictional challenge implies their consent to such application.

By virtue of Rule 12(b)(1), a party may move for dismissal of a proceeding due to a lack of subject matter jurisdiction. See generally Lampe v. Xouth, Inc., 952 F.2d 697, 699 (3d Cir. 1991); Edwards v. Wyatt, 266 B.R. 64, 68 (E.D. Pa. 2001). I shall treat the instant response of the Taxing Authorities as a motion to dismiss under Rule 7012.

grant of power to determine tax disputes. The language of section 505(a), however, does not expressly limit its scope to tax disputes involving only the debtor in bankruptcy.

Some courts have held that the power of a bankruptcy court to resolve tax disputes, granted by Congress in section 505(a), must be restricted solely to those contested matters involving the tax liability of the debtor. See, e.g., In re Prescription Home Health Care, Inc., 316 F.3d 542, 547-48 (5th Cir. 2002); In re Brandt-Airflex Corp., 843 F.2d 90, 95-96 (2d Cir. 1988). In Quattrone, however, the Third Circuit Court of Appeals disagreed with the holding in Brandt-Airflex in part and stated: "[W]e disagree with the IRS that Section 505 limits the bankruptcy court's jurisdiction to determine tax liability to only debtors." Quattrone, 895 F.2d at 924.

Although it was clear to the Third Circuit that some restriction on the application of section 505(a) was contemplated by Congress—Congress did not intend for bankruptcy courts to become another Tax Court, empowered to determine all tax disputes regardless of the parties, id. at 925—if the debtor requests a determination of the tax liability of a non-debtor under section 505, a bankruptcy court has subject matter jurisdiction to do so if permitted by 28 U.S.C. § 1334, the bankruptcy jurisdictional statute. Id. at 926.

In other words, the constraint on the broad application of section 505(a) is provided by section 1334. Thus, a bankruptcy court will possess subject matter jurisdiction over a tax dispute under section 505(a) only if the outcome of the dispute is related to the debtor's pending bankruptcy case. And a tax dispute is "'related to' a bankruptcy proceeding when 'the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy'. . . [because it] could alter the debtor's rights, liabilities,

options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankrupt estate." In re Kaplan, 104 F.3d 589, 594-95 (3d Cir. 1997) (quoting Pacor, Inc. v. Higgins, 743 F.2d 984, 994 (3d Cir. 1984)).

In Quattrone, the Third Circuit concluded, based upon the facts surrounding that litigation, that a determination of the tax liability of a non-debtor was not related to the corporate debtor's bankruptcy case. Quattrone, 895 F.2d at 926. Conversely, in Kaplan, the appellate court concluded that a tax dispute involving a corporate non-debtor was related to the individual debtors' bankruptcy case, and therefore was within the bankruptcy court's power to adjudicate under section 105(a). Kaplan, 104 F.3d at 595. In Kaplan, the Court of Appeals explained:

> Applying these decisions to the facts of this case, we conclude that the dispute between the IRS and KBS is related to the Kaplans' bankruptcy proceeding. Here the debtors, Michael and Morris Kaplan, agreed to section 6672 responsible person liability, in effect guaranteeing that KBS's trust fund taxes would be paid in full. By virtue of their agreement with the IRS, if KBS failed to pay its trust fund taxes in full, the Kaplans would automatically be liable for the shortfall. If the IRS is allowed to allocate the pre-petition tax payments it received to non-trust fund taxes, there is no effect on the Kaplans--they are still 100% liable for the shortfall. If, however, the IRS is not permitted to designate how the payments will be applied, and the bankruptcy court is allowed to order the IRS to allocate the pre-petition payments to trust fund taxes first, then the Kaplans' responsible persons liability is reduced to the extent that the trust fund tax liability of KBS is likewise reduced. Thus, the outcome of the dispute between KBS and the IRS could conceivably affect, in a positive manner, the Kaplans' estate in bankruptcy.
>
> We find, therefore, that the bankruptcy court had jurisdiction over the dispute between KBS and the IRS.

Id.; see In re ACME Music Co., 196 B.R. 925, 930 (Bankr. W.D. Pa. 1996) ("The settled law, at least in the Third Circuit, is that a bankruptcy court, pursuant to 28 U.S.C. §§ 1334

and 157, (a) may determine the tax liability of a debtor regardless of the impact (and binding effect) which such determination may also have on non-debtors, but (b) may not determine the tax liability of non-debtors in those instances where such determination would not, in any way, directly and substantially affect the debtor's bankruptcy case.").

As in Kaplan, the outcome of this dispute is related to the bankruptcy case of the debtor, Plymouth House Health Care Center, Inc.

By its lease contract, the debtor is liable for payment of all real property taxes assessed against the realty. At present, the taxes claimed as owing by the Taxing Authorities are being held in a separate account. If the debtor prevails in its section 505(a) motion and the real estate tax obligation is reduced, the entire amount of the reduction will be payable solely to the debtor's estate, thereby increasing the funds available for distribution to its creditors. Clearly then, the outcome of this contested matter is related to this bankruptcy case. See In re Wolverine Radio Co., 930 F.2d 1132, 1142-43 (6th Cir. 1991) (agreement by debtor to indemnify non-debtor for tax liabilities renders tax dispute of the non-debtor related to the debtor's bankruptcy case); see generally Browning v. Levy, 283 F.3d 761, 773 (6th Cir. 2002) ("NW's claims against SSD are related to the bankruptcy proceeding because, if they had been brought during the proceeding, any recovery received by NW would have represented an asset, available for distribution to Nationwise's creditors and shareholders."); Matter of Xonics, Inc., 813 F.2d 127, 131 (7th Cir. 1987) (a "dispute is 'related to' the bankruptcy--meaning that it affects the amount of property available for distribution or the allocation of property among creditors.").

Accordingly, as the Third Circuit Court of Appeals in Quattrone has instructed that a bankruptcy court has the power to adjudicate a section 505(a) motion

involving the tax liability of a non-debtor, so long as the outcome is related to the debtor's bankruptcy case under 28 U.S.C. § 1334, and as the Court of Appeals also instructed in Kaplan that a debtor's agreement to pay the tax liability of a non-debtor renders the tax dispute related to the bankruptcy case, the request of the Taxing Authorities to dismiss this contested matter for lack of subject matter jurisdiction must be denied.[2]

An appropriate order shall be entered.

[2]This conclusion accords with Pennsylvania state court rulings affording lessees such as the debtor standing to challenge real estate tax assessments when the tenant is contractually liable to the owner/lessor for the payment of such taxes. See West Mifflin Area School District v. Board of Property Assessment, 802 A.2d 687 (Pa. Cmwlth. 2002); In re West Allegheny School District, 797 A.2d 414 (Pa. Cmwlth. 2002). In such situations, the lessee is the real party in interest. In this contested matter, the debtor, not Morris Manor Associates, is the real party in interest, as only the debtor's estate will benefit from the litigation.

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In re	:	Chapter 11
PLYMOUTH HOUSE HEALTH CARE CENTER, INC., et al.	:	
Debtor	:	Bankruptcy No. 03-19135F

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ORDER

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AND NOW, this 10th day of September 2004, for the reasons stated in the accompanying memorandum, it is hereby ordered that the request of the Colonial School District, the Montgomery County Board of Assessment Appeals, the Montgomery County Tax Claim Bureau, Plymouth Township, and Montgomery County to dismiss the debtor's motion is denied.

It is further ordered that on or before September 24, 2004, the parties shall jointly submit a proposed order establishing a discovery deadline and a suggested date for an evidentiary hearing on the merits of this motion.

BRUCE FOX
United States Bankruptcy Judge

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