

In the United States Bankruptcy Court

for the Southern District of Iowa

ROBERT E SHERWOOD and KRISTY A.
SHERWOOD
Debtor(s).

Bankruptcy No. 07-03404
Chapter 7

ROBERT E SHERWOOD
Plaintiff(s)

Adversary No. 07-30143

vs.

UNITED STATES OF AMERICA (IRS)
Defendant(s)

ORDER RE MOTION FOR SUMMARY JUDGMENT

On October 8, 2007, plaintiff Robert E. Sherwood filed the complaint in this proceeding to determine the dischargeability of income tax liability for tax years 2002 and 2003 pursuant to 11 U.S.C. § 523(a)(1). The parties agree that the debt is not of the kind or for the periods specified in 11 U.S.C. § 507(a)(8) and that § 523(a)(1)(A) is not an impediment to dischargeability. The issue is whether the debt is for a tax “with respect to which the debtor . . . willfully attempted in any manner to evade or defeat such tax.” 11 U.S.C. § 523(a)(1)(C).

On August 18, 2008, defendant United States, on behalf of the Internal Revenue Service (“IRS”), filed a motion for summary judgment. Sherwood resists. Telephonic hearing on the motion was held November 14, 2008. Nicole B. Engelhardt appeared as attorney for Sherwood. LaQuita Taylor-Phillips, a trial attorney for the United States Department of Justice, appeared for the IRS.

Standard for Summary Judgment

The Eighth Circuit has recognized that “summary judgment is a drastic remedy and must be exercised with extreme care” Wabun-Inini v. Sessions, 900 F.2d 1234, 1238 (8th Cir. 1990). On the other hand, “summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed to secure the just, speedy and inexpensive determination of every action.” Id. (quoting Celotex Corp. v. Catrett, 477 U.S. 317, 106 S.Ct. 2548 (1986)); Hartnagel v. Norman, 953 F.2d 394, 396 (8th Cir. 1992).

A court should grant summary judgment if the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c), incorporated by Fed.R.Bankr.P. 7056. A court considering a motion for summary judgment must view all inferences from the underlying facts in the light most favorable to the party opposing the motion. Matsushita Electric Industrial Co., Ltd. v.

Zenith Radio Corp., 475 U.S. 574, 587, 106 S.Ct. 1348, 1356 (1986) (quoting United States v. Diebold, Inc., 369 U.S. 654, 82 S.Ct. 993 (1962)).

An issue is genuine if it has a real basis in the record, and a genuine issue of fact is material if it might affect the outcome of the suit. Hartnagel v. Norman, 953 F.2d at 395. The moving party's initial burden is to inform the court of the basis for its motion and identify the portions of the record which show the lack of a genuine issue for trial. Id. When a motion for summary judgment is properly made and supported, an opposing party may not rely merely on allegations or denials in its own pleading; rather, its response must—by affidavits or as otherwise provided in this rule—set out specific facts showing a genuine issue for trial. Fed.R.Civ.P. 56(e)(2).

It is not the court's function to "weigh the evidence and determine the truth of the matter, but to determine whether there is a genuine issue for trial." Waitek v. Dalkon Shield Claimants Trust, 908 F.Supp. 672, 676-77 (N.D. Iowa 1995) (citing Johnson v. Enron Corp., 906 F.2d 1234 (8th Cir. 1990)). Although summary judgment may be appropriate in some cases where mental state or intent is at issue, Demerath Land Co. v. Sparr, 48 F.3d 353, 355 (8th Cir. 1995), issues of intent usually raise questions for determination by a factfinder. United States v. One 1989 Jeep Wagoneer, 976 F.2d 1172, 1176 (8th Cir. 1992).

Undisputed Facts

The following is a brief summary of undisputed facts relevant to this motion. Since 1993, Sherwood has operated a roofing and gutter business known as Home One. In June 2001, Sherwood opened a checking account in the name of Home One at Midstates Bank. He used this account for both business and personal expenses.

Sherwood did not make estimated income tax payments during tax years 2002 or 2003. Sherwood filed a timely 2002 tax return reporting adjusted gross income of \$148,237 and tax due of \$37,481.00. Enclosed with the return was a check for \$38,734.00. Sherwood knew at the time the return was mailed that he did not have sufficient funds in his bank account to cover the check. The check was returned for insufficient funds.

Sherwood's 2003 tax return was timely filed. He reporting adjusted gross income of \$146,699 and tax due of \$34,126.00. When he mailed the return with a check for \$35,007.00 he knew that his bank account balance at that time was not sufficient to cover the check. The check was not honored.

Sometime in 2003, Sherwood entered into an installment agreement with the IRS. Payments made under the agreement were applied toward his income tax liability for tax year 2002. The first payment was made in February 2004. Of the 14 payments made, three were made with checks that were returned for insufficient funds.

In 1999, Sherwood acquired real property at 18143 Bent Tree Ridge, Council Bluffs, and subsequently built a residence on the property that was approximately 7,000 square feet in size. At the time the residence was built, Sherwood considered it a luxury home. He lived at this property from about May or June 2000 until March 2007.

On November 12, 2002, Sherwood prepared a financial statement listing his net worth as \$1,228,600. He valued his residence at \$1,600,000 and stated that his mortgage balance was \$560,000. He listed four vehicles having a total value of \$58,000.

Willful Attempt in Any Manner to Evade or Defeat Tax

A Chapter 7 discharge does not discharge debt for a tax “with respect to which the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat such tax.” 11 U.S.C. § 523(a)(1)(C). The burden of proof under 11 U.S.C. § 523(a)(1)(C) is on the taxing authority to demonstrate by a preponderance of the evidence that the taxes are nondischargeable. May v. Missouri Dept. of Revenue (In re May), 251 B.R. 714, 717 (B.A.P. 8th Cir. 2000).

This ground for nondischargeability contains both a conduct element, that the debtor sought “in any manner to evade or defeat” the tax, and an intent element, that the debtor did so “willfully.” Matter of Birkenstock, 87 F.3d 947, 951 (7th Cir.1996); In re May, 251 B.R. at 718. Nonpayment of the tax is not enough, in itself, to find the debt nondischargeable. Birkenstock, 87 F.3d at 951. In order to prove a willful attempt to evade or defeat a tax, the taxing authority must show that the debtor was aware of the duty to pay his taxes, had the wherewithal to pay the taxes and took steps to avoid paying them. In re May, 251 B.R. at 718. The Bankruptcy Appellate Panel for the Eighth Circuit, in In re May, listed several factors which indicate a willful attempt to evade or defeat a tax obligation. These include “understatements of income, failure to file tax returns, implausible or inconsistent behavior by the taxpayer, the failure to cooperate with the tax authorities, concealment of assets, dealing in cash, shielding income and otherwise frustrating collection efforts.” 251 B.R. at 718.

Discussion

The IRS contends that Sherwood had the ability to pay his taxes but took several affirmative steps to avoid paying them. The government argues that Sherwood repeatedly submitted insufficient funds checks to the IRS as part of an implausible scheme to avoid his tax obligation, that he chose to spend his money on a lavish lifestyle rather than paying his taxes, and that he used his business checking account for personal expenses to shield his income from collection by the IRS. The IRS asks the court to rule that Sherwood’s conduct constitutes a willful attempt to evade or defeat his tax obligations for 2002 and 2003 as a matter of law.

Sherwood denies that he had the wherewithal to pay his tax obligations. His failure to make estimated tax payments, he says, was consistent with his prior practice. He denies that he intentionally submitted bad checks to the IRS. He states that he intended to make the checks good either with business income or with a loan from Midstates Bank as he had done in prior years. He acquired certain valuable assets prior to becoming indebted to the IRS. He contends that he was unable to pay his taxes for 2002 and 2003 because he was struggling to pay necessary personal expenses and to keep his business operating. He argues that his practice of using his business bank account also for personal expenses did not constitute a concealment of income and was not done with the intention of frustrating collection efforts.

The court concludes that Sherwood has met his obligation under Fed.R.Civ.P. 56(e) to identify genuine issues for trial.

IT IS ORDERED that the motion for summary judgment is denied. The clerk shall set a telephonic scheduling conference to pick a trial date.

DATED AND ENTERED January 13, 2009

William L. Edmonds

Bankruptcy Judge