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Changes to Chapter 12 Bankruptcy May Increase Farmers' Ability to Reorganize in Bankruptcy

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Farmers attempting to reorganize under Chapter 12 of the Bankruptcy Code may propose selling land as a means of generating cash to pay creditors. This sale creates a large capital gains tax, as the cost basis for the land is likely low. That capital gains tax has priority over general unsecured creditors, and the farmer needs to pay that capital gains tax in full to get a Chapter 12 plan confirmed.

Congress attempted to create an exception to the priority status for these taxes when it amended the Bankruptcy Code in 2005. That attempt was unsuccessful, as the Supreme Court held that capital gains tax liability arising from a post-petition sale was still entitled to priority in *Hall v. United States*, 132 S. Ct. 1882 (2012). This decision was based on statutory interpretation grounds.

In October 2017, Congress passed the Family Farmer Bankruptcy Clarification Act of 2017 to resolve the issue and annul the Supreme Court's decision. The Act created a new section 1232 of the Bankruptcy Code. Under section 1232, an unsecured claim of a governmental unit arising from the pre- or post- petition sale of property used in the farmer's farming operation is treated as a pre-petition unsecured claim that is not entitled to priority. Additionally, that tax liability can be paid under the plan and is dischargeable. This change should make it easier for family farmers to reorganize under Chapter 12.

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