



Not Reported in F.Supp.2d, 2002 WL 31174181 (E.D.Mich.), 90 A.F.T.R.2d 2002-6307
(Cite as: **2002 WL 31174181 (E.D.Mich.)**)

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United States District Court,
E.D. Michigan, Southern Division.
UNITED STATES OF AMERICA, Plaintiff,

v.

Diane RUSSELL, in her capacity as Representative
of the estate of Gregory Russell (aka Gregory Le-
Coursier), Defendant.

No. 00-75597.

Aug. 22, 2002.

*OPINION AND ORDER (1) GRANTING
PLAINTIFF'S OBJECTIONS TO THE MAGIS-
TRATE JUDGE'S ORDER DENYING PLAINTIFF'S
MOTION TO FOR LEAVE TO AMEND THE COM-
PLAINT, (2) REVERSING THE MAGISTRATE
JUDGE'S ORDER, AND (3) REOPENING THE
CASE*

BORMAN, J.

*1 Before the Court is Plaintiff's appeal of (i.e., objections to) the Magistrate Judge's March 6, 2002 Order^{FN1} denying Plaintiffs' motion for leave to amend the complaint (Docket Entry # 21). Upon consideration of the objections, the submissions of the parties, the oral argument, and the applicable law, the Court will REVERSE the Magistrate Judge's Order, and GRANT leave to permit the United States of America to file an amended complaint.

FN1. The Magistrate Judge had originally denied the motion from the bench on February 14, 2002; the March 6, 2002 Order was the written order which the parties stipulated was consistent with the previous bench ruling.

I. BACKGROUND

The Government now seeks to amend its complaint to sue Diane Russell in her individual capacity. The original suit was filed against Ms. Russell in her representative capacity, as the Independent Personal Representative of the Estate of Gregory Russell (aka Gregory LeCoursier), her late husband. The parties stipulated to a judgment on March 26, 2002, against Ms. Russell in her representative capacity, for the unpaid assessed balance of federal income taxes owed by Mr. Russell (aka LeCoursier) prior to his death. The Government now seeks to pursue its claim for taxes by amending the complaint to state a claim against Ms. Russell personally.

The operative facts are not in dispute. At the time of his death, Mr. Russell (aka LeCoursier) had pre-existing, unpaid federal income tax liabilities for the years of 1984, 1985, and 1995.^{FN2} In December of 1989, the IRS filed a Notice of Federal Tax Lien as to each liability (1984 and 1985) with the Register of Deeds in Wayne and Oakland Counties, in Michigan. Those tax liens operated as to Mr. Russell's only asset-his property (a condominium) located in Southfield, Michigan.

FN2. The 1995 tax liability is not in dispute in the current case-it was paid by Ms. Russell in May of 2000.

Those federal tax liens "self-released" (i.e., expired by their terms) in March of 1998 and September of 1999 respectively. The IRS did not timely re-file the notices.^{FN3} In June of 2000, Ms. Russell, after consulting a tax attorney, caused the condominium to be transferred into her name, allegedly to enable her to mortgage the property in September of 2000 and use the proceeds to pay the debts of Mr. Russell's estate.

FN3. The IRS did file a Revocation of Certificate of Release of Federal Tax Lien and new Notice(s) of Federal Tax Lien on November 21, 2000. However, those filings are immaterial, because the allegedly

improper transfer occurred in June of 2000, five months prior to the re-filing-at the time of the transfer, in other words, there was no effective tax lien on file.

The existence of the underlying tax liability is not in dispute. The parties have stipulated that the Estate of Mr. Russell remains indebted to the Government (IRS) for the tax liabilities.

The Magistrate Judge denied, via Order dated March 6, 2002, Plaintiff's motion to amend its complaint to sue Diane Russell in her personal capacity. Plaintiff is now objecting to that Order.

II. ANALYSIS

A. Standard of Review of Magistrate's Ruling

The standard of review under 28 U.S.C. § 636(b)(1)(A) and Fed.R.Civ.P. 72(a) prescribes that a magistrate's nondispositive pretrial orders shall not be disturbed unless "found to be clearly erroneous or contrary to law." *United States v. Curtis*, 237 F.3d 598, 603 (6th Cir.2001) ("A district court shall apply a 'clearly erroneous or contrary to law' standard of review for the 'nondispositive' preliminary measures of § 636(b)(1)(A)."). The "clearly erroneous" standard mandates that the district court affirm the magistrate's decision unless, on the entire evidence, it "is left with the definite and firm conviction that a mistake has been committed." *Ocelot Oil Corp. v. Sparrow Industries*, 847 F.2d 1458, 1464 (10th Cir.1988) (quoting *United States v. United States Gypsum Co.*, 333 U.S. 364, 395, 68 S.Ct. 525, 92 L.Ed. 746, (1948)). In the absence of clear error, the magistrate's order must stand. See *Farley v. Farley*, 952 F.Supp. 1232, 1235 (M.D.Tenn.1997).

*2 The Magistrate Judge ruled that this claim would be subject to dismissal as a matter of law, it would be "futile," and under Fed.R.Civ.P. 15, and thus that the Government was not entitled to amend

its complaint to bring a futile claim. The Court concludes that Plaintiff has established a clear error of law in the Magistrate Judge's ruling; that it would not be futile to amend the complaint under Rule 15.

B. Analysis

Under FED. R. Civ. P. 15(a), leave to amend a complaint should be freely given "when justice so requires." There are several factors to consider when determining whether to grant a motion to amend: "undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of amendment." *Thiokol Corp. v. Department of Treasury, State of Michigan, Revenue Div.*, 987 F.2d 376, 382 (6th Cir.1993). The controlling factor at issue here is "futility," to wit, the Court should not grant a motion to amend if the amendment could not withstand a motion to dismiss. *Id.* at 382-83.

The Government's argument is that personal liability is imposed upon Ms. Russell via 31 U.S.C. § 3713(b), which states:

A representative of a person or an estate ... paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of the Government.

31 U.S.C. § 3713(b). Subsection (b) is the second part of the Federal Insolvency Statute, 31 U.S.C. § 3713. Subsection (a) provides for a priority benefiting the Government, which is then enforced via subsection (b). In other words, liability under § 3713(b) is predicated upon a priority granted by § 3713(a). If the Government is not entitled to a priority granted by § 3713(a), Ms. Russell cannot be held personally liable under § 3713(b), as a matter of law. Thus, Defendant argues the amendment is futile.

The Government argues that the Federal Insolvency

Statute operates as an alternative to the Federal Tax Lien Act, 26 U.S.C. § 6321 *et seq.* In other words, the Government argues that regardless of whether it maintained a priority via the tax lien, it still maintained a priority via the Federal Insolvency Statute.

In *United States v. Estate of Romani*, 523 U.S. 517, 118 S.Ct. 1478, 140 L.Ed.2d 710 (1998), the Government asserted that it should have been granted a priority for the deceased's unpaid tax liabilities, pursuant to 31 U.S.C. § 3713(a), although it had failed to file its Notice of Tax Lien prior to a judgment creditor's perfection and filing of its secured lien with regard to real property. The Supreme Court engaged in extensive statutory interpretation of the Tax Lien Act and Federal Insolvency Statute, noted that the Tax Lien Act is “the governing statute when the Government is claiming a preference in the insolvent estate of a delinquent taxpayer,” 532 U.S. at 532, and specifically held that “nothing in the text or the long history of interpreting the federal priority statute justifies the conclusion that it authorizes the equivalent of a secret lien as a substitute for the expressly authorized tax lien” which Congress provided in 23 U.S.C. § 6321. *Romani*, 532 U.S. at 534. Put another way, the Supreme Court expressly rejected the Government's argument in *Romani* that if the Government fails to follow the correct procedures for securing/maintaining its statutorily-authorized tax lien, it can somehow fall back onto 31 U.S.C. § 3713 in order to gain a priority over other secured creditors.

*3 In the instant case, because the Government was not entitled to a priority under 31 U.S.C. § 3713(a) since its tax lien had self-released (i.e., lapsed), it was not entitled to be paid before Bank One's secured/perfected lien against the property. However, the analysis does not end there; § 3713(a) operates as to other classes of creditors.

The tax lien priority statute is contained in 26 U.S.C. § 6323. Subsection (a) of that statute states that a tax lien (imposed by § 6321) “shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien credit-

or until notice thereof which meets the requirements of subsection (f) has been filed by the Secretary.” 26 U.S.C. § 6323(a). In other words, a tax lien will be granted a priority against those four types of creditors only if the tax lien is properly (and timely) filed (and refiled). But the statute is silent as to whether the tax liability has a priority against others (i.e., those that are not listed in § 6323). In order to determine whether the tax liability has a priority against all others, the Court must turn to 31 U.S.C. § 3713.

Title 31 U.S.C. § 3713 is not, strictly speaking, an alternative to 26 U.S.C. § 6323. *See, e.g., Romani, supra.* As to the four classes of creditors in § 6323, the statutes cannot operate together. In other words, in the situation presented in *Romani*, the Supreme Court held that because § 6323 specifically addresses judgment lien creditors (and others, for instance, secured creditors), the Government cannot rely on § 3713, when the filing or refiling of the tax lien is not effectuated in accordance with §§ 6323(f) & (g), in order to gain a priority over creditors who have properly perfected their liens. However, *Romani* did not specifically address at least part of the situation here.

Section 3713(a)(1)(B) states that the Government is entitled to be “paid first when ... the estate of a deceased debtor, in the custody of the executor or administrator, is not enough to pay all debts of the debtor.” This statute applies to creditors other than the four classes of creditors specifically addressed in § 6323(a). In other words, the Government is entitled to priority over other creditors except “purchaser[s], holder[s] of a security interest, mechanic's lienor[s], or judgment lien creditor[s]” and those others listed in § 6323(b).^{FN4}

FN4. Section 6323(b) also lists exceptions to the Government's priority, but those individually listed items do not appear to be applicable to the instant case, and neither party has asserted that they are.

At the time Ms. Russell transferred the property to

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herself, and mortgaged it, it was not encumbered by a tax lien. However, the underlying tax liability still existed-it just could not, according to § 6323(a), take priority over “purchaser[s], holder[s] of a security interest, mechanic's lienor[s], or judgment lien creditor[s].” It can still, however, take priority over, for instance, the beneficiaries of Mr. Russell's estate.

Thus, it is factually possible that, at some point, it will be determined that Ms. Russell has appropriated funds to which she is not entitled, in derogation of the estate's debt to the Government. The Government argues that if that becomes true, personal liability under § 3713(b) will attach.

*4 The Government is correct, and is therefore entitled to amend its complaint to set forth a cause of action against Ms. Russell in her individual capacity; such an amendment would not be “futile.” Thus, the Court concludes that Plaintiff has established a clear error in the Magistrate Judge's ruling rejecting the amendment to the complaint.

The Magistrate Judge's ruling is therefore REVERSED.

III. ORDER

For the reasons stated above, the Court REVERSES the Magistrate Judge's Order, and REOPENS the case. Plaintiff should file its amended complaint within ten (10) days of the date of this Order.

SO ORDERED.

E.D.Mich.,2002.

U.S. v. Russell

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