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Liens - Relative Priority of Federal and Municipal Statutory Liens

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Some statutes creating juvenile courts have been held invalid because the jurisdiction had been conferred on courts or officers whose powers were so limited by the constitution of the state as to exclude the exercise of the intended powers.¹¹ Section 103 of the North Dakota Constitution which defines the jurisdiction of the District Courts also limits that jurisdiction as provided elsewhere in the Constitution. Section 113 gives to police magistrates jurisdiction over all cases arising under city ordinances and this would appear to be a limitation on the jurisdiction of the District courts. The dissenting judges in the instant case so considered it.¹²

The contention of the majority in the instant case was that a municipality, being a creature of the state, has only those powers granted to it by the legislature. But the legislature, in passing the juvenile court act, limited the operation of municipal ordinances and not the jurisdiction of city magistrates to hear cases arising under those ordinances. Thus the majority circumvented what appeared to be a conflict between a statute and a constitutional provision. This reasoning appears to give the legislature the indirect power to sharply curtail the constitutionally granted jurisdiction of city magistrates.

Thus while the majority have undoubtedly reached a socially desirable result the reasoning of the minority seems more in keeping with strict legal interpretation.

JAMES A. MURRAY.

LIENS — RELATIVE PRIORITY OF FEDERAL AND MUNICIPAL STATUTORY LIENS.—Two mortgages on the real property of a corporation were foreclosed by judgment sale and the gross sum realized was \$27,071.34. Against this fund were \$31,000 in claims, including expenses of the sale, the two mortgages, a judgment of record, a federal statutory lien and a municipal statutory lien. Following a Connecticut statute providing that real estate tax liens shall take precedence over all transfers and encumbrances in any manner affecting the property subject to the lien,¹ the Supreme Court of Errors of Connecticut affirmed² the lower court's determination that the claims should be paid in the following order: the expenses, the city's liens, the mortgages, the judgment lien and the federal lien. The United States appealed the decision on the ground that the city's liens should not have been given priority over the federal liens. On certiorari the Supreme Court of the United States held that the judgment be vacated. The relative priority of the federal and municipal claims should be determined by the principle, "first in time is first in right." *United States v. City of New Britain, Conn.*, 74 S.Ct. 367 (1954).

Priority of federal tax liens over other liens and encumbrances is governed by § 3466 of the Revised Statutes³ and §§3670-2 of the Internal Revenue

11. *State v. Tincer*, 258 Mo. 1, 166 S.W. 1028 (1914); *Pugh v. Bowden*, 54 Fla. 302, 45 So. 499 (1907); *Hunt v. Wayne Circuit Judges*, 142 Mich. 93, 105 N.W. 531 (1905).

12. See *State ex rel City of Minot v. Gronna*, 59 N.W.2d 514, 541 (N.D. 1953) (dissenting opinion).

1. Conn. Gen. Stat. 1949, c. 88, §1853.

2. *Brown v. General Laundry Service, Inc.*, 139 Conn. 363, 94 A.2d 10 (1952).

3. Rev. Stat. §3466, 31 U.S.C. §191 (1946). "Whenever any person indebted to the United States is insolvent . . . the debts due to the United States shall be first satisfied . . ."

Code.⁴ Section 3466 provides for an "absolute" priority⁵ of federal claims where the debtor is insolvent, while §§3670-2 provide for the establishment of the federal lien, period of the lien, and validity against certain classes of creditors.⁶ There is no schedule of priority, as such, set forth in §§ 3670-2.⁷ The Connecticut Court anticipated the Supreme Court's result, as stated above, when it considered the facts as governed by §§3670 and 3671 alone,⁸ but concluded that when § 3672 was applied a different result ensued. This conclusion was reached via the assumption that if the mortgagee paid the municipal taxes (as was permitted by a Connecticut statute)⁹ the amount paid would become part of the privileged mortgage debt and receive priority as such over the federal lien.¹⁰ As a result, according to the Connecticut Court, the priority of such municipal taxes would depend on the election of the mortgagee to pay the taxes, and this would lead to an anomalous situation¹¹ which could not have been intended by Congress. It was therefore argued that Congress intended the federal liens to rank behind those statutory liens which could enjoy priority over the privileged encumbrances.

In disposing of the Connecticut Court's theory, the Supreme Court deftly avoided any involvement in the problem of circuity of priority by simply stating that the United States is not interested in whether the State receives its revenue prior to other creditors even where the other creditors are privileged under §3672. "That is a matter of state law."¹² The United States, then, is to be paid from any funds in excess of the amount necessary to pay the privileged creditors. The court summed it up by saying that there is nothing to show that Congress intended antecedent federal tax liens to rank behind any interests except those specifically set out in §3672.

The result here seems in accord with the theory of federal tax preference over state or municipal taxes because of wider public interest.¹³ The result also seems equitable in view of the cases holding that a state cannot impair the standing of federal liens without the consent of Congress.¹⁴

4. Int. Rev. Code §§3670-2.

5. The "absolute" portion is subject to conjecture in view of the instant decision.

6. Int. Rev. Code §3670 provides. "If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount . . . shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person." §3671 provides, "Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time." §3672 provides, "Such lien shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector . . . in accordance with the law of the State or Territory in which the property subject to the lien is situated . . . ; or in the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated . . . ; or in the office of the clerk of the District Court of the United States for the District of Columbia . . ."

7. *United States v. City of New Britain, Conn.*, 74 S.Ct. 367, 370 (1954).

8. *Brown v. General Laundry Service, Inc.*, 139 Conn. 363, 94 A.2d 10, 14 (1952).

9. Conn. Gen. Stat. 1949, c. 361, §7192.

10. But see *Anderson, Federal Tax Liens—Their Nature and Priority*, 41 Calif. L. Rev. 241 (1953). "Even if the mortgagee has in fact paid the local lien, he is not by that fact alone entitled to priority over the federal lien; the mortgagee has merely made a subsequent advance, which may or may not be entitled to the priority of the original debt."

11. See *Board of Supr's. of L.S.U. v. Hart*, 210 La. 78, 26 So.2d 361, 366 (1946).

12. *United States v. City of New Britain, Conn.*, 74 S.Ct. 367, 372 (1954).

13. See *Sarner, Correlation of Priority and Lien Rights in the Collection of Federal Taxes*, 95 U. of Pa. L. Rev. 739, 746 (1947).

14. *Michigan v. United States*, 317 U.S. 338 (1943); *United States v. Snyder*, 149 U.S. 210 (1893).

The Connecticut Court, in its adjudication of the case, dealt with the municipal liens as being specific and perfected.¹⁵ This characterization by a state is not conclusive against the federal government,¹⁶ but the Supreme Court in the instant case accepted the state court's holding as to the specificity of the liens, since they attached to specific pieces of real property for the taxes assessed. The court also stated that the liens were perfected in that there was nothing more to be done to have a choate lien.¹⁷ The liens of the United States' were held to be general and perfected¹⁸ but the fact that the federal liens were general and the city's liens specific will not give the city priority.¹⁹

Thus priority, the Supreme Court concluded, should be determined by the principle, "First in time is first in right,"²⁰ since the competing liens were equal in stature.

The acceptance of the city's liens as meeting the requirements of specificity and perfection is worthy of note.²¹ The Supreme Court had heretofore assiduously avoided answering any question of priority until their requirements had been met,²² and their refusal has engendered a great deal of legal opinion as well as some conjectural solutions,²³ with the liens in the instant case admittedly specific and perfected and requiring the priority as set forth by the court, it would seem that the same requirements and priority would govern where the taxpayer was insolvent and within §3466.²⁴ At any rate, if the taxpayer in the instant case were insolvent, the court would, it is assumed, still consider the liens of the city as specific and perfected. As such their priority against the federal liens would, of necessity, be determined, and that determination might well be the same as in the instant case.

LOUIS R. MOORE.

15. *Illinois v. Campbell*, 329 U.S. 362 (1946) (The long established rule requires that the lien must be definite, and not merely ascertainable in the future by taking further steps, in at least three respects as of the crucial time. These are: (1) The identity of the lienor; (2) The amount of the lien; and (3) The property to which it attaches); *United States v. Alabama*, 313 U.S. 274 (1940).

16. *United States v. Security Trust & Sav. Bank*, 340 U.S. 47 (1950); *United States v. Waddill, Holland & Flinn Co.*, 323 U.S. 353 (1944).

17. *United States v. City of New Britain, Conn.*, 74 S.Ct. 367, 369 (1954) ". . . when the identity of the lienor, the property subject to the lien, and the amount of the lien are established."

18. See *Metropolitan Life Ins. Co. v. United States*, 107 F.2d 311 (6th Cir. 1939); *United States v. Sampsell*, 153 F.2d 731 (1946) (Where liens were considered by the court to be specific and perfected).

19. *United States v. City of Greenville*, 118 F.2d 963, 965 (4th Cir. 1941) (A lien is not deprived of validity because it attaches to a number of pieces of property instead of to a single piece, nor is it for that reason to be subordinated to a junior lien attaching to a single piece of property. When properly perfected, the lien under the statute constitutes a charge upon specific property of the taxpayer for the satisfaction of which that property may be sold.)

20. *United States v. City of New Britain, Conn.*, 74 S.Ct. 367, 370 (1954). See *Rankin v. Scott*, 12 Wheat. 177 (U.S. 1827).

21. See the discussion of liens in *Thelussou v. Smith*, 2 Wheat. 396 (U.S. 1817); also Clark, *Federal Tax Liens And Their Enforcement*, 33 Va. L. Rev. 13.

22. *Illinois v. Campbell*, 329 U.S. 362 (1946); *United States v. Waddill, Holland & Flinn Co.*, 323 U.S. 353 (1945); *United States v. Texas*, 314 U.S. 480 (1941); *United States v. Knott*, 298 U.S. 544 (1936); *New York v. Maclay*, 288 U.S. 290 (1933); *Spokane County v. United States*, 279 U.S. 80 (1921).

23. See *United States v. Waddill, Holland & Flinn Co. supra* note 22; *United States v. City of Greenville*, 118 F.2d 963 (4th Cir. 1941); Anderson, *Federal Tax Liens—Their Nature and Priority*, 41 Calif. L. Rev. 241 (1953); Clark, *Federal Tax Liens And Their Enforcement*, 33 Va. L. Rev. 13 (1947).

24. Cf. *United States v. Woodroof*, 253 Ala. 620, 46 S.2d 553, 561 (1950) "We feel justified, therefore, in acting of the assumption that it would hold that the priority set up in §3466 would not supersede a lien which was specific and perfected at the time when the receiver was appointed."