

## Attorneys:

- **Irve J. Goldman**  
igoldman@pullcom.com  
203.330.2213
- **Jonathan A. Kaplan**  
jkaplan@Pullcom.com  
860.424.4379
- **Jessica Grossarth Kennedy**  
jkennedy@pullcom.com  
203.330.2215

## Chapter 11 May Help Save Sales Tax Permits for Distressed Businesses

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Effective July 1, 2013, Connecticut passed a new law providing that the State must refuse to issue or renew a sales tax permit to any person or entity that owes taxes to the state until the taxes are paid or satisfactory arrangements are made for their payment. P.A. 13-150. Whether this new law would be enforceable if the delinquent taxpayer files a case under Chapter 11 of the U.S. Bankruptcy Code has not been tested in the Connecticut bankruptcy courts, but case authority from other jurisdictions suggests that it may be rendered ineffective when bankruptcy intervenes.

There are two sections of the Bankruptcy Code that would arguably apply to prevent the State from refusing to issue or renew a sales tax permit because of unpaid taxes. When a bankruptcy is filed, section 362(a)(1) of the Bankruptcy Code imposes an automatic stay, applicable to all entities, including the government, of any action or proceeding designed to recover a claim against the debtor that arose before the bankruptcy was filed. Such a claim would, of course, include unpaid taxes. Therefore, the refusal to issue or renew a sales tax permit until delinquent taxes are paid can be construed as an action or proceeding to recover a claim against the debtor.

The second provision that would arguably apply to this situation is section 525(a) of the Bankruptcy Code, which provides, in pertinent part, that the government may “not deny, revoke, suspend or refuse to renew a license, permit...or other similar grant to, condition such a grant to, [or] discriminate with respect to such grant against..., a person that is or has been a debtor [under the Bankruptcy Code]...solely because such bankrupt or debtor is or has been a debtor [under the Bankruptcy Code]...or has not paid a debt that is dischargeable [in the bankruptcy case]....”

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The theory for using section 525(a) to prevent the State from denying the issuance or renewal of a sales tax permit for unpaid taxes is that although most taxes, including sales taxes, are non-dischargeable in bankruptcy, Chapter 11 of the Bankruptcy Code allows the debtor to pay them over a period of five years from the date on which the bankruptcy is filed; and, a debtor under Chapter 11 is prohibited by law from making any payments on account of a claim that arose before the Chapter 11 was filed. Thus, a debtor in Chapter 11 would be legally prohibited from making payment on account of the particular unpaid taxes that would be holding up the issuance or renewal of a sales tax permit.

In analogous contexts, sections 362(a)(1) and 525(a), either singly or in combination, have been utilized by federal courts in other jurisdictions to prevent a state from withholding other types of licenses or permits because of non-payment of taxes. For example, courts have enjoined the State from refusing to renew or issue a liquor license, casino license and contractor's license to the debtor for its non-payment of taxes. Thus, there is strong statutory support and case law precedent for achieving the same result in Chapter 11 for a sales tax permit that might otherwise be lost for non-payment of taxes.

For questions about this Alert, please contact Attorney [Irve Goldman](#) in our Bridgeport office, at (203) 330-2213, or [igoldman@pullcom.com](mailto:igoldman@pullcom.com).

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