

## Lesson 4

### PRIORITY OF FEDERAL TAX LIEN

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#### CONTENTS

I.	INTRODUCTION .....	2
II.	OBJECTIVES .....	2
III.	ATTORNEY OUTLINE.....	2
IV.	DETERMINATION OF PROPERTY RIGHTS .....	3
A.	Attachment of Lien .....	3
B.	State Law and Federal Law Interaction .....	3
C.	Recording statutes .....	3
D.	Exemptions from Levy .....	3
E.	Constructive Trust.....	3
V.	PRIORITY OF FEDERAL TAX LIEN: I.R.C. § 6323 .....	4
A.	Framework and Requirements .....	4
B.	Notice.....	4
C.	Purchaser - Defined in Section 6323(h)(6): .....	4
D.	Mechanic's Lienor -- Defined in Section 6323(h)(2). .....	5
E.	Holder of Security Interest -- Defined in Section 6323(h)(1). .....	6
F.	Judgment Lien Creditor -- Not Defined in § 6323(h). .....	8
VI.	PRIORITY OF FEDERAL TAX LIEN: "FIRST IN TIME, FIRST IN RIGHT" .....	9
A.	Statutory Priority.....	9
B.	Common Law Priority - First in Time, First in Right.....	10
C.	Federal Question - Priority.....	10
D.	State Tax Liens .....	11
VII.	OTHER PRIORITY ISSUES .....	12
A.	After-Acquired Property .....	12
B.	Interest and Expenses.....	13
VIII.	FILING NOTICE OF FEDERAL TAX LIEN .....	13
A.	Filing .....	13
B.	When Should the NFTL Be Filed? .....	14
C.	Where Should the NFTL Be Filed? .....	15
D.	Contents of the NFTL .....	17
E.	Effect of Errors .....	17
IX.	REFILING NOTICE OF FEDERAL TAX LIEN .....	19
A.	Effect of Refiling .....	19
B.	Where Is the NFTL Refiled?.....	20
1.	In general, the notice of lien is refiled in the office where prior notice was filed. ...	20
X.	WITHDRAWAL OF THE NOTICE OF FEDERAL TAX LIEN.....	20
A.	Withdrawal Under Certain Circumstances – Section 6323(j).....	20
B.	Where to File Withdrawal.....	20
C.	Notice of Withdrawal.....	20

## **I. INTRODUCTION**

The federal tax lien attaches to all property interests of the taxpayer, but is often not the only lien against a taxpayer's property. In some cases, priority is determined by statute, notably section 6323. In other cases, priority is determined by the order in which the liens attach to the property ("first in time, first in right"). To achieve priority, it may be necessary for a notice of federal tax lien (NFTL) to be filed. The location for filing the NFTL is set by federal law, usually in the place where real property is located or where the taxpayer resides (for personal property). Tax liens may be refiled to extend their effectiveness.

The priority of federal tax liens also arises in other contexts, which are addressed in separate chapters of this text and the text for the GL Bankruptcy School. Bankruptcy law provides its own set of priorities for liens, and a bankruptcy trustee may avoid certain liens (though generally not tax liens). For situations where the taxpayer is in a non-bankruptcy insolvency proceeding, the Insolvency Statute, 31 U.S.C. § 3713(a), provides priority for federal debts. Also, where the taxpayer has transferred property, tax liens may be filed against alter egos, nominees, or transferees of the taxpayer.

## **II. OBJECTIVES**

At the end of this lesson you will be able to:

- Understand the relative priority of the tax lien against competing creditors.
- Be able to determine the location for filing the tax lien and the refiling requirements.

## **III. ATTORNEY OUTLINE**

This chapter deals primarily with the question of priority. This is merely a determination of who, among conflicting claimants, will come first.

**In making the determination you must always ask yourself:**

- Does the taxpayer have a legal interest in the property subject to the lien?
- Was a Notice of Federal Tax Lien properly filed?
- If the competing lien was filed before the tax lien, is the competing lien choate or entitled to a statutory priority?
- If the competing lien was filed after the tax lien, is the competing lien entitled to statutory superpriority?

Also in this chapter you will examine whether a taxpayer has sufficient interest in property for the federal tax lien to attach; where a notice of federal tax lien must be filed to be effective against specific types of property; and how to re-file the tax lien to extend its effectiveness.

## IV. DETERMINATION OF PROPERTY RIGHTS

### ***A. Attachment of Lien***

The federal tax lien attaches to all property and rights to property belonging to a taxpayer. I.R.C. § 6321.

### ***B. State Law and Federal Law Interaction***

**State law** initially determines whether a taxpayer has an interest or right in the property subject to the tax lien. Aquilino v. United States, 363 U.S. 509 (1960).

If a taxpayer has a property interest to which a federal tax lien attaches, the next question is whether that interest is property or rights to property under the Code. If so, the priority of the tax lien vs. competing liens is established by **Federal law**. United States v. Nat'l Bank of Commerce, 472 U.S. 713 (1985); United States v. Dishman Indep. Oil, Inc., 46 F.3d 523 (6th Cir. 1995); Mortgage Elec. Registration Sys., Inc. v. Church, 2009 WL 3498810 (W.D. Mich. 2009).

### ***C. Recording statutes***

The effect of recording statutes on a taxpayer's interest is not entirely clear. Consider the following situation: the taxpayer sells his real property to purchaser; next, the Internal Revenue Service (the "Service") assesses the tax liability, makes notice and demand, and then files a NFTL; then the purchaser records. After the sale of real property, does the taxpayer have an interest under state law to which the assessment lien can attach? In U.S. v. Creamer Indus., Inc., 349 F.2d 625 (5th Cir. 1965), the Fifth Circuit determined that the United States was a "creditor" protected under the Texas Recording Act. The federal tax lien attached to the real property in the gap between the sale and the recording. The Service filed its NFTL before the "purchaser" qualified for section 6323(a) protection. Conversely, the Tenth, Eighth, and First Circuits have rejected Creamer, reasoning that, after a transfer of real property, taxpayers had no property or rights to property in the gap between the sale and the recording date to which the assessment lien could attach. U.S. v. Gibbons, 71 F.3d 1496 (10th Cir. 1995); Thomson v. U.S., 66 F.3d 160 (8th Cir. 1995); U.S. v. V & E Eng'g & Constr. Co., 819 F.2d 331 (1st Cir. 1987).

### ***D. Exemptions from Levy***

The exemptions provided under section 6334 apply only to levy, not to tax liens. American Trust v. American Cmty. Mut. Ins. Co., 142 F.3d 920 (6th Cir. 1998).

### ***E. Constructive Trust***

Where a taxpayer has defrauded third parties of their property, the court may declare a constructive trust as to that property. Although the defrauding taxpayer has possession of the property, he has no interest in the property, and so the federal tax lien will not attach. But see Blachy v. Butcher, 221 F.3d 896 (6th Cir. 2000) (a constructive trust under state law cannot operate retroactively to defeat a

prior perfected federal tax lien).

## V. PRIORITY OF FEDERAL TAX LIEN: I.R.C. § 6323

### ***A. Framework and Requirements***

Section 6323 provides the framework for resolving most priority disputes with the federal tax lien. The rationale for section 6323 is that the section 6321 secret lien is burdensome on commerce. Section 6323 mitigates the burden on unwary and innocent persons who acquire property subject to the secret lien and give value for the property in the normal course of business. The provisions for filing a notice of federal tax lien under section 6323 supplant the case law choateness test, described later.

### ***B. Notice***

The Code requires that a Notice of Federal Tax Lien (NFTL) be filed before it may prime the interests of **purchasers, holders of security interests, mechanic's lienors, and judgment lien creditors.**

**Actual Notice** of an unfiled federal tax lien is of no consequence to interests named in section 6323(a). See Rev. Rul. 2003-108, 2003-2 C.B. 963. Those interests are protected on the grounds the law makes the federal tax lien "not ... valid" against them unless notice was filed, and imposes no condition with respect to lack of knowledge of the unfiled lien.

### ***C. Purchaser - Defined in Section 6323(h)(6):***

#### **1. Requirements:**

##### **a) Adequate and full consideration.**

(1) Marital consideration, love, and affection do not qualify--arm's length transaction price presumably is necessary.

(2) However, if past consideration is sufficient under local law to support the contract, then it is sufficient here. A bargain purchase normally will not be upset unless it is unrealistic.

##### **b) Money or money's worth.**

##### **c) Acquires an interest other than lien or security interest.**

##### **d) Purchaser must be protected under local law against subsequent purchaser without actual notice (interplay of state law again).**

(1) If filing or recording is required of the purchaser, then there is no protection until such filing/recording is accomplished.

(2) Possession of the property, however, may be sufficient under local law.

2. A **lease on property** or a written **executory contract to purchase or lease** are also protected. Likewise, **an option to purchase, lease, or renew a lease** is protected under this section.

#### ***D. Mechanic's Lienor -- Defined in Section 6323(h)(2).***

1. **Elements of a mechanic's lien.**

- a) Must be provided by local law.
- b) Must be on real property (or on the proceeds of a contract relating to real property).
- c) Labor or material in connection with the construction or improvement must have been furnished.

2. **Date of priority.**

- a) May be related back to date mechanic's work began, but not before--not even if state law provides that the lien relates back to the date of commencement of the entire project.
- b) Must be perfected under local law against a subsequent purchaser without actual notice--the mechanic's lien is good from then on.
- c) This date may be the date for the filing of a claim, the filing of a stop notice, etc.

3. A **superpriority** is granted to mechanic's liens for home repairs and improvements not exceeding \$5,000 (indexed annually for inflation) even if a notice of tax lien has been filed. I.R.C. § 6323(b)(7). The theory is that the work adds value to the property. See also § I.R.C. 6323(c)(3) (providing a priority for real property construction or improvement financing agreements).

#### 4. **Maritime Lien.**

- a) Takes priority over federal tax liens whether or not the tax lien had attached before the maritime lien. United States v. Flood, 247 F.2d 209 (1st Cir. 1957).
- b) Maritime liens are normally for work done and are in the general category of expenses for the preservation and maintenance of the ship or to protect a substantial public interest.

#### ***E. Holder of Security Interest -- Defined in Section 6323(h)(1).***

##### 1. **Four elements** of a security interest are:

- a) Must be a contract granting a security interest.
- b) Loan must have been made or obligation incurred.
- c) Collateral to which security interest attaches must be in existence.
- d) Security interest must prime a subsequent judgment lien creditor whose claim arises out of an unsecured obligation. (This is a different test than that for a purchaser). Treas. Reg. § 301.6323(h)-1(a)(1). In order for a security interest to have priority over a filed federal tax lien, it must be protected against all hypothetical judgment lien creditors. The Service's knowledge is not imputed to any hypothetical judgment lien creditor. In re Haas, 31 F.3d 1081 (11th Cir. 1994).

**Note:** These four elements must be met before the date of filing of a notice of federal tax lien in order for the security interest to take priority over the federal tax lien.

2. If the federal tax lien is invalid against the initial holder of a security interest, the lien is also invalid to the same extent against a person who succeeds to the interest of the holder.

##### 3. Uniform Commercial Code (U.C.C.) Security Interest

- a) Many lien priority disputes arise between a NFTL and U.C.C. security interest holders. In order to determine priority, you need to understand the creation and perfection a security interest under Revised Article 9 of the U.C.C.

b) Creation of a security interest— Under state law, attachment is the term used to describe the creation of a security interest in the debtor’s collateral. Under U.C.C. 9-203, attachment requires the following elements:

- (1) creditor has given value to the debtor,
- (2) the debtor has rights in the collateral, and
- (3) an agreement.

The above 3 elements may occur in any order. Note, however, that a security interest does not exist under the U.C.C. until all 3 elements have been met. The definition of a security interest in I.R.C. 6323(h)(1) includes similar requirements to the above 3 elements. In short, if a debtor fails the state definition of attachment, the creditor will also fail the section 6323(h)(1) definition of a security interest.

c) Perfection of a financing statement—Under state law, in order to have priority against other lienors, the security interest not only must attach to the collateral but also must be perfected. U.C.C. 9-301 and the following sections provide that, depending on the facts and type of collateral, perfection may occur under 4 different methods:

- (1) filing a financing statement,
- (2) taking possession of the collateral,
- (3) for some types of collateral, particularly bank accounts, exercising control over the collateral.
- (4) in limited situations, usually a purchase money security interest in consumer goods, automatic perfection exists, i.e., attachment of the security interest automatically perfects it. An example is when a store sells a television for personal use, taking a security interest in the television.

A U.C.C. security interest must have attached and must have been perfected in order to have priority over the Service’s later filed NFTL. Do not assume, however, that a creditor’s security interest is perfected just because a financing statement has been filed. The U.C.C. allows a creditor to file a financing statement before the security interest has attached (come into existence), and creditors frequently do so. U.C.C. 9-308. The Official Comments to U.C.C.

9-308, number 2, explain that “If the steps for perfection have been taken in advance, as when the secured party files a financing statement before giving value or before the debtor acquires rights in the collateral, then the security interest is perfected when it attaches.”

Also, for corporations, limited liability companies, and other business entities created under state law (registered organizations) do not assume that a U.C.C. security interest is filed at the same location where the NFTL is filed. I.R.C. § 6323(f)(2)(B) states that the location of personal property is the taxpayer’s residence, and the residence of a corporation is the principal executive office of the business. In contrast, a U.C.C. security interest for a debtor-corporation is filed in the state of incorporation. For example, a U.C.C. security interest on the inventory of a corporation with a principal executive office in California, which was incorporated in Delaware, would be filed in Delaware.

#### ***F. Judgment Lien Creditor -- Not Defined in § 6323(h).***

1. Treas. Reg. § 301.6323(h)-1(g)--a person who has a valid judgment, in a court of record and of competent jurisdiction, for specific property for a specific sum of money.

a) A judgment lien is not perfected until the identity of the lienor, the property subject to the lien, and the amount of the lien are established.

b) A judgment lien may be perfected by execution, even if the execution is unsuccessful or even invalid. KS Fin. Group, Inc. v. Schulman, 73 F. Supp. 2d 1373 (N.D. Ga. 1999).

2. Must be a judgment of a **court of record**. See United States v. Gilbert Assocs., Inc., 345 U.S. 361 (1953).

a) All courts are not courts of record, but all states have them.

b) This provision applies particularly to state taxing agencies. Some have provisions which would appear to give them "judgments" without the necessity of "going to court." Entry of this kind of judgment is a mere ministerial act, which is not sufficient. See Air Power, Inc. v. United States, 741 F.2d 53 (4th Cir. 1984) (whether a judgment is issued from a "court of record," for purposes of section 6323, is a question of federal and not state law).



c) Filing of a **notice of lis pendens** (which is not of itself a judgment) does not prime a federal tax lien. Redondo Constr. Corp. v. United States, 157 F.3d 1060 (6th Cir. 1998).

3. Judgment must be specific as to the property it affects.

a) **Real property.** Docketing of the judgment or recording an abstract of judgment is the method of creating a lien in most states on real property. See e.g., In re Charco, Inc., 432 F.3d 300 (4th Cir. 2005) (pursuant to West Virginia law, judgment recorded in the county where the real property of the judgment debtor located).

b) **Personal property.** Look to state law to determine when the particular item of personal property is encumbered by a judgment lien. Generally, the sheriff must levy pursuant to a writ of execution to give a judgment creditor a lien on personal property. Anything less than seizure by the local sheriff is suspect and you must carefully examine state law to determine when a judgment creditor becomes a judgment lien creditor. See Don King Productions, Inc. v. Thomas, 945 F.2d 529 (2d Cir. 1991), where the court held that the judgment lien was not perfected until execution was delivered to the sheriff.

4. The doctrine of relation back, a prejudgment attachment or filing of lis pendens, does not create a judgment lien, even though the state statute may provide that the lien will relate back. United States v. Sec. Trust and Sav. Bank of San Diego, 340 U.S. 47 (1950). This is because the fact and amount of liability are contingent upon the outcome of a later suit.

5. **Superpriorities** – Certain interests are protected under section 6323(b), (c), and (d) even though a notice of federal tax lien was previously filed. Under section 6323(b), these are generally commercial interests where it would be impractical to search a record index to determine if a federal tax lien was in existence, such as personal property purchased at retail. Sections 6323(c) and (d) provide a limited priority to security interests that generally would be protected under the U.C.C.

## VI. PRIORITY OF FEDERAL TAX LIEN: "FIRST IN TIME, FIRST IN RIGHT"

### A. Statutory Priority

Certain priorities are established by statute. See e.g., I.R.C. § 6323. Where a competing lien does not have statutory priority, the basic rule in determining the priority of liens is often referred to as "**first in time, first in right.**" United States v. City of New Britain, 347 U.S. 81 (1954).

## ***B. Common Law Priority - First in Time, First in Right.***

Under federal common law, before another lien can compete with the tax lien, the competing lien must be "choate."

1. A **choate** lien is one that is specific and perfected. If the competing lien is choate before the federal tax lien arises, the competing lien is entitled to priority. United States. v. City of New Britain, 347 U.S. 81 (1954).

a) **Specific** means that the lien attaches to specific property or property rights of the taxpayer.

b) **Perfected** means nothing more need be, or can be, done by the lien claimant. Under the New Britain test for choateness, the lien must be perfect as to:

(1) The identity of the lienor. Id. at 84.

(2) The amount of the lien. Id.

(3) The identity of the property to which it attaches. Id.

## ***C. Federal Question - Priority***

The determination of when any lien becomes choate is a federal question.

1. The federal tax lien arises on the date of assessment. §§ 6321 & 6322.

2. An inchoate lien, which is later perfected, does not take priority over a federal tax lien which arose before the competing lien is perfected. United States v. Sec. Trust & Sav. Bank of San Diego, 340 U.S. 47 (1950).

a) State law determines whether the competing creditor has taken all the steps necessary under state law to perfect the lien (See SB/SE local law guides for state specific requirements for perfecting a lien)

b) If a lien is inchoate under state law, it will not be choate for federal purposes.

c) United States v. Sec. Trust & Sav. Bank of San Diego, 340 U.S. 47 (1950), stands for the proposition that a state-created lien cannot be given retroactive effect; that is, if an attachment or garnishment occurred prior to the assessment of a federal tax, the attachment or garnishment lien became choate only after the assessment was made, and the state statute gave the lien retroactive

status to the time of attachment or garnishment, the state determination will be ignored for priority purposes.

d) Judicial decisions, such as divorce decrees, cannot prime federal tax liens.

3. The fact that the taxpayer's property is encumbered by a prior choate lien cannot prevent attachment of the federal tax lien to taxpayer's property. The pre-existing lien is important only in considering the right to priority.

#### ***D. State Tax Liens***

1. **Basic Rule:** A state or local tax lien is entitled to priority over a federal tax lien only if it is a choate lien prior to the time the federal tax lien arises. United States v. City of New Britain, 347 U.S. 81 (1954). But see In re WPG, Inc., 282 BR 66 (D. D.C. 2002) (District of Columbia sales tax lien had superpriority over prior choate federal tax lien in Chapter 11 bankruptcy case, where D.C. superpriority statute constituted federal law).

a) A state's characterization of its tax liens as choate is not conclusive for federal tax lien purposes. Illinois ex. rel. Gordon v. Campbell, 329 U.S. 362 (1946). See also In re Priest, 712 F.2d 1326 (9th Cir. 1983), modified, 725 F.2d 477 (1984), holding a state law ineffective which stated that a tax lien arose when the tax return was "due and payable" on the date the return was required to be filed. A state-created lien arises when the state takes administrative steps to fix the taxpayer's liability - mere receipt of a tax return is insufficient. Minnesota v. United States, 184 F.3d 725 (8th Cir. 1999).

b) State and local tax liens cannot achieve priority over the federal tax lien by being characterized under state law as judgments. United States v. Gilbert Assocs., 345 U.S. 361 (1953).

c) Real property taxes and special assessments may be entitled to superpriority status under section 6323(b)(6). However, a state law which characterizes a state lien as having priority or superpriority status is not controlling.

2. **When does a state tax lien become choate?** Under City of New Britain, supra, it becomes choate when the identity of the lienor, the property subject to the lien, and the amount of the lien are established.

- a) The identity of lienor requirement is met when the tax is assessed.
- b) The specificity of amount requirement is met when the assessed tax is enforceable by levy.
- c) The specificity of the property subject to the lien is the most difficult requirement to meet.
- d) Despite the common origin of the choateness requirements, the Supreme Court held in United States v. Vermont, 377 U.S. 351 (1964), that divestiture of title or possession did not apply in lien priority contests. Thus, a local tax lien enforceable without a judicial proceeding and attaching to "all property and rights to property, whether real or personal, belonging to" the taxpayer, will prevail over a subsequently arising federal tax lien even though the local tax lien has not been enforced by seizure or sale.

3. **Priority determination.** In determining priority between a federal tax lien and a local tax assessment, compare the date the federal tax lien was assessed with the date the local tax lien became choate. If the local tax was first, then look at the taxing statute to ascertain whether it is choate in the federal sense.

4. Another example of a competing lien which must meet the choateness test to take priority over a subsequent federal tax lien is a lien given under local law for unpaid rent (**landlord's lien**). This lien attaches to tenant's or lessee's property located on landlord's premises.

## VII. OTHER PRIORITY ISSUES

### ***A. After-Acquired Property***

1. Because the federal tax lien automatically attaches to property once the taxpayer acquires an interest in that property, a federal tax lien will ordinarily have priority in any property acquired by the taxpayer after the competing liens have attached. United States v. McDermott, 507 U.S. 447 (1993). This is true even if the financing statement or U.C.C. security instrument provides that the competing creditor's security includes any after-acquired property. Rice Inv. Co. v. United States, 625 F.2d 565 (5th Cir. 1980). Limited relief from this general rule exists for commercial lenders under section 6323(c) and (d).

2. Although a federal tax lien generally will have priority to future income, even where the competing creditor's lien arose first, in some cases a prior lien will attach to the taxpayer's vested right to receive a fixed

stream of income, such as an annuity. In such cases, the competing lien, being prior in time to the federal tax lien, will have priority.

## ***B. Interest and Expenses***

Interest and certain expenses enjoy the same priority as the lien or security interest to which they relate if under local law they are added to and become a part of the lien or security interest. I.R.C. § 6323(e); Citizens Co-op Gin v. United States, 427 F.2d 692 (5th Cir. 1970). The types of interest and expenses that are included in section 6323 are:

1. Interest or carrying charges on the obligation secured by the lien or security interest.
2. Reasonable expenses of an indenture trustee or agent.
3. Reasonable expenses incurred in collecting or enforcing the obligation secured including attorneys' fees.
4. Reasonable cost of insuring (fire and casualty) preserving or repairing the property.
5. Reasonable cost of insuring payment of the obligation secured (such as mortgage insurance).
6. Amounts paid by the holder of a lien or security interest to satisfy another lien on the property where this other lien has priority over the federal tax lien.

# **VIII. FILING NOTICE OF FEDERAL TAX LIEN**

## ***A. Filing***

The Code does not directly answer the question of what is a filing. Section 6323(a) suggests, however, that filing a NFTL is an act undertaken “by the Secretary.” More important, the language of section 6323(f)(4) makes a distinction between filing and recordation or indexing for real property. Section 6323(f)(4) requires, under certain conditions, the “fact of filing” of a NFTL with respect to real property to be “entered and recorded.” This indexing requirement applies only if state law provides that an instrument is not valid against a purchaser without knowledge of the instrument unless it is indexed in a manner that a reasonable inspection of the records will reveal its existence.

Case law interpreting section 6323 confirms the distinction between filing and indexing. Section 6323(f)(4) was added to the Code in 1978 to ameliorate the harshness of the decision in Adams v. United States, 420 F. Supp. 27 (S.D.N.Y. 1976). The district court in Adams held that the Service’s mere presentation of a NFTL to a county clerk’s office constituted filing the lien and that filing did not

require recordation in the index. There, the Service presented NFTLs to the county recording clerk, who then failed to index them in the public record. Subsequently, the taxpayers sold their real property to Adams, who searched the public record and did not find the NFTLs. After Adams purchased the real property and discovered that it was encumbered with federal tax liens, he filed a quiet title action, claiming that the Service had failed to file its NFTLs as they had never been indexed in the public record. The district court held for the Government, reasoning that the Service met its filing requirement by presenting the NFTLs to the clerk. Congressional action to amend section 6323 to impose an additional requirement for the validity of NFTLs under certain situations, namely indexing, reinforces the interpretation of filing in section 6323 as separate and distinct from recordation or indexing. Accordingly, for personal property, we interpret filing to mean delivery of a NFTL to the recording office. In some states, for real property, filing will not occur until the NFTL is indexed; in other states, filing will occur when the NFTL is delivered to the recording office.

Case law decided under the 1978 amendment further bears out the conclusion that filing does not always mean indexing. E.g., Hanafy v. United States, 991 F. Supp. 794 (N.D. Tex. 1998). While all states have recording statutes, there may be a question as to whether a particular state requires that, in order for an instrument to be valid against a purchaser without knowledge, the instrument must be indexed in a manner that a reasonable inspection of the records will reveal its existence. For example, under the Texas recording statute, an instrument does not have to be indexed; it is valid notice from the time that it is filed/delivered with the recording office. Id. Note that section 6323(f)(4) does not apply to personal property, so the federal tax lien is perfected on personal property when it is filed/delivered to recording clerk. In re Tracey, 394 B.R. 635 (1st Cir. BAP 2008).

## ***B. When Should the NFTL Be Filed?***

1. See IRM 5.12.2.1 for filing policy. Generally, a NFTL is filed when it appears necessary to protect the interest of the government.
  - a) Because of the possible drastic effect of filing a NFTL, some discretion is given to the Revenue Officer in determining when to file. IRM 5.12.2.4.1.
  - b) Sometimes the NFTL is filed too late which results in the loss of priority and the tax becoming uncollectible.
2. **Collection Due Process** -- Section 6320 provides that the taxpayer must receive written notice after the Service files a NFTL. The taxpayer has the right to challenge the NFTL before Appeals. If Appeals upholds the filing of the lien and the taxpayer has met applicable deadlines, the taxpayer may challenge that determination in court.

3. Section 6326 provides for an administrative appeal of filing of notice of lien on the basis of error in filing. A certificate of release, based on section 6326, must be expeditiously issued if filing is determined to have been erroneous. The certificate of release must include a statement that such filing is erroneous.

### ***C. Where Should the NFTL Be Filed?***

1. Section 6323(f) provides specific rules with respect to the place of filing an NFTL against both real and personal property. The **situs** of property is fixed by section 6323(f) and not by any state law.

a) **Real property**—The notice of lien must be filed in the one office designated by the state where the real property is physically located. In many cases, as described in section 6323(f)(4), the NFTL must be properly indexed to be effective.

b) **Personal property** (tangible or intangible)—The notice of lien must be filed in the office designated by the state where the taxpayer resides at the time of filing.

(1) **Corporations and partnerships**--state and county of residence is where the principal executive office of the business is located. For employment tax and certain excise tax purposes, a single-owner unincorporated business entity is classified as a corporation under Treas. Reg. § 301.7701-2T(c)(2)(iv)(B) and (c)(2)(v)(B), subject to the effective date rules in Treas. Reg. § 301.7701-2T(e)(5)-(6).

Caution: Treasury published proposed regulations in September 2010 regarding series organizations, including series LLCs. Series LLCs and Cell Companies, 75 Fed. Reg. 55699 (proposed Sept. 14, 2010) (to be codified at 26 C.F.R. pt. 301).

At least eight states have enacted statutes providing for the creation of entities that may establish series, including limited liability companies (series LLCs). In general, series LLC statutes provide that a limited liability company may establish separate series. Although series of a series LLC generally are not treated as separate entities for state law purposes and, thus, cannot have members, each series has "associated" with it specified members, assets, rights, obligations, and investment objectives or business purposes. Members' association with one or more particular series is comparable to direct ownership by the members in such series, in that their rights, duties, and

powers with respect to the series are direct and specifically identified. If state statutory requirements are satisfied, the debts, liabilities, and obligations of one series generally are enforceable only against the assets of that series and not against assets of other series or of the series LLC. If you have a case involving a series, series organization, or member of a series or series organization, please contact Division Counsel and the Office of the Associate Chief Counsel (Procedure and Administration).

(2) If taxpayer resides outside the U.S., residence is deemed to be Washington, D.C.-- file with D.C. Recorder of Deeds.

2. If the state designates more than one office or no office where notice must be filed, the NFTL is to be filed with the Clerk of the United States District Court where the property is situated.

3. Section 6323(f) provides that the Code governs filing of a notice of federal tax lien, and that such filing is not subject to any other law for filing, such as where state statutes attempt to define a different situs for filing or recording instruments affecting title to specific types of property, such as interests in civil aircraft.

4. Under the **Uniform Federal Lien Registration Act** (if adopted by the state in question):

a) **Real property:** File the NFTL in the office of the County Recorder where the real property is located.

b) **Personal property:**

(1) **Individual** -- File the NFTL in the office of the County Recorder where the taxpayer resides.

(2) **Corporation and partnership** -- File the NFTL in the office of the Secretary of State. The Uniform Federal Lien Registration Act does not indicate the place for filing a NFTL in regard to an unincorporated single-owner business entity when such a firm will be regarded for employment or excise tax purposes as an entity separate from its owner. Under the temporary section 7701 regulations cited earlier in the “Where should the NFTL be filed?” section of this outline, this type of business entity is classified as a corporation for employment tax and certain excise tax purposes, and therefore the NFTL is filed in the Office of the Secretary of State.



4. It is difficult to explain to bankers, lenders and creditors that the **situs** of personal property for filing a notice of federal tax lien may be in a distant state, where for example the taxpayer moved from one state to another after the notice of lien was filed. A change of name of a corporate taxpayer is equally hard to explain as not affecting the validity of the already filed notice of federal tax lien. The situs of personal property of a corporation or partnership may require filing the NFTL in a distant state to achieve perfection against a creditor where the creditor may file with the designated state office nearby. A corporation may have a large manufacturing operation in Dallas, but have a small office in Mobile, Alabama. If the small office in Mobile, Alabama is designated as the principal executive office of the corporation, the Service **must** file the NFTL in the one location designated by the State of Alabama for filing notice of lien to cover the personal property of a corporation. See e.g., S. D'Antoni, Inc. v. Great Atl. and Pac. Tea Co., 496 F.2d 1378 (5th Cir. 1974) (natural import of statute's language "principal executive office of the business" was the headquarters at which the major executive decisions affecting the business were made). The Service still must file in the location of any real property in order to perfect on that realty.

If the federal statute fixes the situs of the property in one state, another state cannot fix a place for filing and say that there must be a filing in that state in order to perfect on the personal property, even though the property may be physically located in that second state.

#### ***D. Contents of the NFTL***

States cannot require that the NFTL be in any particular form or contain any particular items before it is recordable. I.R.C. § 6323(f)(3). United States v. Union Cent. Life Ins. Co., 368 U.S. 291 (1961). The current NFTL used by the Service is Form 668(Y)(c).

#### ***E. Effect of Errors***

1. Section 6323(f)(4) requires that, in the case of real property, the notice of federal tax lien must be filed in such a manner that a reasonable inspection of the index will reveal the existence of the lien. In other words, the NFTL must be filed in the chain of title. TKB Int'l, Inc. v. United States, 995 F.2d 1460 (9th Cir. 1993).

2. The mere fact that a full name is not given or that there is an addition, omission or substitution of letters in a name, or even errors, does not, in and of itself, invalidate the notice of federal tax lien. The essential purpose of the filing of the lien is to give constructive notice of its existence. The test is not absolute perfection in compliance with the statutory requirement for filing the tax lien, but whether there is

substantial compliance sufficient to give constructive notice and to alert one of the government's claim. United States v. Sirico, 247 F. Supp. 421 (S.D.N.Y. 1965).

3. Several courts have applied, with different results, this substantial compliance standard when considering whether a lien notice adequately identifies the taxpayer. Many courts have enforced liens after finding that there is an error in the taxpayer's name. See e.g., Kivel v. United States, 878 F.2d 301 (9th Cir. 1989) ("Bobbie Morgan" rather than "Bobbie Morgan Lane"); United States v. Polk, 822 F.2d 871 (9th Cir. 1987) ("Roy Bruce Polk" rather than "Bruce Polk"); Tony Thornton Auction Serv., Inc. v. United States, 791 F.2d 635 (8th Cir. 1986) (notice filed against "Davis's Restaurant," a partnership, and one partner, "Joe Davis," was sufficient as notice against the other partner, "Mary Davis"); Richter's Loan Co. v. United States, 235 F.2d 753 (5th Cir. 1956) ("Freidlander" rather than "Friedlander"); Brightwell v. United States, 805 F. Supp. 1464 (S.D. Ind. 1992) ("William S. Van Horn" rather than "William B. VanHorn"); and United States v. Sirico, 247 F. Supp. 421 (S.D.N.Y. 1965) ("Sirico, George" and "Sirico, A." rather than "Assunta Sirico").

Recent revisions in Article 9 of the U.C.C., which require U.C.C. financing statements to use the exact name of corporate debtors, have led to disputes as to the validity of the NFTL. In United States v. Crestmark Bank, 412 F.3d 653 (6th Cir. 2005), the issue was whether the NFTL was invalid because it identified the taxpayer as "Spearing Tool & Mfg. Company Inc." This varied from Spearing's precise Michigan-registered name, because it used an ampersand in place of "and," abbreviated "Manufacturing" as "Mfg.," and spelled out "Company" rather than use the abbreviation "Co." The bank argued that the NFTL was invalid because it could not find the NFTL when it searched electronically under the taxpayer's Michigan registered name. Because Michigan had limited electronic-search technology, searches disclosed only liens matching the precise name searched—not liens such as the IRS's, filed under slightly different or abbreviated names. The Sixth Circuit rejected the bank's argument and held for the Government. The Sixth Circuit adopted the substantial compliance test, and concluded that a reasonable search would have found the NFTL because the Michigan Secretary of State's office recommended a search using abbreviations.

a) Conversely, other courts have invalidated a federal tax lien where the Service misspells or otherwise materially alters a taxpayer's name. See e.g., In re Reid, 182 B.R. 443 (E.D. Va. 1995) ("Gary A. Reid, Jr." rather than Cary A. Reid, Jr., the debtor); Fritschler, Pellino, Schrank & Rosen, S.C. v. United States, 716 F. Supp. 1157 (E.D. Wis. 1988) ("Allen G. Casey" rather than "Allen J. Casey"); Haye v. United States, 461 F. Supp.

1168 (C.D. Cal. 1978) ("Castello" rather than "Castillo"); United States v. Ruby Luggage Corp., 142 F. Supp. 701 (S.D.N.Y. 1954) ("Ruby Luggage Corp." rather than "S. Ruby Luggage Corp."); and Cont'l Invs. v. United States, 142 F. Supp. 542 (W.D. Tenn. 1953) ("W.R. Clark, Sr." rather than "W.B. Clark, Sr.").

b) If the above cases lead to any generalization, it may be that if the error results in a recorded entry very near to where the correct entry should be (so that a reasonable search would locate the NFTL), the error will be harmless. Where the error results in an entry many pages or entries away, a court is more likely to invalidate the tax lien.

c) Also, where the Service is aware that the taxpayer changed her name, as through marriage, the NFTL may need to be refiled. See United States v. Clark, 1981 WL 1790 (S.D. Fla. 1981). But cf. Pioneer Nat'l Title Ins. Co. v. United States, 1981 WL 1816 (D. N.J. 1981) (IRS not required to refile NFTL because taxpayer changed her name through marriage).

## IX. REFILING NOTICE OF FEDERAL TAX LIEN

### ***A. Effect of Refiling***

Section 6323(g) requires the Government to refile its notice of lien. Timely refiling represents a continuation of prior filing and retains priority.

1. Under section 6323(g)(3), **timely refiling** must occur within:
  - a) The one-year period ending 30 days after expiration of 10 years after the date of assessment.
  - b) For additional refilings, within the one-year period ending 10 years from date of closing of the preceding required refiling period.

2. **Failure to refile**—Most of the NFTLs filed since 1982 are self-releasing liens. When the lien self-releases, the underlying assessment lien is extinguished. IRC § 6325(f)(1)(A). If the lien self-releases and the collection period is still open, the Service can revoke the certificate of release and reinstate the tax lien, effective as of a later date. IRC § 6325(f)(2). In other words, even if the federal tax lien is reinstated, it may lose priority, as the reinstatement does not relate back to the original date of the filing of the NFTL. However, neither failure to timely refile the NFTL, nor the release of the lien, shall alter or impair any right of the United States to property or its proceeds that is subject of a levy or judicial proceeding commenced prior to the end of the refiling period of the

release of the lien, except to the extent that a person acquires an interest in the property for adequate consideration after the commencement of the proceeding and does not have notice of, and is not bound by, the outcome of the proceeding. Treas. Reg. 301.6323(g)-1.

### ***B. Where Is the NFTL Refiled?***

1. In general, the notice of lien is refiled in the office where prior notice was filed.
2. When taxpayer has changed residence and the Service is properly notified of change, refiling is done at the place of new residence as well as the former office.

## **X. WITHDRAWAL OF THE NOTICE OF FEDERAL TAX LIEN**

### ***A. Withdrawal Under Certain Circumstances – Section 6323(j)***

Section 6323(j) provides that the Service may withdraw the notice of lien under certain circumstances. The underlying assessment lien is not affected. The Service has the discretion to withdraw a filed lien notice when:

1. the filing was premature or not in accordance with administrative procedures;
2. the taxpayer has entered into an installment agreement with respect to the liability that is the subject of the lien (unless the agreement provides otherwise);
3. withdrawal of the notice will facilitate collection of the tax liability; or
4. with the consent of the taxpayer or the National Taxpayer Advocate, withdrawal of such notice would be in the best interests of the taxpayer (as determined by the National Taxpayer Advocate) and the United States.

### ***B. Where to File Withdrawal***

Withdrawal is made by filing the notice of withdrawal in the same office as the withdrawn notice. A copy of the notice of withdrawal is provided to the taxpayer.

### ***C. Notice of Withdrawal***

Upon written request by the taxpayer, the Service will provide notification to credit reporting agencies, financial institutions or creditors of the notice withdrawal. See also Treas. Reg. § 301.6323(j)-1.