

Lesson 9

REDEMPTION BY THE UNITED STATES

(March 2012)

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I. INTRODUCTION

Chapter 8 addresses how a federal tax lien may be discharged by judicial and nonjudicial foreclosure sales. Notwithstanding discharge of its lien, the United States still may be able to obtain payment of a tax liability through the exercise of its right of redemption.

Counsel must review and approve all proposed redemptions. Counsel may also become involved in the defense of quiet title actions that are brought as challenges to the exercise of the right of redemption. The Internal Revenue Manual (“IRM”) provides guidance with respect to redemptions and related matters. IRM 5.12.5.

II. OBJECTIVES

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

- Explain the law that governs redemptions by the United States and the procedures employed by the Internal Revenue Service (the “Service”) to both exercise and release redemption rights;
- Calculate the amount that is required to be paid when the Service decides to redeem; and
- Identify some of the legal problems connected with the right of redemption.

III. REDEMPTION AUTHORITY

A. The Authority to Redeem

Authority to redeem is found in the following statutes:

1. Judicial sales – 28 U.S.C. § 2410(c). The term “judicial sale” is narrowly defined, and only applies to sales where there is a judicial proceeding that provides a complete and formal hearing on the merits and results in an order directing the sale of the property.
2. Nonjudicial sales – Section 7425(d)(1); see also Treas. Reg. § 301.7425-4(a)(1). The regulations provide that a nonjudicial sale “includes, but is not limited to, the divestment of a taxpayer’s interest in property which occurs by operation of law, by public or private sale, by forfeiture, or by termination under provisions contained in a contract for a deed or a conditional sales contract.” Treas. Reg. § 301.7425-2(a); see also Treas. Reg. § 301.7425-4(a)(1).

B. When the Right of Redemption Arises

The statutory right of redemption arises only when a sale is conducted to satisfy a lien on real property that is prior to the federal tax lien and results in a discharge of the tax lien. State law, that is, the law of the state in which the property is located, determines whether the junior tax lien is discharged.

1. Instances in Which the Right Arises

The following sales create a right of redemption by the United States:

- a) A judicial sale in a proceeding in which the United States was joined as a party.
- b) A nonjudicial sale in which the notice of federal tax lien was on file more than 30 days prior to the sale, and the Service is entitled to notice of the sale (under section 7425(b) and Treas. Reg. § 301.7425-3(a)(1)), and either receives adequate notice at least 25 days in advance of the sale (see section 7425(c)(1)) or consents to the sale (see section 7425(c)(2)). Treas. Reg. § 301.7425-4(a)(1), (3). The right of redemption allows the Service to buy the property from the party that purchased it at the nonjudicial sale that was undertaken to satisfy a lien senior to the federal tax lien.

2. Instances in Which the Right Does Not Arise

The right of redemption does not exist in the following instances:

- a) Judicial sales in which:
 - (1) The lien of the foreclosing lienor is junior to the federal tax lien. The tax lien is not discharged and remains attached to the property. The sale will be made subject to the federal tax lien
 - (2) The United States was not named as a party, whether or not a notice of federal tax lien was on file. The tax lien is not discharged.
 - (3) Local law does not provide for the discharge of junior encumbrances by the sale.
- b) Nonjudicial sales in which:
 - (1) The lien of the foreclosing lienor is junior to the federal tax lien. The tax lien is not discharged, and the sale will be made subject to the federal tax lien.

(2) A notice of federal tax lien was not filed more than 30 days prior to the sale. The tax lien is discharged by the foreclosure sale. But if the tax lien had attached to the property at the time of the sale, the United States has the same right of redemption, if any, afforded to similar creditors under the local law of the place in which the property is situated. Treas. Reg. § 301.7425-4(a)(3). In addition, while the federal tax lien may be discharged from the property sold, the federal tax lien attaches to the proceeds of sale. Caldwell v. Loeb, 742 F. Supp. 650, 652 (N.D. Ga. 1990).

(3) A notice of lien was filed more than 30 days before the sale, but the Service was not given notice of the foreclosure sale in the manner provided under section 7425(c)(1) and the relevant regulations. The tax lien is not discharged unless the foreclosing party gives the Service notice of the sale in the manner prescribed by the regulations. See Treas. Reg. § 301.7425-3(a)(1); Southern Bank of Lauderdale County v. IRS, 770 F.2d 1001 (11th Cir. 1985); Russell v. United States, 551 F.3d 1174 (10th Cir. 2008), cert. denied, 130 S.Ct. 95 (2009) (reversing a district court decision which terminated a federal tax lien and provided the United States a “right of cure and redemption” pursuant to a state statute where the United States was not provided proper notice of a non-judicial sale).

The Service is required, however, to notify the foreclosing party if the notice is inadequate, i.e., one that fails to contain the information described in Treas. Reg. § 7425-3(d)(1). Treas. Reg. § 7425-3(d)(2). If the Service fails to provide written notification of the inadequate notice (which notice was otherwise timely and contained the name and address of the submitting person) more than five days prior to the date of the sale, the notice shall be considered adequate. Treas. Reg. § 7425-3(d)(2); Whiteside v. United States, 833 F. 2d 820 (9th Cir. 1987).

(1) For regulatory limitations on the right of redemption by the United States, see Treas. Reg. § 301.7425-4(a)(3).

C. Elevation of the Service’s Interest

If the Service is entitled to receive a notice of sale under section 7425 but does not receive such notice, the property remains encumbered by the federal tax lien. In many instances, the sale of the property extinguishes or reconveys secured interests that are senior to the federal tax lien. In these situations, the federal tax lien may be elevated to a more senior position by the elimination of the former senior interests. Purchasers of the

property or new lenders may argue against such elevation on three grounds: (1) equitable subrogation; (2) equitable relief from merger; and (3) unjust enrichment.

1. Equitable Subrogation

Section 6323(i)(2) permits subrogation to the extent provided by state law. The most common requirements for subrogation are: (1) the subrogee must have made a payment to protect its own interest; (2) the subrogee did not act as a volunteer; (3) the entire amount of the debt was paid; (4) the subrogee was not primarily liable for the debt; and (5) subrogation does not create an injustice to the rights of others. Mort v. United States, 86 F.3d 890 (9th Cir. 1996) (second mortgagee's right to equitable subrogation allowed in case involving unsophisticated non-commercial lender, despite presence of intervening federal tax lien); Simon v. United States, 756 F.2d 696 (9th Cir. 1985); First Fed. Sav. Bank of Wabash v. United States, 118 F.3d 532 (7th Cir. 1997) (Indiana law does not allow lender subrogation rights where it failed to discover an intervening tax lien); Bednarowski & Michaels Dev., LLC v. Wallace, 293 F. Supp.2d 728, 730-32 (E.D. Mich. 2003) (purchasers denied equitable subrogation and priority of interests through equitable subrogation under Michigan law because they paid off the first mortgage, that was senior to the federal tax lien, voluntarily).

The difficult requirements for the purchaser or new lender to satisfy are the protection of interest and volunteer factors. Purchasers and new lenders typically have no pre-existing interest in the property and are arguably acting as volunteers in purchasing or advancing new loans for the property. Some courts have held, however, that the interest of a purchaser or new lender can be subrogated to the senior lien. Concerning the purchaser, see Dietrich Indus. v. United States, 988 F.2d 568 (5th Cir. 1993) (purchaser entitled to equitable subrogation of senior lienholder under Texas law); but see Little v. United States, 709 F.2d 517 (9th Cir. 1983) (purchaser was not equitably subrogated to position of senior lienholder under California law). Concerning the new lender, see United States v. Baran, 996 F.2d 25 (2nd Cir. 1993) (New York: equitable subrogation allows lender to correct mistake of undiscovered intervening federal tax lien); ContiMortgage Corp. v. United States, 109 F. Supp.2d 1038 (D. Minn. 2000) (denying summary judgment, but finding that equitable subrogation would allow mortgage assignee to assume priority position of mortgage assignor); Robert E. Weiss, Inc. v. United States, 91-1 USTC ¶ 50,170 (N.D. Cal. 1991) (new lender entitled to equitable subrogation of the federal tax lien but only to the principal sum and interest that accrued before the Service recorded the notice of tax lien); but see First Fed. Sav. Bank of Wabash v. United States, 118 F.3d 532 (7th Cir. 1997) (Indiana law does not allow lender subrogation rights where it failed to discover an intervening tax lien); Universal Title Ins. Co. v. United States, 942 F.2d 1311 (8th Cir. 1991) (failure to discover tax lien precludes title insurance company's subrogation rights); Fidelity Nat'l Title Ins. Co. v. United States, 907 F.2d 868 (9th Cir. 1990) (no equitable subrogation for foreclosure sale purchaser).

An interested party that purchases foreclosed property on which the Service holds a lien and then pays the Service's claim to prevent redemption may not rely on equitable subrogation in order to recoup that amount from the debtor. See, e.g., Bevan v. Social Communications Sites, LLC, 327 F.3d 994 (9th Cir. 2003). In Bevan, a lienholder bought the property of the bankrupt debtors on which the Service held a lien that was junior to the deed of trust held by the purchaser at a nonjudicial foreclosure sale. The purchaser, wishing to keep the property, then paid the Service's claim in full in order to obtain a release of the right of redemption. The purchaser next had the Service's claim transferred to it, and then claimed that it was equitably subrogated to the rights of the Service and could require reimbursement from the debtors' estate in the amount paid to obtain the release of the right of redemption. The Ninth Circuit held that the test for equitable subrogation was not satisfied because the creditor had acted as the "volunteer" identified in the Mort test. Id. at 997-98. Moreover, the court observed that allowing the creditor to equitably subrogate the Service claim would frustrate the intent of the redemption statute. The purpose of the statute, according to the Ninth Circuit, is as follows: "[T]o prevent a potential windfall to a foreclosure purchaser, the IRS can repay the purchaser the purchase price and sell the property at closer to fair market value. All excess profit then accrues for the benefit of the taxpayer – to pay off the taxpayer's tax liability. The [Service]'s redemption right protects the taxpayer, who would otherwise be liable to the [Service] for unpaid taxes." Id. at 998. The court asserted that "nothing could be more inequitable" than to apply equitable subrogation in this circumstance to permit the creditor to hold a claim against the bankruptcy debtors for the amount it paid to the Service in order to eliminate that taxpayer benefit. Id.

2. Equitable Relief from Merger

A mortgage creditor who purchases the property at the foreclosure sale also may be entitled to equitable relief. Generally, if the mortgage lien creditor "buys-in" the property, a merger is deemed to occur, i.e., the lien merges into the acquired fee interest and is extinguished. See, e.g., United States v. Polk, 822 F.2d 871 (9th Cir. 1987) (Arizona: merger extinguished senior lien; senior lienor's intent deemed irrelevant); Southern Bank of Lauderdale County v. IRS, 770 F.2d 1001 (11th Cir. 1985) (Alabama: merger extinguished senior lien); but see Tompkins v. United States, 946 F.2d 817 (11th Cir. 1991) (Georgia: mortgagee's senior lien interest in property does not merge into fee when property is purchased at foreclosure); Security Pac. Mortgage Corp. v. Choate, 897 F.2d 1057 (10th Cir. 1990) (Colorado: intent of the mortgagee controls); United States v. Colorado 872 F.2d 338 (10th Cir. 1989) (Colorado: merger occurs automatically unless contrary intent established); Vereyken v. Annie's Place, Inc., 90-1 USTC ¶ 50,298 (E.D. Mich. 1990), aff'd, 964 F.2d 593 (6th Cir. 1992) (Michigan: lienholder/seller's intent that merger should not occur controls). The court may allow equitable

relief from the doctrine of merger if the creditor/purchaser can show: (1) the creditor's best interests would be served by preventing a merger of the lien and the fee interest; (2) justice would be served; and (3) the government cannot prove by a preponderance of the evidence that the creditor actually intended to merge the lien into the fee interest. See, e.g., First Am. Title Ins. Co. v. United States, 848 F.2d 969 (9th Cir. 1988).

3. Unjust Enrichment

Under the doctrine of unjust enrichment, a party with a state-created lien can be restored to its intended position when there is an inadvertent discharge of the lien. Specifically, section 6323(i)(2), which authorizes application of the common law doctrine of equitable subrogation, does not preclude application of the state-created doctrine of unjust enrichment. The federal tax laws do not create property rights but merely attach federally defined consequences to rights created under state law. Accordingly, where the taxpayer refinances a mortgage and the bank makes an inadvertent discharge of that original mortgage, thereby allowing the Service to gain unintended priority over the refinanced mortgage, the bank's mortgage can be restored to first priority over the federal tax lien under the doctrine of unjust enrichment. Progressive Consumers Fed. Credit Union v. United States, 79 F.3d 1228 (1st Cir. 1996) (doctrine of unjust enrichment prevents the Service from elevating its junior lien interest).

D. Time for Redemption

The United States has 120 days from the date of the foreclosure sale to exercise its redemption right. 28 U.S.C. § 2410(c); I.R.C. § 7425(d)(1); see generally Treas. Reg. § 301.7425-4(a)(2). The United States has a longer period to redeem if state law provides one for junior lienors. 28 U.S.C. § 2410(c); I.R.C. § 7425(d)(1); Treas. Reg. § 301.7425-4(a)(2)(ii). The 120-day period is not extended by section 7503 (which, when applicable, extends the time for performance of acts where the last day falls on a Saturday, Sunday, or legal holiday). See Rev. Rul. 83-116, 1983-2 C.B. 264.

The "date of sale" is determined in accordance with the rules set out in Treas. Reg. § 301.7425-2(b). See United States v. Comer, 2000-2 U.S.T.C. 50,618 (E.D. Mich. 2000). But see United States v. Newkirk, 27 A.F.T.R.2d 71-1191 (N.D. Ill. 1971) (Under Illinois law, the date of sale is the date of the tax sale, not the date set forth in Treas. Reg. § 301.7425-2(b)). Where the Service does not attempt to redeem property within the allotted time period, its federal tax liens are extinguished by the foreclosure sale. United States v. Espinoza, 90-1 USTC ¶ 50,073 (D. Colo. 1989); Black v. United States, 683 F. Supp. 770 (N.D. Ala. 1987). Further, where the Service fails to exercise its power of redemption in a timely fashion, its legal and equitable interests in the property may be found to have been extinguished by the foreclosure sale. See, e.g., Ellis v. United States, 2005-2 USTC ¶ 50,518 (M.D.N.C. 2005).

E. Property Rights Redeemed

A redemption reaches the entire property foreclosed even if the federal tax lien had attached only to a partial interest. See Vardanega v. IRS, 170 F.3d 1184 (9th Cir. 1999). Redemption is not limited to the taxpayer's interest in the property. For example, if property in which the delinquent taxpayer had a joint tenancy interest was foreclosed, redemption would ultimately give the United States title to the entire property rather than only the taxpayer's interest. This is because the government redeems by paying the amount that was paid or satisfied by the sale; since the government paid the full amount, the government receives title to the entire property that was being foreclosed. It is our position that in view of the express wording of section 7425(d)(1), there is no authorization that would permit the Service to redeem only a portion or fraction of the actual property that was sold. This is so even where the property may have been sold to more than one purchaser; i.e., in order to successfully redeem property in such a case, the Service would have to redeem from all of the purchasers, not just one or some of them. Thus, by exercising the right of redemption, the Service acquires the same interest as that bought by the purchaser. The property therefore remains subject to encumbrances that exist and are subject to the foreclosed interest at the time of the sale. Little v. United States, 794 F.2d 484, 490 (9th Cir. 1986) (citing section 7425(d)(3)(C); Treas. Reg. § 301.7425-4(c)(3)); Olympic Fed. Sav. & Loan Ass'n v. Regan, 648 F.2d 1218, 1220 (9th Cir. 1981). The redemption does extinguish the interest of any junior encumbrance.

F. Subsequent Encumbrances

If the holder of a second lien interest senior to the federal tax lien forecloses on the same property within the 120-day redemption period, the Service's redemption right survives the second foreclosure. The Service can then redeem the property from the purchaser within the 120-day period following that foreclosure sale. First-Lockhart Nat'l Bank v. United States, 84-1 USTC ¶ 9155 (W.D. Tex. 1984).

If the purchaser subsequently encumbers the property with a mortgage and the Service then redeems the property, the Service receives the property free and clear of the mortgage. See Olympic Fed. Sav. & Loan Ass'n v. Regan, 648 F.2d 1218 (9th Cir. 1981).

IV. AMOUNT TO BE PAID FOR REDEMPTION

A. Statutory Authority

The following statutes provide for the amount to be paid for redemption:

1. Judicial sales – 28 U.S.C. § 2410(d)
2. Nonjudicial sales – § 7425(d)(2), which incorporates 28 U.S.C. § 2410(d)

3. Under section 7810, a revolving fund was established by the Tax Reform Act of 1984 to finance the redemption of real property by the United States, based on the federal tax lien.

B. Computation of Amount Required to Redeem

To redeem, the United States must pay the purchaser, or his successor in interest, the “actual amount paid” for the property, plus certain additional amounts specified by the regulations. 28 U.S.C. § 2410(d); section 7425(d)(2); see Treas. Reg. § 301.7425-4(b)(1); IRM 5.12.5.5.4; 5.12.5.2.2. For examples illustrating the computation of the amount to be paid, see Treas. Reg. § 301.7425-4(b)(5).

1. Actual amount paid

- a) If the property is purchased by a third party (a nonlien-holder), the actual amount paid is the amount paid by such third party at the sale, which includes deferred payments upon the bid price. Treas. Reg. § 301.7425-4(b)(2)(i).
- b) If the property is purchased by a lienholder, the actual amount paid is the amount of the obligation secured by the lien to the extent legally satisfied by the sale, plus any additional amount bid and paid at the sale. Treas. Reg. § 301.7425-4(b)(2)(ii). In Bank of Hemet v. United States, 643 F.2d 661 (9th Cir. 1981), the purchaser was not the foreclosing party, but a lienholder junior to the foreclosing lienor. The Ninth Circuit concluded that the regulatory language referring to the foreclosing lienor also applied to junior lienholders who purchased at foreclosure.
 - (1) Where the lien foreclosed is secured by other property not foreclosed upon, the amount legally satisfied does **not** include the amount of such lien to the extent that it still attaches to the other property. Treas. Reg. § 301.7425-4(b)(2)(ii). See legislative history of 28 U.S.C. § 2410: H.R. REP. NO. 89-1884, at 33 (1996); S. REP. NO. 89-1708, at 34 (1996).

2. Interest

Interest at the rate of 6 percent per annum on the amount paid from the date of sale to the date of redemption. Treas. Reg. § 301.7425-4(b)(1)(ii). (The 6 percent rate is governed by 28 U.S.C. § 2410(d) not the flexible rates of the Internal Revenue Code.)

3. Excess expenses

The amount required to redeem also includes expenses necessarily incurred by the purchaser to maintain the property after the foreclosure sale reduced by rents received (plus the reasonable rental value if purchaser-occupied or is rented at less

than its reasonable rental value). Treas. Reg. § 301.7425-4(b)(1)(iii); Treas. Reg. § 301.7425-4(b)(3)(i).

a) Examples of excess expenses that will be paid can be found in Treas. Reg. § 301.7425-4(b)(3)(i) and include:

- (1) Rental agent commissions
- (2) Repair and maintenance expenses
- (3) Utilities expenses
- (4) Post-sale legal fees incurred in defending the title
- (5) Casualty insurance premiums
- (6) Ad valorem taxes
- (7) Improvements necessary to maintain the property
- (8) Legal expenses necessary to maintain the property. See MWT Properties v. Everson, 336 F. Supp.2d 1163, 1173-75 (D. Utah 2004) (holding that, because legal expenses incurred by the purchaser (during the redemption period) to evict an unauthorized occupant were necessary to maintain the property, the legal fees were an excess expense that was to be reimbursed by the Service following redemption of the property.)

b) Examples of expenses that will not normally be paid can be found in Treas. Reg. §§ 301.7425-4(b)(2)(i), -4(b)(2)(ii), and -4(b)(3)(i) and include:

- (1) Costs of improvement for cosmetic purposes
- (2) Title search costs
- (3) Professional fees prior to purchase, e.g., finder's fees
- (4) Interest on debt incurred to obtain funds to purchase the property
- (5) The rental value of the property between the date of purchase and the date of redemption. See MWT Properties v. Everson, 336 F. Supp.2d 1163, 1173 (D. Utah 2004) (reasoning that, because such rental value is not an "expense necessarily incurred to maintain [the] property," the purchaser is not entitled to so-called rental value compensation.) .

Pre-sale costs and expenses are not part of the “actual amount paid,” unless included in the amount of the lien legally satisfied or in the amount bid and paid at the sale. Treas. Reg. § 301.7425-4(b)(2)(ii).

The regulations under section 7425 provide guidelines under which a purchaser (or successor in interest) may submit a claim for excess expenses incurred after the foreclosure sale but before the Service’s redemption. See Treas. Reg. § 301.7425-4(b)(3)(ii). A purchaser at a nonjudicial sale should submit a written claim for excess expenses within 15 days after the Service makes a request for a written, itemized statement of the amount claimed by the purchaser or his successor in interest. Thus, if the purchaser fails to furnish a statement within the 15 days after the Service’s request, or if there is a disagreement as to the amount properly payable, or if the purchaser incurs any additional expenses after submitting a timely claim, the purchaser has 30 days after the Service’s redemption in which to submit a written itemized statement claiming excess expenses. Failure to submit a timely claim precludes recovery of the expenses. Id.

Excess expenses, however, may be both requested and paid beyond the 120-day redemption period. Accordingly, an otherwise effective redemption is not rendered invalid simply because the government failed to compensate the purchaser for excess expenses until after the 120-day redemption period expired. MWT Props. v. Everson, 336 F. Supp.2d 1163, 1167-72 (D. Utah 2004).

4. Payments to senior lienholders

a) A purchaser (or successor in interest) of real property at a foreclosure sale may request reimbursement for: (1) a payment of principal or interest to a holder of a lien that was, immediately before the foreclosure sale, senior to the lien foreclosed; and/or, (2) a payment by an escrow agent of a real property tax or special assessment lien that was senior to the lien foreclosed. Treas. Reg. § 301.7425-4(b)(1)(iv); Treas. Reg. 301.7425-4(b)(4)(i). A purchaser at a nonjudicial sale must submit a written claim within 15 calendar days after the Service sends notice of the purchaser’s right to request reimbursement for a payment made to a senior lienor. Treas. Reg. § 301.7425-4(b)(4)(ii); IRM 5.12.5.2.4(1).

b) The purchaser’s claim must include “[a] written itemized statement, signed by the claimant, of the amount” for which reimbursement is requested and additional supporting materials and “[a] waiver or other document that will be effective upon redemption by the United States to discharge the property from, or transfer to the United States, any interest in or lien on the property that may arise under local law with respect to the payment made to a senior lienor.” Treas. Reg. § 301.7425-4(b)(4)(ii)(A), (B); IRM 5.12.5.2.4(2). If the purchaser shows reasonable cause and if the

Service consents, however, the purchaser may request an extension for a reasonable period to submit, amend, or supplement a request for reimbursement. A request for an extension must be submitted before expiration of the applicable period for redemption. IRM 5.12.5.2.5(2).

(1) If the request for reimbursement is not provided or is not timely mailed or delivered, no amount shall be reimbursed. Treas. Reg. § 301.7425-4(b)(4)(ii).

(2) The Revenue Officer will review the request for reimbursement under existing guidelines. See IRM 5.12.5.2.5; 5.12.5.2.6.

c) Only payments made after the foreclosure sale and before the redemption may properly constitute part of the amount that is required to redeem. Treas. Reg. § 301-7425-4(b)(1)(iv) (the amount to be paid for redemption includes “the amounts, if any, of a payment made by the purchaser or his successor in interest after the foreclosure sale to a holder of a senior lien (to the extent provided under paragraph (b)(4) of this section)”); Treas. Reg. § 301.7425-4(b)(4). But see Equity Mortgage Corp. v. Loftus, 504 F.2d 1071 (4th Cir. 1974) (holding the Service should pay the purchaser amounts he had paid to a senior lienor both before and after the foreclosure sale, and after the Service had redeemed).

d) With regard to payments made before foreclosure, it is our position that only payments of interest and principal may be reimbursed. A payment to a senior lienholder to obtain forbearance from enforcing a provision that required full payment on sale of the property is not a reimbursable expense.

e) The Service has discretion to pay the purchaser additional amounts for payments made to senior lienholders. See Little v. United States, 794 F.2d 484 (9th Cir. 1986); Treas. Reg. § 301.7425-4(b)(4)(iii).

5. Computation Problems

State law determines the amount of debt legally satisfied by the foreclosure sale. There is considerable variation among the states about the amount of a lien that is deemed satisfied when the foreclosing lienor is the purchaser. For example, some states do not permit deficiency judgments, or limit them, which increases the amount of the lien legally satisfied. Others measure the satisfaction by the fair market value of the property. See, e.g., Delta Sav. & Loan Ass’n v. IRS, 847 F.2d 248 (5th Cir. 1988) (Louisiana law: the amount the mortgagee paid at the foreclosure sale, not the entire amount of the underlying debt, is the amount the Service was required to pay in order to redeem the property); Mikulec v. United States, 705 F.2d 599 (2nd Cir. 1983) (New York law: United States could redeem property from the judgment creditor who purchased the property for the actual

amount paid by the judgment creditor); Bank of Hemet v. United States, 643 F.2d 661 (9th Cir. 1981) (California law: Redemption price is the amount by which the fair market value of the property at the time of the senior lienholder's foreclosure sale exceeds the amount the purchaser (foreclosing lienholder) paid at the sale to purchase the property, plus the purchase price, plus interest. However, the redemption price cannot exceed the sum of the foreclosing lienor's debt and the purchase price); Equity Mortgage Corp. v. Loftus, 504 F.2d 1071 (4th Cir. 1974) (Virginia Law: United States could redeem the property for the sum of the purchase price at the sale and the amount of the payments made to the senior lienholder). See also Treas. Reg. § 301.7425-4(b)(5) (providing examples of how to calculate the amount satisfied depending on the existence of an anti-deficiency statute in a particular state).

The regulations require that a waiver by the foreclosing lienor of his right to a deficiency judgment must be in writing and legally binding on the foreclosing lienor, as of the time the foreclosing sale is completed, in order to count as part of the amount satisfied. Treas. Reg. § 301.7425-4(b)(2)(ii).

V. REDEMPTION PROCEDURES

A. Technical Services

1. In nonjudicial sale situations, before the foreclosure sale takes place, the foreclosing party should send notice of the impending sale to the appropriate Service office. The received notice should be reviewed for compliance with the requirements set forth in the regulations, e.g., Treas. Reg. § 301.7425-3(d)(1). See Treas. Reg. § 301.7425-3(d)(2); IRM 5.12.4.4.2; 5.12.4.4.3. If the notice is inadequate, the Service should notify in writing the person who submitted the notice of the inadequate items of information. Treas. Reg. § 301.7425-3(d)(2). But "a notice of sale which does not contain the name and address of the person submitting such notice shall be considered to be inadequate for all purposes without notification of any specific inadequacy." Id. If the Service fails to give written notification of the inadequate notice, which was timely and indicated the name and address of the submitting party, more than five days prior to the date of the sale, the notice shall be considered adequate. Id. The foreclosure data is entered on the computer tracking system of the Service and followed by a redemption technician.

a) Preparation of notice and filing location. Section 7425(c)(1) provides that notice of nonjudicial sale shall be given to the Secretary, who has delegated that authority to the Technical Services Advisory Group Manager for the area in which the Notice of Federal Tax Lien was filed. Publication 786, "Instructions for Preparing Notice of Non-Judicial Sale of Property & Application for Consent to Sale" (Rev. 1-2006), contains instructions for preparing a notice of nonjudicial sale of property and an

application for consent to sale. This publication, in relevant part, is to be read in conjunction with Publication 4235, "Collection Advisory Group Addresses" (Rev. 6-2010), which provides the relevant addresses. The Service should be on guard to make sure that incoming notices and applications are properly routed and reviewed so that the proper action, e.g., a notice of inadequacy, can be taken to protect the government's interests. See, e.g., Glasgow Realty v. Withington, 345 F. Supp.2d 1025 (E.D. Mo. 2004).

2. With respect to both judicial and nonjudicial sale situations, after the Service receives notice that the foreclosure sale has taken place, or is about to take place, and the taxes outstanding meet the monetary guidelines established by the Service, the case is assigned to a Revenue Officer in the field to conduct a redemption investigation. IRM 5.12.5.1.

B. Redemption Investigations

The Revenue Officer/Property and Asset Liquidation Specialist (PALS) has 60 days from the date of the foreclosure sale to make a preliminary decision whether to redeem. The Revenue Officer/PALS prepares Form 4376, Report of Investigation, or a memorandum report, which, along with the history sheet, is forwarded to Technical Services. A variety of criteria are considered in deciding whether or not to redeem, see IRM 5.12.5.1.3, 5.12.5.1.2, which include a review of the property for potential toxic waste problems and potential clean up costs, IRM 5.12.5.1.3(7). The primary factor in arriving at the decision to redeem or not is whether the fair market value of the property reasonably exceeds the sum of the amount paid by the purchaser and the amount of all liens senior to the foreclosing encumbrance. IRM 5.12.5.1.3(5). The Service also levies upon the escrow company for any surplus proceeds which may remain after the foreclosing lien is fully paid. Caldwell v. Loeb, 742 F. Supp. 650 (N.D. Ga. 1990). (Note: It may be necessary to provide the taxpayer with a Collection Due Process notice before the levy can be issued.) In some jurisdictions an application for the surplus proceeds is all that is necessary.

If the Revenue Officer/PALS tentatively decides to redeem, the purchaser (or successor in interest) of the property should be sent written notice (Pattern Letter P-597) that the government is considering redemption. IRM 5.12.5.1.3(8). Note: The government must serve the purchaser with written notice of intent to redeem the property. See Title Ins. Co. v. United States, 963 F.2d 297 (10th Cir. 1992) (verbal notice is insufficient and invalidates Service's certificate of redemption).

Service policy requires the Revenue Officer/PALS to arrange for a guaranteed bidder, who will agree in writing to bid a certain amount for the redeemed property, and who will deposit 20 percent of that amount. IRM 5.12.5.3; 5.12.5.3.2. In rare circumstances, approval may be given to accept a deposit of less than 20 percent but in no case should the deposit be less than \$1,000 unless the deposit amount represents 20 percent of the

agreed bid. IRM 5.12.5.3.2(2). The Revenue Officer should consider the use of commercial advertising to solicit bids. See IRM 5.12.5.3.1. The Revenue Officer/PALS can use Letter 1879(P) to solicit such an undertaking from prospective purchasers. The Revenue Officer may use Pattern Letter P-338 for the Agreement to Bid.

Notwithstanding the above, obtaining a guaranteed bidder is not a statutory or regulatory requirement and may be waived.

C. Counsel Review and Approval

Counsel reviews the redemption file and advises as to the legality of the proposed redemption, the amount needed to redeem, the title of the taxpayer, and related matters.

If Counsel approves the proposed redemption, the file goes back to Technical Services which will take necessary actions to obtain a check.

D. Tender of Redemption Check

The Revenue Officer/PALS is given the check and tenders it to the purchaser. To exercise the right of redemption, the government must tender payment within the 120-day period. See IRM 5.12.5.5.1. If the purchaser refuses to accept the check, there has, nevertheless, been a valid exercise of the redemption right. See Bain v. United States, 32 A.F.T.R.2d 73-6108 (E.D. Tex. 1973). We have taken the position that the Service cannot tender redemption funds to a designated agent of the purchaser unless the purchaser has executed a power of attorney pursuant to Treas. Reg. § 601.502 et seq. specifically granting the authority to receive a check drawn on the United States Treasury.

E. Certificate of Redemption

As soon as possible **after** the check has been tendered and **before** the redemption period has expired, a certificate of redemption must be issued and filed with the appropriate local recording office. IRM 5.12.5.6; see section 7425(d)(3); see also Treas. Reg. § 301.7425-4(c)(2) (the certificate of redemption must be filed “without delay”). This certificate “constitute[s] prima facie evidence of the regularity of [the] redemption.” I.R.C. § 7425(d)(3)(C); Treas. Reg. § 301.7425-4(c)(3). The recording of a certificate of redemption is not itself the moment of redemption; rather, such recording “serves merely to evidence that redemption occurred and to transfer legal title of the redeemed interest.” Vardanega v. I.R.S., 170 F.3d 1184, 1187 (9th Cir. 1999) (quoting Southwest Prods. Co. v. United States, 882 F.2d 113, 118 (4th Cir. 1989)).

F. Sale of the Redeemed Property

Redeemed property may be leased or sold. See IRM 5.12.5.7.1, IRM 5.12.5.7.2. Redeemed property is “acquired property” within the meaning of section 7506. The

Service must follow the provisions of section 7506 (not sections 6335 through 6338, which apply to the sale of seized property) when preparing the notice of sale, issuing the deed to the buyer, see IRM 5.12.5.7.4, and other sale-related activities.

G. Disposition of Sale Proceeds/Surplus Proceeds

After sale of the redeemed property, the revolving fund (section 7810) is reimbursed, and the remaining proceeds are applied in the manner prescribed by section 6342. See IRM 5.12.5.7.5. Under section 6342(a), money realized from the sale of property either seized or redeemed by the United States must be applied to: (1) expenses of levy and sale; (2) specific tax liabilities of the property; and (3) the liability in respect of which the levy was made or the sale was conducted. Paragraph (b) of section 6342 goes on to provide that after the above applications are made, the surplus proceeds shall be credited or refunded to the persons entitled to them. It is our position that section 6342(b) also authorizes the Service to apply proceeds from redemption sales even to liabilities not stated in the recorded tax lien on which the redemption right was based, e.g., taxes for which no notice of federal tax lien has been filed.

VI. RELEASE OF RIGHT OF REDEMPTION

The right to redeem may be released for its value to a party with a proper interest in the property sold, upon request, although it cannot be sold to a third party. 28 U.S.C. § 2410(e); Treas. Reg. § 301.7425-4(c)(4).

A. Judicial Sales

The authority for granting a release of the right of redemption has been vested in the Department of Justice by § 0.70 of Title 28 of the Code of Federal Regulations, and redelegated to the United States Attorney with respect to (1) real property on which is located only one single-family residence, and (2) all other real property having a fair market value not exceeding \$200,000.

Application is made to the United States Attorney on a Form OBD-225. Detailed information as to the procedure to be followed is set forth on the back of the application form. The United States Attorney refers it to the Service for investigation. The Service is not required to notify Counsel of their determination regarding the release of the right of redemption before transmitting their recommendation to the United States Attorney. CCDDM 34.5.6.5.1(3).

The Department of Justice generally will not release a right of redemption, even where it is valueless, without some consideration being paid. The Department's current policy is that the consideration paid for the release must be equal to the value of the right of redemption or \$50 whichever is greater. The limitations as to value or use of the property and consideration to be paid do not apply, however, in those instances where the release is requested by the Department of Veterans Affairs or any other federal agency.

Any payment is credited to the taxpayer. See IRM 5.12.5.8.5(3).

B. Nonjudicial Sales (IRM 5.12.5.7)

The Service has the authority to release the right of redemption. Treas. Reg. § 301.7425-4(c)(4). The authority to release any such right of redemption is delegated to the advisory group manager for the area in which the property is located. IRM 5.12.5.9.1(1), 5.12.5.9.3.

Payment cannot be less than the value of the right of redemption. If valueless, the right may be released without any payment, (See Treas. Reg. § 301.7425-4(c)(4), in contrast to the policy of the Department of Justice with respect to judicial sales).

Valuing the right of redemption. The Service relies on appraisals to determine the value of the right of redemption. See IRM 5.12.5.8.2(4), 5.12.5.9.1.3(2). Any questions with respect to the value of the right should be referred to Area Counsel for an opinion. IRM 5.12.5.9(3).

Rev. Proc. 68-10, 1968-1 C.B. 758, contains the information that is required by the Service in an application by any person with a proper interest in property for release of the right of redemption under section 7425(d). Applicants should be furnished a copy of Publication 487, "How to Prepare an Application Requesting the United States to Release Its Right to Redeem Property Secured by a Federal Tax Lien" (Rev. 1-2006).

If an application is complete and proper, a field investigation will not be required unless there is information in Technical Services that indicates such investigation is warranted. A field investigation will not be required on any application made by the Veterans Administration or any other federal agency regardless of value or use. IRM 5.12.5.9.1.1.

These type of cases no longer need to be routinely referred to Counsel for advice. Rather, they should only be forwarded to Counsel when advice is needed on a specific issue. IRM 5.12.5.9.1(2).

Any payment secured for the release of the right of redemption is applied to the taxpayer's outstanding liability. IRM 5.12.5.9.3(5).

VII. LEGAL PROBLEMS IN REDEMPTION

A. Proceedings to Quiet Title

Questions regarding the legality of the redemption or adequacy of the amount paid may be resolved in proceedings to quiet title. See, e.g., Bank of Hemet v. United States, 643 F.2d 661 (9th Cir. 1981); Equity Mortgage Corp. v. Loftus, 504 F.2d 1071 (4th Cir. 1974); Bailey v. United States, 43 A.F.T.R.2d 78-532 (D. Utah 1978); Bain v. United States, 32 A.F.T.R.2d 73-6108 (E.D. Tex. 1973).

B. Right to Rents and Profits

The right to rents and profits during the 120-day redemption period is governed by state law.

C. Successor-in-Interest

A party may be a purchaser's "successor in interest" even though the party holds only equitable title, as opposed to legal title, to the property. See, e.g., Olympic Fed. Sav. & Loan Ass'n v. Regan, 648 F.2d 1218 (9th Cir. 1981).

D. Tender of Redemption Check

If purchaser refuses to accept the check which the Revenue Officer/PALS tenders to him, the right of redemption has nevertheless been exercised. Bain v. United States, 32 A.F.T.R.2d, at 73-6108. If the purchaser in bad faith avoids the Revenue Officer so that tender cannot be effectuated, case law supports the government's equitable right to redeem. Guthrie v. Curnutt, 417 F.2d 764 (10th Cir. 1969); Smith v. Kessler, 117 Cal. Rptr. 470 (Cal. Ct. App. 1974); Powers v. Powers, 34 Cal. Rptr. 835 (Cal. Ct. App. 1963); Ayres v. Dozier, 52 S.W. 662 (Tenn. 1899); Francis v. White, 49 So. 334 (Ala. 1909). See also Rosen v. Norton, 970 F.2d 1079 (2nd Cir. 1992).

E. Discharge of tax lien v. release of the right of redemption

The right of redemption arises when the federal tax lien is discharged and is not confined to the amount of taxes owed. In Olympic Federal Savings & Loan Association v. Regan, 648 F.2d 1218 (9th Cir. 1981), the Ninth Circuit held that the Service was not required to accept a foreclosing lienor's tender of the amount of the federal tax lien in exchange for and satisfaction of the Service's redemption rights. The Ninth Circuit found support for its conclusion in the legislative purpose behind section 7425, which was, in part, to prevent taxpayers from losing their equity in property when foreclosure bids do not approximate the value of the property.

It is our position that the tax lien and the right of redemption exist separately and independently. The government may exercise its right of redemption even though the tax liability stated in the lien on which the right of redemption was based is satisfied after foreclosure. A purchaser at foreclosure cannot extinguish the government's right to redeem by simply tendering payment of the full amount of the tax liability stated in the lien.

F. Forfeitures

The Tax Reform Act of 1986 added section 7425(c)(4), which states that a forfeiture is a sale. This subsection overruled Brookbank, Inc. v. Hubbard, 712 F.2d 399 (9th Cir. 1983); Runkel v. United States, 527 F.2d 914 (9th Cir. 1977); and Hedlund v.

Brellenthin, 520 F. Supp. 81 (W.D. Wash. 1981), which had held that section 7425 did not apply to forfeitures of land sales contracts.

G. Gramm-Leach-Bliley Act

A financial institution may assert that the Gramm-Leach-Bliley Act, 15 U.S.C. §§ 6801 et seq., prohibits it from providing the Service with financial and other information relating to a foreclosed property. The general exception under section 6802(e)(3)(D) of the Act, however, generally would permit disclosure of nonpublic personal information, including relevant financial information, by the financial institution to the government as a lien holder on the property.