

Searching for Federal Tax Liens

The Typical Search for UCC Financing Statements May Not Be Good Enough

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Part of virtually every secured transaction is a search or series of searches for existing security interests or other liens encumbering the intended collateral. Such searches either confirm that there are no prior perfected liens or reveal those that do exist so that they can be removed or subordinated prior to closing. It goes without saying that the searches undertaken in each transaction must be sufficiently complete to find any lien of any type that could deprive a secured party of the collateral securing its related obligations.

The most familiar type of such a search is the search for effective financing statements perfecting security interests under Article 9 of the Uniform Commercial Code (UCC). As a result of the enactment of Revised Article 9 in all states, the rules for filing financing statements changed substantially in 2001. We are presently in a transition period during which secured parties must search for financing statements in the filing offices under both Revised Article 9 and former Article 9.¹ This double searching requirement will end on July 1, 2006, when the financing statements filed under former Article 9 will no longer be effective.²

The intricacies of searching for Article 9 security interests have been widely addressed in the literature and appear to be well understood by practitioners.³ However, there exists a substantial variety of security interests and liens that are not governed by Article 9 and may not be disclosed by the standard searches for Article 9 financing statements. In an earlier installment of this column, Michael P. Schuster provided a comprehensive listing of liens that can affect a secured party's rights but lie outside the

filing provisions of Revised Article 9 and former Article 9.⁴ This article focuses on the proper search procedure for one type of these nonstandard liens—the lien for nonpayment of federal taxes (Internal Revenue Service (IRS) lien), which arises under 26 U.S.C. §6321.⁵

The recording of an IRS lien lies outside the scope of the UCC and is governed by a combination of federal statutes and non-UCC state statutes. In order to conduct effective searches for IRS liens, practitioners must become familiar with the complicated procedures for determining the proper filing office for their recording. The IRS lien arises automatically upon the neglect, failure or refusal of a taxpayer to pay taxes due after demand and is a lien upon all real and personal property of the taxpayer.⁶ However, the IRS lien is not valid against any purchaser, secured party, mechanic's lien or judgment lien creditor until notice of the lien is properly filed in the correct filing office.⁷ The IRS files this required notice of lien in the form of IRS Form 668.⁸

All states, including Indiana, have enacted some form of statute designating the proper filing offices for IRS liens and other federal liens.

For both real property and personal property, the notice of lien will be filed in the one office designated by the laws of the state in which the property is located.⁹ This rule requires the searcher to make two determinations: (1) the state in which the property is located, and (2) the filing office within that state that is designated for the filing of IRS notices of lien. The first of these determinations is governed by federal law, the second by each state's law.

In many cases, determination of the location of the property leads to a divergence from familiar procedures under Article 9. Under federal law, for purposes of recording the IRS notice of lien, real property is, not surprisingly, located at its physical location.¹⁰

However, all personal property of the taxpayer (tangible or intangible, wherever it may be physically located) is deemed to be located at the residence of the taxpayer at the time the notice of lien is filed.¹¹ The residence of a taxpayer that is a corporation, limited liability company or partnership is deemed to be the location of its principal executive office.¹²

These rules for determining the state in which the notice of lien will be filed differ significantly from the rules for filing Revised Article 9 financing statements. Under Article 9, the proper state for filing a financing statement if the debtor is a corporation, limited liability company or other registered entity is the state of registration, regardless of where the principal executive office is located and regardless of where the collateral is located.¹³ It is certainly quite common for a business entity debtor to be registered in one state while maintaining its principal executive office in another. As a result, searchers may find themselves searching in one state for a debtor's Article 9 financing statements (the state of incorporation, organization or registration) and in an entirely different state for the same debtor's IRS liens (the state of the principal executive office).

For example, assume debtor ABC Inc. is a Delaware corporation with its principal executive office in Adams County, Ind. After July 1, 2006, the only filing office in which an Article 9 financing statement naming ABC as debtor may be effectively on file is in the office of the secretary of state of Delaware. However, a search of that office will not find effective IRS notices of liens filed against ABC. Those IRS notices will be filed in some office in Indiana as determined by Indiana state law.

All states, including Indiana, have enacted some form of statute designating the proper filing offices for IRS liens and other federal liens.¹⁴ Although many states have adopted the Uniform Federal Lien Registration Act, there are still substantial variances among states, particularly in the filing of liens upon personal property collateral.¹⁵ Where the collateral is real property, the state statutes appear to be quite uniform in designating the same office for filing IRS liens as for conveyances of real property and real property mortgages. However, states may provide for the filing of IRS notices of liens on personal property in

⁴ Schuster, Michael P., "Unknown Secured Claims: Hidden Liens," 22 Am. Bankr. Inst. J., No. 6, July/August 2003.

⁵ While this article has focused on IRS liens, there are two other less common types of federal liens that will be discovered by the same or similar search techniques: (1) liens imposed under the Employee Retirement Income Security Act (ERISA) pursuant to 29 U.S.C. §1368, and (2) liens imposed under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) pursuant to 42 U.S.C. §9607.

⁶ 26 U.S.C. §6321.

⁷ 26 U.S.C. §6323(a).

⁸ 26 C.F.R. §301.6323(f)-1(d).

⁹ 26 U.S.C. §6323(f)(1)(A).

¹⁰ 26 U.S.C. §6323(f)(2)(A).

¹¹ 26 U.S.C. §6323(f)(2)(B).

¹² *Id.*

¹³ U.C.C. §9-307(e) and cmt. 2 (1999).

¹⁴ See Indiana Code 36-2-11-25.

¹⁵ Unif. Fed. Lien Registration Act, 7A-1 U.L.A. 328-362 (2002 and Supp. 2004).

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the state's central filing offices, county recorder's offices, county courts or other offices of county government. The statutes of each state must be consulted to determine its particular rule.

In our example, the Indiana federal lien statute provides that the IRS notice of lien on personal property shall be filed in the office of the recorder of the county in which the personal property subject to the lien is located.¹⁶ Because all personal property of the taxpayer, regardless of its physical location, is deemed to be located in Adams County, Ind.,¹⁷ the IRS notice of lien on ABC's personal property must be filed in the office of the recorder of Adams County. Thus, a potential lender to ABC must conduct at least two searches, one in the office of the secretary of state of Delaware for Article 9 financing statements and another in the office of the recorder of Adams County, Ind., for IRS notices of lien. Even if ABC were an Indiana corporation, two searches would be required: one in the office of the secretary of state of Indiana for Article 9 financing statements and the other in the office of the recorder of Adams County.

The federal statute governing the state of location of the taxpayer contains at least one other trap for the unwary. As noted above, the location of all of a taxpayer's personal property is deemed to be at the taxpayer's residence *as of the date of the filing of the notice of lien*.¹⁸ In contrast to Revised Article 9 and former Article 9,¹⁹ the proper location for filing an IRS notice of lien is not immediately affected by a change in the taxpayer's location after the notice of lien is filed. Even if the taxpayer's principal executive office moves to another jurisdiction, the notice of lien remains effective in the taxpayer's old location. Moreover, the IRS has no obligation to file a notice of lien in the new location of the taxpayer until the current notice of lien expires 10 years after the initial assessment of tax liability.²⁰ In fact, the IRS may continue to refile notices of lien in the taxpayer's old location every 10 years unless the taxpayer reports its new location to the IRS under some very specific and detailed procedures.²¹ This aspect of the federal statute creates a substantial burden of inquiry

for a secured party. In our example, assume ABC Inc. now has its principal executive office in Adams County, Ind., but moved there from Whitley County, Ind., five years ago. A secured party must search in the recorder's offices of both counties to determine whether currently effective IRS notices of lien are on file. Indeed, a prudent secured party might inquire into prior locations of the taxpayer beyond the 10-year horizon. Unless a notice to the IRS of change of location can be produced, earlier notices of lien may have been renewed any number of times in former taxpayer locations.

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In searching for IRS notices of lien, practitioners must also take special care in specifying the search name—the name of the taxpayer that the filing office is asked to find among its records. There is some unresolved doubt regarding the standards that the IRS must meet in correctly stating that name in a notice of lien. For a registered entity, Article 9 requires that the name on a financing statement be exactly the same as the name on the public record establishing the entity. Some minor mistakes are permitted, but they must be so minor that a search under the correct name will still find the financing statement with the error under the filing office's search logic. This usually means that an error in punctuation will pass, but a misspelling or the use of an abbreviation will be fatal. At least one bankruptcy court has ruled that the IRS is not subject to these rules in the filing of a notice of lien and may abbreviate words that cause the notice of lien not to be found by a search using the correct name.²² Although that decision was reversed by the district court, the issue remains unresolved in most jurisdictions.²³ Prudence would dictate a more extensive search using variations of the correct name.

A similar problem in finding IRS notices of lien arises from the IRS's procedures for listing a corporate tax-

payer's name on Form 668. According to some sources, the procedure is to list the name of the taxpayer followed by the term "a corporation."²⁴ This addition will cause the notice of lien not to be found by most computer searches using the exact taxpayer name. Prudence would dictate that a search using the added phrase be conducted.

The search for existing perfected liens on the collateral is an essential step in every secured transaction. Prudent practitioners will ensure that they conduct a search to identify all security interests and other liens wherever they may be recorded or filed. Part of that complete comprehensive process is a search for IRS notices of lien in every filing office in which such notices may be properly filed, recognizing that some modifications in Article 9 search techniques may be required. ■

²⁴ Mather & Weisman, 638-2nd T.M., *Federal Tax Collection Procedure*, A-38 (2003).

Legislative Highlights
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also a part of the stalled omnibus reform bill. Officials now warn that the failure to enact a modernization of the netting provision could increase the risk of economic instability in the event of a terrorist attack, a fact noted by the 9/11 Commission. The House Committee held a markup on the provision on Sept. 29.

**House OKs Disclosure
of Pension Information**

Under an amendment approved by the House in September, U.S. workers in a defined benefit pension plan would have access to information on the health of the plan—information that companies now supply to the Pension Benefit Guaranty Corporation in confidence. The amendment's sponsor, Rep. George Miller (D-Calif.), argued that there is no reason why the PBGC should know how poorly funded some plans are, while workers and retirees affected by the shortfalls are unaware. Miller claims that 290 of 362 companies with defined benefit plans are now underfunded by some \$165 billion. The provision was tacked on to a government spending bill and must be agreed to by the Senate. The Bush administration is believed to support the change. ■

¹⁶ Indiana Code §36-2-11-25(a).

¹⁷ 26 U.S.C. §6323(f)(2)(B).

¹⁸ *Id.*

¹⁹ U.C.C. §9-316(a) (1999).

²⁰ The date of assessment is not necessarily the date of the first notice of lien filing.

²¹ 26 C.F.R. §301.6323(g)-1(b).

²² *In re Spearling Tool and Manufacturing Co. Inc.*, 292 B.R. 579 (Bankr. E.D. Mich. 2003).

²³ *In re Spearling Tool and Manufacturing Co. Inc.*, 302 B.R. 351 (E.D. Mich. 2003).