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IRS v. SNYDER - CAN THE IRS BE PREVENTED FROM ENFORCING A LIEN ON ERISA ACCOUNTS?

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A CLE Presentation

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Section 506(a) of Bankruptcy Code

- (a) *An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.*

Section 541(a)(1) of Bankruptcy Code

- (a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

Section 541(c)(2) of Bankruptcy Code

A restriction on the transfer of a beneficial interest of the debtor in a trust that is *enforceable under applicable nonbankruptcy law* is enforceable in a case under this title.

Summary of IRS v. Snyder

The central issue in *IRS v. Snyder*, 343 F.3d 1171 (9th Cir. 2003) was whether an IRS claim for delinquent taxes secured outside of bankruptcy by a lien on an ERISA-qualified pension plan is “secured” within the meaning of § 506(a). Courts are currently divided on this issue, and the Ninth Circuit held in *Snyder* that the IRS’s claim is not “secured” within the meaning of § 506(a) because “a debtor’s interest in an ERISA-qualified plan is excluded from the bankruptcy estate pursuant to 11 U.S.C. § 541(c)(2).” *Snyder*, 343 F.3d, at 1173.

The property of a bankruptcy estate includes “all legal or equitable interest of the debtor in property as of the commencement of the case,” “except as provided in subsections (b) and (c)(2).” 11 U.S.C. § 541(a)(1). Thus, according to section 541(c)(2), “a restriction on the transfer of a beneficial interest of the debtor in a trust that is *enforceable under applicable nonbankruptcy law* is enforceable in a case under this title.” 11 U.S.C. § 541(c)(2).

The Supreme Court in *Patterson v. Shumate*, 504 U.S. 753 (1992), concluded that “applicable nonbankruptcy law” included federal (including ERISA) as well as state law. *Snyder*, 343 F.3d, at 1174. Therefore, the Court held “that the anti-alienation clause required for ERISA qualification constitutes a restriction on transfer enforceable under ‘applicable nonbankruptcy law’ within the meaning of § 541(c)(2).” *Id.* The Court concluded that a “debtor’s interest in an ERISA-qualified plan is excluded from the property of the bankruptcy estate.” *Snyder*, 343 F.3d at 1174 (citing *Patterson*, 504 U.S. at 765).

In *Snyder*, the IRS argued that despite the anti-alienation clause required for ERISA qualification, the debtor’s interest in the ERISA plan “should be treated as property of the estate for the limited purpose of securing the IRS’s claim.” *Id.*, at 1174. The rationale of the IRS is: the ERISA plan’s anti-alienation clause is not enforceable under applicable nonbankruptcy law against the IRS, thus § 541(c)(2) does not exclude the debtor’s “interest in the plan from the property of the bankruptcy estate insofar as it concerns the IRS.” *Snyder*, 343 F.3d, at 1175. Further, “ERISA expressly provides that it ‘shall [not] be construed to alter, amend, modify, invalidate, impair, or supercede [*sic*] any law of the United States,’ including federal tax law.” *Snyder*, 343 F.3d. at 1175 (quoting 29 U.S.C. § 1144(d)).

The Ninth Circuit stated that there are “two possible results from adopting the IRS’s construction of 11 U.S.C. § 541 and treating its claim as secured in bankruptcy.” *Snyder*, 343 F.3d. at 1175. First, if the debtor’s Chapter 13 plan is confirmed by the court, the debtor would have to “make full payment of the IRS’s secured claim during the life of the bankruptcy plan,” and the IRS would “get in bankruptcy a payment for which it would otherwise have had to wait.” *Id.* Outside of bankruptcy, the IRS would have

had to wait until the plan entered pay-out status to enforce the lien. *Id.* Since the debtor has no right to demand payment until the plan reaches pay-out status, the IRS merely steps into the shoes of the taxpayer, and therefore “does not acquire any greater rights to the property than the taxpayer himself enjoys.” *Id.*

Second, and the “more likely result,” is that the confirmation of the debtor’s Chapter 13 plan would be defeated because of the difficulty in paying the claim during the life of the plan, and the IRS “could escape without having some or all of the non-lien debt wiped out in bankruptcy.” *Id.* Further, the bankruptcy trustee, like the debtor, would not be able to gain access to the collateral securing the IRS’s claim, namely the debtor’s interest in the ERISA plan, until the plan entered pay-out status. *Id.*

The court noted that the position the IRS took in *Snyder* is contradictory to its position after *In re Lyons*, 148 B.R. 88 (Bankr. D.C. 1992). The court in *Lyons* had held that an IRS’s claim secured by a tax lien on the debtor’s pension was “secured” in bankruptcy “even though that pension otherwise qualified for exclusion from the bankruptcy estate pursuant to § 541(c)(2).” *Snyder*, 343 F.3d, at 1176. A few years after *Lyons*, in 1996, the IRS issued a bulletin in which the IRS opposed *Lyons*, and stated that the approach was not consistent with § 506(a) of the Bankruptcy Code. *Snyder*, 343 F.3d, at 1176 (quoting IRS Litig. Bulletin No. 431, 1996 WL 33105615 (Aug. 1996)). The IRS had further argued that “the *Lyons* analysis essentially gives a particular creditor [the IRS] an interest in property where the estate has no interest in that property,” and finds the analysis in *Lyons* to be “legally unsound.” *Id.*

In addition to issuing the bulletin opposing the *Lyons* approach, the IRS reiterated its position in *In re Persky*, 1998 WL 695311 (Oct. 5, 1998). However, the IRS changed its position in April 2000, when the Assistant Chief Counsel for the IRS wrote that the IRS now believes that “the holding in *Lyons* is correct.” *Snyder*, 343 F.3d, at 1177 (quoting IRS Chief Couns. Advis. 20041029, 2000 WL 33120271 (Apr. 11, 2000)).

The Ninth Circuit points out that the cases are split on the central issue in *Snyder*, however the court decides follow “the position the IRS took in its 1996 litigation bulletin and in *Persky*, and disagree with the position it took in 2000.” *Snyder*, 343 F.3d. at 1178. (Cases agreeing with the debtor in *Snyder*, are: *In re Wingfield*, 284 B.R. 787 (E.D. Va. 2002); *In re Persky*, 1998 U.S. Dist. LEXIS 15509; *In re Keyes*, 255 B.R. 819 (Bankr. E.D. Va. 2000); *In re Wilson*, 206 B.R. 808 (Bankr. W.D.N.C. 1996). Cases agreeing with the IRS’s position in *Snyder* include: *In re Berry*, 268 B.R. 819 (Bankr. E.D. Tenn. 2001); *In re Jones*, 206 B.R. 614, (Bankr. D.D.C. 1997); *In re Lyons*, 148 B.R. 88 (Bankr. D.C. 1992); *In re Perkins*, 134 B.R. 408 (Bankr. E.D. Cal. 1991)).

The court believes the IRS’s argument in *Snyder* “misconceives the character of §§ 506(a) and 541. Section 506(a) provides that in order for a claim to be secured in bankruptcy, it must be secured by a lien on ‘property in which the estate has an interest.’” *Snyder*, 343 F.3d. at 1178. Further, section 541 “is concerned with describing what property shall be included in a bankruptcy estate, not with describing the treatment particular creditors shall receive in the course of bankruptcy proceedings.” *Id.* The central issue in *Snyder* is “whether the anti-alienation clause prevents the transfer of the debtor’s interest in the pension to the bankruptcy estate, not to the IRS, or to any other specific creditor.” *Id.*

Although the IRS is precluded from attaining secured status, this does not extinguish the IRS’s liens, which continue to exist outside bankruptcy. *Id.*, at 1179. The court’s holding in *Snyder* only prevents the IRS from using the debtor’s bankruptcy to accelerate the payment of the liens, or from using the liens to prevent the debtor from confirming a Chapter 13 plan that would reduce or even eliminate the IRS’s non-lien debt. *Snyder*, 343 F.3d. at 1179. The IRS could seek relief from the automatic stay to enforce its liens during bankruptcy, or wait until the conclusion of bankruptcy proceeding. *Id.* If the liens are not enforceable until sometime after the conclusion of the bankruptcy, then the IRS will have to wait until then, but WILL eventually be able to enforce their liens. *Id.*