

# Classification Of Tax Claims And Expenses In Bankruptcy Cases

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# IRS Initial Analysis

- ▶ Have the debtor's tax returns been filed?
- ▶ Claim analysis
  - ▶ Secured (with interest)
  - ▶ Priority (must be paid in full)
  - ▶ Unsecured (dischargeable or not)

# Statutes

## Tax Exceptions to Discharge

- ▶ 11 USC § 523(a)

## Unfiled or Late Filed Returns

- ▶ 11 USC § 523(a)(1)(B)

## Priority Taxes

- ▶ 11 USC § 507(a)(8)

## Dishonest Debtor Exception

- ▶ 11 USC § 523(a)(1)(C)

# Priority Taxes – Section 507(a)(8)

- ▶ A) a tax on or measured by income or gross receipts for a taxable year ending on or before the date of the filing of the petition--
  - (i) for which a return, if required, is last due, including extensions, after three years before the date of the filing of the petition;
  - (ii) assessed within 240 days before the date of the filing of the petition (exclusive of tolling events during that period);
  - (iii) other than a tax of a kind specified in section 523(a)(1)(B) or 523(a)(1)(C) of this title, not assessed before, but assessable, under applicable law or by agreement, after, the commencement of the case;
- ▶ (C) a tax required to be collected or withheld and for which the debtor is liable in whatever capacity;
- ▶ (D) an employment tax on a wage, salary, or commission of a kind specified in paragraph (4) of this subsection earned from the debtor before the date of the filing of the petition, whether or not actually paid before such date, for which a return is last due, under applicable law or under any extension, after three years before the date of the filing of the petition

# Hypotheticals



# Question 1

Rick Grimes obtained an extension of time to file his 2013 federal income tax return until October 15, 2014. He commenced a Chapter 13 bankruptcy case on June 1, 2014. Rick filed his 2013 return on October 1, 2014. He reported \$100 in taxes due, but paid nothing with the return. Rick had enough assets to pay his taxes. The taxes were assessed on December 20, 2014.

What is the classification of the claim for taxes for the 2013 income tax year in Rick's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 2

Daryl Dixon obtained an extension of time to file his 2010 federal income tax return until October 15, 2011. He filed his return on June 7, 2011, but failed to pay the \$100 in taxes reported on the return. The IRS assessed the taxes on October 27, 2011. No NFTLs were filed. Daryl has not filed an income tax return since June 7, 2011. Daryl commenced a Chapter 7 bankruptcy case on August 15, 2014.

What is the classification of the claim for taxes for the 2010 income tax year in Daryl's Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \_\_\_\_\_
- ▶ Secured claim: \$\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 3

Glenn Rhee filed his 2009 federal income tax return on November 11, 2012. The return reported \$100 in tax due. The IRS assessed the tax on December 2, 2012. Glenn paid \$100 when he filed the return. There is \$10 in interest due on the tax, plus a delinquency penalty in the amount of \$25, all of which remains unpaid. Glenn commenced a Chapter 7 bankruptcy case on February 4, 2013. Glenn's bankruptcy attorney told him that he did not qualify as a debtor under Chapter 13 of the Bankruptcy Code.

What is the classification of the claim for interest on the taxes and the penalties due for the 2009 income tax year in Glenn's Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_
- ▶ Secured claim: \$\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 4

Michonne timely filed her 2002 federal income tax return and paid the tax reported on the return. The IRS audited the return and issued a notice of deficiency in tax in the amount of \$100, plus fraud penalties in the amount of \$50. Michonne petitioned the U.S. Tax Court on April 11, 2013. She commenced a Chapter 13 bankruptcy case on June 1, 2013. On August 16, 2013, the Bankruptcy Court lifted the automatic stay to permit the Tax Court case to proceed. The Tax Court entered a judgment on June 6, 2015, for the same claims and amounts in the notice of deficiency. The taxes and penalties were assessed on August 17, 2015. Michonne made an offer in compromise thirty days after the assessment was made and the offer remains pending.

What is the classification of the claim for taxes and penalties for the 2002 income tax year in Michonne's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 5

Maggie Greene failed to file a return for the 2003 federal income tax year. On January 10, 2013, the IRS issued a notice of deficiency in tax the amount of \$100, plus failure to file penalties in the amount of \$25. The IRS prepared a return under 26 U.S.C. § 6020(b) on October 3, 2012. No assessments were made by the IRS prior to the petition date. Maggie commenced a Chapter 7 bankruptcy case on June 2, 2013.

What is the classification of the claim for taxes and penalties for the 2003 income tax year in Maggie's Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503):
- ▶ \$\_\_ Secured claim: \$\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_

## Question 6

Hershel Greene timely filed his 1998 federal income tax return. He reported \$100 in tax due. He failed to pay the tax reported on the return and incurred \$25 in failure to pay penalties. Hershel commenced a no-asset Chapter 7 bankruptcy case on June 1, 2005. He obtained a discharge under 11 U.S.C. § 727 on January 15, 2006. In an adversary proceeding, the bankruptcy court determined that the tax debts assessed for the 1998 income tax year were excepted from discharge under 11 U.S.C. § 523(a)(1)(C). An AUSA represented the IRS in the adversary proceeding. On October 1, 2013, Hershel commenced a Chapter 13 bankruptcy case.

What is the classification of the claim for taxes and penalties for the 1998 income tax year in Hershel's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

# Question 7

Echo, Inc., filed a Form 941 for the fourth quarter of 2010 on April 15, 2011, reporting \$100 in taxes due: \$80 of the taxes were withheld income taxes and the employee's portion of the FICA taxes; \$20 was for the employer's portion of the FICA taxes. The taxes were assessed on June 2, 2011. The corporation did not pay any part of the taxes. No NFTLs were filed. The corporation also failed to file its Form 940 for the calendar year 2010, but owes \$50 in FUTA taxes for that year. The corporation has a history of failing to timely pay its payroll taxes and the principal of the corporation may be a tax defier. Echo, Inc., commenced a Chapter 11 bankruptcy case on February 20, 2014.

What is the classification of the claim for employment taxes in Echo's Chapter 11 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 8

Tyreese was assessed \$100 under 26 U.S.C. § 6672 in regard to the wages of the employees of Walkco, Inc., for the first quarter of 2001. On March 15, 2015, Tyreese commenced a Chapter 13 bankruptcy case. The debt remains unpaid. Walkco might have an offshore bank account.

What is the classification of the claim for penalties under 26 U.S.C. § 6672 in Tyreese's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_

## Question 9

During 2013, Eugene Porter was assessed \$100 for his failure to timely report a financial interest in a foreign bank account, as required by 31 U.S.C. § 5314 (the FBAR penalty). On June 1, 2014, Eugene commenced a Chapter 7 bankruptcy case. As of the petition date, Eugene has fully paid all of his income tax debts.

What is the classification of the claim for the FBAR penalty in Eugene's Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

# Question 10

Deadbeatco, Inc., commenced a Chapter 11 bankruptcy case on June 30, 2012. The corporation failed to pay \$1,000 in wages earned the week before the petition date. By order of the bankruptcy court, the wages are paid by the bankruptcy estate on July 10, 2012. The IRS had no notice of the motion to pay the wages. There was \$100 in employment taxes incurred by the payment of the wages (\$80 for the withheld income and the employer's portion of the FICA, and \$20 for the employer's portion of the FICA). The Bankruptcy Court's order did not specifically address the payment of the employment taxes.

What is the classification of the claim for employment taxes in Deadbeatco's Chapter 11 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

# Question 11

During 1999, Abraham Ford bought a machine for \$40,000 with a bank loan in the amount of \$39,000. He failed to pay any part of the loan. On June 1, 2005, Abraham commenced a Chapter 7 bankruptcy case. The Chapter 7 trustee sold the machine for \$19,000. The machine was fully depreciated and had no tax basis at the time of the sale. The capital gains tax (income tax) associated with the sale is \$10,000. The Chapter 7 trustee now thinks that he made a mistake by selling the machine.

What is the classification of the claim for capital gains (income) taxes in Abraham's Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 12

Taxco, Inc., commenced a Chapter 11 bankruptcy case on July 1, 2013. The business prepared tax returns after the commencement of the bankruptcy case and is assessed \$1,000 in penalties under 26 U.S.C. § 6694, Understatement Of Taxpayer's Liability By Tax Return Preparer, in regard to the preparation of a return after the petition date. The penalties remain unpaid. The bankruptcy estate is administratively insolvent and the debtor in possession is considering converting the Chapter 11 bankruptcy case to a Chapter 7 bankruptcy case.

What is the classification of the claim for penalties in Taxco's Chapter 11 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 13

Beth Greene commenced a Chapter 7 bankruptcy case on March 12, 2011. She timely filed a tax return for the 2012 federal income tax year, reporting \$100 in tax due. She failed to pay the tax reported on the return. Beth might have failed to report all of her income. The bankruptcy case is still open.

What is the classification of the claim for taxes for the 2012 income tax year in Beth's Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$ \_\_\_\_\_
- ▶ Secured claim: \$ \_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$ \_\_\_\_\_
- ▶ General unsecured claim: \$ \_\_\_\_\_

## Question 14

Carol Peletier commenced a Chapter 13 bankruptcy case on November 14, 2014. She timely filed her 2014 federal income tax return and reported \$100 in taxes due. No payment was made with her return. The IRS assessed the taxes on May 10, 2015. No claim was filed by the IRS under 11 U.S.C. § 1305. Carol had a prior Chapter 13 bankruptcy case dismissed within one year of the petition date of the current bankruptcy case.

What is the classification of the claim for taxes for the 2014 income tax year in Carol's pending Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$ \_\_\_\_
- ▶ Secured claim: \$ \_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$ \_
- ▶ General unsecured claim: \$ \_\_\_\_\_

## Question 15

On June 1, 2012, Shane Walsh commenced a Chapter 13 bankruptcy case. He filed his return for the 2013 federal income tax late and reported a tax debt in the amount of \$100. He failed to pay the tax. The return was filed after the section 341 hearing was concluded. The IRS assessed the tax, \$20 for the failure to timely file the return, and \$2 for interest on the tax. The IRS filed a claim for the 2013 income tax year under 11 U.S.C. § 1305.

What is the classification of the claim for taxes, penalties, and interest on taxes for the 2013 income tax year in Shane's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 16

Merle Dixon timely filed his 2009 federal income tax return. He reported \$100 in taxes due, but failed to pay the tax reported on the return. The IRS assessed the taxes, plus \$20 for failure to pay penalties. On January 1, 2013, Merle commenced a Chapter 13 bankruptcy case, but the case was dismissed on December 31, 2013. Merle commenced a Chapter 7 bankruptcy case on May 15, 2014. He plans to file a Chapter 13 bankruptcy case after a discharge is entered under 11 U.S.C. § 727.

What is the classification of the claim for taxes and penalties for the 2009 income tax year in Merle's pending Chapter 7 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$ \_
- ▶ Secured claim: \$ \_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$ \_\_\_\_\_
- ▶ General unsecured claim: \$ \_\_\_\_\_

# Question 17

Gabriel Stokes timely filed his 2010 federal income tax return, reporting \$100 in tax due. He did not pay the tax. On June 2, 2011, the IRS assessed the tax. On February 1, 2013, the IRS issued a notice of intent to levy and, on October 1, 2013, Gabriel requested a CDP hearing. An IRS Appeals Officer is considering whether a levy would be economical. On October 1, 2015, Gabriel commenced a Chapter 13 bankruptcy case. As of the petition date, the CDP matter had not yet been resolved.

What is the classification of the claim for taxes for the 2010 income tax year in Gabriel's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$
- ▶ Secured claim: \$\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

# Question 18

Dale Horvath timely filed his 2012 federal income tax return, reporting \$100 in tax due. The IRS assessed the tax on June 15, 2013. Dale failed to pay the tax. He was given notice of the tax debt and a demand for payment. A statutory lien for the debt arose under 26 U.S.C. § 6321 on the date of the assessment. On March 3, 2014, Dale commenced a Chapter 13 bankruptcy case. On the petition date, Dale owned property with a fair market value of \$50,000 and he has no creditors other than the IRS.

What is the classification of the claim for taxes for the 2010 income tax year in Dale's Chapter 13 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

# Question 19

Andrea timely filed her 2007 federal income tax return. She reported \$10,000 in taxes due, but failed to pay the taxes reported on the return. On June 1, 2008, the IRS assessed the taxes and \$250 in failure to pay penalties. The IRS properly filed a NFTL on November 10, 2013. Andrea commenced a Chapter 13 bankruptcy case on February 13, 2014. On the petition date, Andrea owned a house worth \$100,000, which is subject to a first mortgage in the amount of \$98,000. She also owned a pension plan qualified under 26 U.S.C. § 401(k) in the amount of \$5,000, plus tools in the amount of \$2,000 which she exempted under 11 U.S.C. § 522. Andrea was recently hired as the CFO of a large company and is treated as a highly compensated employee.

What is the classification of the claim for taxes and penalties for the 2007 income tax year in Andrea's Chapter 13 bankruptcy case.

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

## Question 20

On May 1, 2013, Lori Grimes commenced a Chapter 11 bankruptcy case. She timely filed her 2014 federal income tax return (Form 1040) based upon wages, but she did not pay the tax reported on the return. As a result, \$100 in tax is owed. On May 15, 2015, the IRS assessed the tax. No bankruptcy plan has been confirmed and the bankruptcy case is still pending.

What is the classification of the claim for taxes for the 2014 income tax year in Lori's Chapter 11 bankruptcy case?

- ▶ Administrative expense (11 U.S.C. § 503): \$\_\_\_
- ▶ Secured claim: \$\_\_\_\_\_
- ▶ Unsecured priority claim (11 U.S.C. § 507(a)(8)): \$\_\_\_\_\_
- ▶ General unsecured claim: \$\_\_\_\_\_

# Questions, Comments, Complaints . . .

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