

2008 TNT 166-25 NATIONAL TAX LIEN REGISTRY. (Section 6323 -- Priority of Liens) (Release Date: AUGUST 18, 2008) (Doc 2008-17911)

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Abstract:

In a Shelf Project proposal, Prof. T. ***Keith Fogg*** recommends the creation of a national federal tax lien registry.

Summary:

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In a Shelf Project proposal, Prof. T. ***Keith Fogg*** recommends the creation of a national federal tax lien registry.

Body

The proposal is made as a part of the Shelf Project, a collaboration by tax professionals to develop and perfect proposals to help Congress when it needs to raise revenue. Shelf Project proposals are intended to raise revenue, defend the tax base, follow the money, and improve the rationality and efficiency of the tax system. The tax community can propose, follow, or edit proposals at <http://www.taxshelf.org>. A longer description of the Shelf Project can be found at "The Shelf Project: Revenue-Raising Projects That Defend the Tax Base," Tax Notes, Dec. 10, 2007, p. 1077, Doc 2007-22632, [2007 TNT 238-37](#).

The national lien registry proposal comes out of the Shelf Project's Tax Procedure Review Committee, managed by Prof. Fogg and Prof. Bryan T. Camp (Texas Tech Law School).

The Tax community can propose projects at <http://www.taxshelf.org>. Shelf Project proposals follow the format of congressional committee reports explaining current law, the reasons for change, and the proposal itself.

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The current system for filing a notice of federal tax lien came into existence before the electronic age. It relies on myriad state laws and the filing of notices in localities -- more than 4,100 in all. The current system hurts both the IRS and

taxpayers by requiring multiple filings and, thus, multiple removals when the underlying obligation is paid or discharged. With increasing complexity comes increasing costs and errors for the IRS, taxpayers, and taxpayers' creditors. A single Web-based system would be cheaper and more efficient. That possibility drives this recommendation.

I. The Problems With Current Law

A. Basic Federal Tax Lien Law

A federal tax lien arises when the IRS assesses tax against a taxpayer who does not pay the assessment within the appropriate time after the mailing of notice and demand under [section 6303.1/1](#). Because the lien arises automatically without any publication requirement, it is often termed a "secret" lien. The federal tax lien attaches to all of the taxpayer's property and rights to property. Nothing further need happen -- not even publication -- to perfect this lien against the taxpayer's property.

Although the federal tax lien is perfected when it arises, it does not always trump competing claims for the taxpayer's property. The general rule for priority is "first in time is first in right." [Section 6323](#) provides that the federal tax lien will not operate against perfected claims of four preferred classes of competing creditors. Called "the four horsemen," they are (1) purchasers of the property for value, (2) holders of security interests in the property, (3) holders of judgment liens perfected against the property, and (4) holders of perfected mechanic's liens. For the federal tax lien to prevail over these types of competing creditors for any property, [section 6323](#) requires the IRS to make the lien public by filing a notice of federal tax lien. The Federal Tax Lien Act of 1966 was designed to create commercial certainty when secret federal tax liens disrupted normal commercial lending practices. At the same time, the act was intended to allow the federal government to continue its position of near primacy among creditors by filing the lien.

Both filing the lien notice and removing or reducing its scope by filing the appropriate certificate have important consequences for taxpayers. The filing of the lien notice puts the world on notice that all of the taxpayer's property or rights to property are encumbered by the tax lien, thereby eliminating the lien's secret status. Similarly, the filing of the certificate described in [section 6325](#) to release the lien or reduce its scope puts the world on notice that the lien has been released or modified as described in the lien notice. Because the filing of the lien notice will affect which creditor has priority, the lien notices affect the taxpayer's ability to borrow. Credit reporting agencies are among those that watch for the filing of notices of federal tax liens.

Note that it is incorrect to say that the IRS files the lien; the lien arises automatically by operation of law. What the IRS files is the notice of federal tax lien.

B. Filing the Lien Notice

Unlike private creditors who almost always need a judgment or the debtor's consent to record a lien against the debtor, the IRS can file the lien notice whenever it decides that such a filing will facilitate collection of the outstanding liability.

Taxpayer information in general may not be disclosed by the IRS, but the disclosure laws permit lien notices.

[Section 6323\(f\)](#) and its regulations govern the form of the lien notice and the place where it must be filed. The primary location for filing the lien notice is designated by each state. The act sets forth default rules in the absence of a state designation. Most states adopted the Uniform Federal Tax Lien Registration Act. That provision directs the federal government to file the lien notice where the individual taxpayer resides at the time of the filing. If the taxpayer is a corporation or business entity, the federal government files with the state corporation commission or similar entity. For real property, the federal government files the lien notice in the city or county in which the property is located. This system often results in multiple filings in multiple locations to publicize the lien for all of a taxpayer's property.

The system described above applies to most states. Some states have adopted different rules for personal property, generally requiring the lien notice to be filed at a central location within the state./2/ States also vary their system for indexing the federal tax lien. [Section 6323\(f\)\(4\)](#) allows state law to govern how liens against real property are indexed, and the variations for real property can affect the timing of the lien notice and its operation against the four horsemen.

States have also adopted a wide variety of filing fees, ranging as high as \$ 150. While these fees get passed on to the taxpayer, if and when the taxpayer satisfies the tax debt, the IRS pays them upfront. The IRS pays millions of dollars each year in filing fees, not all of which are recouped.

The complexities of the system also invite IRS errors. In most states, the Service must ascertain where the taxpayer resides at the time of the filing or its lien will not be properly publicized for personal property. The IRS must also ascertain the city or county in which the taxpayer's property is located to properly file. Often, the IRS files the lien notice in a wrong city or county because the ZIP code or other data do not perfectly match the location of the taxpayer's property. The IRS also commonly fails to find real property owned by taxpayers and so fails to file the lien notice at the location of that property. As a result of misfiling, the IRS does not perfect its lien priority against the four horsemen.

Because the statute of limitations on collection is 10 years and its expiration can be tolled, the lien notice can stay on court records for a relatively long time. During that period, taxpayers commonly move, sometimes multiple times and sometimes to a remote location. This creates problems for the taxpayer and their creditors in determining whether there is a federal tax lien outstanding. The IRS is not required to follow the taxpayer around the country or the world, filing new lien notices each time the taxpayer moves. As a result, the taxpayer and the taxpayer's creditors may have difficulty finding out about the lien if he has moved since the notice was filed.

C. Removing or Modifying the Federal Tax Lien

In addition to problems encountered with where to file the lien, the IRS encounters problems on the back end of the lien process when it needs to modify the lien notice or remove the lien. [Section 6325](#) describes four types of removal actions, and filing location instructions, which are briefly discussed here in turn. The complexity and difficulties of the system creates errors that can hurt either the taxpayer or the IRS.

(1) Release of the lien. [Section 6325\(a\)](#) requires the IRS to issue a certificate of release of any lien within 30 days of the date on which the liability being released has been fully satisfied by payment or has become unenforceable by reason of law. The prompt filing of a notice of release informing the world that the lien no longer exists is a critical act for the taxpayer's financial well-being. Because the current filing system requires the IRS to file lien notices in multiple jurisdictions, at different times, the IRS has had problems filing the lien release certificates for all of the lien notices. Even though the lien was properly released in some jurisdictions, the public record for other jurisdictions has still shown the lien notice with nothing to indicate it had been released.

The IRS tried to address the difficulties of tracking down multiple lien notices on expiration by the adoption of self-releasing lien notices in 1982.^{3/} Under the 1982 provision, the IRS put language in the lien notices stating that it would automatically release the lien at the expiration of the collection limitation period. The self-releasing lien, however, created a new problem because the collection limitations period is variable. The IRS has sometimes allowed an automatic release to take effect and released a lien prematurely. For example, if a lien notice is filed when there are five years left on the collection limitation period, it will contain language releasing the tax lien at the end of that five-year period. However, some events extend the collection period, including bankruptcy, reduction of the assessment to judgment, or an agreement for extension under offers in compromise. Sometimes the IRS fails to properly file a new lien notice before the old lien notice is automatically released.

(2) Discharge for a portion of the property. [Section 6325\(b\)](#) allows the discharge of the federal tax lien for a portion of a taxpayer's property. The discharge allows the taxpayer to sell a portion of the property even without satisfying the entire tax liability. The IRS can discharge the lien for the sold portion of the property as long as the remaining tax liability is adequately secured. Thus, if the IRS has property that remains subject to the lien that is twice the value of the lien, or the taxpayer substitutes the proceeds of a sale of the portion of the lien or substitutes other property for the sold portion, the lien notice will remain in effect for the property the taxpayer continues to hold, but a portion that is no longer subject to the lien may be sold.

(3) Subordination. [Section 6325\(d\)](#) provides for the subordination of the federal tax lien to another property interest. If the IRS believes that it can ultimately collect more of the tax liability if some other creditor will lend to the taxpayer, the IRS

can allow subordination of its claim to that of another creditor. In those circumstances, a certification of subordination is prepared and filed to reflect the subordination of the federal tax lien to another interest.

(4) Nonattachment. Section 6325(e) provides for the filing of a certificate of nonattachment of the lien. The certificate is often used to correct errors or resolve ambiguities. For example, sometimes the taxpayer has the same name as another individual who does not owe federal taxes, but whose credit is damaged because his name is on a lien notice intended to reach another taxpayer. In this situation, the IRS will issue a certificate that the lien does not apply to the individual who does not owe the tax liability.

(5) Removal location. Section 6325(f) describes the manner and effect of filing a certificate of release, a certificate of discharge, a certificate of subordination, and a certificate of nonattachment. These removal certificates are filed in the same place as the filing of the lien notice. If multiple lien notices have been filed, multiple removal certificates may be needed to achieve the desired result. Creating one location for the filing of the lien notices would obviously make removal actions much easier.

D. Other Complications

The complexity of multiple lien notice locations makes it difficult for taxpayers, the IRS, and creditors considering extending credit to the taxpayers.

Because of the multiplicity of locations in which liens are filed, it is difficult for taxpayers to track the federal tax liens and to locate the appropriate IRS office to address their problems with liens. When liens have been recorded in numerous states, different IRS offices control different liens. Coordinating among those offices to ensure that all liens have been removed or modified can be difficult for taxpayers.

Jurisdictions that have not made lien records available electronically require taxpayers to physically visit the courts to determine the current status of the liens.

Lien notices affect real property only if the IRS knows the location of the real property, and individuals may not be forthcoming with the IRS as to the location and existence of all of their real property. The IRS does not file the lien notice in jurisdictions in which it has no knowledge of real property owned by the taxpayer.

II. Reasons for Change

To overcome the problems that exist with the current system, this proposal would establish an electronic, Web-based system for filing the lien notice, which could be easily accessed by the government, taxpayers, and creditors. The system would take advantage of technology that did not exist in 1966, when the current system was designed. Such a system would produce several benefits:

(1) Ease filing and receipt of information. First, the IRS would no longer need to guess about the residence or the principal place of business of a taxpayer at the time of filing the lien notice. Currently, disputes can arise about the validity of a lien notice based on the various state laws for the location in which it should be filed.^{4/} A national federal tax lien registry would create one place to file the liens, without regard to state residency law. The registry would also provide one place for potential creditors of the taxpayer to look to see if liens enforceable against the taxpayer exist. With a Web-based system for filing, retrieval of lien notices and lien removal actions would not be complicated by relocation of a taxpayer within the lengthy period of the statute of limitations on collection.^{5/}

(2) Have better collections. A national lien registry would allow for more complete collection of tax due. Under current law, the IRS must file in all of the places a taxpayer has real property. The IRS misses real property because of its lack of knowledge about where the taxpayer owns property and consequently does not perfect its lien for the four horsemen. This failure favors private creditors over the IRS. It causes the IRS to lose significant revenue to those private creditors that it might otherwise collect were it aware of all of the locations in which a taxpayer had an interest in real property. A national lien registry would eliminate this loss and create a system that does not favor taxpayers who were able to hide their interests in real property, thus making the tax system fairer for all.

(3) Serve commerce. A national lien registry would improve commerce. Self-releasing lien notices create substantial inaccuracies because lien notices filed in a variety of jurisdictions may be filed at different times with periods on the liens that are not coextensive. The different periods could release at different times because of varying assessment dates and collection statute of limitations periods. Adding to this confusion, the IRS sometimes refiles the federal tax lien in some locations and not others because it fails to note all of the locations in which the lien notices have been filed. As a result, creditors and taxpayers have a difficult time knowing which liens are truly outstanding and which ones have actually been released.

(4) Provide uniformity of release. The self-releasing clause in lien notices requires each notice to be monitored because the automatic release of one lien releases them all. When liens have been filed in multiple jurisdictions at various times, the monitoring of their release dates occasionally fails to catch a lien before the self-release date. This effectively releases them all. For instance, assume that the IRS filed lien notices in three localities in California and one in Idaho because it found that a taxpayer had real property in each of these four locations. Assume further that when the time came to refile the federal tax lien, the IRS refiled the liens in California but failed to refile the lien in Idaho. It is possible that neither the taxpayer nor the other creditors (nor the IRS) would realize that the lien had been released since they would be focused on the refile in California. Conversely, those who see just the self-released Idaho federal tax lien would know that the lien was released. The IRS can correct the problem by revoking the release in Idaho under the provisions of [section 6325\(f\)\(2\)](#). Revoking the release, however, causes the IRS to lose its priority position to other creditors based on the original filing date of the lien notice and gives the IRS a new filing date -- one that follows the date of the revocation. Persons looking only at the California lien notice will not appreciate the new date for priority.

(5) Track taxpayer residence. The lien notice perfects the federal tax lien for an individual's personal property when it is filed where the individual resides when the lien notice is filed. There is no legal obligation to refile if the taxpayer moves over 10 years (or more) following the lien notice filing. The Internal Revenue Manual, however, provides that the IRS should refile a notice in the location of the current residence if it knows the location, as a service to creditors.^{6/} The refile serves an orderly credit market. A national lien registry would also eliminate the difficulty of giving notice to potential creditors if a taxpayer moves.

(6) Avoid glitches in state filing systems. Some states (indexing states) require all filings to be indexed before they take effect. [Section 6323\(f\)](#) provides that the federal government will be bound by a state's procedures. Thus, in indexing states the IRS must rely on the indexing of the lien by the local clerk's office before the lien notice takes effect.^{7/} In nonindexing states, however, creditors rely on the index at their peril.

[United States v. Hanafy, 991 F. Supp. 794 \(N.D. Tex. 1998\)](#), Doc 98-7273, [98 TNT 37-21](#), demonstrates what can happen when a local clerk's office is too busy. In that case, an individual bought property from a taxpayer against whom the IRS had filed a lien notice 10 days before the purchase date. Yet since the clerk's office had not yet indexed the lien notice, the purchaser was unaware of the tax lien. Because Texas is not an indexing state, the purchaser lost. However, the IRS would have lost in an indexing state such as New York or California, where the notice would have had no effect until the local clerk indexed the lien. Either the innocent purchaser or the IRS would have lost on its just claim.

Replacing the current system with a national lien registry controlled by the IRS would eliminate these issues. The indexing issue creates significant uncertainty for the IRS and competing creditors in indexing states. The timing and the maintenance of the index is controlled by state and local offices. If the state or local office fails to index a document, the federal government suffers under this system, which the federal government does not control. If the IRS controlled its own system, the lien would become public the date the IRS placed it in the electric lien database. Delays for mailing, processing, and indexing would be a thing of the past.

(7) Reduce government waste. A national lien registry would save a significant amount of money. The cost of filing lien notices would be eliminated through the creation of the national registry. The IRS estimates that moving from a local paper-based tax lien system to a national Web-based system would save about \$ 570 million over 10 years. These savings would come from the elimination of IRS personnel costs, travel costs related to problems with local filing, state filing fees, and the cost of lost taxes whenever the Service makes an error, or when a tax lien filing is misplaced or delayed. The IRS is a perpetually underfunded agency assigned responsibilities that stretch its limited resources thin. A simpler lien filing system would serve not only the taxpayer and taxpayer creditors who need the information but also the IRS.

The elimination of filing fees also helps taxpayers. Currently, the IRS adds filing fees to a taxpayer's bill. If a taxpayer ends up making full payment of the tax on the lien, he bears this cost in addition to all of the interest and penalties he must otherwise pay. If the debt is not fully paid, the filing fees simply become another part of the tax written off at the expiration of the statute of limitations. The current system requires the IRS to account for the filing costs as a part of maintaining a taxpayer's account.

(8) Provide quicker release. A national lien registry would make it easier and faster for the IRS to release, withdraw, and discharge liens. Taxpayers typically seek discharge of tax liens when selling property. Frequently, taxpayers come to the IRS seeking a discharge of the federal tax lien on the eve of the closing of a sale of real property to which the lien attaches. IRS personnel must work quickly in many cases to assist taxpayers trying to close a sale and thus generate funds with which to pay the tax liability. It is in everyone's interest for the sale to close. Placing the system under IRS control instead of that of various local filing offices and making it electronic should facilitate the granting of a discharge in an expeditious manner. It would also allow the closing attorney and title company to close their records sooner.

Similarly, when a tax liability has been satisfied, a taxpayer wants the lien released as quickly as possible so that credit can be restored more quickly. Again, the national registry would facilitate the release.

III. Proposed Legislation

[Section 6323\(f\)](#) would provide for the creation of a national lien registry established and maintained by the IRS. This registry would exist on the Internet and would be available for taxpayers and creditors to easily access. Because only one database would exist, lien filings and lien removal actions would all take place in one open, accessible forum. The IRS would no longer pay lien filing fees.

The opportunity exists to create a system that is fairer to everyone, because the validity of the lien notice would not rest on state or local practices and would not depend on whether the IRS knew about the existence and location of a taxpayer's real property at the time of filing the lien notice. The chance to promote fairness to taxpayers and their creditors, increase the IRS's efficiency in its use of resources, and save taxpayer dollars should not be passed up.

FOOTNOTES

/1/ See [sections 6321](#) and 6322.

/2/ See Internal Revenue Manual 5.17.2.3.2.

/3/ See IRM 5.17.2.3.3(1).

/4/ See, e.g., [S. D'Antoni, Inc. v. Great Atlantic and Pacific Tea Co., Inc., 496 F.2d 1378 \(5th Cir. 1974\)](#) (addressing whether, under Louisiana law, the IRS had properly filed the notice of federal tax lien where the taxpayer had its principal place of business or whether it should have filed where the taxpayer maintained its registered office).

/5/ Two major challenges confront the creation of this registry:

(1) Identity theft. The national tax lien registry must not promote identity theft. Under current law, the notice of tax lien does not fully disclose a taxpayer's Social Security number. The less identifying information is provided in the notice, the less likely a taxpayer's identity is susceptible to theft, but the more difficult it becomes for the taxpayer's own creditors to identify the existence of the lien notice. This leads to the second challenge which results from a national database -- more confusion over names.

(2) Confusion of names. With a national database rather than a local one, there is the real possibility of filing a lien notice that appears to attach to the property of 5,000 people with the same name. Any national system must develop a mechanism for eliminating confusion in the initial filing to the extent possible and remove confusion when it exists. One possible method for reducing confusion is breaking up the database into segments that estimate the current political subdivisions where lien notices are filed. Another possibility is using identifying features of a taxpayer, such as date of birth, which do not identify Social Security numbers or otherwise promote identity theft.

/6/ IRM 5.17.2.3.3(4).

/7/ [Section 6323\(f\)](#).

END OF FOOTNOTES

References

Subject Area:

Tax system administration issues;

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National Tax ***Lien*** Registry

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T. ***Keith Fogg*** is a visiting associate professor and director of the tax clinic at Villanova Law School. The author wishes to thank the Tax Procedure Review Committee of the Tax Shelf Project for very helpful comments on a prior draft. The author is responsible for errors that remain.

The national ***lien*** registry proposal would create a single national online registry to record IRS ***liens*** and to undo ***liens*** when the underlying obligation is paid or discharged. The ease of a Web-based system would make ***lien*** practice easier for both the IRS and the taxpayer.