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MORGAN D. KING EDITOR

The King Law Letter

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& CONSUMER PROTECTION ATTORNEYS

LAW LETTER NO. 11 July 1 2016

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EXCERPT FROM

Richard West's
AVOIDING & STRIPPING LIENS
In Consumer Bankruptcy Cases
 Release 2016 # 1
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WEST'S AVOIDING & STRIPPING LIENS

PART 2 Summary of lien avoidance & lien stripping

¶ 2.3(c) Non-consensual liens

PART 3 Debtor's powers in chapter 7

¶ 3.7 Statutory liens

PART 4 Debtor's powers in chapter 13

¶ 4.4(c) Tax liens on personal or real property

The debtor in Chapter 13 may strip down an under-secured tax claim, even where the lien attaches to the debtor's home.

The prohibition of lien stripping in chapter 13 prescribed at § 1322(b)(2) does not apply to tax liens, for two reasons.

First, the language of § 1322(b)(2) applies only to liens that are "security interests," and tax liens are not security interests; a security interest is an instrument the debtor voluntarily enters into, like a mortgage, loan against the equity, a car loan, etc. Tax liens, of course, are not voluntarily created by the taxpayer. (*Phifer v. City of Milwaukee* (Bankr.E.D.Wis. 2016) (a city of Milwaukee tax lien).

Second, the § 1322(b)(2) prohibition applies only to security interests that are entirely secured only by the debtor's residence, and tax liens, at least IRS liens, are secured on everything the taxpayer owns. Hence, if the taxpayer owns only a toothbrush in addition to his home, the lien is not secured solely on the residence.

Hence, the oft-repeated aphorism that liens survive bankruptcy is misleading in the case of tax liens in chapter 13 cases, at least for dischargeable taxes. If, for example, you have an undersecured tax lien for dischargeable taxes, the lien may be stripped down in chapter 13, and will remain valid only as to property the debtor owned as of the date the petition is filed; the lien may not attach to or affect the debtor's after-acquired income or property (assuming, of course, that the plan is successfully completed).

This is true even in chapter 7; once the final discharge comes through, the undersecured portion is discharged (assuming the tax satisfies the 5 rules for discharge), the lien may not attach to after-acquired income or property, and the



lien remains valid only as to property owned on the petition date. Hence, at least in the case of dischargeable taxes, the effect is basically the same as stripping the lien down to the value of the debtor's property.

Furthermore, a tax lien's life-span, that is, the statute of limitations, is the same as that for IRS tax collection; neither collection nor the lien may go beyond 10 years from the date of assessment, unless there are tolling events. Hence, if the client is around or under 60 years old, the odds are that the statute of limitations for tax liens will have expired, thus leaving untouched the debtor's retirement plans or payments.

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THE LAW & CASE HOTWIRE

HELD: IN CHAPTER 13 - A FILED TAX LIEN MAY BE STRIPPED DOWN TO THE VALUE OF THE DEBTOR'S EQUITY IN A RESIDENCE

Phifer v. City of Milwaukee (In re Phifer) (Bankr. E.D. Wis., 2016)

The city of Milwaukee objected to the debtor's proposed chapter 13 plan, arguing that *Dewsnup v. Timm*, 502 U.S. 410 (1992) prevented the debtor from stripping its tax lien on the debtor's home, arguing, among other things, that liens survive bankruptcy.

The court said, "Cases cited by the city for the proposition that liens pass through bankruptcy unaffected are unpersuasive."

Among other things averred by the debtor, the court said "§ 1327(c) provides that property of the estate vests in the debtor free and clear of any claim or interest of any creditor provided for by the plan."

"A tax lien is not a security interest for lien-stripping purposes in Chapter 13."

Although under current precedent, a debtor cannot use § 506 alone to avoid a creditor's lien, under certain conditions, the debtor can accomplish lien stripping by virtue of completion of a Chapter 13 plan.

The court qualified this by reminding that " ... lien stripping will not be effected unless debtor completes the plan."



HELD: TAX LIEN COULD NOT BE DIVIDED OR STRIPPED - DOWN IN CHAPTER 7.

In re Blackburn, 525 B.R. 153 (Bankr. N.D. Fla., 2015)

In this chapter 7 case the debtors moved to strip off multiple creditors' liens, include tax liens, on property at 6534 Watermark Cove in Gulf Breeze, Florida 32562 (the "Subject Property"). The only creditor to object was the IRS.

The issue before the Court is whether the IRS tax liens are *divisible*. If they are, then the IRS tax liens may be "stripped off" of the subject property. If they are not, then the IRS tax liens may not be "stripped down," and thereby stripped off this particular piece of property, in this Chapter 7.

Citing the rule that liens may not be stripped off or down in chapter 7, the court sustained the IRS objection, and disallowed splitting off the tax lien as to each respective piece of property, and the debtors' Motion to Determine Secured Status and to Strip off Junior Liens.

The term "bifurcate" describes an undersecured lien divided between the secured portion and the unsecured portion; in contrast, a "separated" or "divided" lien typically involves dividing the lien among the debtor's property; some debtors have argued that liens are wholly unsecured as to some of the assets, and hence may to that extent be stripped off the respective properties. Hence, in theory the tax lien could be stripped of the home with no equity beyond the mortgage, but remain secured against other real or personal property.

The court held in favor of the IRS, suggesting that to divide the lien between different parcels of property was an indirect attempt to *strip down* the lien, which is prohibited in Chapter 7 per *Dewsnup*.

CERTIORI GRANTED BY SUPREME COURT

Date Filed: June 28, 2016

JEVIC HOLDING CORP., et al., Debtors, v. CIT GROUP/BUSINESS CREDIT INC.

BANKRUPTCY LAW: Whether a bankruptcy court may authorize the distribution of settlement proceeds in a manner that violates the statutory priority scheme?

Petitioners are former truck drivers for Respondents. They were fired as a result of Respondents entering chapter 11 bankruptcy. Petitioners brought claims that, based on the Bankruptcy Code, they should be given priority of payments in unpaid wages and benefits over other unsecured creditors. They received nothing while the lower priority creditors received their payments. The bankruptcy court approved a "structured dismissal," which subsequently dismissed Petitioners' claims while distributing the remaining assets.

Petitioners appealed to the Third Circuit arguing that the Fifth Circuit had previously held that approval of a distribution plan that violates the statutory payment priorities is impermissible under the Bankruptcy Code. The Third Circuit rejected this argument and affirmed the bankruptcy court's ruling. Petitioner first argues that it is urgent that the Court determines this circuit split because the Third Circuit has denied petitioners' motion for a rehearing and the Second and Fifth Circuits have been split on this issue for nearly a decade.

Second, Petitioners argue that the Third Circuit incorrectly allowed creditors to evade the Bankruptcy Code's absolute priority of the chapter 11 distribution scheme. Lastly, Petitioners contend that this issue is likely to reoccur because this risk of the settlements approved in this decision will loom over every chapter 11 bankruptcies.

[Summarized by: GrantElder]

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IN OTHER NEWS

Bankruptcy - Taxes - Consumer Protection

DISBARRED LAWYER F. LEE BAILEY FILES FOR BANKRUPTCY

Jun 27, 2016
By Debra Cassens Weiss
ABA Journal

Faced with a \$5 million-plus debt to the Internal Revenue Service, disbarred lawyer F. Lee Bailey has filed for bankruptcy.

Bailey filed for Chapter 7 bankruptcy in Maine on Friday, report the Washington Post and the Portland Press Herald.



Bailey tells the Washington Post his only assets are a car worth less than \$2,000, personal property worth less than \$5,000 and a condominium. He owes about \$365,000 on the condo mortgage, and he hopes to keep the property through a reaffirmation agreement, he tells the Portland Press Herald.

Bailey tells the Press Herald he wants to discharge the IRS debt because "at 83, it's a little late to raise that kind of money overnight. It's been a long battle."

FORECLOSURE ACTIVITY FLAT

From Mortgageorb.com

Foreclosure Activity Basically Flat Foreclosure filings, including default notices, scheduled auctions and bank repossessions, were reported on 100,841 properties in May - virtually unchanged compared with April and down 21% from May 2015, according to RealtyTrac's U.S. Foreclosure Market Report. It was the eighth consecutive month with a year-over-year decrease, according to the firm. States with the most foreclosure filings for the month included New Jersey, Maryland, Delaware, Florida and Nevada.

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"DANCE MOM" PLEADS TO BANKRUPTCY FRAUD

PITTSBURGH - "Dance Moms" star Abby Lee Miller is scheduled to plead guilty next week in Pittsburgh to bankruptcy fraud and failing to report more than \$10,000 worth of Australian currency she brought into the country.

U.S. District Judge Terrence McVerry issued orders scheduling Miller's guilty pleas for Monday shortly after she issued a statement to The Associated Press saying she accepts responsibility for the charges.

Miller issued the statement after federal prosecutors added the currency reporting charge. She's accused of violating a law in August 2014 that requires people to report bringing more than \$10,000 worth of foreign currency into the country. The documents also seek to have her forfeit at least \$120,000, though prosecutors wouldn't say whether that's the value of Australian currency she failed to report.

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Donald Trump's companies have declared bankruptcy...more than four times

Hillary Clinton mocked Donald Trump's business failings in a major speech arguing that the presumptive Republican nominee would be disastrous for the economy.

"He's written a lot of books about business. They all seem to end at Chapter 11," Clinton quipped, adding. "He bankrupted his companies not once, not twice, but four times."

We rated a similarly worded claim from Trump's former primary rival Carly Fiorina Mostly True, because it's not accurate to say Trump is solely to blame. (For the record, Trump doesn't deny the charge and instead argues it was a smart business decision.) At the time, we found four bankruptcies, but since then, we've found two more for a total of six. So Clinton was right that Trump bankrupted companies four times, and she could have offered a higher count as well.

Let's go through them one by one.

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Co-signing a loan? That puts more than your name on the line.

By Michelle Singletary

Columnist June 17 at 7:41 PM

Just say "no."

That's the simple reply to a request from a relative or friend to co-sign on a loan. It's one of my absolute money rules. I will not be linked financially to a loan for anyone other than my husband.

I can't say this often enough, and yet too many people still co-sign loans. Look at the results from a recent survey from CreditCards.com:

- 28 percent of co-signers saw a drop in their credit scores because the primary borrower paid late or not at all.

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Compassion and Common Sense Enter Student Loan Discharge Arena

Posted by NCBRC - June 17, 2016

Where there was sufficient evidence to corroborate the debtor's credible testimony of medical disability indicating likelihood of her inability to work in the future, the second prong of Brunner is satisfied even though there may be more or better corroborating evidence the debtor could have presented.

Nightingale v. North Carolina State Educational Assistance Authority, 2016 Bankr. LEXIS

1667, No. 13-10834, Adv. Proc. No.13-2060 (Bankr. M.D. N.C. April 14, 2016).

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