



MANUAL TRANSMITTAL

Department of the Treasury
Internal Revenue Service

5.17.9

JULY 18, 2024

EFFECTIVE DATE

(07-18-2024)

PURPOSE

- (1) This transmits revised IRM 5.17.9, Legal Reference Guide for Revenue Officers, Chapter 7 Bankruptcy (Liquidation).

MATERIAL CHANGES

- (1) The content in IRM 5.17.9, Chapter 7 Bankruptcy (Liquidation), has been updated to provide clarity and expansion of existing material. The table below shows substantive changes within this IRM revision.

Material Changes

Number	IRM	Description of Change
1	5.17.9.1	Added Program Scope and Objectives Internal Controls section to the document. This section includes background, authority, responsibilities, program management and review, program controls, terms and acronyms, and related resources subsections.
2	5.17.9.3	Updated title of section from "Purpose" to "Chapter 7 Bankruptcy".
3	5.17.9.3(1), (2), (3), (4) and (5)	Added titles to subsections.
4	5.17.9.4(1), (2), (3), (4) and (5)	Added titles to subsections.
5	5.17.9.4(5)	Updated IRM reference from IRM 5.9.3.6(10) to 5.9.3.5(10).

Number	IRM	Description of Change
6	5.17.9.6(1), (2), (3) and (4)	Added titles to sub-sections.
7	5.17.9.8(1), (2), (3), (4), (5) and (6)	Added titles to sub-sections.
8	5.17.9.9(3)	Updated IRM reference from IRM 5.17.9.11 to 5.17.9.12.
9	5.17.9.9(5) - 2nd bullet	Updated IRM reference from IRM 5.9.17.7.9 to 5.9.17.8.9.
10	5.17.9.10(1), (2) and (3)	Added titles to sub-sections.
11	5.17.9.12(1), (2), (3) and (4)	Added titles to sub-sections.
12	5.17.9.14(1), (2), (3), (4), (5) and (6)	Added titles to sub-sections.
13	5.17.9.14(2)	Converted alpha list to a table.
14	5.17.9.14.1(1) - Reminder	Updated IRM references: IRM 5.9.3.6.1 to 5.9.3.5.1.1 and IRM 5.9.18.5.8 to IRM 5.9.18.6.8.
15	5.17.9.14.1(3)	Updated IRM references: IRM 5.9.17.7.9 to 5.9.17.8.9; IRM 5.9.17.9(4) to IRM 5.9.17.10(4).
16	5.17.9.14.1(4)	Updated IRM references: IRM 5.9.17.7.2(1) to 5.9.17.8.2(1); IRM 5.9.17.7.1 to 5.9.17.8.1.
17	5.17.9.15(3)	Updated IRM reference from IRM 5.9.17.4 to IRM 5.9.17.5.

Number	IRM	Description of Change
18	Throughout	IRM sections have been renumbered due to the movement of content to internal controls.
19	Throughout	Editorial changes were made throughout this section to provide greater clarity, eliminate duplicate material, and update, correct, or add citations.

EFFECT ON OTHER DOCUMENTS

This material supersedes IRM 5.17.9, Chapter 7 Bankruptcy (Liquidation), dated October 6, 2016.

AUDIENCE

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5.17.9

Chapter 7 Bankruptcy (Liquidation)

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5.17.9.1
(07-18-2024)
Program Scope and Objectives

- (1) **Purpose.** This IRM section contains guidance for revenue officers related to the processing of bankruptcy cases filed under Chapter 7 of the United States Bankruptcy code.
- (2) **Audience.** This section is used primarily by Small Business/Self Employed (SB/SE) revenue officers and management. Specialty Collection Insolvency (SCI) caseworkers and management in the Centralized Insolvency Operation (CIO) and Field Insolvency (FI) may also refer to this section. Caseworkers in functions other than SB/SE may refer to this section when dealing with a taxpayer that has filed bankruptcy.
- (3) **Policy Owner.** The Director of Collection Policy is responsible for issuing policy for the Insolvency program.
- (4) **Program Owner.** The program owner is Collection Policy, Insolvency an organization within the SB/SE division.
- (5) **Primary Stakeholders.** The primary stakeholders are Field Collection, Civil Enforcement Advice and Support Operations (CEASO), Chief Counsel and SCI.
- (6) **Program Goals.** The goal is to provide fundamental knowledge and procedural guidance for working Chapter 7 bankruptcy cases. Following the guidance in this IRM will ensure cases are worked in accordance with bankruptcy laws and regulations.

5.17.9.1.1
(07-18-2024)
Background

- (1) **Liquidation.** Chapter 7 bankruptcy is a liquidation proceeding. The assets of a debtor that are not exempt from creditors are collected and liquidated (reduced to money), and the proceeds are distributed to creditors. A debtor receives a complete discharge from debt under Chapter 7, except for certain debts that are prohibited from discharge by the Bankruptcy Code.

5.17.9.1.2
(07-18-2024)
Authority

- (1) The Insolvency program operates within the guidelines of Title 11 of the United States Code (11 USC) and the Federal Rules of Bankruptcy Procedure.

5.17.9.1.3
(07-18-2024)
Responsibilities

- (1) IRM 5.17.1.8, Revenue Officer's Role, provides the duties and responsibilities of a revenue officer. Revenue officers will use this IRM to gain an understanding when administering cases in which the taxpayer is in a Chapter 7 bankruptcy.

5.17.9.1.4
(07-18-2024)
Program Management and Review

- (1) IRM 1.4.50.8.2.1, ENTITY Case Management System Reports, contains guidance on Field Collection reports.
- (2) National quality reviews and consistency reviews are conducted on a consistent basis. See IRM 1.4.50.12.1, EQRS, and IRM 1.4.50.12.2, NQRS, for more information.
- (3) Operational and Program reviews are conducted on a yearly basis. See IRM 1.4.50.13.2, Operational Reviews, and IRM 1.4.50.13.5, Program Reviews, for more information.

5.17.9.1.5

(07-18-2024)

Program Controls

- (1) Managers are required to follow program management procedures and controls addressed in IRM 1.4.50.11, Group Controls, and IRM 1.4.50.12, Quality.
- (2) Caseworkers and managers use the Integrated Collection System (ICS) for case management, assignment, and documentation.

5.17.9.1.6

(07-18-2024)

Terms and Acronyms

- (1) A glossary of terms used in this section can be found in IRM 5.17.8-1, Glossary of Common Bankruptcy Terms.
- (2) Acceptable acronyms and abbreviations can be found in the ReferenceNet Acronym Database, which may be viewed at: *Acronym Database*.
- (3) The following table lists acronyms and definitions used specifically in this IRM section.

Acronym	Definition
BAPCPA	Bankruptcy Abuse Prevention and Consumer Protection Act of 2005
CIO	Centralized Insolvency Operation
ERISA	Employee Retirement Income Security Act
FI	Field Insolvency
NFTL	Notice of Federal Tax Lien
SB/SE	Small Business/Self Employed
SCI	Specialty Collection Insolvency
SOFA	Statement of Financial Affairs
SRP	Shared Responsibility Payment
USC	United States Code

5.17.9.1.7

(07-18-2024)

Related Resources

- (1) Procedural guidance on insolvencies can be found throughout IRM 5.9, Bankruptcy and Other Insolvencies.
- (2) The United States Bankruptcy Code and Rules, including Local Bankruptcy Court Rules.
- (3) Insolvency Knowledge Base Home Page, *Insolvency Knowledge Base*.
- (4) The Taxpayer Bill of Rights (TBOR) lists rights that already existed in the tax code, putting them in simple language and grouping them into 10 fundamental rights. Employees are responsible for being familiar with and acting in accord with taxpayer rights. See IRC 7803(a)(3), Execution of Duties in Accord with Taxpayer Rights. For additional information about the TBOR, see <https://www.irs.gov/taxpayer-bill-of-rights>

5.17.9.2
(07-18-2024)
Overview

- (1) This section discusses Chapter 7 bankruptcies. It provides legal guidance on the Chapter 7 bankruptcy law. It explains the provisions and concepts of the Chapter 7 bankruptcy law.

5.17.9.3
(07-18-2024)
Chapter 7 Bankruptcy

- (1) **Key Factors of Chapter 7.** The most common form of relief sought by debtors under the Bankruptcy Code is liquidation under Chapter 7.
 - a. A Chapter 7 case may be started by a voluntary or involuntary petition.
 - b. A Chapter 7 case involves three major participants: the debtor, the trustee, and the creditors.
 - c. The trustee's job is to administer a Chapter 7 liquidation. The trustee takes possession of all the debtor's non-exempt assets included as property of the estate. These assets are reduced to cash. The trustee then distributes the proceeds to the creditors in accordance with their legal priorities established in 11 USC 726.
- (2) **Creditor Purpose in Chapter 7.** The primary purpose of Chapter 7 from the creditors' standpoint is fair and equal treatment of creditors in accordance with their relative priorities.
- (3) **Debtor Purpose in Chapter 7.** One of the primary purposes of Chapter 7 from the debtor's standpoint is to obtain a discharge of debts, thereby giving an individual debtor a "fresh start."
- (4) **Discharge on Chapter 7 Cases.** There are some restrictions to receiving a discharge in Chapter 7 cases. Keep the following in mind concerning discharges on Chapter 7 cases:
 - a. A discharge in a Chapter 7 case is given to individuals only. Partnerships, limited liability companies (LLCs), and corporations do not receive a discharge in Chapter 7. However, few or no assets may remain for the collection of the tax liabilities of these business entities when not paid by the bankruptcy estate.
 - b. The right of an individual to a discharge is not absolute, as grounds may exist to oppose a discharge. Generally, if a debtor is honest and follows the rules of the Bankruptcy Code and the court, the debtor will obtain a discharge. A discharge prevents collection from the debtor for most of the debts owed at the time of the filing of the petition.
 - c. Even if a discharge is obtained, certain debts of an individual debtor may not be discharged and may remain after bankruptcy. Many tax liabilities and interest on those taxes are non-dischargeable. In particular, priority tax debts are non-dischargeable. Non-priority tax liabilities may be non-dischargeable when the taxes are on unfiled returns or on late filed returns that are filed within two years of the bankruptcy petition date. Taxes related to fraudulent returns are non-dischargeable. Additionally, taxes are non-dischargeable when the debtor willfully attempted to evade or defeat the tax in any manner.
- (5) **Chapter 7 Liquidation of Assets.** Generally, in a Chapter 7 case, the debtor's non-exempt assets are collected, reduced to cash, and funds distributed to the creditors. To accomplish this, the court must determine:
 - a. The debtor's pre-petition rights and interests;
 - b. The pre-petition rights and interests of some or all of the creditors against other creditors or transferees;

- c. The rights of the debtor or trustee to recover property held by third parties;
- d. The rights of the debtor to retain existing or future (after-acquired) property, including rights to retain certain property as exempt from the bankruptcy process; and
- e. The relief granted to the debtor by the Bankruptcy Code from unpaid creditors.

5.17.9.4
(07-18-2024)
Automatic Stay

- (1) **Automatic Stay Provisions.** The automatic stay is triggered by the filing of a bankruptcy petition. The automatic stay against property of the estate remains until it is no longer estate property. In non-individual cases, the automatic stay of any other prohibited act remains in place until the earlier of dismissal or closure of the case by the court. Unless the debtor is a serial filer, the stay of any other prohibited act in the case of an individual remains in effect until the earliest of:

- Closure of the case by the court,
- Dismissal of the case by the court,
- Granting of a discharge, or
- Denial of a discharge.

- (2) **Automatic Stay and Serial Filers.** If the individual debtor is a “serial filer,” the automatic stay may terminate 30 days after the current petition date or may not go into effect at all. See IRM 5.9.6.5, Automatic Stay, and IRM 5.9.5.7, Serial Filers, for additional information.

- (3) **Automatic Stay Prohibited Actions.** The automatic stay prohibits the following:

- Any act to collect a pre-petition debt;
- Any act to create, enforce, or perfect a lien against property of the estate or property of the debtor to collect a pre-petition debt; or
- The commencement of any proceeding against the debtor to collect a pre-petition debt.

Note: For a complete list of acts prohibited by the automatic stay, see 11 USC 362(a).

- (4) **Automatic Stay Allowed Activities.** The following list contains some common actions taken by the IRS that do not violate the automatic stay. For additional actions that do not violate the stay, see IRM 5.9.3.5(10), Automatic Stay, Certain Activities Allowed.

- Refiling a valid pre-petition Notice of Federal Tax Lien (NFTL) before it expires,
- Making an assessment for certain taxes and issuance of one informational notice,

Caution: Debtors receive one notice of assessment of a pre-petition tax return balance due. Subsequent notices may not be issued. If they are, Insolvency must be contacted immediately.

- An audit to determine a tax liability,
- Conducting, continuing, and completing a Trust Fund Recovery Penalty (TFRP) investigation,
- Demanding tax returns,

- Sending a statutory notice of deficiency, or
- Setting off pre-petition income tax refunds against pre-petition income tax liabilities (11 USC 362(b)(9) and (26)).

(5) **Automatic Stay Violation.** If the IRS willfully violates the automatic stay, the IRS may be subject to damages and attorney's fees under 11 USC 362(k) and IRC 7433(e). See the following cases for additional information:

- **In re Chesnut**, 422 F.3d 298, 300 (5th Cir. 2005) (determined that the creditor violated the stay when it foreclosed on an asset to which the debtor had only an arguable claim of right);
- **In re Price**, 42 F.3d 1068 (7th Cir. 1994) (The IRS willfully violated the stay by sending a post-petition notice of intent to levy to Chapter 13 debtors, with knowledge of the bankruptcy proceedings, and declining to stop collection action); and
- **In re Bulson**, 117 B.R. 537 (B.A.P. 9th Cir. 1990) (The IRS initiated automated collection proceedings, based on the mistaken belief that the bankruptcy case was closed which constituted a willful violation of the stay).

5.17.9.5

(07-18-2024)

Who May Be a Chapter 7 Debtor

(1) Generally, any entity may be a debtor under Chapter 7 except:

- Governmental units,
- Railroads,
- Insurance companies, and
- Banks and other financial institutions.

(2) Eligible entities include individuals, partnerships, limited liability companies, and corporations.

(3) Changes made to the Bankruptcy Code by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) created provisions for bankruptcy petitions filed on or after October 17, 2005. An individual may not file a Chapter 7 petition unless such person received a briefing from an approved non-profit credit counseling agency, including a budget analysis, within 180 days before the petition date. (11 USC 109(h))

Exception: Individual debtors are excepted from this requirement if the United States Trustee determines that the approved non-profit credit counseling agency for the district in which the debtor resides is not reasonably able to provide services to additional debtors, or the bankruptcy court excuses the debtor from the required credit counseling.

5.17.9.6

(07-18-2024)

Initiating a Chapter 7 Case

(1) **Chapter 7 Bankruptcy Petition.** A Chapter 7 case begins with the filing of a bankruptcy petition. The petition may be voluntary or involuntary. A voluntary petition is filed by the debtor. An involuntary petition may be filed by creditors on behalf of the debtor. However, at least three creditors must join together to file an involuntary Chapter 7 petition for the debtor. Spouses can join in one petition. (11 USC 302)

(2) **Bankruptcy Rule 1007.** Bankruptcy Rule 1007 requires the Chapter 7 debtor to file certain supporting documents within a fixed time after filing the petition. These documents include a mailing matrix, statement of financial affairs

(SOFA), and schedules. As part of the schedules, the debtor must also include Form B22A, or a means test calculation statement, which is required by 11 USC 707(b)(2)(C).

- (3) **Federal Income Tax Returns.** For cases filed post-BAPCPA, the debtor must provide the trustee with a copy of the federal income tax return required under applicable law for the most recent tax year ending immediately before the beginning of the bankruptcy case and for which a federal income tax return was filed. However, the debtor may elect to provide the trustee with a transcript instead of a copy of such return. In either case, the copy of the return or transcript must be provided to the trustee at least 7 days before the date set for the first meeting of creditors. (11 USC 521(e)(2))
- (4) **Filing Requirements.** For cases filed post-BAPCPA, 11 USC 521(j) requires the debtor to file all post-petition returns as they become due. If the debtor fails to do so, the IRS may request the court to convert or dismiss the case.

5.17.9.7
(07-18-2024)
The Trustee

- (1) In a Chapter 7 case, the United States Trustee must appoint a member of the panel of private trustees as interim trustee promptly after the order for relief (11 USC 701). The interim trustee serves until a trustee is elected by eligible creditors. This election is held at the first meeting of creditors which must be held within a reasonable time after the order for relief (11 USC 341). If no trustee is elected, the interim trustee will serve as the trustee. The interim trustee has all the rights and powers of a bankruptcy trustee.
- (2) A Chapter 7 trustee is a fiduciary and is accountable to the court for the trustee's actions. The trustee represents the estate and, in particular, the unsecured creditors.
 - a. The Chapter 7 trustee's duties under 11 USC 704 include collecting the assets of the estate. This may include converting property to money, examining claims of creditors, and objecting where appropriate.
 - b. In addition, the trustee must investigate the finances of the debtor, file tax returns where required, and pay taxes when due.
 - c. If the debtor served as the administrator of an employee benefit plan at the time that the bankruptcy petition was filed, the trustee must continue to perform the debtor's duties as administrator.
 - d. At the end of the bankruptcy proceedings, the trustee is required to file a final report with the court and the United States Trustee. Any creditor, including the IRS, may object to this report or account.
 - e. If the debtor is an individual and has mostly consumer debts, the trustee must also file a statement indicating whether the debtor's case would be presumed to be an abuse of the Bankruptcy Code under 11 USC 707(b)(2). The statement must be filed within 10 days after the first meeting of creditors.

5.17.9.8
(07-18-2024)
**Conversion or Dismissal
of a Chapter 7 Case**

- (1) **Conversion to Chapter 11, 12 or 13.** Under 11 USC 706(a), the debtor may convert a Chapter 7 case to Chapter 11, 12, or 13 at any time, as long as the case was not originally converted from a Chapter 11, 12, or 13. The debtor must be eligible under the chapter to which they seek to convert. Also, the court may, upon request of a party in interest and after notice and hearing, convert a Chapter 7 case to Chapter 11 at any time. The court may not convert a Chapter 7 case to Chapter 12 or 13 unless the debtor requests or consents to such conversion (11 USC 706(b) & (c)).

- (2) **Dismissal by Courts.** Under 11 USC 707(a), the court may dismiss a Chapter 7 case only after notice and a hearing. The court must show cause, including:
 - a. Unreasonable delay by the debtor that is prejudicial to creditors;
 - b. Non-payment of any required fees or charges; or
 - c. Failure of the debtor in a voluntary case to file the schedules required by 11 USC 521(a)(1) within 15 days of the commencement of the case. However, dismissal is only on a motion by the United States Trustee.
- (3) **Other Grounds for Dismissal.** The court can dismiss a case on other grounds, including bad faith in filing the petition.
- (4) **Consumer Debt Dismissal.** When an individual's debts are primarily consumer debts, 11 USC 707(b) provides that the court, on its own motion or on a motion by the United States Trustee, trustee, or any party in interest (e.g., panel trustee or a creditor), may dismiss a Chapter 7 case filed by an individual debtor, or convert the case to Chapter 11 or 13 (with the debtor's consent). In this situation, the court must first find that granting Chapter 7 relief would be an abuse under 11 USC 707(b)(2). There is a presumption of abuse if the debtor fails to meet a means test calculation based on income, expenses, and certain debts. In a joint case, the means test calculation would be based on the financial information of both spouses.
- (5) **Disabled Veteran Dismissal and Conversion Restriction.** A Chapter 7 case cannot be dismissed or converted based on any form of means testing if the debtor is a disabled veteran and the indebtedness occurred primarily during a period of active duty or while the debtor was performing a homeland defense activity (11 USC 707(b)(2)(D)(i)).
- (6) **Active Duty Dismissal and Conversion Restriction.** A Chapter 7 case cannot be dismissed or converted based on any form of means testing with respect to the debtor while the debtor is on, and during the 540 day period beginning immediately after the debtor is released from, a period of active duty of not less than 90 days or performing a homeland defense activity of not less than 90 days (11 USC 707(b)(2)(D)(ii)).

5.17.9.9
(07-18-2024)
Proofs of Claim

- (1) Generally, in Chapter 7 cases, a proof of claim must be filed in order to share in the distribution of the estate. The procedure for filing claims in Chapter 7 are set forth in Bankruptcy Rules 3001 and 3002.
- (2) In a Chapter 7 case, the schedules may indicate that there are no assets from which a dividend can be paid. In such cases, the court may include a statement that it is unnecessary to file proofs of claim in the notice of the first meeting of creditors (Bankruptcy Rule 2002(e)). If the payment of a dividend subsequently becomes possible, further notice will be given for the filing of claims.
- (3) In Chapter 7 cases, to be timely, an IRS claim must be filed within 180 days after the order for relief (Bankruptcy Rule 3002(c)). A late filed priority claim may still receive priority treatment, as discussed in IRM 5.17.9.12 (2)(a) below. See 11 USC 726(a)(1) for additional information.
- (4) As a result of BAPCPA's amendments to 11 USC 503(b)(1), for cases commencing on or after October 17, 2005, the IRS may file a proof of claim for its

administrative expenses as a condition to being allowed a claim for such expenses. The IRS is not required to file for that action but has the option to do so.

- (5) When the IRS is timely noticed in a case, Insolvency caseworkers must file claims prior to the governmental bar date. If the IRS was not notified in sufficient time to file a proof of claim prior to the governmental bar date, the liability in the individual Chapter 7 Asset case may be excepted from discharge. For additional information, see the guidance in IRM 5.9, Bankruptcy and Other Insolvencies, along with the following:
 - IRM 5.9.6.12(7), Proof of Claim - Asset Cases, Expired Bar Dates
 - IRM 5.9.17.8.9 , Procedures for Processing Bankruptcy Discharges when the IRS Received No Notice or Late Notice in the Asset Case

5.17.9.10
(07-18-2024)
**Bankruptcy Estate
Income Taxes**

- (1) **Individual Chapter 7 Cases.** The bankruptcy estate in an individual Chapter 7 case is a separate taxable entity that must file its own tax return. The Chapter 7 trustee has the duty to file the estate tax return.
- (2) **Corporate and Partnership Chapter 7 Cases.** In corporate and partnership Chapter 7 cases, no separate taxable entity is created. The trustee is responsible for filing required tax returns.
- (3) **Termination of Tax Year for Individuals.** If certain requirements are met, individuals in Chapter 7 have the right to terminate their tax year when the petition is filed (IRC 1398). This creates two short taxable periods in the year in which the bankruptcy petition is filed. One taxable period is the pre-petition liability for which the estate is liable. The other taxable period is the post-petition liability which is the debtor's responsibility. See IRM 5.9.6.13, Post-petition Liabilities — Individuals, and IRM 5.9.6.14, Bankruptcy Estate Income Taxes - Separate Taxable Entity, for further discussion on the separate taxation of an individual Chapter 7 debtor and the bankruptcy estate.

5.17.9.11
(07-18-2024)
Treatment of Tax Liens

- (1) Under 11 USC 724(b), tax lien claims are subordinated to priority claims under 11 USC 507(a)(1) through 507(a)(7), including administrative expenses and certain other priority claims. If a case was converted from Chapter 11 to 7, administrative expenses (other than wages, salaries, or commissions arising after the date of the petition), only include the expenses incurred during the Chapter 7 case (11 USC 724(b)(2)).
- (2) Property of the estate that is subject to a tax lien or proceeds of such property is distributed in the following order:
 - a. To the holders of liens senior to the tax lien;
 - b. To priority claims specified in 11 USC 507(a)(1) – (7), up to the amount of the allowed tax claim that is secured by the tax lien;
 - c. To the holder of the tax lien, in the amount equal to the difference between the amount of the priority claims above and the actual amount of the tax lien;
 - d. To the holders of liens junior to the tax lien;
 - e. To the holder of the tax lien in the amount of the allowed tax claim that is not paid under c above; and
 - f. To the estate.

- (3) Before subordinating a tax lien claim to the priority claims described above, the trustee must first use all unencumbered assets of the estate to satisfy those claims (11 USC 724(e)).

5.17.9.12
(07-18-2024)
**Distribution of Property
of the Estate**

- (1) **Trustee's Goal.** The trustee's main goal is to recover and liquidate the assets in the bankruptcy estate for the debtor's unsecured creditors. This is done by liquidating the debtor's non-exempt and unsecured assets and taking actions to recover money or property.
- (2) **Distribution Order.** Under 11 USC 726, the property of the estate is to be distributed as follows:
 - a. Timely filed priority claims (or if late filed, on or before the earlier of 10 days after the date that the summary of the trustee's final report is mailed to creditors, or the date of final distribution) in the order specified in 11 USC 507;
 - b. General unsecured claims, including claims filed late due to the claimant's lack of notice or actual knowledge of the case;
 - c. Other late filed general unsecured claims;
 - d. Claims (secured or unsecured) for a fine, penalty, or forfeiture, or for multiple, exemplary, or punitive damages to the extent such claims are not for actual pecuniary loss;
 - e. Interest at the legal rate from the date of the petition on any claim paid under the above; and
 - f. The debtor.
- (3) **Administrative Claims on Chapter 7 Conversions.** Upon conversion to a Chapter 7, administrative claims of the previous chapter retain their administrative status, but are paid after the administrative claims of the Chapter 7 (11 USC 726(b)).
- (4) **Insufficient Funds.** If funds are insufficient to pay all the creditors in a certain class, the creditors within that class will share those funds on a pro-rata basis (11 USC 726(b)).

5.17.9.13
(07-18-2024)
**Adequate Protection and
Turnover**

- (1) The concepts of adequate protection and turnover in bankruptcy are explained in IRM 5.17.8.11, Adequate Protection, and IRM 5.17.8.24 , Turnover to the Trustee — Assets Seized Pre-petition, respectively.
- (2) In Chapter 7 cases, adequate protection should rarely be the basis for the IRS to resist turning over property of the estate to the trustee. In most instances, adequate protection arguments are not warranted or reasonable. A secured tax claim in a Chapter 7 case can be subordinated to unsecured priority claims pursuant to 11 USC 724 if the trustee cannot pay them with unencumbered assets of the estate. The IRS is only entitled to amounts determined by the distribution scheme established in 11 USC 726.
- (3) 11 USC 721 allows the court to authorize the Chapter 7 trustee to operate the debtor's business for a limited period. The operation must be in the best interest of the estate and consistent with the orderly liquidation of the estate. For example, the trustee may continue operating the debtor's business to sell it at a higher price as a going concern. It may be more reasonable for the IRS to make an argument for adequate protection of the IRS's secured interests in these rare cases.

5.17.9.14
(07-18-2024)

Discharge of Chapter 7 Cases

- (1) **Discharge of Chapter 7 Debt.** Under 11 USC 727, discharge is available to individuals in Chapter 7 cases unless there are grounds for denial of discharge. When the debtor is eligible for discharge, the individual is discharged from most debts that arose prior to the filing of the Chapter 7. Debts that are excepted from discharge and which are non-dischargeable are listed in 11 USC 523.
- (2) **Denial of Discharge.** Under 11 USC 727, the grounds for denial of discharge are listed in the table below:

Grounds for Denial of Discharge

11 USC 727 Subsection	Grounds for Denial of Discharge
(a)(2)	With the intent to defraud or delay, debtor has transferred, destroyed, or concealed property of the debtor within one year before the bankruptcy or property of the estate during bankruptcy.
(a)(3)	Debtor has concealed, falsified, destroyed, or failed to preserve financial records, unless justified under the circumstances.
(a)(4)(A) through (a)(4)(D)	In connection with the bankruptcy case, debtor knowingly and fraudulently: <ul style="list-style-type: none"> • Made a false oath or account; • Presented or used a false claim; • Gave, offered, or received money, property, or advantage for acting or forbearing to act; or • Withheld any recorded information relating to the debtor's property or financial affairs from an officer of the estate.
(a)(5)	Debtor has failed to satisfactorily explain any deficiency in assets available to meet liabilities.
(a)(6)(A) through (a)(6)(C)	Debtor has refused to obey a lawful order of the court or to testify, unless the order was to respond to a material question or to testify to a matter on which the debtor has asserted the privilege against self-incrimination and not been granted immunity.
(a)(7)	Debtor has committed an act specified in items 1 through 5 of this table on or within one year before the date the bankruptcy was filed, or during the case, in connection with the bankruptcy of an insider.
(a)(8)	Debtor has received a discharge in a Chapter 7 or Chapter 11 case commenced within eight years of the filing of the petition.

11 USC 727 Subsection	Grounds for Denial of Discharge
(a)(9)(A) and (a)(9)(B)	Debtor has received a discharge in a Chapter 12 or Chapter 13 case commenced within six years of the filing of the petition unless the unsecured debts provided for in the plan were entirely satisfied, or at least 70 percent of the claims were satisfied and the plan was proposed in good faith and was the debtor's best effort.
(a)(10)	Debtor executed and the court approved a written waiver of discharge after the order for relief.
(a)(11)	After filing the bankruptcy petition, debtor has failed to complete the required personal financial management course (unless the court or trustee determines that the debtor is not required to complete such a course).
(a)(12)(A) and (a)(12)(B)	The court finds that there is reasonable cause to believe that 11 USC 522(q)(1) applies to the debtor, and there is a proceeding pending in which debtor may be found guilty of a felony as described in 11 USC 522(q)(1)(A) or liable for a debt as described in 11 USC 522(q)(1)(B) (includes certain debts arising from violations of securities laws and criminal acts or willful misconduct that causes serious physical injury or death to another individual in the preceding 5 years).

- (3) **Revocation of Discharge.** A discharge may be revoked by the court upon the request of the trustee, a creditor, or the United States Trustee under 11 USC 727(d) if:
- The discharge was obtained through fraud of the debtor which the requesting party did not know of until after the discharge was granted;
 - The debtor knowingly and fraudulently failed to report the acquisition of or entitlement to property of the estate;
 - The debtor has refused to obey a lawful order of the court or to testify;
 - The debtor has failed to explain a material misstatement in an audit or failed to make documents related to the audit available for inspection.
- (4) **Discharge Revocation Requests.** The request for revocation must be made:
- Within one year of the discharge in the case of a discharge obtained through fraud; or
 - Before the later of one year after the discharge or the date the case is closed, in the case of failure to report property or failure to obey an order of the court.
- (5) **Non-Dischargeable Debt.** While a Chapter 7 debtor may be granted a general discharge, any debt that is non-dischargeable under 11 USC 523 will not be barred from further collection activity. Additionally, post-petition interest on non-dischargeable taxes is non-dischargeable.
- (6) **Discharge Injunction.** If a debt is discharged, the discharge injunction under 11 USC 524 prohibits any act to collect the debt against the debtor personally.

If the IRS willfully violates the discharge injunction, it may be subject to damages and attorney's fees under IRC 7430 and IRC 7433(e).

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Discharge and the Individual Shared Responsibility Payment (SRP) Liability Assessed under MFT 35 on IDRS and/or Mirrored on IDRS under MFT 65

- (1) Liabilities assessed under the Individual Shared Responsibility Payment (SRP) of the Affordable Care Act (ACA) are assessed on the Individual Master File (IMF) under Master File Tax (MFT) Code 35. Joint SRP MFT 35 liabilities may be mirrored into separate SRP liabilities for each spouse on IDRS under MFT 65. In either case, the SRP liability is treated as an income or excise tax under 11 USC 507(a)(8)(A) or (E), which both give priority status when the return is due within three years of the bankruptcy. However, since the liability on the SRP MFT 35 and/or SRP MFT 65 module is derived from the debtor's Form 1040, U.S. Individual Income Tax Return, certain information from the debtor's Form 1040 is used in determining dischargeability of the SRP. When determining dischargeability, the SRP MFT 65 liability of the debtor spouse is treated in the same manner as the SRP MFT 35 liability of the debtor spouse for the specific tax year. Similarly, the SRP MFT 65 liability of the non-debtor spouse (NDS) is treated in the same manner as the SRP MFT 35 liability of the NDS.

Reminder: In community property locations, the NDS is treated in the same manner as the debtor spouse. For additional information, see IRM 5.9.3.5.1.1 , Community Property; IRM 5.9.18.6.8 , Community Property; and IRM 25.18 , Community Property.

- (2) An individual or joint debtor may not be eligible for discharge in the current Chapter 7 case if they received a discharge in a prior bankruptcy case. Eligibility is determined by the type of bankruptcies filed by the debtor and the petition date of the prior bankruptcies. See IRM 5.9.5-3 , Allowable Elapsed Time Between Bankruptcy Filings and Discharges, for additional information.
- (3) Discharge may depend upon whether the IRS was properly noticed of the bankruptcy filing. See IRM 5.9.17.8.9 , Procedures for Processing Bankruptcy Discharges when the IRS Received No Notice or Late Notice in the Asset Case, and IRM 5.9.17.10(4) , Chapter 7 Discharge Actions, Lack of Notice in Chapter 7 No Asset Cases, for determining if taxes may be excepted from discharge due to improper notice.
- (4) The list below contains the exceptions to discharge for the SRP MFT 35 and/or SRP MFT 65 module(s) when the individual or joint debtor receives a discharge in a Chapter 7 case and the IRS was properly noticed in the case:
 - The SRP is non-dischargeable if the Form 1040 was due, with extensions, within the three-years prior to the bankruptcy petition date.
 - The SRP may be non-dischargeable if the tax on the Form 1040 is non-dischargeable due to willful evasion or fraud. When the SRP may be non-dischargeable due to willful evasion or fraud, refer the case to Area Counsel for guidance. See IRM 5.9.17.8.2(1) , The Fraud or Willful Evasion Exception to Discharge, Exception to Discharge.
 - The SRP is non-dischargeable if the income tax on the Form 1040 is non-dischargeable because the Form 1040 was filed after assessment. See IRM 5.9.17.8.1, Determining Dischargeability of Late Filed Returns in Which a SFR was Prepared, for additional information on SFRs and discharge.
 - The SRP is non-dischargeable if the Form 1040 was filed late and after the date that is two-years before the date of the bankruptcy petition.

Note: The three-year “look-back” provision in 11 USC 507(a)(8) and two-year period with regard to late returns are automatically tolled during a prior bankruptcy while the automatic stay is in effect. See IRM 5.9.13.19.3(4), Unsecured Priority, BAPCPA Tolling, for additional information.

- (5) 11 USC 507(a)(8)(A) and (E) govern income and excise taxes. Because SRP liabilities are a tax for which a return is required, the IRS employs the same dischargeability analysis as 11 USC 507(a)(8)(A)(i). If the tax on the Form 1040 is non-dischargeable, the tax on the SRP MFT 35 module and/or SRP MFT 65 module is non-dischargeable. The interest is always non-dischargeable when the tax is non-dischargeable. No penalty is assessed or accrued on the SRP.

Example: A taxpayer timely files their 201712 income tax return on 04/15/2018. There is no tax due on the Form 1040. The taxpayer listed \$350 as the SRP amount on Line 61 of their Form 1040. The IRS assesses a MFT 35 and/or MFT 65 module for the SRP for 201712 in the amount of \$350. On 02/15/2021, the IRS assesses an Examination deficiency (TC 300) for \$1500 on the 30-201712 income tax module. The taxpayer files Chapter 7 on 05/18/2021.

➤ *The tax and interest due on the Form 1040 are not dischargeable.* The TC 300 was assessed 89 days prior to the bankruptcy petition date. The TC 300 is a priority debt under 11 USC 507(a)(8)(A)(ii). It is excepted from discharge under 11 USC 523(a)(1)(A).

➤ *The tax and interest on the SRP MFT 35 and/or SRP MFT 65 module are dischargeable.* The 30-201712 module was due on 04/15/2018. The return due date was more than three-years prior to the bankruptcy petition date. The SRP MFT 35 and/or SRP MFT 65 module is an excise tax. The tax and interest on the excise tax on the MFT 35 and/or MFT 65 module are not excepted from discharge under 11 USC 523(a).

Example: A taxpayer files their 1040 for 201712 late on 05/03/2019. The taxpayer did not have an approved extension (TC 460) for filing the 201712 income tax return. There is no tax due on the Form 1040. The taxpayer listed \$350 as the SRP amount on Line 61 of their Form 1040. The IRS assesses a MFT 35 and/or MFT 65 module for the SRP for 201712 in the amount of \$350 on 06/19/2019. On 02/15/2021, the IRS assesses an Examination deficiency (TC 300) for \$1500 on the 30-201712 income tax module. The taxpayer files Chapter 7 on 05/14/2021.

➤ *The tax and interest due on the Form 1040 are not dischargeable.* The TC 300 was assessed 89 days prior to the bankruptcy petition date. It does not matter that the return due date was more than three-years prior to the petition date. It does not matter that the return was filed late and more than two-years prior to the petition date. The determining factor is that the TC 300 is a priority tax under 11 USC 507(a)(8)(A)(ii). It is excepted from discharge under 11 USC 523(a).

➤ *The tax and interest on the SRP MFT 35 and/or SRP MFT 65 module are dischargeable.* The 30-201712 module was due more than three-years prior to the bankruptcy petition date. The 30-201712 return was filed more than two-years prior to the bankruptcy petition date. The tax and interest on the excise tax on the MFT 35 and/or MFT 65 module are not excepted from discharge under 11 USC 523(a).

5.17.9.15
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**Collection Outside
Bankruptcy**

- (1) The IRS can collect non-dischargeable liabilities from all assets of the debtor after the automatic stay is lifted. These assets include the exempt, abandoned, non-administered, excluded and after-acquired property of an individual debtor.
- (2) With a properly filed pre-petition NFTL, the IRS may collect dischargeable liabilities from property exempted from the bankruptcy estate after the automatic stay lifts if the lien remains valid to the specific property.
- (3) The IRS may collect dischargeable liabilities from property excluded from the estate or abandoned by the trustee after the stay lifts due to the statutory lien. A NFTL is not required prior to levy on excluded or abandoned assets. Excluded property includes ERISA-qualified pension plans and other plans described in 11 USC 541(b).

Note: See IRM 5.9.17.5, Exempt, Abandoned or Excluded Property (EAEP), for additional information on collecting dischargeable liabilities after the discharge if the lien remains valid against the specific property.