Nothing is Certain but . . . : Tax Liens and the Judgment Creditor

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By James C. Eschen

A client had an award from the Department of Labor Standards Enforcement for unpaid wages to enforce. He wanted fast action—the employer was liquidating and had posted the company's equipment on eBay. Fortunately, a sheriff's levy or two would go a long way to paying him what he was due.

But the Secretary of State's website[1] showed bad news. Like many employers not paying their employees, this one was not paying other bills, either. Specifically, it had outstanding tax liens to the Internal Revenue Service and the Franchise Tax Board. Any money that my client got from a sheriff's levy, and any fee I received, could well end up in Uncle Sam's pocket. We closed the file—at least for the time being.

THE TAX LIEN'S CREATION AND BREADTH

When a taxpayer fails to pay "any tax" after demand, the Internal Revenue Code (title 26, United States Code ["I.R.C."]) creates a lien for any unpaid amounts, including not just the taxes but penalties, interests, and costs of collection.[2] The term "any tax" is broad, including more than just income taxes owed by the taxpayer. For example, the lien commonly arises from unpaid payroll taxes.[3]

The lien's purpose is to "insure prompt and certain collection of taxes due the United States from tax delinquents."[4] Generally, the lien does not arise automatically when a taxpayer fails to pay but only upon the "assessment" of unpaid taxes.[5] "Assessment of tax as defined consists of no more than the ascertainment of the amount due and the formal entry of that amount on the books of the secretary."[6] The lien exists until the tax is paid or liability for it "becomes unenforceable by reason of lapse of time"—generally ten years from the date of assessment.[7]

Once the IRS assesses a taxpayer's delinquency, the lien extends to "all property and rights to property, whether real or personal, belonging to such person."[8] This language "reveals on its face that Congress meant to reach every interest in property that a taxpayer might have."[9] Although federal law determines priority, state law defines the rights the taxpayer has in the property.[10] For example, the lien attaches to an escrow for a sale of a California liquor license because the license is property under state law.[11] The IRS enforces the lien by bringing a foreclosure action or by levying on the property.[12]

THE TAX LIEN'S PRIORITY

Once a tax lien arises, federal law governs the priority of competing liens.[13] Even without recording, the tax lien is effective upon assessment against all persons.[14] In the absence of a statutory exception, it takes priority over any other claim to property.[15] Even workers who have not received their wages must defer to an IRS lien.[16]