Federal Income Tax in Chapter 7

Generally, taxes are treated the same as other debts in a **chapter 7** bankruptcy case. Taxes may be treated as secured, unsecured, or non-priority unsecured, or some combination. IRS Code, found in 26 U.S.C. 6321, states that the government is secured if it has recorded a notice of lien. Taxes that have been recorded as a lien are a priority and must be paid in bankruptcy and cannot be discharged.

A colleague of mine, John Greifendorf, addressed the question, Can I discharge Federal Income Tax in Bankruptcy? His article is concise and outlines five conditions for discharging what the debtor owes to the IRS and even sets forth and example to follow.

The Five Conditions are:

1. The due date for filing the tax return was not less than three years ago
2. The tax return was filed at least two years ago
3. The tax assessment is at least 240 days old
4. The tax return was not fraudulent
5. The tax payor is not guilty of tax evasion

If the debtor meets the qualifications, then the tax liability is not a priority and is discharged in bankruptcy; 11 U.S.C. 523(a)(1). Unsecured taxes that are deemed a priority, fall outside the scope of the conditions discussed by Mr. Greifendorf and cannot be discharged in bankruptcy.

Timing is a critical component in deciding to file for bankruptcy protection and the advice of a bankruptcy attorney will address this issue. Best practices include filing all tax returns prior to filing a bankruptcy petition with the court. Seek the advice of a CPA or tax attorney regarding IRS claims.