Bankruptcy Taxation/Consumer Bankruptcy

Resolving Tax Issues in Bankruptcy Court

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Resolving Tax Issues in Bankruptcy Court

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Bankruptcy Taxation Committee
Consumer Bankruptcy Committee

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A Primer on Diagnosing Bankruptcy Tax Problems and Determining Jurisdiction

By: Hon. Robert Kwan
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1. How do I get started as a bankruptcy practitioner who may have to handle a client's bankruptcy-related tax problems?

First, you need to find out if your client (i.e., "debtor" in bankruptcy parlance, or "taxpayer" in tax parlance) has tax problems, and if so, what are the nature of the problems. Second, ideally, you will have identified these problems before filing for bankruptcy. However, clients often either, intentionally or unintentionally, hide certain problems (taxes and intra-family debts being the most common) from their lawyers. Bankruptcy lawyers, without formal training in tax controversies and IRS procedures, are frequently called upon to address technical tax issues.

Often, bankruptcy lawyers are afraid of handling tax related issues. While referring tax matters to a tax specialist is usually advisable, as a bankruptcy lawyer you should know enough about bankruptcy taxation to identify issues. Moreover, for many bankruptcy practitioners, an outside referral may not be practical given monetary or time constraints. Further, in consumer or small business cases , the bankruptcy practitioner may be required to handle a client's bankruptcy tax problems. (N.B. The rare criminal tax problem should be referred out unless you are an experienced criminal defense attorney.)

Thus, you need to obtain certain basic information including: (a) communicating with the client's accounting or bookkeeping professionals, if any, about tax compliance; (b) you need to obtain "taxpayer account transcripts" from you client (these are the official records of IRS contacts with your client), which shows the nature of the tax debts owed and whether tolling events (such as offers in compromise) exist; and (c) you need to obtain copies of the client's recent federal and state tax returns, which are also needed to comply with BAPCPA compliance obligations in business and individual cases.

Often, the client does not know or understand the tax problems. By obtaining the baseline tax reporting and account information, you will have clues to assist the clueless, such as tax collection notices and demand letters, tax levy and lien notices, tax assessment notices and demands for payment, tax audit notices and correspondence, visits from tax auditors and collectors (or criminal tax investigators).

Next, you need to make a list of the tax liabilities, what type, what time period, what amount, whether assessed or not, whether under audit or in collection and whether secured or not.

You need to know different types of taxes: income, employment, excise, estate/gift, sales, and property taxes. Taxes can be imposed at federal, state and local levels.

It is absolutely essential to obtain accurate information about the client's tax liabilities by getting tax account transcripts and copies of the tax returns. Once you identify specific tax liabilities, you should obtain transcripts of the client's tax accounts to see the amounts of the liabilities and

payments and credits. Transcripts will show useful account information, such as the type of liability, the due dates of tax returns as extended, the dates of assessment of taxes, the amounts of principal, interest and penalty, and collection activity, such as dates of notice and tax lien recordation, pendency of offers in compromise. This information is absolutely critical to enable you to ascertain whether the taxing authorities have tax claims against the client, and if so, how to characterize the claims as priority, unsecured general, or secured, and whether the claims are non-dischargeable. The tax claim analysis cannot be practically done without this information. Moreover, tax transcripts will show when payments are made and posted to past due tax accounts, which may reveal potential preference claims under 11 U.S.C. § 547.

Tax transcripts and copies of tax returns can be ordered from taxing authorities, usually through their websites. There is special access for tax practitioners on a dedicated website or hotline (you should consider yourselves tax practitioners for this purpose). For the IRS, you will submit an IRS Form 2848, Power of Attorney and Declaration of Representative, to request and receive tax information, and to represent a client before the IRS.

Priority status of tax claims is generally determined by 11 U.S.C. § 507(a)(3) and (8). Careful analysis of the statutory definitions of priority tax claims under this provision is absolutely essential.

Secured status of tax claims should be verified by reviewing tax transcripts and copies of recorded tax lien notices against the compliance requirements of 26 U.S.C. § 6323 and the Uniform Federal Tax Lien Registration Act of the taxpayer's state of domicile, e.g., California Code of Civil Procedure, § 2101 et seq. In order to perfect a tax lien against third parties, including a bankruptcy trustee with avoiding powers, tax lien notices must be perfected through recordation with the county recorder where individual taxpayers live and with the state Secretary of State for an entity taxpayer as to personal property and with the county recorder where the property is situated as to real property. (N.B. Some states have unitary registries for lien filing other have dual registries, make to perform proper title/UCC searches as part of your due diligence to determine the secured nature of a tax claim.) While public record searches may reveal recorded tax liens through computer databases like Westlaw and Lexis/Nexis, the actual tax lien notices should be reviewed for correctness of information or coverage of the claims.

Dischargeability of tax claims of individual debtors is generally determined under 11 U.S.C. § 523(a)(1). Priority tax claims under 11 U.S.C. 507(a)(8) are non-dischargeable under 11 U.S.C. § 523(a)(1)(A). Tax claims for which a tax return or equivalent report or notice were not filed or given less than two years before petition date are non-dischargeable under 11 U.S.C. § 523(a)(1)(B). Tax claims based on fraud or evasion are non-dischargeable under 11 U.S.C. § 523(a)(1)(C). Tax transcripts need to be scrutinized for the dates of assessment, return due dates, failure to file returns or late filed returns, imposition of penalties which may indicate fraud.

2. What should I know about the differences between tax determination and tax collection problems?

Tax practitioners (including those who are handling bankruptcy tax controversies) must understand the differences between *tax liability determination* (*assessment* in tax parlance) problems and tax collection problems (*collections* in tax parlance) or liability versus collections, because these differences are important substantively and procedurally.

Tax liability determination problems involve disputes over the correct amount of the tax liability due. Tax collection problems involves disputes over payment of a tax liability. A client could have one or both problems with respect to a particular tax liability, that is, the taxpayer raises doubts about whether the tax is validly due or his/her/its ability to pay the tax. Audits are the IRS' method for determining tax liabilities and can take place in the form of a letter request, office meeting with an IRS revenue agent (auditor) or a field visit from an IRS revenue agent.

Most tax liabilities are self-reported on tax returns, and the taxing authorities "assess" or record the tax liabilities on their books based on what is shown as due on the tax returns. Once the taxing authority assesses the tax liability, its administrative powers to collect the tax become effective, including the existence of a federal tax assessment lien against the taxpayer and all of his or her property and rights to property, which can then be perfected as to third parties by the recording of a notice of federal tax lien. Before assessed tax is collected, the taxing authority must give notice of the assessment and demand for payment, and a certain number of notices are generally required to be given before tax lien and levy or seizure notices may be issued and/or executed. As a result of the 1998 IRS Restructuring and Reform Act, the IRS also must give taxpayers notice of so-called collection due process rights to be heard before enforced tax collection of tax lien notice recordation and tax levy and seizure notice issuance, but these administrative remedies must be invoked by certain time limits or tax court rights are lost (30 days in the case of a collection due process hearing).

If a taxpayer fails to file a return or the return is considered inaccurate, the taxing authority may audit the tax liability and will determine a tax liability in accordance with administrative procedures. Before the taxing authority may assess a tax liability based on an audit, generally speaking, it provides notice and opportunity for the taxpayer to be heard on the audit findings by conferring with the auditor (called a revenue agent at the IRS) and to request a conference with the auditor's supervisor.

At the IRS, the initial audit report is called a "30-day letter," which the taxpayer can request a meeting with the revenue agent and manager. If there is no agreement, you can file a protest for review by the IRS Appeals Office, or the IRS will issue a statutory notice of deficiency for income taxes (also known as a "90-day letter"), and the taxpayer has the right to file a petition for review with the U.S. Tax Court. The IRS cannot assess the proposed tax deficiency until the time for Tax Court review expires or a final judgment of that court. The IRS generally has three years from the assessment based on a filed return to determine audit deficiencies, six years for substantial understatements of income, and an open statute if no return is filed. *See*, 11 U.S.C. 507(a)(8)(income taxes not assessed, but assessable as of the petition date). The audit periods for state taxes may differ, though often they piggyback on IRS audits and limitations periods.

The deficiency procedures for income taxes do not apply to certain taxes like employment taxes. Employment taxes are self-assessed based on the return filed by the taxpayer, or determined after audit. There is an opportunity for administrative review of an audit report with meetings with the agent, the manager and the Appeals Office, but there is no notice of deficiency issued for Tax Court review. The unagreed to audit amount is assessed, and the taxpayer may only challenge the employment tax liability in a tax refund suit, or in defense of a collection lawsuit by the government. However, while the administrative tax refund claim procedures must be exhausted, the divisible tax rule applies in federal employment tax refund suits, where the taxpayer need only pay the tax for one employee per taxable period (usually a calendar quarter) to contest the tax liability.

The rules applicable to state income, employment and sales taxes may differ. They may follow the income tax deficiency procedures model for state income taxes, but the federal employment tax refund procedures for state employment and other taxes.

3. *What are the various remedies or fora that I might consider as a bankruptcy practitioner in resolving my client's bankruptcy-related tax problems?*

Before filing for bankruptcy, you and your client may consider the regular tax dispute remedies outside of bankruptcy, through an offer-in-compromise, installment agreement or placing the taxpayer in currently not collectable status. Which option is available for a taxpayer largely depends on the financial resources of the taxpayer. These options are open to both businesses and consumers.

As with any dispute, the nature and complexity of the tax problem impacts the ability of the taxpayer and government to settle the dispute. Simple, low dollar amounts may be handled at lower levels, while complex, high dollar amounts may need additional approvals. Also, higher levels of approval may require write-ups, which take time and effort, not only for you as the taxpayer's representative, but also, your counterpart on the government side. Also, you should be aware that sometimes there are disagreements within the government side about settling or litigating a matter, and just because you reached a tentative settlement with the front line staff, it does not mean that approval by higher levels of authority is automatic. Oftentimes, there is some deference to front line staff, but it is not complete (i.e., if someone higher up thinks the store is being given away, which may or may not be true). You may need to cooperate and help your counterpart sell the deal with further information or evidence to support it.

Taxing authorities are governmental agencies which have hierarchal institutional structures ("bureaucracy"), and finding the right personnel with jurisdiction and authority over your matter is your goal if you want to resolve a bankruptcy tax controversy. The government as a creditor is concerned about collecting as many dollars as it can like other creditors, but it is a special creditor because it is a regulatory institution charged with enforcement of the tax laws, which must be applied uniformly and consistently as a matter of policy. So it must be considered that when dealing with the government, the bottom line is whether a resolution of a bankruptcy tax controversy protects the revenue (i.e., collecting as many dollars as possible) and satisfies the policy mission to apply the tax laws uniformly and consistently. The government is guided by,

and considers, the applicable law governing taxation and debtor/creditor rights, including bankruptcy, which is embodied in the statutes (including the tax and bankruptcy codes) and the case law, but also, its own pronouncements of policy in regulations and other published guidance, including regulations, revenue rulings and procedures.

On larger or more complex transactions, the IRS may issue private letter rulings to taxpayers, which gives guidance on how the IRS will treat a prospective transaction. Thus, a wise practitioner will take into account the government's interests of collecting revenue and uniformity in enforcing tax law and policy in developing an approach to resolving a bankruptcy tax controversy.

As to tax liability determination of federal taxes by the IRS ("doubt as to liability"), during the audit, the taxpayer may discuss the proposed audit findings with the auditor (revenue agent), request a conference with the auditor's supervisor, and/or request review by the Appeals Office. The taxing authority representatives at the administrative level will be IRS administrative staff. If these remedies are unsuccessful, the taxpayer may litigate the audit determination by filing a timely petition for review with the U.S. Tax Court (an Article I legislative court like the Bankruptcy Court) in response to a statutory notice of deficiency applicable to certain taxes, including income taxes.

In Tax Court, the government is represented by IRS Chief Counsel attorneys on behalf of the Commissioner of Internal Revenue, and there is no right to a jury trial. Tax Court cases may be settled with IRS counsel, who have discretion to request informal assistance of IRS administrative staff to settle through audit reconsideration resulting in a stipulated disposition. Settlement authority is within IRS Chief Counsel's Office, but agency representatives are consulted. If a tax is determined by the Tax Court either by settlement or litigation, the tax may be assessed, and the Tax Court judgment is considered res judicata.

As another alternative to litigation, the IRS administratively may consider an installment payment arrangement with the taxpayer, or an offer in compromise ("OIC") based on doubt as to collectability or doubt as to liability. Tax practitioners differ in opinion on whether the OIC procedures are useful in settling tax disputes. Once a tax is assessed, the IRS gives notice of the assessment and demands payment, and if no payment is made, as part of its collection due process procedures, the IRS gives notice that it may take enforced collection actions, such as file tax lien notices or issue and execute tax levies, but that a taxpayer may seek administrative review of the IRS's decision to file tax lien notices and issue tax levies in collection due process procedures (known as "CDP").

If a tax is assessed after a defaulted statutory notice of deficiency, or if the statutory deficiency procedures are not applicable (i.e., federal employment taxes), the taxpayer may litigate the determination of the tax liability on the merits in the U.S. District Court or the U.S. Court of Federal Claims by filing a tax refund action. However, as a jurisdictional prerequisite, a taxpayer must pay the tax in full, file an administrative claim for refund by the IRS and wait for denial of the claim or the passage of six months before filing suit (i.e., a statutory opportunity for

the IRS to resolve the claim administratively; however, a taxpayer may request the IRS to immediately deny the refund claim to proceed to suit).

Generally speaking, paying the tax in full is a jurisdictional prerequisite for a tax refund suit (this includes income taxes, but not employment taxes, which the rule is payment of tax for one employee per each calendar quarter disputed). In a tax refund suit, the taxpayer has the burden of proof to show that the tax is erroneous by a preponderance of the evidence, but there is a right to a jury trial.

Federal tax litigation outside the Tax Court is handled by attorneys of the Tax Division of the Justice Department, the government's litigation agency. The IRS makes referrals to the Justice Department in civil suits against the government over federal taxes and for affirmative litigation on behalf of the government. The Justice Department is separate from its client agencies, and has different personnel (i.e., attorneys and supervisors) and different litigation and settlement policies and procedures than the IRS administratively or with its Chief Counsel.

Justice Department handling of referred tax cases take time. Once a DOJ Tax Division lawyer is assigned a case, the lawyer must communicate with the IRS and get up to speed about the matter from the IRS by obtaining the internal administrative file (which you may obtain much of by way of a Freedom of Information Request). To settle a case, a recommendation must be approved by many levels of supervisors in both the DOJ Tax Division and IRS.

The taxpayer may litigate the merits of a tax liability in defending against an affirmative tax collection suit brought by the government in federal district court. The government brings these suits to reduce a tax assessment to judgment before the normal 10-year collection statute of limitations expires, to set aside a fraudulent transfer or to collect the tax through judicial foreclosure on real property owned by the taxpayer. In such cases, there is a jury trial right, and the government is represented by the Justice Department. Settlement is authorized through Justice Department review procedures. Tax litigation disputes also come up in third party actions naming the government as a lien creditor in interpleader or quiet title actions.

From a bankruptcy practitioner's perspective, the major downside of tax dispute resolution outside of bankruptcy is length of time it takes to resolve a tax dispute compared to the fast pace of bankruptcy litigation. Bankruptcy offers a number of advantages in resolving tax disputes. First, the automatic stay halts the government's administrative tax collection activity, stopping execution of administrative levies and perfection of tax liens post-petition. The automatic stay also stays non-bankruptcy tax litigation, such as affirmative tax collection suits or pending Tax Court review litigation. Second, the taxpayer as bankruptcy debtor may initiate litigation to determine the merits of a tax liability on a relatively expedited basis without no required prepayment of the tax as required in tax refund litigation or without having to comply with the tax deficiency procedures for Tax Court review.

Specifically, a debtor may seek a re-determination of tax liability under 11 U.S.C. § 505 upon motion, or may file an objection to a proof of claim for taxes under Fed. R. Bankr. P. 3007, or may file a motion to determine a secured tax claim under Fed. R. Bankr. P. 3012, or may file an

adversary proceeding to determine validity, extent or priority of tax lien under Fed. R. Bankr. P. 7001, or to determine dischargeability of a tax debt under 11 U.S.C. § 523.

Due to the full payment rule to challenge many tax liabilities in the nonbankruptcy courts, the bankruptcy court may be the only available judicial forum due to the debtor's inability to pay the tax. For example, in a no asset Chapter 7 liquidation bankruptcy case, a taxpayer may bring a debt dischargeability adversary proceeding to challenge a tax liability for state sales taxes, which he could not do in state court without full payment of the liability. As well, since the case is no asset, there is no ability to object to a claim that is not filed, and state sovereign immunity might bar a determination of the state tax under 11 U.S.C. § 505. Further, § 505 permits the bankruptcy court to abstain and in no asset cases the DOJ will ask the court to abstain for lack of a bankruptcy purpose. Whether such a motion is granted is within the discretion of the court.

The debtor-in-possession, bankruptcy trustee or a debtor-in-possession may also bring avoidance actions to set aside preferential transfers to taxing authorities or turnover of collected assets. Whether such cases are viable is very fact specific, but generally, only payments on account of unsecured non-priority claims can be avoided.

After the IRS is given notice of a bankruptcy filing, it enters a bankruptcy freeze code on its computer database to prevent inadvertent collection activities that would violate the automatic stay. The IRS has a Special Procedures Staff (SPS) (and similar staff with state and local taxing authorities) to take actions to protect the government's interests in bankruptcy cases, and SPS staff is local and an important point of contact for practitioners with respect to tax issues in bankruptcy cases.

SPS (or insolvency) advisors are senior revenue officers who are promoted from the general collection ranks are not usually not attorneys, but have extensive in-house training in bankruptcy law and procedures and experience dealing with bankruptcy issues. SPS advisors interact with the various functions in the IRS to address and resolve bankruptcy tax problems on behalf of the IRS, such as communicating between the public (i.e., taxpayer and representative) and IRS audit staff, nonbankruptcy collection staff, including the automated collection staff, IRS and Justice Department attorneys on a particular matter. Unlike general IRS collection officers, SPS advisors are assigned to work on bankruptcy tax matters and have experience in dealing with tax issues in bankruptcy, and understand the risks of litigation for the government creditor in bankruptcy court. In contrast, IRS auditors (revenue agents) and collection (revenue) officers have minimal, if any, knowledge or experience about bankruptcy or litigation hazards in general (though revenue officers are given training about the hazards of automatic stay violations). Trying to resolve a matter at the SPS level cannot be overemphasized in routine, smaller dollar bankruptcy cases, because at this level, you have the possibility of resolving a matter with minimal time, effort and expense for you and the government.

Practitioners should understand that they may have opportunities to resolve bankruptcy tax disputes informally with the taxing authorities, such as the IRS, before initiating formal litigation. This is particularly helpful in trying to negotiate consensual treatment of tax claims for a plan of reorganization. Often, the initial efforts of counsel for a bankruptcy debtor is to

focus on the particular creditor whose action has prompted the bankruptcy filing, usually, the major secured creditor, the landlord of debtor's business premises, or a judgment lien creditor, and not as to tax creditors unless they are in active collection.

Taxing authority representatives know what treatment the tax authorities are entitled to under the Bankruptcy Code, whether under Chapter 7, 11 or 13. The taxing authorities, and the IRS in particularly, are given notice of the filing of new bankruptcy cases and will generally make sure that timely proofs of claim are filed in asset Chapter 7 cases, and in Chapter 11 and 13 cases. The taxing authorities will have checked the tax accounts of new bankruptcy debtors based on the tax identification numbers on the petition documents, and whereas, counsel for the debtor may not have complete knowledge of the client's tax accounts until the transcripts are obtained. Counsel for a Chapter 11 debtor should probably sound out the IRS through SPS if treatment of the IRS claims is less than what is required under the Bankruptcy Code, such as full payment of priority claims within 5 years of petition date.

Generally speaking, SPS will refer the case to the Justice Department to object to a Chapter 11 plan which provides for less favorable treatment of the tax claims than required under the Bankruptcy Code, and the objection will be litigated or settled as a contested matter under Justice Department procedures. Debtor's counsel might be able to contact and persuade the IRS through SPS to consent to less favorable treatment of its claims under a plan by showing that the government would benefit by such agreement because it would receive more than it would under a Chapter 7 liquidation before the plan becomes a contested matter. Or for example, a debtor may want to contact SPS to persuade the IRS that a claim is not secured and should be amended because it is undersecured due to insufficient collateral value of collateral or improper perfection. However, if the debtor seeks a straight concession of tax liabilities based on doubt as to liability on the merits, formal litigation will be needed through an objection to claim, which would be referred to the Justice Department for defense. Moreover, settlement based on collectability generally is not possible in a Chapter 13 case because many of the priority tax claims would survive a Chapter 7 discharge and would be collectible post-bankruptcy.

Resolving Tax Issues in Bankruptcy Court

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PRE-PLANNING CONSIDERATIONS AND POINTERS

TRANSCRIPTS OF ACCOUNT

ALWAYS obtain a tax account transcript (sometimes referred to as a record of account by the I.R.S.) prior to the filing of a bankruptcy. The practitioner should obtain similar information regarding state income taxes from the applicable state authority.[2]

PREPARE TAX RETURNS FOR FILING

Unfiled or late filed return: § 523(a)(l)(B) excepts from discharge any tax for which a return was required and was not filed or for which a return was filed within two years from the date that the bankruptcy petition was filed. *NOTE: This exception to discharge also applies to Chapter 13 bankruptcies.*

Returns Effect Tolling: Generally, in order for an income tax liability to be dischargeable in a Chapter 7 bankruptcy, at least three years must have expired since the due date of the tax return (including extensions), at least two years must have to expired since the tax return was filed by the taxpayer, and at least 240 days must have expired since the date the tax was assessed. See Bankruptcy Code § 523(a)(1) which incorporates by reference and renders non-dischargeable the priority tax claims set out in § 507(a)(8).

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[1] A portion of the materials in this presentation, and the remarks of Susan A. Berson, are based on discussions in Chapter 1 and 14 of Federal Tax Litigation by Susan A. Berson, and presented with the permission of the copyright holder, ALM Properties, LLC, and the publisher, Law Journal Press, a division of ALM Media, LLC. All rights reserved. Copies of the complete work may be ordered online at www.lawcatalog.com or at www.lawjournalpress.com/player/Book 98 Federal Tax Litigation.html.

[2] There are a few ways to obtain transcripts from the IRS: (i) e-Services, http://www.irs.gov/Tax-Professionals/e-services---Online-Tools-for-Tax-Professionals;
(ii) Practitioner Priority Hotline 1-866- 860-4259; (iii) Form 8821 Tax Information Authorization (permits transcripts for the tax types/forms listed but is not a "power of attorney" so IRS will not send you notices). Reviewing the transcripts helps counsel learn which categories of tax claims apply to your client (e.g. secured, unsecured), and especially when --and sometimes whether-returns were filed for purposes of calculating dischargeability consequences.

FEDERAL TAX LIENS

Generally, "if any person liable to pay any tax neglects or refuses to pay same after demand, the amount . . . shall be a lien in favor of the United States." *See* IRC § 6321. To perfect its lien, the IRS files a Notice of Federal Tax Lien ("NFTL"). Section 6323(f) allows the states to designate the place for filing a notice of federal tax lien. If a lien is filed by the IRS in the designated recording site for a taxpayer's residence of record, a lien on the taxpayer's personal property exists. Even if the IRS lien secures taxes which are dischargeable in bankruptcy proceedings, the IRS is not required to release its liens. *See In re Isom*, 901 F.2d 744 (9th Cir. 1990). The tax lien remains in place as to the property that the debtor owns on the date that the bankruptcy petition is filed. Be aware that when sufficient equity exits in the debtor's property, the IRS may seek to satisfy its lien in such property post-discharge. A Notice of Federal Tax Lien's statute of limitations on collection is 10 years, plus, 30 days.

OFFER-IN-COMPROMISE ("OIC")

An Offer in Compromise is the IRS version of a settlement program. By filing an Offer in Compromise (IRS Form 656, Offer in Compromise (rev. May 2012)) with the IRS, the taxpayer is seeking an agreement from the IRS to pay less than the full amount of the tax liabilities owed. There is no one-size fits all approach, and significant financial information must be disclosed by the taxpayer. Wage earners complete IRS Form 433-A (OIC) Collection Information Statement for Wage Earners and Self-Employed Individuals (rev. May 2012), or Form 433-B (OIC), Collection Information Statement for Businesses (rev. May 2012).

Unlike the flexible ease certain "pennies on the dollar" advertisements[3] suggest, successfully achieving IRS acceptance of a reasonable OIC is a time-consuming process. It is also a detailed-oriented one. The IRS OIC examination officers follow very specific guidelines and criteria for analyzing whether an offer is ripe for IRS acceptance, including prerequisites a taxpayer must satisfy before the IRS will engage in an OIC application review.

OIC Prerequisites

Before the IRS will consider an OIC (or any other resolution of a tax debt), the taxpayer must have (1) filed Forms 1040 for all required years, and (2) be in compliance with his or her current year income tax payment obligation. This means: (i) a self-employed individual must have made adequate estimated income tax payments for the current year to date (of the OIC), (ii) for wage earners, income tax withholding during the current year must be made; (iii) an offer to pay a lump sum must be accompanied by a payment of at least 20 % of the offer amount, in addition to a $186.00 OIC application fee. An offer of more than five periodic payments must be accompanied by the first proposed payment, and a $186.00 OIC application fee, and, during the time the offer is being considered, all proposed payments must be submitted;(iv) no pending bankruptcy. If you have a client who does not satisfy (i), (ii), (iii) and (iv) above, do not pursue the OIC. [4] The IRS will reject the OIC and keep the "deposit" payment.

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[3] For a discussion of the debt settlement companies to avoid, see the free publication, "Tax Debt Settlement Hucksters Secrets Revealed: If You Owe The IRS, Read This Before You Pay Anyone to Help You Try To Settle" (free publication on iTunes, https://itunes.apple.com/us/book/tax-debt-settlement-hucksters/id531145315?mt=11).

[4] For low income individuals, waiver of the fees may be sought.

Also, upon acceptance, the taxpayer will be required to file and pay all required taxes for five years. (When the IRS sends a letter of acceptance, the date in the upper right hand corner of the letter determines when the taxpayer's five-year period starts.)

OIC Mechanics

There are three reasons the IRS will accept an amount less than the full liability due: "Doubt as to Liability"; "Doubt as to Collectability"; or, because the "Efficient Tax Administration (ETA)" requires it.[5] "Doubt as to Liability" is only for people who do not believe that they owe the tax liability. Litigation hazards, calculation errors when the assessment was made are examples of when an OIC based on "Doubt as to Liability" may be pursued.

For "Doubt as to Collectability" or "ETA," the reasonable collection potential must be determined before extending an offer amount or period of time for payment. "Reasonable Collection Potential" is the term for calculation made by the IRS to determine whether the taxpayer liability will be settled for less than the total amount owed. If after utilizing the IRS "reasonable collection potential" formula it is determined that the liability can be paid in full as a lump sum, or a through an installment agreement, the IRS will reject an OIC application.

Reasonable collection potential occurs after the IRS verifies the taxpayer's income and assets for purposes of whether the taxpayer's offer satisfies IRS legal requirements. There is a set formula to determine the amount it is willing to accept, though the factors that go into formula are based on the National Standards for living standards. Be prepared that the "Allowable Living Expense" standards of the IRS commonly differ than what the taxpayer views as average expenditures for basic daily living necessities. IRS processing time varies once an application is filed. On average, expect a six-month processing wait, though the longest processing time has been approximately two years. (If more than two years have passed and the IRS has not responded, the offer is considered accepted.) Before submitting the IRS Form 433-A (Form 433-B Businesses) and Form 656, consult the National Standards for purposes of determining allowable expenses for housing, transportation, and related expenses.[6] Payments for student loans guaranteed by the federal government are allowed in the calculation, and payments for delinquent state and local taxes may be allowed based on a percentage basis of tax owed to the state when calculating the reasonable collection potential, and corresponding offer amount.

For many taxpayers/debtors, the precise amount they should offer and length of time for payment is complicated. Concerning income-producing assets in a viable on-going business, the equity in those assets will not be considered when adding the value of total assets to disposable income. Generally speaking, ongoing, viable businesses are allowed their tools of the trade, up to a threshold amount which is subject to change according to inflationary standards. Concerning dissipated assets, the IRS does not include them in calculating the OIC reasonable collection potential. (Historically, the IRS looked to them – even after the taxpayer had lost the assets – for purposes of an OIC.) Disclosure of a taxpayer's total household income and expenses is required.

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[5] For more information on this category, see the IRM, Part 5, 5 008 011, available online at http://www.irs.gov/irm/part5/irm_5-008-011.html.

[6] There are various software programs available now providing OIC assistance. Caution should be used, as with all programs, because a computer program is only as good as the information put into it, and the updates made to it concerning inflationary changes and the like.

For offers proposing to pay within five months or less, the IRS looks at one year of future income. For offers proposing to pay within 24 months of less, the IRS looks at two years of future income. All offers must be fully paid within 24 months of the date the offer is accepted.

Should an OIC be rejected, the Internal Revenue Code provides for an administrative appeal.[7] Collection activity may not occur while the appeal is pending.[8] When considering the merits of an appeal, be aware that pursuing an appeal may have tolling consequences, as further discussed below.

OIC Tolling Consequences

The 240-day period.[9] During the time period that an OIC was "in effect"[10] or pending overlaps the 240-day period, the running of the 240-day period is tolled, plus 30 days. Should an OIC be denied, and an appeal occur, the time period in which the appeal occurs is defined as "pending."

The Three-Year Period.[11] The OIC, without more, does not toll the three-year period. Ordinarily, the three-year period is computed from most recent date the tax return is **due** for the tax year (typically April 15 of the year following the taxable year).

Other Commonly Overlooked Tolling Situations That May Coincide with OIC

Collection actions – and challenges to them – take various forms. Financially struggling taxpayers have unique factual circumstances, but, common to many of them are activities that coincide with OIC's. Below are some activities to inquire about of the taxpayer/debtor because they could have effect of tolling the 240-day period, as well as the 3-year period. The IRS Account Transcripts[12] for a taxpayer's tax year(s) also detail the activity should the taxpayer/debtor not be a reliable source of information. (It should be mentioned that if the transcript shows the taxpayer made an installment agreement application, the installment agreement generally does not toll either the 240-day assessment nor the 3-year period.)[13]

Collection Due Process Hearing Request.[14] Essentially, a collection due process hearing is an appeal of a proposed collection effort. It often coincides with an OIC. A CDP tolls the 3-year period and the 240-day period.

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[7] I.R.C. § 7122.
[8] I.R.C. § 6331(k); IRM § 8.23.1.2.
[9] 11 U.S.C. § 507(a)(8)(A)(ii) (During the time a pending or "in effect" OIC overlaps the 240-day period, the running of the 240-day period is tolled plus 30 days. Tax claim was assessed at least more than 240 days preceding the filing date of the bankruptcy. 11 U.S.C. § 507(a)(8)(A)(ii).
[10] IRM § 5.8.1.9.4. "Periodic payment Offer" or "Deferred Periodic Payment Offer" means "in effect."
[11] 11 U.S.C. § 507(a)(8)(A)(i) (OIC is not listed as tolling the three- year period governed by this three-year rule).
[12] Obtain Account Transcripts from the IRS via (i) Online: Password, Practitioner ID requires previous set-up with the IRS; (ii) IRS Priority Hotline: (866) 860-4259. Have an executed IRS Form 8821, Form 2848 Power of Attorney (including your CAF number) by the client ready to be faxed to the IRS, along with the client's taxpayer identification number(s); and, (iii) IRS agent/officer may also be able to provide expedited access.
[13] 11 U.S.C. § 507(a)(8)(G) (absent from code list of tolling events is installment agreement).
[14] I.R.C. §§ 6220, 6330.

Extension to File Return. Consult the transcripts for whether an extensions of time for filing returns was made. If so, an extension to file delays the start of the 3-year period.[15]

Tax Court, Appeals, "Closing" statements. Generally speaking, the IRS litigation process may delay assessment. Consequently, the start of the 240-day assessment period needs to be verified, especially if Tax Court litigation resulting in appeal(s), or a closing statement.

SHORT-YEAR TAX ELECTION IN CHAPTER 7 AND CHAPTER 11

The short-year tax election is found in Section 1398, and applies only to the bankruptcy estate of an individual debtor in cases filed under Chapter 7 or Chapter 11. This is because it is only in these circumstances where the bankruptcy filing creates a separate taxable entity. Before explaining the potential benefits and mechanics of a short-year tax election, it is important to understand that for purposes of life as a Chapter 7 filer or Chapter 11 debtor-in-possession, it is akin to a parallel universe where everything may appear the same, but, because the filing occurred, new rules of conduct must be followed. Indeed, for Federal income tax purposes, a separate entity is created for an individual or married couple when relief is sought under Chapter 7 or Chapter 11 of the Bankruptcy Code.[16] In Chapter 12 or Chapter 13 filings, a separate taxable entity is not created, nor in any case, where the debtor is not an individual.

Determining The Bankruptcy Estate Tax Liability

Analysis of the short-year election starts with defining the estate. The bankruptcy estate will succeed to the same tax attributes (*e.g.* deduction, net operating loss (carrybacks/carryforwards) that the debtor had been entitled prior to the bankruptcy filing. Upon conclusion, or dismissal, of the bankruptcy proceedings (and the estate), any unused attributes are transferred back to the debtor for tax purposes.[17] Generally, the estate tax liability is limited to the scope of the estate and its assets. This means that upon the filing of bankruptcy, income and losses generated are those of a separate taxable entity, and computed separately from the individual debtor. So, the estate would compute its own taxable income just as an individual would do so. Practitioners who represent financially struggling taxpayers may find the short-year election to be of benefit in that a timely short-year election can result in a portion of the debtor's tax liability being shifted to the estate (as a priority claim under § 507(a)(8)).[18]

Importantly, even when the estate appears to have generated no income, additional events may cause a reporting obligation to arise. For example, an obligation to file a tax return can still arise in circumstances of cancellation of indebtedness income, or a sale or exchange. In the context of cancellation of indebtedness income, it is a common scenario in Chapter 7 proceedings. If the taxable event (cancellation of indebtedness) occurs before the commencement of the case, the debtor would recognize the income[19], unless the exclusion under § 108 applies.[20]

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[15] 11 U.S.C. § 507(a)(8)(A)(i).
[16] IRC §§ 1398(a), (b); See also S. Rep. No. 1035, 96th Cong., 2d Sess. 24-25 (1980) (Fresh start purpose).
[17] IRC § 1398(I).
[18] IRC § 1398(d).
[19] IRC § 61(a).
[20] IRC § 108.

Given that administrative expenses are allowed as deductions by the bankruptcy estate, any administrative expenses which have been accrued, and properly deducted by the debtor before bankruptcy should not also be deducted by the estate when paid.[21] Administrative expenses incurred, but not deducted, in the current year may be carried back three years and carried forward seven years. However, be aware that the implementation of how the carryback and carry-forward tools are used, should be done in a certain order. First, calculation of the administrative costs for carryover purposes is done after a separate net operating loss carryover calculation is made.[22] Then, the administrative expense carryover is used after the net operating loss has been applied.

A Chapter 11 plan of reorganization generally vests all the property of the estate in the debtor, except as otherwise provided in the plan or order of confirmation. For most Chapter 11 cases, the debtor-in-possession remains in control without a trustee, and the debtor-in-possession must perform all the functions and duties of a trustee.[23]

Individual Debtor/Taxpayer

For purposes of calculating the individual taxpayer's assets and income, a transfer (other than by sale or exchange) of an asset from the debtor to the bankruptcy estate is not treated as a disposition for income tax purposes. (In other words, gain or loss, recapture of deductions or credits, acceleration of income or deductions does not automatically occur when the petition for bankruptcy is filed.) To the extent that the taxpayer is a partner in a partnership or S Corporation shareholder, such interest(s) the individual owns when then bankruptcy petition are filed become property of the estate.[24] (The tax considerations the partnership, or S Corporation, respectively, should analyze when a partner or shareholder seeks Chapter 7 protection is a subject that is beyond the scope of the presentation. For now, it is important to know that there additional concerns that a filing presents to a partnership or S Corporation, however.)

Upon termination of the bankruptcy, any transfer (other than by sale or exchange) of the estate's assets to the debtor is not treated as a disposition. In those circumstances where the Trustee/estate abandons property which makes its way back to the debtor, this is a nontaxable disposition of property. Yet, when the debtor receives the abandoned property from the estate, the debtor calculates the basis in the property. It should also be mentioned that carrying back a net operating loss occurring on a tax year ending after commencement of the bankruptcy to any pre-bankruptcy tax year is not permitted by the debtor.

The "Short-Year" Election Shift[25]

A timely short-year election made by the debtor can shift some, or all, of what would ordinarily be the taxpayer/debtor's tax burden to the bankruptcy estate. By making a proper election, the debtor splits the taxable year into two taxable years. It does not apply when the debtor has no assets other than exempt property, however.[26] Also, only individual debtors may

[21] 11 U.S.C. § 503. Administrative expenses include wages, salaries and fees paid to attorneys and accountants for services performed subsequent to filing the bankruptcy petition.
[22] IRC § 172 (b)(2).
[23] 11 U.S.C. § 1107(a), except for the duties found in 11 U.S.C. §§1106(a)(2), (3) and (4).
[24] 11 U.S.C. § 541.
[25] IRC § 1398(d)(2).
[26] IRC § 1398(d)(2)(C).

make a short-year election.[27]

EXAMPLE Debtor files for bankruptcy protection under Chapter 7 on March 15. A timely election is made shortly thereafter resulting in two tax years. The first year covers January 1 through March 14, and, the second year covers March 15 through December 31. If no election had been made, the debtor's taxable year remains, as it would normally be, January 1 through December 31.

Mechanics[28]

The first taxable year-ends on the day before the day the bankruptcy case was commenced. The second taxable year begins on the commencement date. The short-year election must be made by the debtor on or before the date due for filing his or her Federal return for the short-taxable year. The short-year election is considered made if the complete tax return for the short period is timely filed.[29] An election can be made on the debtor's tax return for the short year, by writing the words "SECTION 1398 ELECTION" at the top of the return.[30] On or before the fifteenth day of the fourth month following the close of a fiscal year, a return indicating the short-election must be filed, in other words, the fifteenth day of the fourth full month following the close of the taxable year.[31] The short-year election is irrevocable.[32] Where a debtor is married and files a joint tax return, separate elections are permissible as long as they are timely, and the return is considered filed jointly.

Tangible Benefits

By making a proper election, the tax liability for the first short-year is a priority claim under § 507(a)(8). If a debtor files a Chapter 7 bankruptcy petition in which there are assets for distribution to creditors, and the debtor makes a short-year election, then the income tax liability attributable to the earlier or pre-petition short year will constitute a priority tax claim under § 507 of the Bankruptcy Code. If this occurs, then it is possible for this tax liability for the pre-petition short year to be paid from assets of the debtor's bankruptcy estate (assuming that those assets are sufficient to pay some or all of that liability). The remainder would be a non-dischargeable administrative expense claim. In Chapter 11, there can be a significant difference in treatment required under the Bankruptcy Code. Without the election, the tax obligation is a post-petition administrative expense claim that would need to be paid in full when due or at the effective date of a plan. With the election, the pre-petition portion of the year can be paid over five years from the petition date as a priority claim.

Also, when a debtor makes a proper short-year election, the tax attributes of the debtor as of the end of the first taxable year are transferred to the estate. This is essentially a tool for the estate to shelter income. Otherwise, a debtor's tax attributes as of the end of the full taxable year will carryover when an election is not properly made.

Making an election requires careful analysis as to what will benefit the bankruptcy filer.

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[27] IRC §§ 1398, 1399.

[28] See Treas. Reg. §§ 1.1398-1, 2, and 3.

[29] See Treas. Reg. § 1.6081-1(b)(2).

[30] For additional examples, 1A Collier on Bankruptcy at § 9.05[b].

[31] Temp. Treas. Reg. § 7a. 2(d); IRC § 6072.

[32] IRC § 1398(d)(2)(D).

A couple general rules of thumb to keep in mind are (i) when a debtor has taxable income for the short tax year ending the day before the bankruptcy petition is filed, it's likely an election could be beneficial for the debtor because the tax liability arising from the income, would become a claim against the estate; (ii) in contrast, when a loss for the first short year tax year has been generated, the debtor should carefully consider not making the election because the loss would be carried over to the bankruptcy estate. With no election, the loss becomes part of the debtor's return for the full year, and this could enable the debtor to use it to offset income earned later in the year. When a loss exists for the entire year, it would become a net operating loss carryover that is not acquired by the bankruptcy estate, so it is still available to the debtor.

Ultimately, the § 1398 election depends on (i) the likelihood that the bankruptcy estate can pay the short-year pre-petition tax liability; (ii) the individual's tax situation in the year of the bankruptcy filing. Put another way for those who represent individuals considering bankruptcy, the core examination for tax purposes is whether as a debtor, the client will have a better "fresh start" when the use of a short-year election results in carrying forward a net operating loss from the first short-year to reduce the nondischargeable tax debt. If the answer is in the affirmative, then, it is more likely than not after filing bankruptcy, the debtor should prepare to make a timely short-year 1398 election. If bankruptcy filing is to occur regardless of the tax consequences, a possible scenario where an election would not be made is if the net operating loss could be used against the filer's projected income after the filing of the petition. For illustration purposes of how to implement the general rules of thumb when analyzing a situation, consider the following:

EXAMPLE 1: Debtor's income totals $20,000 as of August 16, 2013. Debtor had generated net operating losses that can be carried forward or back to other tax years. Debtor files for Chapter 7 relief on August 17, 2013.Without the election, the tax owed is due on April 15, 2014 for the period January 1 through December 31. The NOL attributes will pass to the bankruptcy estate, and the trustee can use to reduce the estate's tax liability. Any unused losses would then pass back to Debtor upon termination of the bankruptcy case.

Applying the General Rule of Thumb: the debtor should consider making a proper election because the first year, January 1 through August 16, the post-petition tax claim would become a pre-petition obligation § 507(a)(8) priority claim due for payment at the end of the short-year tax return, so, if debtor makes a timely 1398 election, debtor would be entitled to use the net operating losses.

EXAMPLE 2: During the January 1 through August 16, Debtor has had little income. Net operating losses have arisen, however. Debtor files for Chapter 7 relief on August 17, 2013. Debtor expects to receive a total of $30,000 in payments over September through December. If Debtor does not make the election, the Chapter 7 Trustee can use the losses, even though Debtor's little income earned pre-bankruptcy is not going to be offset.

Applying the General Rule of Thumb, it appears that making an election would not be the best choice for the debtor. This illustrates how a person with little income and more losses in the portion of the tax year before the bankruptcy petition was filed, would be financially better off retaining the loss(es) for use in later years.

Bankruptcy and Tax Implications from a Business Perspective.

Prepared by: Gerald M. Gordon and Kirk D. Homeyer

Gordon Silver

Tax Implications of Sales in Bankruptcy – § 363 v. Plan of Reorganization

§ 363 Sales

- Sale of Debtor's Assets
  - The debtor retains the tax attributes of the sale; the purchaser does not acquire them.
  - The debtor will recognize any gain or loss on the asset transferred and the purchaser receives a cost basis in the asset. Such gain or loss is the difference between: (1) the amount realized from the sale, which can include cash, the fair market value of any property received from the buyer, and any liabilities assumed by the buyer; and (2) the seller's adjusted tax basis of the transferred asset, which is the debtor's initial purchase price of the asset, adjusted based on depreciation and cap-ex.
  - The buyer takes a tax-basis for the amount of consideration the buyer paid for the asset. That is, the buyer will obtain a "step-up" in the tax basis of the asset, which may be desirable to the buyer as the tax-basis step-up can result in future depreciation or amortization income deductions for the buyer.
  - COD Income – A debtor will usually have cancelation of debt income (COD income), which can be excluded from gross income. 26 U.S.C. § 108(a)(1)(A).
    - If the debtor benefits by excluding COD income from its gross taxable income, the debtor must also reduce its other advantageous tax attributes. Net operating losses (NOLs), capital loss carryforwards, and tax basis in the asset are reduced dollar-for-dollar. Moreover, credits (such as general business credits, minimum tax credits, and foreign tax credits) are reduced by 33.3 cents per dollar of COD income. 26 U.S.C. § 108(b).
  - Even if the debtor takes a net loss from the sale, there still may be taxes that are owed. For example, a debtor may still owe taxes if it is unable to offset net capital losses against net capital gains, for depreciation recapture, and of course, state taxes, such as transfer taxes.
- Sale of Debtor's Stock

- The buyer may want to retain and benefit from the debtor's tax attributes, such as NOLs and the debtor's tax basis in the asset. In such a case, it is preferable to purchase the debtor's stock rather than its asset.

- In a stock purchase under § 363, the buyer acquires a tax-basis in the debtor's stock equal to the amount of consideration paid for such stock, but assumes the debtor's tax basis in the debtor's asset.

Sale Pursuant to a Plan of Reorganization or Liquidation

- Sales pursuant to a plan of reorganization or liquidation will generally have the tax consequences applicable to § 363 sales.

- § 1146(a) provides: "The issuance, transfer, or exchange of a security, or the making or delivery of an instrument of transfer under a plan confirmed under section 1129 of this title, may not be taxed under any law imposing a stamp tax or similar tax."

    - Courts have held that this provision provides that debtors are exempt from state law transfer taxes. In re T.H. Properties, LP, 509 B.R. 490, 493 (Bankr. E.D. Pa. 2013); In re Jacoby-Bender, Inc., 758 F.2d 840, 841 (2d Cir. 1985).

    - If the debtor sells assets in accordance with § 1146(a), the debtor can avoid paying certain taxes, such as stamp and transfer taxes.

- Importantly, § 1146(a) only applies to sales that are consummated pursuant to the terms of a plan of reorganization or liquidation; it does not apply to sales that occur prior to or outside a plan, such as a sale of the debtor's assets pursuant to § 363. Florida Dep't of Revenue v. Piccadilly Cafeterias, Inc., 554 U.S. 33, 52 (2008).

Bankruptcy/Tax Effects on Various Debtor Entities

Partnerships and LLCs taxed as a partnership

- Income and losses generally flow through to the partners or interest holders.

- COD Income - If there is a discharge of debt of a partnership or LLC taxed as a partnership, each partner is taxed on his allocable share of entity level COD income. 26 U.S.C. § 704. COD income exclusions under 26 U.S.C. § 108(a) are applied at the partner level, not the entity level. 26 U.S.C. § 108(d)(6).

    - The flow-through allocation of entity level COD income produces a corresponding increase in each partner's outside basis in his partnership interest under 26 U.S.C. § 705. If the COD income allocated to the partner is greater than the partner's outside basis in the partnership entity, then the allocated COD

income will be deemed a distribution and thus a gain subject to taxation. 26 U.S.C. § 731(a)(1).

- NOLs – Generally, no NOL deductions are available to partnerships and LLCs taxed as partnerships, but their investors may use their distributive shares to calculate individual NOLs.

S-Corps and LLCs taxed as S-Corps

- COD Income – If there is a discharge of S-Corp debt, COD income is first recognized (or rather, excluded with corresponding reductions in other tax attributes) at the corporate level pursuant to 26 U.S.C. § 108(b). To the extent COD income is not otherwise excluded by the various statutory exclusions under 26 U.S.C. § 108(b) at the corporate level, each shareholder is taxable on his allocable share of remaining COD income, and may use any of the §108(b) exclusions at the shareholder level.

- NOLs – Generally, no NOL deductions are available to S corps. However, their shareholders may use their distributive shares to calculate individual NOLs.

C-Corps

- COD Income – COD income is recognized at the corporate level and attributes are reduced at the corporate level.

- NOLs – In the event of a change in ownership of a C-Corp, 26 U.S.C. § 382 provides limitations on the use of NOLs.
    - In general, an ownership change is a more than 50% ownership change of the value of stock of the C-Corp with NOLs within a three-year period.
    - These NOL limitations generally restrict the amount of income against which pre-change NOLs can be applied in any taxable year after the ownership change.
    - However, bankruptcy can reduce these limitations. For example, 26 U.S.C. § 382(l)(5) provides that the § 382 limitations will not apply to a debtor corporation if (1) immediately before an ownership change, the corporation was under the jurisdiction of a bankruptcy court, and (2) after an ownership change, the pre-change shareholders and certain "qualified creditors" of the debtor own stock constituting 50 percent or more of the vote and value of the new purchasing corporation.

Tax Implications of a Prepetition Sale v. Postpetition Sale

Prepetition Sale

- § 507(a)(8) priority tax claims include income and excise taxes, among others.
  - These priority tax claims are nondischargeable pursuant to § 523(a)(1). They will take priority over general unsecured claims, but are subject to administrative tax claims (see below).
  - In a Chapter 11 case, such claims are not generally assigned to a class of claims, but rather, are paid in full on the effective date of the plan. § 1129(a)(9).
  - If the debtor sells its assets prior to filing bankruptcy, the taxes incurred in connection with the sale will be afforded priority status ahead of general unsecured claims, among others.
  - Tax claims that do not fall within any of the categories of taxes set forth in § 507(a)(2), (3), or (8) will be treated the same as general unsecured claims and are subject to discharge.

Postpetition Sale

- First, the sale is subject to court approval pursuant to § 363 and/or § 1129 of the Bankruptcy Code.
  - Under § 363, the sale must be within the debtor's reasonable business judgment and must meet certain requirements such as: (1) a sufficient business reason for the sale; (2) the sale is in the best interest of the estate; and (3) sufficient notice of the sale. Walter v. Sunwest Bank (In re Walter), 83 B.R. 14, 19-20 (B.A.P. 9th Cir. 1988)
  - A sale pursuant to a plan of reorganization or liquidation must comply with all of the plan confirmation requirements enumerated in § 1129.
  - As a practical matter, the value of avoiding bankruptcy court scrutiny by conducting a sale prior to filing bankruptcy may outweigh any tax benefit that could be derived from an asset sale during the bankruptcy proceeding.
- Administrative tax claims
  - If the debtor sells assets during bankruptcy, the taxes incurred in connection with such sale will be afforded administrative tax priority under § 507(a)(2), which priority is the highest among all claims against the debtor, including priority prepetition tax claims (except in the case of an individual debtor, in which domestic support obligation claims have first priority).

- In a Chapter 11 case, administrative tax claims, similar to priority tax claims, must receive cash payments equal to the allowed amount of such claims on the effective date of the plan. § 1129(a)(9).
- In a Chapter 7 case, taxes incurred in connection with a sale after the debtor files bankruptcy are administrative claims and are thus not subject to discharge under § 727.
- § 507(a)(3) – Taxes incurred after the filing of an involuntary petition but before the entry of an order for relief (the "gap period") are afforded the next level of priority.
    - While it is unlikely that there will be a sale of part or all of the debtor's assets during this period, if the debtor continues to operate, it will incur tax liabilities during the "gap period" that will receive priority over prepetition taxes.
- Non-Recourse Debt v. Recourse Debt – Sale/Exchange Income or COD Income
    - Non-Recourse Debt – COD income is not realized when an asset that secures non-recourse debt is disposed/sold via sale, foreclosure, deed-in-lieu of foreclosure, abandonment, etc. Rather, the non-recourse debt is included the amount realized (that is, sales proceeds). Tufts v. CIR, 461 U.S. 300 (1983); 26 C.F.R. 1.1001-2(c). It does not matter that the fair market value is equal to or less than the amount of the debt.
        - However, if the debtor retains the asset and the creditor reduces non-recourse debt, COD income will be realized Gershkowitz v. CIR, 88 T.C. 984 (1987); Rev. Rul. 91-31.
    - Recourse Debt - COD income may be realized when an asset that is security for recourse debt is disposed/sold. If cancelled recourse debt is more than the fair market value (or, sales price) of the asset, the difference is treated as COD income. 26 U.S.C. § 1001(a).
        - If the debtor retains the asset and the creditor reduces recourse debt, COD income will be realized.

Is a Valuable Tax Status Property of the Estate? – A Close Look at Majestic Star.

In re Majestic Star Casino, LLC, 716 F.3d 736 (3d Cir. 2013)

Issue: Whether a valuable tax status, such as a S-Corp or QSub status, constitutes property of the bankruptcy estate the revocation of which can be voided: (1) as an avoidable postpetition transfer pursuant to §§ 549 and 550; and (2) a violation of the automatic stay of § 362?

Background: In 2009, Majestic and other affiliated debtors (collectively, the "Debtors") filed Chapter 11 bankruptcies. Neither Barden Development, Inc. ("BDI"), an S-Corp and Majestic's parent, nor was its sole shareholder, Barden, a debtor. Because Majestic was wholly owned by an S-Corp parent, prior to the petition date, a subsidiary debtor (which was an operating casino) was a QSub for tax purposes, which caused the subsidiary to be a disregarded entity for tax purposes. After the petition date, BDI revoked its S-Corp status which resulted in BDI and Majestic becoming taxable C-Corps and terminating the subsidiary's disregarded-entity status.

The Debtors' reduction of liabilities through their bankruptcy restructuring resulted in approximately $170 million of COD income. The revocation of BDI's S-Corp status resulted in Majestic's COD income staying at Majestic's corporate entity level rather than passing through to BDI and Barden. As such, Majestic would have to recognize the COD income and reduce its valuable tax attributes accordingly. As for the subsidiary (the former QSub), the revocation by BDI resulted in the subsidiary and the other Debtors having to recognize income for tax purposes during the bankruptcy cases.

The Debtors commenced an action before the bankruptcy court to avoid the shareholder's revocation of BDI's S-corp status arguing the S-corp. election was property of the estate. The bankruptcy court agreed with the Debtors, and ordered the IRS, BDI and Barden to take all actions necessary to restore the QSub status. An appeal was taken directly to the Third Circuit.

Debtor's Argument: Prior to Majestic Star, a line of case law developed providing an expanded definition of property for purposes of bankruptcy to include favorable tax attributes. For example, in Official Committee of Unsecured Creditors v. PSS Steamship Co. (In re Prudential Lines, Inc.), 928 F.2d 565 (2d Cir. 1991), the Second Circuit prohibited the debtor's parent company from taking a worthless stock deduction because it would have eliminated the value of the debtor's NOLs for future use. In In re Trans-Lines West, Inc., 203 B.R. 653 (Bankr. E.D. Tenn. 1996), relying on Prudential Lines, the bankruptcy court held that S-Corp status was property of the bankruptcy estate. Trans-Lines thus provided that a corporation's prepetition revocation of its S-Corp status could constitute a voidable fraudulent transfer.

The Third Circuit's Decision: Contrary to the Prudential Lines and Trans-Lines, the Third Circuit held that the subsidiary's QSub status was not property of the bankruptcy estate. The court found that BDI's S-Corp status for tax purposes was not property of the Debtors' estates and, therefore, the subsidiary's QSub status was not property of the estate. The court distinguished between NOLs, which have a quantifiable value to the estate, from the S-Corp status, the value of which is dependent upon the amount and timing of future earnings and which can be terminated at any time at the whim of the shareholders or the IRS. The court concluded

that "a tax classification [such as QSub status] over which a debtor has no control and that is not alienable or assignable is not a 'legal or equitable interest[ ] of the debtor in property.'"

Accordingly, the Third Circuit held that the QSub status did not constitute property of the estate and therefore was not subject to avoidance as a postpetition transfer and is not void by virtue of the automatic stay.

Tax Issues in Employment Settlements in Bankruptcy[1]

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I. Settlement Authority

A. While employees are often represented by independent counsel, likely class action counsel, or under collective bargaining, in the absence of collective bargaining or class counsel, statutory committees are often instrumental in negotiating and settling the interests of employee constituencies.

B. Section 1114 of title 11 of the United States Code, 11 U.S.C. § 101, *et seq*. (the "Bankruptcy Code") "was enacted to protect the retirees of chapter 11 debtors." *Gen. DataComm Indus., Inc. v. Arcara (In re Gen. DataComm Indus., Inc.),* 407 F3d 616, 620 (3d Cir. 2005) (quoting 7 *Collier on Bankruptcy* ¶ 1114.02[1] (Alan N. Resnick & Henry J. Sommers eds., 15th ed. 2002)).

C. Section 1114 requires a debtor to continue paying "retire benefits" under certain circumstances after a bankruptcy filing. Retiree benefits are defined as "payment to any entity or person for the purpose of providing or reimbursing payments for retired employees, their spouses and dependents, for medical, surgical or hospital care, or benefits in the event of sickness, accident, disability or death under any plan, fund or program (through the purchase of insurance or otherwise) maintained or established in whole or in part by the debtor prior to filing a petition commencing a case under this title." 11 U.S.C. § 1114(a).

D. Pursuant to § 1114, "notwithstanding any other provision of this title, the debtor… shall timely pay and shall not modify any retiree benefits, except" upon court order or agreement with the retirees' authorized representative. 11 U.S.C. § 1114(e). Section 1114 was enacted, along with its counterpart § 1129(a)(13), as the primary substantive components of the Retiree Benefits Protection Act of 1988 ("RBBPA"), Pub. L. 100-334, June 16, 1998, 102 Stat. 610 (codified as amended at 11 U.S.C. §§ 1114, 1129(a)(13); *see In re Visteon Corp.*, 612 F.3d 210 (3d Cir. 2010).

E. Section 1113 contains procedures governing any proposed rejection of a collective

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[1] Materials prepared by Rafael Zahralddin special thanks to Cameron Fee, Esq. and Alice Barone of Elliott Greenleaf for the editing and assisting.

bargaining agreement with a union in a chapter 11 case. Section 1113 sets forth a detailed process that a debtor must follow to obtain bankruptcy court approval of rejection of a collective bargaining agreement and prohibits unilateral modification of the agreement prior to obtaining bankruptcy court approval. If a debtor fails to reject a collective bargaining agreement it may result in assumption and duty to cure defaults, including funding pension trusts, and failing to cure will give rise to an administrative expense claim. *Adventure Res., Inc. v. Holland*, 137 F.3d 786 (4th Cir. 1998).

F. A statutory committee appointed to negotiate on behalf of employees under § 1103 and acting on behalf of employees including in matters related to the settlement of the constituencies' disputes with the debtors or other parties in interest is acting squarely within the powers prescribed by § 1109(b) and § 1103(c)(5).

G. A statutory Committee has standing to appear or initiate actions under § 1109(b), which provides that a committee has the right to appear and be heard on any issue arising in a chapter 11 case. *See* 11 U.S.C. § 1109(b); *Unsecured Creditors' Comm. v. Marepcon Fin. Corp. (In re Bumper Sales, Inc.)*, 907 F. 2d 1430 (4th Cir. 1990).

H. There is an argument that once an agreement is reached between the debtors and an 1102 committee, the agreements reached with the debtors are binding. Resolving issues surrounding how a settlement will be distributed, for example, comports with the a committee's powers under § 1103(c)(1). Analysis of the tax and eligibility impact on government benefits, such as Social Security and Medicare, concerning how a settlement is structured, is also within the powers to investigate "any other matter relevant to the case" under § 1103(c)(3) and to perform services in the interest of the committee constituency under § 1103(c)(5).

I. There is an argument that, although the determinations of the unsecured creditors' committee about a proposed reorganization plan are influential, committees are not vested with the power to bind their constituent creditors, and the individual unsecured creditors themselves must eventually cast a vote accepting or rejecting the plan. *See In re Donlevy's Inc.*, 111 B.R. 1, 2 (Bankr. D. Mass. 1990).

J. One possible solution is to use FRCP 23(b)(2) FRBP 7023(b)(2) authorizing the settlement and binding all members of the settlement class. Under a Rule 23(b)(2) class action notice is authorized but not required. *See Crawford v. Honig*, 37 F.3d 485, 487 n.2 (9th Cir. 1995) (stating that Fed. R. Civ. P. 23(b)(2) "does not require notice or permit members to opt out, although a court in its discretion" may provide otherwise).

II. Fiduciary Duty to Examine Tax and Benefits Issues

A. It is well established that members of an official committee have a fiduciary duties to the *constituency* of creditors the committee was appointed to represent. *In re Refco Inc.*, 336 B.R. 187, 195 (Bankr. S.D.N.Y. 2006) ("It is well recognized that . . . the members of an official committee owe a fiduciary duty to their constituents – in the case of an official creditors committee, to all of the debtor's unsecured creditors.")

B. A committee must take care to obtain maximum value for its constituents and act in good faith toward its constituency. *See, e.g., Motorola v. Official Comm. of Unsecured Creditors* (*In re Iridium Operating, LLC*), 478 F.3d 452, 466 (2d Cir. 2007) (remanding to determine whether plan provision met fiduciary duty to maximize recovery of estate's assets); *In re Gen. Homes Corp.*, 181 B.R. 870, 882 (Bankr. S.D. Tex. 1994) ("The fiduciary duty that exists between the members of the Unsecured Creditors Committee and the other unsecured creditors includes the duty to act in good faith and to insure to the greatest extent possible its actions are based on 'accurate and correct' information.").

C. This means, among other things, that a committee must engage professionals when appropriate to ensure competent representation of constituents' interests, and preserve the confidentiality of sensitive information obtained in the course of representation. *See In re United Steel Workers v. Lampl Mesta Mach. Co.*, 67 B.R. 151, 163–64 (Bankr. W.D. Pa. 1986). The committee is required to be reasonably informed and particularly considerate when acting on behalf of its constituents. Before a committee makes a decision, it must be reasonably informed of all material information and remain up-to-date with respect to the chapter 11 proceedings. If a committee is not sufficiently informed, it risks jeopardizing the financial returns to its constituency as a whole. **Of special note, is the need to prevent dissipation of funds when dealing with disabled employees with catastrophic injuries, whether mass tort through personal injury. Life care plans cannot allow for adverse tax consequences which would deplete or harm access to living expenses and medical care.**

III. Taxation of Settlements and Federal Benefit Eligibility

Employees who are creditors in bankruptcies often have significant economic concerns and their difficulties can be compounded if they are retired or disabled and relying on benefits from a now insolvent company. Many recent bankruptcies have legacy costs of employees as a central element or issue. The manner in which a settlement is structured could displace or prevent access to benefits in the first year after settlement is reached and then disproportionally impact in future years both the employee and the government authority supervising government programs designed to assist people in need.

A. Taxation of Settlements

1. Prior to the day that health benefits are terminated, for example, some of the benefits provided to the employees, such as life insurance, AD & D insurance, and medical expense reimbursement benefits, are non-taxable to the recipients. Other benefits, such as disability income continuation payments and benefits under a long term investment plan are potentially taxable. Under most settlements related to benefits, the value of these benefits for each employee would be actuarially determined, and the payments under the settlement could be factored (sold) for settlement proceeds that would be allocated to the employee in accordance with their respective actuarially-determined benefits.

2. Notwithstanding that some of the pre-termination date benefits were or would have been non-taxable or taxable over a number of taxable years as received, an employee's

allocated share of a settlement amount, if paid to her or him in a lump sum, would be fully taxable in the year it is received in cash. Under the cash method of accounting for tax purposes, which applies to most individual taxpayers, income is reportable in the year in which it is actually or *constructively* received by the taxpayer. Therefore, if an employee receives her or his allocated portion of the settlement as a lump sum payment, it will be fully taxable in the year received and subject to income tax withholding.[2]

3. A voluntary employees' beneficiary association ("VEBA") is a form of trust fund permitted under United States federal tax law, whose sole purpose must be to provide employee benefits. A VEBA is established to provide "life, sick, accident or other benefits" to its members, their dependents or their designated beneficiaries. This structure has been used in many insolvencies to continue or administer benefits for legacy employees. In order for the VEBA to be qualified as a tax-exempt entity under I.R.C. § 501(c)(9), an application for exemption will need to be filed with and approved by the IRS. The principal benefit to the VEBA of tax-exempt status is that earnings of the VEBA pending distribution to (or for the benefit of) the employees/trust beneficiaries will not be subject to federal income tax.

B. Constructive Receipt

1. Under the constructive receipt rule, an LTD Employee with an unrestricted option to receive all cash will be treated as having received all cash in the year a final order is entered, even if he or she actually receives part or all of the settlement payments on a deferred basis, that is, spread over more than one year. As described briefly above, under the cash method of accounting for federal income tax purposes an item of income becomes subject to tax in the year it is "actually or constructively received by the taxpayer." *Childs v. Commissioner*, 103 T.C. 634, 654 (1994), *aff'd*, 89 F.3d 856 (11th Cir. 1996).

2. If the constructive receipt rule applies to an employee who receives part or all of her allocated share of amount of a settlement amount on a deferred basis, this could have significantly detrimental tax effects on the employee. Income would be taxable under the constructive receipt rule prior to the year the cash (perhaps even cash necessary to pay the tax) is received, and the employee's entitlement to certain exclusions and benefits that are dependent in part on a taxpayer's annual income, such as the exclusion of Social Security benefits from taxation and the premium costs of and eligibility for certain benefits under Medicare and Medicaid, could be adversely affected.

3. Each individual employee in a constituency cannot simply be given an option to receive her or his share of the settlement amount all in cash; all in a form that would achieve deferral; or any combination of the two. Such a simple, unrestricted choice would result in the employee being treated as constructively receiving the full amount in cash. Accordingly, class counsel or a committee and its professionals should consider possible ways in which an employee's benefits might be paid so as not to become subject the

[2] The IRS could also take the position that the lump sum should be treated as "wages" and thus subject to the Federal Insurance Contributions Act ("FICA") tax, and other employment taxes.

amounts to tax in one taxable year.

C. Economic Benefit Doctrine

1. Even if an employee receives her or his payments on a deferred basis, and does not have the unrestricted option to receive all cash in a lump sum, the employee may nonetheless be taxed currently under the "economic benefit doctrine." A taxpayer may be held to have a current economic benefit if a separate fund or trust of assets is unconditionally and irrevocably established exclusively for their benefit. In *Sproull v. Commissioner*, 16 T.C. 244 (1951), *aff'd per curium*, 194 F.2d 541 (6th Cir. 1952) (for tax purposes, present value of future earnings included in year that right to income stream is first obtained).

D. Potential Exceptions to the Constructive Receipt Rule and the Economic Benefit Doctrine

1. Funds paid into and held by a "qualified settlement fund" as described and governed by I.R.C. § 468B and the Treasury Regulations thereunder, are not currently taxed to the beneficiaries of the fund under either the constructive receipt rule or the economic benefit doctrine. However, it is not clear that I.R.C. § 468B would apply by its specific terms to qualified settlement funds. I.R.C. § 468B(d)(2)(D) provides that in order to be subject to these favorable rules, the fund must be, among other requirements, "established for the principal purposed of resolving and satisfying present and future claims against the … [payor into the fund] (or any related person or formerly related person) arising out of personal injury, death or property damage. . . ." *C.f. Will v. General Dynamics Corp.*, No. 06-698-GPM, 2010 BL 318430, 49 EBC 2032 (E.D. Ill. Aug. 9, 2010) (involving the settlement of claims that an I.R.C. § 401(k) plan provider had breached its fiduciary obligations under ERISA by paying excessive fees for the plan's investments; court found that the fund established to resolve the claims would be a "qualified settlement fund" within the meaning of the Treasury Regulations under I.R.C. § 468B).[3]

E. Annuity Tax Issues

1. Annuity payments are subject to state and federal income tax reporting and withholding, but allow for tax deferral of the settlement proceeds as the proceeds are only taxed in the year in which they are paid. However, despite the fact that an annuity might be approved by the IRS as a means of deferring taxes, it is likely that the IRS would view the settlement proceeds as "nonqualified deferred compensation," subject to Federal

[3] Notwithstanding this finding, it is by no means clear that the IRS would consider itself bound when a fund fails to meet the requirements of I.R.C. § 468B, and by no means clear that the beneficiaries of the fund will not be treated as taxable currently when the fund is established, particularly under economic benefit doctrine. As much as a committee may desire to achieve the tax result provided by I.R.C. § 468B for the employees who wish to avoid current taxation, *Will v. General Dynamics Corp.* seems a slender reed to rely upon.

Insurance Contributions Act ("FICA") taxes. *See United States v. McKean*, 33 Fed. Cl. 535 (1995); Rev. Rul. 75-241, 1975-1 C.B. 316 (writing that the employee had complete control of the disposition of the amounts paid and there was no contractual or legal obligation imposed on the employer to verify that the amounts paid were used by the employee to purchase health and welfare benefits, the amounts paid were held to be wages subject to income and FICA tax withholding).

2. In *In re Nortel Networks Corp.*,[4] Case No. 09-10138, pending in the United Sates Bank of the District of Delaware, the Long Term Disability Plan Participants Committee ("LTD Committee"), which was established as a 1102 Committee, discussed the FICA tax issue with the IRS regarding its proposed settlement with the debtors. The IRS informally advised the LTD Committee that it would likely view the use of an annuity as simply spreading the lump sum (concededly FICA wages) over several years and thus treat the payments as "nonqualified deferred compensation" subject to FICA taxes in full in 2013, the year when the settlement order was entered. The IRS has indicated that its position would be based on I.R.C. § 3121(v)(2), which provides that "nonqualified deferred compensation", as broadly defined in the Code, is treated as FICA wages when the right to the deferred payments arises, in the IRS's way of thinking, when the LTD Employee receives rights to an annuity contract. FICA liability can be as much as 5% of a total settlement. So while the use of an annuity may potentially prevent the application of the doctrines of constructive receipt and economic benefit to the funds attributable to a settlement funds not associated with medical benefits such as income continuation, it has FICA implications that must be considered.

3. In contrast to the negative view it has of the annuity, the IRS has informally indicated that it could consider the establishment of a new income continuation plan, in the form of a disability plan, which would serve as replacement for the income continuation portion of the LTD benefits which were terminated by the Nortel debtors. The new disability plan, which is not sponsored by the debtors and instead is governed by a proposed VEBA ("VEBA LTD Plan"), and administrated by a third party administrator, if approved by the IRS as a disability plan, would not be subject to FICA and could be used to defer taxes and administer payments on the schedule as proposed in the Motion. The VEBA Trust, the successor to the LTD Committee is seeking a PLR from the IRS regarding the tax implications of the VEBA, HRA, and VEBA LTD Plan as new benefit plans instead of the VEBA, annuity, and HRA.

F. Effects on Federal (and State[5]) Benefits

1. For example, disabled employees (usually considered retirees) are likely currently covered by Medicare Parts A and B because of their disability. For health care costs not covered by Medicare Parts A and B, including pharmaceutical costs, disabled employees would likely, under most benefits packages, receive health benefits (medical and

[4] Jointly administered.

[5] Many of the federal programs have counterparts administered by the states and there is Medicare counseling available through the State Health Insurance Assistance Program ("SHIP") in most states.

dental/vision/hearing) under a debtor's health plans. When a debtor terminates benefits, the disabled employees will have to pay for the cost of Medicare Part B premiums,[6] as well as the cost of insurance to cover the costs of health care, including pharmaceutical costs, not covered by Medicare Parts A and B.

2. The Social Security Administration determines the cost of Medicare Part B and Part D premiums based on an individual's modified adjusted gross income as reported on the federal income tax return.

3. There is a standard premium amount for those with income below a certain threshold Those with a modified adjusted gross income higher than the threshold will pay higher premiums for both Medicare Parts B and D based on an income scale (see below). The additional premium amount for Parts B and D is called the "income-related monthly adjustment amount."[7] *See generally* 20 C.F.R. § 418, Subpart B (Medicare Part B Income-Related Monthly Adjustment Amount).

4. Based on the foregoing, settlement amounts received by a disabled employee in any given year may increase his/her income into income brackets triggering an increase in Medicare Parts B and D premiums.

5. The amount of Social Security benefits received by the disabled employee will not change as a result of settlement amounts received.[8] However, settlement amounts received by the disabled employees may cause Social Security benefits to be taxable. The amount of Social Security benefits one may receive are revised annually.[9]

6. Whether, and how much, Social Security benefits are taxable may be affected by the settlement received by the disabled employee.

7. Finally, a settlement may preclude eligibility for needs based programs including, but not limited to, Medicaid, Supplemental Security Income ("SSI"),[10] the "Medicare Savings

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[6] Under the terms of the a typical long term disability plan, disabled employees would be to enroll in Medicare Parts A and B after receiving Social Security Disability Income for two years. A company would likely credit the disabled employees with the Part B premium. As of the termination of the LTD Plans, the Part B premium previously paid for by the company will be borne by the former employees. Part A is "free" for those who worked 40 qualifying quarters.

[7] 20 C.F.R. § 418.1101 *et seq*., 42 U.S.C. § 1395r, and 42 CFR Parts 407 and 408.

[8] However, workers' compensation and other public disability benefits may reduce Social Security benefits. *See* 20 C.F.R. § 404.408.

[9] *See* Social Security and Equivalent Railroad Retirement Benefits, U.S. Dept. of Treasury, Internal Revenue Service, available at http://www.irs.gov/pub/irs-pdf/p915.pdf (last visited September 16, 2014) and What You Need to Know When You Get Social Security Disability Benefits Social Security Administration, available at http://www.ssa.gov/pubs/10153.pdf (last visited September 16, 2014).

[10] The purpose of the SSI program is to assure a minimum level of income for those age 65 and over or who are blind or disabled and do not have sufficient income and resources to maintain a standard of living at the federal poverty level. *See* 20 C.F.R. § 416.

Program,"[11] which is administered through Medicaid to provide assistance with Medicare premiums, and the "Extra Help" or "Low Income Subsidy" ("LIS") programs for those with limited resources and income that provide assistance with the payment of premiums, annual deductibles, and prescription co-payments related to the Medicare prescription drug plans.[12]

8. Some individuals within the constituency may be eligible for pension benefits which will be likely administered by the Pension Benefit Guarantee Corporation ("PBGC"). Counsel for the PBGC has advised pension-eligible employees who have made inquiries to the PBGC that the PBGC may view the receipt of settlement funds as precluding the commencement of Pension Benefits before age 65, thus precluding the eligibility for "Early Retirement" or "Disability Retirement," if applicable. According to the PBGC, assessments of the effect of the Settlement Agreement on pension-eligible employees can often not be made until a court enters a final order approving a settlement and, thereafter, on individualized assessments of the settlement apportionment received by pension-eligible employees.

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[11] *See* Medicare Savings Programs, Medicare.gov http://www.medicare.gov/your-medicare-costs/help-paying-costs/medicare-savings-program/medicare-savings-programs.html (last visited September 16, 2014).

[12] This is not meant as an exhaustive list of needs based programs. Eligibility for programs such as Medical Assistance for Workers with Disabilities and the Supplemental Nutrition Assistance Program (SNAP), formerly known as food stamps, as well as needs based programs administered through the States may also be affected by settlement amounts received.