EFFECTIVE DATE

(01-27-2023)

PURPOSE

(1) This transmits revised IRM 5.17.10, Legal Reference Guide for Revenue Officers, Chapter 11 Bankruptcy (Reorganization).

MATERIAL CHANGES

(1) IRM 5.17.10, Chapter 11 Bankruptcy (Reorganization), has been updated to provide clarity and expansion of existing material. The following table shows substantive changes within this IRM revision.

Number	IRM	Change
1	IRM 5.17.10.1(3)	Rephrased the sentence for clarity.
2	IRM 5.17.10.1(4)	Changed program owner to Collection Policy, Insolvency.
3	IRM 5.17.10.1.3	Removed paragraph (2) on Taxpayer Bill of Rights
4	IRM 5.17.10.1.7	Added paragraph (3) on Taxpayer Bill of Rights references.
5	IRM 5.17.10.3(4)	Updated SCI contact site.
6	IRM 5.17.10.5.3(4)	Rearranged paragraph to meet 508 compliance.
7	IRM 5.17.10.7.2	Removed information on pre-BAPCPA cases. Updated the small business debtor debt limits.
8	IRM 5.17.10.7.2.1(1)	Added SBRA debt limitations.
9	IRM 5.17.10.7.2.1(2)(b)	Clarified trustee roles in a SBRA case.
10	IRM 5.17.10.9.4.3(1)	Removed note on pre-BAPCPA cases.
11	IRM 5.17.10.10	Removed information on pre-BAPCPA cases.
12	IRM 5.17.10.10.1	Removed information on pre-BAPCPA cases. Rearranged section to meet 508 compliance.
13	IRM 5.17.10.10.1.3	Updated to reflect changes in how ESRP liabilities are handled.

Number	IRM	Change
	IRM 5.17.10.10.3	Changed title from **Collection SOL** to **CSED**.
14	Throughout	Remove breaks to meet 508 compliance.
15	Throughout	Removed outdated BAPCPA information.
16	Throughout	Changed **Service** to **IRS.**
17	Throughout	Changed **lien** to **NFTL**
18	Throughout	Editorial changes were made throughout this section to provide greater clarity, eliminate duplicate material, and update, correct, or add citations

EFFECT ON OTHER DOCUMENTS

This revision supersedes IRM 5.17.10, Chapter 11 Bankruptcy (Reorganization), dated January 3, 2020. T .

AUDIENCE

Small Business / Self-Employed Revenue Officers and Specialty Collection Insolvency

Kareem Williams, Director
Collection Policy

5.17.10
Chapter 11 Bankruptcy (Reorganization)

Table of Contents

5.17.10.1
(01-27-2023)
Program Scope and Objectives

(1) **Purpose.** This IRM section discusses the basic purpose and procedural workings of a Chapter 11 bankruptcy case. It explains the ways in which a Chapter 11 bankruptcy case is different from a bankruptcy case brought under other chapters of the United States Bankruptcy Code (USBC). It highlights issues of particular significance to the IRS in Chapter 11 bankruptcy cases.

(2) **Audience.** This section is used primarily by Small Business / Self Employed (SB/SE) Revenue Officers (ROs) and management. Specialty Collection Insolvency (SCI) caseworkers and management in the Centralized Insolvency Operation (CIO) and Field Insolvency (FI) may also refer to this section. Caseworkers in functions other than SB/SE may refer to this section when dealing with a taxpayer that has filed bankruptcy.

(3) **Policy Owner.** The Director of Collection Policy is responsible for issuing policy for the Insolvency program.

(4) **Program Owner.** The program owner is Collection Policy, Insolvency an organization within Small Business Self Employed (SB/SE) division.

(5) **Primary Stakeholders.** The primary stakeholders are Field Collection, Civil Enforcement Advice and Support Operations (CEASO), Chief Counsel and Specialty Collection Insolvency.

(6) **Program Goals.** The goal is to provide fundamental knowledge and procedural guidance for working Chapters 11 bankruptcy cases. Following the guidance in this IRM will ensure cases are worked in accordance with bankruptcy laws and regulations.

5.17.10.1.1
(01-03-2020)
Background

(1) **Reorganization.** Chapter 11 bankruptcy is a rehabilitative case that gives the debtor a *breathing period* from the petition filing to plan confirmation, during which time business affairs can be reorganized and a plan devised for the orderly payment of creditors. Chapter 11 is frequently referred to as the *reorganization bankruptcy*. However, a debtor may choose to liquidate instead of reorganizing in a Chapter 11 bankruptcy. After a plan is confirmed, the creditors must monitor their receipt of payments under the terms of the plan. A Chapter 11 bankruptcy case can last for several years. For further information on Chapter 11 bankruptcies, see IRM 5.9.8, Processing Chapter 11 Bankruptcy Cases.

5.17.10.1.2
(01-03-2020)
Authority

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

5.17.10.1.3
(01-27-2023)
Responsibilities

(1) IRM 5.17.1.8, Revenue Officer's Role, provides the duties and responsibilities of a Revenue Officer.

5.17.10.1.4
(01-03-2020)
Program Management and Review

(1) IRM 1.4.50.8.2.1, Management Information Systems (MIS) Reports, contains guidance on Field Collection reports.

(2) National quality reviews and consistency reviews are conducted on a consistent basis. See IRM 1.4.50.12.1, EQRS, and IRM 1.4.50.12.2, NQRS, for more information.

(3) Operational and Program reviews are conducted on a yearly basis. See IRM 1.4.50.13.2, Operational Reviews, and IRM 1.4.50.13.5, Program Reviews, for more information.

5.17.10.1.5
(01-03-2020)
Program Controls

(1) Managers are required to follow program management procedures and controls addressed in IRM 1.4.50.11, Group Controls, and IRM 1.4.50.12, Quality.

(2) Caseworkers and managers use the Integrated Collection System (ICS) for case management, assignment, and documentation.

5.17.10.1.6
(01-27-2023)
Terms and Acronyms

(1) A glossary of terms used in this section can be found in Exhibit 5.17.8-1, Glossary of Common Bankruptcy Terms.

(2) Acceptable acronyms and abbreviations can be found in the ReferenceNet Acronym Database, which may be viewed at: *http://rnet.web.irs.gov/Resources/Acronymdb.aspx*.

(3) The following table lists acronyms and definitions used specifically in this IRM section.

Acronym	Definition
AIS	Automated Insolvency System
APOC	Automated Proof of Claim
BAPCPA	Bankruptcy Abuse Prevention and Consumer Protection Act of 2005
CIO	Centralized Insolvency Operation
ERISA	Employee Retirement Income Security Act
ESRP	Employer Shared Responsibility Payment
FI	Field Insolvency
J&C	Judgment and Commitment
NFTL	Notice of Federal Tax Lien
SBRA	Small Business Reorganization Act
SCI	Specialty Collection - Insolvency
SRP	Shared Responsibility Payment
TEGE	Tax Exempt/Government Entities
USBC	United States Bankruptcy Code
USC	United States Code
UST	United States Trustee

5.17.10.1.7
(01-27-2023)
Related Resources

(1) Procedural guidance on Insolvencies can be found throughout IRM 5.9, Bankruptcy and Other Insolvencies.

(2) The United States Bankruptcy Code and Rules, including Local Bankruptcy Court Rules.

(3) Pub 5170, Taxpayer Bill of Rights and Taxpayer Bill of Rights page *https://www.irs.gov/taxpayer-bill-of-rights*

5.17.10.2
(01-03-2020)
Purpose of Chapter 11 Bankruptcy

(1) Chapter 11 is the primary reorganization chapter of the United States Bankruptcy Code (USBC) for non-individual debtors.

(2) Chapter 11 allows the financially distressed debtor a "breathing period" to reorganize their affairs while under the protection of the bankruptcy court. The debtor may continue to operate their business while negotiating debts and ownership interests with creditors as they restructure their business operations. The individual debtor with no business interests may also negotiate their personal debts with creditors during this period. In either case, the debtor's main goal is usually to formulate a plan to repay creditors while continuing to operate. However, the debtor may choose to liquidate instead of reorganizing in the Chapter 11. Unless the court appoints a trustee, reorganization or liquidation is usually accomplished by the debtor, referred to as the debtor in possession or DIP. See IRM 5.17.10.4, The Debtor in Possession (DIP), for additional information. The reorganization or liquidation takes place with court approval through confirmation of a bankruptcy plan.

   a. Ideally, a Chapter 11 plan of reorganization is preferred to liquidation by most of the debtors' creditors to satisfy pre-bankruptcy debts. That is because creditors will likely receive a greater distribution from plan payments over time than through liquidation of the debtor's business. When businesses are liquidated, creditors may only receive "pennies on the dollar" of the pre-bankruptcy debt owed them.
   b. In addition, a Chapter 11 plan often gives the debtors' creditors some form of new ownership interest in the debtor.

(3) Individuals are eligible to file Chapter 11. See IRM 5.17.10.11, Individuals in Chapter 11, for further discussion on individuals in Chapter 11.

   a. An individual who wishes to pay creditors over time through a plan and not liquidate in a Chapter 7 case generally files a Chapter 13 case rather than a Chapter 11 case.
   b. Most individuals find Chapter 13 proceedings to be more advantageous than a Chapter 11 proceeding. First, Chapter 13 proceedings are less expensive for the individual debtor. Then, more debts (including tax debts) may be discharged for individuals in Chapter 13 without payment than for individuals in Chapter 11.
   c. Changes to the USBC made by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) have made Chapter 11 cases filed by individuals similar to Chapter 13 cases. As in Chapter 13, individual Chapter 11 debtors must now complete payments under the plan before they can receive a discharge when reorganizing (11 USC 1141(d)(5)(A).
   d. Similar to Chapter 13, an individual debtor may also receive a "hardship discharge" at any time after confirmation of the plan when modification of the plan is not practicable and plan payments cannot be completed (11 USC 1141(d)(5)(B)).

(4) A large percentage of Chapter 11 debtors fail to reorganize successfully. Failure may be either before or after confirming a plan.

a. In these circumstances, the business debtor may liquidate assets in Chapter 11 instead of through trustee liquidation in Chapter 7. Assets of the business may be sold for a higher price when the business is sold as a going concern. No administrative fees of the Chapter 7 trustee are incurred. As a result, liquidation in Chapter 11 may result in a greater return for creditors than a liquidation in Chapter 7.
b. Similar to business debtors, individual debtors may also liquidate assets in Chapter 11 with a greater return to creditors than a Chapter 7 liquidation.

(5) Chapter 11 bankruptcy cases require more monitoring and evaluation than bankruptcies filed under other chapters of the USBC because:

- The debtor may incur new significant debts while they are in the process of deciding whether to sell its assets or whether to reorganize.
- The debtor may dissipate its assets trying to keep the business going.
- The Chapter 11 bankruptcy case can last for several years.

5.17.10.3
(01-27-2023)
Initiating a Chapter 11 Case

(1) A Chapter 11 case is commenced with the filing of a bankruptcy petition. The Chapter 11 may be a voluntary bankruptcy petition filed by the debtor. The Chapter 11 may be an involuntary bankruptcy petition filed by creditors.

Note: An involuntary case may not be filed against a farmer or a non-commercial corporation.

(2) A debtor need not be insolvent or even unable to pay its debts when due, in order to file a voluntary Chapter 11 case. A debtor's inability to pay debts as they become due may be relevant if a debtor contests an involuntary petition filed against it. (11 USC 303(h))

(3) The IRS should be served with copies of all voluntary Chapter 11 petitions. It does not matter if the IRS is listed on the debtor's schedules as a creditor or not. Additionally, Bankruptcy Rule 2002(f) provides for all creditors, which would include the IRS, to be noticed of:

- Any cases converted to Chapter 11 from another chapter of bankruptcy;
- Orders for relief entered for any Chapter 11 cases;
- The time allowed for filing claims pursuant to Rule 3002; and,
- Entry of an order confirming a Chapter 11 plan.

Bankruptcy Rule 2002(j)(3) provides that copies of these Chapter 11 notices are mailed to the IRS at the address set out in the register maintained by the clerk of the bankruptcy court under Rule 5003(e). The address for the IRS on the court's register is the CIO in Philadelphia. (See IRM 5.9.5.2.2, Mailing Matrix, and IRM 5.9.11.2, Insolvency Mail, for additional information.) For the duration of the Chapter 11 case, the IRS should continue to be served with bankruptcy pleadings, orders, and other documents in the Chapter 11 case that are required to be served on "all creditors" whether or not the IRS has filed a claim in the case. (Bankruptcy Rule 2002(a), (b), (f), and (j)(3))

(4) Chapter 11 bankruptcy cases are worked by Insolvency caseworkers in Field Insolvency (FI) within Specialty Collection Insolvency. When becoming aware that a taxpayer has filed Chapter 11, promptly contact Insolvency to notify

them of the bankruptcy filing. Notification may be made by faxing Form 4442, Inquiry Referral, to the Centralized Insolvency Operation (CIO) within Specialty Collection Insolvency, or by telephonic contact with CIO. The CIO caseworker will ensure assignment of the case to FI. CIO can also provide the name and telephone number of the FI caseworker assigned the bankruptcy case.

Note: CIO phone and fax numbers for internal IRS communications are found on SERP at *SERP - Insolvency (Bankruptcy) Tools - Who/Where (irs.gov)*.

(5) When an Advisor or Revenue Officer learns that a taxpayer assessed a restitution assessment has filed Chapter 11, they should contact the CIO to inform them that the bankruptcy involves a restitution assessment. Contact should be made with the CIO even if the IRS has otherwise received notice of the bankruptcy case.

5.17.10.3.1
(01-03-2020)
Documents Required When Chapter 11 Case Is Initiated

(1) Within 14 days, a Chapter 11 debtor must file a number of standardized schedules, statements, and other specified documents with the court. It does not matter if the debtor filed a voluntary or involuntary case. (Bankruptcy Rule 1007(b) and (c)) These documents filed in Chapter 11 cases tend to be more voluminous than documents filed in other bankruptcy chapters.

(2) In a voluntary case involving an individual Chapter 11 debtor, the debtor must file the following documents with the petition:

a. A certificate indicating that the debtor has received credit counseling during the 180-day period before the filing of the petition, as required by 11 USC 109(h);
b. The debt repayment plan developed during that credit counseling, if any; or
c. A court determination excusing the debtor from the required credit counseling.

Note: See Bankruptcy Rule 1007(b)(3) and (c). Failure to file these documents can be grounds for dismissing the debtor's bankruptcy case.

(3) A list of creditors is filed with the Chapter 11 case. The list may assist the United States Trustee in appointing members of the Unsecured Creditors' Committee for the debtor's case.

- When a voluntary petition is filed, the Chapter 11 debtor files a mailing matrix indicating the names and addresses of each of its creditors. Additionally, a list of creditors holding the 20 largest unsecured claims against the debtor is filed. (Bankruptcy Rule 1007(a)(1) and (d))
- In an involuntary case, the debtor must file the mailing matrix within 7 days after the entry of the order for relief. Within two days after the entry of the order for relief, the list of creditors holding the 20 largest unsecured claims must be filed. (Bankruptcy Rule 1007(a)(2) and (d))

(4) The debtor's required schedules and Statement of Financial Affairs (SOFA) may help the IRS:

a. Identify some of its potential tax claims against the debtor;
b. Identify some of the IRS's setoff rights; and,
c. Compare debtor's security interest schedules with the IRS records to ensure the schedules contain all applicable Notices of Federal Tax Lien (NFTLs) and evaluate the federal tax lien position.

5.17.10.3.2
(01-27-2023)
Prepackaged Chapter 11 Cases

(1) Many large Chapter 11 debtors have been able to file their proposed disclosure statements and plans with their bankruptcy petition or immediately after filing bankruptcy. These debtors may have negotiated restructuring of their debts and ownership with their major secured and general unsecured creditors and stockholders before filing Chapter 11. In doing so, they hope to obtain enough votes for confirmation of their Chapter 11 plan before going into bankruptcy. They hope to shorten the time they are under the supervision of the bankruptcy court. This type of Chapter 11 case is called a "prepackaged" Chapter 11. The "prepackaged" Chapter 11 case is more commonly filed in Delaware and the Southern District of New York. Prepackaged cases are filed pursuant to 11 USC 1126(b) and Bankruptcy Rule 3018(b).

(2) In a prepackaged Chapter 11 case, the debtor may seek consideration of its proposed disclosure statement and confirmation of its proposed plan at the same time. The debtor may request hearings to approve the disclosure statement and to confirm the proposed plan within a short time frame. Sometimes, the hearings may be held as little as 45 days after the filing of the petition. Prepackaged cases can be a problem for the IRS. Many times, the IRS is one of the debtor's few major creditors that are not aware of the debtor's plans to file a prepackaged bankruptcy. In the prepackaged case, confirmation of the proposed plan may occur before the bar date for the IRS and other governmental units to file a proof of claim. The IRS may have an ongoing audit of the debtor and may not have sufficient time to evaluate and file claims prior to confirmation. If the debtor filed a prepackaged case, and IRS was not a part of the plan negotiations, FI must take additional actions during the initial case review. This includes securing a copy of the proposed plan, reviewing it expeditiously, and consulting with Area Counsel if the plan is not adequate (IRM 5.9.8.4.2(12), Pre-packaged Chapter 11).

(3) Prepackaged plans that propose a sale or transfer of substantially all of the debtors' assets are a particular problem for the IRS. The principal purpose of these transactions may be tax avoidance. (See In re Scott Cable Communications. Inc., 227 B.R.596 (Bankr. D. Conn. 1998)) For additional information on Chapter 11 cases involving major tax liabilities or significant issues for the IRS, refer to:

- The Chief Counsel Directives Manual (CCDM) at IRM 34.3.1.3, Significant Bankruptcy Case Program
- IRM 5.9.4.15.3, Significant Bankruptcy Case Referrals
- IRM 5.9.8.4.2(15), Significant Cases and Referrals to Area Counsel

5.17.10.4
(01-03-2020)
The Debtor in Possession (DIP)

(1) In a Chapter 11 case, the debtor usually operates as a "debtor in possession" (DIP) unless the court appoints a trustee to replace the DIP. The individual debtor may be a DIP, managing their personal affairs or operating the individual's sole proprietorship. The non-individual debtor may be a DIP. The DIP in the non-individual case may be the debtor's management team, members of a LLC, partners in a partnership, etc. The DIP usually remains in control of the business and assets of the debtor. (USC 1101, 1104(a), 1107 and 1108))

(2) A DIP is given the rights and powers of a bankruptcy trustee (11 USC 1107(a)).

5.17.10.4.1
(01-03-2020)
Appointing a Chapter 11 Trustee

(1) Prior to confirmation of a Chapter 11 plan, any interested party in the case may request the appointment of a trustee to replace the DIP. The party in interest may be an individual creditor, the Creditors' Committee, or the United States Trustee (UST). The trustee appointed by the bankruptcy court manages the debtor's business and assets as well as administers the estate. (11 USC 1104(a) and Bankruptcy Rule 2007.1(a))

(2) The appointment of a trustee is rare because the change in management can disrupt the debtor's business. A trustee is only appointed for "cause." "Cause" includes fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by its current management either before or after the commencement of the case. (11 USC 1104(a) and (e))

Exception: If a debtor files a Chapter 11 case under the Small Business Reorganization Act (SBRA), a trustee will be automatically appointed to oversee the case. See IRM 5.17.10.7.2.1, Small Business Reorganization Act and 11 USC 1183.

(3) If the bankruptcy court does not order the appointment of a Chapter 11 trustee, an examiner may be appointed. Prior to confirmation of the plan, an interested party or the United States Trustee (UST) may make a motion for appointment of an examiner. An examiner may be appointed to investigate the debtor for various matters. The matters may include allegations of fraud, dishonesty, misconduct, or irregularity in managing the debtor's affairs. The allegations may be against current or former management of the debtor. (11 USC 1104(c) and Bankruptcy Rule 2007.1(a) and (c)) The examiner does not replace the DIP in the management of the debtor's affairs. The examiner does not deprive the DIP of their rights to propose a plan for the debtor.

(4) The court may determine that appointing a trustee or examiner serves the interests of creditors and the estate better than dismissal or conversion. In these instances, a trustee or examiner may be appointed instead of dismissing or converting the case, even though grounds exist for dismissal or conversion. (11 USC 1112(b)(1))

5.17.10.4.2
(08-01-2010)
Chapter 11 Committees

(1) The USBC provides a mechanism that allows unsecured creditors to oversee the debtors' operations and voice their concerns throughout the Chapter 11 case. The UST appoints a committee of unsecured creditors as soon as practicable after:

- A voluntary Chapter 11 petition is filed; or,
- An involuntary petition is filed by creditors and an order for relief is entered in the case.

(2) The powers of the Unsecured Creditors' Committee in a Chapter 11 case are very significant and extensive (11 USC 1102 and 1103). The views of the Unsecured Creditors' Committee are important to the bankruptcy court.

(3) The Unsecured Creditors' Committee ordinarily consists of the creditors who are willing to serve on the committee and that hold the seven largest unsecured claims against the debtor (11 USC 1102(b)).

(4) 11 USC 1103 authorizes the Unsecured Creditor's Committee to employ various parties to represent or perform services for the committee. These parties may include:

- One or more attorneys,
- Accountants, or
- Other agents.

(5) The IRS and most governmental units are not eligible to serve as members of the Unsecured Creditors' Committee (11 USC 101(41)).

5.17.10.5
(12-05-2016)
Early Events in a Chapter 11 Case

(1) In a typical Chapter 11 case, the debtor seeks bankruptcy court approval for a number of "first day" orders. This commonly includes an order allowing the debtor to continue using its cash collateral. The court will grant the debtor authority to continue using cash collateral for operations when creditors with security interests are adequately protected. A secured creditor is adequately protected when the creditor will not lose the value of its security interest while the debtor continues to operate. The security interest may be cash, accounts receivable, inventory, etc.

a. The IRS should become involved in a case as soon as possible when pre-petition NFTLs were filed. The NFTLs may secure attachment to cash collateral being used by the debtor. The IRS needs to ensure that its security interests are protected as the debtor continues to operate.
b. A debtor may request a "turnover" order early in a Chapter 11 case (11 USC 542). The order may require the IRS to release a levy served pre-petition. The order may require the IRS to surrender property seized before the petition date. Coordination with Area Counsel is required when the IRS seeks to hold levy funds or seized property in anticipation of an adequate protection order.

(2) The IRS and other creditors may take advantage of their opportunity to question a debtor at the First Meeting of Creditors under 11 USC 341.

5.17.10.5.1
(01-27-2023)
Mandatory Referrals to Counsel and TEGE

(1) When non-Insolvency IRS employees become aware that a taxpayer meeting "significant case" criteria has filed Chapter 11, they must notify Field Insolvency (FI). FI will refer cases meeting Significant Bankruptcy Case Program criteria to the appropriate Area Counsel office. It does not matter if the debtor has no outstanding pre-petition liability. Significant cases include cases in which the debtor has major tax liabilities, cases with significant audit issues, or there are other significant or sensitive issues for the IRS. (See IRM 5.9.4.15.3, Significant Bankruptcy Case Referrals, for a list of all circumstances that make a case meet "significant case" criteria. Also, see IRM 5.9.8.4.2(16), Significant Cases and Referrals to Area Counsel, for additional information.)

(2) FI is required to notify TEGE when a taxpayer files Chapter 11 and the case meets "significant case" criteria. FI also notifies TEGE when a nationally known company files Chapter 11. (See IRM 5.9.8.4.2(12), Notice to TEGE, for additional information.)

5.17.10.5.2
(01-27-2023)
Limitations on a Debtor's Right to Use Cash Collateral

(1) In a Chapter 11 case, the DIP typically wants to continue running the business until it can be reorganized or sold as a going concern.

a. The DIP may automatically continue routine ("ordinary course") use, sale, or lease of most of its pre-petition property (other than cash collateral) without court approval. (11 USC 363(c)) However, the DIP must obtain court approval to use, sale, or lease property of the estate other than in the ordinary course of business. (11 USC 363(b))

b. Prior to the use of the cash collateral, the DIP must obtain consent to use cash collateral. Consent must be obtained from each creditor with an interest in such cash collateral or with bankruptcy court authorization. It does not matter if the proposed use of cash collateral is routine or otherwise. The court evaluates the DIP's request for authorization to use cash collateral. The court may only authorize the use of cash collateral when the creditors interest in the property is adequately protected against loss. (11 USC 363(a), (c)(2), and (e))
c. The DIP's unauthorized use of cash collateral which causes substantial harm to one or more creditors is grounds for dismissal or conversion of the bankruptcy case. (11 USC 1112(b)(4)(D))

(2) The DIP often negotiates agreed first day orders for the use of its cash collateral with its significant pre-petition lenders before entering bankruptcy. However, the DIP may neglect to consider the secured position of the IRS in cash collateral after the IRS has filed NFTLs against the debtor.

a. When the IRS is a secured creditor because an NFTL was filed pre-petition, the IRS must frequently take initiative to protect its interest in the case. The IRS may need to point out to both the DIP and the court the DIPs use of cash collateral where the IRS' interest is secured by an NFTL.
b. The Automated Proof of Claim (APOC) program used by FI identifies Chapter 11 cases with an NFTL on file. Caseworkers in FI are required to determine if adequate protection is a consideration in a Chapter 11 case within ten calendar days of APOC identifying the NFTL. When necessary, FI contacts debtor's counsel to negotiate adequate protection for the IRS as a condition for the debtor's continued use of cash collateral. For additional information, see IRM 5.9.8.4.1(4), Aspects of the Review Requiring Action within Ten Calendar Days, IRM 5.9.14.2.7(1)(b), Time Frame Requirements; and, IRM 5.9.14.2.9(5) , Period Flag Conditions and Resolutions, Secured Period Flag.

(3) 11 USC 361 discusses adequate protection in a bankruptcy case. The most common form of adequate protection to the IRS for a DIP's use of its cash collateral usually includes periodic cash payments on the IRS's secured claim. Payments to the IRS generally begin immediately on the secured claim. The IRS may also provided a replacement NFTL on property acquired by the DIP after the petition date. See the discussion on adequate protection in IRM 5.17.10.5.3, below, and in IRM 5.9.8.6, Adequate Protection. In all instances, referrals to Area Counsel for litigating adequate protection are subject to the #

5.17.10.5.3
(01-27-2023)
Turnover and Adequate Protection

(1) A voluntary Chapter 11 filing by a debtor is often preceded by the IRS levying upon or seizing certain assets of the debtor. After filing bankruptcy, the debtor may immediately file a motion with the bankruptcy court for a release of the levy. The debtor may also file a motion for an order for the IRS to turn over the seized property to the debtor. (11 USC 542)

(2) In U.S. v. Whiting Pools, Inc., 462 U.S. 198 (1983), the Supreme Court affirmed a debtor's right under 11 USC 542 to the return of tangible property seized by the IRS, subject to the requirement of 11 USC 363(e) that the debtor provide the IRS with adequate protection for the use of property to be turned over in which the IRS has a secured interest.

(3) The protection that is adequate to a creditor for turnover of property to the debtor depends on the factual circumstances of the case. This includes the type of property involved, tangible or intangible property. See IRM 5.9.8.7, Pre-petition Levies, and IRM 5.9.8.8, Cash Collateral/Property Depreciation of the Estate, for additional information.

(4) The IRS seldom seeks periodic cash payments as adequate protection for the turnover of seized real property as real property does not usually depreciate rapidly. However, the IRS does want the DIP to be required to maintain adequate insurance coverage for its buildings and other improvements to real property. On the other hand, the value of personal property may dissipate rapidly after turnover to the DIP by the IRS. This includes levied upon cash, accounts receivable, and inventory. In these situations, the IRS is interested in securing an adequate protection agreement that provides for:

a. The IRS retaining a portion of the cash received;
b. The IRS receiving future periodic payments (with post-petition interest) before a plan is devised or confirmed;
c. The IRS being provided replacement NFTLs on after-acquired assets; such as, the DIP's inventory and accounts receivable
d. Providing for the DIP's post-petition compliance with its continuing federal tax obligations; and,
e. Default provisions should the debtor not comply with the terms of the adequate protection order.

5.17.10.5.4
(01-27-2023)
The First Meeting of Creditors

(1) The Section 341 Meeting in a Chapter 11 case is an opportunity for creditors (including the IRS) to question the debtor while under oath. Questions may cover a wide range of relevant matters concerning the debtor's past behavior, its present finances, and the likely future of the bankruptcy case. (11 USC 341 and Bankruptcy Rule 2003) See IRM 5.9.8.4.2(2), 341 Meeting, for a list of examples of items that may be discussed at the Section 341 Meeting.

(2) Generally, FI caseworkers attend the Section 341 Meeting in Chapter 11 cases when issues are present that require a discussion at the meeting. In some areas, SCI may ask selected ROs for their assistance and expertise in listening to and questioning the debtor's witnesses at the Section 341 Meeting.

(3) It may be advantageous for an RO or other non-Insolvency employee to question the debtor at the 341 Meeting. For example, an RO may question the debtor about issues regarding unpaid trust fund taxes to complete a TFRP investigation.

(4) Insolvency may ask Area Counsel to arrange a more thorough examination of the debtor or other witnesses under Bankruptcy Rule 2004. However, this is usually only requested when the debtor provides inadequate information or documentation for the IRS purposes at the Section 341 Meeting.

5.17.10.6
(01-27-2023)
Claim Bar Dates in Chapter 11

(1) The time for filing claims in a Chapter 11 case is not determined by statute or rule. The bankruptcy court fixes (by an order) the date by which creditors are to file their pre-petition claims in a Chapter 11 case. (Bankruptcy Rule 3003(c)(3))

(2) The claim of a governmental unit is considered timely if the claim is filed before 180 days after the order for relief to file a timely claim for a pre-petition period. The order for relief is the petition date in a voluntary case. (See 11

USC 502(b)(9) for additional information.) However, in "prepackaged cases," it may be in the best interest of the IRS to file a claim as soon as possible. Confirmation of the plan may occur before the 180-day period for filing a proof of claim expires in a "prepackaged case."

(3) When certain debts are listed on the debtor's bankruptcy schedules, a proof of claim is deemed as filed on behalf of the IRS. Debts are not deemed as filed on behalf of the IRS when they are scheduled as disputed, contingent, or unliquidated in the Chapter 11 case. (11 USC 1111(a) and Bankruptcy Rule 3003(b)(1) and (c)(2))

(4) The Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) amended 11 USC 503(b)(1)(D) for cases commencing on or after October 17, 2005. The IRS and other governmental tax creditors are no longer required to file requests for payment of administrative expense taxes and related penalties. However, it is the policy of the IRS to file a request for payment of post-petition administrative liabilities. FI files Form 6338-A(C), Request for Payment of Internal Revenue Taxes, to put the debtor and creditors on notice of the post-petition liability and of the amount due. See IRM 5.9.8.13(8), Request for Payment, for additional information.

(5) Individuals who file Chapter 11 bankruptcy cases are required to report income of the bankruptcy estate on Form 1041, U.S. Income Tax Return for Estates and Trusts. These post-petition income tax liabilities are claimable on Form 6338-A(C). FI files Form 6338-A(C) to request payment of unpaid post-petition Form 1041 liabilities in the Chapter 11 case. See the following subsections in IRM 5.9.8, Processing Chapter 11 Cases, for additional information:

- IRM 5.9.8.14.1, Post-petition Debts - Chapter 11 Individuals
- IRM 5.9.8.14, Internal Revenue Code 1398 Issues
- IRM 5.9.8.19.4.2, Post-Confirmation Tax Liabilities of the Individual Debtor

5.17.10.6.1
(01-27-2023)
Setoffs

(1) In the course of many Chapter 11 cases, the IRS discovers that its pre-petition tax debts are secured even though it did not file an NFTL. The IRS may be secured due to setoff rights held by the IRS against carryback tax refunds for pre-petition years. The IRS may be secured against amounts owed the debtor by other federal agencies. All federal agencies are generally considered one creditor (the United States) for setoff purposes under the USBC. See In re Hal, Inc., 122 F.3d 851 (9th Cir. 1997) and Turner v. SBA, 84 F.3d 1294 (10th Cir. 1996).

(2) Rather than through ordinary refund procedures, Chapter 11 corporate debtors may request carryback tax refunds through tentative carryback procedures. The IRS commonly refers to these as "quickie refund procedures." Be aware of these "quickie refund" requests that may be filed immediately after the Chapter 11 case is filed.

(3) The IRS has the right to offset the quickie refund against federal tax liabilities of the taxpayer. This right of setoff becomes particularly important when the taxpayer is in bankruptcy. The dollar amounts of quickie refunds can be large. Setoff may be the only assured way of collecting liabilities owing from the taxpayer. Difficult mutuality issues are raised, however, when losses from post-petition periods are carried back to pre-petition years. Consult Area Counsel in such cases. See IRM 5.9.8.9, Quickie Refunds, for further discussion.

(4) The automatic stay in 11 USC 362(a)(7) prevents the actual making of a setoff of any pre-petition debt owed the debtor to any claim against the debtor. But, 11 USC 553 nevertheless preserves pre-petition setoff rights in bankruptcy. If a debtor is owed a pre-petition refund that could be credited against a liability owed by the debtor, the IRS should:

a. Freeze the refund until the stay is lifted;
b. Refer the case to Area Counsel to request an order lifting the stay and permitting setoff; and,
c. Setoff the refund once the stay is lifted.

See Citizens Bank of Maryland v. Strumpf, 516 U.S. 16 (1995), in which the court ruled that temporarily freezing a refund while requesting relief from the stay to allow offset did not violate the automatic stay against offsets. The IRS's setoff rights extend to unassessed liabilities identified on a proof of claim (Rev. Rul. 2007-52). However, referrals to Area Counsel to request lifting of the stay to allow setoffs are subject to referral tolerances. The tolerances are adjusted by local Counsel depending on staffing and caseloads. (IRM 5.9.4.5(8),

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Note: The automatic stay does not prohibit setting off pre-petition income tax refunds against pre-petition income tax liabilities. (11 USC 362(b)(26))

(5) When the FDIC has taken over a bank, the bank's parent holding company often files for bankruptcy protection. The FDIC as well as the parent holding company may file a claim for refund if proper procedures are followed. (Treas. Reg. 301.6402-7) The FDIC's claim for refund does not affect the IRS's setoff rights. See IRM 5.9.20.3.1, Federal Deposit Insurance Corporation (FDIC) Receivership Proceedings of Insolvent Financial Institutions, for a discussion of receivership cases where the FDIC is appointed receiver of a financial institution.

(6) Refer to the following subsections in IRM 5.9, Bankruptcy and Other Insolvencies, for more detailed information on setoffs in bankruptcy cases:

- IRM 5.9.4.5, Credits, Refunds and Offsets;
- IRM 5.9.4.5.1, Addressing Credits, Refunds, and Offsets;
- IRM 5.9.4.5.2, Post-Petition Payments and Credits;
- IRM 5.9.4.5.3, Offsets to Other Agencies, and subsections;
- IRM 5.9.4.5.4, Federal Payment Levy Program (FPLP);
- IRM 5.9.4.5.5, Offsets, Payments, and the Individual Shared Responsibility Payment (SRP); and,
- IRM 5.9.13.19.2, Secured Claim.

5.17.10.6.1.1
(01-03-2020)
Setoff and the Individual Shared Responsibility Payment (SRP) MFT 35 and/or MFT 65 Mirror Assessment and/or Employee Shared Responsibility Payment (ESRP) MFT 43 Liabilities

(1) Although the USBC allows setoff of pre-petition income tax refunds to pre-petition income tax liabilities without a lifting of the stay, this does not apply to individual SRP and ESRP liabilities. Offsets are not permitted between pre-petition SRP MFT 35 modules, pre-petition SRP MFT 65 mirror assessment modules (for the debtor spouse), and/or ESRP MFT 43 modules. SRP MFT 35, SRP MFT 65 mirror assessment, and ESRP MFT 43 liabilities are not included in the exception to the automatic stay under 11 USC 362(b)(26), which refers only to income tax liabilities. Therefore, setoffs are **not** permitted between pre-petition SRP MFT 35, SRP MFT 65 mirror assessment, and/or ESRP MFT 43 modules, nor are they permitted between pre-petition income tax MFT 30 modules and SRP MFT 35, SRP MFT 65 mirror assessment, and/or ESRP MFT 43 modules, without a lifting of the stay.

(2) Setoffs between *post-petition* MFT 30 income tax modules or SRP MFT 35 modules, SRP MFT 65 mirror assessment, and/or ESRP 43 modules are permitted, as setoffs of post-petition debts are not prohibited by the USBC. No lifting of the stay is required.

Note: For additional information, see IRM 5.9.4.5.5, Offsets, Payments, and the Individual Shared Responsibility Payment (SRP) and/or IRM 5.9.4.5.6, Offsets and the Employer Shared Responsibility Payment (ESRP).

5.17.10.6.2
(01-27-2023)
Straddle-Year and Split Period Claims in Non-Individual Cases

(1) Chapter 11 non-individual debtors ordinarily continue to operate their businesses after filing for bankruptcy. They seldom file bankruptcy on the first day of a new tax reporting period. Frequently, there are federal tax liabilities owed by Chapter 11 non-individual debtors for taxes arising in the year in which the bankruptcy petition was filed. This may include employment and excise taxes due for the quarter in which the bankruptcy was filed.

a. Employment and some excise taxes are divisible or transactional taxes. Employment taxes are incurred when the wages reported on the employment tax return are paid. However, they are treated as pre-petition liabilities when the wages reported on the employment tax return were earned pre-petition. Excise taxes on fuel reported on Form 720, Quarterly Federal Excise Tax Return, are incurred when the tax (i.e., fuel tax) is collected. For divisible or transactional taxes, the IRS splits the taxes into the pre-petition and the post-petition portion of the tax due. The pre-petition taxes are priority tax debts. The post-petition portion of the tax debts are administrative tax debts. The IRS frequently refers to claims for these liabilities as “straddle period” or “split period” claims. (See IRM 5.9.13.18(2), Pre-petition versus Post-petition Employment Taxes.)

b. Income taxes are incurred on the last day of the income tax year. BAPCPA amended 11 USC 507(a)(8)(A) to clarify that only income taxes for tax years ending on or before the petition date will receive priority treatment in the bankruptcy case. Thus, income taxes that accrue for the non-individual debtor in the year in which the bankruptcy petition was filed are entirely administrative expense taxes. (See IRM 5.17.10.11, Individuals in Chapter 11, for information regarding income taxes in individual Chapter 11 cases.)

Note: BAPCPA amended Section 507(a)(8)(A) to provide that income taxes will be considered pre-petition (priority) claims only when the tax year ended before the bankruptcy petition was filed. This overturned pre-BAPCPA case law that relied on that section to hold that

the petition-year liability should be split into pre-petition and post-petition portions. See In re Pacific-Atlantic Trading Co., 64 F.3d 1292 (9th Cir. 1995).

5.17.10.6.3
(12-05-2016)
Pensions and Penalties

(1) Assessments arising under IRC 4971 for failure to meet minimum funding standards of a pension plan are considered a "tax" in the IRC. However, the Supreme Court has ruled that the liability assessed under IRC 4971 is a penalty. For USBC proof of claim classification purposes, unsecured IRC 4971 liabilities are general unsecured claims. IRC 4971 liabilities may be a secured priority claim when the liability is secured by an NFTL or right of setoff. See United States v. Reorganized CF&I Fabricators of Utah, Inc., 518 U.S. 213 (1996) and IRM 5.9.13.19.3, Unsecured Priority, for additional information.

(2) Chapter 11 debtors may incur post-petition IRC 4971 underfunding liabilities. The IRS may find it appropriate to assert that these liabilities were incurred as part of the actual and necessary costs of preserving the estate. As such, the IRS may argue that the liabilities are entitled to be claimed as an administrative priority claim under 11 USC 503(b)(1)(A). When there are outstanding IRC 4971 liabilities in a case, contact Area Counsel.

5.17.10.6.4
(01-27-2023)
Post-Petition Tax Compliance

(1) The DIP or Chapter 11 trustee is required to file periodic reports and summaries of the operation of the business. The reports include a statement of receipts and disbursements as well as any other information required by the U.S. Trustee (UST) or the court. The reports must be filed with:

a. The bankruptcy court;
b. The UST; and,
c. Any governmental unit charged with the responsibility for collection or determination of any tax arising out of such business.

Hence, the IRS should receive a report of:

a. Payments made to employees;
b. The amount of taxes required to be withheld or paid for and on behalf of employees; and,
c. The place where these amounts are deposited.

(11 USC 704(a)(8); 11 USC 1106(a)(1); and Bankruptcy Rule 2015(a))

(2) Chapter 11 cases require monitoring by Insolvency even if the IRS has not found any pre-petition taxes owed by the debtor. DIPs often become delinquent in paying withholding tax, FICA, and other taxes. This may be taxes incurred while the DIP operates the business after the petition date. It may be personal or estate income taxes incurred in cases filed by individual debtors after the petition date. Large dollar or chronically non-compliant taxpayers may merit manual monitoring by Insolvency. Manual monitoring may include putting the DIP on deposit verification regimes. Monitoring is not limited to business debtors.

(3) 11 USC 1112(b) requires the court to dismiss or convert a case to Chapter 7 on request of a party in interest for various reasons. Once cause is shown, the court must show that the failure to dismiss or convert the case is in the best interest of creditors and the estate. Reasons for dismissal or conversion include but are not limited to:

- Failure to file post-petition tax returns as they become due and no filing extension has been obtained
- Failure to pay post-petition taxes as they become due
- Failure to confirm a plan within the time frames established by the USBC
- Failure to file the periodic reports required by the court
- Failure to comply with an order of the court or pay a fee of the court

The court cannot convert the debtor to Chapter 7 when the debtor is:

a. A farmer;
b. A corporation which is not moneyed, business or commercial; or,
c. An entity not eligible to file Chapter 7.

(4) Corporate Chapter 11 debtors frequently report net operating losses (NOLs) on income taxes. They may report a NOL for their recent pre-petition income tax year. They may report NOLs for their post-petition income year. In either instance, they may carryback these NOLs to earlier income tax years. In doing so, they seek to obtain refunds of the taxes they paid in the earlier tax years.

a. Corporate Chapter 11 debtors often need large cash infusions to keep their businesses operating. Rather than go through ordinary refund procedures, they may request immediate carryback tax refunds from the IRS through tentative carryback (quickie refund) procedures. Usually, the refunds are issued within 45 days of filing a Form 1139, Corporation Application for Tentative Refund. But, the tentative refund should be frozen until the stay can be lifted when the IRS has a right of setoff.
b. The IRS may audit a loss year return and find that a quickie refund was excessive. If the quickie refund was paid to the DIP post-petition, IRS is entitled to file an administrative expense claim for the excess refund amount. (11 USC 503(b)(1)(B)(ii))
c. The IRS is not required to file requests for payment of administrative expenses. However, it is the policy of the IRS to file administrative expense claims to put the debtor and creditors on notice of the liability and amount due.

(5) Corporate Chapter 11 debtors sometimes use a Chapter 11 case to liquidate substantially all of their assets. The liquidation may be through mid-stream asset sales that are approved by the bankruptcy court under 11 USC 363. The debtor may also seek confirmation of a liquidating plan. The liquidating plan may provide for the sale of the debtor's assets to a third party. The liquidating plan may also provide for the transfer of substantially all of the debtor's assets to a Liquidating Trust. In any of these liquidations, the bankruptcy estate may realize substantial capital gains income after considering the debtor's adjusted basis in the property. Income is generated for the bankruptcy estate because the debtor's property was either sold or there was a taxable transfer to a third party. There may be a federal income tax liability for the bankruptcy estate. However, the debtor's other taxable events in the year and available NOL carryovers from prior years are considered in calculating the tax.

5.17.10.7 (12-05-2016) **The Plan Process**

(1) The plan process begins with the debtor filing a plan of reorganization and disclosure statement. The disclosure statement should contain information about:

a. The nature and history of the debtor,
b. The condition of the debtor's books and records, and

c. A discussion of any potential material federal tax consequences of the plan to the debtor, any successor to the debtor, and to any typical "hypothetical investor."

The disclosure statement generally contains a summary of the proposed plan. The disclosure statement should contain sufficient information for creditors to make an informed decision on whether or not to vote for the plan. The bankruptcy court must approve the disclosure statement before the debtor may solicit creditors' votes on the plan. As discussed below, the bankruptcy court may determine that the plan itself provides sufficient information in small business cases.

(2) For purposes of determining how creditors are to be treated under the plan and voting, the USBC requires that a plan group claims into classes. Generally, claims may only be put in the same class if they are similar. Creditors within a class vote together. Claims within a particular class should be treated the same under the plan.

(3) The plan is confirmed when the court determines that it meets USBC confirmation requirements and votes necessary for acceptance of the plan are obtained. A plan can be confirmed through the cram down process over the dissension of classes of creditors. However, at least one class of creditors impaired in the plan must vote to accept the plan (11 USC 1129(a)(10) and 1129(b)). For a definition of an "impaired class", see IRM 5.17.10.9.2, Impairment of Claims in a Chapter 11 Plan, below. The debtor and all creditors are bound by the terms of a confirmed plan (11 USC 1141(a)).

5.17.10.7.1
(01-03-2020)
The Debtor's Control of Plan Development (Exclusivity)

(1) Ordinarily, Chapter 11 debtors enjoy the exclusive right to propose their Chapter 11 plans for the first 120 days after the petition date. The bankruptcy court may extend or reduce the debtor's 120-day exclusivity period "for cause" upon the request of any party in interest. A party in interest party may be the debtor, creditors, or the U.S. Trustee. (11 USC 1121(d)(1)) The court may not extend the debtor's exclusivity period to a date that is more than 18 months after the petition date.

(2) "Small business" Chapter 11 debtors have the exclusive right to file a Chapter 11 plan during the first 180 days following the entry of the order for relief (11 USC 1121(e)(1)).

5.17.10.7.2
(01-27-2023)
Mandatory Small Business Debtor Treatment

(1) Small business treatment is mandatory for all debtors that fall within the small business debtor definition in 11 USC 101(51C) and (51D). Debtors who file a voluntary Chapter 11 petition must state in the petition whether they are a small business debtor (Bankruptcy Rule 1020). The small business provisions are designed to:

- Prevent abuses of the bankruptcy system in small business cases,
- Make small business cases less costly for the small business debtor, and
- Move the small business case more quickly toward confirmation.

(2) A small business debtor is defined as a business debtor whose non-contingent, liquidated debts do not exceed $3,024,725, per the debt adjustment effective on April 1, 2022. The debt total cannot include debts owed to affiliates and insiders. The small business treatment only applies in a case:

- Where the U.S. Trustee has not appointed a committee of unsecured creditors, or
- Where the court has determined that the committee is not sufficiently active and representative to provide effective oversight of the debtor.

(3) The small business debtor has the exclusive right to file a plan during the 180 days after the petition date. Chapter 11 debtors who do not meet small business criteria are only guaranteed a 120-day exclusivity period. (11 USC 1121(b) and (e))

a. However, the small business debtor must file its plan and disclosure statement within 300 days after the petition date (11 USC 1121(e)).
b. The 180-day and 300-day periods may only be extended if the debtor demonstrates that it is more likely than not that the court will confirm a plan within a reasonable period of time. Failure to timely file or confirm a plan or file a disclosure statement is a basis for conversion or dismissal of a Chapter 11 case under 11 USC 1112.
c. In a small business case, the court must confirm a plan that complies with the USBC no later than 45 days after the plan was filed. (11 USC 1129(e))

(4) The IRS employees should be aware that the automatic stay will not apply in a small business case in the following situations:

a. The debtor already has a small business case pending at the time the current petition was filed;
b. The debtor was in a prior small business case that was dismissed for any reason, by a court order, within the two-year period ending on the petition date;
c. The debtor was in a prior small business case in which a plan was confirmed in the two-year period ending on the date of petition; or
d. The debtor is an entity that has acquired substantially all of the assets or business of a small business debtor described in a), b), and c) above. However, the stay will apply if the debtor can demonstrate that it acquired the assets or business of such small business debtor in good faith and not for the purpose of avoiding the application of 11 USC 362(n).

(5) 11 USC 1116 lists a number of duties required of small business debtors. The small business debtor is required to file a copy of the most recent federal tax return with a voluntary petition. In an involuntary case, the debtor must provide a copy of the return within seven days after the entry of the order for relief. Small business debtors must also timely file and pay post-petition taxes. Failure to comply with any of these requirements is a basis for conversion or dismissal of the case. (11 USC 1112(b)(4)(I))

5.17.10.7.2.1
(01-27-2023)
Small Business Reorganization Act

(1) On August 23, 2019, the President signed the Small Business Reorganization Act of 2019 (SBRA). The SBRA went into effect in February 2020. The debt limit for the SBRA was $2,725,625 of non-contingent liquidated secured and unsecured debt, but was temporarily increased to $7,500,000 under the CARES Act from March 27, 2020 to March 27, 2022. On June 21, 2022, the Bankruptcy Threshold and Technical Corrections (BTATC) Act was signed and restored the $7,500,000 limit retroactively for cases commenced on or after March 27, 2020 through June 21, 2024 (two years after the date of enactment of the BTATC Act). The SBRA aims to make small business bankruptcies faster and less expensive by creating Subchapter V of Chapter 11 of

the Bankruptcy Code specific to small businesses. A small business debtor must elect to proceed under Subchapter V of Chapter 11. The SBRA gives small business debtors the ability to maintain their ownership interests. In exchange, they must pay for a period of three to five years pursuant to a court-confirmed plan of reorganization. During the Chapter 11 proceeding, the debtor's management will have the right to continue operating the business, but may be removed for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the company's affairs. Additionally, after the bankruptcy court approves the debtor's plan of reorganization, so long as "the plan does not discriminate unfairly, and is fair and equitable", the debtor will remain in possession of all property of the estate, which includes all of the property owned by the company before it filed for bankruptcy, and any property acquired by the debtor after filing, including earnings received from services.

(2) Some of the major changes include:

a. An appointed trustee will be assigned to each case.
b. The trustee will ensure that the debtor commences making timely payments required by a confirmed plan.
c. The debtor will contribute all of its disposable income for three to five years.
d. There is no unsecured creditor's committee formed.
e. The plan is required to include the history of the debtor, financial analyses and projections, and a breakdown of how the debtor's property and/or future earnings, and income will be transferred to the standing trustee to execute the plan. The debtor does not have to file a separate disclosure statement or solicit votes to confirm a plan.
f. The plan is due 90 days after the case is filed and only the debtor may file the plan.
g. The debtor may elect to pay their administrative expense claims over the term of the plan.
h. All exceptions to discharge in 11 USC 523(a) of the Bankruptcy Code apply to the debtor.

For more information see IRM 5.9.8.5.1, Small Business Reorganization Act.

5.17.10.8
(01-03-2020)
The Disclosure Statement

(1) Chapter 11 requires a debtor to file a disclosure statement along with a proposed plan of reorganization. (Bankruptcy Rule 3016(b))

Exception: If a debtor files a Chapter 11 case under the Small Business Reorganization Act (SBRA), they are not required to file a disclosure statement. See IRM 5.17.10.7.2.1, Small Business Reorganization Act.

(2) The disclosure statement must be provided to all creditors. The bankruptcy court must approve the disclosure statement before the debtor may solicit the creditors' votes for the acceptance or rejection of the proposed plan.

(3) The disclosure statement should provide "adequate information" for creditors and other interested parties to decide if they will vote to accept the plan. (11 USC 1125(a)(1))

(4) During a hearing, the bankruptcy court determines if the disclosure statement contains adequate information and if it should be approved. In determining adequacy, the court is required to consider the cost and benefits of additional

information as well as the complexity of the case (11 USC 1125(a)(1)). Once the disclosure statement is approved, a proposed plan may move to confirmation in a relatively short time frame.

(5) In small business debtor cases, the court may determine that the plan provides adequate information and that a separate disclosure statement is not necessary. The court may also approve a disclosure statement submitted on standard forms. (11 USC 1125(f))

5.17.10.8.1
(01-27-2023)
The Content of a Disclosure Statement

(1) The USBC does not specify all of the information that needs to be included in the disclosure statement. However, it does require the disclosure statement to discuss the potential federal tax consequences of the plan to the debtor, any successor of the debtor, and a "hypothetical investor." (11 USC 1125(a))

(2) Generally, the disclosure statement discusses:

- The recent history of the debtor,
- The reasons why the debtor filed a bankruptcy petition, and
- The measures the debtor has undertaken to reverse financial setbacks.

The disclosure statement should also provide a summary of the plan and the treatment given to the various creditors.

(3) Bankruptcy courts have required that a disclosure statement contain a discussion of the following matters:

a. The debtor's available assets and their value;
b. Claims made against the estate;
c. A liquidation analysis, setting forth the estimated return that creditors would receive if the debtor was in a Chapter 7 case;
d. The future management of the debtor;
e. The risks being taken by creditors and interest holders under the proposed plan; and
f. The existence, likelihood, and possible success of litigation involving the debtor.

Note: The USBC clarifies that the disclosure statement should discuss the federal tax consequences of the plan (11 USC 1125(a)(1)).

(4) A careful review of the proposed disclosure statement may lead Insolvency to conclude that a referral to Area Counsel for assistance is appropriate. The case may or may not meet Significant Case procedures. A referral may be necessary because the disclosure statement does not include adequate information for the IRS to decide if the plan should be accepted. Or, a referral may be necessary because the case meets Significant Bankruptcy Case handling procedures. For instance, the proposed disclosure statement may indicate that the plan will create a Liquidating Trust to pay creditors' claims. The disclosure statement may indicate that the plan will effect a sale of substantially all of the debtor's assets to a third party. Insolvency may conclude that Area Counsel's assistance is required to evaluate the potential tax consequences of the plan. Insolvency may need Counsel's assistance in devising appropriate procedures to protect the IRS interests under the proposed plan. See the following citations for additional information:

- Chief Counsel Directives Manual (CCDM) at IRM 34.3.1.3.5, Disclosure Statement and Plan Review

- IRM 5.9.4.15.3, Significant Bankruptcy Case Referrals
- IRM 5.9.8.17, Disclosure Statements and Plans of Reorganization

5.17.10.8.2 (08-01-2010)
The Disclosure Statement Approval Process

(1) After a plan proponent files a proposed disclosure statement with the bankruptcy court, the court typically enters an order that a hearing will be held. The notice of hearing is given to the debtor, all creditors, and other interested parties. (Bankruptcy Rule 3017(a))

(2) When the disclosure statement notice order is served on the IRS, Insolvency uses the event as an opportunity to:

- Fine tune and amend the amount of any IRS claims;
- Re-evaluate the security for any claims the IRS has filed as secured and amend the characterization of its secured claim (to priority or general unsecured status), if appropriate, and
- Conduct updated post-petition tax compliance reviews for the debtor to see if any further administrative expense claims should be filed.

(3) The general purpose of the disclosure statement approval process is informational. The Government has limited resources for litigating cases in the bankruptcy court. Ultimately, the IRS does not object to a disclosure statement unless it is grossly deficient and the IRS plans on objecting to the proposed plan. However, an objection to a proposed disclosure statement should be considered if it incorrectly describes the IRS's claim as this will affect other creditors.

5.17.10.9 (08-01-2010)
Plans in Chapter 11

(1) The Chapter 11 plan in a particular case is ordinarily a matter for intense negotiations between interested parties. Those parties include the debtor, creditors, and other interested parties (e.g., the debtor's stockholders).

5.17.10.9.1 (01-27-2023)
Classification In Chapter 11 Plans

(1) For the purpose of determining the treatment of creditors in a Chapter 11 plan, the USBC requires "classification" of claims. Classification is based on the nature of the creditor's claims. Most plans group creditors into Class 1, Class 2, etc. (11 USC 1123). Claims or interests may be included in a particular class only if such claims or interests are substantially similar to the others in that class. (11 USC 1122(a))

(2) In practice, each secured claim is commonly placed in its own class or subclass. This is because of:

- A secured creditor's often unique interest in certain property of the debtor's bankruptcy estate;
- The extent and priority of the creditor's NFTL; or,
- The specific mutual debt subject to offset.

(3) Administrative expense claims, gap period claims, and priority tax claims should not be classified by a Chapter 11 plan (USC 1123(a)(1)).

5.17.10.9.2 (01-27-2023)
Impairment of Claims in a Chapter 11 Plan

(1) A Chapter 11 plan must specify any class of claims or interests that is not impaired under the plan (11 USC 1123(a)(2)).

a. A class of claim or interest holders is impaired unless the plan leaves the claim or interest holders' non-bankruptcy legal, equitable, and contractual rights unaltered. (11 USC 1124(1))

b. In general, the IRS's secured claims and general unsecured claims are almost always impaired by a Chapter 11 plan.

(2) Unless a claim or interest holder agrees to less favorable treatment, the plan must provide the same treatment for all parties within a particular class. (11 USC 1123(a)(4)) This is one reason why general unsecured creditors may be placed in several different classes in a complex Chapter 11 case.

(3) When the debtor or other plan proponent disputes the IRS's claim, the dispute should be resolved in a contested proceeding outside the confirmation process. It does not matter if the dispute is to the classification or the amount of the disputed tax claim. It is improper for a plan proponent to dispute the IRS's claim by providing for a different claim amount or classification in the proposed plan. See In re Taylor, 132 F.3d 256 (5th Cir. 1998). When a proposed plan contains language disputing the IRS's claim, such language should not be ignored. A referral to Counsel may be necessary to object to confirmation of the plan.

5.17.10.9.3 (01-03-2020) **Acceptance and Voting on a Chapter 11 Plan**

(1) In Chapter 11 cases, most of a debtor's creditors and interest holders may "vote" to accept or reject a proposed plan. They may also file an objection to the proposed plan. In the USBC, voting on acceptance or rejection of a plan most commonly occurs in Chapter 11 cases.

(2) Classes of creditors and interest holders who are unimpaired are deemed to have accepted the plan (11 USC 1126(f)). A class is deemed not to accept the plan if it receives no property under the plan. A class is deemed not to accept the plan if the class is not entitled to retain property under the plan. (11 USC 1126(g))

(3) An impaired class of creditors is considered to have accepted the plan:

a. Other than an entity whose acceptance or rejection of the plan was not in good faith as determined by the court,
b. The plan is accepted by creditors holding at least two-thirds of the amount of the combined claims, and
c. The plan is accepted by more than one-half in number of the allowed claims of those in the class who vote.

See 11 USC 1126(c) and 1126(e).

(4) Administrative expense claims, gap period claims, and priority tax claims should not be classified by a Chapter 11 plan. Ordinarily, the IRS does not vote with respect to these types of claims. However, Field Insolvency (FI) may refer the case to Area Counsel to request an objection to confirmation of the plan. Referrals to Area Counsel are subject to the tolerances in IRM 5.9.4.15.4, #

(5) However, IRS claims that are secured or general unsecured should be classified. These secured or general unsecured claims are frequently impaired by the plan. The IRS should have an opportunity to vote to accept or reject a plan with respect to these types of claims.

a. 11 USC 1126(a) gives the Secretary of the Treasury authority to accept or reject a Chapter 11 plan on behalf of the United States. This includes Chapter 11 plans where the IRS or other agencies of the United States are creditors in the case.

b. Chief Counsel was given the authority to accept or reject plans where the U.S. is a creditor by General Counsel Order No. 4 (Jan. 19, 2001). See CCDM 30.2.2, Exhibit 30.2.2-6, for additional information. This delegation covers proceedings where the U.S. has only a tax claim. It also covers proceedings in which there are other claims of the U.S., in addition to the claim of the IRS.

(6) When the U.S. has claims for taxes owed to the IRS and there are debts owed to other agencies, the different agencies must coordinate their votes. Disagreements on voting may be referred to the General Counsel of the Treasury Department for resolution. See Chief Counsel Directives Manual (CCDM) at Exhibit 30.2.2-6, General Counsel Order No. 4, Delegation of Authority to Chief Counsel.

5.17.10.9.4
(12-05-2016)
Chapter 11 Plan Confirmation Process

(1) Once eligible creditors have voted on the plan and any modifications are made, the court notices creditors and holds a confirmation hearing (11 USC 1128). The plan is finalized at the confirmation hearing.

(2) Under procedures commonly referred to as “cram down” procedures, a plan can be confirmed over the dissenting vote of an impaired class. However, the plan cannot “discriminate unfairly.” It must be “fair and equitable” with respect to each impaired, dissenting class. (11 USC 1129(b)) Thus, a plan can be “crammed down” over the vote of a dissenting class of creditors as long as one impaired class has voted to accept the plan.

(3) The USBC describes how each classification a creditor may have against a Chapter 11 debtor should be treated for the plan to be confirmed. This includes the claims of the IRS. The IRS should ensure that its various claims are properly treated under a plan. The IRS should object to confirmation of the plan if it fails to provide for such treatment. Failure to object to a plan’s proposed treatment of a claim may be interpreted as consent to that treatment.

(4) The IRS should attempt to ensure the Chapter 11 plan includes specific default provisions. The provisions should specify the manner in which the IRS notifies the debtor of the default. The provisions should clarify the opportunities the IRS affords the debtor to cure the default. The default provisions may clarify that the IRS can exercise administrative collection provisions of the IRC to collect amounts due under the plan.

Note: The default provision language should be modified in individual cases. The discharge in the individual case does not usually occur until completion of all payments under the plan. The plan default language should provide for dismissal or conversion upon plan default.

(5) Once a plan is confirmed, it is binding on the debtor and all interested parties. (11 USC 1141(a))

5.17.10.9.4.1
(08-01-2010)
Objection to a Chapter 11 Plan

(1) *Objecting* to a proposed Chapter 11 plan is a separate process from *voting* to accept or reject a plan. The IRS votes to accept or reject a plan only when:

a. The IRS does not believe confirmation of the plan would be in its best interest and
b. The IRS holds a secured claim, or
c. The IRS holds a general unsecured claim.

The IRS objects to confirmation when the plan does not meet the legal requirements for confirmation under the USBC. For example, the IRS objects to confirmation when it holds unsecured priority tax claims that are not provided for as required under section 11 USC 1129(a)(9). In most cases, the IRS holds all three types of claims. So the IRS votes on the plan and objects to confirmation.

5.17.10.9.4.2
(01-27-2023)
Plan Treatment Of Administrative Expense and Gap Period Claims

(1) Unless a claimant, including the IRS agrees otherwise, all administrative expense claims (11 USC 507(a)(2)) and Gap period claims (11 USC 507(a)(3)) must be fully paid in cash on the "effective date" of the plan. See 11 USC 1129(a)(9)(A) for additional information.

Exception: If a debtor files a Chapter 11 case under the Small Business Reorganization Act (SBRA), the debtor may stretch payment of administrative expense claims out over the term of the plan. See IRM 5.17.10.7.2.1, Small Business Reorganization Act.

a. The IRS should rarely agree to any different treatment. However, see paragraph (4) in this subsection for an example of when the IRS may agree to a different treatment of an administrative or gap period claim.
b. In some cases, the IRS may request that the bankruptcy court order the DIP or trustee to deposit money into a special or "segregated" account prior to confirmation. Generally, these deposits are amounts required to pay administrative and gap period claims. These deposits ensure the monies are available for the payment of these claims on the effective date of the plan. (Bankruptcy Rule 3020(a))

(2) The effective date of the plan is ordinarily defined in the plan.

a. If not, the effective date may be considered to be the date that the plan confirmation order becomes final and non-appealable. Generally, this is the day that plan distributions begin. However, it is no sooner than 14 days after the confirmation order is entered. (Bankruptcy Rule 3020(e))
b. The IRS should object to the plan if the IRS holds a significant administrative expense claim against the debtor's bankruptcy estate and: The proposed plan suggests an effective date for the plan that is too vague or is too long after the plan is confirmed. See In re Potomac Iron Works, Inc., 217 B.R. 170 (Bankr. D. Md. 1997) for additional information.

(3) Administrative expense tax liabilities include penalties and interest on taxes incurred by the bankruptcy estate. See United States v. Friendship College, Inc., 737 F.2d 430 (4th Cir. 1984); In re Preferred Door Company, Inc., 990 F.2d 547 (10th Cir. 1993).

Note: Administrative claims for penalties may not be equitably subordinated (paid less or differently from other administrative expense claims) under 11 USC 510. See United States v. Noland, 517 U.S. 535 (1996).

(4) Plans typically set a bar date for administrative expense requests. The IRS should consider additional actions when the bankruptcy estate is incurring administrative period tax liabilities. This includes requesting an extension of the administrative expense bar date when the bar date falls before or shortly after a tax return is due. The requested bar date should generally be a date that is due a reasonable period after the return due date. In these circumstances:

a. The IRS may agree to payment after the effective date of the plan when an administrative tax return is due after the effective date of the plan.
b. The IRS may want to ensure that the debtor has a cash reserve available to pay potential administrative period taxes. It does not matter if the reorganized debtor or another entity is responsible for paying the administrative period taxes.
c. The IRS may negotiate for plan language that allows pre-confirmation liabilities on unfiled returns to pass through the bankruptcy unaffected by the bar date and the discharge.

Note: Governmental units are not required to file requests for payments of administrative expenses (11 USC 503(b)(1)(D)). However, it is the policy of the IRS to file Form 6338-A(C), Request for Payment of Internal Revenue Taxes, for any assessed and estimated delinquent administrative taxes and returns. The filing of an administrative claim puts the debtor and creditors on notice of the liability and of the amount due. It also assists in the referral of the case to Counsel for dismissal or conversion. It makes the delinquent taxes or returns a matter of "tax administration." The administrative claim helps ensure that the liability will be treated as an allowed administrative claim.

5.17.10.9.4.3
(01-27-2023)
Plan Treatment of Priority Tax Claims in Chapter 11

(1) For a Chapter 11 case to be confirmed, the plan must provide for unsecured priority tax claims (11 USC 507(a)(8)) of the IRS to be paid in full and in cash. Full payment may be on the effective date of the plan or in regular installment payments. If the plan provides for regular installment payments, the unsecured priority claim must be paid within five years of the petition date. Payments must include interest on any unpaid claim amounts after the effective date of the plan. (11 USC 1129(a)(9)(C)) The IRS may consent to other treatment of its priority tax claims by a Chapter 11 plan. Consent may be knowingly or by not objecting to the proposed plan.

(2) Irregular or fluctuating payments may be acceptable to the IRS when the reorganized debtor operates a seasonal business. However, the IRS should object to any Chapter 11 plan that proposes a large balloon payment at the end of a five-year payment period. See IRM 5.9.8.17.1(6), Plan Review **Red Flags**, for a list of factors that FI must consider when reviewing proposed plans.

(3) The interest rate required for installment payments of priority taxes is the IRC 6621 rate for the calendar month the plan is confirmed. Interest is compounded daily pursuant to IRC 6622. (See 11 USC 511.)

5.17.10.9.4.4
(01-27-2023)
Plan Treatment of Secured Tax Claims in Chapter 11

(1) If a confirmed plan or confirmation order fails to address the IRS's secured claim, property of the debtor's estate may no longer be secured by the IRS'sNFTL (11 USC 1141(c)). If the confirmed plan or confirmation order provide for incomplete payment of the IRS's secured claim, property of the estate may no longer be secured. However, the IRS may still be secured by exempt, abandoned, or excluded property.

(2) In addition to security arising from properly filed NFTLs, the IRS claims are often secured by IRS rights to setoff (11 USC 506(a)). Setoff may be against pre-petition federal tax refunds owed to the debtor. Setoff may be against other amounts payable to the debtor from another agency of the United States.

a. Case law is split on whether a creditor loses its setoff rights by failing to provide specifically for preservation of these rights in a confirmed Chapter 11 plan or confirmation order. Compare In re De Laurentis Enter-

tainment Group, Inc., 963 F.2d 1269 (9th Cir. 1992) where there was no loss of setoff rights and In re Deutchman, 192 F.3d 457 (4th Cir. 1999), with In re Continental Airlines, 134 F.3d 536 (3d Cir. 1998). In the latter, the courts ruled setoff rights were lost if not preserved in the plan.

b. When the IRS knows it has setoff rights, the IRS should request that the plan provide for those rights. When the IRS is uncertain if it has setoff rights, the IRS should request that the plan confirm setoff rights. For example, the IRS may be unsure about setoff rights in a prepackaged plan situation. At minimum, the IRS should ensure that the plan does not impair setoff rights of the IRS.

(3) Generally, the USBC requires a reorganized debtor to make deferred cash payments to the IRS when they retain property encumbered by an IRS NFTL after confirmation. Payments must be for at least the allowed amount of the IRS secured claim with interest. Interest is determined pursuant to IRC 6621 as of the calendar month in which the plan is confirmed (11 USC 511). However, 11 USC 1129(b)(2)(A)(i)(II) does not specify the time period by which full payment of a secured tax claim must be completed.

a. 11 USC 1129(a)(9)(D) provides for secured claims to be treated in the same manner as an unsecured priority claim. However, for this treatment, the claim must be a priority claim absent its secured status. (See 11 USC 507(a)(8) to determine if a claim would be a priority claim.) The claim must be paid in regular installments which satisfy the liability within five years of the petition date. Payment must include interest on any unpaid claim amounts after the plan becomes effective. See IRM 5.17.10.9.4.3, Plan Treatment of Priority Tax Claims in Chapter 11, for additional information.

b. For other secured tax claims, the IRS generally opposes long payout periods in a Chapter 11 case. The IRS has defeated some Chapter 11 plans which have proposed long payout periods for the IRS secured claims on grounds of feasibility. See In re Haas, 162 F.3d 1087 (11th Cir. 1998).

(4) The IRS is entitled to be paid post-petition, pre-effective date interest, when the claim of the IRS is over secured (11 USC 506(b)). The IRS commonly refers to this as “administrative period interest.”

Note: The IRS should ensure the plan recognizes the over secured status of the IRS’s claim when administrative period interest is not paid before confirmation. The plan should specifically provide for the full payment of this administrative period interest through the plan.

(5) If property encumbered by a NFTL was not sold, IRS is usually entitled to payment of post-effective date interest on its secured claim under the plan. It does not matter if the secured claim of the IRS is over secured or under secured. The interest is determined pursuant to IRC 6621 as of the month in which the plan is confirmed (11 USC 511).

(6) Some bankruptcy courts allow a Chapter 11 DIP to strip down the value of NFTLs before confirmation. The value of NFTLs may be stripped-down in a proceeding to challenge the secured claim or to determine the extent of a NFTL. Courts have no authority; however, to modify secured claims other than through the plan. 11 USC 1123(b)(5) allows the court to confirm a plan that modifies the rights of holders of secured claims. So, any NFTL stripping in

Chapter 11 must happen through a provision in a confirmed Chapter 11 plan. It should be noted while NFTL stripping is permitted in Chapter 11 cases, it is prohibited in Chapter 7 cases. (Dewsnip v. Timm, 502 U.S. 410 (1992))

(7) A Chapter 11 plan may modify the rights of holders of secured claims against property of the estate. However, individual debtors often have pre-petition property which is:

- Excluded from their bankruptcy estates (such as ERISA qualified pension interests, as in Patterson v. Shumate, 504 U.S. 753 (1992));
- Exempted from their bankruptcy estates (see 11 USC 522, Bankruptcy Rule 4003, and Taylor v. Freeland & Kronz, 503 U.S. 638 (1992)); or
- Abandoned by their bankruptcy estates prior to plan confirmation (11 USC 554(a)-(b)).

(8) A Chapter 11 plan does not generally deal with an individual debtor's non-estate property which is excluded, exempted, or abandoned in the bankruptcy. As such, this property is ordinarily not at risk of being stripped of pre-petition tax NFTLs by the plan. (11 USC 1141(c); In re Isom, 901 F.2d 744 (9th Cir. 1990))

5.17.10.9.4.5
(12-05-2016)
Plan Treatment of General Unsecured Tax Claims in Chapter 11

(1) If the IRS has general unsecured claims, it may vote to reject a plan. IRS may subsequently file an objection to confirmation of a plan based on the plan's proposed treatment of those claims.

(2) In general, a Chapter 11 plan may be confirmed despite a vote to reject the plan by a class of creditors holding impaired, general unsecured claims. However, the plan cannot improperly discriminate between general unsecured claims. The plan must be "fair and equitable" in its treatment of the dissenting class of impaired, general unsecured claims holders to be confirmed by the bankruptcy court under "cram down" procedures. (11 USC 1129(b)(1))

(3) A plan is "fair and equitable" if it provides full payment, with interest, to the holders of claims in a dissenting class of general unsecured creditors. A plan is "fair and equitable" if it provides that the claims or interests of any "junior" claim or interest holder will not receive or retain any property or interest under the plan. (11 USC 1129(b)(2)(B)(ii)) This latter requirement is commonly referred to as the "absolute priority rule."

a. The classes of claims or interests that are "junior" to a class of general unsecured creditors under the USBC include any class of subordinated holders of debt and the debtor's owners. Subordinated bondholders are an example of subordinated holders of debt. Stockholders and partners are examples of the debtor's owners.
b. Thus, a plan may provide for owners of the debtor to retain a part of their ownership interest in the reorganized debtor. These owners may include stockholders or the parent company of the debtor. A dissenting class of general unsecured creditors may object to confirmation of the plan by raising the absolute priority rule.
c. Some courts recognize a "new value exception" to the absolute priority rule. Under this exception, the owners of the debtor may retain some of their ownership interests in the debtor in a cram down situation. However, the owners must be making a new contribution to the reorganized debtor. The new contribution may be money or other capital.

d. The Government has argued that there is no new value exception to the absolute priority rule. The Supreme Court has not addressed whether such an exception to the absolute priority rule should be recognized. See Bank of America NT & SA v. 203 North LaSalle Street Partnership, 526 U.S. 434 (1999); U.S. Bancorp Mortgage Co. v. Bonner Mall Partnership, 513 U.S. 18 (1994); Norwest Bank Worthington v. Ahlers, 485 U.S. 197 (1988).

(4) The IRS may file an objection to confirmation based on the absolute priority argument. Additionally, the IRS may file an objection to confirmation of a Chapter 11 plan in the following situations:

a. The plan improperly classifies the IRS's general unsecured claims apart from other similar, general unsecured claims. Then, the plan provides for better treatment of those other classes of general unsecured claims. For example, the plan provides for earlier payment or closer to full payment of those claims than for the general unsecured claims of the IRS. (11 USC 1129(a)(1) and (3), 1123(a)(1), and 1122(a))
b. The plan attempts to subordinate the IRS penalty claims or other IRS general unsecured claims to the claims of all other classes of general unsecured creditors. This may include taxes for the debtor's underfunding of a pension plan under IRC 4971 which the Supreme Court has ruled is a penalty. See U.S. v. Reorganized CF&I Fabricators of Utah, Inc., 518 U.S. 213 (1996). Also, see IRM 5.17.10.6.3, Pensions and Penalties, for additional information.
c. The plan provides for less total payments on the general unsecured claims of the IRS than the IRS would receive for those claims in a Chapter 7 liquidation. (11 USC 1129(a)(7)(A)(ii)) This is commonly referred to as the "best interests of creditors" test. However, it can be difficult for a creditor to successfully argue that a plan fails the best interests of creditors test regarding its own unsecured general claim.

5.17.10.9.4.6
(12-05-2016)
Plan Treatment of Restitution Assessments

(1) Following the conviction of a defendant for a criminal tax violation or tax-related offense, the court may order the defendant to pay restitution. The requirement that the defendant pay restitution will be contained in a document signed by the judge called a Judgment and Commitment (J&C) Order. In 2010, Congress amended IRC 6201 to provide that the IRS shall assess and collect tax-related restitution in the same manner as if such amount were tax. This change in IRC 6201 applies to restitution in all J&C Orders entered after August 16, 2010.

(2) For purposes of a bankruptcy case, a restitution assessment is classified in the same manner as the tax module to which it relates. Interest on the restitution assessment will have the same classification as the tax assessment. If the failure to pay penalty accrued on the restitution assessment, it will either be secured or general unsecured.

(3) The J&C Order will usually contain a payment schedule specifying the manner in which the restitution amount must be paid. The order will normally specify that restitution payments are to be made to the office of the clerk of the district court in the district in which the J&C Order was entered. The clerk of the court office disburses the payments to the appropriate victims of the criminal action. In the case of the IRS as a victim, the payments are mailed to the Kansas City Submission Processing Center (KCSPC). KCSPC applies the payments to the

restitution assessment. Insolvency caseworkers can inquire about the restitution payment schedule contained in the J&C Order from the appropriate Advisor in the Dallas Advisory Group.

Note: Any reconciliation of the payments must come from the Kansas City Teller Unit which processes such payments.

Initial collection actions on restitution assessments were centralized to the Dallas Advisory Group in 2015. They can be reached via e-mail at *SBSE EEF Dallas Restitution or by researching the SBSE Probation/Restitution page at *http://mysbse.web.irs.gov/collection/aiqorg/contacts/19176.aspx*.

(4) Restitution payments are monitored by the office of the clerk of the court. For this reason, the bankruptcy plan may provide for restitution payments to be made to the office of the clerk of court outside the terms of the plan. If the taxpayer provides for the restitution payments outside the plan, caseworkers should not object to the plan solely for this reason.

(5) If the plan states payment of the restitution assessment will be made according to the J&C Order, the IRS should:

a. Verify that the plan complies with the payment amount scheduled in the J&C Order,
b. Verify that the plan provides for payments to be made according to the schedule in the J&C Order, and
c. Accept plan terms when the plan mirrors the provisions of the J&C Order.

Note: The IRS may still object to the plan for some other reason.

(6) The case should be referred to Counsel for an objection to confirmation when the terms of the plan do not agree with the J&C Order.

(7) In all cases, plans should be reviewed for language providing for a discharge of the restitution assessment. If the plan contains such language, the case should be referred to Counsel for an objection to confirmation of the plan.

5.17.10.9.5
(01-27-2023)
IRS Feasibility Concerns with Chapter 11 Plans

(1) UA Chapter 11 plan should not be confirmed unless it proposes liquidation or further reorganization by the debtor or a successor to the debtor. For example, a plan should not be confirmed if further reorganization will be required by the filing of another bankruptcy case. (11 USC 1129(a)(11)) This is commonly referred to as the “feasibility” test.

(2) Common Chapter 11 feasibility concerns and objections of the IRS have included the following types of plan proposals:

a. Balloon payments of the IRS priority tax claims.
b. The effective date of the plan is an unreasonable period of time after confirmation.
c. The debtor remains in possession and control of the business.
d. The plan does not provide for full payment of the IRS administrative expense or gap period claims on the effective date of the plan.
e. Extended deferred payment periods for the IRS secured claims.

(3) Identifying other IRS feasibility concerns with a proposed Chapter 11 plan may require a closer review of the entire structure of the proposed plan. For example:

a. A proposed Chapter 11 plan provides that the reorganized debtor will pay the entire allowed priority tax claims of the IRS in regular even installments within five years of the petition date. However, a careful review of other provisions of the plan may show that this promise is empty.
b. Parts of the proposed plan provide that the debtor will transfer substantially all of its assets to a new entity. The entity is separate from the reorganized debtor. The debtor does not receive sufficient funds from the transfer of assets to pay the claims of creditors.
c. The debtor's pre-confirmation debts assumed by the new entity are limited to claims of certain categories of creditors. For example, debts assumed represent secured debts and unsecured trade creditor debts. The debts do not include the tax debts to the IRS. There will never be sufficient funds to pay outstanding IRS claims.
d. Payments are not required to many pre-petition creditors after the bankruptcy petition is filed and until confirmation. The IRS has a significant administrative claim for post-petition taxes. The taxpayer could not pay their current taxes as they became due. Is it "feasible" that the debtor can make plan payments on pre-confirmation IRS tax debts and pay their current taxes as they become due?

5.17.10.9.5.1
(08-01-2010)
IRS Tax Avoidance Concerns with Chapter 11 Plans

(1) If a proposed plan otherwise meets confirmation requirements, the USBC should deny confirmation if the principal purpose of the plan is the avoidance of taxes. However, the burden of proof is on the IRS when the IRS objects to confirmation because the principle purpose of the proposed plan is tax avoidance. (See 11 USC 1129(d) for additional information.)

(2) It may be appropriate for the IRS to object to a proposed plan by arguing the purpose of a plan is tax avoidance when:

a. The plan proposes to sell or transfer substantially all of a debtor's assets after confirmation,
b. The sale or transfer is expected to produce a sizeable federal income tax liability for the debtor's bankruptcy estate, and
c. The plan does not provide a mechanism for paying this federal tax liability to the IRS.

See In re Scott Cable Communications, Inc., 227 B.R. 596 (Bankr. D. Conn. 1998).

(3) When a taxpayer does not liquidate through a Chapter 11 plan, and the IRS suspects tax avoidance, the IRS may still have recourse. After plan confirmation, the IRS may be able to review facts and legal implications of transactions through a regular audit pursuant to IRC 269. Pursuant to IRC 269, the IRS takes the position that the IRS may challenge transactions effected by a confirmed plan in a post-confirmation year audit. See Treas. Reg. 1.269-3(e); In re Hartman Material Handling Systems, Inc., 141 B.R. 802 (Bankr. S.D. N.Y. 1992).

5.17.10.9.5.2
(01-27-2023)
Designation of Payments in Chapter 11 Plans

(1) In cases where a corporate debtor owes the IRS significant amounts of pre-petition trust fund taxes, the DIP may seek to designate payment application in the plan. The DIP may designate the IRS application of payments under the Chapter 11 bankruptcy plan first to the corporation's outstanding trust fund taxes. See IRM 5.9.8.11, Trust Fund Considerations in Chapter 11, for additional information.

   a. The DIP may still be controlled by parties whom the IRS has found responsible for the debtor's unpaid trust fund taxes under IRC 6672. The DIP may be controlled by parties the IRS may find responsible for the debtor's unpaid trust fund taxes under IRC 6672 at a later date.
   b. The IRS and the DIP typically have different views regarding attempts to designate payments to trust fund taxes first in the plan. The IRS views the designation as a means of shifting the risk of plan failure before completion from responsible parties to the IRS. The DIP views it as relieving responsible parties from distraction by worry about the IRS collecting the taxes from them before the plan is completed.

(2) In U.S. v. Energy Resources, 495 U.S. 545 (1990), the Supreme Court ruled on payment designation in Chapter 11 bankruptcy plans. The USBC has the authority to approve Chapter 11 plans which designate the IRS application of Chapter 11 plan payments to trust fund taxes first. However, the court must conclude that the designation of payments in this manner is necessary for the success of the reorganization plan.

(3) The courts are split on whether the USBC may designate plan payments first to trust fund when the debtor liquidates instead of reorganizes in the bankruptcy plan. The court allowed no designation in In re Kare Kemical, Inc., 935 F.2d 243 (11th Cir. 1991). The court allowed designation in In re Deer Park, Inc., 10 F.3d 1478 (9th Cir. 1993).

(4) Energy Resources does not provide that bankruptcy courts have the jurisdiction to determine the tax liability of non-debtors. See In re Prescription Home Health Care, Inc., 316 F.3d 542, 549 (5th Cir. 2002). For this reason, the IRS maintains that the USBC lacks the proper authority or jurisdiction:

   a. To enjoin the IRS from investigating a corporate debtor's potentially responsible persons for their liability for the trust fund recovery penalty (TFRP),
   b. To enjoin the IRS from assessing the TFRP against the debtor's responsible persons, and
   c. To prohibit the IRS from attempting to collect the TFRP from the debtor's responsible persons while the debtor's trust fund tax liabilities remain unpaid.

   See the following:

   - In re Prescription Home Health Care, Inc., 316 F.3d 542 (5th Cir. 2002)
   - In re U.S. v. Huckabee Auto Co., 783 F.2d 1546 (11th Cir. 1986)
   - In re LaSalle Rolling Mills, Inc., 832 F.2d 390 (7th Cir. 1987)
   - In re A to Z Welding & Mfg. Co., Inc. v. U.S., 803 F.2d 932 (8th Cir. 1986)
   - In re American Bicycle Assoc., 895 F.2d 1277 (9th Cir. 1990)

(5) Absent statute of limitation period considerations, the general policy of the IRS is to refrain from asserting the TFRP against non-debtor responsible persons in cases where the corporate debtor's confirmed Chapter 11 plan provides for full

payment of trust fund taxes as long as the plan is not in default. See IRM 1.2.1.6.3, Policy Statement 5-14 (Formerly P-5-60), Trust fund Recovery Penalty Assessments.

5.17.10.10
(01-27-2023)
The Effects of Confirmed Chapter 11 Plans

(1) The discharge of taxes upon a confirmed Chapter 11 plan becoming effective depends on a number of factors (whether or not a proof of claim was filed). These factors include:

a. Whether the debtor is an individual or a non-individual (e.g., corporations, partnerships, limited liability companies, etc.),
b. Whether a non-individual debtor is liquidating or reorganizing,
c. Whether a debtor is eligible for discharge, and
d. What the specific terms of the plan provide.

(2) For a debt to be discharged, the debtor must first be eligible to receive a discharge. This is discussed in detail in IRM 5.9.8.18(6), The Chapter 11 Discharge and the Effects of Confirmation, Non-Discharge.

Note: Some debtors may not be eligible for discharge in the current Chapter 11 case because they received a discharge in a prior bankruptcy case. For additional information, see IRM 5.9.5.7.1(5), Discharge Limitations, and IRM 5.9.5-3, Allowable Elapsed Time Between Bankruptcy Filings and Discharges.

In general, 11 USC 1141(d)(3) specifies that a debtor is not eligible to receive a discharge if:

a. The plan provides for liquidation, not reorganization, of the debtor;
b. The debtor does not engage in business after confirmation of the plan; and,
c. The debtor would be denied a discharge in a Chapter 7 case.

(3) The automatic stay goes into effect on the Chapter 11 petition date. In non-individual cases, the automatic stay under 11 USC 362 is generally lifted at confirmation, regardless of petition date. A discharge injunction arises upon confirmation of the plan. The injunction generally continues to prohibit the IRS from collecting a tax debt that is discharged. The injunction also prohibits the IRS from collecting a tax debt that is fully provided for by the plan (unless the plan substantially defaults).

(4) In , individual cases, debtors do not generally receive a discharge until all payments provided for in the plan have been made. In such cases, property of the debtor's bankruptcy estate includes post-petition wages and property (11 USC 1115). Similar to Chapter 13, an individual debtor may be granted a hardship discharge in appropriate circumstances (11 USC 1141(d)(5)).

(5) Under 11 USC 362(c), the automatic stay generally terminates upon the earlier of three events:

- The granting or denial of discharge
- Closure of the case by the USBC
- Dismissal of the case

However, the automatic stay prohibiting acts against property of the estate remains in effect until the property is no longer property of the estate. A Chapter 11 plan typically provides for the revesting of property of the estate in

the debtor or some other entity, but it may not. (11 USC 1141(b))In some individual cases , the automatic stay may terminate after 30 days or may never go into place. The automatic stay may not apply when the small business debtor had a previous case that was dismissed or had a plan that was confirmed within two years of the present case. For additional information, see IRM 5.9.5.7, Serial Filers, subsections, and related exhibits.

(6) IRC 6503(h) provides for suspension of the Collection Statute Expiration Date (CSED) while the IRS is prohibited from taking collection actions due to bankruptcy plus six months. The CSED is generally extended when a confirmed Chapter 11 plan fully provides for a debt and that plan is not in substantial default. Calculation of the CSED suspension in a Chapter 11 case can be complicated. See IRM 5.9.8.9, Collection Statute of Limitations and Chapter 11 Plans, for more detailed guidance.

5.17.10.10.1
(01-27-2023)
The Chapter 11 Discharge

(1) The overwhelming majority of debtors with confirmed and effective Chapter 11 plans are non-individual debtors (e.g., corporations, partnerships, limited liability companies, etc.). The discharge granted a non-individual debtor in a Chapter 11 case is substantially different from the discharge granted an individual debtor. See IRM 5.17.10.11, Individuals in Chapter 11, for a discussion on the Chapter 11 discharge for individual debtors. When the Chapter 11 debtor is an individual, the exceptions to discharge in 11 USC 523(a) apply. The provisions of a confirmed plan cannot affect the dischargeability of tax liabilities of individuals when the liabilities are excepted from discharge under 11 USC 523(a)(1).

Note: Chapter 11 debtors who are individuals are generally not entitled to receive a discharge until after completion of all payments under the plan. (11 USC 1141(d)(5)(A)) However, a debtor who cannot complete all payments under the plan may be entitled to a hardship discharge. To receive a hardship discharge, that individual must have paid to creditors an amount no less than they would have received in a Chapter 7 case (11 USC 1141(d)(5)(B)).

(2) Unless otherwise provided for in the plan or confirmation order, non-individual Chapter 11 debtors generally receive a “super discharge” of all of their pre-confirmation debts (11 USC 1141(d)(1)(A)). However, BAPCPA made tax debts for which the debtor filed a fraudulent return non-dischargeable. BAPCPA also made tax debts non-dischargeable when the debtor willfully attempted to evade payment of the taxes. The fraud and willful evasion exceptions to discharge are applicable to non-individual debtors; as well as, to individual debtors (11 USC 1141(d)(6)(B) and 11 USC 523(a)(1)(C)).

(3) In general, a debtor’s Chapter 11 plan is required to provide for full payment of allowed claims for administrative expense taxes, gap period taxes, priority taxes, and secured taxes. Governmental units are not required to file requests for payments of administrative expenses (11 USC 503(b)(1)(D)). The plan should not require the IRS to file a claim for administrative expense taxes. The plan should not discharge pre-confirmation administrative expense liabilities that are not included on an administrative expense claim, Form 6338-A(C) , Request for Payment of Internal Revenue Taxes.For additional information on plans and administrative expense claims, see IRM 5.9.8.17.1(4)(a), The Plan of Reorganization, Plan Provisions, Administrative Expenses, and IRM 5.9.8.17.1(4)(b), Plan Provisions, Administrative Expenses -Proofs of Claim.

For a discussion of plan requirements in an individual case, see IRM 5.17.10.11, Individuals in Chapter 11.

(4) When the IRS has a secured claim, the IRS should ensure that a plan provides for retention of tax NFTLs on the debtor's property securing the IRS's claim. Otherwise, the NFTLs may be stripped from all of the debtor's property when the plan becomes effective (11 USC 1141(c)).

(5) Prepackaged Chapter 11 plans sometimes provide for most of a debtor's unsecured debts to pass through confirmation with no alteration. This may include some or all of the debtor's potential tax debts. A prepackaged Chapter 11 plan may provide pass-through treatment for many unsecured debts because the debtor is only concerned with restructuring its most significant debts. The debtor may be concerned with restructuring stock ownership in a pre-agreed manner. Involving all of its creditors in the bankruptcy proceeding could slow down approval of its narrowly drawn prepackaged plan. Nevertheless, the IRS should carefully review the proposed terms of a prepackaged plan that provides for pass-through treatment of some of a debtor's unsecured debts. The IRS should be sure that the pass-through terms of the proposed plan actually cover all of the potential claims of the IRS against the debtor.

(6) A non-individual may not receive a discharge because the non-individual may not be eligible for discharge. See IRM 5.9.8.18(6), The Chapter 11 Discharge and the Effects of Confirmation, Non-Discharge. The non-individual debtor is not eligible for discharge if the confirmed plan provides for liquidation of all or substantially all property of the estate and the debtor will not engage in business after the plan is confirmed. The debtor may be denied a discharge in the current Chapter 11 case because they were granted a discharge in a prior bankruptcy case (IRM 5.9.5.7.1(5), Discharge Limitations, and IRM 5.9.5-3, Allowable Elapsed Time Between Bankruptcy Filings and Discharges). They may also be denied a discharge when they have committed fraud or they have not been open and truthful during the bankruptcy (11 USC 1141(d)(3) and (6)).

a. In many liquidating Chapter 11 cases, the Chapter 11 plan may provide for the non-individual debtor's pre-confirmation debts to be discharged. The plan may provide for pre-confirmation debts to be released under the plan.
b. Creditors of the debtor may choose not to object to the discharge or release provided by the plan. They may feel that there is little collection potential for their debts apart from the liquidating Chapter 11 plan.
c. When the plan contains language that discharges debts contrary to the provisions in 11 USC 1141, the IRS refers that case to Area Counsel for an objection to confirmation. The referral is subject to the tolerances in #

(7) Small Business debtors under SBRA have discharge limitations. The court must grant the debtor a discharge after completion of all payments due within the first three years of the plan, or a longer period as the court may fix (not to exceed five years). The discharge relieves the debtor of personal liability for all debts provided under the plan except any debt:

a. on which the payment is due after the first three years of the plan, or such other time as fixed by the court (not to exceed five years); or
b. that is otherwise non-dischargeable

All exceptions to discharge in 11 USC 523(a) of the Bankruptcy Code apply to the small business debtor. This is a different from a typical corporate Chapter 11 case which has limited exceptions to discharge set forth in 11 USC 1141.

5.17.10.10.1.1
(01-03-2020)
Chapter 11 Discharge and Restitution Assessments

(1) Pursuant to 11 USC 523(a)(13) and 1328(a)(3), restitution amounts ordered to be paid in a Judgment and Commitment (J&C) Order are not dischargeable in an individual case filed in any bankruptcy chapter. If restitution is ordered against a non-individual entity, the liability will not be discharged to the extent the Chapter 11 plan provides for payment of the liability. (11 USC 1141(d)(1)(A))

(2) In the individual or non-individual case, the tax loss ordered to be paid as restitution would likely be excepted from discharge under 11 USC 1141(d)(6)(B) or 11 USC 523(a)(1)(C) because it either qualified as:

- A tax for which the debtor made a fraudulent tax return or
- A tax where the debtor willfully attempted in any manner to evade or defeat such tax.

Insolvency refers restitution cases to Area Counsel when taxes may be non-dischargeable because of fraud or willful evasion. See IRM 5.9.17.8.2, The Fraud or Willful Evasion Exception, for additional information. Insolvency refers the case to Area Counsel when a Chapter 11 plan contains language providing for discharge of a non-dischargeable restitution assessment.

(3) For purposes of the discharge, interest is treated in the same manner as the tax to which it relates. Accordingly, interest will not be discharged if the restitution assessment is not discharged. The only penalty that may accrue on a restitution assessment is the failure to pay (FTP) penalty. Generally, the FTP penalty will not be subject to discharge if the failure to pay occurred within three years of the bankruptcy case.

(4) See IRM 5.9.17.8.8, Discharge and Restitution Assessments, for additional information.

5.17.10.10.1.2
(01-03-2020)
Chapter 11 Discharge and the Individual Shared Responsibility Payment (SRP) MFT 35 and/or MFT 65 Liability

(1) The SRP liability is assessed on the Individual Master File (IMF) under Master File Tax (MFT) Account Code 35. It may be mirrored into separate SRP MFT 65 modules for each spouse. The SRP MFT 35 and/or MFT 65 liability is treated as an excise tax under 11 USC 507(a)(8)(E). Since the liability on the SRP MFT 35 and/or MFT 65 module is derived from an individual's federal income tax return, certain information from that return is used in determining dischargeability of the SRP.

(2) The individual SRP liability of the debtor is taken from the debtor's Form 1040 (or appropriate individual income tax return), when the debtor's gross income reportable on Form 1040 meets the threshold requiring the debtor to file Form 1040. As such, post-petition SRP MFT 35 and/or MFT 65 liabilities are treated in the same manner as post-petition Form 1040 liabilities in Chapter 11 cases:

- While collection of the post-petition SRP is not prohibited by the automatic stay, a TC 520 cc 84 will be placed on post-petition MFT 35 and/or MFT 65 modules for the debtor to prevent any inadvertent collection activity against any property of the bankruptcy estate.

- Like income tax reported on the debtor's post-petition Form 1040, the post-petition SRP MFT 35 and/or MFT 65 module is not claimable as an administrative expense on Form 6338-A(C), Request for Payment of Internal Revenue Taxes.
- The post-petition SRP MFT 35 and/or MFT 65 module is non-dischargeable in the individual debtor's Chapter 11 case.

Reminder: Insolvency caseworkers must ensure that the debtor's plan does not discharge the debtor's post-petition/pre-confirmation Form 1040 or MFT 35 and/or MFT 65 liabilities which are not being paid through the bankruptcy plan. Insolvency should refer the case to Counsel to object to confirmation of the proposed plan if it discharges these post-petition liabilities.

(3) In January of 2016, the IRS began mirroring certain joint SRP MFT 35 liabilities as separate SRP MFT 65 liabilities. Mirroring of joint SRP MFT 35 modules into separate MFT 65 modules may take place when:

- Only one spouse on a joint return filed a bankruptcy petition,
- Only one spouse on a joint return submitted an Offer in Compromise (OIC), or
- "Upfront" mirroring is requested by Exam, AUR, or another function with the IRS so the liability of the non-debtor spouse (NDS) can be pursued by the IRS, the NDS can exercise appeal rights, or an agreed deficiency can be assessed against the NDS when the debtor spouse does not agree with the proposed deficiency, etc.

For purposes of proof of claim classification, bankruptcy plans, and determining dischargeability, the SRP MFT 65 liability of the debtor spouse is treated in the same manner that the SRP MFT 35 liability of the debtor spouse would be treated. Similarly, the SRP MFT 65 liability of the NDS is treated in the same manner as the SRP MFT 35 liability of the NDS.

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

(4) Discharge may depend on whether the IRS was properly noticed of the bankruptcy case. See IRM 5.9.17.8.9, Procedures for Processing Bankruptcy Discharges when the IRS Received No Notice or Late Notice in the Asset Case, for determining if taxes may be excepted from discharge due to improper notice.

(5) When an individual debtor completes the Chapter 11 plan and receives a discharge under 11 USC 1141(d)(5)(A), the SRP MFT 35 and/or MFT 65 liability:

- Is non-dischargeable if the Form 1040 was due, with extensions, within the three-years prior to the bankruptcy petition date.
- May be non-dischargeable if the tax on the Form 1040 is non-dischargeable due to willful evasion or fraud. However, the IRS must be able to show that the debtor willfully evaded the SRP. When the SRP may be non-dischargeable for these reasons, concurrence from Area Counsel is required (IRM 5.9.17.8.2(1)).

- May be non-dischargeable if the tax on the Form 1040 was assessed before the return was filed. Discharge can depend on the jurisdiction where the bankruptcy case was filed. Discharge can also depend upon when/if the debtor filed their return for the respective year. See IRM 5.9.17.8.1, Determining Dischargeability of Late Filed Returns in Which a SFR was Prepared, for additional information on SFRs and discharges.
- Is non-dischargeable if the Form 1040 was filed late and after the date that is two-years before the date of the bankruptcy petition.

Note: The two-year period with regard to late filed returns is tolled during a prior bankruptcy. See IRM 5.9.13.19.3(4), BAPCPA Tolling, for additional information.

(6) In addition to the exceptions to discharge above, most rules for determining the discharge of income tax are applied to the SRP MFT 35 and/or MFT 65 liability when the debtor receives a "hardship discharge" under 11 USC 1141(d)(5)(B). The exceptions are the "240 day rule" and the "unassessed but assessable rule" set forth in 11 USC 507(a)(8)(A)(ii) and (iii).

(7) If the tax on the SRP MFT 35 and/or MFT 65 liability is non-dischargeable, the interest is always non-dischargeable. No penalty is assessed or accrued on the SRP MFT 35 and/or MFT 65 liability.

5.17.10.10.1.3
(01-27-2023)
Chapter 11 Discharge and the Employer Shared Responsibility Payment (ESRP) MFT 43

(1) The Employer Shared Responsibility Payment (ESRP) MFT 43 liability is treated as an excise tax. . Unless secured by a valid NFTL, the ESRP MFT 43 assessment is considered a priority claim under 11 USC 507(a)(8)(E) if the liability arose pre-petition and less than 3 years from the petition date. See If not secured by a valid NFTL and theESRP MFT 43 liability arose more than 3 years prior to the petition date, the liability is unsecured general.

(2) The enrollment date and the Letter 226-J issuance date need to be considered when determining if a liability is pre-petition or post-petition claim. In some cases, the IRS will file both types of claims to protect the IRS's interests and ensure the IRS has filed a timely claim. See IRM 5.9.4.19.2(10) , Determining if the ESRP Liability is Pre-Petition/Post-Petition. The enrollment date is usually November 1st of the year before the ESRP year. The date the Letter 226-J was issued is identified by a TC 971 AC 782 in the MFT 43 module.

a. Individual Chapter 11 Cases. Post-petition/pre-confirmation ESRP MFT 43 liabilities owed by an individual debtor who is an applicable large employers (ALE) sole-proprietor qualify as an administrative expense of the Chapter 11 estate if the estate was the employer for the purposes of the ESRP. If the post- petition/pre-confirmation ESRP MFT 43 liability was incurred by the estate, it can be claimable as an administrative expense on Form 6338-A(C), Request for Payment of Internal Revenue Taxes.
b. Non-Individual Chapter 11 Cases. In Chapter 11 non-individual cases, the bankruptcy estate is not a separate taxable entity. Post-petition/pre-confirmation ESRP MFT 43 liabilities owed by the non-individual debtor in a Chapter 11 case are claimable as administrative expenses on Form 6338-A(C), Request for Payment of Internal Revenue Taxes.

Any tax liability that is incurred during the Chapter 11 case, including the ESRP, should be paid when due under the tax laws, or the case is subject to

conversion or dismissal under 11 USC 1112(b)(4)(I). However, if the IRS doesn't bring a motion to convert or dismiss, the plan should provide for payment on the effective date of the plan. Post-confirmation ESRP MFT 43 liabilities owed by a Chapter 11 debtor are not claimable on Form 6338-A(C) and they are not paid under the bankruptcy plan.

(3) If the ESRP liability is a pre-petition liability that arose three years before the petition date, it is a priority excise tax debt (unless secured by a NFTL).

a. Individual Chapter 11 Cases. Pre-petition ESRP priority taxes in individual Chapter 11 cases are excepted from discharge pursuant to 11 USC 523(a)(1)(A) *unless the confirmed plan provides otherwise*. Any portion of the post-petition ESRP (whether incurred by the estate or the debtor) that should have been paid under the plan will be non-dischargeable.
b. Non-Individual Chapter 11 Cases. In reorganizing Chapter 11 cases of non-individual debtors, debtors generally receive a "super discharge" of pre-confirmation tax debts when the Chapter 11 plan is confirmed except to the extent that the plan or confirmation order provides otherwise (11 USC 1141(d)(1)(A))

For more information on dischargeability, see IRM 5.9.17.8.11(5),Chapter 11 Bankruptcies.

5.17.10.10.2
(06-09-2015)
The Binding Effect of Chapter 11 Plans

(1) The provisions of a confirmed Chapter 11 plan generally bind the debtor, any entity acquiring property under the plan, and any creditor (including the IRS). It does not matter whether or not the claim of such creditor is impaired under the plan. It does not matter whether or not the creditor has accepted the plan (11 USC 1141(a)). The IRS should object to any proposed plan with inappropriate provisions.

5.17.10.10.3
(01-27-2023)
Status of the Automatic Stay and CSED after Plan Confirmation for Non-Individuals

(1) When a Chapter 11 plan becomes effective, the non-individual, non-liquidating debtor generally receives a discharge of at least some of its debts. Pursuant to 11 USC 362(c), the stay of acts against property of the estate ends only when the property is no longer in the estate. Property of the estate typically revests in the debtor upon confirmation of a plan. Section 362(c) provides that the stay of any other act remains in effect until the earliest of three events:

- Granting or denial of discharge,
- Closing of the case, or
- Dismissal.

(2) In a non-individual Chapter 11 case, the discharge is typically granted or denied when the plan is confirmed.

Reminder: For the non-individual debtor to receive a discharge, the debtor must first be eligible to receive a discharge. See IRM 5.17.10.10(2), The Effects of Confirmed Chapter 11 Plans, for additional information.

(3) The plan is binding upon the debtor and all creditors (11 USC 1141(a)). The automatic stay generally lifts at confirmation of the plan. However, the IRS is not free to resume its normal collection activity for the debtor's pre-confirmation tax debts. This prohibition is due to the discharge injunction which typically takes effect when the plan is confirmed and the discharge is granted. (11 USC 524(a)) However, the discharge injunction does not prohibit:

a. The commencement or continuation of proceedings concerning the debtor before the U.S. Tax Court, or
b. The setoff of discharged tax liabilities against pre-petition refunds.

(4) When a Chapter 11 plan provides for full payment of pre-confirmation tax debts, the IRS is generally precluded from attempting to collect these tax debts outside the plan. This includes pre-confirmation tax debts for:

- Administrative or gap period liabilities,
- Secured tax claim liabilities,
- Unsecured priority tax claim liabilities, and
- Unsecured general tax claim liabilities.

In most instances, the IRS can only collect these pre-confirmation tax claims through payments under the bankruptcy plan and through making setoffs. However, the IRS may have been successful in negotiating default provisions during the confirmation process which allow for administrative collection actions upon substantial plan default. The default provisions may also require the IRS to petition for dismissal or conversion if the debtor defaults on required payments under the plan. The IRS should follow default provisions in the confirmed plan. See IRM 5.17.10.12.1, Chapter 11 Plan Default Procedures, and IRM 5.9.8.19.3, Plan Default, for more detailed information.

(5) The CSED on pre-confirmation tax liabilities is suspended after a Chapter 11 plan becomes effective and the automatic stay is lifted. Pursuant to IRC 6503(h)(2), the CSED remains suspended until the debtor substantially defaults on making plan payments plus six months. See United States v. Wright, 57 F.3d 561 (7th Cir. 1995); United States v. McCarthy, 21 F. Supp.2d 888 (S.D. Ind. 1998).

5.17.10.11
(01-27-2023)
Individuals in Chapter 11

(1) Chapter 11 cases of individuals is similar to Chapter 13 cases, often adopting language from relevant Chapter 13 provisions.

(2) Under 11 USC 1115, an individual Chapter 11 debtor's bankruptcy estate includes post-petition property and earnings from services of the debtor. 11 USC 1129(a)(15) provides that individuals must apply their projected disposable income to the plan for a minimum of five years. If the plan provides for payments for a period longer than five years, disposable income must be applied to the plan for that period. In either instance, the period begins on the day the first plan payment is due. These changes impact how the individual debtor and the debtor's bankruptcy estate are each taxed under IRC 1398.

a. For an individual debtor filing a Chapter 11 case (as in individual Chapter 7 cases), the individual and the individual debtor's bankruptcy estate are treated as separate taxpayers by IRC 1398. See IRM 5.9.8.14, Internal Revenue Code 1398 Issues, which discusses the separate taxation of an individual Chapter 11 debtor and the bankruptcy estate.
b. Income generally taxable to the Chapter 11 debtor is now taxable to the Chapter 11 estate, under 11 USC 1115. Such income may include all wages and other income from the performance of services earned after the bankruptcy filing. Such income may include all rents, dividends, and other income from property acquired after the bankruptcy filing.
c. This approach was, however, not likely intended by Congress at least insofar as post-petition income from the performance of services is

concerned. IRB 2006-40, Notice 2006-83, provides further guidance on the effects of 11 USC 1115 on the taxation of Chapter 11 bankruptcy estates and individuals.

(3) Bankruptcy cases of individuals in Chapter 11 need to be closely monitored for compliance with their administrative period income tax obligations pursuant to IRC 1398. IRM 5.9.8.14.1, Post-petition Debts - Chapter 11 Individuals, discusses post-petition monitoring in Chapter 11 individual cases.

a. In general, the IRS has made Chapter 7 panel trustees aware of their federal income tax obligation to file Form 1041, U.S. Income Tax Return for Estates and Trusts, returns for an individual debtor's bankruptcy estate. The IRS has circulated Pub 908, Bankruptcy Tax Guide, and participated in various meetings with the trustees.
b. Insolvency sends Letter 4914, Notice to Individual Chapter 11 Debtor Regarding Income Tax Filing Responsibilities, to individual debtors during the initial case review of Chapter 11 cases. The letter informs the debtor of their income tax filing requirements. They may be required to report income on Form 1041 and on Form 1040, U.S. Individual Income Tax Return. If the debtors file a joint bankruptcy petition, a Letter 4914 is sent to each individual on the joint petition.
c. In some cases, it may be appropriate for the IRS to ask for abandonment of estate property to the debtor before taxable transfer of that property occurs (11 USC 554). The IRS may ask the DIP to voluntarily abandon the property. The IRS may ask the bankruptcy court to order abandonment of the estate property. See In re Olson, 930 F.2d 6 (8th Cir. 1991); In re Nevin, 135 B.R. 652 (Bankr. D. Haw. 1991).

(4) Upon the request of the debtor, the trustee, the United States trustee, or the holder of an allowed unsecured claim, the amount or timing of plan payments can be modified any time before completion of the plan (11 USC 1127(e)).

(5) The Chapter 11 discharge for individuals is similar to the discharge for individuals in Chapter 13 cases.

a. Pursuant to 11 USC 1141(d)(5), Chapter 11 individual debtors do not receive a discharge upon confirmation of the plan. As in Chapter 13, the discharge occurs after completion of payments under the plan. The court may, however, grant the debtor a hardship discharge before the completion of plan payments.
b. The types of tax debts excepted from discharge have not changed. Many pre-petition secured and unsecured tax debts survive plan confirmation. It does not matter whether or not the IRS files a claim for the tax in the bankruptcy case. See Matter of Fein, 22 F.3d 631 (5th Cir. 1994); In re DePaolo, 45 F.3d 373 (10th Cir. 1995); In re Gurwitch, 794 F.2d 584 (11th Cir. 1986). In particular, tax debts that are excepted from discharge under 11 USC 523(a)(1)(A)-(C), are not discharged when an individual completes payments under the plan (11 USC 1141(d)(2)). For example, priority taxes are not discharged. See IRM 5.9.8.18(7), Individuals/Certain Taxes Not Discharged.

(6) Claims for post-petition administrative period interest that is due on non-dischargeable taxes against an individual in Chapter 11 are not allowed. They cannot be paid under the Chapter 11 plan. However, the individual debtor remains personally liable for paying this post-petition interest, after confirmation, outside of the plan. See In re Tuttle, 291 F.3d 1238 (10th Cir. 2002).

(7) In Chapter 11 cases, a claim for an individual debtor's own post-petition federal tax liabilities may not be filed in the bankruptcy case. However, these post-petition pre-confirmation debts of the individual survive confirmation and may be collected from the individual. See In re Johnson, 190 B.R. 724 (Bankr. D. Mass. 1995); In re Wood, 240 B.R. 609 (C.D. Cal. 1999). A claim for the estate's post-petition income tax liabilities reported on Form 1041 is claimable in the bankruptcy case.

5.17.10.12
(01-03-2020)
Monitoring Compliance with Chapter 11 Plans

(1) A "party in interest" may file an adversary complaint to revoke a confirmation order. The adversary may seek to revoke the discharge received by the debtor. The adversary must be filed before the 180th day after the confirmation order was entered. The complainant must show that plan confirmation was procured by fraud (11 USC 1144 and Bankruptcy Rule 7001). The circumstances constituting procurement by fraud must be plead with particularity and proven by a preponderance of the evidence (Bankruptcy Rule 7009 and Federal Rule of Civil Procedure 9(b)). It is relatively rare for the IRS to seek revocation of a Chapter 11 plan.

(2) Field Insolvency monitors Chapter 11 plan compliance. Those procedures are discussed in IRM 5.9.8.19.2, Monitoring the Plan and Reviewing for Refiling of the Notice of Federal Tax Lien (NFTL).

5.17.10.12.1
(01-03-2020)
Chapter 11 Plan Default Procedures

(1) Many Chapter 11 plans specify the procedures applicable to all creditors for addressing defaults on payments under the bankruptcy plan. If the plan does not contain provisions, FI attempts to negotiate default provisions in the proposed plan. The terms negotiated depend upon whether the debtor is an individual or a non-individual debtor. It may also depend upon when an individual Chapter 11 case was filed.

(2) When the taxpayer is non-compliant with the terms of a confirmed plan, FI reviews the plan for default provisions. The FI caseworker must comply with the default provisions in the confirmed plan. IRM 5.9.8.19.3, Plan Default, discusses plan default in detail.

(3) In the case of a default, Insolvency may refer the case to a revenue officer to resume administrative collection activity. The IRS can usually collect the full amount of the liabilities provided for in the Chapter 11 plan. The IRS may not be able to collect liabilities not provided for in the plan. They may have been discharged upon confirmation.

(4) Insolvency may also refer the case to Area Counsel to file a motion to dismiss or convert the debtor's Chapter 11 case to a Chapter 7 case. However, dismissal or conversion is usually only appropriate if the bankruptcy estate retained property after confirmation. Or, it may be because the confirmed plan requires creditors to address plan defaults through the filing of a motion for dismissal or conversion. There is no provision that reinstates the automatic stay upon conversion.

Note: Dismissal of a Chapter 11 case due to a default by a debtor with respect to a confirmed plan does not revoke any discharge which has been granted in the case. This is an issue in a Chapter 11 case of a non-individual debtor that receives a discharge on confirmation of a plan.