Social Security Benefits and the IRS Stretch Levy

By Neal Nusholtz

In 1997, Congress passed 26 USC 6331(h), which limited continuous IRS levies on Social Security benefits to 15 percent of the payments. After 26 USC 6331(h) was promulgated, four federal district court cases held that it does not limit continuous levies on Social Security to 15 percent.[1] In short, they achieved that result by analogizing Social Security benefits to periodic payments on one promissory note and, therefore, a levy on all monthly payments was not a continuous levy under 26 USC 6331(h). One appellate court referred to those four district court cases but only on a jurisdictional issue.[2] One bankruptcy court has applied the 15 percent limit.[3]

Two types of levies in 26 USC 6331

Ten days after demand and nonpayment of taxes, the IRS may levy on all property belonging to a delinquent taxpayer.[4] A levy is effective by serving a notice to a person who has property owed to or owned by a delinquent taxpayer.[5] Failure to honor a levy subjects the obligor to substantial penalties under 26 USC 6332.

Two different types of levies are provided for under 26 USC 6331: continuous and noncontinuous. A noncontinuous notice of levy covers "property possessed and obligations existing at the time thereof."[6] A payor's obligation under that type of levy is a matter of timing. If property of a taxpayer is not possessed or an obligation is not owed to a delinquent taxpayer at the time of the notice of levy, then the notice has no effect even if the obligation to the taxpayer arises later or property belonging to a taxpayer is received at a later date. Successive levies may be issued "as often as may be necessary."[7]

A second type of levy is a continuous levy, such as one on wages. It covers after-acquired property and lasts until it is released.[8] Situations in which noncontinuous levies stretch out into the future, like in the case of Social Security benefits, are identified here as "stretch levies."

at a glance

Congress provided for continuous levies of only 15 percent of Social Security benefits, but some courts, at the behest of the government, have allowed the IRS to take 100 percent.

At least one court has held that if someone owes taxes and files bankruptcy after receiving Social Security, the Social Security benefits will still be subject to tax levy after the taxes are discharged in bankruptcy.

Normally, the statute of limitations for tax collection runs only for 10 years, but under 26 CFR 301.6343-(1)(b)(1)(ii), the statute never runs out on Social Security payments because some courts treat them as "fixed and determinable."

The Social Security issue

Before the Balanced Budget Act of 1997, continuous levies only applied to wages and salaries,[9] with a small part of wages exempted from the continuous wage levy.[10] The act added 26 USC 6331(h), which also permitted continuous levies for pensions and certain government payments that were not subject to means testing, such as Social Security payments. Before that change, a single Social Security payment could be seized in full under 26 USC 6334(c), but thereafter, continuous levies on Social Security would be limited to 15 percent of the monthly payments.[11]

The four district court cases that did not apply the 15 percent limit to a continuous levy on Social Security benefits adopted the viewpoint expressed in *Hines v United States*. The *Hines* court found that future Social Security benefits are fixed and determinable under 26 CFR 301.6331-1(a), which states that "[o]bligations exist [under 26 USC 6331(b)] when the liability of the obligor is fixed and determinable although the right to receive payment thereof may be deferred until a later date."[12]

The ruling in *Hines* was to the effect that Social Security benefits over a lifetime are one big obligation, like a promissory note. For periodic installment payments on a promissory note, successive levies under 26 USC 6331(c) need not be served on the maker of the note because at the time of the execution of the note, the holder has a fixed right to payment that is merely deferred over a future period.[13]

Fixed and determinable

The word "fixed" is not defined in 26 CFR 301.6331-1(a). A review of caselaw suggests that a "fixed obligation" is a chose in action where a taxpayer could have successfully maintained a suit to collect on it.[14] That is to say, if all of the events giving rise to the obligation have occurred, then the obligation is fixed.

Obligations subject to a condition precedent

In *United States v Puyallup Tribe of Indians*, the council for the Puyallup Tribe made discretionary per capita distributions to qualified tribe members when circumstances would permit. One of the members, Joshua D. Turnipseed, owed taxes and the IRS served a notice of levy on the council. After the council ignored the levy and paid Turnipseed anyway, the government sued for penalties under 26 USC 6332. The court held that until the council decided to make a distribution, the distributions were not fixed and determinable and, therefore, not subject to the notice of levy.[15]

Obligations subject to complete legal defenses

An attorney who owed federal taxes sued his client, Morey, for fees. After the IRS learned about the lawsuit, it served Morey with a notice of levy in June 1987. Morey did not honor the levy and paid the lawsuit settlement to the deceased attorney's estate in August 1989. The government sued Morey for failing to honor the levy. Morey claimed that at the time of the levy, he was not in possession of property or obligated to the attorney. Morey had alleged in the lawsuit a lack of consideration, a failure of performance, mutual mistake of fact, unconscionability, and rescission.[16]

The issue in the *Morey* case was "whether, at the time the levy was served on Morey, Morey was obligated [to the attorney] with respect to property or rights to property subject to the levy." The court held that the "[attorney's] rights were not vested on the date of the levy" and because of that, the levy did not attach to the future payment.[17]

Executory contracts

A contract obligation to pay money is "fixed" when performance by the taxpayer has occurred.[18] Performance by a third party may also be necessary to create an enforceable obligation to pay money to a delinquent taxpayer. In the *Tull* case,

the Ninth Circuit reversed a district court decision that held a levy on auction proceeds was valid even though the levy was made before the auction had occurred. The issue over the levy was whether there was sufficient performance upon which a suit could be maintained.[19]

At the time the notice of levy in *Tull* was served, the auction contract was open-ended as to what was to be sold. The lower court held that there was sufficient partial performance of the auction contract (advertising the auction and cleaning the equipment to get it ready for sale) to make the contract enforceable. The Ninth Circuit reversed, saying that the obligation "to sell some as yet undetermined amount of property for an as yet undetermined price to as yet undetermined buyers" was not fixed and determinable.[20]

In *In re John Mill Hawn*, the taxpayer (Hawn) had assigned his mineral rights to the bank as security for a loan. The IRS served the bank with a levy in 1987. At the time of receiving the notice of levy, the bank had no funds belonging to Hawn. Three years later, the bank had received funds over and above the amount of the loan. The bank paid the surplus of $131,679 to a group that included Hawn, his ex-wife, and some of his creditors. The IRS sued the bank for the money.[21] The *Hawn* court found that the bank was not liable for failing to honor the levy: "Since the right to receive future income from production and sale of oil thus was a contingent, non-vested and non-determinable right, the IRS levy could not reach it."[22]

Are future Social Security payments vested?

Hines was the first case to hold that Social Security payments are fixed and determinable. It relied on a case called *Schmiedigen v Celebrezze*, which held that a person who has contributed part of his or her salary to Social Security has "a vested right to the payments prescribed by the statutory scheme."[23]

Under 42 USC 402(a), a person "shall be entitled to an old-age insurance benefit for each month, beginning with" the first month after a fully insured individual who has attained age 62 and has filed application for benefits "and ending with the month preceding the month in which he dies." Payments of Social Security are subject to two conditions: the recipient must have applied for benefits and the recipient must live the full month preceding payment. For example, a senior citizen with a $2,400 monthly benefit subject to a continuous IRS levy would receive $2,040, with $360 paid to the IRS.

A person receiving Social Security has no present right to payments beyond the current month in which he or she is alive.[24] Future benefits are not assignable or transferable under 42 USC 407(a), which states "[t]he right of any person to any future payment under this title shall not be transferable or assignable, at law or in equity." Social Security benefits are not one big obligation paid in monthly installments. Benefits are a series of distinct separate payments contingent on the recipient's surviving the preceding month. A person receiving Social Security cannot maintain an action to collect beyond the current month. The Social Security Administration has no obligation to pay Social Security beyond the current month. It's strange that Congress would pass a law allowing continuous levies on Social Security benefits limited to 15 percent and then be told by the courts that a law allowing continuous levies on Social Security benefits was unnecessary and would be ignored.

Treating future Social Security benefits like installment payments on a promissory note has negative ramifications for taxpayers after a bankruptcy discharge, after the 10-year statute of limitations for collection has expired, and after back taxes are fully paid and the government levies on extra money.

Bankruptcy

In the bankruptcy case *In re Anderson* cited earlier in this article, the government argued it had a 26 USC 6321 tax lien on all future Social Security benefits for a delinquent taxpayer who had filed for bankruptcy after starting to receive Social Security benefits. The bankruptcy judge held that there was a lien on Social Security benefits and that lien continued

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on all future Social Security payments after the bankruptcy discharge, making Social Security subject to future IRS levies after a bankruptcy discharge.[25]

The statute of limitations on collection

Some delinquent taxpayers who are in over their heads can get relief from their tax liability expiring after the 10-year collection statute of limitations under 26 USC 6529(a)(1) has run out. In 1994, the IRS added 26 CFR 301.6343-1(b)(1)(ii), which, like a tax lien in bankruptcy, permits collection on payments of Social Security to continue beyond the 10-year statute of limitations if the payments are fixed and determinable.

Under 26 CFR 301.6343-1(b)(1(ii), Social Security benefits are essentially treated like a promissory note, which creates an anomaly after a bankruptcy discharge or after the period for tax collection has expired. For example, a senior citizen with an expired tax liability will lose future Social Security benefits under this regulation because he or she *used to owe taxes*.

Excess seizures

A continuous unmonitored stretch levy of Social Security benefits could eventually collect funds in excess of the tax liability. The official position of the IRS is to keep the excess if the overpayment occurs more than two years after the notice of levy.[26] A taxpayer would need to know of the overpayment and then pursue a claim for refund within two years of the date of the overpayment under 26 USC 6511(a). If levies were limited to a single Social Security payment, the government would always return the extra money seized because a two-year delay between a notice of levy and an overpayment would never happen.

Conclusion

In these examples of stretch levies, bankruptcy discharges, and expired tax liabilities, Social Security recipients with an unpaid tax liability were given the short end of the stick. Sometimes those senior citizens had nothing left but their monthly Social Security benefits the government had taken, which resulted in district court lawsuits and a precedent allowing the taking of 100 percent of the Social Security payment. That is how our tax system evolves. Even if Congress specifically said that only 15 percent of Social Security benefits can be taken in a continuous levy, the intended beneficiaries of that statute can eventually lose that protection over time. ■

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ENDNOTES

1. *Hines v United States*, 658 F Supp 2d 139, 146–147 (D DC, 2009); *Beam v United States*, opinion of the United States District Court of Oregon, issued June 6, 2007 (Case No. 07-6035-TC), p 1; *Duran v IRS*, opinion of the United States District Court for the Eastern District of California, issued March 16, 2009 (Case No. 12-2650 No. CV-F-09-345OWW/DLB), p 4; *Clift v United States IRS*, opinion of the United States District Court for the Western District of Washington, issued February 8, 2017 (Case No. C16-5116 BHS).
2. *Bowers v United States*, 498 F App'x 623, 627 (CA 7, 2012).
3. *In re Anderson*, 250 BR 707 (Bankr D Mont, 2000).
4. 26 USC 6331(a).
5. 26 CFR 301.6331-1(a).
6. 26 USC 6331(b).
7. 26 USC 6331(c).
8. 26 USC 6331(e).
9. *Id.*
10. 26 USC 6334(d).
11. 26 USC 6331(h)(2)(A).
12. *Hines v United States*, 658 F Supp 2d at 146.
13. *Id.* See also Rev Rul 55-210, 1955-1 C.B. 544.
14. *United States v Morey*, 821 F Supp 1438, 1442 (WD Okla, 1993) and Rev Rul 55-210, 1955-1 C.B. 544.
15. *United States v Puyallup Tribe of Indians*, opinion of the United States District Court for the Western District of Washington, issued April 9, 2014 (Case No. C13-5122 BHS).
16. *United States v Morey*, 821 F Supp 1438 (WD Okla, 1993).
17. *Id.* at 1440, 1442.
18. *United States v Hemmen*, 51 F3d 883, 890 (CA 9, 1995).
19. *Tull v United States*, 69 F3d 394 (CA 9, 1995).
20. *Id.* at 397.
21. *In re John Mill Hawn*, 149 BR 450 (Bankr SD Tex, 1993).
22. *Id.* at 457.
23. *Schmiedigen v Celebrezze*, 245 F Supp 825, 827 (D DC, 1965).
24. 42 USC 402(a).
25. *In re Anderson*, 250 BR 707.
26. IRS Significant Svc Ctr Advice 200028036 (July 14, 2000) <https://www.irs.gov/pub/irs-wd/0028036.pdf> (accessed August 22, 2018). The two-year period references the statute of limitations for filing a wrongful levy claim under 26 USC 6532(c) (it used to be nine months before the Tax Cuts and Jobs Act changed it to two years).