



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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MEMORANDUM FOR AREA COUNSEL SB/SE: Area 5

St. Paul
Attn: John Schmittiel

FROM: Alan C. Levine, Chief, Branch 1
(Collection, Bankruptcy, and Summonses)

SUBJECT: Opin re: Custodia Legis Issue, Failure to Honor Levy

By telephone on July 6, 2001, and via e-mail dated July 9, 2001, you requested our advice as to whether the Service has an interest (either by a levy served under Section 6332 of the Internal Revenue Code or by virtue of its lien under Section 6321 of the Code), or an interest worth asserting, in money in a bank account deposited by the clerk of the state court pursuant to a state court action. Additionally, you inquired as to how, if the Service an interest, it should go about asserting its interest, particularly before the state court arrives at a decision and the money disappears.

ISSUE:

Whether the Service has an interest, pursuant to its tax lien or by levy, in money in a bank account deposited by the clerk of a state court pursuant to a state court action. If the Service does have an interest, how should it assert its interest.

CONCLUSION:

By virtue of its tax liens, the Service has an interest in the money deposited with the state court (which was subsequently deposited with a bank). This interest has priority over any interest of [redacted] and [redacted]

FACTS:

In late 1997 and early 1998, the [redacted] (the Health Department) began investigating allegations of improper disposal of asbestos-

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containing material on properties owned by either the corporation,
 , or .

The Health Department subsequently issued an Environmental Cleanup Order (ECO) and it appears that then retained the corporation,
 , as its environmental consultant and to conduct asbestos abatement and cleanup of the properties cited in the ECO. submitted a plan of action for removal of the asbestos on and then subcontracted with the company to perform some of the asbestos abatement work.

On April 9, 1998, requested an extension to comply with the Order, noting that compliance had been delayed due to insufficient payments to .

On , the Health Department issued Notices of Violation against .

On , the IRS made an assessment against for unpaid Form 941 taxes for the quarter of in the amount of \$.

On , the filed a complaint against , (hereinafter, "defendants") in state court. The complaint alleged numerous violations of statutes pertaining to inspection, removal, transportation, and disposal of asbestos from properties the defendants owned, and t the imposition of civil penalties.

On that same date, the parties filed a consent agreement with the court. This agreement stipulated that the defendants had violated numerous provisions of the Code relating to hazardous waste management and asbestos removal. In settlement of these violations, the consent agreement provided for the levying of a civil penalty against the defendants in the amount of \$

Additionally, section of the consent agreement provided as follows:

" , shall satisfy any monetary obligations owing to , the environmental remediation contractor who performed the asbestos cleanup on the identified buildings in , within two

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years of the date of entry of judgment herein. The contractors shall retain the right to seek compensation from Defendant prior to the two year period.”

Section further provided that, if were current on their installment payments of the \$, the Health Department would not execute on its judgment. Additionally, the Health Department agreed to provide partial releases of any real estate or other property encumbered by the judgment as long as the net proceeds from such sale, after payment of closing costs and superior lienholders, were distributed in fulfillment of obligations encumbered by the consent agreement.

The consent agreement provided that the defendants agreed to the entry of judgment in accordance with its terms and an Order for Judgment was signed that day.

On , judgment was entered in the state action which ordered that the defendants be levied a \$ civil penalty, subject to the terms and conditions delineated in the Order for Judgment. The judgment set forth the payment terms of the \$ penalty, i.e., \$ to be paid over years, \$ to be suspended under certain conditions. The judgment also included the exact language from Sections and of the consent agreement.

Subsequently, in , the IRS made assessments against for unpaid Form 941 tax liabilities for the quarter of , and the quarters of , respectively, totaling approximately \$. Additionally, on , a notice of federal tax lien was filed against in , and with the for the corporation’s unpaid Form 941 tax liabilities.

On (hereinafter, “plaintiffs”) filed a complaint in state court against the Health Department and . In their complaint, the plaintiffs allege that they retained to conduct the asbestos removal and cleanup required by the ECO and thereafter subcontracted with to perform some of the asbestos removal work.

Plaintiffs contend that issued two bills to for its services, one dated , in the amount of \$ and one dated , in the amount of \$. Plaintiffs further allege that they made payments totaling \$ in and , to , but that charges exceeded the work set forth in plan of action as well as the usual and customary rates charged for said services. Plaintiffs cited to the , judgment which provided for payment to and and noted that it had negotiated a settlement with and had attempted to settle with but had been unable to do so. Accordingly, the plaintiffs requested a determination of their rights and obligation with respect to and the

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proper amount of compensation, if any to which was entitled for the work performed.

On that same date, the plaintiffs filed an ex parte motion to deposit \$ with the Clerk of the Court and requested that the Clerk of the Court deposit the funds in an interest bearing account. The source of these funds is not known. The plaintiffs' motion was granted, however, and the money was subsequently deposited with the

On , the Health Department filed an answer to the complaint, alleging that the plaintiffs' action was barred by estoppel and laches because it had years to resolve the payment issue. It also argued that the court should decide whether the plaintiffs had complied in good faith with the , judgment.

 also filed an answer on , alleging that plaintiffs' action was barred by the affirmative defenses of accord and satisfaction, laches, estoppel, release, waiver and fraud. further alleged that the complaint was barred by res judicata and collateral estoppel because, pursuant to the previous judgment, the plaintiffs were required to satisfy any monetary obligation owing to within two years of the date of entry of the judgment.

On , the Service served a levy on for Form 941 tax liabilities as had previous accounts at the bank. In response to the levy, the bank identified accounts in s name, one of which was a in the amount of \$, issued as follows:

Signers by court order only

The bank refused to honor the levy, stating that withdrawals were only permitted pursuant to a court order.

On filed a motion for summary judgment in the state court action, arguing res judicata. A hearing on the motion was scheduled for .

LAW & ANALYSIS:

Section 6321 of the Internal Revenue Code provides that a lien arises in favor of the United States upon all property and rights to property, real or personal, belonging to any person who refuses to pay his taxes. 26 U.S.C. § 6321. The lien arises upon

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assessment, 26 U.S.C. § 6322, and attaches to all after-acquired property of the taxpayer. Glass City Bank v. United States, 326 U.S. 265 (1945).

Upon assessment of the Form 941 tax liabilities, the IRS had a lien on all property of . This lien attached to the money when acquired it and continued even though the money was subsequently deposited with the state court (which then deposited it with the bank).

Under section 6323 of the Code, the lien imposed by section 6321 is not valid against any purchaser, holder of a security interest, mechanic's lienor or judgment lien creditor until the Service has filed a notice of its lien. [REDACTED]

Section 6323(h)(2) defines a mechanic's lienor as any person who, under local law, has a lien on real property (or on the proceeds of a contract relating to real property) for services, labor or materials furnished in connection with the construction or improvement of such property. mechanic's lien statute, , further provides:

"Any person who improves real estate by the contribution of labor, skill, or materials, whether under contract with the owner of such real estate or under contract with any agent, trustee, contractor, or subcontractor of the owner, has a lien upon the improvement and upon the land on which it is situated or to which it may be removed for the price or value of such contribution."

This lien attaches, as against an encumbrancer without notice, upon the "actual and visible beginning of the improvement."

[REDACTED] removed hazardous materials from properties owned by the plaintiffs, one could argue that made improvements on said properties. However, the statute indicates that would have a lien on the property it improved, not money, in this case the source of which is unknown.

[REDACTED] The parties in the original state action did not include , nor did a representative from sign the consent agreement which was subsequently incorporated into the judgment. Instead, there is only a judgment which requires the plaintiffs to "satisfy any monetary obligations owing to" . [REDACTED]

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The issue then arises as to whether the Service can obtain the funds given the doctrine of custodia legis, i.e., a court's power to assume complete control over assets in its possession. (We assume the Collection Due Process requirements under I.R.C. § 6330 have been met.)

