Department of the Treasury

Internal Revenue Service Office of Chief Counsel

Notice

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September 09, 2004

Change in Litigating Position
Application of Bankruptcy Code
§ 506(a) to Pension Plans Excluded
From the Bankruptcy Estate Under

From the Bankruptcy Estate Under Upon incorporation

Subject: Bankruptcy Code § 541(c)(2) **Cancel Date**: into CCDM

Purpose

This notice announces a change in the Service's litigating position concerning the application of Bankruptcy Code § 506(a) to pension plans that are excluded from the bankruptcy estate under Bankruptcy Code § 541(c)(2).

Discussion

Under section 506(a) of the Bankruptcy Code, a creditor with a lien on property of the estate holds a secured claim to the extent of the value of the creditor's interest in the estate's interest in such property. Section 541(a) provides that, upon the commencement of the bankruptcy case, an estate is created which consists of all legal or equitable interests of the debtor on that date. An exception to this rule is found in section 541(c)(2), which provides that restrictions on the transfer of a beneficial interest in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a bankruptcy case.

In *Patterson v. Shumate*, 504 U.S. 753 (1992), the Supreme Court determined that the anti-alienation clause required for ERISA compliance and tax qualification and contained in the debtor's plan constituted a restriction on transfer enforceable under "applicable nonbankruptcy law" within the meaning of section 541(c)(2). Accordingly, the Court held that the ERISA-qualified pension plan was excluded from the debtor's bankruptcy estate under section 541(c)(2).

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In *In re Lyons*, 148 B.R. 88, 94 (Bankr. D.D.C. 1992), the bankruptcy court held that because the anti-alienation provisions in a pension plan were "ineffective against Federal tax liens," they were not, under the terms of section 541(c)(2), "enforceable under applicable nonbankruptcy law" against the Service. The court held that the debtor's rights in the pension plan remained property of the bankruptcy estate under section 541(c)(1) and were included in the value of the Service's secured claim under section 506(a).

The Office of Chief Counsel has advanced the position that the Service's secured claim includes the value of a debtor's interest in a pension plan that was subject to a federal tax lien with mixed success. *Compare In re McIver*, 255 B.R. 281 (D. Md. 2000) (finding the reasoning in *Lyons* persuasive, court holds that the Service-s secured claim included the value of annuity payments the debtor received under teacher retirement plans); *with In re Keyes*, 255 B.R. 819 (Bankr. E.D. Va. 2000) (discussing the split of authority, court holds that an ERISA-qualified pension plan is not included in the debtor-s estate for purposes of securing the Service's claim).

In *United States v. Snyder*, the Ninth Circuit rejected the approach taken in *Lyons* and held that the Service did not hold a secured claim with respect to the debtor's interest in an ERISA-qualified pension plan because the interest was excluded from the bankruptcy estate under section 541(c)(2). *United States Internal Revenue Service v. Snyder*, 343 F.3d 1171 (9th Cir. 2003). The court reasoned that the anti-alienation clause in the debtor's plan prevented the transfer of the debtor's interest in the plan to the bankruptcy estate with respect to all creditors, including the Service. Because the debtor's interest in the pension plan did not become property of the bankruptcy estate, the court concluded that it could not be used to secure the Service's claim under section 506(a). The court noted, however, that the Service's liens are not extinguished or otherwise affected, and continue to exist outside of bankruptcy. *Id.* at 1179.

Change in Position

The Office of Chief Counsel will no longer argue that the Service may include in the value of its secured claim the debtor's interest in a pension plan that is excluded from property of the estate under section 541(c)(2). In cases where the debtor's interest in a pension plan is excluded from property of the estate, the Service will not include the value of the debtor's interest in the pension plan in its secured claim. The Service's lien against the debtor's interest in the pension plan is not extinguished and will continue to exist outside of the bankruptcy proceeding.

Questions about this Notice should be directed to Collection, Bankruptcy & Summonses, Branch 2, at (202) 622-3620.