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IRS Liens, After Acquired Property and the Doctrine of Choateness

Internal Revenue Service liens attach to all a taxpayer's "property and rights to property, whether real or personal, belonging to such person." 26 U.S.C. Section 6321.[1] A taxpayer's "property" is determined by relevant state law, but federal law determines lien priority.

The IRS lien extends to property acquired by the taxpayer after the lien arises. IRS Regulation 301.6321-1[2] and has priority in that property. *United States v. McDermott*, 507 U.S. 447 (1993) (A federal tax lien filed before a delinquent taxpayer acquired real property has priority in that property over a private creditor's previously filed judgment lien. Although priority for purposes of federal law is governed by the common law principle that "the first in time is the first in right," a state lien that competes with a federal lien is deemed to be in existence for "first in time" purposes only when it has been "perfected" in the sense when the property subject to the lien [is] established.)

The *McDermott* case held that because the bank's judgment lien could not actually attach to the property at issue until the McDermotts acquired rights in that property, which occurred after the United States filed its tax lien. The bank's lien was not perfected before the federal filing. It was irrelevant that the federal lien similarly did not attach and become perfected until the McDermotts acquired the property, since 26 U.S.C. Section 6323(c)(1) demonstrates that such a lien is ordinarily dated, for purposes of "first in time" priority against competing interests, from the time of its filing.

The *McDermott* decision is the application of the requirement that a lien superior to a federal tax must be "choate." A lien is "choate" for the purposes of determining priority under federal tax lien law when (1) the identity of the lienor; (2) the property subject to the lien; and (3) the amount of the lien are all established. Thus, a federal tax lien will take priority over most other valid judicial liens, mortgages and security interests in property that has not yet come into existence

because, even if both interests attach at the same time, the federal lien is deemed first in time regardless of when competing security interests were otherwise perfected under state law. *J.D. Court, Inc. v. United States, Inc.*, 712 F.2d 758 (7th Cir. 1983).[\[3\]](#)

The choate doctrine is very powerful and well established. “That collection of taxes is vital to the functioning, indeed existence, of government cannot be denied. *McCulloch v. Maryland*, 4 Wheat. 316, 425, 428, 431, 4 L.Ed. 579 (1819); *Springer v. United States*, 102 U.S. 586, 594, 26 L.Ed. 253 (1881). Congress recognized as much over 100 years ago when it authorized creation of federal tax liens. Act of July 13, 1866, ch. 184, § 9, 14 Stat. 107, recodified as amended in [26 U.S.C. §§ 6321–6323](#). The importance of securing adequate revenues to discharge national obligations justifies the extraordinary priority accorded federal tax liens through the choateness and first-in-time doctrines.” *United States v. Kimball Foods, Inc.*, 440 U.S. 715, 734 (1979).

The choate requirement applies to all sorts of liens that compete with IRS liens. In *United States v. Pioneer American Insurance Company*, 374 U.S. 84 (1963) the tax lien prevailed over an attorney’s lien because the claim for attorney’s fees remained inchoate until finally fixed in amount by a mortgage foreclosure decree entered subsequent to filing of federal tax liens. The claim for attorney’s fees was subordinate to federal tax liens, even though federal tax liens were filed after claim for fees had become enforceable under Arkansas law and after commencement of suit in which fees were earned.

The choateness doctrine is not defeated by many traditional state law remedies like:

- Relation back, *Blachy v. Butcher*, 221 F.3d 896 (6th Cir. 2000) (“Even if Michigan law allows the doctrine of ‘relation back’ to give . . . priority over private intervening interests, this would not be determinative as to the IRS. The priority of a federal tax lien against competing claims is governed by federal law.”) or
- Constructive trust, *Blachy v. Butcher*, 221 F.3d 896 (6th Cir. 2000) (“Under Michigan law, a ‘constructive trust is strictly not a trust at all, but merely a remedy administered in certain

fraudulent breaches of trusts.’ Soo Sand & Gravel Co. v. M. Sullivan Dredging Co., 244 N.W. 138, 140 (1932). Accordingly, a constructive trust does not arise until a judicial decision imposes such a trust under Michigan law.”) or

- Prejudgment attachment when the IRS lien is filed after the prejudgment attachment but before the attaching creditor is awarded a judgment, *U.S. v. Security Trust and Savings Bank of San Diego*, 340 U.S. 47 (1950) (“When the tax liens of the United States were recorded, Morrison did not have a judgment lien. He had a mere ‘caveat of a more perfect lien to come.’”) citing People of State of New York v. Maclay, 288 U.S. 290 (1933); or
- *Lis pendens*, *Dowdy v. Charter Financial Group*, 122 F. Supp.2d 1347, 1352 (U.S.D.C. M.D. Fla. 2000) (“In several federal decisions, courts have found that inchoate attachments, such as a *lis pendens*, do not have priority over perfected federal tax liens.”) But, compare, *Feiler v. U.S.*, 62 F.3d 215 (9th Cir. 1995). The *Feiler* case offers hope for claimants who file *lis pendens* and seek specific performance of a real estate sale contract executed before the IRS lien was filed.

In sum, for your mortgage, security interest or judgment lien to defeat an IRS lien (1) the identity of the lienor; (2) the property subject to the lien; and (3) the amount of the lien are established when the IRS lien is filed, unless your lien qualifies as a protected “secured commercial financing transactions” [commonly a UCC Article 9 security interest in future collateral such as inventory or accounts receivable] and that protection is only good for 45 days. *J.D. Court, Inc. v. United States, Inc.*, 712 F.2d 758 (7th Cir. 1983).

For more information, see the Internal Revenue Manual, Part 5: Collection Process, Chapter 17: Legal Reference Guide for Revenue Officers, Section 2: Federal Tax Liens. If you have questions about this article, contact Vince Mauer at vmauer@fbtlaw.com

[1] The tax lien arises when the tax is “assessed,” the government records in its records that taxes are owed. That tax lien begins to compete with other liens for priority when the government makes a proper Notice of Federal Tax Lien Filing. See IRM 5.17.2.2.1, *et seq.*

[2] The same is not true for filed liens in many states. See, current Ohio Revised Code Section 2329.01(A) and decisions thereunder.

[3] [26 U.S.C. § 6323\(c\)](#) provides a limited exception to this rule for certain secured commercial financing transactions. See [McDermott, 507 U.S. at 453–454](#), (observing that [26 U.S.C. § 6323\(c\)\(1\)](#) accords priority over filed federal tax liens to certain “commercial transactions financing agreements.” A state created lien against collateral resulting from such an agreement may be deemed “first in time” against a federal tax lien even though the underlying collateral technically has not yet come into existence. To fall within this statutory exception, the competing state law created lien must be (1) in qualified property; (2) covered by the terms of a written agreement that was entered into before the tax lien was filed; (3) constitute a “commercial transactions financing agreement;” and (4) superior, under local law, to any judgment lien arising out of an unsecured obligation. See also, [Plymouth Savings Bank v. IRS, 187 F.3d 203, 206 \(1st Cir.1999\)](#).

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