How to Handle Abandoned Properties That Have IRS Liens
National Resource Network - 311 for Cities

In July 2014, a city reached out to the National Resource Network's 311 for Cities with a question about how to handle five abandoned properties that are held by a now defunct non-profit organization and have IRS payroll tax liens. The Network connected city officials with an expert from the Center for Community Progress who specializes in affordable housing and community development issues; the following is a brief summary of an hour-long conference call discussing the city's challenges and several strategies for them to consider when addressing the issue.

Background Information

The city has been dealing with these properties for nearly a dozen years and is eager to move the properties into the city's control. All five of the single-family, detached, residential properties were previously owned by a nonprofit that went out business; three of the properties are in a historic district.

During a title exam, the city learned that there are extensive IRS liens (estimated to be 10 years old) against the now defunct owner for outstanding payroll taxes. There is also a federal judgment (related to taxes) against one of the former employees. The city doesn't recall seeing any mortgages on the properties, but was encouraged to confirm this. Because the organization was a certified non-profit, the city granted an exemption on their property taxes, so there are no delinquent property taxes on the buildings.

Analysis and Recommendations

The city learned that it can be challenging to get the IRS to release a lien; success is more likely when a city is able use a public leverage point to move the property into foreclosure, at which point the IRS has to make a decision of whether to obtain the property or not by redeeming it from the foreclosure process. There is value in having distinct strategies for the salvageable houses and the ones to be demolished; after doing the title exam, the city should identify the house with the lowest value and pursue it first. The idea behind all of this is to develop an approach that can then be adapted for use on other abandoned properties in the community.

The first thing to look for when trying to address an abandoned property with an IRS lien is an opportunity for the local government to do a property tax enforcement proceeding, because property taxes take precedent over the federal tax lien and force a foreclosure. To do this, the city would have to give the IRS notice of the sale; the IRS would have 120 days after the foreclosure sale to take over the property or to have its lien terminated. Because the city granted the former owner an exemption on their property taxes, it could consider revoking the property tax exemption retroactively to put the properties back on the tax rolls, giving the city the right to outstanding ad valorem taxes.

A second strategy would be to explore housing and building code enforcement liens. The law varies by state, but sometimes these liens can only be based on actual expenditures (e.g. cutting grass, boarding up a house). If state law permits, a code enforcement lien could be added to the property tax liens prior to running the property through the foreclosure process. If there are no code expenditures, the city could consider doing boarding or demolition and then putting the code liens on the property immediately. A large caveat exists here – the city has to consider whether the code lien would maintain its stature if the costs were incurred after the federal lien was established.

These first two strategies can be combined, so that there is both the property tax and code lien enforcement.

A third tactic would be to double check if there are any mortgage liens on the property from a bank, foundation, etc. (i.e. a mortgage of record) and ask to transfer the mortgage to the city so that they can foreclose on the properties.

Regardless of which strategy is pursued, the city should research the revocation of the organization's non-profit status to determine when they dissolved and to see if there have been any proceedings at the state level related to the dissolution to the corporation. In most states, when a non-profit dissolves, it has to get approval from the state to ensure that the assets are transferred appropriately. This information can be helpful, even if the city is able to say that the property should have been taxed by virtue of the factual, if not legal, loss of non-profit status of the owner.

If none of these strategies work, the city can explore going to either the State Attorney General to take control of the nonprofit and its assets, or to force the nonprofit's assets into a judicial receivership. This is more complicated, but can be pursued as needed.

Next Steps

The city is to research whether there are mortgages of record on the properties; whether there have been public expenditures to maintain the properties; and the possibility of leveling retroactive property taxes. After completing that research, the Network will set up a follow up call to provide guidance on next steps for this particular challenge, and to explore other community development issues they are dealing with.