

Special information relating to

Purchase Money Mortgages, Purchase Money Security Interests, and Subordination of the Federal Tax Lien

If the IRS has recorded a Notice of Federal Tax Lien (NFTL) against you and you are trying to obtain a loan to buy real or personal property, the following questions frequently arise:

Does the lien prevent a bank, mortgage company, or other lender from lending you money to buy a house, a motor vehicle, or other consumer goods or property?

When a loan is made to purchase real property, the lender may obtain a Purchase Money Mortgage (PMM); when a loan is made to purchase personal property, the lender may obtain a Purchase Money Security Interest (PMSI). Provided all requirements of state law are complied with, these types of financing agreements allow lenders to finance the purchase of real and personal property even though a NFTL has been filed against you.

If you borrow money from a lender for such a purpose and give the lender a security interest in the property purchased with the proceeds of the loan, will the lender's security interest have priority over the tax lien?

In 1968 the Internal Revenue Service published Revenue Ruling 68-57, which states that it is the position of the IRS that a PMM or a PMSI given in good faith to secure a loan for the purchase of real property or goods, has priority over an already recorded Notice of Federal Tax Lien. (See *Revenue Ruling 68-57 at the end of this publication.*)

Is it necessary for the Internal Revenue Service to issue a certificate of subordination giving the security interest priority over the NFTL?

It is not necessary for the Internal Revenue Service to issue a certificate of subordination in order for the lender's PMM or PMSI to have priority over the lien.

In order for the PMM or PMSI to have priority over the lien, the PMM or PMSI must meet all of the requirements under state law, including the following. The PMI or PMSI must:

Be allowed under local law – The creation of a PMM or a PMSI is based on state law. While allowed by all states, you or your lender should be familiar with the laws of the state in which you live. Make sure that your state's law does not put a limit on the dollar amount of a PMM or a PMSI.

The proceeds of the loan must be used to purchase the property – The PMM or PMSI will have priority over the federal tax lien in the property you are purchasing in an amount equal to the proceeds of the loan that are directly used to purchase the property.

If the PMM or PMSI must be recorded – Make sure that the PMM or PMSI is recorded in the place directed by your state's law, and that it is recorded within any time frame that your state's law may require.

If the security interest that will be securing the loan you are making qualifies for the priority given to a PMM or a PMSI, you do not need a certificate of subordination from the Internal Revenue Service, and a certificate will not be provided if applied for.

If you or your lender have any questions about whether your loan is being secured by a qualifying purchase money mortgage or purchase money security interest, please call or write the Technical Services (Advisory) office in your area. Contact information is found in Publication 4235, *Technical Services (Advisory) Group Addresses*.

Revenue Ruling 68-57

Section 6321 – LIEN FOR TAXES

26 cfr 301.6321-1: Lien for Taxes
Rev.Rul. 68-57

The Federal Tax Lien Act of 1966, P.L. 89-719, C.B. 1966-2, 623, does not refer to a purchase money security interest of mortgage. However, the General Explanation of the Act, as set forth in House of Representatives Report No. 1884, C.B. 1966-2, at page 817, states as follows:

Although so-called purchase money mortgages are not specifically referred to under present law, it has generally been held that these interests are protected whenever they arise. This is based upon the concept that the taxpayer has acquired property or a right to property only to the extent that the value of the whole property or right exceeds the amount of the purchase money mortgage. This concept is not affected by the bill.

In view of the legislative history of the Federal Tax Lien Act of 1966, the Internal Revenue Service will consider that a purchase money security interest or mortgage valid under local law is protected even though it may arise after a notice of Federal tax lien has been filed.

