

## Can I get rid of my back income taxes with a bankruptcy?

We all know that "Nothing is certain but death and taxes", but the fact is that back income taxes may not stay around as long as death. Let's look at when back income taxes may be discharged (eliminated) with a bankruptcy. "Discharged" means they are eliminated, quickly in a Chapter 7 bankruptcy or over three or five years after making payments to the bankruptcy trustee in a Chapter 13 bankruptcy. It's the same for federal (IRS) or state income taxes.

**Back income taxes owed are discharged in bankruptcy if they meet all of the following rules.** This is not simple stuff because, as you'll see, there are "gotcha's" waiting in the wings.

### Three Year Rule

The tax return was due more than three years before filing bankruptcy.

For example, looking at tax year 2008, if there was no extension, you start counting on April 15, 2009, when the return was normally due. The bankruptcy for that tax year 2008 can be filed on or after April 16, 2012 to satisfy the Three Year Rule.

Note that the due date can include extensions (out to October 15), and also if the due date is the 15th and that day is a Sunday, then the due date is the 16th.

### Two Year Rule

The income tax return for that tax year must have been filed more than two years before filing bankruptcy. The Two Year Rule applies to all tax returns that were filed late, including those filed late without obtaining an extension that would have made the filing not late. Although the Three Year Rule above considers the age of the tax, the Two Year Rule only deals with the date the return was actually filed.

Late-filed income tax returns filed after the due date are considered filed on the date the taxing authority actually receives the return. The two-year time period starts to run on the date that IRS or California Franchise Tax Board actually receives the return.

Also, the IRS may file a substitute return you if you don't file the return. You can consent to the return by signing it, or the IRS can file the return without your consent. If you don't sign the IRS-prepared return, it does not count as a filed tax return for purposes of the two-year filing rule. However, if you do sign the return, it will count as a filed return for purposes of the Two Year Rule.

### 240 Day Rule

The income taxes were assessed (if they were assessed) by the IRS (or California FTB) more than 240 days prior to the bankruptcy filing.

### The Fraud Rule

You did not file a fraudulent return or willfully attempt to evade paying taxes.

### Events that Toll (Stop) the Time Periods

Certain events may interrupt the running of the three-year, two-year, or the 240-day rules. Essentially, any event that prevents the taxing authority from collecting the tax serves to toll the running of the respective discharge time limits.

**Offers in Compromise:** An offer in compromise extends the 240-Day Rule by the number of days the offer in compromise is pending, plus an additional 30 days.

**Prior Bankruptcies:** The filing of a bankruptcy also tolls the 240-day rule. If a debtor files bankruptcy, the 240-day time period is extended by the number of days the bankruptcy is pending, plus an additional 90 days.

**Request for a “Due Process” hearing:** Both the three-year rule and the 240-day rules are tolled if a taxpayer makes a request for a due process hearing after a notice of assessment pursuant to IRC §§ 6320, 6330.10 The amount of time that the rules are tolled is equal to the full amount of time that the appeal was pending plus 90 days.

**Tax Installment Plans are not tolling events.** You can make installment plan payments with the IRS and then file bankruptcy after the time limits have run.

### **Conclusion**

As I said earlier, this isn't simple. It requires that you get an IRS "account transcript" and a similar item for your state taxing authority. Your bankruptcy attorney will examine the transcripts and tell you if it's likely that the taxes will be discharged in your bankruptcy.

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