

NAFER Leads the Way to Advance Legislation Expediting Receivership Tax Returns

By N. Neville Reid and Ira Bodenstein

Introduction – The Unjust Inequality in the Law That Must be Fixed

As receivers, we are skilled at liquidating claims and assets to return as much money to victims as possible, a measure of “economic justice” for them that gives each of us much professional and ethical satisfaction. We don’t get them into these fraudulent investments, but are grateful when we can get them substantially out. However, as we all know, such economic justice is tempered by the reality that we cannot make all of our distributions until the Internal Revenue Service (IRS) approves our federal returns, a process that can take up to three years or longer in some cases.

There is a painful unjust asymmetry in our current insolvency system. Assume Investor A puts a substantial sum of her life savings in a business run

by someone else that turns out to be a fraudulent “Ponzi scheme” through no fault of her own. If the business later lands in bankruptcy court in which a trustee is appointed to liquidate assets and distribute the proceeds to Investor A and the other victims, under the Bankruptcy Code there is a mechanism for a trustee to have the IRS fast track its review and determination (collectively, the “Tax Determination”) regarding the trustee’s tax returns so that the victims/creditors can get their money as soon as possible. By contrast, assume Investor B invests the same amount of money as Investor A in a different enterprise that also turns out to be a fraudulent scheme, but the case lands in a non-bankruptcy court and a receiver is appointed to do the same job of pursuing recoveries for the victims as the bankruptcy trustee would do were the case in bankruptcy

court. In Investor B’s case, the IRS has no obligation to fast track the Tax Determination regarding the receiver’s tax returns for the estate. Under the current statutory framework, the receiver must often wait for the expiration of the three-year statute of limitations on Tax Determinations in order to safely complete the distributions of liquidation proceeds to victims.¹ Consequently, Investor B is *victimimized twice* – first by the fraud and then by the delay caused by the absence of any statutory fast track mechanism for Tax Determinations in receivership cases.

There is no good policy reason why Investor B must wait possibly up to three years longer than Investor A to receive a distribution merely because Investor B’s distribution is through a non-bankruptcy court. The disparate treatment of

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About The Authors

N. Neville Reid



N. Neville Reid is a capital partner who co-chairs the Bankruptcy, Restructuring and Creditors’ Rights Group at Fox Swibel in Chicago. He has represented a wide array of clients in all aspects of bankruptcy, restructuring, insolvency and creditors’ rights cases and transactions for over 34 years. He has been a bankruptcy panel trustee (for chapter 7 and chapter 11 bankruptcy cases) since 1994, and in that capacity frequently investigates and recovers fraudulent transfers and various assets for the benefit of creditors of corporate entities and individual debtors.

Ira Bodenstein



Ira has a keen understanding of the trustee process and how to efficiently achieve the optimum resolution for the involved parties. He counsels bankruptcy clients on the necessity and timing of filing reorganization cases, and the rights of unsecured and secured creditors prior to and subsequent to bankruptcy filing. Ira is experienced in all facets of Chapter 11 reorganization cases, including preparing and confirming plans of reorganization in debtor cases, representing creditors’ committees, opposing debtors’ plans on behalf of creditors, and representing creditors and debtors in preference and fraudulent conveyance litigation. He also counsels lenders on their rights as secured creditors.

these two investors is a gross inequity in the law that daily burdens thousands of innocent investors and other victims of fraud throughout the country. Often these defrauded investors have invested their life savings in the fraud and now need their distributions to live, retire, support children or grandchildren, and/or pay bills.

Working with our stellar lobbyists over the past 18 months (Jim Moran and Ryan Dattilo), NAFER's Legislative Committee, Co-Chaired by Neville Reid and Ira Bodenstein, has drafted and advanced the Federal Receivership Fairness Act, which proposes the obvious fix to this unjust inequality by creating the same parallel fast track statutory mandate for receivers' tax returns as the IRS must already undertake in bankruptcy cases.² Insofar as the bankruptcy fast track mechanism has been around for over 46 years and has worked smoothly to expedite distributions to victims and creditors, there is every reason to think the parallel fast track mechanism will work equally well, justly, and efficiently in receivership cases. The Bill has broad support among various professional organizations, including the Turnaround Management Association, the National Association of Bankruptcy Trustees, the American Bankruptcy Institute and the Association of Insolvency and Restructuring Advisors.

Summary of the Bill

The Bill is premised on Section 505 of the Bankruptcy Code, 11 U.S.C. § 505, which works as follows:

1. A bankruptcy trustee³ may request a determination by the IRS as to whether any greater tax is owed than the tax admitted to be owed on a return that the trustee submits to the IRS.⁴
2. Upon receiving a request for a determination, the IRS has 60 days to either respond to the request or indicate that the return has been selected for "an examination."⁵
3. Absent an extension, if the IRS (i) fails to notify the trustee within such 60 day period that the return has been selected for an examination, or (ii) fails to complete such an examination within 180 days after the trustee's initial request for a determination (or such later date as the court sets "for cause"), then the trustee, the estate and the underlying bankruptcy debtor are discharged from any liability for any unpaid tax on the return other than the tax the return indicates is owed. The discharge does not apply if the return is fraudulent or contains a material misstatement.⁶
4. The bankruptcy court has jurisdiction and authority to decide any dispute between the trustee and the IRS

regarding unpaid tax liability of the debtor or the estate.⁷ Sovereign immunity is waived so that the IRS is subject to the bankruptcy judge's order resolving any tax disputes with the trustee.⁸

The Bill contains substantively the same language as § 505 summarized above, using the term "receiver" in place of the trustee and the "receivership estate" in the place of "estate". The Bill would be effective as to all current and future receivership returns submitted to the IRS for review, and waives sovereign immunity so that the IRS is subject to the order of the non-bankruptcy court⁹ resolving any tax dispute between the receiver and the IRS.

Current Status of the Bill

In the House, the Bill has bipartisan co-sponsors, Reps. Darin LaHood (R. - IL), Eugene Vindman (D. - Va.) and Donald S. Beyer, Jr. (D. - Va.). There has not yet been a bill introduced in the Senate, but there is growing bipartisan support there, including from Senator Mark Warner (D. - Va) who has agreed to co-sponsor it when it is formally introduced. While Congress is currently actively engaged on many other pressing issues, our lobbyists Jim and Ryan are cautiously optimistic that the Bill will substantially advance in both chambers by the end of this year. Let's hope this is the year when timeliness of economic justice for similarly-situated fraud victims will be unaffected by the forum in which that justice is sought.

ENDNOTES

¹ For federalism purposes, only federal courts will decide the dispute between the receiver and the IRS as to federal taxes. The bill bars state courts from resolving such disputes. However, it does currently allow federal courts to resolve disputes as to federal taxes owed by state court receivers, and requires that any such disputes be removed from state court to federal court.

² See *Federal Receivership Fairness Act*, H.R. 5146, 119th Cong. (2025).

³ Section 505 also fast tracks returns for cases in which a debtor has filed for bankruptcy but a trustee has not been appointed, such as "debtors in possession" under chapter 11.

⁴ See *id.* § 505(b)(2).

⁵ See *id.* § 505(b)(2)(A)(i).

⁶ See *id.* § 505(b)(2)(A)(i), (ii).

⁷ See *id.* § 505(a).

⁸ See 11 U.S.C. § 106(a)(1).

⁹ A receiver who makes a distribution during this period of uncertainty runs the risk of facing personal liability under federal law for federal taxes owed by the receivership estate for which she serves as a fiduciary. See 31 U.S.C. § 3713(b).