Settling Tax Debt: Offers in Compromise

Course #3132A

Taxes

2 Credit Hours

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SETTLING TAX DEBT: OFFERS IN COMPROMISE

This course covers major tools that can be used to settle tax debts with the IRS. Topics include: the grounds for seeking, applying for, appealing, and rejecting an Offer in Compromise.

LEARNING ASSIGNMENTS AND OBJECTIVES

As a result of studying each assignment, you should be able to meet the objectives listed below each individual assignment.

SUBJECTS

Grounds for Seeking an Offer in Compromise
Applying for an Offer in Compromise
Rejecting Offers in Compromise
Financial Analysis of Offers in Compromise

Study the course materials from pages 1 to 90

Complete the review questions at the end of each chapter

Answer the exam questions 1 to 10

Objectives:

- Identify different methods the IRS can use to settle claims
- Recognize steps in the process of applying for an Offer in Compromise
- Identify how long a taxpayer has to appeal an Offer in Compromise
- Recognize some of the factors the IRS considers in determining the amount the taxpayer should be able to pay under a Doubt as to Collectibility Offer in Compromise

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EXAM OUTLINE

- **TEST FORMAT:** The final exam for this course consists of 10 multiple-choice questions and is based specifically on the information covered in the course materials.

- **ACCESS FINAL EXAM:** Log in to your account and click Take Exam. A copy of the final exam is provided at the end of these course materials for your convenience, however you must submit your answers online to receive credit for the course.

- **LICENSE RENEWAL INFORMATION:** This course qualifies for **2** CPE hours.

- **PROCESSING:** You will receive the score for your final exam immediately after it is submitted. A score of 70% or better is required to pass.

- **CERTIFICATE OF COMPLETION:** Will be available in your account to view online or print. If you do not pass an exam, it can be retaken free of charge.

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CHAPTER 1: GROUNDS FOR SEEKING AN OFFER IN COMPROMISE

Chapter Objective

After completing this chapter, you should be able to:

- Identify different methods the IRS can use to settle claims.

I. OVERVIEW

In many ways, the IRS is like any other creditor. They want to get paid everything they are owed. Like other creditors, however, they sometimes realize that it is impossible to collect all or a portion of a debt. It is in such a case that the IRS will consider allowing a taxpayer to enter into an Offer in Compromise (OIC). An OIC is an agreement between a taxpayer and the IRS that settles the taxpayer's tax liabilities for less than the full amount owed. An OIC is generally not accepted if the IRS believes the liability can be paid in full, either as a lump sum or through a payment agreement. The IRS looks at the taxpayer's income and assets – as well as a variety of other factors – to make a determination of the taxpayer's reasonable collection potential.

On the IRS website, there is an Offer in Compromise Pre-Qualifier tool. A taxpayer may use this tool to see if he or she may be eligible for an Offer in Compromise. The taxpayer enters his or her financial and tax filing status to calculate a preliminary offer amount. Note that the IRS makes its final decision based on the taxpayer's completed OIC application and the IRS's associated investigation. This tool should only be used as a guide. Although it may show that a taxpayer can fully pay his or her liability, he or she may still file an OIC and discuss his or her individual financial situation with the IRS.

A. GROUNDS FOR OFFERS IN COMPROMISE

The Internal Revenue Code gives the IRS very broad authority to compromise federal tax liabilities (IRC Section 7122). Specifically, the IRS is authorized to settle claims in one of three circumstances:[1]

- Doubt as to Collectibility (DATC);
- Doubt as to Liability (DATL); or
- Effective Tax Administration.

IRS Policy Statement P-5-100 states:

> *The Service will accept an offer in compromise when it is unlikely that the tax liability can be collected in full and the amount offered reasonably reflects collection potential.*

1. Treasury Regulation § 301.7122-1.

An OIC is a legitimate alternative to declaring a case currently not collectible or to a protracted installment agreement. The goal is to achieve collection of what is potentially collectible at the earliest possible time and at the least cost to the Government.

In cases where an OIC appears to be a viable solution to a tax delinquency, the Service employee assigned the case will discuss the compromise alternative with the taxpayer and, when necessary, assist in preparing the required forms. The taxpayer will be responsible for initiating the first specific proposal for compromise.

The success of the compromise program will be assured only if taxpayers make adequate compromise proposals consistent with their ability to pay and the Service makes prompt and reasonable decisions. Taxpayers are expected to provide reasonable documentation to verify their ability to pay. The ultimate goal is a compromise that is in the best interest of both the taxpayer and the service. Acceptance of an adequate offer will also result in creating for the taxpayer an expectation of a fresh start toward compliance with all future filing and payment requirements.

The three circumstances under which the IRS may enter into an OIC each further, in some way, the objectives of the OIC program. Those objectives are to:

- Facilitate collection of what can reasonably be collected at the earliest possible time and at the least cost to the government;
- Achieve a resolution that is in the best interests of both the taxpayer and the government;
- Provide the taxpayer with a fresh start toward future voluntary compliance with all filing and payment requirements; and
- Secure collection of revenue that may not be collected through other means.

B. GENERAL RULES

1. Deal Must Be Good for IRS

The IRS will generally approve an offer in compromise when the amount offered represents the most they can expect to collect within a reasonable period of time. There are some precise calculations involved in coming up with that number that will be explored in great detail later. As with all choices, there are pros and cons to an OIC for a delinquent taxpayer, so a tax advisor should consider all options for their client before applying for an OIC. There are also eligibility criteria, i.e., a taxpayer in the midst of a bankruptcy proceeding is not eligible for an OIC.

2. Where Offers Must Be Denied

The IRS generally does not have the authority to accept an OIC when:

- Questions concerning the amount of the taxpayer’s liability or the collection of a liability for all or part of the periods the taxpayer owes is in litigation being handled by the Department of Justice;

- The federal tax liability for all or part of the periods the taxpayer owes has been reduced to a judgment;

- An offer is received that covers tax periods for which restitution was ordered. The IRS cannot accept an OIC that in any way modifies the terms of a restitution order. The IRS may consider an OIC for periods for which restitution was ordered only if the defendant has paid or will pay the full amount of the restitution as part of the offer;

- The IRS has a civil or criminal prosecution pending against the taxpayer in the Department of Justice or U.S. Attorney's Office; or

- Acceptance by the IRS is dependent upon the Department of Justice accepting a related offer or settlement.

Another limitation is that offers based on Doubt as to Collectibility or Effective Tax Administration must include all unpaid tax liabilities and periods for which the taxpayer is liable.

Example

If a taxpayer submits an OIC for income tax liabilities and the taxpayer is also responsible for employment taxes for a sole-proprietorship, both the income tax and business liabilities must be included in the accepted offer.

An OIC is effective for the entire assessed liability for tax, penalties, and interest for the years or periods covered by the offer. All questions of tax liability for the years or periods covered by the agreement are conclusively settled. Neither the taxpayer nor the government can reopen a compromised tax year or period unless there was falsification of information or documents, concealment of ability to pay, or a mutual mistake of a material fact which would be sufficient to set aside or reform a contract.

3. Unassessed Liability

The IRS will not consider an offer that is solely for a tax period or tax year that has not been assessed unless a return has been received or an assessment is pending. Taxpayers may submit, and the IRS will consider, an offer to compromise taxes due on tax returns which have been filed but have not yet been assessed when unpaid liabilities already exist. However, before the offer can be accepted, the unassessed taxes must be assessed.

4. Lapsed Statute of Limitations

If the statute of limitations has passed, the taxpayer is obviously not obligated to pay. Therefore, the IRS will not enter into a compromise when the taxpayer is indeed no longer liable for the tax. If a taxpayer makes a voluntary payment to a liability barred by statute, the IRS is required, pursuant to the Internal Revenue Manual, to inform the taxpayer that the payment is not required and ask if they want the payment applied to their account or returned. The taxpayer must be advised that the payment is purely voluntary.