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Helping Your Clients With Offers in Compromise



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What is an Offer In Compromise?

- **Internal Revenue Code (IRC) § 7122**
- An agreement between the taxpayer and government
- To settle a tax liability
- For payment of less than the full liability amount



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Basis for Granting an OIC

- Doubt as to liability
- Doubt as to collectibility
- Effective Tax Administration (ETA)

Treas. Reg. § 301.7122-1(b)



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Forms and Payments for Application

- Form 656 or 656-L accompanied by:
 - Form 433-A (OIC)
 - Form 433-B (OIC)



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Forms and Payments for Application (Cont.)

- Application Fee - \$186.00 as of 1/1/2014
 - Notice 2006-68
 - Not refundable
 - Waived for individual taxpayers who qualify for the low-income exception
- Not applicable for DATL OICs



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Forms and Payments for Application (Cont.)

- Lump–Sum OIC: 20% of the offer at the time of application
- Periodic Payment OIC: First proposed installment payment must be included with application



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Low-Income Certification

- **Form 656, Section 4**
- Taxpayer's income is less than 250% of the poverty level
- Fees/payments associated with OICs not required while OIC is pending



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Doubt as to Liability Offer

- Genuine dispute as to the existence or amount of liability under law
- Submitted on Form 656-L
- No financial statement required
- No application fee or initial offer payment required



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Doubt as to Collectibility

- Taxpayer's assets and projected future income are less than the total liability
- Meets or exceeds reasonable collection potential (RCP)
- May be accepted for less than RCP if special circumstances exist
- Submitted on Form 656



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Doubt as to Collectibility with Special Circumstances

- DCSC qualifications
- Factors establishing special circumstances
- IRM 5.8.4.3



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Calculating Reasonable Collection Potential

- Calculation of RCP is the same for both DATC and DCSC offers
- $RCP = \text{Value of Taxpayer's Assets} + \text{Future Disposable Income (FDI)}$
- Reasonable – Doesn't include maintenance of an affluent or luxurious standard of living



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RCP Assets and Future Disposable Income

- Assets include all of taxpayer's assets:
 - Assets available to TP but beyond IRS's reach; and
 - Assets collectible from third parties
 - Exclude value of assets exempt from levy
- Future Disposable Income:
 - $FDI = \text{Gross income} - \text{necessary expenses}$
 - Use schedules of national and local standards to determine allowed basic living expenses



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Effective Tax Administration Offers in Compromise

- Same submission requirements as a DATC OIC
- No doubt the tax is owed and
- No doubt that the full amount owed can be collected from the taxpayer



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ETA Offers in Compromise, cont.

- Economic Hardship ETA
 - Taxpayer may qualify for an ETA offer when their RCP is greater than the liability but collecting the full amount would result in economic hardship
- Non-Economic Hardship ETA
 - Taxpayer presented facts that would support acceptance under the public policy/equity basis
- Compromise would not undermine compliance with tax laws



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Non-Economic Hardship ETA

- **Non hardship ETA offers must demonstrate:**
 - The taxpayer has remained in compliance since incurring the liability
 - Overall their **compliance history** does not weigh against compromise



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Non-Economic Hardship ETA, cont.

- The taxpayer must have **acted reasonably and responsibly** in the situation giving rise to the liabilities
- The circumstances of the case must be such that other taxpayers would view the compromise as a **fair and equitable result**



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ETAs in Situations Involving Criminal or Fraudulent Acts of Third Parties

- Criminal or fraudulent acts of a third party are directly responsible for the tax liability
- Actions and Impact of Third Party Can Be Documented
- Taxpayer Misled to Believe Taxes Were Paid



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ETAs in Situations Involving Criminal or Fraudulent Acts of Third Parties, cont.

- Funds to Pay Taxes Were Available
- Taxpayer's Compliance Has Otherwise Been Good
- Taxpayer took reasonable precautions to prevent the criminal or fraudulent acts at issue



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When might a Non-Hardship ETA be appropriate?

In a third party payer arrangement where the Payroll Service Provider PSP did not deposit payroll taxes.



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What is a Third Party Payer?

- Third party agrees to take over some or all of employer's federal employment tax withholding, reporting and payment obligations
- Some common third party arrangements include:
 - Payroll Service Provider
 - Reporting Agent
 - Section 3504 Agent (Aggregate Filer)
 - Professional Employer Organization



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ETA Offers Due to IRS Error

- Compromise may promote ETA where a taxpayer's liability was directly caused by a processing IRS error and would otherwise have been avoided
- Compromise may promote ETA where the taxpayer incurred the liability because they followed erroneous advice or instructions from the Service



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ETA OICs Due to IRS Error, cont.

- If actions or inaction of the Service unreasonably delayed resolution of the taxpayer's case and interest or penalty abatement is not available, compromise may still be warranted if the circumstances are sufficiently compelling.



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OIC Outcomes

- Returned
- Denied
- Granted
- Withdrawn

IRS must rule on OIC request within 24 months or it is deemed accepted. IRC sec. 7122(f).



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While an Offer is Pending

- No levy while offer pending, for 30 days after rejection or, during appeal of rejection
 - Other collection action OK
 - Do not have to release prior levies
- Suspension of the collection statute of limitations
- No proceedings in court to collect
- Statute begins running again when accepted



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OIC Not Processable - Returned

- TP is in bankruptcy
- TP has not paid the application fee or qualified for fee waiver
- TP has not submitted the required partial payment or qualified for its postponement
- Liability has been referred to DOJ
- Liability has not yet been assessed



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Processable OIC -Returned

- Failure to provide necessary or requested financial information
- Failure to file all required tax returns
- Failure to make required estimated tax payments
- Failure to make required Federal Tax Deposits
- OIC submitted to delay collection



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OIC Outcomes - Rejection

- Offered amount does not equal or exceed RCP or special circumstances are not substantiated.
- IRS issues pre-rejection letter prior to official rejection letter.
- Taxpayer has 30 days from days of date of rejection letter to request a hearing with the IRS Office of Appeals.



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OIC Outcomes - Withdrawn

- A taxpayer may withdraw an OIC
- Payments are not made according to the proposed schedule while the offer is pending – mandatory withdrawal



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OIC Outcomes - Acceptance

- The taxpayer must follow all terms proposed in the accepted offer
- IRS Office of Chief Counsel review is required for all acceptances of OICs where compromised liability \geq \$50,000



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Future Compliance

- Five years of compliance following the completion of the OIC terms
- Notice of Federal Tax Lien released upon final payment



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OIC Termination

- OIC may be terminated if taxpayer defaults on an offer term:
 - Fails to pay offer amount
 - Fails to pay collateral agreement amount
 - Fails to return an erroneous refund
 - Fails to file returns and make payments in full compliance with the provisions of OIC



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OIC Rescission

- An accepted OIC can be set aside if:
 - False information or documents supplied
 - Taxpayer conceals assets or ability to pay
 - Mutual mistake of material fact
- IRM 5.8.9.2



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Contact TAS

- Call 877.777.4778
- File Form 911, *Request for Taxpayer Advocate Service Assistance (And Application for Taxpayer Assistance Order)*
- Megan Kenney, Attorney Advisor, National Taxpayer Advocate –
Megan.B.Kenney@irs.gov



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