

Offer in Compromise



Overview

- Three types of offers
- Offer requirements
- Benefits/risks of the offer program
- Financial analysis
- Reasonable Collection Potential (RCP)
- Payment methods
- Tips for submitting offers

What an Offer is Not

- Auction
- Bid
- Let's Make a Deal
- Let's Send Something In to See If They Take It

What an Offer Is

- A mathematical calculation
- Amount offered reasonably reflects collection potential (RCP).
- Unlikely tax liability will be collected in full.
- First hurdle: can the taxpayer pay in full
 - Equity in assets
 - Through a payment agreement over CSED

Types of Offers

- Doubt as to Liability – I don't owe it
- Doubt as to Collectibility – I can't pay it all
- Effective Tax Administration
- Doubt as to Collectibility Special Circumstances

Doubt as to Liability

- Form 656L
- Can't Use if Tax Liability Established by Tax Court

Doubt as to Collectibility

- Form 656
- Form 433A (OIC) and/or 433B (OIC)
- Attachments
- Mail to IRS OIC Unit in the Service centers
- Copy to revenue officers

Effective Tax Administration

- RCP is greater than liability but economic or public policy or equity issues exist
- Long term illness
- Can't meet basic living expenses
- Can't borrow against assets
- Old age
- Liquidation of assets leaves them penniless

Special Circumstances

- Cannot fully pay the tax liability but have special circumstances warranting acceptance of less than RCP

Comparison

- ETA Offer
 - Tax liability = \$100,000
 - RCP = \$150,000
 - Offer amount accepted = \$75,000
- Special Circumstances Offer
 - Tax liability = \$100,000
 - RCP = \$80,000
 - Offer amount accepted = \$50,000

Is the Offer Processable?

- Taxpayer is in Compliance
- All tax returns are filed
- Estimated tax payments being made
- Federal Tax Deposits being made
- Not in bankruptcy
- Not trying to compromise criminal restitution

Risks / Benefits

- CSED stops running – CSED extended if OIC not accepted
- Roadmap to client's finances
- Future non-compliance with OIC terms

- Stops collection activity
- Permanent contract
- Fresh start – tax liability gone

Can IRS File a NFTL?

- Yes – not considered a collection action
- Levy action stops
- Installment agreement payments can stop
- IRS can immediately reject is deemed to delay collection.
 - Example: \$100 on a \$100,000 tax liability with \$50,000 equity.

Financial Analysis

- Form 433A (OIC) – DATC and ETA/SC
- Form 433B (OIC) – including single member LLC
- Penalties of perjury
- Fill in all blocks and lines – N/A or \$0.00

Equity Component

- Fair Market Value
- X 80% Quick Sale Value
- - Encumbrance
- = Equity

$\$200,000 \text{ FMV} \times 80\% = \$160,000 - \$50,000$
Encumbrance = \$110,000 Equity for OIC purposes

exclusions

- \$1,000 reduction to personal bank account amounts
- \$3,450 exclusion per vehicle, up to two vehicles
- Household contents not included
- Equity in income-producing assets

Income Component

- Gross Wages/Net Monthly Income
- Less Allowed Living Expenses
- Net Difference

- Net Difference x 12 if OIC paid within 5 months
- Net Difference x 24 if OIC paid within 24 months

Income Component Example

- Gross Monthly Wages = \$10,000
- Allowed Living Expenses = \$8,000
- Net Difference = \$2,000

- Pay OIC within 5 months: $\$2,000 \times 12 = \$24,000$
- Pay OIC with 24 months: $\$2,000 \times 24 = \$48,000$

Reasonable Collection Potential

- What IRS can collect from
 - Equity in Assets
 - Income
 - Business Equity
 - Business Income
- Example: Client has \$10,000 in bank and \$5,000 equity for OIC purposes in residence. Wants to offer only \$10,000.

Financial Analysis

- List all assets
- Determine FMV of each asset
- Determine encumbrances against each asset
- Multiple FMV by 80% QSV
- Subtract encumbrances
- Subtract any taxes if asset liquidated, e.g., IRA
- Result = RCP of assets

Dissipation of Assets

- Assets disposed of within last 3 years not for health and welfare or production of income.
- Examples:
 - Liquidated IRA 3 years ago to pay for daughter's wedding (FMV will be included in RCP)
 - Sold vacant land to take European vacation (FMV will be included in RCP)
 - Sold residence and used money to pay for medical expenses (FMV will not be included in RCP)

Paying the Offer

- Lump Sum Offer
 - Pay offer amount within 5 months of date of letter of acceptance

- Periodic Payment Offer
 - Pay offer amount within 24 months of acceptance
 - Payments made while offer is pending
 - Example: \$24,000 offer amount, \$1,000 submitted with Form 656 and \$1,000 payable each month thereafter until the offer is accepted

review

- Can client full pay through equity and/or payment agreement? Calculate CSED. Yes – no offer
- Is client in current compliance? No – no offer
- Can client fund the offer? Borrow all or some of the money
- Knock down FMV of assets

review

- Apply collection financial standards to expenses
- Calculate best and worst case scenarios
- Identify challenges to acceptance
- Cover letter describing clients and financial condition


