Arizona Tax Essentials:
Will the Offer In Compromise Work for You?

By Lawrence 'D' Pew, [AZ Tax Resolution Attorney]

Maybe you recently overheard some tax chatter in the break-room or at your local watering hole about the *IRS' offer in compromise (OIC)* program. Word is out! The OIC is an effective way for delinquent taxpayers to seek a reduction in the amount of back taxes they owe to the U.S. Treasury. When paying your full tax liability would create a financial hardship or if there is simply no way you can pay what you owe, then an offer in compromise may be the solution.

This segment of the Pew Law Center's Arizona Tax Essentials series will focus on several important aspects of the OIC, including how taxpayers utilize this IRS program to reduce their overdue tax burden.

What Is the Offer in Compromise Program?

The offer in compromise (OIC) is a settlement agreement between the IRS and the taxpayer – individuals and businesses may use the program, which is purely voluntary. The "offer" in the OIC comes from the taxpayer who offers less than the entire tax obligation. The "compromise" comes into play when the IRS accepts less than what the taxpayer owes in taxes.

Why would the IRS agree to accept less money? Accepting a reasonable offer saves on agency resources, avoids further delays in tax collection, and avoids the necessity of taking further action (such as imposing a tax lien against the person's assets). Needless to say, there are incentives on both sides of the isle to cooperate. For the IRS to take the taxpayer's OIC seriously, however, the offer must satisfy specific criteria.

What Are the Grounds Supporting an Offer in Compromise?

To be considered by the IRS, the taxpayer's offer must fit into one or more of the following three grounds:

- ***Taxpayer does not have the money to pay the tax debt.*** There is doubt that more than the offered amount can be collected from the taxpayer.

- ***Taxpayer does not owe what the IRS is trying to collect.*** There is a verifiable doubt as to the amount the taxpayer owes.

- ***Compromise is expedient for the IRS.*** There is a need to promote effective tax administration.

The OIC settles the tax liability for less than the full amount owed. Consequently, if the IRS is convinced that the taxpayer is capable of paying the total tax obligation in a lump sum or through installments under a payment plan, then the OIC will not be accepted.

How Does the Taxpayer Submit an Offer in Compromise to the IRS?
The offer in compromise application package in IRS Form 656 includes two forms used to calculate the amount of the offer. The eligible *individual taxpayer* files IRS Form 433-A (OIC); the eligible *business taxpayer* files IRS Form 433-B (OIC).

You may be wondering what it means to be an "eligible" taxpayer. To be eligible for the OIC program, the taxpayer:

- Must have filed every tax return that the person was legally required to file.

- Must have made all estimated tax payments for the current tax year.

- For businesses with employees, must have made all federal tax deposits for the current tax quarter.

Along with the completed OIC application, the taxpayer must include a *$150 application fee* (this fee may be waived for low income applicants).

How Is the Offer in Compromise Processed?
Once the complete OIC is received by the IRS, an investigator is assigned to the taxpayer's case. The investigator is expected to make prompt and reasonable decisions; the taxpayer is expected to provide documentation to verify his or her ability to make the OIC payments. Should the investigator conclude that the taxpayer's offer is not supported by the financial evidence, the offer may be rejected or a different payoff amount with different terms may be negotiated – that is, the IRS makes a counteroffer.

If the OIC is rejected, the taxpayer has 30 days to appeal the IRS decision. If the case "falls between the cracks" and the taxpayer does not get a determination from the IRS within two years of its having received the OIC, then the offer is automatically accepted. When the OIC is accepted, the taxpayer must timely file all tax returns and pay all taxes for the next five years to avoid default.

Most people are unprepared to enter into negotiations with the IRS or pursue an appeal without legal representation. This is why having a knowledgeable tax resolution attorney like Lawrence 'D' Pew involved from the very beginning of the process is invaluable and, quite often, essential to a successful OIC outcome.

Does the Taxpayer Provide Financial Documentation With the OIC?
In determining whether to reject, counteroffer, or accept the taxpayer's offer in compromise, the IRS assesses the offeror's ability to pay and closely examines documentation of assets, income and projected income, and monthly allowable living expenses. After applying an OIC settlement formula, the resulting monthly dollar amount reflects what the taxpayer can actually pay on the tax liability. What the offeror can actually pay is the amount the IRS will accept in compromise – no more, no less.

The amount offered in compromise must be equal to or greater than the *reasonable collection potential*. The IRS does not want to be in the position of trying to collect beyond the 10-year statute of limitations period for tax collections. Therefore, the OIC should be for an amount that can actually be paid off in full within the statutory period.

This is important! To get the IRS to accept an offer in compromise, it is essential that the taxpayer persuade the investigator that the OIC is necessary because the full amount owed in taxes cannot be paid within the 10-year collection period. The IRS' goal is to collect whatever money is potentially available, in the shortest period of time, with the least expense to the federal government.

As with so many IRS forms, the challenge is as much about gathering and presenting all of the information and documentation as it is about completing the requisite forms. Seeking help from a tax professional to complete the offer in compromise process will save time, money, and stress over the long run.

Should the Taxpayer Include an Initial Payment?

Along with the forms and supporting documentation, the taxpayer must include an initial payment. In addition to the $150 application fee, the amount of the non-refundable initial payment will depend upon whether:

> ***1. The OIC is for five or fewer payments.*** At least 20% of the total amount offered must be included with the OIC; or,
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> ***2. The OIC is for more than five monthly installments.*** At least one month's installment must accompany the offer. The taxpayer must continue making payments, though, while the IRS evaluates the OIC.

With either of these alternatives, when the taxpayer is certified as low-income the initial payment that would ordinarily accompany the OIC is waived.

The OIC process – from submission of all forms and documentation to the final approval and finalization – may take a year to two years to complete. Any taxpayer considering the offer in compromise program should consult with a licensed Arizona tax resolution attorney first. That means taking a little time to explore other tax alternatives to the OIC that may be more suitable to the circumstances, less time consuming, and even less costly.

When the offer in compromise *is* the best option, the taxpayer must satisfy the eligibility requirements listed above. Any refund the taxpayer was expecting for the year in which the OIC is accepted will be redirected to pay down the delinquent tax obligation. Although other collection activities will be suspended, the IRS may still file a *Notice of Federal Tax Lien* while the OIC is being considered. And if a tax lien already exists, it will not be released until after the final payment is made under the compromise agreement. Lastly, should the taxpayer default on the OIC, the IRS may revoke the entire agreement and reinstate the original tax obligation, along with penalties and interest.

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Lawrence 'D' Pew is an experienced tax, bankruptcy, and transactional attorney, and founder of the Pew Law Center, PLLC, a leading Arizona tax and bankruptcy law firm focused exclusively on debt relief. With offices in Mesa, the law firm serves Arizona residents in the greater Phoenix area, including Scottsdale, Mesa, Tempe, Gilbert and Chandler. As a client-oriented law firm with a mission to always exceed client expectations, the Pew Law Center has helped over 2,000 people file for bankruptcy and eliminate over $100 Million in debt.
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