Simple Offer In Compromise for Individuals

The starting point for determining whether an Offer In Compromise (OIC) with Doubt as to Collectibility will help solve your tax problem is to analyze the information that you gather on Form 433A. When you have completed form 433A, you will add together the "asset component" and the "Disposable Income" component, and add an "incentive" so the IRS will accept your Offer.

The asset component consists of an amount of money equal to 100% of your assets, at liquidation value. The income component consists of a multiple of any "disposable income", as determined in the gray column on the final page of Form 433A.

The Internal Revenue Manual requires the IRS to get "more than would otherwise be collected." This means you have to add some amount to the total of the asset component and the disposable income component of the Offer. If you have substantial assets or disposable income, I usually recommend adding about 10%. If you have very little assets and no disposable income, then I recommend:

for income of less than $1,000 a month, offer $1,200 ($50 a month for 24 months)
for income of $1,000 to $2,000 a month, offer $2,400 ($100 a month for 24 months)
for income over $2,000 a month, offer $4,800 ($200 a month for 24 months).

Once you have determined how much your Offer would be, compare it to the amount of taxes. If the Offer amount is attractive to you, Prepare Form 656 and submit the Offer to your Revenue Officer or IRS Service Center.

If the Offer would be more than the taxes, forget about an Offer with Doubt as to Collectibility. Your choices now are: Pay the tax, or consider an Effective Tax Administration (ETA) Offer or a Bankruptcy. The ETA used to be called "Hardship" Offer. It is used in very unusual circumstances, and less than one percent of all accepted Offers are ETA.

Complex Offer In Compromise for Individuals

If you are married, and only one of you owes the tax, normally neither the income nor the assets of the other should be used in calculating the Offer. However, you MUST disclose the assets and income of the "non-liable" spouse. This is because you will not be granted an Offer if your spouse has extremely high income (over $100,000 per year) or is very wealthy (this is due to "public policy"–it would not look good for the IRS to forgive the taxes of a person married to a millionaire).

Also, if you live in a Community Property State, and your current spouse does not owe any taxes, but you do, then your "disposable income" component becomes much more complex. Some community property states hold that income from the "non-liable spouse" can be used to satisfy pre-marriage debts of the other spouse. Therefore, the IRS may attempt to count your spouse's income in calculating disposable income. Only rarely, however, is it necessary to get a divorce to overcome this problem. Other circumstances such as previous transfers of assets, etc, can also make an offer more complex. For cases such as those, you probably should call a TaxLand Guide!

them. Your accounts, those of your former spouse, your Children's Christmas Savings Account, your mother's account that your name is on only for convenience, etc. PROVIDE AN EXPLANATION FOR ALL ACCOUNTS THAT YOUR NAME IS ON, BUT ARE NOT YOUR PROPERTY.

YES, YOU DO HAVE TO FILL IN THE LIFE INSURANCE ACCOUNT NUMBERS. REMEMBER, THE BOG IS FULL OF FORMS WITH BLANK LINES. DO NOT LEAVE ANY BLANK LINES.

Section 6. Remember, do not leave any blank spaces. If you do not know the exact amount, put your best guess and put a question mark after it. If there is a judgement, do not leave that line blank because you don't know how much it is. If you really don't know, ask yourself this question:

Is it closer to $500, $5,000, $50,000 or $5,000,000? Whichever one is closer, put that number with a question mark after it. **Fill every blank – an amount, "none" or "not applicable"!**

Section 7. Automobiles: This should be liquidation value. If you have Internet access, go to www.kbb.com (Kelly Blue Book). Find your vehicle, and find the trade in value. If you do not have Internet access, look in the classified ads in your local newspaper. The "current value" you list is 80% of trade in value. DO NOT ASSUME THAT BECAUSE IT DOES NOT RUN YOU DO NOT HAVE TO LIST IT. Old pickups, motorcycles, motorhomes that do not run, boats that you gave away but are still in your name, must all be listed. They WILL check with the Department of Motor Vehicles in your state, and if your name appears on a title you did not tell them about, they will be suspicious of you. LIST EVERY ITEM YOU OWN. They cannot put you in jail for owing taxes. They CAN put you in jail for fraud if you sign Form 433 and intentionally do not tell them about assets you own. NEVER LIE TO THE IRS...

Real Estate: Most of us have a good idea of how much our house would sell for. If you just can't guess, do two things. One, find out how much it is assessed at for tax purposes. Two, ask a Real Estate Agent for a "Market Analysis". They are usually glad to do that for you, hoping to be the agent you call when you sell. For current value, you will put down 80% of Fair Market Value. "Real Estate" includes vacation lots, time shares, vacant land, ANYTHING that your name shows up on, or in which you are entitled to a share of the value, whether or not your name shows up on the title.

For most personal assets, use garage sale values, which is probably 5% of what you paid. If you have really valuable assets (antiques, etc), try to get a purchase appraisal from a dealer. The number you want is the number someone else would pay you, not what it is worth to you (most of us think our antiques are worth more than other people think they are... Here, we need liquidation value, not how much it is worth to us as a memory, etc.) BUT REMEMBER: One of the documents they may ask for is your home owners insurance. You valued it at

Autagua county, and only paying $300 a month, then your allowable housing cost is $300 a month.

For Line 37, there are maximum amounts for car payments and cost of operation (based on regions of the country). The maximum amount you are allowed for the first car payment is the **lower** of your actual payment or $407. Therefore, if you are paying $250 a month, you are only allowed $250 for the payment. If you are paying $700 a month, you are allowed $407. In addition to the car payment, you are allowed a certain amount for gas, insurance, repairs, etc. For Autuaga County, Alabama, you would look at "South Region" and find, for one car, $235. Therefore, if you have only one car, and the payment is $250, you add $250 and $235 to find that your allowable transportation cost is $485.

Everyone is allowed to count one car payment. A second car payment will be allowed ONLY if it is necessary for "production of income", or medical necessity. The maximum allowed for a second auto is $313 a month. With two cars in the South region, you are allowed up to $289 for costs of operation. Therefore, the maximum amount allowed in the South region for a single individual would be $642 ($407 payment, $235 for operation). A family would have a maximum of $1,009; ($407 first payment, $313 second payment, $289 operation).

If you have a business, and use your auto for the business, you may be able to split some of your payments and costs between your business and personal use of the auto, thereby increasing the total cost you are allowed to include.

Note, again, it is the **lower** of allowable or actual. If the allowable auto expense is $235, and you put down $100, then $100 is all you will be allowed.

Line 38, health care depends on how much you are actually spending for current medical necessity. I have seen $1,500 a month allowed in an extraordinary case. However, it must be necessary for **current** care. Payments on past care are not allowed. An exception might be made if payments on the past care are required to continue receiving current care. But such payments would have to be truly required, not merely wished for by a hospital or Doctor.

Line 39 The allowed amount for taxes is what you should be paying now for this year's tax. It includes all required taxes for Federal Income Tax, Social Security, Medicare, and State Income Taxes. No amount is allowed for payments on past taxes.

Line 40. The most common Court ordered payment is child support. Child support, and most other court ordered payments are fully allowable. Note, however, that such payments are allowable only if they are actually being paid. If you are supposed to be paying it, but are not, it does not count.

Line 41. Child/dependent care has to be necessary for the production of income. Paying someone to babysit so you can go play golf everyday works only if you expenses. Suppose this situation:

For Purposes of Illustration, we will use the year 2000 Standards for Autuga County, AL. Work through the following example, using the Standards below. The current standards should be available on the internet. The address is www.irs.gov (NOT .com; that is a private site; it has some good information, but is not as complete as irs.gov). Search for "National Standards". The Standards used below are now outdated, but the new ones work exactly the same. Work through this example to learn how the calculation is performed!.

Total Monthly National Standards

Except Alaska and Hawaii

	Number of Persons				
Total Gross Monthly Income	**One**	**Two**	**Three**	**Four**	**Over Four**
Less than $830	345	466	579	726	+125
$831 to $1,249	391	525	646	762	+135
$1,250 to $1,669	433	630	737	800	+145
$1,670 to $2,499	527	685	781	830	+155
$2,500 to $3,329	554	769	863	924	+165
$3,330 to $4,169	620	830	948	1,063	+175
$4,170 to $5,829	773	957	1,018	1,170	+185
$5,830 and over	991	1,235	1,399	1,473	+195

Financial Analysis - Local Standards: Housing and Utilities (effective 10/1/2000)

Maximum Allowance

County	Family of 2 or less	Family of 3	Family of 4 or more
Autauga County	690	812	934
Baldwin County	717	844	970
Barbour County	604	711	817
Bibb County	646	760	874

insurance policy, because your best friend sells them and said you really need it, since you ride motorcycles every weekend. Your child support payment is $225 a month, and you are fully committed to making that payment. As a single individual making $3,000 a month, your allowance for food, clothing, etc, is $554 a month. So even if you claim you work at a restaurant where they furnish all your food and clothes, you are still spending about $6 a month more than you make.

So, here is how it looks to your Revenue Officer:

Income			Actual	Allowed
24. Wages	$3000	35. Food	600	554
25, Wages (Spouse)		36 Housing & Util	950	690
27. Interest-Dividends		37 Transportation	760	642
28 Net Rental Income		38 Health Care	135	135
29 Pension /Soc Sec		39 Taxes	760	760
30 Pension/Soc Sec		40 Court ordered	225	225
31 Child Support		41 Child care		
32 Alimony		42 Life Insurance	75	
33 Other		43 Other Secured	345	
34 Total	$3,000	44 Other Expense		
		45 Total Living	$3,850	$3,006

In this case, perhaps you can explain it by showing how much you owe on credit cards, or how much your family has been helping you.

Now, let's change the situation a little. You are married, and your spouse works, but you still have only one car. However, you decide to make your husband drive the car and you use your Harley for your work vehicle. That way, you get to count both vehicle payments.

Income			Actual	Allowed
24. Wages	$3000	35. Food	1200	830
25, Wages (Spouse)	1000	36 Housing & Util	1025	690
27. Interest-Dividends		37 Transportation	1159	1,009
28 Net Rental Income		38 Health Care	235	235
29 Pension /Soc Sec		39 Taxes	920	920
30 Pension/Soc Sec		40 Court ordered	225	225
31 Child Support		41 Child care		
32 Alimony		42 Life Insurance	75	
33 Other		43 Other Secured		
34 Total	$4,000	44 Other Expense		
		45 Total Living	$4,839	$3,909

Subtracting Allowed expense of $3,909 from $4,000 of income, the IRS will require a payment of $91 a month. Even this small amount may be difficult to do, since you are already actually spending $4,839 a month out of $4,000

There are several ways to approach the problem. You can set up a payment plan of $91 a month and eat nothing but spaghetti. Another possibility is to ask for a one year temporary plan during which you could reduce your auto expense and housing expense to the allowable amounts. You would have to move to a less expensive apartment where your total cost would be $690 a month, reducing your housing cost. You could refinance your car for a longer period, bringing your car payment down to $407 a month, reducing your transportation cost. After moving and refinancing, the $91 a month should be quite feasible. If this is more complex than you want to tackle, it is time to hire a TaxLand Guide. If none of these options work, you may choose to consider a Bankruptcy.

Some legal ways to reduce the amount of your Offer In Compromise

What is an Offer In Compromise?

It is a business decision on the part of the IRS to accept less than owed.

How much do I have to give them?

An amount of money equal to 100% of your assets, and a lump sum for what they think they could collect on a monthly basis (using their "standards") over the next five years.

What about my 401-k?

You have to give it to them. In the past, you would get to take a reduction for the taxes (30%), and for the 10% penalty if you are under 59 and a half. However, at the present time, the Internal Revenue Manual says you must give them an amount of money equity to the value of the account, *including any value that you owe to the accout!.*

What about the equity in my house?

You have to give it to them. Homestead does not matter. You do get to take 20% off for the cost of selling, and you get to take off the mortgage. So, house is worth $100,000, and you owe $70,000, you give them $10,000 ($100,000 Fair Market Value, times 20%, take $20,000 of $100,000. Value, $80,000, minus $70,000 mortgage, they get $10,000.

What about my CDs?

They get 100%.

Offer Amount Reduction Techniques:

1. Use assets such as cash or CDs to pay off debts. Use the CD and other cash equivalents to pay off credit cards and any and all legitimate debts. **Note: you cannot just give it away, nor hide it. That is fraud. If they prove you did that, they could send you to jail. Do not do that.**

2. Convert it to an asset that shows no value. For instance, when $5,000 in the bank is used for the down payment on a car, it disappears into the depreciation on the car. When a lump sum in an IRA or CD is used to buy an *annuitized* annuity, the equity disappears into a monthly income stream. **Note: you must distinguish between the accumulation phase of an annuity, and the *annuitized* annuity.** An annuity in its accumulation phase is still an asset you can get (if you can get it, you have to give it to them). An annuitized annuity is one where you have converted the lump sum to an income stream. After you do that, you cannot getthe lump sum. If you cannot get it, neither can the IRS.

3. Increase your "allowable expenses". If you do not have health insurance, get some. If you do not have a car payment, get one (but only the "allowable" amount). Only one car payment is allowed, unless more is needed for work or medical reasons