CPA
Practice Advisor

How to Settle Tax Debts With the IRS

Are any of your clients up to their ears in debt to the IRS? Tell them to listen carefully: You don't have to flee the country or pull off a bank heist to get out from under. There are a couple of ways to resolve a tax debt in a reasonable manner ...

Ken Berry • Aug. 18, 2017

Are any of your clients up to their ears in debt to the IRS? Tell them to listen carefully: You don't have to flee the country or pull off a bank heist to get out from under. There are a couple of ways to resolve a tax debt in a reasonable manner, including using the "offer in compromise" program or installment agreements.

OIC program: An offer in compromise (OIC) is an agreement settling tax liability for less than the full amount owed. Usually, the IRS won't accept an OIC unless the amount offered by a taxpayer is equal to or greater than the reasonable collection potential (RCP). The RCP includes the value that can be realized from the taxpayer's assets — such as real estate, automobiles, bank accounts and other property — plus anticipated future income less certain amounts allowed for basic living expenses.

The IRS may accept an OIC based on three grounds:

1. There's doubt as to liability. A compromise meets this requirement only when there's a genuine dispute as to the existence or amount of the tax debt under law.
2. There's doubt that the amount owed is fully collectible. This occurs when the taxpayer's assets and income are less than the full amount of the tax liability.
3. The compromise is based on effective tax administration. To qualify, requiring payment in full would either create an economic hardship or would be unfair and inequitable.

Generally, a taxpayer must submit a $186 application fee. Don't combine this fee with any other tax payments. However, there are two exceptions:

- No application fee is required if the OIC is based on doubt as to liability.
- The fee isn't required if the taxpayer is an individual (not a corporation, partnership or other entity) who qualifies for a low-income exception.

Note: An offer received after March 28, 2017 will be returned without consideration if the taxpayer hasn't filed all required tax returns.

Installment agreements: If a taxpayer can't pay the full amount owed within 120 days, he or she may apply for a installment agreement through an Online Payment Agreement (OPA) or by filing Form 9465 with the IRS. An installment agreement allows you to make a series of monthly payments over time.

The IRS offers various options for making monthly payments, including the following:

- Direct debit from your bank account;
- Payroll deduction from your employer;
- Payment by the Electronic Federal Tax Payment System (EFTPS);
- Payment by credit card via phone or Internet;
- Payment via check or money order; or
- Payment with cash at a retail partner.

The IRS charges a user fee of $225 when you enter into a standard installment agreement or a payroll deduction agreement. If you enter a standard installment agreement and choose to pay via direct debit from your bank account, the user fee is $107. When using the OPA application to request an installment agreement, the user fee is $149. If you use the OPA application to request an installment agreement and choose to pay via direct debit, the user fee is $31, regardless of your income level. Otherwise, certain low-income taxpayers may qualify for a $43 fee.

Note: The user fee for restructuring or reinstating an established installment agreement is $89 regardless of the payment method ($43 for certain low-income taxpayers).

Which method is better? It depends. Installment agreements are generally easier to negotiate. However, with an OIC, any IRS tax liens are removed once the offered amount is paid, while liens remains in effect during repayment under an installment agreement. Work with your clients and the IRS to come to the optimal solution for their situation.