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ECONOMIC HARDSHIP FOR OFFER IN COMPROMISE (OIC) PART B

By Victor Sy, CPA, MBA

Congress mandated the IRS to improve its offer in compromise (OIC) program as part of the IRS Restructuring and Reform Act. Prior laws dictated the IRS to accept your offer in compromise only when there was a doubt as to (1) whether the debt was actually owed, (2) whether it could ever be collected from you, or (3) **whether it would advance effective tax administration to settle the liability**. New regulations require the IRS to add a third situation: economic hardship.

Under the new provisions, you are eligible to make an offer in compromise of your tax liability if such a compromise will not undermine compliance with tax laws and either collection of the entire tax liability would **create economic hardships** or exceptional circumstances exist where collection of the entire liability would be detrimental to our voluntary tax compliance system regardless of your financial circumstances.

How does the IRS determine economic hardship? Here are some factors to support your case:

1. You are incapable of earning a living because of a medical condition, long-term illness, or disability and that providing for your care and support will exhaust your financial resources,
2. Although you have certain assets, liquidating them to pay outstanding taxes will render you unable to meet **basic living expenses**, and
3. Despite owning certain assets, you cannot borrow against your equity and that disposition by seizure or sale of the assets would have sufficient **adverse consequences** that would make forced collection unlikely to be successful.

How does one determine that your offer would not undermine compliance with tax laws?

The following factors would help:

1. You do not have a history of non-compliance with both filing and paying your taxes,
2. You have not taken deliberate action to avoid paying taxes, and
3. You have not encouraged others to refuse to comply with tax laws.

Let's try a few examples of taxpayers going through economic hardships:

1. You have developed a **serious illness** that resulted in almost continuous hospitalization for a number of years. Your medical condition is such that you have been unable to manage your financial affairs. You did not file your tax returns for years. The IRS therefore prepared a substitute return and assessed you with taxes, penalties and interests. The bill had grown to more than three times its original size. If you used to have a good history of complying with tax laws, you qualify for an offer in compromise based on exceptional circumstances.

2. You provide time, care and assistance to your **child who has a serious long-term illness**. Although you have sufficient assets to pay taxes, you will need the equity in your assets to provide basic living expenses and medical care for your child. Before your child got sick, you filed and paid your taxes on time. Based on these facts, you should qualify for an offer in compromise because of an economic hardship.

3. You are **disabled and live on a fixed income** that will not permit full payment of your taxes after allowing for basic living expenses. You own a house that has been especially equipped to accommodate your

disability. Because of your disability and limited earning potential, you have not been able to refinance your mortgage. A forced sale of your house would create severe consequences making such a sale unreasonable. Assuming that you have a good history of complying with tax laws, you should be able to qualify for an offer in compromise based on economic hardship.

4. You are [retired and your only income is from a meager pension](#). While your retirement account has enough funds to pay off your taxes, doing so would leave you without adequate means to provide for your basic living expenses. You have filed and paid your taxes faithfully before these current problems. Based on these facts, you should be able to qualify for an offer because of economic hardship.

5. You submit an e-mail inquiry to the IRS at its WebPages and are [advised by IRS personnel](#) that you can withdraw your IRA savings and roll these over to a new account within 90 days. You withdraw the funds and roll these back within 80 days. You later find out that you should have redeposited the funds within 60 days. Assuming that you have a good compliance history, you should qualify for an offer in compromise based on exceptional circumstances.

These are a few situations where you can take advantage economic hardship. Use the new application Form 656-A in addition to the standard Form 656.