

Legislative Recommendation #15

Improve Offer in Compromise Program Accessibility by Repealing the Partial Payment Requirement and Restructuring the User Fee

PRESENT LAW

IRC § 7122(a) authorizes the IRS to settle a tax debt by accepting an offer in compromise (OIC). According to Policy Statement 5-100, the IRS will “accept an offer in compromise when it is unlikely that the tax liability can be collected in full and the amount offered reasonably reflects collection potential.” Taxpayers whose offers are accepted must file and pay their taxes for the next five years, as stated on IRS Form 656, Offer in Compromise (2019) (items l and m), or the IRS may seek to collect the amounts it compromised.

IRC § 7122(c)(1)(A) requires a taxpayer who would like the IRS to consider a “lump-sum” offer — payable in five or fewer installments — to include a nonrefundable partial payment of 20 percent of the amount of the offer with the application. IRC § 7122(c)(1)(B) requires a taxpayer who would like the IRS to consider a “periodic payment” offer — an offer payable in six or more installments — to include the first proposed installment with the application and to continue to make installment payments while the IRS is considering it. In addition to these partial payments, Treas. Reg. § 300.3 requires that most offer applications include a \$205 user fee. IRC § 7122(c)(3) provides that taxpayers with low incomes (*i.e.*, not more than 250 percent of the Federal Poverty Level) are not subject to the user fee or the partial payment requirement. They may apply for a waiver on Form 656.

REASONS FOR CHANGE

By accepting an offer, the IRS generally collects money it would not otherwise collect and may convert a noncompliant taxpayer into a compliant one by requiring the taxpayer, as a condition of the agreement, to timely file returns and pay taxes for the following five years. The Treasury Department’s General Explanations of the Administration’s Fiscal Year 2017 Revenue Proposals acknowledged the benefit of offers by proposing to repeal the partial payment requirement, explaining that the requirement “may substantially reduce access to the offer in compromise program. ... Reducing access to the offer-in-compromise program makes it more difficult and costly to obtain the collectable portion of existing tax liabilities.” The Treasury Department estimated that repealing the requirement would raise revenue.¹

A 2007 TAS study found that taxpayers above the low-income threshold were no better able to afford to make partial payments than those below it and that those below it frequently did not obtain a waiver. Similarly, a 2005 Treasury Inspector General for Tax Administration report found that when the IRS first imposed a \$150 OIC fee in 2003, offer submissions declined by more than 20 percent among taxpayers at every income level, including those who were eligible for a fee waiver. Furthermore, after the partial payment requirement was imposed, the offer acceptance rate did not increase, suggesting that higher up-front costs did not deter bad

¹ In the past, the IRS expressed concern that repealing the partial payment requirement or limiting the user fee might have the effect of increasing the number of frivolous offers. To address concerns about frivolous submissions, Congress enacted a frivolous submissions penalty under IRC § 6702(b). In general, it imposes a penalty of \$5,000 on any person who submits a frivolous OIC application (among other frivolous submissions).

offers at a higher rate than good ones. Thus, upfront payments such as the user fee and the partial payment requirement likely reduce collections and increase enforcement costs.

RECOMMENDATION

- Amend IRC § 7122(c) to remove the requirement that taxpayers include a partial payment with offer applications and restructure the user fee so that it is collected out of amounts otherwise due on accepted offers.²

² For legislative language generally consistent with this recommendation, see Taxpayer Protection Act, H.R. 2171, 115th Cong. § 206 (2017); Taxpayer Protection Act, H.R. 4912, 114th Cong. § 206 (2015); Taxpayer Assistance Act, H.R. 4994, 111th Cong. § 202 (2010). For additional background, see, e.g., National Taxpayer Advocate 2006 Annual Report to Congress 507-519 (Legislative Recommendation: *Improve Offer in Compromise Program Accessibility*).