

A Tax Debt Only Comparison of Offer-In-Compromise & Chapter 7 Bankruptcy in California From a Homelessness Base Case

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Introduction

Table 1 indicates some comparison of the conditions through which one may enter and take advantage of either offer-in-compromise or chapter 7 bankruptcy shown side by side for a partial comparison.

Table 2 involves a progression starting with an individual with tax debt only with additions to property by category and with level income used only for fee waiver effects. Graduation of

wealth going into either an offer-in-compromise or chapter 7 bankruptcy starts as a base case for one single person increases with three types of assets, each subsequent asset added to the prior asset, in this order: (money), (automobile), & (tools of the trade):

- (A) Homeless, owns nothing, no income
- (B) Individual with income lower than the lowest fee waiver threshold
- (C) Individual, waiver ineligible with income slightly above the higher waiver threshold.
- (D) Individual, waiver ineligible having Bank Cash \$30,825
- (E) Individual, waiver ineligible having Bank Cash \$30,825 + automobile
- (F) Individual, waiver ineligible having Bank Cash \$30,825 + automobile + tools of the trade

Table 3 illustrates a magnitude of the advantage of either offer-in-compromise v. chapter 7 bankruptcy considering income only. Income drives the amount that must be repaid to IRS. Income also sets the cost of entry into either offer-in-compromise v. chapter 7 bankruptcy.

- (G) Homeless, owns nothing, no income
- (H) Individual, income between fee waiver threshold for bankruptcy and OIC
- (I) Individual, income near the median income amount, computing an offer amount based solely on income..

Table 1: Rules for entry eligibility compared for Offer-In-Compromise & Chapter 7 Bankruptcy

Offer-In-Compromise v. Chapter 7 Bankruptcy Base Case For One Person	
Offer-In-Compromise	Chapter 7 Bankruptcy
Federal Tax Debt = Eligibility	Admission Eligibility: < \$57,962 Median I
RCP> Income Threshold & Asset Threshold	Or High M.Test Expenses, OR Tax debt>50%
Multiply X 12 month or 24 month basis	To Discharge, meet 3Y, 2Y, 240d, No SFR, Trust Fund, No fraud, Credit card Ineligible Tax Pay
Offer Accepted	Tax debts discharged for each eligible cat/Yr
Payments Made	(most non-tax debts discharged in addition)
Excess owed over offer paid = discharged	Next Chapter 7 is in 8 years
Unfortunately, Offer-In-Compromise & bankruptcy are collection statute of limitation tolling events	

Table 2: Comparison Starting from \$0 Long Term Homelessness

Comparison Assumes That Taxpayer is Admittable to Both Programs			
Asset Gradient (1)	Offer-In-Compromise	Bankruptcy	After Result
LongTermHomeless	Fee Waiver <\$2602.00/mo (250% of U.S. Poverty Level)	Fee Waiver <\$1,561.25/mo (150% of U.S. Poverty Level)	\$0 (\$-1offer)
Waiver Ineligible	Lumpsum: Fee \$186 + 20% of Offer	Chapter 7 Filing Fee \$335	IRS can oppose discharge and
	Periodic: Fee Series of Even Offer Payments over 6-24mo		IRS can reject offer later on
Bank Cash \$30,825 (2)	\$29,825(30,825-1000 oic exemption is added to Offer	Keep \$30,825 in cash	\$1000 kept both
	Govt Picks up \$29,825 value	All else equal Gov.	Bk by \$29,825
Car: \$5850 FMV (3)	Exclude \$4312.50 FMV for 20% discount to \$3450	\$5850 is exempt	5850-4312-1000 bank adds \$537 to Offer
Tools:\$8725 FMV(4)	Exclude all \$4470 FMV tools	Exclude all \$8725 FMV tools	\$4255 Offer add
	+ \$4255(8725-4470) to offer		

(1) To best indicate the divergent nature of these two remedies, a starting point is \$0 homelessness (which enables fee waivers), and thence to a low income in excess of the higher fee waiver limit, then cash in the bank, and then a car, and lastly tools of the trade. Under the wild card rules, some available cash property is sacrificed to cover the greater of two exemptions.

(2) \$30,825 was chosen as it is the sum of the maximum cash exemption under the highest cash alone exemption available to non-cash bankrupts.

(3) Car equity that matches the bankruptcy exemption (greater of the two exemptions \$4312.50 and \$5850) illustrates that the \$1537 shortfall means that the \$1000 “Exempted” bank account money is essentially committed to the collection potential as well as an additional \$537 will be added to the commitment to the offer. Overall \$1537 additional is committed to Offer, regardless of whether low income is below a national standards threshold.

(4) The Lump Sum offer form of offer-in-compromise is the most beneficial to the taxpayer, and it can be seen that a taxpayer with assets above the \$1000 bank deposit, \$4312.50 FMV car and \$4470 tools

adds directly to the collection potential offer. If taxpayer lives frugally and below some of the national standards (that don't involve subtraction for actual), such as Food, Clothing and Misc; Public Transportation; & Out of Pocket Health Cost, the above-threshold assets add directly to the reasonable collection potential.

The other part of the contribution to reasonable collection potential is income minus necessary business expenses and extraordinary expenses, which is too diverse and unique in each case to meaningfully discuss beyond the base cases treated here. We see that in each case of (a) cash, (b) car, and (c) tools; that bankruptcy is more generous. Everyone has some cash, most people have a car, and not everyone has "tools of the trade" But, the bankruptcy exemptions allow the taxpayer to exempt more value in each of the cited cases and before going deeply enough to begin to counter personal property exemptions unrelated to making a living.

Because table 2 involves asset categories having different threshold values, those relatively lower exemption threshold values for offer-in-compromise quickly consume the value of the initial cash exemption of \$1000 in the offer-in-compromise case for the higher value of item's bankruptcy exemption compared to the exemption for offer-in-compromise.

Table 3: Magnitude of the advantage of either Offer-In-Compromise v. Chapter 7 Bankruptcy Considering Income Only

Summary of Categories Advantage, Offer-In-Compromise v. Bankruptcy, By Income Only	
Income Category	Advantage and Magnitude of Advantage
Destitute Homeless with \$0	Tie, although saving \$1 offer requirement gives a micro advantage to Bankruptcy
Monthly Income between \$1,561.25 and \$2602.00/mo (5) (\$9 - \$15/hr)	For tax debt only, Advantage to Offer-In-Compromise higher Fee Waiver for income <\$2602.00/mo; saving \$187 (\$186+\$1 offer)
Monthly Income between \$2602.00/mo and \$4830 (Assume housing maximum, older car owned) (6) (>\$15-\$24/hr)	For bankruptcy eligible tax debt only, bankruptcy seems a better choice. The only cost is the bankruptcy filing fee. More additional debt give bankruptcy even more advantage

(5) National Standards not subject to subtraction for actuals include Food, Clothing and Misc(\$727); Public Transportation (\$217); & Out of Pocket Health Cost (\$55) totaling \$999, leaving between \$562.25 and \$1603.00/mo. The maximum housing for LA county is \$2258. For a single person living alone, housing and utilities actual expenses should easily cost at least the \$1603.00/mo at the upper

end of the range in the row example. If this is the case, a \$1 offer should be acceptable assuming all other categories don't contribute to a higher reasonable collection potential. In the range the bankruptcy cost is \$0 while the offer-in-compromise cost is \$186 + \$1 offer. Based just upon tax debt, bankruptcy wins.

(6) Monthly national standards of \$999 + local automobile standard \$273 = \$1272. Also, assume the \$2258 LA county housing and utilities Monthly excess reasonable collection potential is \$4830- $\$1272-2258 = \1300 . 12 months of this excess is $12 \times \$1300 = \$15,600$. The filing cost of the bankruptcy is \$335 and the filing cost of the Offer-in-Compromise is \$186 + 20% of Offer (\$15,600) or \$8,725 with a full cost if accepted of \$15,786. This creates a break-even if \$15,786 of tax is owed (no discharge advantage).

Table 3 illustrates that, as to California, where income is less than (\$9 - \$15/hr) that most tax debts are discharged in both the OIC and bankruptcy cases. For income (>\$15-\$24⁺/hr), bankruptcy's cash exemptions predominate.

For bankruptcy, if all tax is eligible for discharge, then it is discharged. This does not depend upon the amount of earnings nor the amount of tax. What this indicates, is that if tax debt is all the debt involved, that bankruptcy might be the more advantageous option, and especially for California taxpayers earning over \$15 per hour. In other states the results will vary based upon the level and configuration of that state's bankruptcy exemptions.