

IRS Offers New Tax Penalty Relief, Higher Thresholds for Installment Agreements

IRS Expands Fresh Start Initiative

By Diane Freda

Key Development: IRS offers penalty relief for unemployed filers, and increases threshold for taxpayers eligible for some installment agreements.

Potential Impacts: Some taxpayers may get six-month grace period on penalties for failure to pay, while higher thresholds will apply to some installment agreements, allowing more people to enter into one.

March 7, 2012 - The Internal Revenue Service announced an expansion of its Fresh Start Initiative to help struggling taxpayers by providing new penalty relief to the unemployed and installment agreements that will be available to more people. Under the new provisions, part of a broader effort started at IRS in 2008, certain taxpayers who have been unemployed for 30 days or longer will be able to avoid failure-to-pay penalties, IRS said in IR-2012-31.

In addition, IRS is doubling the dollar threshold for taxpayers eligible for streamlined installment agreements to help more people qualify for the program.

One attorney-certified public accountant told Bloomberg BNA that the penalty relief is limited and will not greatly impact those who choose to use it, while the expansion of the installment agreement program is significant. More taxpayers will have the ability to use streamlined installment agreements to catch up on back taxes, IRS said. Effective immediately, IRS raised the threshold for using the agreements without having to supply IRS with a financial statement, from \$25,000 to \$50,000.

Taxpayers who owe up to \$50,000 in back taxes will now be able to enter into a streamlined agreement with IRS that stretches the payment out over a series of months or years. The maximum term for streamlined installment agreements has been raised to 72 months from the current 60 months.

“We have an obligation to work with taxpayers who are struggling to make ends meet,” IRS Commissioner Douglas Shulman said. “This new approach makes sense for taxpayers and for the nation's tax system, and it's part of a wider effort we have under way to help struggling taxpayers.”

Take Advantage of It

E. Martin Davidoff, a certified public accountant and tax attorney with E. Martin Davidoff & Associates, said March 7 that the expansion of the streamlined installment agreement program has been in effect for several months, and is something all affected taxpayers should take advantage of.

“It's a wonderful thing,” he said, because it allows taxpayers to avoid liens. IRS's real motive for allowing that when taxpayers get into the agreements is to get them into a direct debit installment agreement in which IRS can automatically take money out of their account, he said.

“IRS has a greater success rate when the money comes out that way,” Davidoff said. Therefore, allowing the higher threshold was “a quid pro quo.”

Six-Month Grace Period

Failure-to-pay penalties are one of the biggest factors a financially distressed taxpayer faces on a tax bill, IRS said in the news release. A six-month grace period on those penalties will be made available to certain wage earners and self-employed individuals. The failure-to-pay penalty is generally one-half of 1 percent per month with an upper limit of 25 percent.

Under the new relief, taxpayers can avoid that penalty until Oct. 15, which is six months beyond this year's filing deadline. However, IRS said it is still legally required to charge interest on unpaid back taxes and it does not have the authority to waive the charge, which is currently 3 percent on an annual basis.

Even with the new penalty relief becoming available, IRS strongly encouraged taxpayers to file their returns by April 17 or file for an extension. Failure-to-file penalties applied to unpaid taxes remain in effect and are generally 5 percent per month, also with a 25 percent cap.

Requesting an extension of time to pay will result in relief from the penalty for tax year 2011 only if the tax, interest, and any other penalties are fully paid by Oct. 15, IRS said.

The penalty relief will be available to two categories of taxpayers:

- Wage earners who have been unemployed for at least 30 consecutive days during 2011 or in 2012 up to the April 17 deadline for filing a federal tax return this year, and
- Self-employed individuals who experienced a 25 percent or greater reduction in business income in 2011 due to the economy.

Davidoff said on this relief, the amount of work needed to secure the grace period may be more trouble than it is worth. “If someone gets to delay the payment of \$5,000 for six months, this relief at most would give them \$150 in savings,” he said. “You're not talking a lot of dollars and the taxpayer has to file a form separate from their tax return.”

People would have to know about the form, go and get it, and once filed, would have no confirmation from IRS that it has been received, all for a relatively small savings, Davidoff said.

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