

## When Will the IRS Compromise Tax Liability?

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We have all seen the television commercials hawking tax relief with “satisfied clients” shilling for the promoter. But will the IRS really compromise a tax liability? If so, when, how, and why? There are four grounds on which the IRS is authorized to compromise a tax liability: (1) Effective tax administration on grounds of equity or public policy; (2) Effective tax administration on grounds of economic hardship; (3) Doubt as to liability; and (4) Doubt as to collectability.

Because the business is the taxpayer, a request to compromise must be made in the name of the business. This means that partners in a partnership cannot compromise an individual's portion of a partnership tax debt. The partnership must submit its own offer in compromise based upon the partnership's and the individual partner's ability to pay.

The Internal Revenue Manual (IRM) is the IRS's internal policies and procedures manual and contains a wealth of information regarding how the IRS evaluates offers in compromise (among many other topics). To see what factors the IRS considers and how it evaluates offers in compromise as set forth in the IRM, click [here](#).

### Effective Tax Administration on Grounds of Equity or Public Policy

This means there is no doubt the tax liability is owed, and that the full amount could be collected. In this case, compelling public policy or equity considerations exist, such that collection of the full liability would undermine public confidence that the tax laws are administered in a fair and equitable manner. Not to say the IRS has never compromised a tax debt on these grounds, but a successful result is almost unprecedented.

### Effective Tax Administration on Grounds of Economic Hardship

Like its sibling, a compromise on grounds of public policy, this exception also means there is no doubt the tax liability is owed and that the full amount could be collected. This ground would apply where full collection would cause **severe** economic hardship, such as an inability to pay basic, reasonable living expenses. Most efforts to compromise a tax debt under this exception fail because other, more common grounds exist.

### Doubt as to Liability

This means there is a genuine dispute whether the amount of the assessed tax is correct or whether the assessment is correct. Tax protester arguments, i.e., the Income Tax Act is unconstitutional, the income tax is a voluntary tax, wages are not income, the sovereign citizens theory, and a plethora of other arguments **do not constitute** a genuine dispute. In fact, all these tax protester arguments have been repeatedly characterized as frivolous, which, if made, will subject the person making them to possible sanctions under IRC § 6673(a). For information on tax protester arguments (and the consequences) click

here.

Doubt as to liability frequently arises in cases involving innocent spouse relief, but may arise in other areas as well. Doubt as to liability can arise in a number of circumstances such as a missed notice from the IRS resulting in the IRS disallowing all deductions, which, assuming the time for correction has not expired, can be proven and credited, mistaken or incorrect reporting such as when a payroll service reports (and pays) employment taxes for one affiliate when it should have been the other affiliate, or the IRS examiner made a mistake in applying the law or in calculating a tax liability. It happens.

Doubt as to liability could arise when the IRS seeks to impose a Trust Fund Recovery penalty—the Trust Fund Recovery penalty, or TFR for short, is a 100% penalty—on a corporate official for not making payroll tax deposits and a genuine issue exists whether the person is a “responsible party” for purposes of withholding, collecting, and remitting payroll taxes. In virtually all the litigated tax cases, the issue is doubt as to liability. In each case, the determination of whether there is any doubt as to liability will be made on the totality of the facts and circumstances.

To raise the issue of doubt as to liability, several conditions must be met: (1) there cannot be a final court determination regarding the tax liability; (2) there must be a legitimate dispute regarding the tax liability (no tax protester arguments); and (3) you **must** have supporting documentation. Typically, doubts as to liability are resolved well before the offer in compromise stage; but if not, an offer in compromise on the basis of doubt as to liability is made using Form 656-L.

The last category, doubt as to collectability, is the most often used ground for compromising a tax debt.

### **Doubt as to Collectability**

This means the IRS does not think it can collect the full amount of the tax liability through forced collection, so it would rather have something rather than nothing. Before the Service will consider compromising a tax debt due to doubt as to collectability, it will require the taxpayer to submit Form 433-B, Collection Statement for Businesses (for individuals, there is Form 433-A).

Form 433-B requires a business to list extensive financial information. Though it may seem intrusive at first blush, the purpose of Form 433-B is to determine what the IRS can achieve through force collections. After all, the IRS will not compromise a tax debt for doubt as collectability where the full amount can be paid through available assets or income, either in full immediately or through an installment agreement.

Though some may be tempted to understate assets and overstate liabilities on Form 433-B, this is a very bad idea. Form 433-B, like all forms submitted to the IRS, is signed under penalty of perjury. Intentionally understating assets or overstating liabilities on a Form 433-B is a 1001 violation (a crime punishable by up to five years imprisonment) just as if the person signing the form had lied to a federal agent.

As thorough as Form 433-B is, it is just numbers on a piece of paper. To maximize the chances of getting the IRS to compromise a business tax debt, the business's story needs to be told, in writing, ideally accompanying Form 433-B. An offer in compromise (OIC) for doubt as to collectability is made on Form 656-B. If the taxpayer can demonstrate that it is unlikely that the IRS will collect the full amount through forced collection and the offer in compromise reflects the taxpayer's reasonable collection potential (RCP), the IRS will likely accept the offer and compromise the tax debt.