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|  | **AREAS OF PRACTICE****TAX CONTROVERSY****ENTITY CREATION****ESTATE PLANNING** |

# Getting your offer in compromise approved

***Understanding National Standards***

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There are many things to consider in evaluating your chances of, and preparing your offer for, approval. One of the most important factors is understanding the interplay between your actual living expenses and the living expenses the IRS allows you to have. When first introduced to the National Standards, many people are offended. They do not understand how the IRS can question their very personal and often reasonable decisions on what expenses are necessary to raise and support themselves and their families. It seems unfair and even outrageous for the IRS to not allow them to spend money on what they view as very necessary expenditures. However, getting over that very emotional initial reaction is crucial so that proper analysis and planning can be done.

There are four main areas of the National Standards: Food/Miscellaneous; Housing, Transportation, and Health. The IRS may allow expenses that are not within these categories, but within these categories, the amount that you spend may not be allowed.

*Housing Standards.* Often the largest expense incurred by families is the cost of their home. Whether renting an apartment or paying a mortgage, the cost is usually in the thousands. Like with the transportation and Food/Misc. categories, the IRS bases the amount it allows on the location of the taxpayer. The standard acknowledges the reality that some cities and states are just a lot more expensive in which to live. For example, for a family of 4 living in Atlanta, the IRS allows up to $2,515, but that same family living in Los Angeles would be allowed up to $3,133. Pity the person with an expensive house that gets into tax trouble! Obviously, the fewer the family members the less expense allowed. But be aware…if your living with your parents and not paying rent or utilities…you get zippo!

*Transportation.* Again, with transportation costs, where you live makes a difference, at least with the cost of operating a vehicle. In Atlanta, the IRS allows a maximum of $512 in operating expense for two cars, and $590 in LA. Ownership costs have a truly national standard, with the IRS allowing $1,034 for two vehicles. The IRS only allows a maximum of two cars per family and, as with the housing standards, the IRS allows the lesser of the standard or actual expenses.

*Out of Pocket Health.* Unlike the transportation and housing costs, the IRS allows an exact amount for health and Food/Misc costs, regardless of what the taxpayer actually spends on such expenses. For a person under 65, the amount allowed is 60; for a person 65 or older, the amount allowed is $144. Each person in the family gets their respective amount. The taxpayer with higher out of pocket health expenses must be able to show that such additional expenses are necessary living expenses. In addition to out of pocket health costs, the taxpayer also is allowed their actual insurance premium costs.

*Food/Miscellaneous.* Again, for this catchall category, the taxpayer is allowed a set amount ($1,513 for 4 people) regardless of what they actually spend. There are several categories within this category, but in my experience, this category is effectively a catchall category.

*Summary.* For all of these categories of national standards, although the national standards provide maximum limits, those limits can be increased if the taxpayer can establish that the additional expenses are necessary living expenses. In my experience, this is not an easy task to accomplish, especially when it comes to expensive houses or expensive cars…remember, most of these IRS employees are not rich! So be sure and be reasonable or your efforts to get additional allowances will be counterproductive.

Another way of getting higher allowances is the Six Year Rule. Under this rule, you will be allowed higher allowances if you can pay off the IRS debt in full in six years. In other words, the IRS is saying that they don’t care what you spend things on as long as you can pay off your debt in six years. Of course, for larger tax liabilities, it is often hard to accomplish this.

The bottom line is that if you get your offer in compromise accepted, you may have to live like a miser for the duration of the offer repayment period. Just remember that once you are done paying the debt off, your life will get immeasurably less stressful!

STEPS TO INCORPORATE

 ***Part One***

There are numerous steps to a successful incorporation. Some of the steps are complicated and others are not…but all are important to positioning your business correctly. Therefore, attention to detail during this process is of the utmost importance. Suffice it to say that corporate attorneys get a lot of their work from people who tried to do it themselves at first…and screwed up. Don’t be one of those people.

The first step in incorporating is determining whether incorporation is in fact the right choice for your business. There are many possible structures for a business…C corporation, S corporation, general partnership, limited partnership, limited liability company, limited liability partnership, and sole proprietorship. Each structure has its’ advantages, tax or otherwise. Understanding these differences, and the advantages and drawbacks of each, proves very valuable when creating the game plan for what you want to do with your business and where you want to go with it.

If a corporation is desired, then the choice between a C corporation and a S corporation must be made. Multiple levels of taxation, greater flexibility in types of shares, and more robust expense deductions are some of the main factors to consider when determining between S and C. How many people do you want involved in your business? How many investors, if any do you plan on having? Will the investors want different types of rights to income, losses? If it is reasonable to assume that the business will incur losses in the early years, will the investors want the tax benefit of those losses since they will have to wait longer to be paid back or to otherwise receive a return.

Will you want to operate only one type of business in the company or more than one? Is it important to avoid paying employment taxes? And what about employees. Do you anticipate having any? Will they have a chance to share in the equitable growth of the company? What type of retirement planning do you envision for you and the other participants?

These are all very important factors that can have a severe impact on the choice of S v. C. Sometimes it is hard to get a new business owner to think about the future with such detail. But doing so gives the owner great insight and helps not just with the legal determinations such as proper legal structure but also with planning in all kinds of other ways. As they say, it is always better to know where you are going before you actually get there!

Next Month, I will discuss Part Two…Its all in a Name!

# Calculating the costs of probate

Probate in California is usually time consuming. Average probate court processing times are well over a year. But the time delays are only part of the negatives of probate. The actual costs, in filing fees, publication fees, attorney fees and executor fees can be daunting. These two negatives – time delay in getting access to the assets and costs of probate, are the two main reasons why people look to revocable living trusts, and why California has, as of 1/1/2016, instituted the new Transfer on Death Deed to transfer real estate without having to probate or set up a revocable living trust.

As for the costs of probate, they are substantial. The 2015 basic filing fee charged for a probate petition was $450. There is also a $435 filing fee to file the petition for final distribution of the estate assets. Additional fees for items such as publication of the probate notice, probate referee, and certified copies of court documents will be required.

The most substantial fees are attorneys’ fees and executor fees, which are statutorily set (although the executor can waive the fee and may be inclined to do so since an executor fee is taxable income). The executor and attorneys’ fees are the same and are calculated based on a percentage of the gross value of the estate. Probate Code Section 10810 sets the fees as follows: 4% of the first $100,000, 3% of the second $100,000, 2% of the next $800,000, 1% of the next $9,000,000, and ½% of the next $15,000,000.

So, for an estate of, say $3,000,000, the combined attorney fees and executor fees would be $84,000. Of course, on an estate with a gross value of $3m, that may not seem like a lot of money, but it is important to understand that the fees are based on the “gross” value of the estate, not on the net value after reduction for liabilities. So if an estate is comprised of a $3m piece of real estate with equity of $200,000, that $84,000+ in probate expenses seems all the more daunting.

What is the takeaway from this article – unless there is a good reason for probating the estate – such as resolving potential claims to the estate, the best strategy is to AVOID PROBATE!

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