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## *What to Do When You Owe the IRS Money?*

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*My wife and I just prepared our 2008 individual tax return. To our dismay, we owe over \$6,000 to the Internal Revenue Service and we do not have the money to pay this in full. I want to wait to file the tax return until we have the money to pay the full amount. My wife thinks we should file the tax return now and pay the balance due with our credit cards. What should we do?*

Federal tax law requires all of us to file our tax return and settle our tax liability in full by April 15<sup>th</sup>. Failure to file your return or pay on time will trigger various interest and penalties. Although owing interest and penalties to the IRS sounds distressing, you can save significant amounts of money if you handle this properly. There are three assessments that the IRS can levy on you. They are summarized as follows:

**Failure to file** – If you do not file your tax return by April 15<sup>th</sup> and owe taxes, the IRS will assess you a “late-filing penalty” of five percent per month of the tax owed. In your case, this penalty would be over \$300 per month. The late-filing penalty is capped at 25 percent per year. This assessment is the most destructive of all penalties and can easily be avoided. By merely filing your tax return on time, you will avoid this penalty. So PLEASE make sure you file your tax return by April 15<sup>th</sup>, regardless of your ability to pay.

**Interest** – The next assessment the IRS will levy on you is interest. You will be charged interest on any unpaid tax balance. This assessment will commence April 15<sup>th</sup> and will continue until you have paid the balance in full. The interest rate charged to the taxpayer is the federal short term interest rate plus three percent. For the first quarter of 2009 the interest rate charged by the IRS is five percent.

**Failure to pay penalty** – The final assessment that the IRS will levy on you is a “failure to pay” penalty. You will have to pay a penalty of one half of one percent per month of the tax owed. As such, this will work out to approximately six percent per year.

I suggest you file your tax return no later than April 15<sup>th</sup>. Submit the maximum payment you can afford with your tax return. For any remaining balance due, you will be subject to penalties and interest totaling approximately 11 percent. The 11 percent is much more manageable than the 36 percent you would be charged if you also did not file your tax return.

If you can borrow money at a rate of 11 percent or less from your credit card company, you should do so and pay off the tax liability. If not, just “borrow” the money from the US Treasury and pay them back as quick as you can.

For more information, please send an email to James Downey at [jmdowney@downeycocpa.com](mailto:jmdowney@downeycocpa.com).

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