



The 2014 Voluntary Disclosure Program: Important Changes for the Still Non-Compliant Taxpayer with Foreign Accounts

On June 18, 2014, the Commissioner of the Internal Revenue Service (IRS), John Koskinen, announced significant changes to the IRS's offshore voluntary disclosure program (referred to as the "2014 OVDP"). The changes to the program are described in this Alert. The changes are significant in many ways and add encouragement to those who have yet to make a voluntary disclosure.

According to the IRS Commissioner, these changes allow "a new pathway for people with offshore assets to come into tax compliance." In fact, these changes are very timely. A host of Swiss financial institutions are joining a non-prosecution program that allows the banks to avoid prosecution by the U.S. government in exchange for, among other things, information about the banks' U.S.-related accounts. It is expected that eventually the U.S. government, through treaty requests or otherwise, will obtain information about the banks' U.S. clients. Furthermore, the Foreign Account Tax Compliance Act (FATCA) will force foreign banks, no matter where they are located, to divulge the identities of their U.S. clients to the IRS.

This new era of transparency and tax enforcement is forcing many people who have not yet come into compliance for the past to do so now before the consequences get worse.

By way of background, the 2012 Offshore Voluntary Disclosure Program is an IRS program that limits a qualifying U.S. person's potential criminal exposure and civil penalties associated with the failure to disclose foreign accounts and assets and/or to report the income generated from them. Under this program, a non-compliant U.S. individual typically must file eight years of amended (or delinquent) tax returns and foreign bank account reports (FBARs) and make other disclosures, and pay the taxes, interest

and penalties on the taxes that are due, and an additional miscellaneous penalty of 27.5% of the highest aggregate value of the individual's foreign assets related to tax non-compliance, including foreign bank accounts, during the last eight years.

The 2014 OVDP takes a dual-headed approach, easing the rules for individuals (whether they live abroad or in the United States) who were not "willful" in their noncompliance, but at the same time potentially raising the penalties for those whose non-compliance was willful and who have not participated in the prior programs. The increased penalty for 2014 OVDP participants is based on whether their accounts and advisors were under investigation and this fact is publically known, as described below.

The changes include:

- Modifying the "streamlined" filing program applicable to U.S. persons living abroad. This program, as modified, allows U.S. taxpayers who reside abroad, and who certify that they were non-willful, to file three years of income tax returns and six years of FBARs, to only pay three years of back-taxes and interest, and to avoid all penalties.
- Expanding the streamlined program to apply to U.S. persons who reside in the U.S. and have filed tax returns in the past. This expansion allows U.S. persons who reside in the U.S., and who certify that they were non-willful, to file three years of income tax returns and six years of FBARs, pay three years of back-taxes and interest, and pay a penalty of 5% (rather than 27.5% or higher) of the value of their foreign financial assets.
- Requiring more information to be presented by individuals who participate in the 2014 OVDP. Under the changes, foreign bank statements must be submitted regardless of the accounts' value, and taxpayers must pay the offshore penalty earlier in the process than before.
- Increasing the 27.5% offshore penalty to 50% if, prior to the taxpayer's offshore submission to the IRS, it becomes "public" that a financial institution where the taxpayer holds an account or another party facilitating the taxpayer's offshore arrangement is "under investigation by or cooperating with" the IRS or the Department of Justice.

As has always been the case, an individual will not qualify for the 2014 OVDP (or even for the streamlined procedure) if the IRS already has information regarding his or her noncompliance, such as an existing or prior audit during one of the disclosure years.

At the moment, there is a good deal of uncertainty about the application of the 2014 OVDP, including the application of the transition rules for those who had started the 2012 OVDP process but have not completed it. Moreover, the IRS's application of the new streamlined program, particularly the IRS's evaluation of what constitutes a "non-willful" failure to file an FBAR remains and can be perilous for the affirming taxpayer.

Given the new era of transparency that the U.S. has ushered in, which will eventually lead to the detection of many U.S. persons with undisclosed foreign accounts and assets, taxpayers with offshore compliance issues should speak to their tax advisors to see if they qualify for the 2014 OVDP or the streamlined program. Taxpayers should take seriously the Commissioner's warning that "the days of hiding assets in accounts overseas are coming to an end," particularly as the U.S.'s investigations of foreign banks intensify, and as the U.S. gathers information regarding U.S. taxpayers under FATCA.

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