CANADIAN TAX Highlights

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Update on IRS Streamlined Foreign Offshore Procedures

In July 2014, the IRS reworked its offshore voluntary disclosure program (OVDP) and streamlined foreign offshore procedures (SFOP) for taxpayers with unreported income from non-US bank and financial accounts. The OVDP is designed for an individual who wilfully failed to comply with US income tax and information reporting obligations (including the Report of Foreign Bank and Financial Accounts (FBAR)). In contrast, the SFOP assists (1) a non-resident individual who did not wilfully fail to comply but was unaware of the requirement to file a US income tax return and FBAR annually, and (2) a non-resident individual who may have filed a US income tax return but was unaware of the requirement to include non-US income. Since July 2014, the IRS has indicated that there is no set deadline for an individual to apply to the OVDP or the SFOP, but the terms could change at any time, including through complete termination by the IRS. Most individuals eventually will become ineligible for the SFOP, and therefore that program may soon end.

In December 2015, the IRS commissioner, John Koskinen, issued the following statement regarding the SFOP:

> At some point, we will have assumed that people have had enough notice that they should have become voluntarily compliant. At that point—after some period of time and you're not compliant—it will be assumed that logically you are purposely not compliant.

Koskinen said that the IRS had no plan to end the SFOP. In May 2016, an IRS attorney who was a drafter of the OVDP and the SFOP since their first iterations in 2009 and 2012, respectively, attributed the absence of a plan to the IRS's currently strained resources. The attorney also said that the IRS constantly re-evaluates the business case for continuation, but reasonable notice will be given when the IRS decides to end the SFOP.

Regardless of the actual lifespan of the SFOP, the IRS comments in December 2015 touch on an important issue: failure to comply may not be wholly non-wilful. The test for wilfulness is whether there has been a voluntary, intentional violation of a known legal duty. In the last five years, many Canadians became aware of their US income tax and FBAR obligations because of the IRS's programs and marketing efforts and because of articles in Canadian publications and comments from Canadian government officials about the IRS's enforcement tactics. Non-compliance may have been non-wilful up to the time of learning about the US obligations, but a Canadian who did not (or has not) promptly come forward to the IRS after learning of his or her filing obligations may have become wilfully non-compliant at that time and thus ineligible to use the SFOP. Absent extenuating circumstances, that individual may now not be able to certify a non-wilful failure to comply with filing obligations for the years after he or she learned of those obligations.

The IRS commissioner's comments are somewhat misleading because, apart from the SFOP requirements, the IRS could not bear its burden of proving that an individual's non-compliance was wilful without regard to the specific facts; such a conclusion could not be based solely on the fact that an individual had not complied by a time chosen by the IRS. Under the SFOP, however, the individual bears the onus and must show the IRS that all past non-compliance was not wilful; such certification is made under penalties of perjury. The commissioner's position also assumes that every individual has access to information about the US filing requirements; the reality is different. Not everyone has access to that information, and even those with such access do not always encounter the relevant information. Further, some individuals do not even know that they are US citizens. The commissioner's point, however, is that an individual must come forward promptly after discovering his or her US filing obligations because failure to do so obviates the individual's ability to certify his or her non-wilfulness for subsequent years' filings and thus renders him or her ineligible for the SFOP.

Canadians should not wait to come forward after learning of their non-compliance: it is unlikely that the SFOP will always be available. More importantly, failure to enter that program expeditiously may render an individual unable to certify non-wilfulness for the years in the lookback period and thus render him or her ineligible for the SFOP. To date, the United States has been lenient with US citizens residing in Canada, but recent comments from the IRS imply that, given the IRS's outreach efforts over the last few years, even non-residents may soon be presumed to have had notice of their filing obligations. The United States is not going to change the filing requirements for US citizens living outside the country, and the IRS is probably not going to offer a more favourable amnesty than is currently offered by the SFOP. Thus, now is the time for a Canadian to rectify his or her past US non-compliance. Many individuals have already done so and are now proceeding to renounce US citizenship after five years of compliance, the period necessary to avoid triggering US expatriation tax. Non-resident individuals who have not already come forward should act now.

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