

IRS ANNOUNCES CHANGES TO ITS OFFSHORE VOLUNTARY DISCLOSURE AND STREAMLINED PROCEDURES

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On June 18, 2014, [the IRS announced](#) a number of significant changes to its Offshore Voluntary Disclosure Program (OVDP) and 2012 streamlined procedure for nonresidents and the addition of a streamlined procedure for U.S. residents, all of which took effect on July 1. The IRS's goal in making these changes and additions was to encourage taxpayers to rectify noncompliance through these programs by providing additional flexibility. These latest changes provide welcome relief to many U.S. taxpayers who have failed to report income from their non-U.S. bank and financial accounts on a U.S. income tax return and failed to report the accounts on a Report of Foreign Bank and Financial Accounts (FBAR).

Expansion of the IRS Streamlined Procedures

The IRS has expanded the parameters of its [streamlined procedure](#) for nonresidents to include a much broader group of U.S. taxpayers and also created a streamlined procedure for U.S. resident taxpayers. Thus, the IRS now has streamlined procedures for both nonresident U.S. citizens and U.S. individual taxpayers residing in the United States. However, U.S. resident taxpayers [qualifying for the streamlined procedure](#) must have already filed U.S. income tax returns and must pay a penalty equal to five percent of their unreported offshore assets.

With respect to the [revised streamlined procedure for nonresidents](#), the IRS modified the eligibility criteria by eliminating the \$1,500 tax threshold. The IRS also eradicated the risk assessment analysis and the questionnaire that nonresident taxpayers previously had to complete to enter the streamlined procedure. Taxpayers will still be required to file three years of delinquent or amended U.S. income tax returns and six years of delinquent or amended FBARs. The full amount of the tax and interest due in connection with these filings must be remitted with the delinquent or amended returns.

To be eligible for the IRS's revised streamlined procedure for nonresidents of the United States, taxpayers must: 1) meet an applicable non-residency requirement (for joint return filers, both spouses must meet the applicable non-residency requirement) and 2) have failed to report the income from a foreign financial asset and pay tax as required by U.S. law, and such failures must have resulted from non-

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willful conduct.

Individual U.S. citizens or lawful permanent residents, or estates of U.S. citizens or lawful permanent residents will meet the applicable non-residency requirement if, in any one or more of the three most recent years for which the U.S. income tax return due date (or properly applied for extended due date) has passed, the individual did not have a U.S. abode and the individual was physically outside the United States for at least 330 full days. Therefore, U.S. citizen snowbirds who consistently have spent their winters in warmer U.S. climates will not qualify as nonresidents under the new guidelines. Also, U.S. citizens living close to the border who travel to the United States frequently will also not be classified as nonresidents. The IRS indicated that it devised this definition of a nonresident in an attempt to resolve some questions that had arisen in connection with the 2012 streamlined procedure for nonresidents. However, this narrow definition has an apparently unintended result of making ineligible for the streamlined procedures U.S. citizen/green card-holder snowbirds and those living near a U.S. border who have not previously filed U.S. income tax returns.

A taxpayer who made a submission under the IRS's 2012 streamlined filing compliance procedure for nonresident non-filers prior to July 1, 2014, and has not already been notified of a high- or low-risk determination, will not receive correspondence from the IRS related to their risk determination, and the U.S. income tax returns submitted pursuant to that procedure will be processed without regard to that risk assessment.

Modifications to the OVDP

The IRS has also revised the terms of its OVDP. The intent of this change is to cover those taxpayers whose failure to comply with the reporting requirements is considered willful in nature and to cover those who do not qualify for the streamlined procedures. Furthermore, the changes to the OVDP attempt to shift the focus to taxpayers who are seeking certainty and relief from criminal prosecution.

Going forward, taxpayers who wish to participate in the OVDP will be required to provide more information than in the past, including the submission of all account statements at the time they apply to the OVDP. The 27.5 percent miscellaneous offshore penalty under the OVDP continues to apply in many cases. For certain voluntary disclosures filed on or after August 3, 2014, though, taxpayers will face a 50 percent penalty on the maximum value of unreported assets.

The foregoing changes are in part the result of feedback the IRS received from many tax practitioners (including attorneys from our firm) and the National Taxpayer Advocate. The IRS discovered that there were many taxpayers for whom the existing program penalties were too harsh. Some taxpayers did not need the protection from criminal prosecution offered by the OVDP, but they also did not neatly fit within the confines of the 2012 nonresident streamlined procedure criteria.

The IRS has warned taxpayers, though, that anyone who continues to willfully and aggressively evade the tax laws by hiding money overseas will have to pay a higher price for such noncompliance. Although the IRS is tightening up the components of the OVDP, it still believes the program offers a better deal than the alternative and is warning taxpayers that if the IRS finds you first, you will face higher penalties and possibly criminal prosecution and jail time. The IRS has also warned taxpayers that it is continuing its efforts to track down individuals who continue to hide assets overseas. Notably, in light of the new reporting requirements under the Foreign Account Tax Compliance Act (FATCA), more foreign banks will be disclosing information on their U.S. customers beginning July 1. Thus, the IRS continues to warn taxpayers that the

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days of hiding assets in accounts overseas are coming to an end.

