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Streamlined Penalty Structure Available To Those in OVDP by June 30, Official Confirms

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BNA Snapshot

Key Development: Taxpayers must be in Offshore Voluntary Disclosure Program by June 30 to qualify for streamlined relief.

Key Takeaway: IRS will carefully scrutinize assertions of non-willful conduct under streamlined program.

Next Step: Information from offshore enforcement activities continues pouring in from Switzerland and other countries.

By Alison Bennett

June 24 — Taxpayers who are in the Offshore Voluntary Disclosure Program to report their overseas assets can request the favorable penalty structure under newly expanded streamlined compliance procedures without giving up the audit and criminal liability protection offered by the OVDP, an Internal Revenue Service official said.

To be considered "in" the OVDP for purposes of the transition rules, taxpayers must have submitted a voluntary disclosure intake letter by June 30, according to Jennifer Best, senior adviser to the IRS deputy commissioner (International).

During a June 24 webinar sponsored by the American Bar Association Section of Taxation and the ABA Center for Professional Development, Best said if taxpayers get their submissions in by that deadline, their cases may be considered under the set of OVDP frequently asked questions and answers in effect before then.

The IRS June 18 announced it was expanding its streamlined procedures so both U.S. and non-U.S. residents who certify their tax noncompliance was non-willful can qualify for low to zero penalties.

At the same time, the IRS said it was making the OVDP—generally designed for taxpayers with willful failure to report their offshore assets—tougher by requiring disclosure of more information and payment of the 27.5 percent penalty up front.

OVDP Penalties Rising

In addition, the penalty will rise to 50 percent after Aug. 4 for taxpayers whose banks or facilitators of their offshore arrangements are publicly identified by the Justice Department as under investigation (118 DTR GG-1, 6/19/14).

Both Best and fellow panelist Kathryn Keneally, who recently left her post as assistant attorney general of the Tax Division at the Department of Justice, said taxpayers need to be very careful in asserting their conduct was non-willful through the streamlined procedures, noting that information from IRS offshore enforcement initiatives is pouring in.

In response to a question, Best said if taxpayers at the beginning of the process have already submitted their voluntary disclosure intake letters but decide they would rather apply for relief through the streamlined compliance procedures outside of the OVDP, they can do so, but should correspond with the IRS to let the government know they have changed their minds.

OVDP Protection Remains

Best stressed that if taxpayers stay in the OVDP, they can still request the penalty structure of the streamlined program if they believe their conduct wasn't willful. In answer to a question from panel moderator Scott D. Michel, a member of Caplin & Drysdale LLP in Washington, Best said even if taxpayers are denied the streamlined penalty, they will remain in the OVDP "at all times" and will still qualify for the 27.5 percent penalty and the protection from criminal prosecution.

Best said taxpayers who are in the OVDP and have decided to "opt out" of the process that would result in a closing agreement can request the lighter streamlined penalty as long as they haven't received formal notice that the IRS is opening an audit.

She reaffirmed that the IRS won't reopen cases or offer refunds to anyone who already has a closing agreement through the OVDP, noting that the OVDP program and the streamlined program are different initiatives aimed at different sets of taxpayers.

Both Best and Keneally counseled caution in certifications that conduct was non-willful.

Cross-Checking Certifications

Best said the IRS will be cross-checking certifications against information that it gets in through treaty requests, John Doe summonses, and other government enforcement activities. "We're still finalizing our plans of how we're going to review these, but we'll be balancing and cross-checking data that we get from all sources," Best said. "We want to ensure the certifications that we're getting are accurate and complete."

Keneally stressed DOJ is getting information from around the world and those in the streamlined program don't have criminal or audit protection. "Certification of non-willfulness when you are willful is itself another crime," Keneally cautioned. "For anyone who thinks 'Yippee, I can get 5 percent instead of 27.5 percent and all I have to do is sign a piece of paper and say I wasn't willful,' that's a very risky approach," she said.

Both Michel and panelist Michel Stein, a principal with Hochman, Salkin, Rettig, Toscher & Perez PC in Los Angeles, said tax advisers will have a tough road in working with their clients in the next few days and weeks to decide whether they should assert their conduct wasn't willful in the attempt to qualify for the streamlined penalties inside or outside of the OVDP.

Difficult Choices

Particularly for those who have begun the clearance process into the OVDP, the decision about whether to submit the voluntary disclosure intake letter in time to make the June 30 deadline will be a difficult one, Stein said.

“The transition rules are extremely valuable to those with the right set of facts,” he said. “The downside, if you do submit your letter by June 30, you are bound by the terms of the OVDP and you need to file eight years of returns and pay accuracy-related penalties. It needs to be analyzed on a case-by-case basis. If you have taxpayers with a bad set of facts, streamlined probably wouldn't fit.”

Both Michel and Stein said disclosure letters might be rushed in the next few days and be submitted with information that is the “best available” but possibly not complete.

Keneally stressed the IRS and the Justice Department are getting information from a broad range of sources, including treaty requests, whistleblowers, cooperators and the like.

With regard to the 50 percent penalty for clients of banks under investigation, “It's to get everybody sitting on the fence to come in now,” Keneally said, adding that the government is frustrated with taxpayers who continue to play a “waiting game” to see if the Justice Department will zero in on their bank.

Swiss Bank Disclosures

She noted that the government plans to make public the non-prosecution agreements it is negotiating with dozens of Swiss banks under a special program. “It's a dangerous misperception that Swiss banks are not handing over names,” she said.

Michel emphasized that even though Swiss banks aren't allowed to disclose the specific names of account holders under Swiss law, the Justice Department has been able to get substantial amounts of information from banks in the program trying to minimize their penalties—information the DOJ can then turn into treaty requests.

“Many banks are having meetings with DOJ and are providing cases for the filing of treaty requests,” Michel said.

Keneally said the Justice Department got “a wave of names” when it negotiated a deferred prosecution agreement with Swiss banking giant UBS AG. “It's fair to expect similar results from the Swiss bank program,” she said.

With regard to public identifications of banks under investigation, Keneally said this could happen in a variety of ways, including court filings.

Re-Evaluations Possible

Speaking at a separate event in New York June 20, Best said it is possible that the IRS could go back and re-evaluate willfulness certifications if the client's bank, through treaty requests or other means, produces account records or other information indicating the client was willfully keeping the account secret.

“We could do that,” she said at the New York University School of Continuing and Professional Studies tax controversy conference in New York, answering a question from Caplin's Michel, who moderated that panel as well (120 DTR G-4, 6/23/14).

John C. McDougal, special trial attorney in the Office of Chief Counsel, Small Business/Self-Employed Division, also spoke at the June 20 event.

Public Action Key

In answer to a question from Michel, McDougal said that with regard to the 50 percent penalty for clients whose banks are under investigation, a bank would not be put in that category if it has disclosed in a financial statement that it is under investigation and has set aside a reserve to cover any possible settlement or other outcome.

“The only thing that would put the bank in that category would be a public announcement by the Justice Department,” McDougal said. However, “People would be behooved to get their disclosures in earlier rather than later,” he said. “It's very risky now to wait.”

Speaking June 20, McDougal and Best both discussed the audit procedures that could be faced by taxpayers who sign up for the streamlined procedures and assert that their conduct was non-willful.

McDougal said the IRS would continue to waive delinquency and accuracy-related penalties on “whatever you reported. If it turns out, on audit, that there was something else that wasn't reported, that might be subject to those penalties.”

Further, he said, if the audit results in a determination of fraud or willful failure to report a foreign bank account, penalties could apply there, too.

Accidental Americans

Asked about “accidental Americans”—those born in the U.S. who have lived most of their lives in a foreign country, but who spend time in the U.S. each year, such as many Canadians—Best said the streamlined procedures don't currently make an exception for them.

“That's a tough one,” she said. “We had to make policy decisions somewhere. If you spend a substantial amount of time in the United States, you need to be responsible with respect to your tax obligations in this country.”

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