IRS/Offshore Voluntary Disclosure Program (as amended 7/1/14)

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Under the IRS Offshore Voluntary Disclosure Program ("OVDP") 7/1/14 amendment the taxpayer who enters the program increases their cost since the payment is now due up front for all taxes, penalty and interest. The OVDP is now quite expensive and may wipe out the entire taxpayer offshore account.

The IRS Offshore Voluntary Disclosure Program Frequently Asked Questions and Answers (2014) #25 states that after the taxpayer is notified by IRS Criminal Investigation that the disclosure is preliminarily accepted the taxpayer will have 90 days to submit the full voluntary compliance to the IRS (Austin, Texas).

In addition to complete documentation (as required under FAQ #25), providing information on foreign accounts and assets, institutions and facilitators, and signing agreements to extend the time period for assessing Title 26 liabilities and FBAR penalties (see FAQ #7), the taxpayer must make a substantial up front payment in the total amount of tax, interest, & penalties including: offshore penalty (up to 50% of account balance) accuracy-related penalty, and any failure to file and failure to pay penalties, for the voluntary disclosure period with the information identifying the taxpayer name, taxpayer identification number and years to which the payment relates.

These payments are advance payments; consequently, any credit or refund of the payments is subject to the limitations of IRC sec, 6511.

As detailed under FAQ #7, this up front payment includes: income tax due with interest. The following penalties also apply:

1) 20% accuracy-related penalties under IRC Sec. 6662(a), on the full amount of the off-shore-related underpayments of tax for all years;

2) Failure to file (IRC Sec. 6651(a)(1), failure to pay (IRC 6651(a)(2) up to maximum of 25 % of tax due for each penalty;

3) Pay in lieu of all other penalties that may apply to the undisclosed foreign accounts, assets and entities, including FBAR and offshore related information return penalties and tax liabilities for years prior to the voluntary disclosure period, a misc. Title 26 offshore penalty equal to either 27.5% of the highest account balance of OVDP assets (as defined in FAQ# 35 during the period covered by the IRS Voluntary Disclosure) or 50% penalty for those foreign financial institutions and facilitators listed in IRS FAQ 7.2 (144 as of 10/14/16).

In summary, the tax, interest & penalty due up front may wipe out the account (or in some cases be in excess of the account balance).

Under FAQ #25(h) as of 7/14 taxpayers must provide copies of all statements for all financial accounts reflecting all account activity for each of the tax years covered by the voluntary disclosure. So for those taxpayers who are unable to provide complete account statements they risk not being accepted into the OVDP after submitting detailed financial information under the initial offshore voluntary disclosure letter to IRS Criminal Investigation who will notify taxpayers whether the offshore voluntary disclosures have been accepted as timely or declined. Once a taxpayer’s disclosure has been preliminarily accepted by CI as timely, the taxpayer must complete the submission and co-operate with the civil examiner in the resolution of the civil liability before the disclosure is complete (see FAQ #24).

Under FAQ #21, once the IRS or DOJ obtains taxpayer information under a John Doe summons (for a class of taxpayers) a treaty request, or other similar action that provide evidence of a taxpayer's non-compliance with the tax laws that particular taxpayer will become ineligible for OVDP. In addition, the IRS may determine that certain taxpayer groups that have or had accounts held at a specific financial institution will be ineligible due to US government actions in connection with the specific financial institution (as happened at Bank Leumi in Israel).

For those US taxpayers who willfully cheated on their taxes and intentionally failed to report their offshore holdings the IRS/OVDP may be their only recourse. The IRS/OVDP risks include waiver of constitutional protections under the 4th amendment (unreasonable searches), 5th amendment (right against self-incrimination), 8th amendment (excessive fines). In addition the statute of limitations is extended to 8 years (from a maximum of 6 years) and the evidence is submitted without either transactional or use immunity so if the taxpayer is not accepted into the program or is otherwise later disqualified the same evidence submitted may be used against them.

However, if the taxpayer was mislead by 3rd party advisors, or had a mistaken good faith belief that they were not obligated to report the accounts (see US Supreme Court 1991 case Cheek v. US) they may have alternative to the IRS/OVDP which I have successfully used on behalf of taxpayers which is a full disclosure(protective election), request for a waiver of penalties under a reasonable cause exception supported by a tax opinion (citing legal authority) and if advisable a lawsuit against those responsible third party advisors who mislead taxpayers (the lawsuit may eliminate scienter i.e. willfulness which may pre-empt criminal tax evasion charges, or civil tax fraud penalties, as well as provide a source of recovery for damages; in addition if the lawsuit is for fraud, taxpayer may be entitled to a theft tax loss which is an ordinary tax loss (IRC Sec. 165) and can be carried back for 3 tax years for tax refunds and carried forward for 20 years for tax free income up to the amount of the theft/tax loss).