

NEW VOLUNTARY DISCLOSURE PROCEDURE FOR OFFSHORE ACCOUNTS

Gideon Rothschild
Moses & Singer LLP

Amidst the UBS investigation of offshore bank accounts, the Internal Revenue Service announced, in a memo dated March 23, a new guideline to encourage US taxpayers to come clean on their offshore accounts without the risk of criminal prosecution and significantly increased penalties.

Although there has been a voluntary compliance program in place for many years on an informal basis, many taxpayers have been reluctant to come forward for fear that the penalties can exceed the amounts in the offshore accounts. The new program sets forth maximum civil penalties and an agreement not to criminally prosecute. It is to be administered centrally in the Philadelphia service center to ensure uniformity in the assessment of tax and penalties. Taxpayers who wish to avail themselves of this offer must come forward prior to September 23, 2009. Commissioner Shulman said that “[F]or taxpayers who continue to hide their head in the sand, the situation will only become more dire”, including potential criminal prosecution.

Taxpayers may avail themselves of the reduced penalties provided they are not yet subjects of a criminal investigation and cooperate fully with the IRS. It is not clear to what extent such cooperation will be a prerequisite to accepting the reduced penalties. This writer believes that all details regarding the source of the funds, how the taxpayer opened the account and whether there were other professionals involved in the establishment of the account or any company or trust formations will be required to be disclosed.

Voluntary disclosure requests will be resolved under the following framework::

1. The taxpayer must file amended returns including Form TDF 90-22.1 (Foreign Bank Account Return (FBAR)) and informational returns (i.e. Form 3520 or 5471) for the preceding six years (unless the account(s) were opened less than six years ago, then for such number of years they existed)
2. The payment of tax and interest for the six years plus a payment of the accuracy related penalty of 20% or a 25% penalty for failure to timely file. Reasonable cause will not be accepted as a defense to such penalties.
3. The payment of a 20% penalty on the highest balance in the offshore account during such six year period. This penalty may be reduced to 5% if the taxpayer did not open or create the foreign account (e.g., it was inherited), has never withdrawn funds from the account or added funds thereto and all US taxes were previously paid on the funds deposited in the account.

A taxpayer who wishes to come clean will proceed through the Criminal Investigation Division which will then process the returns in accordance with the IRM Section 9.5.11.9. (<http://www.irs.gov/irm/part9/ch05s13.html>) If the taxpayer meets all the requirements, the returns will then be forwarded to the Philadelphia Offshore Identification Unit (POIU) for examination, which will then issue a closing letter.

Prior to this announcement, taxpayers had the option of making a formal voluntary compliance offer through the CID (often referred to as a “noisy filing”) or simply filing the amended returns in the mail (a “stealth filing”). The unknown factor up until now in either case has been how the FBAR penalties will be assessed. These penalties were recently increased to the greater of \$100,000 or 50% of the highest balance in the account for each year of nonfiling. The current initiative will resolve this uncertainty in favor of a one time 20% penalty. Taxpayers who file under this initiative will also avoid numerous other potential penalties and possible criminal prosecution. It is this author’s view that taxpayers with unreported offshore income should RUN, not walk, to their tax attorney and seek to resolve their delinquency prior to the six month deadline.

Further information can be found at:

<http://www.irs.gov/newsroom/article/0,,id=206012,00.html>

MOSES & SINGER LLP

Disclaimer

Viewing this document or contacting Moses & Singer LLP does not create an attorney-client relationship.

This document is intended as a general comment on certain recent developments in the law. It does not contain a complete legal analysis or constitute an opinion of Moses & Singer LLP or any member of the firm on the legal issues herein described. This document contains timely information that may eventually be modified or rendered incorrect by future legislative or judicial developments. It is recommended that readers not rely on this general guide in structuring or analyzing individual transactions or matters but that professional advice be sought in connection with any such transaction or matter.

Attorney Advertising

It is possible that under the laws, rules or regulations of certain jurisdictions, this document may be construed as an advertisement or solicitation.