



Federal Bar
Association

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Updated Voluntary Disclosure Procedures

Is this the Correct Path for Your
Noncompliant Client?



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Speakers

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Objectives

- History of Voluntary Disclosure Practice
- New Guidance Issued November 20, 2018
- Benefits and Burdens of Proceeding under New Framework
- Alternatives for Noncompliant Taxpayers



History of Voluntary Disclosure Practice



History of Voluntary Disclosure Practice

Long before offshore financial accounts became an enforcement target for IRS and DOJ, both IRS and DOJ observed voluntary disclosure practices.

- IRS practice to consider truthful, timely and complete disclosure of noncompliance as a factor in deciding whether to refer for prosecution.
- DOJ policy that if putative defendant complied in all respects with IRS voluntary disclosure practice, Tax Division may consider that factor in its exercise of prosecutorial discretion.

Neither created substantive or procedural rights, but, as a practical matter, truthful, timely and complete voluntary disclosure protected taxpayers from criminal prosecution.



History of Voluntary Disclosure Practice

IRS Voluntary Disclosure Practice IRM 9.5.11.9 (12-02-2009)

- Legal source income only.
- Disclosure must be truthful, timely and complete.
- Disclosure is timely if received before:
 - IRS initiated civil exam or criminal investigation of taxpayer
 - IRS received information from third party re specific taxpayer
 - IRS initiated civil exam or criminal investigation directly related to specific liability of taxpayer
 - IRS acquired information directly related to specific liability of taxpayer from a criminal enforcement action.
- Taxpayer must cooperate with IRS in determining correct liability.
- Taxpayer must make good faith arrangements to pay in full.



History of Voluntary Disclosure Practice

Practice was more informal and varied before offshore enforcement.

Taxpayer's counsel would have anonymous conversations with agents in IRS Criminal Investigations, then disclose identifying information after ascertaining anticipated result for the taxpayer.

Practices changed considerably over the years of various offshore voluntary disclosure initiatives and programs.

Counsel faced considerable uncertainty about what rules applied to domestic disclosures and whether informal practice of the past remained acceptable.



Summary of OVDP Evolution

	2009 Offshore Voluntary Disclosure Program	2011 Offshore Voluntary Disclosure Initiative	2012 Offshore Voluntary Disclosure Program	Modified 2012 Offshore Voluntary Disclosure Program
CI protection	Yes	Yes	Yes	Yes
Information required for preclearance by CI	Name, address, date of birth, and TIN	Name, address, date of birth, and TIN	Name, address, date of birth, and TIN	Name, address, date of birth, TIN, telephone number, identifying information of all financial institutions at which undisclosed accounts were held, and identifying information of all foreign and domestic entities (e.g., corporations, partnerships, LLCs, trusts, foundations) through which undisclosed accounts were held
Penalty terms	Miscellaneous Title 26 offshore penalty of 20% in lieu of other applicable penalties	Miscellaneous Title 26 offshore penalty of 25% in lieu of other applicable penalties Reduced penalty of 5% offered to taxpayers meeting certain criteria deemed to be non-willful conduct Reduced penalty of 12.5% for taxpayers with accounts with balances below \$75,000	Miscellaneous Title 26 offshore penalty of 27.5% in lieu of other applicable penalties Reduced penalty of 5% offered to taxpayers meeting certain criteria deemed to be non-willful conduct Reduced penalty of 12.5% for taxpayers with accounts with balances below \$75,000	Miscellaneous Title 26 offshore penalty of 27.5% in lieu of other applicable penalties The miscellaneous offshore penalty increases to 50% if the taxpayer has or had an undisclosed foreign financial account held at a foreign financial institution or if the account was established with the help of a facilitator where the institution or facilitator has been publicly identified as being under investigation or cooperating with a government investigation.
Covered period	6 years	8 years	8 years	8 years
Closing agreement	Yes	Yes	Yes	Yes
Relief for taxpayers who did not timely elect to defer U.S. income tax on undistributed income earned by certain registered Canadian retirement and savings plans	No	No	Yes	Yes

History of Voluntary Disclosure Practice

OVDP

More than 57,000 taxpayers made disclosures

Over \$11.6 billion collected

Streamlined Procedures

More than 73,000 taxpayers made submissions

Statistics from September 2018



History of Voluntary Disclosure Practice

OVDP closed on September 28, 2018

The closing of the OVDP ends the unique civil settlement structure of OVDP and terminates all special provisions of OVDP (including but not limited to the alternative PFIC computation and the “miscellaneous offshore penalty”).

“Since the announcement, the IRS has not received any public comments addressing a continued need for the OVDP.” IR-2018-176, Sept. 4, 2018

However, the ABA submitted public comments to the OVDP on May 2, 2018 and those comments have been published in the recent edition of the Tax Lawyer.



New Guidance Issued November 20, 2018



Procedures in November 2018 Guidance

- The voluntary disclosure practice will remain centralized with Criminal Investigation in Philadelphia.
- Criminal Investigation now requires preclearance for all voluntary disclosures.
- IRS is revising Form 14457 to be used for two steps in the voluntary disclosure process.



Procedures in November 2018 Guidance

- Once Criminal Investigation preliminarily accepts submissions, it will forward cases to a civil compliance unit in Austin for distribution to the appropriate civil examination unit.
- All voluntary disclosures will be assigned for examination and follow standard examination procedures.
- The IRS expects the majority of cases to be resolved by agreement.



Framework in November 2018 Guidance

- Voluntary disclosures will generally include a 6 year disclosure period.
- Taxpayers must submit all required returns and reports for the disclosure period.
- Taxpayer cooperation is required.
- Examiners will use the interim guidance in considering penalties.



Framework in November 2018 Guidance

Fraud Penalties will be asserted as follows:

- Civil fraud penalty will apply to one year with the highest tax liability
- Examiners may apply civil fraud penalty to more than one year, up to all six years, based on facts and circumstances, for example, if there is no agreement to tax liability
- Examiners may apply civil fraud penalty beyond six years if taxpayer fails to cooperate and resolve examination by agreement



Framework in November 2018 Guidance

Other Penalties will be asserted as follows:

- Willful FBAR penalties will be asserted in accordance with existing IRS penalty guidelines under IRM 4.26.16 and 4.26.17
- Penalties for failure to file information returns will be at examiner's discretion
- Penalties related to excise taxes, employments taxes, estate and gift tax, etc. will be based on facts and circumstances with examiners coordinating with subject matter experts



Framework in November 2018 Guidance

Taxpayers may:

- Request imposition of accuracy related penalties instead of civil fraud penalties or non-willful FBAR penalties instead of willful penalties. Given the objective of the voluntary disclosure practice, granting requests for the imposition of lesser penalties is expected to be exceptional. The taxpayer must present convincing evidence to justify the reduction.
- Request an appeal with the Office of Appeals.



Framework in November 2018 Guidance

Revocation of Preliminary Acceptance:

“The Service will provide procedures for civil examiners to request revocation of preliminary acceptance when taxpayers fail to cooperate with civil disposition of cases.”

Revocation = potential criminal prosecution



Benefits and Burdens of Proceeding under New Framework



Benefits of New Framework

- Avoidance of criminal prosecution if taxpayer is willing to concede to all demands by civil examiner.
- Some degree of predictability.
- Some reduction in likely penalty exposure.
- Most beneficial for clients with high risk of criminal prosecution who are willing to pay anything to mitigate that risk.



Burdens of New Framework

- Fraud penalty and/or willful FBAR penalty with limited exceptions
- Failure to reach agreement with examiner may trigger penalties for all years in scope.
- Failure to cooperate could result in expansion of exam beyond six years, multiple penalties and revocation of acceptance.



Alternatives for Noncompliant Taxpayers



Alternatives for Offshore Compliance Issues

Eligibility for Streamlined Procedures

- US individual and estates only
- Failed to report foreign financial assets or pay all related tax due
- Certify non-willfulness
- Not currently under IRS civil exam or criminal investigation
- Valid TIN



Alternatives for Offshore Compliance Issues

Streamlined Procedures

- SFO (streamlined foreign offshore), Form 14653
 - Meet non-residency requirement
 - Provide delinquent or amended income tax returns
 - No penalties
- SDO (streamlined domestic offshore), Form 14654
 - Do not meet SFO residency requirements
 - Must have filed income tax returns before submitting amended returns through procedures
 - 5% penalty on foreign financial assets



Alternatives for Offshore Compliance Issues

Streamlined Foreign Offshore Non-Residency Requirements

In any one or more of the most recent three years

- Not have a U.S. abode and
- Physically outside the United States for at least 330 full days

Both taxpayers on joint return must meet residency requirements

• Snowbird Issue— some taxpayers fail SFO if present in US more than 35 days/year but cannot use SDO because they did not file income tax returns



Alternatives for Offshore Compliance Issues

Certifications for Streamlined Procedures

- Non-willful conduct is conduct that is due to negligence, inadvertence, or mistake or conduct that is the result of a good faith misunderstanding of the requirements of the law.
- Must include narrative signed under penalties of perjury
 - Specific reasons and background
 - Whole story, including favorable and unfavorable facts
 - Explain source of funds
 - Explain contacts with account / asset



Alternatives for Offshore Compliance Issues

Delinquent FBAR Procedures

- File all FBARs electronically with FinCEN
- Select reason for filing late on cover page
- Include statement explaining late filing



Alternatives for Offshore Compliance Issues

Delinquent Information Return Procedures

Taxpayers who:

- have not filed required international information returns,
- have reasonable cause,
- are not under civil examination/criminal investigation, and
- have not been contacted about the delinquent information returns

May file the delinquent information returns with a statement of all facts establishing reasonable cause for the failure to file.

Penalties may be imposed if the Service does not accept the explanation of reasonable cause.



Alternatives for Domestic Compliance Issues

Voluntary Classification Settlement Program

- Allows taxpayers to reclassify workers as employees for employment tax purposes
 - Agree to prospectively treat class of workers as employees
 - Pay 10% of employment tax liability for those workers for most recent tax year, no interest or penalties
 - Protection from employment tax audit on those workers for prior years
- Apply using Form 8952
- Announcement 2012-45
 - Taxpayers under IRS audit other than employment tax audit are eligible



Alternatives for Domestic Compliance Issues

File Original and/or Amended Returns and Pay

Payment or Deposit without Disclosure or Amended Return

Future Compliance Only

- Benefits
- Consequences
- Limitation issues

