

Tax

IRS to end Offshore Voluntary Disclosure Program

By **Veronika Chang**

Veronika Chang

(March 21, 2018, 9:07 AM EDT) -- On March 13, 2018, the Internal Revenue Service (IRS) announced it will begin to "ramp down" the 2014 Offshore Voluntary Disclosure Program (OVDP) and close it Sept. 28.

In 2009, the IRS launched the 2009 Offshore Voluntary Disclosure Initiative. It encouraged taxpayers with hidden offshore assets and income to come clean with the IRS. In exchange for voluntary disclosure, taxpayers were offered a fixed-penalty structure, rather than face substantial civil penalties and risk criminal prosecution.

Under the 2009 OVDI, taxpayers had to file six years of tax and information returns, including FBARs (Report of Foreign Bank and Financial Accounts). They also had to pay the taxes and interest due, a fixed penalty under the *Internal Revenue Code*, and a 20 per cent miscellaneous offshore penalty based on the amount in their non-U.S. bank accounts in the year with the highest aggregate balance. In October 2009, the OVDI closed after only seven months, but the IRS opened another voluntary disclosure program in February 2011.

Terms of the 2011 OVDI were similar to the 2009 OVDI, but now taxpayers had to disclose eight years of tax and information returns, and were subject to an offshore penalty of 25 per cent. The new program offered a break for those with offshore assets of \$75,000 or less by reducing the miscellaneous offshore penalty to 12.5 per cent. Like its predecessor, the 2011 OVDI closed seven months later.

In January 2012, the IRS opened the 2012 Offshore Voluntary Disclosure Program (2012 OVDP). This time the IRS kept the number of years for disclosure to eight, but increased the offshore penalty to 27.5 per cent. Unlike the previous two voluntary disclosure initiatives, the 2012 OVDP was open-ended with no closing date. However, in mid-2014, the IRS altered terms of the 2012 OVDP.

The major change was that the offshore penalty was increased to 50 per cent for taxpayers with an undisclosed bank account which had been subject to investigation by the U.S. Department of Justice or the IRS. Big name Swiss banks such as UBS and Credit Suisse are on the IRS' blacklist. At the same time, the IRS simplified things for innocent taxpayers (those with "non-willful" violation) by opening a Streamlined Filing Compliance Procedure. Under this streamlined program, taxpayers had to file three years of tax returns and six years of FBARs. Most importantly, the IRS imposed no penalty for those residing outside the country and a five per cent penalty for those residing in the country.

Many U.S. citizens and green card holders residing in Canada took advantage of the streamlined program and fared better than those who had come forward earlier and paid penalties. There was an option to opt-out of the OVDP and transition into the streamlined program, but by then taxpayers who had initially applied to the OVDP would have invested heavily in compliance and legal costs. Like the 2014 OVDP, the streamlined program is open-ended with no closing date.

So, why is the IRS closing the OVDP now?

The IRS says "there has been a significant decline in the number of taxpayers participating, as well as an increase in awareness of offshore tax and reporting obligations." The IRS also stressed that "stopping offshore tax noncompliance remains a top priority." Since its launch in 2009, the OVDP has netted the IRS more than \$11 billion from some 56,000 taxpayers.

An additional 65,000 taxpayers came into compliance with the streamlined program, which remains open for now, but like the OVDP it could close anytime. Thus, those eligible for the streamlined program should consider taking advantage of it now.

Here is an important thing to note with the streamlined program. It requires the taxpayer to certify that their failure to file all required tax and information returns was due to non-willful conduct. The IRS defines that as "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.”

The IRS voluntary disclosure program, along with FATCA (*Foreign Account Tax Compliance Act*), has garnered much publicity. As a result, it is less likely now than in 2009 for a U.S. citizen living in Canada to argue they didn't know about U.S. tax-filing requirements. Whether or not one can certify about “non-willfulness” for the streamlined program should be analyzed closely.

Merely filing returns without making a voluntary disclosure to the IRS is not recommended. The IRS calls this a “quiet disclosure.” In announcing the closing of the 2014 OVDP, the IRS warned that all quiet disclosures will be reviewed and subject to civil or criminal penalties.

Without the OVDP or the streamlined program, penalties can be significant. Failure to file certain returns, including FBAR, carries a minimum penalty of \$10,000 per year. A maximum penalty for failing to file FBAR can cost up to 50 per cent of your account balance. With the increased co-operation between the countries (and better technology), it is now certain that Canada and the U.S. will exchange information.

Today it is not unusual for a Canadian bank to ask customers if they are American citizens or U.S. green card holders when they open a new account. It is recommended that a U.S. citizen or someone who holds a green card come into compliance sooner rather than later. You will sleep better at night.

Veronika Chang is a lawyer with Morris Kepes Winters LLP in Toronto. She is a tax specialist with extensive experience working in the United States.

Photo credit / mj0007 ISTOCKPHOTO.COM