

Voluntary Disclosure

In June 2014, the IRS announced modifications to the existing 2012 Offshore Voluntary Disclosure Programme “OVDP” which would take effect on July 1, 2014 in conjunction with the implementation of FATCA (Foreign Account Tax Compliance Act).

In addition, several modifications were also announced to the Streamlined Filing Compliance Programme which were helpful in allowing significantly more taxpayers to participate, including those living in the US and those who had previously filed incomplete US tax returns.

Offshore Voluntary Disclosure Program

The 2012 OVDP followed on from earlier programs that were available in 2009 and in 2011 both of which were only available for limited time periods, being 23 March 2009 to 15 October 2009, and 8 February 2011 to 9 September 2011 respectively. The 2012 OVDP was open-ended although the IRS announced that it reserved the right to change the terms of the program on a prospective basis at any time as well as the right to end the programme.

The focus of the initial 2009 program was on taxpayers in the US who had knowingly failed to report the existence of funds situated outside the US, and the income from these funds. The program was drawn so broadly that it applied equally to US taxpayers outside the US who had failed to file information and tax returns. The 2011 program was introduced to follow up on the success of the 2009 program and included some reductions in the fixed penalties for overseas taxpayers falling within certain categories.

For the IRS, both of these programs proved very successful: at the same time as the 2012 OVDP was announced IRS Commissioner Shulman announced that the 2009 program at that time had raised \$3.4bn with a further \$1bn arising from the 2011 program. At the time the 2014 changes were announced, it was revealed that \$6.5bn had been collected from 45,000 disclosures in all programs.

The programs have required full disclosure and operate on a fixed non-negotiable penalty basis. In return the taxpayer once accepted into the program is protected against any criminal prosecution (unless the income now disclosed is from illegal sources). In addition the IRS will not go back beyond the earliest year required to be filed under the particular program.

If a taxpayer thinks they may be a candidate for the program they should consider consulting with an attorney in the first instance as the attorney-client privilege does not exist between a tax advisor and his client.

Taxpayers in the OVDP must file tax returns and all information returns for eight years. They must pay all back taxes and any interest, accuracy or delinquency penalties that might apply.

Taxpayers must also pay a 27.5% or 50% 'offshore penalty' equal to the highest total asset value in all unreported foreign financial accounts and entities. The fixed penalty is based on the highest value of these during the period not on the income arising from them. IRS agents have no discretion in assessing this penalty under the program and will not consider reasonable cause. The value of foreign businesses, real estate, and artwork producing, or acquired with, unreported income may be considered for the penalty calculation.

Taxpayers are also required to submit copies of their bank statements for all foreign accounts for the disclosure period.

For submissions made beginning July 1, 2014, the IRS has modified some terms of the 2012 program and may be referred to as the 2014 OVDP.

A 50% offshore penalty (rather than the 'regular' 27.5% penalty) will be applied where the foreign financial institution in which the taxpayer held the account or advisor who helped set up or maintain the account has been publicly identified by the IRS or is under investigation or cooperating with an investigation. The current list of such parties is found here: <http://www.irs.gov/Businesses/International-Businesses/Foreign-Financial-Institutions-or-Facilitators>.

Another key change is that the offshore penalty must be computed and paid with the OVDP submission

The full list of instructions for submission under OVDP, presented as a series of frequently asked questions is found here: <http://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers-2012-Revised>

Streamlined Filing Compliance Procedures

The introduction of the original Streamlined Procedures which were introduced from September 1, 2012, acknowledged that many taxpayers coming forward were US citizens living and working overseas who had been fully compliant in the country where they lived, but had for some reason or another been delinquent in filing US tax returns and did not need to seek the criminal protection offered by the OVDP program.

The Streamlined Procedures simplified the filings required in coming forward to just three years of delinquent tax returns and six years of FBARs, and provided penalty protection.

However the original procedure suggested taxpayers making submissions should fall under strict "low risk" parameters which included such conditions as owing less than \$1,500 per year in US tax, having bank accounts only in the country of their residence and living outside the US during the entire disclosure period. Many people failed to fall within these parameters and this created a significant pool of taxpayers that really did not fall into either program.

Our firm, along with the others in our industry, had been actively advocating on behalf of our clients with the IRS in expressing our views and providing feedback on the shortcomings of the original Streamlined Procedures. Important changes have now been made to the program which went into effect on July 1, 2014 which make it available to a much wider demographic.

Taxpayers living both the US or outside the US may use the new Procedures and must enter under the Streamlined Foreign Offshore Procedures or under the Streamlined Domestic Offshore Procedures based on where they have been resident. There are penalties attached to the Domestic Procedures which do not apply to the Foreign Procedures.

The threshold question under the revised procedures is whether the taxpayer's non-reporting of foreign assets is non-willful. All taxpayers whose conduct was non-willful, regardless of tax owed and the other previous 'high risk' factors are invited to take advantage of the appropriate Streamline Procedure.

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."

Taxpayers whose conduct was willful should consider entering the OVDP.

Below are some frequently asked questions in respect of the revised procedures:

Which type of taxpayer is eligible to file under the Streamlined Procedures?

Individuals & estates of individuals

How do I determine if I qualify for the Foreign or Domestic Procedures?

Generally, if you have lived outside the US for one of the three years in the submission period, you will qualify for submission under the Foreign Procedure (although more than 35 days back in the US in that year may be problematic). For a joint return, both spouses must qualify, otherwise you will fall under the domestic procedures.

Is there a difference between the two programs? What are the penalties?

The Domestic Procedures require that the taxpayer has previously submitted all returns, failing only to disclose in respect of to foreign assets. The taxpayer will also be subject to a penalty of 5% of the highest aggregate balance/value on the undisclosed assets during the years covered by the returns and FBARS. Those participating under the foreign offshore procedures will not be subject to this – or indeed any - penalty.

What do I file under the Streamlined Procedures?

You will file three years of tax returns (or amended tax returns) and/or information returns, pay all tax due including interest along with six years of foreign bank reports (the so-called, FBARS now FinCEN Form 114) and a signed declaration of non-willful conduct. This declaration will require you to disclose the specific reasons for your non-compliance. This document is key to the submission being accepted under the Streamline Procedures.

What if I submitted my returns through the 2012 Streamlined Procedures?

If you have already submitted returns through the prior Streamlined Procedures but have not received a risk determination letter, the submission will be processed under the updated procedures.

What is the deadline for submission?

There is no set deadline as it is an ongoing program until further notice. However, following the onset of FATCA and other information exchange, taxpayers should be advised to correct any errors in filing as quickly as possible.

What if I am currently under audit/investigation with the IRS?

If you are currently under investigation with the IRS even if it does not relate to the undisclosed foreign asset, you will be ineligible.

I received an FBAR warning letter, am I disqualified from filing under the Streamlined Procedures?

If you have received a letter of warning or penalty assessment, you are ineligible.

I filed under the Streamlined Procedures but think I should go through the OVDP – can I switch?

Once you have made a submission under Streamlined, you are no longer eligible to apply for acceptance under OVDP. If you are concerned with criminal prosecution, please consult with an attorney before making any submission. If you have submitted a voluntary disclosure letter under OVDP prior to July 1, 2014 but have not received a closing letter and would qualify under the new streamlined procedures, you can request treatment under the penalty terms of Streamlined rather than opting out. You will still need to certify that failure to comply was non-willful.

Will I receive a closing letter once my returns have been processed under the Streamlined Procedures?

You will not receive a closing letter. All returns submitted under Streamlined will be processed with other returns and will not automatically be subject to audit, only under the normal audit selection process.

For more detailed information please use the links below:

<http://www.irs.gov/Individuals/International-Taxpayers/Streamlined-Filing-Compliance-Procedures>

<http://www.irs.gov/Individuals/International-Taxpayers/U-S-Taxpayers-Residing-Outside-the-United-States>

<http://www.irs.gov/Individuals/International-Taxpayers/U-S-Taxpayers-Residing-in-the-United-States>

Further information and important notice

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