

## IRS Promises New Procedure for Taxpayers Who Haven't Filed But Owe No Tax And Indefinitely Extends Offshore Voluntary Disclosure (OVDI) Program

By Roy A. Berg JD, LL.M. (US Tax) on Monday, 09 January 2012

On January 9, 2012 the IRS issued [IR 2012-5](#), which makes two very important announcements: First, it promises new procedures to bring unfiled returns current for taxpayers who have not filed, but owe no tax. Second, it indefinitely extends the basic terms of the 2011 Offshore Voluntary Disclosure Initiative ([OVDI](#)).

### **Promise of New Procedure to Bring Unfiled Returns Current if No Tax is Owed**

Although cryptic, this statement is the most important element of the IRS's announcement and warrants setting it forth in full:

*"The IRS recognizes that its success in offshore enforcement and in disclosure programs has raised awareness related to tax filing obligations. This includes awareness by dual citizens and others who may be delinquent in filing, but owe no US tax. The IRS is currently developing procedures by which these taxpayers may come into compliance with US tax law."*

There is already a process in place, it just isn't very pleasant and does contain some risk.

While Canadian politicians and the US Ambassador [have made similar promises](#), this is the first time the IRS has made such an announcement. It remains to be seen what these procedures will entail and whether they will be different than the IRS announced in [FS 2011-13](#) issued on December 7, 2011. It is, however, a very promising development.

### **Indefinite Extension of the Basic Terms of 2012 OVDI**

The announcement makes clear that basic terms of the 2011 OVDI will be extended indefinitely for those who wish to avail themselves of that procedure to bring unfiled returns current. Under the OVDI taxpayers were required to file eight years of returns (including income tax returns, FBARs, and other forms), and pay a penalty in exchange for relief from criminal prosecution. The penalty ranged from 25% of the taxpayer's foreign assets and, in some cases, was reduced to 5% of the amount held in foreign accounts.

Under the procedure announced today, the maximum penalty is increased to 27.5% of the taxpayer's foreign assets, but the reduced 5% penalty remains unchanged. However, the IRS states that the rules of the procedure could change at any time:

*"For example, the IRS may increase penalties in the program for all or some taxpayers or defined classes of taxpayers - or decide to end the program entirely at any point."*

While this is welcome news for those who missed the deadlines imposed by the 2011 OVDI, it fails to address the many ambiguities and uncertainties that persist in the program. In particular:

- Are registered accounts (Canadian RRSPs, RIFs, RESPs and the like) to be included in the penalty calculation?
- Are Canadian spousal RRSPs included in the penalty calculation?

- Are we able to reduce the penalty base for gains, withdrawal penalties, and taxes?
- Will we be able to make a “reasonable cause” argument for a late election to defer tax in an RRSP?

Finally, while the OVDI made clear that the taxpayer could not argue “reasonable cause” for abatement of penalties within the program, it is unclear whether this preclusion will continue under the new initiative.

### **Possible IRS Motivation**

It is possible that the IRS's decision to make the announcement is the result of three important developments:

- First, the Taxpayer Advocate Service's Directive issued on August 16, 2011. The Directive acknowledged problems in the 2009 OVDP that resulted in inequitable treatment of similar taxpayers and directed the IRS to address these problems - see [Shamik Trivedi's article](#) on the issue.
- Second, the IRS likely recognized that the publicity surrounding the OVDI and OVDP will make it increasingly difficult for the taxpayer to assert that failure to file FBARS was not willful.
- Third, and similarly, the IRS likely recognized that such publicity will make it difficult for the taxpayer to assert ignorance as a basis of making a reasonable cause argument.
- Fourth, objections raised by the US expatriate communities in Canada and India and sympathetic foreign officials like Minister Flaherty.

Considering the foregoing, we believe the new program is very beneficial to unwitting taxpayers who, otherwise, would have no mechanism to bring returns current without the possible application of draconian penalties.