TAX ALERT

***By Robert J. Alter, Esq.*[1]**

The Internal Revenue Service (IRS) announced that it reopened its previously closed offshore voluntary disclosure program. The program offers taxpayers who are concealing offshore accounts/assets, and who failed to participate in prior programs, one more chance to get current with their taxes.

By way of background, the IRS unveiled its first offshore voluntary disclosure program in 2009, directed toward voluntarily disclosing unreported offshore income for 2003 through 2008. In February, 2011 the IRS followed up with a second offshore voluntary tax disclosure program directed to the 2003 through 2010 period, imposing higher penalties than the original disclosure program, but with mitigation in certain circumstances. The 2011 program expired on September 9, 2011

As a result of those programs, the IRS collected $4.4 billion from over 33,000 disclosures and continues its aggressive enforcement initiatives in this area, which include ongoing efforts with the U.S. Department of Justice to pursue criminal investigations/prosecutions of offshore tax evasion. In that regard, recent news articles have identified several Swiss, Asian, Israeli and Indian banks as being under scrutiny, and those investigations will, in all probability, result in the eventual disclosure of *thousands* of taxpayers' identities to the IRS. This is an extremely target rich environment for the government.

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The terms of the third program are similar in many ways to the 2011 program with some key differences. Unlike the prior program, there is no set deadline for taxpayers to apply and the program will remain open for an indefinite period. However, the IRS has said that this program can change at any time going forward (e.g., IRS may increase penalties, or decide to end the program).

The overall penalty structure of the new program is the same as the 2011 structure, except that the highest penalty was raised to 27.5 percent from the 25 percent charged in 2011 and 20 percent in 2009. Accordingly, the five-tier penalty structure for the miscellaneous penalty under the revived program is as follows:

- 27.5 percent of the highest aggregate balance in foreign accounts/entities or value of foreign assets during the eight years prior to the disclosure;
- 12.5 percent for taxpayers with unreported accounts/assets under $75,000;
- 5 percent for some taxpayers who meet certain narrowly defined conditions;
- No penalty for taxpayers who have no unreported income associated with the unreported account or entities; and
- Taxpayers who believe that they owe no penalties or smaller penalties under applicable law can opt out of the program and possibly undergo a full-scale examination.

Participants in the reopened program must file all original and amended tax returns, include a payment for back taxes and interest for up to eight years, as well as pay accuracy related and/or delinquency penalties and disclose the banks and advisers that helped them escape U.S. tax laws.

By reopening the offshore voluntary disclosure program in the manner in which it did, the IRS made things easier for all affected taxpayers and their advisers by removing the significant uncertainty which had existed concerning the ultimate financial consequences of coming forward after the 2011 offshore voluntary disclosure program expired.

In addition, the IRS' extension of its Offshore Voluntary Compliance Initiative was intended to dovetail with Congress' recent enactment of the Foreign Account Tax Compliance Act ("FATCA") under which banks, investment advisory firms, and similar financial institutions outside the United States are required to report to the IRS information about financial accounts held by U.S. taxpayers, or by foreign entities in which U.S. taxpayers hold a substantial ownership interest.

As more countries decide to work with the IRS to implement FATCA, the tax information the IRS seeks will become increasingly available, making it more likely that the IRS will discover the vast majority of unreported foreign accounts of U.S. taxpayers.

Furthermore, FATCA requires that taxpayers report foreign accounts by attaching Form 8938 to their 2011 federal income tax returns, as well as timely file Foreign Bank Account Reports (FBAR's).

For many individuals and entities with undisclosed foreign accounts/assets and unreported income from international sources, the revived voluntary disclosure program – with its known civil penalty outcome – is their last, best option to escape criminal prosecution and avoid much larger civil tax penalties in an environment where the IRS is getting more information under new disclosure requirements and following more leads from ongoing foreign bank investigations. However, it is critical that these taxpayers and their advisers recognize that time is of the essence here, since it will be too late to participate in this program if a foreign bank discloses the taxpayer's name to the IRS first. Waiting is simply not a viable option.

For assistance in determining how these developments may affect you, and whether to make a voluntary disclosure to become compliant with the IRS and State tax rules, please contact Bob Alter at McElroy Deutsch.