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IRS to Allow Extensions of August 31 OVDI Application Deadline

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Summary by [taxanalysts](#)

Taxpayers may request a 90-day extension of the August 31 offshore voluntary disclosure initiative application deadline, the IRS announced June 2 in an update to the initiative's frequently asked questions Web page.

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Taxpayers may request a 90-day extension of the August 31 offshore voluntary disclosure initiative (OVDI) application deadline, the IRS announced June 2 in an update to the initiative's frequently asked questions Web page.

The IRS also released a new Opt Out and Removal Guide that includes steps that should be taken before and after opting out or being removed, sample letters, a rundown of penalties that may apply to a taxpayer, and a list of possible exceptions to the three-year statute of limitations for individuals who have opted out or been removed. (For the FAQ, see [Doc 2011-11976](#) . For the guide, see [Doc 2011-11975](#) .)

Significant offshore penalty relief was also added in FAQ 52 for U.S. citizens who reside in foreign countries, have been fully compliant with the tax laws in those countries, and have U.S.-source income of \$10,000 or less per year. Rather than being subject to a 25 percent offshore penalty on their net worth under the general OVDI, those individuals may be eligible for a reduced 5 percent offshore penalty that would apply only to the value of their financial accounts.

The deadline extension "is huge for a lot of people," said Mark E. Matthews, a partner at Morgan, Lewis & Bockius LLP, who added that the relief may enable some practitioners to take on additional clients.

"Everybody's scrambling with this August 31 deadline," said Larry A. Campagna, an attorney with Chamberlain, Hrdlicka, White, Williams & Martin. He said it's a struggle to get the necessary documents from foreign financial institutions. "We had people under the first program where it took literally two years to gather the documents we needed to answer the questions," he said.

FAQ 25 states that a written request for an extension must include properly completed and signed agreements to extend the period of time to assess tax and foreign bank account report penalties and a statement outlining which materials are missing from the taxpayer's submission, why they are missing, and what steps the taxpayer has taken to secure those materials.

Only those taxpayers who can demonstrate a good faith attempt to fully comply with FAQ 25 on or before August 31 will be considered for an extension. Among other things, the FAQ 25 submission must include copies of filed original and amended returns, various completed forms required by the initiative, and in some cases, copies of offshore financial account statements. If the submission is not full and complete, the taxpayer will not be accepted into the program.

The OVDI, which was announced February 8, provides an opportunity for a taxpayer to disclose his previously unreported offshore financial account in exchange for a reduced 25 percent penalty (or in some cases, a 5 or 12.5 percent penalty) on the highest aggregate amount in the account between 2003 and 2010 and payment of up to eight years of taxes and interest. The 2009 special offshore voluntary disclosure program (OVDP) had offered a base 20 percent penalty and resulted in about 14,700 disclosures over a period of nearly seven months. (For prior coverage, see *Doc 2011-9908* or *2011 TNT 90-2*.)

Opt Out and Removal Procedures

A taxpayer who opts out of or is removed from the civil settlement structure of either the 2011 OVDI or the 2009 OVDP will generally be subject to a full-scope exam under the standard audit process. The new guidance provides that a taxpayer may choose to opt out because the results under the applicable voluntary disclosure program "appear too severe given the facts of the case" and that "the taxpayer should not be treated in a negative fashion merely because he or she chooses to opt out."

"The 2009 program said that if you were entitled to a lesser penalty, then you would get it, but now you have to opt out to get it," Campagna said. But by opting out, he said, "you have to go through a full-blown examination and risk that a revenue agent asserts much greater penalties to exert leverage on the taxpayer to settle the case. Those threats have been made."

Campagna said that even if a taxpayer in the OVDP believed he had a good argument for reasonable cause, he wouldn't be willing to risk being hit with penalties amounting to 300 percent of the value of the account. "Hopefully the new guide will eliminate these threats of excessive penalties," he said.

Under the procedures outlined in the guide, a centralized review committee will make a determination as to whether the case merits a normal examination, should be reassigned to a Special Enforcement Program agent, or should receive some other treatment. "The committee will decide the appropriate level of examination, keeping in mind that the taxpayer is not to be punished (or rewarded) for opting out," the guide states.

"The agents are taking the position that they are not there to make decisions. They're there to apply the penalties and move on," Campagna said. The guidance empowers someone other than the agent to make exam scope decisions, he added. The guidance states that the committee will consider the apparent severity of the results under the OVDI or the OVDP and the cooperation of the taxpayer, "including whether removal was under consideration at the time of opt out," and that all committee decisions are final.

Penalty Relief for Nonresidents

The additional reduced 5 percent offshore penalty carve-out for nonresidents, which applies only to financial assets, was especially welcome news to practitioners. "The IRS is to be commended for new FAQ 52 regarding long-term nonresidents in compliance in their foreign country of residence," said Charles P. Rettig of Hochman Salkin Rettig Toscher & Perez PC. "Such individuals clearly did not intend to avoid their filing obligations."

Scott D. Michel, a partner at Caplin & Drysdale, pointed out that until the change, individuals now eligible for the carve-out "had to basically forfeit 25 percent of their net worth -- not just their financial accounts, but their homes, their cars." He said the relief "now makes this program far more attractive to potentially tens of thousands" of U.S. citizens outside the United States.

The relief is available only to taxpayers who -- during all years of their voluntary disclosure -- resided in a foreign country, were in compliance with the tax laws of their resident countries, and had \$10,000 or less of U.S. source income each year. Any offshore-related taxable income not reported on the individual's U.S. tax return must have been reported on the individual's income tax return filed with his resident foreign country.

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