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Beware IRS Audits Of Offshore Account Filings

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Perhaps you only recently became aware that the IRS wants you to report your worldwide income on your taxes, and (separately) to report your foreign accounts. Perhaps you only woke up to it because of FATCA, the massive 2010 American tax law that took effect in countries and banks worldwide June 1, 2014. If this is all new to you, you have some catching up to do. The IRS has been pushing hard for nearly a decade, and it is becoming harder to claim ignorance.

The gasping and scrambling largely started in 2009. The IRS and Justice Department took on Swiss banking, and in 2008, started to win big in court. With huge potential exposure for helping Americans, on February 18, 2009, UBS settled with the U.S. government for a fine of $780 million. Since then, vast numbers of Swiss and other banks have either faced criminal charges or settled with big civil settlements. And American taxpayers have too. There have been several different IRS 'amnesty' programs to encourage individuals to come forward. Until mid-2014, most people were resigned to the Offshore Voluntary Disclosure Program, or OVDP. At this point, the IRS offshore account collections haul has topped $10 billion, and it isn't over yet.

But there has been one huge change, and it has ominous possibilities for the future. A mid-2014 announcement of domestic and foreign Streamlined programs radically changed the playing field. Rather than 8 years of tax returns and FBARs, with taxes, penalties and interest (OVDP), the Streamlined program involves filing 3 tax returns (plus 6 FBARs) and paying taxes and interest.

Financially, the comparison can be stark. Understandably, many taxpayers have an easier time deciding to file Streamlined rather than OVDP. The biggest difference is the overall asset-based penalty. In the OVDP, the penalty is 27.5% or even 50% of the highest balance (over 8 years) of the non-declared funds/assets. In contrast, Streamlined filers pay either 5% or zero. Those residing outside the United States, pay no penalty. While Streamlined filers in the U.S. pay 5% of the foreign accounts/assets.

In some ways, the IRS gives you what you pay for. The OVDP precludes criminal prosecution and ends in a closing agreement. In contrast, Streamlined filers can face a civil audit or conceivably even prosecution. Prosecution may be highly unlikely, provided that the taxpayer cooperates if the IRS audits, but that audit may not be easy. A key for any Streamlined filer is to be non-willful. One must certify that. Negligence, inadvertence, or mistake are all OK, but intent to conceal or to evade taxes is not. The certification requires the taxpayer to:

> ‘ Provide specific reasons for your failure to report all income, pay all tax, and submit all required information returns, including FBARs. If you relied on a professional advisor, provide the name, address, and telephone number of the advisor and a summary of the advice. If married taxpayers submitting a joint certification have different reasons, provide the individual reasons for each spouse separately in the statement of facts.”

You may believe your inadvertence was non-willful, but the IRS may not agree. And the IRS has a treasure trove of data now. If you knew you were supposed to report, the IRS may say you were willful. What's more, the IRS uses a concept of "willful blindness."
Essentially, it is a conscious effort to avoid learning about the IRS or FBAR

reporting. Willfulness involves a voluntary, intentional violation of a known legal duty. In taxes, it applies for civil and criminal violations. The failure to learn of filing requirements, coupled with efforts to conceal the facts, can spell willfulness. Watch out for conduct meant to conceal, such as:

- Setting up trusts or corporations to hide your ownership.
- Filing some tax forms and not others.
- Keeping two sets of books.
- Telling your bank not to send statements.
- Using code words over the phone.
- Cash deposits and cash withdrawals.
- Moving money from one bank to another when banks don't want undisclosed American accounts.

Even if you can explain one failure to comply, repeated failures can morph conduct from inadvertent neglect into reckless or deliberate disregard. Those taxpayers who have not yet made the OVDP v. Streamlined choice should consider their facts carefully. Most taxpayers who filed a Streamlined disclosure will not be audited. But those who are should be very careful about how to respond and precisely how to conduct the audit.

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.