



Section of Taxation

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October 14, 2015

The Honorable John Koskinen
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Comments on 2014 Offshore Voluntary Disclosure Program and the Streamlined Programs

Dear Commissioner Koskinen:

Enclosed please find comments on the 2014 Offshore Voluntary Disclosure Program and the Streamlined Programs ("Comments"). These Comments are submitted on behalf of the American Bar Association Section of Taxation and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

The Section of Taxation would be pleased to discuss the Comments with you or your staff if that would be helpful.

Sincerely,

A handwritten signature in black ink, appearing to read "George C. Howell, III".

George C. Howell, III
Chair, Section of Taxation

Enclosure

cc: William J. Wilkins, Chief Counsel, Internal Revenue Service
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**AMERICAN BAR ASSOCIATION
SECTION OF TAXATION**

**COMMENTS ON THE 2014 OFFSHORE VOLUNTARY
DISCLOSURE PROGRAM AND THE STREAMLINED PROGRAMS**

These comments (“Comments”) are submitted on behalf of the American Bar Association Section of Taxation (the “Section”) and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by Niles A. Elber (Vice Chair of the Committee on Civil and Criminal Tax Penalties (“CCTP”)), John M. Colvin (Chair of CCTP), Sebastian N. Chain, Michael J. Desmond, Mitchell I. Horowitz, Matthew F. Kadish, Jeffrey A. Nieman, Jennifer M. O’Brien, Michel R. Stein, Kevin R. Tabor, Bonita Wang, and Zhanna A. Ziering. These Comments were reviewed by Charles P. Rettig of the Section’s Committee on Government Submissions, by Larry A. Campagna, Council Director for CCTP, and by Peter H. Blessing, the Section’s Vice Chair (Government Relations).

Although the members of the Section who participated in preparing these Comments have clients who would be affected by the federal income tax principles addressed by these Comments, or have advised clients on the application of such rules, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments.

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Date: October 14, 2015

EXECUTIVE SUMMARY

These Comments are presented in connection with the Department of the Treasury's and Internal Revenue Service's effort to collect information on the paperwork and other burdens facing U.S. taxpayers who are participating in one of the IRS programs to voluntarily disclose their previously unreported offshore assets. Programs available to such taxpayers include the Offshore Voluntary Disclosure Program ("OVDP"), the Streamlined Domestic Offshore Program ("SDOP"), and the Streamlined Foreign Offshore Program ("SFOP").

The IRS voluntary disclosure programs have been remarkably successful with more than 50,000 taxpayers participating in the OVDP since 2009 and thousands more taking advantage of one of the Streamlined alternatives. For many taxpayers, the opportunity to participate in one of these programs has helped solve an unsolvable problem, namely the repatriation of foreign assets without fear of criminal prosecution. However, taxpayers who choose to participate in the voluntary disclosure programs do so at considerable cost both in terms of time and resources.

While we recognize the IRS needs to do a certain amount of due diligence and information gathering to determine the appropriate amount of tax, interest, and penalties taxpayers must pay to resolve their cases, we think there are adjustments the IRS could make in its information gathering process to make things less onerous on taxpayers. Additionally, although taxpayers making use of a voluntary disclosure program should expect that they will be subject to a rigorous verification process, we think that all IRS programs should be administered fairly and equitably and not be unnecessarily punitive. As to this consideration, we think the IRS could make some modest improvements in the administration of its voluntary disclosure programs.

With the foregoing thoughts in mind, we provide the following Comments (both solicited and unsolicited) for consideration:

I. Comments Provided in Direct Response to IRS Notice and Request for Comment

- A. Whether the Collection of Information is Necessary for the Proper Performance of the Functions of the Agency. As a general matter, we believe the forms, specifically Forms 14653 and 14654, created to facilitate the collection of data in connection with the SFOP and SDOP are a necessary and appropriate effort to standardize the process and perform an initial risk assessment of Streamlined submissions from the perspective of the IRS. However, we think it would be helpful for the IRS to: 1) provide additional guidance on the types of information it would like to see in the narrative section of each form; 2) create a mechanism to inform taxpayers of errors on or in the submission of Forms 14653 and 14654 and provide an opportunity to correct; 3) confirm that the forms are subject to the doctrine of substantial compliance; and 4) provide guidance on the relationship between the forms submitted by spouses filing returns as married filing jointly and the innocent spouse rules of section 6015.¹

¹ References to a "section" are to a section of the Internal Revenue Code of 1986, as amended (the "Code"), unless otherwise stated.

- B. Comments on the Accuracy of the Agency's Estimate of the Burden of the Collection of Information. We believe the IRS's estimate of 1 hour and 40 minutes to complete the forms associated with the Streamlined Programs (Forms 14653 or 14654) is grossly underestimated, particularly as it applies to the requirement on each form that the taxpayer "provide specific reasons for [their] failure to report all income, pay all tax, and submit all required information returns." In all but a few cases, the time required to gather the information necessary to prepare a complete explanation for the taxpayer's prior compliance shortfalls will be considerable. This situation is made more complicated by the IRS's unwillingness to provide guidance on the issue of "willfulness" which is a key component of the Streamlined Program. Similarly, we believe the IRS's estimate of 474,000 filers of Form 14653, Form 14654 and, to a lesser extent, Form 14708, grossly understates the number of taxpayers who should be working to file these forms.
- C. Ways to Enhance the Quality, Utility, and Clarity of the Information to be Collected. We think certain forms associated with the OVDP could be eliminated or modified to either be more useful to the IRS or prevent duplicative requests for the same data, and thus, be less burdensome on taxpayers. Included among the forms we think could be eliminated or modified are Forms 14452 (*Foreign Account or Asset Statement*), 14467 (*Statement on Dissolved Entities*), and 14453 (*Penalty Computation Worksheet*).
- D. Ways to Minimize the Burden of the Collection of Information on Respondents, including through the use of Automated Collection Techniques or other Forms of Information Technology. At present we do not have sufficient information to provide meaningful substantive comments on this request.
- E. Estimates of Capital or Start Up Costs and Costs of Operation, Maintenance, and Purchase of Services to Provide Information. At present we do not have sufficient information to provide meaningful substantive comments on this request.

II. Additional Comments Provided With Respect to 2014 OVDP

- A. Upfront Payment of the Miscellaneous Penalty. Requiring taxpayers to remit the miscellaneous penalty prior to closing the voluntary disclosure unnecessarily puts taxpayers at a disadvantage in negotiating a resolution of their case with the IRS. As there is no discernible harm to the IRS, we recommend that the IRS revert back to its prior practice of not requiring taxpayers to remit the miscellaneous penalty until the closing agreement is executed.
- B. 50% Miscellaneous "Super" Penalty. To promote equity and fairness in the OVDP and to encourage additional disclosures, we believe the 50% penalty should only apply to accounts on the Foreign Financial Facilitators List and not extend to all accounts held by the taxpayer. We also recommend that 2014 OVDP Frequently Asked Questions (FAQ) 7.2 be amended to provide that the only banks that trigger the 50% miscellaneous penalty are those listed on the 50% Bank List

available on the IRS website as of (1) the date the taxpayer files a request for preclearance under 2014 OVDP FAQ 23, or (2) the date the taxpayer files the initial voluntary disclosure letter and attachment under 2014 OVDP FAQ 24, whichever is earlier.

- C. Requiring PFIC Computations on Small Account Cases. Requiring expensive PFIC computations to be done in all OVDP cases creates an unnecessary and costly expenditure for certain taxpayers. Thus, we recommend that the IRS provide the Revenue Agent (or Group Manager) the discretion to waive PFIC computations when the additional amount of tax to be generated is immaterial compared to the cost that would be incurred in gathering the associated information and performing the calculations.
- D. IRS Use of Statute Extension Forms. Blanket statute extensions have the potential to promote inefficiencies in the processing of OVDP cases and increase the cost of compliance for taxpayers. Though the IRS does have a legitimate interest in protecting against the relatively small numbers of taxpayers who choose to opt out of OVDP, we think a more judicious approach to the use of statute extension forms would be wholly appropriate and should be considered by the IRS. Along these lines, we recommend that the IRS only require taxpayers to commit to a single two-year extension when making their complete OVDP submission.
- E. Protection of Refund Claims Otherwise Barred by Statute. Taxpayers are presently barred from offsetting refunds against taxes due for other years of their voluntary disclosures where the time for seeking a refund has passed. As a matter of law, the IRS cannot grant refunds for a statutorily barred year, but in the context of OVDP, where the IRS makes the rules, disallowing losses because of a closed statute serves little purpose other than being punitive. We believe the IRS should reconsider its position here and allow theoretically barred refunds to offset liabilities in any of the eight years that a taxpayer is required to submit an amended tax return pursuant to the OVDP.

III. Additional Comments Provided With Respect to the Streamlined Programs

- A. Making a Submission Without a Social Security Number (“SSN”). Given the lengthy delays associated with obtaining a SSN for U.S. persons living abroad, and the legitimate risk that a taxpayer, who wants to make a Streamlined submission might be excluded because of such delays, we recommend the IRS implement one of the following options presented in the alternative: 1) assigning taxpayers a temporary SSN or control number solely for the purpose of making a Streamlined submission; 2) creating a mechanism whereby taxpayers can inform the IRS of their intent to make a Streamlined submission and request the IRS’s assistance in obtaining a SSN on an expedited basis; 3) allowing taxpayers to submit a letter of intent to participate in the Streamlined Program and accepting this letter as an initial submission; 4) accepting taxpayers’ Streamlined submissions without a SSN and subsequently letting them supplement the number once received; or 5) permitting taxpayers to use an identification number of their

choice with the proviso that they will update the IRS when a SSN has been assigned.

- B. Basing Penalty Computation Solely on Assets Connected to Unreported Income. The SDOP requires participants pay a penalty equal to 5% of the highest aggregate balance/value of the taxpayer's foreign financial assets subject to the penalty. Based on the way taxpayers are presently instructed to compute the penalty for their SDOP submission, the penalty base will potentially include assets that were not associated with tax non-compliance. We believe this result is contrary to the tenet of the SDOP and recommend that the IRS modify the penalty base so it excludes assets that did not generate reportable income, or for which gross income was accurately reported.
- C. Further Expanding Streamlined Filing Compliance Procedures to Allow for Individuals Who Don't Presently Qualify for Either the SDOP or the SFOP. Certain U.S. persons do not presently qualify for either the domestic or foreign Streamlined programs. One such example is the Canadian "snowbird," U.S. citizens (many who are "accidental citizens" with U.S. citizenship solely as a result of birth in United States, who have lived most of their life in Canada) or green card holders who were unaware the United States requires them to report their worldwide income. However, we do not see any useful policy reason served by denying these individuals an opportunity to correct their offshore compliance issues within the Streamlined framework. Our recommendation is for the IRS to allow any taxpayer who fails to qualify for the SFOP to disclose via a SDOP submission.
- D. Improving Forms 14653 and 14654. Forms 14653 and 14654 are the certification forms used by taxpayers seeking to make Streamlined submissions. We believe the forms could be improved by providing taxpayers additional guidance as to the specific factors the IRS deems relevant in determining whether a submission is sufficient. Proposed revisions to the current language on the forms is provided herein.

INTRODUCTION

Unlike the vast majority of industrialized countries, the United States taxes its citizens and residents on their worldwide income, though it typically provides credits or deductions with respect to taxes paid in other jurisdictions. To implement this worldwide taxation system, there are a series of statutory rules that require U.S. taxpayers to disclose foreign business and financial information on their tax returns, as well as a requirement to report information about foreign bank accounts to the Financial Crimes Enforcement Network (FinCEN). There are penalties associated with failing to file or incorrectly filing the required disclosures. For example, the penalty for willfully failing to file a foreign financial account report with FinCEN is the greater of \$100,000 or 50% of the balance in the account. If the failure to report a foreign financial account was negligent rather than willful, the penalty is \$10,000.

For a variety of reasons, ranging from the intentional evasion of taxes to an innocent lack of understanding of the requirements, many taxpayers failed to properly report all of their foreign income and failed to make the required disclosures of their foreign activities and accounts. These taxpayers are potentially subject to a variety of civil and criminal penalties.

The Criminal Investigation Function of the Internal Revenue Service has long had a voluntary disclosure program, under which the IRS undertakes not to criminally prosecute those individuals who come forward and disclose errors or omissions on tax returns before the government has started to audit or investigate their tax affairs. While taxpayers who made voluntary disclosures were not prosecuted criminally, they were required to pay taxes, statutory interest, and – in some circumstances – a substantial penalty. The amount of any penalty was ordinarily determined by the civil side of the IRS on a case-by-case basis.

In late February of 2009, the IRS announced a special Offshore Voluntary Disclosure Program (“2009 OVDP”) for taxpayers who had offshore accounts and had failed to disclose all income related to those accounts. Taxpayers had to elect to participate in the program by October 15, 2009. Taxpayers who elected to participate in this program were required to file amended tax returns for the preceding six years (2003-2008).

The 2009 OVDP differed from prior voluntary disclosure programs in that it also offered taxpayers an optional package civil settlement, which included not only the payment of taxes, interest, and tax-related penalties, but also the payment of a miscellaneous Title 26 offshore-related penalty (“miscellaneous penalty”) based on a percentage of the unreported foreign assets. With some limited exceptions, this penalty was set at 20% of the unreported foreign assets. Taxpayers were required to pay taxes, interest and the tax-related penalties at the time they submitted their corrected income and information returns, but were not required to pay the miscellaneous penalty until a final agreement was reached with the IRS. Also, taxpayers were not required to accept the penalty structure proposed by the IRS, but were permitted to “opt out” and have their cases evaluated on their individual merits by the IRS, with the understanding that this could result in either lower overall penalties, or higher penalties. All of the 2009 OVDP cases were audited by IRS Revenue Agents, and the IRS required taxpayers to enter into closing agreements in order to preserve the finality of the determinations.

From the IRS perspective, the 2009 OVDP was a successful program, and brought thousands of taxpayers into compliance. In 2011, the IRS announced an Offshore Voluntary Disclosure Initiative (“2011 OVDI”). Like the 2009 OVDP, the 2011 OVDI was also only available to taxpayers who elected to participate during a limited time frame. The 2011 iteration differed somewhat from the 2009 OVDP, requiring eight years (rather than six) of amended tax returns, as well as increasing the miscellaneous penalty to 25%.

Many of the taxpayers who participated in the 2009 OVDP and 2011 OVDI held interests in foreign mutual funds or similar investments. Such investments were subject to the Passive Foreign Investment Company (“PFIC”) rules of sections 1291-1298. One of the goals of the PFIC rules is generally to eliminate any advantage of holding foreign-based mutual funds over holding domestic mutual funds. The PFIC rules achieve this by imposing tax on gains at the highest marginal rate for each tax year, and also imposing an interest factor (equal to the IRS deficiency interest rate) based on the length of time that the taxpayer held the investment.

In 2011, the IRS announced a special elective rule for PFICs applicable to taxpayers who did not opt out of the IRS penalty structure. This rule reduced both the rate and the interest component for taxpayers who wished to pay tax based on marking PFIC investments to market during the eight years of the OVDP/OVDI. While the alternative mark-to-market (“MTM”) methodology substantially reduced the administrative and financial burden on taxpayers, determining whether an investment is a PFIC and whether to make the MTM election remains one of the most time-consuming tasks that taxpayers and their advisors must undertake in determining their liability under the OVDP/OVDI.

Like the 2009 OVDP, the IRS also considered the 2011 OVDI to be successful at bringing taxpayers into compliance. This prompted the IRS in 2012 to announce an open-ended Offshore Voluntary Disclosure Program (“2012 OVDP”). The most notable difference between the 2011 OVDI and the 2012 OVDP was that the miscellaneous penalty was increased to 27.5%.

Also during 2012, reacting to criticism from other countries (particularly Canada), the IRS announced an alternate program available to certain “low risk” taxpayers who were living outside the United States. This program, known as the “Streamlined Program,” allowed foreign taxpayers to come into compliance with their filing obligations by filing three years of tax returns. Taxpayers who qualified for the 2012 Streamlined Program were required to pay taxes and interest, but were not required to pay any penalty. Unlike the OVDP/OVDI Programs, the IRS did not audit all of the Streamlined Program filings.

Finally, in June of 2014, the IRS modified the OVDP program again (“2014 OVDP”). One major change was to require full payment up front of the taxes, interest and all penalties. The 2014 OVDP eliminated the reduced penalty classifications which had been present in prior programs. At the same time, the IRS announced an expansion of the Streamlined Program (hereinafter referred to as the “expanded Streamlined Procedures”). With respect to foreign taxpayers, it was opened to a broader group of taxpayers. Also, a Streamlined regularization mechanism was made available to taxpayers who are resident in the United States. While taxpayers resident in foreign countries still pay no penalty, domestic taxpayers pay a penalty of 5% of the amount of assets that should have been reported on a Foreign Bank Account Report (FBAR) with FinCEN or a Form 8938 filed with a tax return. Like the 2014 OVDP asset-based

penalty, this 5% penalty must be paid with the initial filing. A key feature of the expanded Streamlined Procedures is that taxpayers must certify that their failure to properly report their income and file required forms about their foreign assets was not “willful.”

I. Comments Provided in Direct Response to IRS Notice and Request for Comment

A. Whether the Collection of Information is Necessary for the Proper Performance of the Functions of the Agency

In August 2014, in connection with the June 18 announcement of the expanded Streamlined Procedures, the IRS released Form 14653, *Certification by U.S. Person Residing Outside of the United States for Streamlined Foreign Offshore Procedures*.² In January 2015, a parallel Form 14654 applicable to persons participating in the SDOP was released. In the Notice and Request for Comments, input was specifically requested on the extent to which the collection of information through Forms 14653 and 14654 is necessary for the proper performance of the functions of the IRS.

Under the expanded Streamlined Procedures, the IRS has consolidated the processing of submissions and amended returns in its Austin Service Center. Given the expected volume of submissions, including a large percentage of submissions that involve relatively routine corrections of past compliance shortfalls, we believe the new Forms 14653 and 14654 are an appropriate effort to facilitate and standardize processing by the IRS. More specifically, the forms will allow the IRS to perform an initial risk assessment of Streamlined submissions in order to make timely determinations as to which submissions warrant further inquiry. For example, the forms will facilitate screening returns based on the tax years at issue and the amount of previously unreported tax. In addition, utilizing automated scanning procedures, the forms should allow the IRS to screen submissions based on both the geographic origin of the compliance shortfall and the foreign financial institution(s) involved. In this regard, it may be helpful for the IRS to provide additional guidance to taxpayers (e.g., through form instructions) regarding the types of information that it expects to see in the narrative section of each form, allowing for some flexibility depending on the facts and circumstances of each particular case.

We also believe that Forms 14653 and 14654 will assist taxpayers in making, and the IRS in processing, Streamlined submissions by ensuring the use of standard jurat language and by reminding taxpayers of the eligibility requirements for the expanded Streamlined Procedures. In this regard, although we agree that Forms 14653 and 14654 are necessary for implementation of the Streamlined Program, we also believe that in most cases the detailed information required by that program is an imperfect fit for the forms and that they should be viewed by taxpayers and the IRS as only a framework for the Streamlined submission. We have several related and more specific comments on the appropriate use of the forms:

1. The IRS should have a mechanism in place to promptly notify taxpayers of errors on or in the submission of Forms 14653 and 14654, and provide taxpayers with an opportunity to correct those errors;

² Form 14653 replaced IRS Form 14438, *Streamlined Filing Compliance Procedures for Non-Resident, Non-Filer Taxpayers*, to reflect an expansion of the Streamlined Procedures to allow for participation by taxpayers needing to file amended U.S. income tax returns.

2. The IRS should confirm that submission of Forms 14653 and 14654 is subject to the doctrine of substantial compliance, which will discourage agents from finding procedural foot faults with submitted forms, encourage more taxpayers to make Streamlined submissions, and reduce the burden on taxpayers and the IRS in processing the submissions; and
3. The IRS should provide guidance on the relationship between Forms 14653 and 14654 submitted by spouses filing returns as married filing jointly and the innocent spouse provisions of section 6015. Signing and submitting a Form 14653 or 14654 should not, for example, be construed to preclude a spouse from later making a claim for innocent spouse relief.

B. Comments on the Accuracy of the Agency's Estimate of the Burden of the Collection of Information

We believe that the estimate in the Notice and Request for Comments of 1 hour and 40 minutes to complete either Form 14653 or Form 14654 is inaccurate. In particular, the estimate is inaccurate as it applies to the requirement on each form that the taxpayer “provide specific reasons for [their] failure to report all income, pay all tax, and submit all required information returns.”

We agree that the request for specific information regarding prior compliance shortfalls is necessary and relevant to allow the IRS to evaluate whether a taxpayer might be subject to the elevated civil penalties under 31 U.S.C. § 5321(a)(5)(C) for acting “willfully” in failing to file FBARs and, in turn, whether the taxpayer is ineligible for the expanded Streamlined Procedures. This information may also be relevant in determining whether the IRS should consider criminal prosecution under applicable provisions of the Bank Secrecy Act and the Internal Revenue Code.

Although a relevant inquiry, the “willfulness” determination is highly fact specific and the IRS has provided little guidance on the factors it looks to or considers important in reviewing Forms 14653 and 14654. The absence of any meaningful guidance on the definition of willfulness significantly complicates the task of preparing and submitting an explanation of the “specific reasons” for a taxpayer’s prior compliance shortfalls and results in taxpayers and their advisors preparing more detailed explanations than might otherwise be necessary.³ For taxpayers who are appropriate candidates for the expanded Streamlined Procedures, the reasons for their past compliance shortfalls are often quite complicated and include personal and professional fact patterns that have evolved over many years. Past compliance failures are also often the result of a misunderstanding of the complex interrelationship between U.S. and foreign tax regimes. In our experience, an appropriately detailed explanation of even the simplest fact patterns involves a minimum of 10 hours of work to understand and explain the taxpayer’s U.S. tax and FBAR

³ The “willfulness” inquiry often focuses on whether the taxpayer checked “no” in response to question 7a of Part III on Schedule B of Form 1040 asking if the taxpayer has a foreign financial account. This targeted inquiry is not relevant in cases where no U.S. income tax return was filed or where no Schedule B was included with the return. Moreover, even if a Schedule B was filed, the IRS appropriately recognizes that an inaccurate response to the foreign account inquiry is not definitive. IRM 4.26.16.4.5.3(6) (July 1, 2008) (“The mere fact that a person checked the wrong box, or no box, on a Schedule B is not sufficient, by itself, to establish that the FBAR violation was attributable to willful blindness.”).

compliance history, evaluate all relevant facts, and present those facts in a manner that allows the IRS to conduct a fair and appropriate evaluation of “willfulness.” Relevant court decisions have only added to the uncertainty over what constitutes “willful” conduct, compounding the burden on taxpayers and their advisors in evaluating and preparing an appropriate explanation of prior noncompliance.⁴

In more complicated cases, where a taxpayer has—often for reasons that have nothing to do with tax—moved between foreign jurisdictions or had complex foreign property holdings, business dealings and sources of income, preparation of a narrative explanation for the prior compliance shortfall as required by Forms 14653 and 14654 can take well in excess of 10 hours. Moreover, our estimate of 10 hours or more to complete the required narrative description does not include the time necessary to complete three years of amended income tax returns (or, in some cases, original income tax returns) or to complete six years of FBARs. Those documents are, we understand, subject to their own burden estimate. Aside from the narrative explanation of prior noncompliance, once the returns and FBARs are complete, the task of preparing the balance of Forms 14653 and 14654 is relatively straightforward.

With respect to the 1 hour and 40 minute burden estimate, we also believe that even if it were accurate in a handful of simple cases, the burden of preparing Forms 14653 and 14654 will often be grossly disproportionate to the amount of potential tax, penalties and interest at stake. In this regard, many U.S. persons, particularly those residing outside the United States, will have income that is below the thresholds provided in section 911 or that is subject to creditable foreign tax that reduces the ultimate U.S. tax liability to zero or close to zero. In many of these cases, taxpayers are required to incur thousands of dollars in legal and accounting fees and spend dozens of hours gathering relevant records only to prove that their ultimate tax and penalty liability is zero or close to it. While recognizing that compliance with U.S. tax law is generally not subject to *de minimis* thresholds, and that similar issues exist for taxpayers who are fully compliant with their obligations, in order to maximize compliance, we believe that there should be some mechanism for taxpayers with *de minimis* tax and penalty liability to participate in the expanded Streamlined Procedures without incurring fees and costs that are orders of magnitude greater than the liability at issue. We suggest as a possibility that where taxpayers and/or their representatives can certify in good faith that the estimated U.S. income tax liability is less than \$1,000 and the potential miscellaneous penalty is less than \$5,000 (calculated at 5% for persons residing in the United States), they be permitted to pay a proxy tax equal to the highest marginal rate on \$1,000 of income and a proxy miscellaneous penalty of \$5,000.⁵ The requisite PFIC and foreign tax credit computations often require a substantial investment on the part of taxpayers to hire a competent professional. In many cases, the professional fees dwarf the tax and miscellaneous penalty amounts determined at the end of the day. As a backstop to the taxpayer’s certification, eligibility for the expanded Streamlined Procedures would be contingent on the tax

⁴ See, e.g., *United States v. Williams*, 489 F. App’x 655 (4th Cir. 2012), *rev’g*, 2010 U.S. Dist. LEXIS 90794 (E.D. Va. Sept. 1, 2010); see also *United States v. Sturman*, 951 F.2d 1466, 1477 (6th Cir. 1991); *United States v. McBride*, 908 F. Supp. 2d 1186 (D. Utah 2012).

⁵ Similar proxy regimes exist in the context of partnership audits, where the IRS has recognized that the costs of applying partnership-level adjustments to numerous partners can outweigh the tax at issue and has, through Form 906 Closing Agreements, allowed a partnership to pay a proxy for its partners’ tax liability.

estimate being sustained if the certification and supporting information submitted were subject to examination.

We also believe that the IRS's estimate of 474,000 filers of Form 14653, Form 14654 and, to a lesser extent, Form 14708, either grossly understates the population of taxpayers who should file these forms or illustrates that the expanded Streamlined Procedures are still too narrowly targeted and will not accomplish the IRS's goal of ensuring compliance by U.S. persons living abroad or U.S. persons living in the United States with foreign financial interests. According to the U.S. State Department, approximately 7.6 million U.S. citizens reside abroad.⁶ Because the United States taxes its citizens on their worldwide income it is likely that the vast majority of these individuals have both U.S. income tax filing obligations and FBAR filing obligations with respect to foreign financial accounts worth more than \$10,000. Yet according to published reports, only 807,000 FBARs were filed in 2012 (the latest year for which data are available)⁷ and this includes an unknown but presumably large segment of U.S. persons who file FBARs only to disclose signature authority over, but no ownership interest in, foreign financial accounts. While it is difficult to draw any concrete conclusions from this data, we believe it is clear that there are far more than 474,000 U.S. citizens living abroad who could be making submissions under the expanded Streamlined Procedures and filing Form 14653, because their prior compliance shortfalls were not "willful." This is to say nothing of the unknown but very large number of persons who live in the United States, have foreign financial accounts, and could also be making submissions and filing Form 14654 because their prior compliance shortfalls are also not "willful."

C. Ways to Enhance the Quality, Utility, and Clarity of the Information to be Collected

A significant burden associated with preparing an OVDP submission is the repeated requests for the same information, but on a different form. Asking for the same information twice (and sometimes three or four times) does not improve the quality of the information received, and asking for the same information at different points in the process of preparing an OVDP submission can lead to inadvertent mistakes that could be considered a misrepresentation or deception. Duplicative requests for the same information also waste taxpayer time and money as representatives must spend additional time answering the same questions.

For example, Form 14452 (Foreign Account or Asset Statement) is required to be submitted with the final OVDP package, but Form 14452 asks for the same information that was provided in forms that were submitted earlier in the OVDP process or in other forms that are being submitted with the final OVDP submission. The following illustrates this point:

1. Information requested by boxes 1-3 (Name of Foreign Financial Institution; Country where Institution is Located; and Contact person at this Institution) and 9-12 (Name under which the account was held; If held by an entity, type of entity; Date account was opened; and Date

⁶ See <http://travel.state.gov/content/dam/travel/CA%20Fact%20Sheet%202014.pdf>.

⁷ National Taxpayer Advocate, 2013 Annual Report to Congress, Volume 1 at 229 and n.9.

account was closed) of Form 14452 has already been provided on Form 14454.

2. Information requested by boxes 4-7 (Is the offshore account a bank account holding cash, money market, or CD; Is the offshore account a custodial account holding securities; Is the offshore account another type of account or asset; and If so, what type of account or asset) of Form 14452 is included in the provided bank statements required by FAQ 25.
3. Information requested by box 8 (Source of funds within the account) of Form 14452 has been provided on Form 14457.
4. Information requested by box 13 (Does the account include Passive Foreign Investment Company (PFIC) or mutual funds) of Form 14452 has been provided as a statement required by FAQ 25.⁸
5. Information requested by box 14 (Description and location of the asset) of Form 14452 is provided on Form 14453 as part of the Penalty Computation Worksheet.
6. Information requested by boxes 15a-16b (Purchase price; Date acquired; Sales price (if sold); and Date of disposition) of Form 14452 is provided on the amended U.S. tax returns.
7. Information requested by box 17 (FMV at 12/31/2010 if asset is still owned) of Form 14452 is vague as taxpayers do not understand the legal significance of the FMV of the asset as of 12/31/2010.

Form 14452 has no utility, and it does not clarify any other information. We believe that it should be withdrawn and no longer required to be submitted as part of the taxpayer's OVDP submission.

Below are additional examples of forms that could be updated to improve quality, utility and clarity of the information to be collected:

Form 14467. Although Form 14467 is relatively clear and serves a useful purpose within the OVDP, there are currently two different versions of Form 14467 in circulation – i.e., the *Statement on Dissolved Entities* and the *Statement on Abandoned Entities*. While the two forms are very similar, the *Statement on Abandoned Entities* is slightly broader and covers situations where taxpayers have been unable to formally dissolve or terminate the offshore entity. Oftentimes a taxpayer submits a *Statement on Dissolved Entities* with his final OVDP package with the intention that he will dissolve the foreign entity, but for a variety of reasons he is later unable to do so. In these situations, the IRS has required the taxpayer to resubmit the *Statement on Abandoned Entities* version of Form 14467

⁸ See FAQ 25 (2)(l), Offshore Voluntary Disclosure Program Frequently Asked Questions and Answers 2014 (“2014 OVDP FAQs”).

because the entity was not technically dissolved, but rather abandoned. To eliminate this occurrence in future submissions, the IRS should rescind the March 2013 version of Form 14467, *Statement on Dissolved Entities*, because the language provided in the May 2014 version of Form 14467 covers more taxpayers and situations.

Form 14453 – Penalty Computation Worksheet. Form 14453 has little utility because it does not permit taxpayers to show duplicate transfers between accounts as required by FAQ 37 of the 2014 OVDP FAQs to reduce the miscellaneous penalty.⁹ Currently, if a taxpayer has multiple accounts Form 14453 only allows him to add the balances between those accounts – it does not allow for duplicate funds through account transfers to be deducted from the aggregate account balance for the year. The removal of duplicate funds in the computation of the miscellaneous penalty is critical to any OVDP submission because it ensures that the miscellaneous penalty is being imposed on the actual net amount of funds that were associated with tax noncompliance. Because of this limitation, taxpayers must include attachments to Form 14453 to explain and show transfers, which adds to the taxpayer’s burden of preparing Form 14453 and complicates the IRS’s processing of the calculation of the miscellaneous penalty. To address this concern, we recommend that the IRS modify Form 14453 so that it can add and subtract amounts when calculating the miscellaneous penalty or revert to the Excel template previously used in the prior iterations of the OVDP.

D. Ways to Minimize the Burden of the Collection of Information on Respondents, including through the use of Automated Collection Techniques or other Forms of Information Technology

At present we do not have sufficient information to provide meaningful substantive comments on this request.

E. Estimates of Capital or Start Up Costs and Costs of Operation, Maintenance, and Purchase of Services to Provide Information

At present we do not have sufficient information to provide meaningful substantive comments on this request.

II. Additional Comments Provided with Respect to 2014 OVDP

The following Comments were not specifically solicited in the IRS Notice and Request for Comment, but we believe they address important issues in the administration of the 2014 OVDP and hope that the IRS will give them due consideration.

⁹ 2014 OVDP FAQ 37 states, “if a taxpayer can establish that funds were transferred from one account to another, any duplication will be removed before calculating the offshore penalty [but] the burden will be on the taxpayer to establish duplication.”

A. Upfront Payment of Miscellaneous Penalty

The 2014 OVDP FAQs changed the timing for payment of the miscellaneous penalty. In all prior iterations of the voluntary disclosure program, the miscellaneous penalty was only required to be paid at the time the executed Form 906 Closing Agreement was submitted to the IRS. FAQ 25 now requires that payment of the miscellaneous penalty be made when the other OVDP documents are submitted to the IRS. This is well in advance of the signing of the closing agreement, assuming a closing agreement is in fact eventually entered into. We recommend that the IRS revert to the prior procedure of requiring the miscellaneous penalty to be remitted at the time when the closing agreement is executed for the following reasons:

1. In all prior versions of the voluntary disclosure program (i.e., 2009 OVDP, 2011 OVDP, and 2012 OVDP), the timing of payment of the miscellaneous penalty was at the execution of the closing agreement by the taxpayer. An executed closing agreement signifies an agreement made by the IRS and the taxpayer with respect to the exact amount of the miscellaneous penalty. It is only reasonable for the taxpayer to submit this payment once it is agreed upon because it is a penalty, not a tax. However, the 2014 OVDP FAQ 25 requires this payment be made when the tax returns, FBARs and other OVDP documents are submitted, which is well prior to execution of the closing agreement.

With respect to the tax, interest, miscellaneous penalty, accuracy-related penalty and, if applicable, failure to file and failure to pay penalties, FAQ 25 states that the remittance made with the OVDP submission is treated as an “advance payment,” consistent with Regulation section 301.6213-1(b)(3). This regulation authorizes (but does not require) an immediate assessment with respect to an advance payment “if such action is deemed proper.”¹⁰ In the event that a closing agreement is not ultimately reached, treatment of the remittance as an advance payment may act to defeat jurisdiction in the Tax Court if the IRS determines that additional tax is due and the taxpayer disagrees with that determination.¹¹ In addition, in the event that all or some portion of the remittance is returned to the taxpayer, until the IRS applies it to an assessed tax liability (potentially months or years after the remittance), the taxpayer is not entitled to interest. To address these issues, we recommend that FAQ 25 be revised to permit a taxpayer to designate the remittance as a deposit pursuant to section 6603 and Rev. Proc. 2005-18.¹² When the closing agreement is signed and the tax and penalties are assessed, the IRS would apply the deposit to the assessment, returning any balance with interest. If a closing agreement is not entered into, the taxpayer could request a return of the deposit, with interest, which would trigger an automatic withdrawal from

¹⁰ Reg. § 301.6213-1(b)(3).

¹¹ *Id.*

¹² 2005-1 C.B. 798.

the OVDP. If a closing agreement is not entered into, Tax Court jurisdiction over any determined deficiency would be preserved.

2. Once paid prior to execution of the closing agreement, a taxpayer loses the leverage to receive the miscellaneous penalty amount back if the taxpayer disagrees with the IRS on the amount of the miscellaneous penalty. Even though FAQ 25 states that any credit or refund of the payment is subject to the limitations of section 6511, this provision does not guarantee that the IRS will return to taxpayer his or her advanced offshore penalty payment. Section 6511 provides rules on limitations for credit or refund of any “tax” imposed by Title 26 of the U.S.C. In addition, *even assuming arguendo*, that the statute of limitations set forth under section 6511 is applicable, it provides that no credit or refund is allowed after the expiration of the limitations period, which generally is two years from the time the tax was paid.¹³ If taxpayers were permitted to designate the payment as a deposit pursuant to Rev. Proc. 2005-18, the two year refund claim limitations period would not start running when the remittance was made, but only when the deposit was applied to an assessed liability.¹⁴ It is not uncommon that a taxpayer’s OVDP case is not resolved within two years. Thus, the limitation functions as a trap for the unwary or unrepresented taxpayer. As currently structured, under FAQ 25, this could require the filing of a protective and ultimately unnecessary refund claim.

For the foregoing reasons, we recommend that the miscellaneous penalty payment not be required to be remitted to the IRS until the closing agreement is executed. Moreover, if the IRS decides for some reason to continue the up-front remittance requirement, we urge that the remittance take the form of a deposit pursuant to Rev. Proc. 2005-18.

B. 50% Miscellaneous “Super” Penalty

2014 OVDP FAQ 7.2 provides as follows:

Beginning on August 4, 2014, any taxpayer who has an undisclosed foreign financial account will be subject to a 50-percent miscellaneous offshore penalty, increased from the normally applicable 27.5%, if, at the time of submitting the preclearance letter to IRS Criminal Investigation, an event has already occurred that constitutes a public disclosure as to one of the following: (a) the foreign financial institution where the account is held, or another facilitator who assisted in establishing or maintaining the taxpayer’s offshore arrangement, is or has been under investigation by the IRS or the Department of Justice in connection with accounts that are beneficially owned by a U.S. person; (b) the foreign financial institution or other facilitator is cooperating with the IRS or the Department of Justice in connection with accounts that are beneficially owned by a U.S. person or (c) the foreign financial institution or other facilitator has been identified in a

¹³ I.R.C. § 6511(a) , (b).

¹⁴ See *Boensel v. United States*, 99 Fed. Cl. 607, 611 (2011).

court- approved issuance of a summons seeking information about U.S. taxpayers who may hold financial accounts (a “John Doe summons”) at the foreign financial institution or have accounts established or maintained by the facilitator. Examples of a public disclosure include, without limitation: a public filing in a judicial proceeding by any party or judicial officer; or public disclosure by the Department of Justice regarding a Deferred Prosecution Agreement or Non-Prosecution Agreement with a financial institution or other facilitator. A list of foreign financial institutions or facilitators meeting this criteria is available at <http://www.irs.gov/Businesses/International-Businesses/Foreign-Financial-Institutions-or-Facilitators>.

Once the 50-percent miscellaneous offshore penalty applies to any of the taxpayer’s accounts or assets in accordance with the terms set forth in the paragraph above, the 50-percent miscellaneous offshore penalty will apply to all of the taxpayer’s assets subject to the penalty (see FAQ 35), including accounts held at another institution or established through another facilitator for which there have been no events constituting public disclosures of (a) or (b) above.

A foreign financial institution or facilitator (“foreign financial institution”) is treated as “blacklisted” as of the effective date provided on the IRS website listing of Foreign Financial Institutions or Facilitators (the “50% Bank List”).

Some taxpayers had accounts of nominal value held at foreign financial institutions that are on the 50% Bank List and also had accounts of significant value held at foreign financial institutions that are not on the 50% Bank List. Accordingly, by virtue of the current rules set forth in 2014 OVDP FAQ 7.2, the taxpayer’s accounts held at the foreign financial institutions that are not on the 50% Bank List are tainted (and thus subject to the 50% miscellaneous “super penalty”) as a result of the account(s) of nominal value held at the foreign financial institution on the 50% Bank List. In such cases, the application of the 50% miscellaneous “super penalty” rate to *all* of the taxpayer’s accounts is overly harsh, and does not accurately reflect the likelihood that the taxpayer was willful as to the accounts at the non-blacklisted foreign financial institutions.

2014 OVDP FAQ 7.2 should be amended to limit the application of the 50% miscellaneous “super penalty” only to accounts on the 50% Bank List. Doing so will encourage more disclosure by taxpayers under the OVDP.

Additionally, the language in the first paragraph of FAQ 7.2 is vague and makes it difficult for a taxpayer to know whether the applicable miscellaneous penalty will be 27.5% or 50%. To make things simpler, we recommend that FAQ 7.2 be amended to provide that the only banks that trigger the 50% miscellaneous penalty are those listed on the 50% Bank List as of (1) the date the taxpayer files a request for preclearance under 2014 OVDP FAQ 23, or (2) the date the taxpayer files the initial voluntary disclosure letter and attachment under 2014 OVDP FAQ 24, whichever is earlier. Providing more certainty and clarity will encourage more voluntary disclosures via the OVDP.

C. Requiring PFIC Computations on Small Account Cases

A significant number of offshore voluntary disclosures involve accounts holding foreign mutual funds or other securities which may be treated as passive foreign investment companies (“PFICs”) for U.S. tax purposes. To help ameliorate what can be harsh and complicated rules, 2014 OVDP FAQ 10 allows for the use of an alternate mark-to-market (“MTM”) methodology that does not require a complete reconstruction of historical data.

During the standard course of examinations (i.e., outside of the OVDP), auditors have discretion over whether to perform or require PFIC calculations. By contrast within the OVDP, Technical Reviewers have been refusing to approve and allow the processing of cases involving possible PFICs, unless the taxpayer submits PFIC calculations either under (a) Section 1291 or (b) the alternate MTM methodology as permitted under 2014 OVDP FAQ 10. (In some cases, Revenue Agents have been willing to prepare PFIC calculations; however, in many cases they are requiring the taxpayer to do the calculations).

In either case, the resources expended by the taxpayer, the taxpayer’s accountant, and the Revenue Agent to prepare such complex calculations often are excessive when compared to the increased tax liability (if any) that results through application of the PFIC rules. While the availability of the modified MTM methodology helps, in many cases the value of the potential PFIC accounts involved was very small, and the cost of performing the necessary calculations (even utilizing the modified MTM methodology) can dwarf the amount of potential additional tax due.

We recommend that the IRS provide the Revenue Agent (or Group Manager) the discretion to waive PFIC calculations where the amount of additional tax to be generated is immaterial when compared to the time and cost which would be incurred by all parties in gathering the necessary data and performing the calculations.

D. IRS Use of Statute Extension Forms

Taxpayers participating in the OVDP are required to execute Form 872, *Consent to Extend the Time to Assess Tax* and a *Consent to Extend the Time to Assess Civil Penalties Provided by 31 U.S.C. 5321* (the “FBAR consent form”). The terms of the OVDP require taxpayers to agree to extend the statute of limitations for all eight years covered by the disclosure period for at least two years after the deadline specified in the letter from IRS Criminal Investigation acknowledging receipt of a timely voluntary disclosure. For example, a Form 872 or FBAR consent form submitted in 2015 requires the taxpayer to extend the statute of limitations to December 31, 2017. Delays in the processing of OVDP submissions at the Austin Service Center and assignment of cases to Revenue Agents in the field mean that most taxpayers who complete their submissions in 2015 will be asked to execute a new Form 872 and FBAR consent form in 2016 which would then extend the statute of limitations for another full calendar year. The delays experienced by the IRS in processing should not be handled in a manner that requires taxpayers to repeatedly agree to statute extensions that are of little to no benefit to themselves. Further, every request for additional extensions made by the Austin Service Center or field agent increases the overall cost of compliance to any taxpayer who has engaged an accountant or lawyer to shepherd them through the voluntary disclosure process. While the IRS

may seek to protect its interests in the face of possible opt-out cases, this interest should not come at a cost to the taxpayers.

For the foregoing reasons, we recommend that the IRS only require taxpayers to commit to a single two-year extension when completing their OVDP submission.

E. Protection on Refund Claims Otherwise Barred by Statute

A taxpayer should be entitled to receive an offset for any refunds the taxpayer may be owed as a result of coming into compliance through the OVDP. As the program currently exists, taxpayers must agree to file amended tax returns and pay taxes for eight previous years. This requires taxpayers to pay taxes for years in which the statute of limitations has already expired. Despite being required to pay a tax liability for years in which the statute has expired, taxpayers are barred from seeking a refund for any year in which the statute has expired. This is inherently unfair. While we recognize that in the ordinary course the IRS as a matter of law cannot grant refunds for statutorily barred years, the OVDP is an IRS created program where it makes all the rules. In this environment, refunds should be available as offsets where it is otherwise assumed that the tax years are open due to fraud, false returns, or foreign reporting noncompliance.

Note that in many instances, taxpayers who elect to use the alternative MTM methodology prescribed by FAQ 10 are being denied refunds that result purely from MTM losses (common during the Great Recession of 2008-2009) that would otherwise be allowable under the published guidance. If the program requires the payment of taxes for eight years, it should also allow for an offset of refunds forgone by taxpayers against taxes owed for these same eight years.

III. Additional Comments Provided with Respect to the Streamlined Program

The following Comments were not specifically solicited in the IRS Notice and Request for Comment, but we believe they address important issues in the administration of the Streamlined Program and hope that the IRS will give them due consideration.

A. Making a Submission without a Social Security Number

Current provisions of expanded Streamlined Procedures require U.S. citizens, U.S. residents, and certain other individuals to have a valid SSN to participate in the expanded Streamlined Procedures.¹⁵ It is our belief and understanding that a submission made pursuant to the Streamlined Procedures without a valid SSN will not be processed.

The SSN application process for U.S. persons who have resided outside of the United States for many years is onerous and protracted. Individuals above the age of twelve must apply in person and may be required to provide voluminous background information such as education, employment, and residence history.¹⁶ For a U.S. person who has been residing abroad for a significant period of time, this process is burdensome and incredibly time consuming. Even after

¹⁵ Streamlined Procedures (“SDOP”), available at <http://www.irs.gov/Individuals/International-Taxpayers/Streamlined-Filing-Compliance-Procedures>.

¹⁶ See <http://www.ssa.gov/ssnumber/ss5doc.htm>.

all the necessary documents are collected and submitted, it may take anywhere from six to fifteen months for a taxpayer to receive an SSN. Moreover, U.S. persons who do not reside in countries where SSNs can be applied for in person are required to undertake expensive travel in order to apply, which may make participation in the Streamlined Program economically impossible.

There is currently no mechanism in the expanded Streamlined Procedures that allows for taxpayers to put the IRS on notice of their intent to participate in expanded Streamlined Procedures similar to a Request for Pre-clearance permissible in the OVDP. Meanwhile, taxpayers who are under audit and criminal examination are ineligible to participate in the IRS's voluntary disclosure programs to report offshore assets. The lack of such a procedure creates uncertainty and discomfort for taxpayers who want to make an SFOP submission but must wait to receive a valid SSN. The overwhelming concern is that while taxpayers are waiting for their SSN, the IRS may initiate an audit, thus disqualifying them from participating in the SFOP. This concern is buttressed by the fact that the IRS is actively receiving information about U.S. foreign account holders as a result of its various settlement initiatives with the foreign banks as well as the Foreign Account Tax Compliance Act ("FATCA"). Indeed, one of the criteria for identifying potential U.S. persons under the FATCA regulations and the Intergovernmental Agreements is whether the person was born in the United States.

In theory, if the taxpayer's noncompliance was due to non-willful conduct, the taxpayer would be similarly situated in an audit or the SFOP, but the practical reality is that the cost and uncertainty involved in an audit far outweigh the already significant costs incurred in making an SFOP submission.

To remedy this situation, we propose several alternatives for the IRS's consideration. First, the IRS may consider allowing taxpayers to request a temporary SSN or control number for the sole purpose of making an SFOP submission – similar to the internal submission index numbers assigned to taxpayers participating in the OVDP. Once the taxpayer obtains a valid SSN, the taxpayer would update the submission accordingly. The second option is to create a process by which a taxpayer can put the IRS on notice of his or her intent to make an SFOP submission and request assistance in obtaining a SSN on an expedited basis. The IRS in turn can communicate with an appropriate government agency, which could expedite the SSN application process for taxpayers. Our third proposed option is that the IRS could allow taxpayers to submit a letter of intent to participate in the expanded Streamlined Procedures and treat that as the initial SFOP submission, which will be supplemented once the taxpayer receives a valid SSN and is able to complete the submission. A fourth option is to allow taxpayers to make an SFOP submission without a valid SSN and supplement it once the SSN is received. Finally, the IRS may consider allowing taxpayers to make an SFOP submission using an identification number of the taxpayer's choice (e.g., U.S. or foreign passport number or foreign tax ID number), which can already be used to file an FBAR, and update the IRS once a valid SSN is received. Any one or a combination of these options would allow many taxpayers to come into compliance sooner and diminish the possibility that they may become ineligible for SFOP while waiting for a SSN.

B. Basing Penalty Computation Solely on Assets Connected to Unreported Income

Currently, the SDOP requires the payment of a miscellaneous penalty equal to 5% of the highest balance/value of the taxpayer's foreign financial assets subject to such penalty. The

miscellaneous penalty is calculated by aggregating the year-end account balances and asset values of all the foreign financial assets subject to the penalty for each year in the covered period and multiplying the highest aggregate balance/value by 5%.¹⁷

The procedures provide that a “foreign financial asset” is subject to the 5% penalty in a given year if (1) the asset should have been, but was not, reported on an FBAR; (2) if the asset should have been, but was not, reported on Form 8938, *Statement of Specified Foreign Financial Assets*; or (3) the asset was properly reported on an FBAR and/or Form 8938 but gross income in connection with the asset was not reported in that year. “Foreign financial asset” is defined by reference as an asset required to be reported on the FBAR and/or Form 8938.

SDOP FAQ 1 excludes certain assets from the 5% penalty base. Specifically, it excludes assets in which the taxpayer had either no financial interest but rather only signatory authority, or portions of assets in which the taxpayer had no financial interest. In connection with determining the penalty base, SDOP FAQ 1 also incorporates by reference OVDP FAQ 31 (exchange rate), FAQ 32 (inclusion of personal and business accounts in the penalty base), FAQ 33 (no *de minimis* income exception), FAQ 35.1 (disallowance of valuation discounts), FAQ 38 (exclusion of accounts with only signatory authority), FAQ 39 (children not required to pay penalty for parents’ accounts), FAQ 40 (allocation of penalty among co-owners of the offshore asset), and FAQ 41 (reporting and penalties for signatories of a trust account). Yet, omitted from this list is a reference to OVDP FAQ 35, discussing the type of assets to which the offshore penalty applies.

It is understandable that incorporating by reference OVDP FAQ 35 in the definition of foreign financial assets subject to the SDOP penalty base may create some confusion as the FAQ covers a broader group of assets, such as real estate, than the SDOP penalty base was intended to include. However, as a consequence, a key premise of OVDP FAQ 35 regarding what triggers inclusion of the asset in the penalty base, fails to be included in any of the SDOP provisions. OVDP FAQ 35 provides that the miscellaneous penalty, applies to taxpayer’s offshore holdings that “are related in any way to tax noncompliance.”¹⁸ For the purposes of this FAQ, “tax noncompliance” is defined to include “failure to report gross income from the assets” and “failure to pay U.S. tax that was due with respect to the funds used to acquire the asset.”¹⁹ Relying on OVDP FAQ 35 in conjunction with former OVDP FAQs 17 and 18, which provided that the IRS would not impose a penalty for failure to file an FBAR or information returns if all the income in connection with the asset was reported and the tax was paid,²⁰ the IRS has excluded accounts and assets from the OVDP penalty base.

The SDOP currently does not have an analogous provision that would allow exclusion of an asset with no unreported income from the penalty base. Consequently, assets like non-interest bearing accounts and assets for which the gross income was properly reported on the tax return

¹⁷ SDOP FAQ 6 discusses the mechanics of calculating the 5% penalty. Available at <http://www.irs.gov/Individuals/International-Taxpayers/Streamlined-Filing-Compliance-Procedures-for-U-S-Taxpayers-Residing-in-the-United-States-Frequently-Asked-Questions-and-Answers>.

¹⁸ 2014 OVDP FAQ 35.

¹⁹ *Id.*

²⁰ 2012 OVDP FAQ (“2012 FAQ”) 17, 18, available at <http://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers>.

are, nevertheless, included in the SDOP penalty base for the year in which the asset was not reported on an FBAR or Form 8938. This over-inclusion can grossly inflate the penalty base despite the fact that there is no tax loss in connection with the asset.

The absence of such an exclusion is contrary to the tenet of the SDOP, which provides a simpler and less costly alternative of coming into compliance for taxpayers whose failure to report foreign assets was due to non-willful conduct.²¹ It is difficult to imagine that the IRS would allow such assets to be excluded from the OVDP penalty base, a much broader and more punitive base with a significantly higher penalty, but include it in the SDOP penalty base where the taxpayer's failure to report the assets is usually due to a lack of familiarity with or misunderstanding of the foreign asset reporting requirements. Furthermore, the IRS has exhibited its intent to make the SDOP penalty base narrower than the OVDP penalty base by excluding tangible assets, real estate, and the portion of an asset over which the taxpayer does not have a beneficial interest from the SDOP penalty base. Therefore, the inclusion of assets that do not have unreported income in the penalty base is inconsistent with the spirit of the SDOP.

For the foregoing reasons, we recommend that the IRS expand SDOP FAQ 1 to provide that assets that did not generate reportable income, or for which gross income was accurately reported, be excluded from the 5% penalty base. To effectuate that, we propose adding the following fourth sentence to the answer to SDOP FAQ 1: "Nor is the penalty intended to reach assets for which there was no underreported tax liabilities even if the assets were omitted from the FBAR or Form 8938." This revision would ensure that the SDOP penalty base is narrower than the OVDP penalty base in all aspects, which appears to be the underlying intent of the IRS in connection with the expanded Streamlined Procedures.

C. Further Expanding the Streamlined Procedures to Allow for Individuals Who Don't Presently Qualify for Either the SDOP or the SFOP

In addition to the OVDP, the IRS currently offers two other primary avenues for voluntary disclosures involving offshore accounts – the expanded Streamlined Procedures, and the Delinquent Return Submission Procedures ("Delinquent Return Procedures"). Each is further divided into two types – the expanded Streamlined Procedures are subdivided into domestic and foreign (i.e., SDOP and SFOP); and the Delinquent Return Procedures are subdivided into FBAR and Information Return Submission Procedures.

The expanded Streamlined Procedures were designed to reduce the time and expense to both taxpayers and the government for lower-risk offshore voluntary disclosure cases. Early reports indicate that they are greatly assisting in that regard, enabling the government to focus its limited resources on more substantial cases, and eliminating the need for lower-risk taxpayers to undergo the much more extensive and expensive OVDP process.

The expanded Streamlined Procedures offer protection from additional penalties (i.e., beyond any penalties specified by the SDOP) for eligible taxpayers who are found to be non-

²¹ Statement of IRS Commissioner John Koskinen (June 18, 2014), available at <http://www.irs.gov/uac/Newsroom/Statement-of-IRS-Commissioner-John-Koskinen>.

willful. Taxpayers are eligible for the expanded Streamlined Procedures if they meet all of the requirements for either the SDOP or the SFOP.

A significant number of taxpayers fail to meet the requirements of either the SDOP or the SFOP. One example (recently acknowledged at the ABA Tax Section meeting in Chicago) is the Canadian “snowbird.” These are U.S. citizens (many “accidental citizens” with U.S. citizenship solely as a result of birth in United States, who have lived most of their life in Canada) or green card holders who were unaware the United States requires them to report their worldwide income. As snowbirds, they spend too much time in the United States to qualify as non-residents for purposes of the SFOP (as they are not physically outside the United States for at least 330 full days). However, they are also ineligible for the SDOP because they have not previously filed U.S. tax returns (being unaware of their U.S. filing obligations, and in many cases, even unaware that they are U.S. citizens).

While such taxpayers can submit delinquent international information returns and delinquent FBARs via the Delinquent Return Procedures, there is no mechanism, other than the OVDP, for these taxpayers to correct any failure to report income and pay U.S. tax. There does not appear to be any useful policy reason to subject them to the onerous and costly burden of the OVDP when their failure was otherwise non-willful.

For the foregoing reasons, we recommend allowing any taxpayer who fails to qualify for the SFOP to disclose via the SDOP. Such a change will substantially simplify the existing procedures and will increase voluntary compliance. Taxpayers will pay the required 5% miscellaneous penalty, which will provide taxpayers with at least some measure of predictability, and the cost of which will discourage them from future noncompliance.

Additionally with respect to the Delinquent Information Return Procedures, we suggest that the IRS provide guidance that three years of delinquent returns is sufficient (as required under the Streamlined Procedures), to provide more certainty and promote voluntary disclosures and future voluntary compliance.

D. Improving Forms 14653 and 14654

The expanded Streamlined Procedures are available to taxpayers certifying that their failure to report foreign financial assets and pay all tax due in respect of those assets did not result from willful conduct on their part. These procedures are available to both U.S. individual taxpayers residing outside the United States (i.e., the SFOP) and U.S. individual taxpayers residing in the United States (i.e., the SDOP).

The certification for SFOP or SDOP is made through a signed submission of either a Form 14653, *Certification by U.S. Person Residing Outside the United States*²² or Form 14654, *Certification by U.S. Person Residing Inside the United States*.²³ Among other things, each form

²² IRS Form 14653 – Certification by U.S. Person Residing Outside the United States for Streamlined Foreign Offshore Procedures, available at <http://www.irs.gov/pub/irs-pdf/f14653.pdf>.

²³ IRS Form 14654 – Certification by U.S. Person Residing Inside the United States Streamlined Domestic Offshore Procedures, available at <http://www.irs.gov/pub/irs-pdf/f14654.pdf>.

requires certification that the failure to report all income, pay all tax, and submit all required information returns, including FBARs, resulted from non-willful conduct.

The IRS website containing instructions for the expanded Streamlined Procedures states that failure to submit a statement, or submission of an incomplete or otherwise deficient statement, will result in returns being processed in the normal course without the benefit of the favorable terms of these procedures.²⁴

The current version of Form 14653 and Form 14654 contains the following note, in red:

“Note: You must provide specific facts on this form or on a signed attachment explaining your failure to report all income, pay all tax, and submit all required information returns, including FBARs. Any submission that does not contain a narrative statement of facts will be considered incomplete and will not qualify for the streamlined penalty relief.”

Forms 14653 and 14654 also state:

“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. The field below will automatically expand to accommodate your statement of facts.”

The Streamlined certification process poses unique challenges to taxpayers and their representatives. Taxpayers are expected to certify reasons for failing to report income and file required information returns relating to events arising in past years. The current forms warn that specific facts are required and that certifications deemed incomplete or insufficient may not qualify for the favorable terms of these procedures. However, the forms contain little guidance as to what specific factors will assist the IRS with this process. While experienced tax professionals may be familiar with case law and secondary source materials as to what factors bear relevance in these cases, the IRS guidance should assist to the extent possible those taxpayers who choose to complete the forms without access to professionals. Moreover, expressly indicating that both beneficial and adverse factors should be provided will remind potential participants that few, if any, Streamlined cases involve only beneficial facts, and that individuals with a mixed bag of facts may still be appropriate candidates for the expanded Streamlined Procedures.

For the foregoing reasons, we recommend that current language in the Form 14653 and Form 14654 note be replaced as follows (underline reflects portion added):

Note: You must provide specific facts on this form or on a signed attachment explaining your failure to report all income, pay all tax, and submit all required information returns, including FBARs. Specific facts, whether beneficial or adverse to you, may include discussion of all or some of the following factors: your age; educational background; health; language barriers; mental capacity issues; communication with professional advisors; ties to country where

²⁴ SFOP available at <http://www.irs.gov/Individuals/International-Taxpayers/U-S-Taxpayers-Residing-Outside-the-United-States>.

financial assets are located; foreign and domestic tax compliance history; source of funds; and involvement with withdrawals, deposits or investment decisions relating to the account. Any submission that does not contain a narrative statement of facts will be considered incomplete and will not qualify for the streamlined penalty relief.