

IRS OFFERS NEW COMPLIANCE PROCEDURES FOR U.S. CITIZENS LIVING ABROAD

On June 27, 2012, the Internal Revenue Service published a press release that offers a simpler and more palatable way for U.S. citizens who are non-filers and who do not live in the United States to become tax compliant. For many, this is a very welcome change from the Offshore Voluntary Disclosure amnesty programs that the IRS introduced in 2009 that allowed non-resident non-filers back in the system at the cost of high penalties and compliance costs.

The new program will take effect on September 1, 2012. A non-resident must file three years of back tax returns and six years of foreign bank account reporting forms (the so-called "FBARs"). Although details are still emerging, the filing does not involve the criminal division, which differs from the Offshore Voluntary Disclosure program (where pre-clearance from the criminal division is mandatory for participation). Moreover, the level of paperwork is substantially reduced, as it appears that the returns, the FBARs, and a checklist regarding the taxpayer's activities is all that will be required.

This new program is not a complete amnesty – back taxes for the three years will need to be paid, together with interest and, where appropriate, penalties. The IRS is planning on categorizing late filers based upon compliance risk factors, with "low risk" persons likely having no further action taken against them. Higher risk taxpayers have the risk that a full audit will be conducted that could cover years prior to the three years of returns that are filed. A taxpayer will be required to submit a checklist as to whether they meet the risk factors, which likely will include:

- (1) Understatement of tax of more than \$1,500 (this will generally not be an issue for UK residents taxpayers who are paying UK tax on their earned income and do not have significant investment income);
- (2) Additional noncompliance with U.S. tax laws in the past;
- (3) Receipt of U.S. source income; and
- (4) A history of sophisticated planning and avoidance (giving the impression that failure to file was a deliberate act rather than merely negligent).

Note that the IRS will not guarantee that criminal referrals would not be made from taxpayers using this program, although it must be assumed that such a statement is designed for the most egregious cases, for whom the Offshore Voluntary Disclosure program remains available and which, although substantially more intrusive with high penalties, does remain an option.

We are waiting for more details regarding the actual mechanics of the new program, but we are pleased to see that the IRS has finally recognized that the Offshore Voluntary Disclosure program, which is aimed at taxpayers that have actively hidden amounts offshore, is plainly misfocused when applied to non-resident U.S. taxpayers who did not open foreign bank accounts to evade U.S. tax and whose failure to file is due to negligence or inadvertence, rather than a deliberate attempt to violate the U.S. tax laws.