

Streamline Disclosure One Year Anniversary

On September 1, 2012 the IRS implemented a new program aimed at nonfilers living outside the United States. While the program is not restricted to U.S. citizens and green card holders (non-resident aliens holding, say, U.S. rental property are eligible as well), the program is designed to get U.S. citizens and residents back into compliance with a relatively pain-free procedure. The procedure involves filing three years of back returns, six years of bank account disclosure forms (so-called FBARs) and a short questionnaire aimed in part at establishing whether any tax professional aided or abetted the nonfiler in the prior failure to comply with his or her tax reporting obligations.

To date, our experience with the program has been positive. While the IRS reserves the right to audit filings where it deems the risks to the fisc as high, we have found only a few have been subject to audit. Those audits have not been unduly harsh and have asked relatively routine questions, such as determining whether the taxpayer was a U.S. resident, proof of wage and foreign taxes paid, or the proper characterization of certain gains. We are very pleased with the program and would invariably recommend proceeding under the streamline program to a client that meets the program guidelines.

Our principal criticism of the program is its limit in scope. A taxpayer who is fully compliant with the filing requirements in his or her jurisdiction of residence may have a residual U.S. tax liability of more than \$1,500 in a tax year, the upper limit of the program, due to the vagaries of the U.S. and non U.S. tax rules. For example, a U.S. taxpayer with a U.K. ISA may find that the U.K. tax-free income from the ISA is not tax-free in the U.S., thereby potentially causing a U.S. liability in a year; most often over \$1,500. Similarly, mismatches in tax years, tax payment dates or retirement payments may make the U.S. liability greater in one year than \$1,500.

In such situations, a nonfiler faces a number of options, none of which are palatable. The nonfiler may file for the past tax year only and hope the IRS does not ask for earlier returns (the so-called "quiet disclosure") again hoping this action does not cause heightened IRS scrutiny. In extreme cases, the nonfiler can participate in the offshore voluntary disclosure initiative (the OVDI), where a penalty of 27 ½ percent of the nonfiler's financial assets is levied in exchange for immunity from prosecution. None of these alternatives are anywhere near as favorable to a nonfiler as the streamline disclosure program.

In summary, we believe the program should be expanded to give the IRS discretion to accept nonfilers who may have a tax liability in excess of \$1,500. A once famous jurist said "even a dog knows the difference between a kick and a misstep" and the IRS in our view should accept nonfilers into the system even where they have U.S. tax liabilities for a particular year in excess of \$1,500. Through our experience, though limited in its scope, the streamline disclosure program has been very successful and useful to bring nonfilers back into the system. Our clients have had almost universal success with the program and we urge all nonfilers to take advantage of this where possible.