IRS: Tax Cheats Face Higher Penalty for Hiding Assets From IRS

BNA Snapshot

- Previous offshore disclosure program netted $11 billion
- New penalty could discourage some from coming forward

By Siri Bulusu

Individuals with hidden money who want to come clean with the IRS will face higher fines for unpaid tax debts and will have to contend with new rules to disclose their assets.

The agency's new voluntary disclosure program—applicable to both domestic and international disclosures made after Sept. 28—includes a larger minimum fine for evasion: 75 percent of the additional taxes owed, according to a Nov. 20 Internal Revenue Service **memorandum** that was posted on Nov. 29.

The program allows taxpayers to possibly avoid criminal prosecution by revealing assets to the IRS, and comes after the agency ended an offshore disclosure program that ran from 2009 through September. While the memo gives some certainty for taxpayers to know what to expect, practitioners say it could scare off some individuals from coming clean.

The rules make it more painful for taxpayers to come forward about income and assets hidden overseas, but also standardizes the IRS's system for disclosure of income and assets previously undisclosed in the U.S.

“If someone is considering a voluntary disclosure, the presumption of 75 percent can appear as a big number—the question is whether that penalty will be so onerous it has a chilling effect on the program,” said Josh Ungerman, former IRS senior trial attorney and Department of Justice special assistant U.S. attorney. He is now a partner at Meadows, Collier, Reed, Cousins, Crouch & Ungerman LLP in Dallas.

The IRS will apply the 75 percent penalty, in line with tax code Sections 6663 and 6651(f), on top of the IRS's standard willful Reports of Foreign Bank and Financial Accounts (FBAR) penalty on the year with the highest value of undisclosed assets.

If your returns are inaccurate but not fraudulent there is a standard 20 percent accuracy-related penalty for underpayment of tax, according to Section 6662.

Best Option?

More than 56,000 people came forward in the original offshore disclosure program, according to the IRS. The taxpayers paid more than $11 billion in back taxes, interest, and penalties.

The IRS is demonstrating its willingness to offer a “second chance” to individuals who didn't participate in the original program, and the steep penalties are still a better choice than filing an amended return—a move that could result in much higher penalties, Robert Russell, an attorney at Alliantgroup LP who formerly worked at the IRS and Treasury Department, told Bloomberg Tax.

Amended returns are filed when taxpayers want to correct a previously filed return. But if the IRS sees willful evasion in an amended return, there is no protection for that taxpayer from whatever the agency deems the appropriate penalty.

“Agree or disagree with the new costs that are coming in, today's information was very helpful to give a framework for corrective filings as a voluntary disclosure post-OVDP,” Russell said.

Ray of Hope

After shuttering the program in September, the IRS vowed to continue to have a streamlined procedure for returning offshore assets.

The new rules allow taxpayers to appeal whatever penalty the IRS issues upon completion of its investigation—a welcome move that offers taxpayers a ray of “hope” in the voluntary disclosure process, Ungerman said.

The program gives certainty, which taxpayers value, despite the stiff penalty, practitioners said.

“Without such an announcement, there would have been fear of the unknown and thus less voluntary compliance,” said Michael Sardar, a tax attorney at Kostelanetz & Fink LLP in New York.

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