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September 15, 2009

NORTHERN CHAPTER, VIRGINIA  
SOCIETY OF CPAs

**“CHOOSING YOUR POISON:  
THE IRS’ NEW ‘VOLUNTARY’ DISCLOSURE PROGRAM  
FOR FOREIGN BANK ACCOUNTS”**

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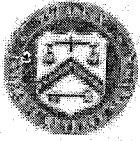
### **FBAR Documents and Resources**

12. IRM 4.26.16 – FBAR provisions
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14. IRC Section 7701(b) – Definition of Resident Alien, Non-resident Alien
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### **Additional Resources**

16. “FBAR Enforcement – An update (Toscher, Stein), Journal of Tax Practice and Procedure (April-May, 2006)
17. “Avoid Criminal Prosecution” (Packman, Holland & Knight memo – 2009)
18. 31 CFR Ch.1, Section 103.25 (Reports of Foreign Financial Accounts)
19. [www.fincen.gov](http://www.fincen.gov)

1. Memo of Linda Stiff to Commissioner, announcing the FBAR Voluntary Disclosure Program (March 23, 2009)



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

DEPUTY COMMISSIONER

March 23, 2009

MEMORANDUM FOR COMMISSIONER, LARGE AND MID-SIZE BUSINESS  
DIVISION  
COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED  
DIVISION

FROM:

Linda E. Stiff *Linda E. Stiff*  
Deputy Commissioner for Services and Enforcement

SUBJECT:

Authorization to Apply Penalty Framework to Voluntary  
Disclosure Requests Regarding Unreported Offshore Accounts  
and Entities

The purpose of this memorandum is to set forth a penalty framework to be applied to voluntary disclosure requests containing offshore issues. The outlined framework will be applied to all such requests that have been submitted to the IRS and are not yet resolved, and will remain in effect for six months from the date of this memorandum. All voluntary disclosure requests are mandatory work.

As Criminal Investigation (CI) makes preliminary determinations that taxpayers are eligible to make voluntary disclosures, it will forward voluntary disclosure requests with offshore implications to the Philadelphia Offshore Identification Unit (POIU) for civil processing. Those requests will be distributed to and worked by examiners who specialize in offshore examinations. All resulting closing agreements will be reviewed and executed as prescribed by existing delegation orders.

Effective as of the date of this memorandum, you are authorized to execute agreements to resolve the tax liabilities related to offshore issues of taxpayers who make voluntary disclosure requests in the following manner:

- (1) Assess all taxes and interest due going back six years (exception: where an account/entity was formed or acquired within the six year look back period, taxes and interest will be assessed starting with the earliest year in which an account was opened/acquired or entity formed). Require the taxpayer to file or amend all returns, including information returns and Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, commonly known as an "FBAR".

(2) Assess either an accuracy or delinquency penalty on all years (no reasonable cause exception may be applied), and

(3) In lieu of all other penalties that may apply, including FBAR and information return penalties, assess a penalty equal to 20% of the amount in foreign bank accounts/entities in the year with the highest aggregate account/asset value.

If, (a) the taxpayer did not open or cause any accounts to be opened or entities formed, (b) there has been no activity in any account or entity (no deposits, withdrawals, etc.) during the period the account/entity was controlled by the taxpayer, and (c) all applicable U.S. taxes have been paid on the funds in the accounts/entities (where only account/entity earnings have escaped U.S. taxation), then the penalty in (3) is reduced to 5%.

The terms outlined herein are only applicable to taxpayers that make voluntary disclosure requests, and who fully cooperate with the IRS, both civilly and criminally.

cc: Acting Chief Counsel  
Senior Advisor to the Commissioner  
Commissioner, Tax Exempt and Government Entities  
Chief, Criminal Investigation

## 2. Commissioner's Statement re Offshore Income (March 26, 2009)

## Statement from IRS Commissioner Doug Shulman on Offshore Income

March 27, 2009

Internal Revenue Service : Statement from IRS Commissioner Shulman : Offshore income .

## Statement from IRS Commissioner Doug Shulman

On Offshore Income

March 26, 2009

My goal has always been clear --to get those taxpayers hiding assets offshore back into the system. We recently provided guidance to our examination personnel who are addressing voluntary disclosure requests involving unreported offshore income. We believe the guidance represents a firm but fair resolution of these cases and will provide consistent treatment for taxpayers. The goal is to have a predictable set of outcomes to encourage people to come forward and take advantage of our voluntary disclosure practice while they still can.

In the guidance to our people, we draw a clear line between those individual taxpayers with offshore accounts who voluntarily come forward to get right with the government and those who continue to fail to meet their tax obligations. People who come in voluntarily will get a fair settlement. We set up a penalty framework that makes sense for them - they need to pay back-taxes and interest for six years, and pay either an accuracy or delinquency penalty on all six years. They will also pay a penalty of 20% of the amount in the foreign bank accounts in the year with the highest aggregate account or asset value. Just to be clear, this is 20% of the highest asset value of an account anytime in the past six years. This gives taxpayers - and tax practitioners - certainty and consistency in how their case will be handled.

We have instructed our agents to resolve these taxpayers' cases in a uniform, consistent manner. Those who truly come in voluntarily will pay back taxes, interest and a significant penalty, but can avoid criminal prosecution.

At the same time, we have also provided guidance to our agents who have cases of unreported offshore income when the taxpayer did not come in through our voluntary disclosure practice. In these cases, we are instructing our agents to fully develop these cases, pursuing both civil and criminal avenues, and consider all available penalties including the maximum penalty for the willful failure to file the FBAR report and the fraud penalty.

We believe this is a firm, but fair resolution of these cases. It will make sure that those who

hid money offshore pay a significant price, but also allow them to avoid criminal prosecution if they come in voluntarily. As we continue to step up our international enforcement efforts, this is a chance for people to come clean on their own. Our guidance to the field is for the next six months only, after which we will re-evaluate our options.

For taxpayers who continue to hide their head in the sand, the situation will only become more dire. They should come forward now under our voluntary disclosure practice and get right with the government

### 3. IRM 9.5.11.9 (Voluntary Disclosure Program)

## IRS Voluntary Disclosure Practice

March 27, 2009

Tax crimes : Voluntary disclosure : Updated practices .

## IRS Voluntary Disclosure Practice

### TAX CRIMES - GENERAL

#### IRM 9.5.11.9

### Voluntary Disclosure Practice

(1) It is currently the practice of the IRS that a voluntary disclosure will be considered along with all other factors in the investigation in determining whether criminal prosecution will be recommended. This voluntary disclosure practice creates no substantive or procedural rights for taxpayers, but rather is a matter of internal IRS practice, provided solely for guidance to IRS personnel. Taxpayers cannot rely on the fact that other similarly situated taxpayers may not have been recommended for criminal prosecution.

(2) A voluntary disclosure will not automatically guarantee immunity from prosecution; however, a voluntary disclosure may result in prosecution not being recommended. This practice does not apply to taxpayers with illegal source income.

(3) A voluntary disclosure occurs when the communication is truthful, timely, complete, and when:

- a. the taxpayer shows a willingness to cooperate (and does in fact cooperate) with the IRS in determining his or her correct tax liability; and
- b. the taxpayer makes good faith arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable.

(4) A disclosure is timely if it is received before:

- a. the IRS has initiated a civil examination or criminal investigation of the taxpayer, or has notified the taxpayer that it intends to commence such an examination or investigation;
- b. the IRS has received information from a third party (e.g., informant, other governmental

agency, or the media) alerting the IRS to the specific taxpayer's noncompliance;

c. the IRS has initiated a civil examination or criminal investigation which is directly related to the specific liability of the taxpayer; or

d. the IRS has acquired information directly related to the specific liability of the taxpayer from a criminal enforcement action (e.g., search warrant, grand jury subpoena).

(5) Any taxpayer who contacts the IRS in person or through a representative regarding voluntary disclosure will be directed to Criminal Investigation for evaluation of the disclosure. Special agents are encouraged to consult Area Counsel, Criminal Tax on voluntary disclosure issues.

(6) Examples of voluntary disclosures include:

a. a letter from an attorney which encloses amended returns from a client which are complete and accurate (reporting legal source income omitted from the original returns), which offers to pay the tax, interest, and any penalties determined by the IRS to be applicable in full and which meets the timeliness standard set forth above. This is a voluntary disclosure because all elements of (3), above are met.

b. a disclosure made by a taxpayer of omitted income facilitated through a barter exchange after the IRS has announced that it has begun a civil compliance project targeting barter exchanges; however the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intention to do so. In addition, the taxpayer files complete and accurate amended returns and makes arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable. This is a voluntary disclosure because the civil compliance project involving barter exchanges does not yet directly relate to the specific liability of the taxpayer and because all other elements of (3), above are met

c. a disclosure made by a taxpayer of omitted income facilitated through a widely promoted scheme regarding which the IRS has begun a civil compliance project and already obtained information which might lead to an examination of the taxpayer; however, the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intent to do so. In addition, the taxpayer files complete and accurate returns and makes arrangements with the IRS to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable. This is a voluntary disclosure because the civil compliance project involving the scheme does not yet directly relate to the specific liability of the taxpayer and because all other elements of (3), above are met.

d. A disclosure made by an individual who has not filed tax returns after the individual has received a notice stating that the IRS has no record of receiving a return for a particular year and inquiring into whether the taxpayer filed a return for that year. The individual files

complete and accurate returns and makes arrangements with the IRS to pay the tax, interest, and any penalties determined by the IRS to be applicable in full. This is a voluntary disclosure because the IRS has not yet commenced an examination or investigation of the taxpayer or notified the taxpayer of its intent to do so and because all other elements of (3), above, are met.

(7) Examples of what are not voluntary disclosures include:

a. a letter from an attorney stating his or her client, who wishes to remain anonymous, wants to resolve his or her tax liability. This is not a voluntary disclosure until the identity of the taxpayer is disclosed and all other elements of (3) above have been met.

b. a disclosure made by a taxpayer who is under grand jury investigation. This is not a voluntary disclosure because the taxpayer is already under criminal investigation. The conclusion would be the same whether or not the taxpayer knew of the grand jury investigation.

c. a disclosure made by a taxpayer, who is not currently under examination or investigation, of omitted gross receipts from a partnership, but whose partner is already under investigation for omitted income skimmed from the partnership. This is not a voluntary disclosure because the IRS has already initiated an investigation which is directly related to the specific liability of this taxpayer. The conclusion would be the same whether or not the taxpayer knew of the ongoing investigation.

d. a disclosure made by a taxpayer, who is not currently under examination or investigation, of omitted constructive dividends received from a corporation which is currently under examination. This is not a voluntary disclosure because the IRS has already initiated an examination which is directly related to the specific liability of this taxpayer. The conclusion would be the same whether or not the taxpayer knew of the ongoing examination.

e. a disclosure made by a taxpayer after an employee has contacted the IRS regarding the taxpayer's double set of books. This is not a voluntary disclosure even if no examination or investigation has yet commenced because the IRS has already been informed by the third party of the specific taxpayer's noncompliance. The conclusion would be the same whether or not the taxpayer knew of the informant's contact with the IRS.

#### 4. CCH Summary of the VDP (March 27, 2009)

Federal Tax - Current Features and Journals - Federal Tax Day - INTERNAL REVENUE SERVICE -

## NEWS-FEDERAL, 2009 TAXDAY, (Mar. 27, 2009), Item #1.3, IRS Announces New Voluntary Disclosure Terms for Offshore Account Holders, Sets Six-Month Deadlines

### IRS Announces New Voluntary Disclosure Terms for Offshore Account Holders, Sets Six-Month Deadlines

The IRS has announced new steps to coax U.S. taxpayers with undisclosed foreign bank accounts to come forward. In return for paying back taxes for the past six years, plus interest and a set of stiff penalties, the IRS will promise not to bring criminal charges or the 75-percent fraud penalty. IRS Commissioner Douglas H. Shulman announced this policy shift and clarification at a press briefing from his Washington, D.C. offices on March 26, at which he also released internal IRS documents that put the plan into motion.

"We believe the guidance represents a firm, but fair, resolution of these cases and will provide consistent treatment for taxpayers," Shulman explained. "The goal is to have a predictable set of outcomes to encourage people to come forward and take advantage of our voluntary disclosure practice while they still can." He set a deadline of six months for disclosures under the terms of the guidance, at which time the program will be re-evaluated.

The IRS has issued a series of three memoranda, and has revised the Internal Revenue Manual (IRM), to reflect updated policies concerning voluntary disclosure, primarily in connection with offshore transactions. Voluntary disclosure occurs when a taxpayer timely discloses information necessary to determine or correct the taxpayer's liability. The IRM continues to provide that its voluntary disclosure practices do not create any substantive or procedural rights for taxpayers, but are a matter of internal IRS practice.

#### Voluntary Disclosure Terms

Shulman emphasized that the terms being offered for the disclosure of offshore accounts are an outgrowth of current policy and carry penalties at a level consistent with voluntary disclosure programs in the past. Within this framework, Shulman enumerated the amounts that would need to be paid by taxpayers with heretofore undisclosed offshore accounts who "come clean" under the program:

--Back taxes due on newly disclosed assets for the last six years;

--Interest due on these back taxes for the last six years;

--A 20-percent accuracy-related under Code Sec. 6662 or a 25-percent delinquency penalty under Code Sec. 6651 for each tax year at issue; and

Looking to the past six years, a 20-percent penalty on the total balance of all the taxpayer's foreign bank accounts or assets during the year among the past six in which the accounts had their highest aggregate value.

**CCH Comment.** This latter penalty is reduced to 5 percent for passive investors in certain transactions.

While Shulman observed that the penalties demanded under the program are not insubstantial, he pointed to

several advantages to participating taxpayers regarding what the IRS will not do:

- The IRS will not pursue charges of criminal tax evasion against taxpayers who voluntarily disclose their offshore assets under this new policy; and
- The IRS will not pursue other penalties against participating taxpayers, such as the Code Sec. 6663 fraud penalties (75-percent of the unpaid tax) or the statutory penalty for willful failure to file a TD F 90-22.1, Report of Foreign Bank and Financial Accounts Report, (FBAR) (the greater of \$100,000 or 50-percent of the foreign account balance) that both annually apply to undisclosed accounts and assets during the relevant tax years.

Shulman also touted the advantage to offshore account holders of "getting the matter behind them" and giving them certainty as to their tax liability.

In a follow-up comment, an IRS spokesman emphasized that "it is too late for any taxpayer who is under criminal investigation to make a voluntary disclosure. The IRS cannot discuss specific situations, but the voluntary disclosure process does not apply when the IRS has information related to a specific taxpayer from a criminal enforcement action."

**CCH Comment.** The issue apparently remains unclear as to whether taxpayers recently disclosed by the Swiss Bank, UBS, as holding undisclosed bank accounts in Switzerland may successfully participate in this initiative. The IRS provided reporters during the March 26 briefing a copy of Section 9.5.11.9 of the Internal Revenue Manual that holds taxpayers to have timely participated in the voluntary disclosure program if they disclose before the IRS has initiated a civil or criminal examination or notified the taxpayer of such an investigation. Their failure to disclose their accounts/assets before the IRS received notice under the UBS deferred prosecution agreement may, therefore, be irrelevant.

#### Other Documents Provided

In addition to the announcement of its penalty framework for voluntary disclosures of offshore accounts, the IRS also provided reporters with the following documents:

**Offshore Case Development.** An SBSE memorandum provides that field personnel should give priority treatment to offshore transactions and entities during examinations, with a special emphasis on detecting unreported income. Examiners are instructed to use all tools, including interviewing taxpayers, making third party contacts, and timely issuing summonses in order to gather information and make determinations about applicable penalties. Managers are asked to ensure that income and penalty considerations are fully developed and documented. The memorandum also advises that as of March 23, 2009, taxpayers will no longer be permitted to minimize penalties through the Last Chance Compliance Initiative (LCCI). Relevant portions of the IRM addressing the LCCI are in the process of being obsoleted. Taxpayers in open examinations where LCCI terms have been offered will be able to resolve their cases under LCCI if they respond to the examiner within 15 days of their prior notification.

**Voluntary Disclosure.** Another SBSE memorandum addresses a change in the processing of voluntary disclosure requests containing offshore issues. Such requests will continue to be initially screened by Criminal Investigation (CI) to determine eligibility for voluntary disclosure and, if involving only domestic issues, will be forwarded to Area Planning and Special Programs for civil processing. Voluntary disclosure eligibility for offshore issues, including those in current inventory, will be initially screened by CI, and forwarded to the Philadelphia Offshore Identification Unit (POIU) for processing.

For submitted, but as yet unresolved, disclosure requests forwarded to the POIU, an internal LMSB memorandum sets forth a liability and penalty framework to be used for processing such cases during the next six months. POIU is authorized to assess all taxes and interest going back six years, or the period of existence of an account/entity if shorter, require the taxpayer to file or amend all returns, and impose an applicable penalty as set forth in the memorandum.

Finally, the Internal Revenue Manual (IRM) has been updated to reflect the initial evaluation of voluntary disclosure requests by CI. Minor revisions to the examples of what constitutes voluntary and not voluntary disclosures have also been made.

By Torie Cole and Sherri Morris, CCH News Staff

[IRS SB/SE Division, LMSB Division Memorandum on Routing of Voluntary Disclosure Cases](#)

[Memorandum for IRS SB/SE Division Commissioner, LMSB Division Commissioner on Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts and Entities](#)

[IRS SB/SE Division, LMSB Division Memorandum on Emphasis on and Proper Development of Offshore Examination Cases, Managerial Review, and Revocation of Last Chance Compliance Initiative](#)

[IRS Voluntary Disclosure Practice](#)

[Statement from IRS Commissioner Shulman on Offshore Income](#)

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5. 2009 ARD 060-2 – Memo for SBSE Area Directors  
(March 27, 2009)

Federal Tax - Current Features and Journals - ADVANCE RELEASE Documents -

**MISC-DOC, 2009ARD 060-2, IRS Small Business/Self-Employed Division,  
Large and Mid Size Business Division, Criminal Investigation Division  
Memorandum on Routing of Voluntary Disclosure Cases, Tax crimes :  
Voluntary disclosure : Updated practices ., (March 27, 2009)  
IRS Small Business/Self-Employed Division, Large and Mid Size Business Division, Criminal Investigation  
Division Memorandum on Routing of Voluntary Disclosure Cases**

March 27, 2009

**Tax crimes : Voluntary disclosure : Updated practices .**

**DEPARTMENT OF THE TREASURY**

INTERNAL REVENUE SERVICE

Washington, D.C. 20224

Small Business/Self-Employed Division

Large and Mid-Size Business Division

Criminal Investigation Division

March 23, 2009

MEMORANDUM FOR SBSE EXAMINATION AREA DIRECTORS

LMSB INDUSTRY DIRECTORS

CI DIRECTORS OF FIELD OPERATIONS

FROM: Faris R. Fink

Deputy Commissioner, SBSE

Barry B. Shott

Deputy Commissioner, LMSB International

Victor Song

Deputy Chief, Criminal Investigation

SUBJECT: Routing of Voluntary Disclosure Cases

The purpose of this memorandum is to alert you to a change in the processing of voluntary disclosure requests containing offshore issues. All voluntary disclosure requests are mandatory work.

(All incoming voluntary disclosure requests will continue to initially be screened by Criminal Investigation (CI) to determine if the taxpayer is eligible to make a voluntary disclosure. Refer to IRM 9.5.11.9 for questions pertaining to taxpayer eligibility. For voluntary disclosure requests containing only domestic issues, where CI has preliminarily determined taxpayer eligibility, CI will continue to forward those requests to the appropriate Area/Industry PSP for civil processing.

Effective as of the date of this memorandum, voluntary disclosure requests containing offshore issues, where CI has preliminarily determined taxpayer eligibility, will now be forwarded by CI to the Philadelphia Offshore Identification Unit (POIU) for civil processing. Additionally, any voluntary disclosures with offshore issues that are currently in Area/Industry case inventories (whether or not there has been prior taxpayer contact by SBSE or LMSB) should also be forwarded to the POIU.

The address for the POIU follows:

Internal Revenue Service  
11501 Roosevelt Blvd.  
South Bldg., Room 2002  
Philadelphia, PA 19154  
Attn: Charlie Judge, Offshore Unit, DP S-611

If you have questions, members of your staff may contact Karen Warfel, SBSE Offshore Program Manager \*\*\*\*\*  
Frank Bucci, SBSE Offshore Technical Advisor \*\*\*\*\* or Lon Nichols, LMSB Director, International Compliance Strategy and Policy.

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Federal Tax - Current Features and Journals - ADVANCE RELEASE Documents -

**MISC-DOC, 2009ARD 060-3, IRS Large and Mid-Size Business Division Memorandum for IRS Small Business/Self-Employed Division Commissioner, Large and Mid Size Business Division Commissioner from Deputy Commissioner for Services and Enforcement on Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts and Entities, Tax crimes : Voluntary disclosure : Updated practices ., (March 27, 2009)**

IRS Large and Mid-Size Business Division Memorandum for IRS Small Business/Self-Employed Division Commissioner, Large and Mid Size Business Division Commissioner from Deputy Commissioner for Services and Enforcement on Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts and Entities

March 27, 2009

**Tax crimes : Voluntary disclosure : Updated practices .**

DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

WASHINGTON, D.C. 20224

DEPUTY COMMISSIONER

March 23, 2009

MEMORANDUM FOR COMMISSIONER, LARGE AND MID-SIZE BUSINESS DIVISION

COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

FROM: Linda E. Stiff

Deputy Commissioner for Services and Enforcement

SUBJECT: Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Unreported Offshore Accounts and Entities

The purpose of this memorandum is to set forth a penalty framework to be applied to voluntary disclosure requests containing offshore issues. The outlined framework will be applied to all such requests that have been submitted to the IRS and are not yet resolved, and will remain in effect for six months from the date of this memorandum. All voluntary disclosure requests are mandatory work.

As Criminal Investigation (CI) makes preliminary determinations that taxpayers are eligible to make voluntary disclosures, it will forward voluntary disclosure requests with offshore implications to the Philadelphia Offshore Identification Unit (POIU) for civil processing. Those requests will be distributed to and worked by examiners who specialize in offshore examinations. All resulting closing agreements will be reviewed and executed as prescribed by existing delegation orders.

Effective as of the date of this memorandum, you are authorized to execute agreements to resolve the tax liabilities related to offshore issues of taxpayers who make voluntary disclosure requests in the following manner:

- (1) Assess all taxes and interest due going back six years (exception: where an account/entity was formed or acquired within the six year look back period, taxes and interest will be assessed starting with the ~~4/10~~

earliest year in which an account was opened/acquired or entity formed). Require the taxpayer to file or amend all returns, including information returns and Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts, commonly known as an "FBAR".

(2) Assess either an accuracy or delinquency penalty on all years (no reasonable cause exception may be applied). and

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(3) In lieu of all other penalties that may apply, including FBAR and information return penalties, assess a penalty equal to 20% of the amount in foreign bank accounts/entities in the year with the highest aggregate account/asset value.

If, (a) the taxpayer did not open or cause any accounts to be opened or entities formed, (b) there has been no activity in any account or entity (no deposits, withdrawals, etc.) during the period the account/entity was controlled by the taxpayer, and (c) all applicable U.S. taxes have been paid on the funds in the accounts/entities (where only account/entity earnings have escaped U.S. taxation), then the penalty in (3) is reduced to 5%.

The terms outlined herein are only applicable to taxpayers that make voluntary disclosure requests, and who fully cooperate with the IRS, both civilly and criminally.

cc: Acting Chief Counsel

Senior Advisor to the Commissioner

Commissioner, Tax Exempt and Government Entities

Chief, Criminal Investigation

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Federal Tax - Current Features and Journals - ADVANCE RELEASE Documents -

**MISC-DOC, 2009ARD 060-4, IRS Small Business/Self-Employed Division, Large and Mid Size Business Division Memorandum on Emphasis on and Proper Development of Offshore Examination Cases, Managerial Review, and Revocation of Last Chance Compliance Initiative, Examination of offshore transactions : Updated practices : Revocation of Last Chance Compliance Initiative ., (March 27, 2009)**

IRS Small Business/Self-Employed Division, Large and Mid Size Business Division Memorandum on Emphasis on and Proper Development of Offshore Examination Cases, Managerial Review, and Revocation of Last Chance Compliance Initiative

March 27, 2009

**Examination of offshore transactions : Updated practices : Revocation of Last Chance Compliance Initiative .**

DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

Washington, D.C. 20224

Small Business/Self-Employed Division

Large and Mid-Size Business Division

March 23, 2009

MEMORANDUM FOR SBSE EXAMINATION AREA DIRECTORS LMSB INDUSTRY DIRECTORS

FROM: Faris R. Fink

Deputy Commissioner, SBSE

Barry B. Shott

Deputy Commissioner, LMSB International

SUBJECT: Emphasis on and Proper Development of Offshore Examination

Cases, Managerial Review, and Revocation of Last Chance Compliance Initiative

The purpose of this memorandum is to ensure examinations with offshore transactions and/or entities continue to be emphasized and receive priority treatment during the examination process. This memorandum also provides for managerial oversight of offshore cases, and revokes the Last Chance Compliance Initiative.

***Offshore Case Development***

The IRS Strategic Plan for 2009-2013 outlines the Service's commitment to meet the challenges of international tax administration and of allocating compliance resources to target existing and emerging high-risk areas.

Similarly, both the SBSE Examination Program Letter and the Servicewide Approach to International Tax Administration documents address our continuing commitment to prioritize and investigate abusive offshore transactions designed to defeat our tax system.

Offshore cases sent to the field are work of the highest priority. Examiners should utilize the full range of information gathering tools in properly developing offshore issues, with special emphasis on detecting unreported income. This includes interviewing taxpayers, making third party contacts, and timely issuing summonses to taxpayers and third parties. In particular, examiners should request foreign-based information through exchange of information under applicable treaties and tax information exchange agreements (TIEAs) in any cases where the taxpayers have accounts or transactions in countries with such agreements. Examiners should be alert to the badges of fraud and consult with Fraud Technical Advisors in developing cases for criminal referrals or the assertion of the civil fraud penalty. Counsel is available to assist SBSE and LMSB personnel as needed. Attachment 1 contains a brief summary of potential foreign information reporting requirements and civil penalties that could apply to a taxpayer depending on his/her particular facts and circumstances.

### ***Managerial Oversight***

Managers should ensure that income and penalty considerations are sufficiently developed and documented during both unagreed and Embedded Quality reviews. Cases should be discussed with employees regarding the need for additional income probes, use of indirect methods of proof to reconstruct income, penalty development and/or other considerations as necessary.

### ***Revocation of Last Chance Compliance Initiative***

Effective as of the date of this memorandum, the Service will no longer afford taxpayers the opportunity to minimize their exposure to penalties through the terms of the Last Chance Compliance Initiative (LCCI). All notices and letters with respect to the LCCI and relevant portions of IRM sections 4.26.16, 4.26.17 and 25.6.23 are in the process of being obsoleted. On any currently open examinations where the LCCI terms have already been offered, taxpayers will be afforded the opportunity to resolve their cases under LCCI if they respond to the examiner within 15 days of their prior notification.

If you have questions, members of your staff may contact Karen Warfel, SBSE Offshore Program Manager at \*\*\*\*\*, Frank Bucci, SBSE Offshore Technical Advisor \*\*\*\*\* or Lori Nichols, LMSB Director, International Compliance Strategy and Policy at

Attachment

### ***Attachment 1***

The following summary of potential reporting requirements and civil penalties is not necessarily all encompassing, and it is unlikely that any one taxpayer would be subject to all of the reporting obligations or penalties listed below.

#### **(1) Penalties for failure to comply with the Bank Secrecy Act requirement that United States persons report their financial interest in, or authority over, financial accounts located in a foreign country.**

U.S. citizens, residents, and certain other persons, must annually report their financial interest in, or signature authority (or other authority that is comparable to signature authority) over, a financial account (such as a bank or investment account) that is maintained with a financial institution located in a foreign country if, for any calendar year, the aggregate value of all foreign accounts exceeded \$10,000 at any time during the year. This reporting requirement is met by filing *Form TD F 90-22.1* (Report of Foreign Bank and Financial Accounts, commonly known as an "FBAR"). FBARs are filed with a Department of the Treasury facility located in Detroit and are not to be filed with tax returns; the filing date for FBARs is June 30th. The requirement to file FBARs is in the regulations

under 31 U.S.C. § 5314 (which is a provision of the Bank Secrecy Act). Generally, the civil penalty for willfully failing to file an FBAR can be as high as the greater of \$100,000 or 50 percent of the total balance of the foreign account. Criminal penalties may also apply. Refer to IRM 4.26.16.4 for additional FBAR penalty considerations.

**(2) Fraud Penalties (Sections 6651(f) and 6663):**

Where an underpayment of tax, or a failure to file a tax return, is due to fraud, the taxpayer is liable for penalties that, although calculated differently, essentially amount to 75 percent of the unpaid tax.

**(3) Failure to File Tax Return (Section 6651):**

When a taxpayer is required to file a tax return and does not do so on or before the due date of the return, Section 6651(a)(1) imposes a penalty of 5 percent of the net tax amount required to be shown on the tax return for each month (or fraction of a month) that the return is late. The maximum penalty is 25 percent. This penalty is increased to 15%, with a maximum of 75%, if the taxpayer's failure to file is fraudulent.

**(4) Failure to Pay Tax Penalties (Sections 6651(a)(2) and 6651(a)(3)):**

When a taxpayer fails to timely pay the amount of tax shown on the return, Section 6651(a)(2) imposes a late payment penalty equal to .5 percent of the late payment for each month (or part of a month) that the payment is late. The maximum penalty is 25 percent.

When a taxpayer fails to pay a tax that is required to be (but was not) shown on a return within 21 days after the date of the Service's notice and demand for that tax, Section 6651(a)(3) imposes a penalty of .5 percent for each month (or part thereof) that the assessment remains unpaid. The maximum penalty is 25 percent.

**(5) Accuracy- Related Penalty (Section 6662):**

The accuracy-related penalty for underpayments is imposed at the rate of 20 percent on the portion of any underpayment of tax required to be shown on a return attributable to negligence, a substantial understatement of tax, a substantial overstatement of pension liabilities or a substantial estate or gift tax valuation understatement. The accuracy-related penalty with respect to a substantial valuation misstatement can be as high as 40 percent.

**(6) Penalties for failure to file certain information returns (Sections 6035, 6038, 6038A, 6038B, 6038C, 6039F, 6046, 6046A, and 6048):**

**Form 5471**, Information Return of U.S. Persons With Respect To Certain Foreign Corporations. U.S. persons who are officers, directors, or shareholders in certain foreign corporations (including, for example, an International Business Corporation used in an offshore scheme) report information required by Sections **6035, 6038, and 6046**, and compute income from controlled foreign corporations under Sections 951-964. The penalty for failing to file each one of these information returns is \$10,000, with an additional \$10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of \$50,000 per return.

**Form 5472**, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Reports transactions between a 25% foreign-owned domestic corporation or a foreign corporation engaged in a trade or business in the United States and a related party as required by Sections **6038A and 6038C**. The penalty for failing to file each one of these information returns, or to keep certain records regarding reportable transactions, is \$10,000, with an additional \$10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of \$50,000 per return.

**Form 926** , Return by a U.S. Transferor of Property to a Foreign Corporation. Reports transfers of property to a foreign corporation and to report information under Section **6038B** . The penalty for failing to file each one of these information returns is ten percent of the value of the property transferred, up to a maximum of \$100,000 per return, with no limit if the failure to report the transfer was intentional.

**Form 3520** , Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts. Reports various transactions involving foreign trusts, including creation of a foreign trust by a U.S. person, transfers of property from a U.S. person to a foreign trust, and receipt of distributions from foreign trusts under Section **6048** . This return also reports the receipt of gifts from foreign entities under Section **6039F** . The penalty for failing to file each one of these information returns, or for filing an incomplete return, is 35 percent of the gross reportable amount, except for returns reporting gifts, where the penalty is five percent of the gift per month, up to a maximum penalty of 25 percent of the gift.

**Form 3520-A** , Annual Information Return of Foreign Trust with a U.S. Owner. Reports ownership interests in foreign trusts, by U.S. persons with various interests in and powers over such trusts under Section **6048(b)** . The penalty for failing to file each one of these information returns, or for filing an incomplete return, is five percent of the gross value of trust assets determined to be owned by the U.S. person.

**Form 8865** , Return of U.S. Persons With Respect to Certain Foreign Partnerships, U.S. persons with certain interests in foreign partnerships use this form to report interests in and transactions of the foreign partnerships, transfers of property to the foreign partnerships, and acquisitions, dispositions, and changes in foreign partnership interests under Sections **6038**, **6038B**, and **6046A** . Penalties include \$10,000 for failure to file each return, with an additional \$10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of \$50,000 per return, and ten percent of the value of any transferred property that is not reported, subject to a \$100,000 limit.

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## 6. Voluntary Disclosure – Interview Outline

VOLUNTARY DISCLOSURE  
Interview outline

1. Are you currently the subject of a criminal investigation or civil examination? (If yes, specify)
2. Has the IRS notified you that it intends to commence an examination or investigation? (If yes, specify)
3. Are you under investigation by any law enforcement agency? (If yes, Specify)
4. Is the source of any of your income from illegal activity? (If yes, specify)
5. Do you have any reason to believe that the IRS has obtained information concerning your tax liability? (If yes, specify)
6. Does this request involve a business entity? (If yes, provide name, address and EIN)
7. For which tax periods does this request apply?  
Type of Returns (Form 1040, 1120, 941 etc.)  
Type of Tax (income, employment, excise, etc.)
8. Provide a brief description of all omitted income, the tax scheme used by the taxpayer, and a dollar estimate of the total taxes owed?
9. Is the taxpayer willing to cooperate with the IRS in determining the correct tax liability and make good faith arrangements to pay in full, the tax, interest, and any penalties determined by the IRS to be applicable in full?
10. What prompted you to want to participate in Voluntary Disclosure?

11. Where are the funds held regarding the disclosure?
12. When was the account opened?
13. How was the account opened?
14. In whose name was the account opened?
15. Who has access to funds in the account?
16. Who assisted you with the account opening?
17. Who told you about the bank and how to initiate opening an account?
18. Do you have a trust set up relating to the account or the funds?
19. How did you withdraw money from the account?
20. How did you deposit money into the account?
21. Did you have any credit or debit cards associated with the account?
22. How did you correspond with the bank? Do you have records relating to the correspondence?
23. Who is your current point of contact with the bank?
24. Did you ever meet face to face with anyone from the bank? If so, who? Where? When?

25. Did you travel outside the United States to conduct business relating to your account and tax activities?
26. Where was your bank statements sent?
27. What is the source of the funds?
28. Do you have tax returns? Have you prepared amended tax returns? If so, have you submitted them to the IRS?
29. Who prepared your tax returns?
30. When were your returns prepared?
31. Did your preparer know about the voluntary disclosure issues?
32. Did you file FBARs? If not, why not?
33. For those who inherited the account When did you take control of this account? Who were the original account holders? What was the balance at the time you took control? What is the balance today? When did you begin taking distributions? How did you take the distribution? What did you do with the funds? Was this account disclosed in the estate?
34. Did you trade US or Foreign securities with this account? If yes, describe the mechanism for doing that (buy/sell orders, etc.)
35. Do you or have you directly or indirectly controlled any foreign entities? Did you file the required returns for them?
29. For USB clients Have you been notified that the US requested information relating to your account?

30. What countries do you have accounts in?

## 7. Voluntary Disclosure – Optional Format (“Form” letter for disclosure)

***Offshore Voluntary Disclosures – Optional Format***

*If taxpayer has domestic issues only, please have them contact their local Criminal Investigation office for a traditional voluntary disclosure.*

<DATE>

**Internal Revenue Service  
Criminal Investigation  
ATTN: Voluntary Disclosure Coordinator  
<CITY Field Office>  
<Address>  
<CITY, ST ZIP CODE>**

**Re: Taxpayer Name  
Tax Identification Number  
Taxpayer Date of Birth  
Taxpayer Address**

**Dear Voluntary Disclosure Coordinator:**

To assist in a timely determination of my acceptance into the Voluntary Disclosure Program, *(for Voluntary Disclosures involving offshore accounts or assets)* I have addressed *all* of the following items:

- Please include your:
  - Complete name:
  - Social Security Number:
  - DOB:
  - Address:
  - Passport Number (and Country):
  - Current Occupation
  
- Taxpayer Representative and his/her contact information.
  
- Explain the source of the funds.

- Disclose if you or any related entities are currently under audit or criminal investigation by the Internal Revenue Service or any other law enforcement authority.
  - Has the IRS notified you that it intends to commence an examination or investigation? **Yes No**
  - Are you under criminal investigation by any law enforcement authority? **Yes No**
  - If yes, please explain.
  
- Do you believe that the IRS has obtained information concerning your tax liability? **Yes No**
  - If yes, please specify.
  
- Please check the box to estimate the annual range of the highest aggregate *value* of your offshore accounts/assets.

<b>Highest Aggregate Account/Asset Value</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
\$0 to \$100,000						
\$100,000 to \$1,000,000						
\$1,000,000 to \$2,500,000						
\$2,500,000 to \$10,000,000						
Greater than \$10,000,000						
Greater than \$100,000,000						

- Please check the box to estimate the potential total unreported *income* from the offshore account(s) during each disclosure period. If known, please enter exact amounts/assets.

<b>Estimated Total Unreported Income</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
\$0 to \$100,000						
\$100,000 to \$1,000,000						
\$1,000,000 to \$2,500,000						
\$2,500,000 to \$10,000,000						
Greater than \$10,000,000						

- For accounts or assets where you have control or are a beneficial owner of the account or asset, list any and all financial institutions and the country where the institution is located. For accounts, please also list the dates the accounts were opened and/or closed. Provide your point of contact at each financial institution.
- Explain the purpose for establishing the offshore account or assets. For example: Holocaust Compensation or Restitution; inherited account; account established prior to World War II, etc.; if tax non-compliance – please explain.
- List each person or entity affiliated with the account, their formal structure (i.e., if a corporation, foundation, or trust), and the nature of their relationship to the account (i.e. owner, power of attorney, parent entity of corporate account holder, etc.).
- Explain all face to face meetings, and any other communications you had regarding the accounts or assets with the financial institution(s). Also include face to face meetings or communications regarding the accounts or assets with independent advisors/investment managers not from the financial institution(s) where the funds are held. Provide the names, locations and dates of these meetings and/or communications.

**To be included with all letters:**

By signing this document, I certify that I am willing to continue to cooperate with the Internal Revenue Service, including in assessing my income tax liabilities and making good faith arrangements to pay all taxes, interest, and penalties associated with this voluntary disclosure.

Under penalties of perjury, I declare that I have examined this document and accompanying statements, and to the best of my knowledge and belief, they are true, correct, and complete.

\_\_\_\_\_  
Signature of Taxpayer

\_\_\_\_\_  
Print Name

\_\_\_\_\_  
Date

**IRS reserves the right to make further contacts with the taxpayer to clarify his/her submission.**

8. VDP Q & A 1-52 (and 7/14/09 update from [irs.gov](http://irs.gov))

7/8/09

## Frequently Asked Questions – Revised June 24, 2009

### 1. Why did the IRS issue internal guidance regarding offshore activities now?

The IRS has had a voluntary disclosure practice in its Criminal Manual for many years. Once IRS Criminal Investigation has determined preliminary acceptance into the voluntary disclosure program, the case is referred to the civil side of IRS for examination and resolution of taxes and penalties. Recent IRS enforcement efforts in the offshore area have led to an increased number of voluntary disclosures. Additional taxpayers are considering making voluntary disclosures but are reportedly reluctant to come forward because of uncertainty about the amount of their liability for potentially onerous civil penalties. In order to resolve these cases in an organized, coordinated manner and to make exposure to civil penalties more predictable, the IRS has decided to centralize the civil processing of offshore voluntary disclosures and to offer a uniform penalty structure for taxpayers who voluntarily come forward. These steps were taken to ensure that taxpayers are treated consistently and predictably.

### 2. What is the objective of these steps?

The objective is to bring taxpayers that have used undisclosed foreign accounts and undisclosed foreign entities to avoid or evade tax into compliance with United States tax laws. Additionally, the information gathered from taxpayers making voluntary disclosures under this practice will be used to further the IRS's understanding of how foreign accounts and foreign entities are promoted to United States taxpayers as ways to avoid or evade tax. Data gathered will be used in developing additional strategies to inhibit promoters and facilitators from soliciting new clients.

### 3. Why should I make a voluntary disclosure?

Taxpayers with undisclosed foreign accounts or entities should make a voluntary disclosure because it enables them to become compliant, avoid substantial civil penalties and generally eliminate the risk of criminal prosecution. Making a voluntary disclosure also provides the opportunity to calculate, with a reasonable degree of certainty, the total cost of resolving all offshore tax issues. Taxpayers who do not submit a voluntary disclosure run the risk of detection by the IRS and the imposition of substantial penalties, including the fraud penalty and foreign information return penalties, and an increased risk of criminal prosecution.

### 4. What is the IRS's Voluntary Disclosure Practice?

The Voluntary Disclosure Practice is a longstanding practice of IRS Criminal Investigation of taking timely, accurate, and complete voluntary disclosures into account in deciding whether to recommend to the Department of Justice that a

## **Frequently Asked Questions**

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taxpayer be criminally prosecuted. It enables noncompliant taxpayers to resolve their tax liabilities and minimize their chances of criminal prosecution. When a taxpayer truthfully, timely, and completely complies with all provisions of the voluntary disclosure practice, the IRS will not recommend criminal prosecution to the Department of Justice.

### **5. How do I make a voluntary disclosure and where should I submit my voluntary disclosure?**

A voluntary disclosure is made by following the procedures described in I.R.M. 9.5.11.9. Tax professionals or individuals who want to initiate a voluntary disclosure, should call their local CI office. For a list of CI offices, visit: <http://www.irs.gov/compliance/enforcement/article/0,,id=205909,00.html>

Taxpayers with questions may call the IRS Voluntary Disclosure Hotline at (215)516-4777, visit [www.irs.gov](http://www.irs.gov), or contact their nearest CI office.

### **6. What form should my voluntary disclosure take?**

You should send a letter to the nearest Special Agent in Charge, IRS Criminal Investigation, stating that you wish to make a voluntary disclosure. Ideally, the letter should contain all your identifying information, including name, address, Social Security Number or other Taxpayer Identification Number, passport number and date of birth, and should also include an explanation of any previously unreported or underreported income or incorrectly claimed deductions or credits related to undisclosed foreign accounts or undisclosed foreign entities, including the reason(s) for the error or omission. It should also include a power of attorney (Form 2848), if you are represented, and daytime contact information for you or your representative. If you have already completed the amended or delinquent returns, those should be submitted with the letter, but it is not necessary to include them with the initial submission if you are unable to do so. At a minimum, however, the initial submission must include the taxpayer's name and identifying information described above. IRS Criminal Investigation will follow up on the facts and circumstances to assess the timeliness, completeness, and truthfulness of the voluntary disclosure.

### **7. I'm currently under examination. Can I come in under voluntary disclosure?**

No. If the IRS has initiated a civil examination, regardless of whether it relates to undisclosed foreign accounts or undisclosed foreign entities, the taxpayer will not be eligible to come in under the IRS's Voluntary Disclosure Practice.

### **8. I have an offshore merchant account upon which I have not reported all of the income. Can I come in under the IRS's voluntary disclosure practice?**

## Frequently Asked Questions

Yes. Taxpayers with unreported income from an offshore merchant account can make a voluntary disclosure.

- 9. I have properly reported all my taxable income but I only recently learned that I should have been filing FBARs in prior years to report my personal foreign bank account or to report the fact that I have signature authority over bank accounts owned by my employer. May I come forward under the voluntary disclosure practice to correct this?**

*Proper  
report Y/T*

The purpose for the voluntary disclosure practice is to provide a way for taxpayers who did not report taxable income in the past to voluntarily come forward and resolve their tax matters. Thus, if you reported and paid tax on all taxable income but did not file FBARs, do not use the voluntary disclosure process.

For taxpayers who reported and paid tax on all their taxable income for prior years but did not file FBARs, you should file the delinquent FBAR reports according to the instructions and attach a statement explaining why the reports are filed late. Send copies of the delinquent FBARs, together with copies of tax returns for all relevant years, by September 23, 2009, to the Philadelphia Offshore Identification Unit at:

Internal Revenue Service  
11501 Roosevelt Blvd.  
South Bldg., Room 2002  
Philadelphia, PA 19154  
Attn: Charlie Judge, Offshore Unit, DP S-611

The IRS will not impose a penalty for the failure to file the FBARs.

- 10. What if the taxpayer has already filed amended returns reporting the additional unreported income, without making a voluntary disclosure (i.e., quiet disclosure)?**

The IRS is aware that some taxpayers have attempted so-called "quiet" disclosures by filing amended returns and paying any related tax and interest for previously unreported offshore income without otherwise notifying the IRS. Taxpayers who have already made "quiet" disclosures may take advantage of the penalty framework applicable to voluntary disclosure requests regarding unreported offshore accounts and entities. Those taxpayers must send previously submitted documents, including copies of amended returns, to their local CI office by September 23, 2009. See FAQ 5.

*Quiet*

Taxpayers are strongly encouraged to come forward under the Voluntary Disclosure Practice to make timely, accurate, and complete disclosures. Those taxpayers making "quiet" disclosures should be aware of the risk of being examined and potentially criminally prosecuted for all applicable years.

## Frequently Asked Questions

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The IRS has identified, and will continue to identify, amended tax returns reporting increases in income. The IRS will be closely reviewing these returns to determine whether enforcement action is appropriate.

**11. Is a taxpayer who sought relief under the IRS's Voluntary Disclosure Practice before this internal guidance was issued, eligible for the terms described in this internal guidance?**

Yes. If a taxpayer sought relief under the IRS's Voluntary Disclosure Practice before this internal guidance was issued he or she may be eligible, as long as the voluntary disclosure has not yet resulted in an assessment.

**12. How does the penalty framework work? Can you give us an example?**

Assume the taxpayer has the following amounts in a foreign account over a period of six years. Although the amount on deposit may have been in the account for many years, it is assumed for purposes of the example that it is not unreported income in 2003.

Year	Amount on Deposit	Interest Income	Account Balance
2003	\$ 1,000,000	\$ 50,000	\$ 1,050,000
2004		\$ 50,000	\$ 1,100,000
2005		\$ 50,000	\$ 1,150,000
2006		\$ 50,000	\$ 1,200,000
2007		\$ 50,000	\$ 1,250,000
2008		\$ 50,000	\$ 1,300,000

(NOTE: This example does not provide for compounded interest, and assumes the taxpayer is in the 35-percent tax bracket, files a return but does not include the foreign account or the interest income on the return, and the maximum applicable penalties are imposed.)

**If the taxpayer comes forward and has their voluntary disclosure accepted by the IRS, they face this potential scenario:**

They would pay \$386,000 plus interest. This includes:

- Tax of \$105,000 (six years at \$17,500) plus interest,
- An accuracy-related penalty of \$21,000 (i.e., \$105,000 x 20%), and
- An additional penalty, in lieu of the FBAR and other potential penalties that may apply, of \$260,000 (i.e., \$1,300,000 x 20%).

**If the taxpayer didn't come forward and the IRS discovered their offshore activities, they face up to \$2,306,000 in tax, accuracy-related penalty, and FBAR penalty. The taxpayer would also be liable for interest and possibly**