Forbes

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THE TAX LAWYER

Jun. 15 2011 — 4:02 pm

How Do You Opt Out Of IRS Voluntary Disclosure?

Announced February 8, 2011, the IRS 2011 Offshore Voluntary Disclosure Initiative (OVDI) program is a welcome but conditional amnesty allowing taxpayers to come clean with foreign accounts and get into compliance with the IRS. The program runs through August 31, 2011, but in some cases can be extended until November 29, 2011. See IRS Updates Voluntary Disclosure Amnesty: What You Should Know.

Some find the system inflexible and fear they may be paying more than necessary given their facts. See IRS Voluntary Disclosure A Mistake For Some. There's been discussion of "opting out" of the program to take your chances in audit, but it's a topic fraught with fear. Now, however, there is guidance about opting out of the program that makes much of it transparent.

Program Basics. Under the OVDI, taxpayers are subject to a penalty of 25 percent of the highest aggregate account balance on their undisclosed account(s) between 2003 and 2010. If the value was less than $75,000 at all times during those years, the penalty is only 12.5 percent. See FAQ 53. Moreover, in limited inheritance situations, a penalty of only 5 percent may be imposed. See FAQ 52.

These account balance penalties are in lieu of all other penalties that may apply, including FBAR and offshore-related information return penalties. Plus, participants are required to pay taxes and interest on any monies (such as interest income on foreign accounts) they previously failed to report. Finally, they must pay an accuracy-related penalty equal to 20 percent of the underpayment of tax, plus interest.

Opting Out. Opting out of the program can make sense for some, though it involves taking your chances with an IRS examination. The IRS has published a separate guide detailing the rules and procedures for opting out. See Opt Out and Removal Guide for the 2009 OVDP and 2011 OVDI. The IRS illustrates pros and cons of opting out with examples. See FAQ 51.

Here are some of the rules.

1. ***Program Status Report.*** Before you can opt out, the IRS sends a letter reporting on the status of your disclosure and what you still must submit. If you've given enough data, the IRS will calculate what you would owe under the OVDI. You should provide any missing items within 30 days.

2. ***Written Warning.*** The IRS sends another letter explaining that opting out must be in writing and is irrevocable. You have 20 days thereafter to opt out in writing.

3. ***Taxpayer Submission.*** Within 20 days, the taxpayer opts out in writing and makes a written case what penalties should apply and why.

4. ***IRS Summary.*** The IRS employee who has been handling your case summarizes it, agreeing or disagreeing with your view of penalties, and listing how extensive an audit he or she recommends.

5. ***Central Committee.*** A Committee of IRS Managers reviews the summary and decides how extensive an audit to conduct. The IRS says ***"the taxpayer is not to be punished (or rewarded) for opting out."*** See Opt Out and Removal Guide for the 2009 OVDP and 2011 OVDI. The Committee also decides whether to assign your case for a

normal civil audit or to assign it for a Criminal exam.

6. ***Interview?*** Some audits will include taxpayer interviews.

Bottom Line? The opt out procedure is helpful but still a bit daunting. If you are considering it, make sure you get some solid advice from an experienced tax lawyer about the nature of your facts. See FAQ 51.

For more, see:

Latest Foreign Account Prosecution Fuels Fears

IRS Foreign Account Disclosure: What About The States?

IRS Will Find Your Offshore Account

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