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Slash IRS Penalties By ‘Opting Out’

Since 2009, Americans with secret offshore accounts and income sought forgiveness in a quasi-amnesty program, the IRS Offshore Voluntary Disclosure Program ([OVDP](#)). It involved predicable penalties in exchange for freedom from bigger penalties or even prosecution. The [OVDP closed to new entrants](#) on September 28, 2018, but many cases remain in the pipeline. For them, the decision whether to “[opt out](#)” may still be relevant. Opt-outs *sound* odd. Why enter a special program, only to exit before completion? The OVDP is rigid, so the penalties are fixed. By the end, some taxpayers feel that OVDP penalties are downright punitive, particularly when another disclosure method (such as Streamlined with lower or nonexistent penalties) might have been as good.

No matter how sympathetic your facts might be, the IRS agents do not have discretion to settle OVDP cases for less than the set penalties. If you find yourself on the receiving end of an unfavorable formulaic deal, one option is to ‘opt out’ of the OVDP. The decision to opt-out is typically made after the IRS has calculated a proposed penalty and provided a closing agreement. That might be a year or even more after you entered the OVDP. Rather than paying a penalty of 27.5% or 50% of the highest account balance, opting out allows you to request a reduced penalty based on your facts and circumstances. Yet in opt outs, the IRS can demand additional documents and even a phone interview, which are unpleasant thoughts for most people.

You might save big, but could you actually end up paying *more* by opting out? It is theoretically possible, although it seems pretty unlikely. Still, that is one reason to look at your facts and numbers carefully before you act. If you are facing a small penalty (say \$50,000), opting out probably cannot save you too much, particularly after legal fees. Yet larger OVDP penalties such as

\$500,000, \$1M, or more may make opting out hard to resist if you have good facts. Some penalties can still apply in an opt out, but [much will hinge on willfulness](#). If you aren't willful, the penalties are vastly smaller. However, even non-willful violations can add up when taxpayers have multiple accounts for multiple years.



Non-willful FBAR penalties can range up to \$10,000 per account per year. The statute of limitations is usually six year. Therefore, even for non-willful violations, the penalty could be \$60,000 per account. If you have five accounts that you fail to list for six years, that could be \$300,000. Despite these warnings, most opt outs come out well, in my experience. Remember the old consumer warnings not to try this at home, or warnings that past results are not an indication of future results?

Those cautionary labels are appropriate, but with a little luck, opt outs *can* be home runs on the right facts. In one opt out case, an older man moved from one bank to the next after one bank closed his accounts. He failed to report accounts accurately even after entering the OVDP, and he made inconsistent statements to the IRS when represented by prior counsel. We submitted medical records showing he was experiencing memory loss, and emphasized that he had made significant efforts to come into compliance. The IRS's opt out exam resulted in penalties under \$200,000 compared to the nearly \$2 million penalty he would have paid under the OVDP formula.

In another case, an older expatriate moved money from one country to another after her accounts were closed. She had even used a shell company.

However, we emphasized that her late husband had controlled the accounts, and that she had little understanding of U.S. reporting. She paid less than \$200,000 after an opt out exam, compared with more than a \$1.5M penalty under the OVDP. An even more striking comparison was a formulaic OVDP penalty of over \$3M, which ended up whittled to less than \$50,000 in an opt out. In two other cases, OVDP penalties of \$1.5M were cut below \$75,000. In one more, a \$2M OVDP penalty landed under \$100,000 via an opt out. A less dramatic comparison was an opt out result of about \$45,000, down from the OVDP formula of more than \$200,000. Still, even this reduction can be worth the trouble.

The facts matter, as does the judgment and handling of the case by the IRS, no matter how sympathetically one presents the taxpayer. A sober discussion with any opt out candidate is a good idea. The OVDP is predictable, and opting out is much less so, so think about your facts. If you have no evidence of willfulness, the sheer numbers may make opting out awfully hard to resist. Ask whether the potential risks of opting out offset the potential rewards. Advice about the facts and the taxpayer's conduct is important. Using a different passport, moving banks, or giving a FATCA certification to a bank that turns out not to be true might be explainable in some cases. But these kinds of acts can raise eyebrows so must be thought through carefully.

It can be hard to turn away from certainty in favor of something that could be better or worse. Examine your numbers and risk profile, and be careful. For those with the right facts and a willingness to endure some risk, opting out can offer vast savings.

Check out my [website](#).