Tax Insights
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New IRS relief for US citizens living outside the US

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In brief

On June 18, 2014, the US Internal Revenue Service (IRS) announced changes to its offshore voluntary compliance programs that are expected to significantly increase the number of US persons that can participate in these programs.

The announcement responds to criticism from US taxpayers and the IRS's own Taxpayer Advocacy Service. It is good news for US citizens living in Canada who are struggling with how to meet their US filing obligations. The latest changes make it easier for those US citizens who have filed their Canadian tax returns and paid all of their Canadian taxes while living in Canada.

In detail

Background

Two IRS programs have allowed US persons who have not complied with their US filing obligations to come forward and avoid criminal prosecution and substantial penalties:

- The 'streamlined' process – Simplified procedures (more commonly used by Canadians) were introduced in 2012 for US persons who live outside of the US and owe little or no tax.
- The 2012 Offshore Voluntary Disclosure Program (OVDP) – A 27.5% penalty is assessed on the highest aggregate balance or value of the person's offshore assets during the previous eight years (penalties of 5% or 12.5% also apply in certain cases).

Changes to the streamlined process

To use the streamlined process, a taxpayer must still file three years of past US federal tax returns and six years of past Foreign Bank Account Reports (FBARs).

However, the recent changes:

- remove the limit of $1,500 or less of unpaid US tax per year to qualify for the program
- remove the need for applicants to complete a risk questionnaire
- require participants to certify that previous failures to comply were due to non-wilful conduct
- treat individuals as meeting the non-residency requirement if certain criteria were met in at least one of the last three years for which the US tax return date (including extensions) has passed

As with the previous program, individuals will be granted retroactive relief for failing to timely elect income deferral on certain RRSPs where the election is permitted under a treaty.

Changes to the OVDP

For US persons who do not qualify for the streamlined process, the IRS has changed the OVDP to provide more certainty and relief from prosecution.

This OVDP may be available when the failure to comply is viewed as wilful. Under the changes, taxpayers:

- will be required to provide more information when applying (though records may now be submitted electronically)
- must submit all account statements when applying
- may face an increased 50% penalty (up from 27.5%) when the financial institution holding the account or another party facilitating the taxpayer's offshore arrangement is under investigation by the IRS or the Department of Justice
- must pay the offshore penalty at the time of the submission

When do the changes apply?

The changes to both programs apply to all submissions made after June 30, 2014.

US persons who made an OVDP submission before July 1, 2014, but do not have a fully executed OVDP closing agreement by that date, can elect to have their case considered under the new rules by:

- communicating this request in writing, and
- submitting all additional required documents to the examiner assigned to the case or, when no examiner is assigned, to the IRS OVDP Determination team

The takeaway

These changes become effective at the same time as the new information reporting regime under the *Foreign Account Tax Compliance Act* (FATCA).

Under FATCA, Canadian and other foreign financial institutions will report to the IRS foreign accounts held by US persons.

Therefore, US persons not previously compliant are strongly encouraged to take advantage of these new voluntary disclosure programs while there is still time.

Complying with the reporting requirements may be difficult and time-consuming. Taxpayers should contact their PwC advisors to determine which program is appropriate in their circumstances.

Let's talk

For a deeper discussion of these issues, please contact any of the following or your PwC HRS advisor.

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