Recent Changes in Federal Tax Law: Fresh Start Program and Offshore Disclosures

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The IRS' Fresh Start program

It is getting easier to strike a deal with the Internal Revenue Service ("IRS"). Over the last two years, the IRS has implemented its "Fresh Start Initiative" program that makes it easier for taxpayers to pay back unpaid federal taxes and avoid tax liens. Although the Fresh Start program was announced by the IRS over two years ago, very few taxpayers are aware of the remarkable benefits that are available to them through the program or the recent expansions that favor taxpayers even further. The following highlights some of the changes made by the IRS in the Fresh Start program:

- **Higher lien filing thresholds.** Under Internal Revenue Code ("Code") § 6321, when a taxpayer fails to pay a tax liability after notice and demand, a lien arises that attaches to all of the taxpayer's property and rights to property. The Fresh Start program has increased the amount taxpayers can owe before the IRS generally will file a Notice of Federal Tax Lien ("NFTL"). Currently, that amount is $10,000. Additionally, the program has modified procedures making it easier for taxpayers to obtain lien withdrawals, which are more favorable than simply a lien release because a withdrawal requires the tax laws be applied as if the NFTL had not been filed. The IRS will now allow lien withdrawals once a taxpayer enters into a direct debit installment agreement or upon full payment of the taxes. Taxpayers must request this in writing using Form 12277, Application for Withdrawal.

- **Installment agreements.** The Fresh Start program significantly expanded access to streamlined installment agreements. Now, individual taxpayers who owe up to $50,000 (previous limit was $25,000) can pay through monthly direct debit payments up to six years. Typically, the IRS will not require a thorough financial statement to set up a direct debit installment agreement. Taxpayers can use Form 9645, Installment Agreement, to apply. Also, the IRS will allow a lien withdrawal when the balance is less than $25,000, the taxpayer enters into a direct debit installment agreement, and the taxpayer requests the withdrawal.

- **Liberalized offer in compromise terms.** Lastly, but not definitely not least, the Fresh Start Initiative has generously expanded the terms of the IRS' offer in compromise ("OIC") program. Under Code § 7122, the IRS will accept an OIC when: 1) the taxpayer is unable to pay the tax; 2) there is doubt as to the taxpayer's liability for the tax; or 3) a compromise would promote effective tax administration because collection of the tax would cause economic hardship for the taxpayer, or there are compelling public policy or equity considerations that provide a sufficient basis for compromising the liability. As a result of the Fresh Start program, the IRS will now calculate a taxpayer's offer that will be paid in five or fewer months by looking at only one year of future income, rather than four years. For offers paid in six to 24 months, the IRS will now look at only two years of future income, rather than five years. These policy changes have significantly increased the number of taxpayers eligible for an OIC and drastically reduced the dollar amount of accepted OIC's. In its latest expansion of the program, the IRS revised the calculation for the taxpayer's future income by allowing taxpayers to repay their student loans and state and local delinquent taxes and expanded the amount of allowance living expenses, among other changes.

Offshore Voluntary Disclosure Program

In 2009, the IRS announced an Offshore Voluntary Disclosure Program ("OVDP") to enable taxpayers to report previously unreported foreign account income without fear of criminal prosecution. In 2011, the IRS announced a second OVDP. In 2012, the IRS announced a third OVDP which was similar to the 2011 OVDP, but had no participation deadline. The IRS also provided streamlined filing compliance procedures for certain "low risk" nonresident U.S. taxpayers.

In June of this year, the IRS issued IR 2014-73, which made key expansions in the streamlined procedures. On October 16, 2014, the IRS clarified its streamlined offshore account compliance program procedures to include U.S. citizens residing in the U.S. the IRS calls this the streamlined program.

To use this program, an individual U.S. taxpayer residing in the U.S. (or his estate) must:

1. be a U.S. resident living in the U.S. for the past three years;
2. have previously filed a U.S. tax return (if required) for each of the most recent three years;
3. have failed to report gross income from a foreign financial asset and pay tax as required by law and/or failed to file certain required forms such as Foreign Bank Account Reports (FBARs); and
4. have committed the failures in (3) above as a result of non-willful conduct.

In general, U.S. taxpayers who want to come into compliance under the new streamlined program must:

1. for each of the most recent three years for which the U.S. tax return was due, file amended tax returns, together with all required information returns and pay the tax due plus interest;
2. for each of the most recent six years for which the FBAR due date has passed, file any delinquent FBARs online; and
3. pay a miscellaneous offshore penalty equal to five percent of the highest aggregate balance/value of the taxpayer's foreign financial assets.

These recent changes made to the federal tax laws with respect to delinquent tax collection clearly illustrate the IRS' efforts to be a kinder and gentler IRS.

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