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GETTING PERSONAL:Quiet Disclosure Now An Offshore-Saver Risk

By Arden Dale
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NEW YORK (Dow Jones)--Flying in under the radar is no longer safe for people with secret offshore bank accounts who want to get back on legal ground.

New IRS guidance has raised questions about whether the agency will continue allowing account holders to simply file amended returns and pay back taxes and fines to avoid heavy penalties for tax evasion. That had been common practice.

Now, individuals must flag their accounts to the IRS and go through a formal voluntary disclosure program, the agency indicated on May 6. That may lead to higher penalties, including criminal prosecution, according to tax experts.

Account holders who are already trying use the so-called "quiet" approach have until Sept. 23 to make a formal disclosure, which generally starts by having an attorney contact IRS Criminal Investigation agents.

The move comes as the IRS continues its crackdown on offshore accounts through a high-profile investigation involving thousands of people with Swiss bank accounts managed by UBS AG (UBS).

It is creating a stir among tax practitioners, who say the guidance contradicts advice some have been making to clients for generations.

The IRS disagreed with criticisms. "There has not been a substantive change involving 'quiet disclosures,'" says IRS spokesman Bruce Friedland.

Scott D. Michel, an attorney in the Washington D.C. office of law firm Caplin & Drysdale, says the IRS should clarify its message.

"IRS representatives have repeatedly confirmed the correctness" of quiet disclosure, he says. He believes the agency may have intended, in its new guidance, to say that account holders who were already under IRS investigation were at risk if they didn't use the more formal process.

"But that is not what they said, and it will undermine the IRS's compliance objectives if they do not clarify this," says Michel.

In the May 6 guidance, the IRS said it was aware some taxpayers have attempted quiet disclosures by filing amended returns and paying any related tax and interest for previously unreported offshore income. It said taxpayers are "strongly encouraged" to use the voluntary disclosure program, and those who didn't "should be aware of the risk of being examined and potentially criminally prosecuted for all applicable years."

Last month, the IRS announced limits on tax penalties for offshore accounts, hoping to coax some in from the cold. Instead, the rules are scaring many back into the shadows.

The new limits apply to voluntary disclosure cases already under way and to people who step forward within the next several months. Account holders must pay back taxes and interest for six years and an additional penalty on all six years. In addition, they owe a penalty of 20% of the account value for the year in which it was worth most.

Some tax experts have calculated that now, with accounts down by as perhaps 50% because of the slump in financial markets, a penalty of 20% of the highest balance effectively equals 40% of the account balance. Added to back income taxes owed on the account and a 20% income tax penalty plus interest, the total cost of voluntary disclosure is 60% or more.

One fear of tax attorneys is that the IRS may intend to prosecute more account holders who make timely voluntary disclosures, whether quiet or formal. Edward M. Robbins Jr., a partner at the law firm Hochman Salkin Rettig Toscher & Perez in Beverly Hills, Calif., said the government has not previously done so.

"This is a seismic shift," he says.

Teig Lawrence, a tax-problem-resolution attorney at Teig Lawrence, P.A. in Miami, says the May 6 guidance implies the IRS is tracking quiet disclosures, something he says he doesn't think the agency had done in the past.

Lawrence generally has recommended against quiet disclosures in UBS cases, he says, because they are too much like "rolling the dice." The account holder, he adds, is essentially saying 'Look, I'll file the returns and hope for the best, pay the tax and penalties due and hope I don't open a can of worms."

In light of attention on UBS, advising clients to pursue quiet disclosures was probably aggressive advice that now may come back to bite some tax professionals, says Lawrence.

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