DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

DEPUTY COMMISSIONER

June 1, 2011

MEMORANDUM FOR COMMISSIONER, LARGE BUSINESS AND INTERNATIONAL DIVISION
COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION

FROM: Steven T. Miller
Deputy Commissioner for Services and Enforcement

SUBJECT: Guidance for Opt Out and Removal of Taxpayers from the Civil Settlement Structure of the 2009 Offshore Voluntary Disclosure Program (2009 OVDP) and the 2011 Offshore Voluntary Disclosure Initiative (2011 OVDI)

Based on the feedback received from agents, managers, and practitioners, which demonstrated the need for additional guidance in the processing of offshore voluntary disclosure cases, I am issuing the attached guide to set forth the steps to be taken before and after a taxpayer opts out or is removed from the civil settlement structure of the 2009 OVDP or 2011 OVDI. Opt out and removal are two additional processes for resolving voluntary disclosure cases. The procedures have been designed to balance the interests at stake, to ensure fairness and consistency for all taxpayers in the 2009 OVDP and 2011 OVDI, and to allow for flexibility where necessary.

I want to thank you for all the hard work that has been done on these cases to date. I recognize that some of these cases involve difficult issues. I want to thank you for your continued diligence and professionalism especially as we continue to fine tune the program.

If you have any questions or comments about these procedures, please send an email to: *Opt Outs Removals Offshore Voluntary Disclosures.

Attachment

cc: Chief Counsel
Commissioner, Tax Exempt and Government Entities
Chief, Criminal Investigation
Chief, Appeals

OPT OUT AND REMOVAL GUIDE
FOR 2009 OVDP AND 2011 OVDI

The purpose of this guide is to discuss procedures that apply when a taxpayer requests to opt out of the civil settlement structure of the 2009 OVDP or 2011 OVDI or when the Service determines that a taxpayer should be removed from the civil settlement structure.

An opt out is an irrevocable election made by a taxpayer to have his or her case handled under the standard audit process. This is different from removal, which is a determination made by IRS personnel to remove a taxpayer from the civil settlement structure of the 2009 OVDP or 2011 OVDI. In either scenario, after certain procedures are followed, the voluntary disclosure case is removed from the civil settlement structure and an examination is initiated. The procedures are set forth below.

It should be recognized that in a given case, the opt out option may reflect a preferred approach. That is, there may be instances in which the results under the applicable voluntary disclosure program appear too severe given the facts of the case. There will be other instances where this is less clear. In the latter case, the Service will look to ensure that the best interests of the government and the integrity of the voluntary disclosure program remain intact. In these cases, it is expected that full scope examinations will occur if opt out is initiated. It is expected that opt out will be appropriate for a discrete minority of cases. Moreover, to the extent that issues are found upon a full scope examination that were not disclosed, those issues may be the subject of review by the Criminal Investigation Division. In either case, opting out is at the sole discretion of the taxpayer and the taxpayer should not be treated in a negative fashion merely because he or she chooses to opt out.

The procedures in this guide do not apply to any taxpayers that have already signed a Form 906 closing agreement.

OPT OUT AND REMOVAL GUIDE
FOR 2009 OVDP AND 2011 OVDI

I. Opt Out Procedures

***Steps to be taken before Opt Out*:**

The Service has a responsibility to any taxpayer considering opting out and undergoing an examination to ensure that the taxpayer is making an informed decision. An opt out could result in a taxpayer owing more than the taxpayer would under the civil settlement structure, but it also could result in a taxpayer owing less. Moreover, the scope of any resulting examination may change from being limited to offshore accounts. To that end, examiners will take the following steps before a taxpayer makes the irrevocable decision to opt out:

1. Send Letter 4728 (Attachment 1) to the taxpayer setting forth the status of the voluntary disclosure certification, documents required to finalize the certification, and, if known, the tax, interest, and penalties likely to be due under the terms of the 2009 OVDP or 2011 OVDI civil settlement structure through the issuance of a closing agreement and related Form 4549-A.

2. If the taxpayer does not provide the documents or make arrangements to provide the documents within 30 days of the status letter in 1. above, the examiner will issue Letter 4564 (Attachment 2) explaining that the decision to opt out is irrevocable and must be made in writing. The letter reminds the taxpayer of the continuing responsibility to cooperate with the Service under Criminal Investigation's Voluntary Disclosure Practice and instructs the taxpayer to provide a written statement setting forth the facts of the case and a recommendation of the penalties that should apply and the rationale for the penalty recommendations within 20 days of receiving the letter from the IRS.

Steps to be taken after Opt Out:

3. Once the taxpayer has provided the items described in 2. above, the examiner will prepare a summary of the case. The summary will document whether the examiner agrees with the taxpayer's statement of facts and recommendation of the penalties that should apply. If the examiner disagrees with either, the examiner will document the disputed facts (or note the lack of evidence in a given area) and penalty recommendations as well as any other facts or circumstances of which the reviewing committee should be aware. The examiner's summary should also include a recap of the income tax and accuracy-related penalties for each of the years, the case history notes, and the examiner's recommendation as to applicable penalties and whether or not the opt out would likely result in a determination of a non-willful FBAR penalty and the dollar amount of that penalty if known. Finally, the examiner's summary will include a recommendation regarding the scope of the examination.

4. After the examiner has documented the items described in 3. above, the examiner will forward the taxpayer's statement of facts, penalty recommendation, and rationale along with the examiner's summary of the case, including the items described in 3. above, and the examiner's case history notes to the centralized review committee, which will be comprised of managers.

5. The centralized review committee will review the taxpayer's statement of facts and recommendation of the penalties that should apply and the rationale for the penalty recommendations along with the examiner's statement and case history notes in order to determine how the examination will proceed. The committee will decide on the appropriate level of examination, keeping in mind that the taxpayer is not to be punished (or rewarded) for opting out. The committee will determine whether to reassign the case for a normal examination along with a determination of the likely scope of such examination, to reassign the case to a Special Enforcement Program agent, or to assign the case for other treatment. In making this determination, the committee will consider whether the results under the applicable voluntary disclosure program appear too severe given the facts of the case. The committee will also consider the cooperation of the taxpayer and the representative during the certification process, including whether removal was under consideration at the time of opt out. The decision of the committee is final.

6. If the case is assigned for a full-scope examination, the examiner ordinarily will interview the taxpayer to finalize the scope of the exam. Unless otherwise instructed by the centralized review committee, the examiner must open all years included in the taxpayer's voluntary disclosure. Examiners must take steps to protect the statute of limitations for any year with an ASED within 210 days (see Attachment 6). Examiners must also ensure that the case is updated to project code 1089.

II. Removal Procedures

It is anticipated that removal will occur only in those cases where the taxpayer or the taxpayer's representative has been demonstrably uncooperative, the lack of cooperation has been documented by the examiner, and the examiner has concluded that the case will not be resolved in an appropriate timeframe pursuant to the civil settlement structure of the 2009 OVDP or 2011 OVDI. This may occur, for example, in cases where the taxpayer/representative has not communicated with the agent after repeated requests since first filing the offshore disclosure; where the taxpayer/representative has been nonresponsive to both written and telephonic requests for longer than 60 days; or where a taxpayer/representative has received the Form 906 Closing Agreement for signature, but after 60 days, the taxpayer refuses to sign it and declines to opt out of the program.

Removal is an IRS determination based upon all of the facts and circumstances of the case and such determinations will only be made where agreement with the taxpayer cannot be reached within the parameters of the civil settlement structure of the 2009 OVDP or 2011 OVDI. If removal occurs, the protection from criminal prosecution under the 2009 OVDP and 2011 OVDI may be compromised. This does not mean prosecution will occur, merely that the taxpayer does not continue to have OVDP or OVDI protections.

Steps to be taken before Removal:

The Service has a responsibility to advise any taxpayer being considered for removal that an examination could result in a taxpayer owing more than the taxpayer would under the civil settlement structure of the 2009 OVDP or 2011 OVDI. To that end, examiners should take the following steps before a removal is effected:

1. Send Letter 4729 (Attachment 3) to the taxpayer setting forth the status of the voluntary disclosure certification, the documents required to finalize the certification, and, if known, the tax, interest, and penalties likely to be due under the terms of the civil settlement structure of the 2009 OVDP or 2011 OVDI. This letter should include the dates the examiner has contacted or attempted to contact the taxpayer during the course of the certification process.

2. If the taxpayer or representative responds to the letter with a documented, legitimate explanation for the apparent non-cooperation, the taxpayer's deadline may be extended up to 60 additional days. A decision to extend the deadline is a determination to be made by the examiner and manager and will be based upon the facts and circumstances put forward by the taxpayer.

3. In those instances where the letter results in productive discussions with the taxpayer, the examiner will take steps to ensure that the taxpayer understands the specific information, documentation, and cooperation that is required for the civil settlement to proceed. The examiner will document all discussions and retain copies of all written correspondence.

4. Continued non-response or inability to timely reach agreement with the taxpayer within 30 days after issuance of the letter described in 1. above will result in the issuance of Letter 4566 to the taxpayer that the taxpayer's case will be removed from the civil settlement structure of the 2009 OVDP or 2011 OVDI (Attachment 4). Taxpayers who receive this notice will be given an opportunity to seek review of the decision to remove the case by the examiner's Territory Manager. Requests for review must be in writing and postmarked within 30 days of the date of the notice. The notice will provide instructions as to how to request review of the decision to remove. The Territory Manager will respond to the taxpayer in writing. If the Territory Manager agrees with the taxpayer, the written response will set forth new deadlines for the taxpayer to provide the outstanding information. If the taxpayer does not meet these new deadlines, the taxpayer's case will be referred to the centralized review committee for assignment as a normal examination.

Steps to be taken after Removal:

5. If after review the Territory Manager agrees with the decision to remove the taxpayer from the civil settlement structure of the 2009 OVDP or 2011 OVDI, the centralized review committee comprised of managers will review the case and the examiner's case history notes to determine how the examination will proceed. The committee will determine whether to reassign the case for a normal examination including likely scope, to reassign the case to a Special Enforcement Program agent, or to reassign the case for other treatment. The decision of the committee is final.

6. If the case is assigned for a full-scope examination, the examiner ordinarily will interview the taxpayer to finalize the scope of the exam. Unless otherwise instructed by the centralized review committee, the examiner must open all years included in the taxpayer's voluntary disclosure. Examiners must take steps to protect the statute of limitations for any year with an ASED within 210 days (see Attachment 6). Examiners must also ensure the case is updated to project code 1090.

OPT OUT AND REMOVAL GUIDE
FOR 2009 OVDP AND 2011 OVDI

Attachments:

1. Letter 4728 Opt Out Status Letter
2. Revised Letter 4564
3. Letter 4729 Removal Status Letter
4. Letter 4566 Removal Letter
5. Potential Penalties
6. Statutes of Limitation

Attachment 1
Letter 4728 Opt Out Status Letter

Internal Revenue Service
Office Mailing Address
City/State/Zip

Department of the Treasury

Date:

Taxpayer Identification Number

Tax Form:

Tax Period(s):

Person to Contact:

Employee ID:

Telephone Number:

Fax Number:

Dear (Insert Taxpayer Name):

Based on the information you've provided to date, we've prepared the following enclosed documents to provide you with the status of your voluntary disclosure:

- Form 906, *Closing Agreement on Final Determination Covering Specific Matters,*
- Form 4549-A, *Income Tax Discrepancy Adjustments, and*
- Form 4564, *Information Document Request,* if additional information is required.

If you have additional information you believe may impact our findings, please provide it to me within 30 days. Providing this information timely will result in a prompt resolution of your case.

Sincerely yours,

[Insert signature]
[Insert name]
[Insert title]

Attachments:

Dates of contacts and requests for information
Form 906 Closing Agreement on Final Determination Covering Specific Matters
Form 4549-A Income Tax Discrepancy Adjustments
Form 4564 Information Document Request (if applicable)

We have requested information from you or attempted to contact you as follows:

Date	Contact initiated by	Contact method	Result

Attachment 2
Revised Letter 4564

Internal Revenue Service
Office Mailing Address
City/State/Zip

Department of the Treasury

Date:

Taxpayer Identification Number:

Tax Form:

Tax Period(s):

Person to Contact:

Employee ID:

Telephone Number:

Fax Number:

Dear (Insert Taxpayer Name):

We are sending you this letter because you indicated you want to withdraw from the civil settlement structure relating to your voluntary disclosure. If you withdraw, the election is irrevocable. Further, you are still required to cooperate fully with the IRS in resolving your case. The preliminary acceptance letter you received from IRS Criminal Investigation states, in part, that you:

> "...must fully cooperate with the IRS in determining the correct and appropriate tax liability and pay or make bona fide arrangements to pay in full, any tax, interest, and penalties determined by the IRS to be applicable. This required cooperation includes the production of all requested documents and the taxpayer submitting to an interview if requested by the examining agent."

Therefore, whether you choose for your case to be resolved under the civil settlement structure of the initiative or under standard examination procedures, you must provide all information.

Within 20 days of the date of this letter, please indicate, in writing, whether you wish to withdraw. If you wish to withdraw, also include in your letter the facts of your case and a recommendation of the penalties that you believe should apply. Include in your letter a discussion of any mitigating factors such as reasonable cause or lack of willfulness.

Once you withdraw, the tax, interest, and penalties will not be determined under the terms of the initiative. Rather, your case will be audited under standard examination procedures. At the end of the examination, the agent will discuss with you the tax, interest, and penalties determined to be owed. A list of possible penalties that may be proposed is enclosed.

If you don't provide the requested information within 20 days of the date of this letter, we'll assume you do not wish to opt out. We'll remove you from the civil settlement structure and initiate an audit under standard examination procedures. It is important that you contact us immediately.

Sincerely,

[Insert signature]
[Insert name]
[Insert title]

Enclosure: List of Penalties

Attachment 3
Letter 4729 Removal Status Letter

Internal Revenue Service
Office Mailing address
City/State/Zip

Department of the Treasury

Date:

Taxpayer Identification Number:

Tax Form:

Tax Period(s):

Person to Contact:

Employee ID:

Telephone Number:

Fax Number:

Dear (Insert Taxpayer Name):

You submitted a voluntary disclosure requesting the civil settlement structure relating to offshore issues. Internal Revenue Service Criminal Investigation sent you a letter preliminarily accepting your voluntary disclosure as timely, but stating that the acceptance was conditional upon your cooperation with the IRS in the determination and payment of the civil tax liability for those years.

Since that time, as noted in the attached, we've requested documents necessary to resolve the tax, interest, and penalties resulting from your offshore account(s) and/or transaction(s). You haven't provided these documents; therefore, we're unable to resolve your case.

We're enclosing the Form 4564, *Information Document Request*, that we previously sent you. If we don't receive the documents within 30 days from the date of this letter, you will be removed from the civil settlement structure of the voluntary disclosure program. Removal from the civil settlement structure will result in your case being audited under standard examination procedures.

Sincerely,

[Insert signature]
[Insert name]
[Insert title]

Attachments:

Dates of contacts and requests for information
Form 906, Closing Agreement on Final Determination Covering Specific Matters (if applicable)
Form 4549-A, Income Tax Discrepancy Adjustments (if applicable)
Form 4564, Information Document Request

We have requested information from you or attempted to contact you as follows:

Date of contact:	**Contact initiated by:**	**Contact method:**	**Result:**

Attachment 4
Letter 4566 Removal Letter

Internal Revenue Service
Office Mailing Address
City/State/Zip

Department of the Treasury

Date:

Taxpayer Identification Number:

Tax Form:

Tax Period(s):

Person to Contact:

Employee ID:

Telephone Number:

Fax Number:

Dear (Insert Taxpayer Name):

You submitted a voluntary disclosure requesting the civil settlement structure relating to your offshore issues. We've requested documents necessary to resolve the case, most recently on (insert date of Removal Status Letter).

We haven't received the requested documents; therefore, you will be removed from the civil settlement structure of this voluntary disclosure initiative. Your case will be audited under standard examination procedures.

You may request a review of this decision by submitting a written statement within 30 days from the date of this letter. Your request should include:

- a statement of the facts of the case,
- the documents in support of the facts, including any previously requested documents not yet provided, and
- your suggested course of action necessary to resolve your case.

Please direct your request to:

(2nd Level Management or designee)
Address 1
Address 2

Sincerely,

[Insert signature]
[Insert name]
[Insert title]

Attachment 5

Potential Penalties

Depending on a taxpayer's particular facts and circumstances, the following penalties may apply (these should be explained to the taxpayer):

- A penalty for failing to file the Form TD F 90-22.1 (Report of Foreign Bank and Financial Accounts, commonly known as an "FBAR"). United States citizens, residents and certain other persons must annually report their direct or indirect financial interest in, or signature authority (or other authority that is comparable to signature authority) over, a financial account that is maintained with a financial institution located in a foreign country if, for any calendar year, the aggregate value of all foreign accounts exceeded $10,000 at any time during the year. Generally, the civil penalty for willfully failing to file an FBAR can be as high as the greater of $100,000 or 50 percent of the total balance of the foreign account per violation. See 31 U.S.C. § 5321(a)(5). Non-willful violations that the IRS determines were not due to reasonable cause are subject to a $10,000 penalty per violation.

- A penalty for failing to file Form 3520, Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts. Taxpayers must also report various transactions involving foreign trusts, including creation of a foreign trust by a United States person, transfers of property from a United States person to a foreign trust and receipt of distributions from foreign trusts under IRC § 6048. This return also reports the receipt of gifts from foreign entities under IRC § 6039F. The penalty for failing to file each one of these information returns, or for filing an incomplete return, is 35 percent of the gross reportable amount, except for returns reporting gifts, where the penalty is five percent of the gift per month, up to a maximum penalty of 25 percent of the gift.

- A penalty for failing to file Form 3520-A, Annual Information Return of Foreign Trust With a U.S. Owner. Taxpayers must also report ownership interests in foreign trusts, by United States persons with various interests in and powers over those trusts under IRC § 6048(b). The penalty for failing to file each one of these information returns, or for filing an incomplete return, is five percent of the gross value of trust assets determined to be owned by the United States person.

- A penalty for failing to file Form 5471, Information Return of U.S. Persons with Respect to Certain Foreign Corporations. Certain United States persons who are officers, directors or shareholders in certain foreign corporations (including International Business Corporations) are required to report information under IRC §§ 6035, 6038 and 6046. The penalty for

failing to file each one of these information returns is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return.

- A penalty for failing to file Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. Taxpayers may be required to report transactions between a 25 percent foreign-owned domestic corporation or a foreign corporation engaged in a trade or business in the United States and a related party as required by IRC §§ 6038A and 6038C. The penalty for failing to file each one of these information returns, or to keep certain records regarding reportable transactions, is $10,000, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency.

- A penalty for failing to file Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation. Taxpayers are required to report transfers of property to foreign corporations and other information under IRC § 6038B. The penalty for failing to file each one of these information returns is ten percent of the value of the property transferred, up to a maximum of $100,000 per return, with no limit if the failure to report the transfer was intentional.

- A penalty for failing to file Form 8865, Return of U.S. Persons With Respect to Certain Foreign Partnerships. United States persons with certain interests in foreign partnerships use this form to report interests in and transactions of the foreign partnerships, transfers of property to the foreign partnerships, and acquisitions, dispositions and changes in foreign partnership interests under IRC §§ 6038, 6038B, and 6046A. Penalties include $10,000 for failure to file each return, with an additional $10,000 added for each month the failure continues beginning 90 days after the taxpayer is notified of the delinquency, up to a maximum of $50,000 per return, and ten percent of the value of any transferred property that is not reported, subject to a $100,000 limit.

- Civil fraud penalties imposed under IRC §§ 6651(f) or 6663. Where an underpayment of tax, or a failure to file a tax return, is due to fraud, the taxpayer is liable for penalties that, although calculated differently, essentially amount to 75 percent of the unpaid tax.

- A penalty for failing to file a tax return imposed under IRC § 6651(a)(1). Generally, taxpayers are required to file income tax returns. If a taxpayer fails to do so, a penalty of 5 percent of the balance due, plus an additional 5 percent for each month or fraction thereof during which the failure continues may be imposed. The penalty shall not exceed 25 percent.

- A penalty for failing to pay the amount of tax shown on the return under IRC § 6651(a)(2). If a taxpayer fails to pay the amount of tax shown on the return, he or she may be liable for a penalty of .5 percent of the amount of tax shown on the return, plus an additional .5 percent for each additional month or fraction thereof that the amount remains unpaid, not exceeding 25 percent.

- An accuracy-related penalty on underpayments imposed under IRC § 6662. Depending upon which component of the accuracy-related penalty is applicable, a taxpayer may be liable for a 20 percent or 40 percent penalty.

OPT OUT AND REMOVAL GUIDE
FOR 2009 OVDP AND 2011 OVDI
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Attachment 6

Statutes of Limitation

There are a number of exceptions to the general three-year statute of limitations under IRC § 6501(a). Depending on a taxpayer's particular facts and circumstances, one or more of these exceptions may apply:

1. IRC §§ 6501(c)(1) and (c)(2) allow assessment at any time if a tax return is false or fraudulent or there is a willful attempt to evade tax.

2. IRC § 6501(c)(8) allows an assessment within three years after the date certain offshore information returns are filed, including Forms 3520, 3520-A, 5471, and 5472.

3. IRC § 6501(e)(1)(A)(i) allows assessment within six years after the later of the due date or date filed if the taxpayer omits from gross income an amount properly includible therein and such amount is in excess of 25% of the amount of gross income stated in the return.

4. IRC § 6501(e)(1)(A)(ii) allows assessment within six years after the later of the due date or date filed if the taxpayer omits from gross income an amount properly includible therein and such amount exceeds $5,000 and is attributable to one or more foreign financial assets described in IRC § 6038D. This exception was added to the law in 2010 and applies to (1) returns filed after March 18, 2010, and (2) returns filed on or before March 18, 2010, if the statute of limitations has not otherwise expired as of March 18, 2010.

5. IRC § 6501(c)(4) allows the period for assessment to be extended for any period of time agreed upon in writing by the taxpayer and the IRS (e.g., by submitting Form 872).

6. The statute of limitations for assessment of the FBAR penalty is 6 years from the due date of the FBAR (Form TD-F-90-22.1). The FBAR due date is June 30 of the year following the reporting year. For example, the statute of limitations for a 2004 FBAR will expire June 30, 2011. The FBAR statute continues to run whether or not the FBAR was filed. The FBAR statute may be extended by consent.