

Delivering New York's Voluntary Disclosure Gold

by Timothy P. Noonan and Joseph N. Endres

Over the past year, the authors have been engaged in a lively discussion with officials of the New York State Department of Taxation and Finance regarding the state's revised voluntary disclosure program. Some of that discussion has appeared in the pages of this publication.¹ Our September 2008 article raised a few concerns about how this new program would operate. And recently Deputy Commissioner William Comiskey wrote a follow-up article detailing the voluntary disclosure program's success during its first year and explaining how the new program has struck gold.² We — the deliverers of some of that gold (not personally, of course, but through our clients) — are writing this article to provide a practitioner's perspective on the new program. And maybe, just maybe, we'll eat a little crow too.



Concerns With the New Program

The new voluntary disclosure program was enacted as part of Democratic Gov. David Patterson's 2008 budget. Details of how it works are in both our September 2008 article and Comiskey's recent article. Before the change, as we noted in our September 2008 article, the program was somewhat amorphous because it existed exclusively as a result of departmental policy. Still, it worked well, and the implementation of a new, statutory-based program raised some concerns in practitioner circles.

For instance, under the old program, taxpayers would contact the department through a representative to discuss a possible settlement of a past-due liability. The taxpayer's representative and the department would negotiate mutually acceptable terms that typically included a limited lookback period. Taxpayers would be required to reveal their identities only after they had a clear understanding of the terms of the disclosure. If they were unsatisfied with the negotiations, they could walk away without losing their anonymity. That is essentially how voluntary disclosure programs work in every other state. Under the new program, however, taxpayers are required to reveal their identities during the initial application process. Thus, taxpayers may be rejected from the new program and receive none of its benefits, yet would have revealed themselves to the department. We believed that could discourage some from participating in the program.

There was also a concern that the new lookback periods defined by the department could have potentially eliminated one of the primary benefits of the old program: its flexibility. By detailing specific periods and requiring taxpayers to follow predefined frameworks, the voluntary disclosure process lost the "negotiation" aspect and became more of a one-sided discussion. Indeed, as we noted in our September 2008 article, the implicit quid pro quo of the voluntary disclosure process is that the taxpayer gets a break for coming forward because, absent its coming forward, the state would have no reason to know about the noncompliance. That lended itself to a negotiated resolution, and the fear was that this aspect of the process would be eliminated under the new program.

How's It Going?

In a word: great.

We've been active in the program over the past year, with many of our clients contributing to the pot of gold highlighted by Comiskey in his article. And we could not be more pleased with how the program has been run. The Web-based application process has worked with the ease and simplicity noted by Comiskey in his article. Guidance is available not

only on the Web site, but also by calling some of the individuals charged with the responsibility of running the program and processing the agreements. In fact, one of the concerns we had going into the new program was that — since it now appeared to be automated - taxpayers might lose the ability to have direct contact with the person in the department in charge of processing the voluntary disclosure cases. But by far the best aspect of the new program — and the reason it has run smoothly thus far — is that the department personnel are available to respond to questions and concerns throughout every step of the process.

So hats off to Comiskey and the department. By all accounts, the program's first year has been a great success. Being from Buffalo, we'll take our crow deep-fried, with hot sauce.

But the concerns highlighted in our September 2008 article to some extent still exist. In practice, many of our clients continue to express concern about disclosing their identity before any agreement with the department. We don't expect that fear to dissipate. But what we now are able to tell clients — and what we understandably could not last year at this time — is that the new program runs smoothly and that none of our clients have been harmed by disclosing themselves at the outset of the process. We can also point to the helpful articles written by Comiskey in this and other publications describing the provisions of the program and the reasoning used in determining some criteria. Finally, and perhaps most importantly, we can now point to the department's track record, thus far, of treating taxpayers who come into the program in a fair manner. Knowing that other taxpayers have gone through the process and come out alive makes most clients feel a lot better.

All that being said, taxpayers will continue to have some apprehension about coming forward and disclosing their identities at the outset of the voluntary disclosure process. Comiskey has pointed to the new program's provision prohibiting the department from sharing information obtained during the voluntary disclosure process. The new law prohibits the dissemination of information obtained under the voluntary disclosure program as long as the taxpayer complies with the program's terms and conditions. But what if the taxpayer applies to the program and is not accepted? The department thus far has indicated that it would not use that information against the taxpayer, but there does not appear to be any prohibition in the law from doing so.³ So until the law is more specific on that issue, the fear that a rejected (or incomplete) voluntary disclosure application will lead to an immediate audit or investigation is going to remain.

Also, since the voluntary disclosure process is now a creature of statute, the Legislature has the ability to change the law or amend some provisions. Indeed, one noteworthy change on this very issue was passed this year. The antidisclosure provisions in Tax Law section 1700(4) were recently amended to include the following provision:

However, the disclosure of any returns or reports filed under this program with the secretary of the treasury of the United States, his or her delegates, or the proper tax officer of any state or city is permitted as otherwise provided for in this chapter.⁴

So practitioners should be tracking those changes. When the program started, the law prohibited any sharing of information. That important provision was changed just a few months into the new program.

Tips/Traps

Having participated in several voluntary disclosures over the past year, we can also offer some tips and suggestions for taxpayers and practitioners as they work through the process. Here goes:

- **Lookback Period.** As noted above, the new voluntary disclosure program contains a predefined set of lookback periods applicable to different taxpayers. Those taxpayers whose noncompliance relates to negligence or other unintentional wrongdoing can choose a three-year period. Those whose noncompliance was intentional or the result of fraud are required to use a six-year lookback. In practice, sometimes taxpayers might fall somewhere between those two categories. It's important for practitioners and their clients to carefully consider each of the issues associated with their noncompliance and pick the right period. Indeed, in filling out the application, taxpayers are required to indicate

the reasons why a limited three-year lookback period should apply. That issue has to be well thought out and the reasons communicated to the tax department on the application.

- **Foreign Bank Account Report Compliance Issues.** There has been a lot of press recently concerning disclosure of foreign bank accounts and the federal voluntary disclosure process associated with undisclosed income from foreign bank accounts. A federal voluntary disclosure process is in place requiring taxpayers to file tax returns for six prior years and pay taxes, interest, and related penalties. The tax department has informally indicated that taxpayers can use the new voluntary disclosure program to disclose the same types of issues regarding foreign bank account income. And the department's view is that a six-year disclosure period is applicable here. That being said, presumably if the noncompliance is unintentional, a three-year lookback period could apply.
- **Find a Person.** As noted above, one of the best parts of the new program isn't something you'll necessarily find listed in tax department articles or even on the Web site. The best part of the program is that there are plenty of capable individuals running the program who are available and willing to talk to taxpayers and practitioners about questions or concerns about the program. So if you have a question, give them a call and ask them. We found that to be the most effective way of assisting our clients through the process.
- **Use of Standard Agreements.** The tax department has developed a standard agreement that taxpayers are required to sign to gain entrance to the program. The provisions of that agreement do not vary much from taxpayer to taxpayer. That being said, we've also seen a little bit of flexibility, or at least a willingness to make modifications to the form. For instance, some initial forms contained provisions whereby taxpayers waived their rights to "protest or otherwise challenge the taxes and interest that the Department determines [are owed] as a result of [the] disclosure." That may have suggested, albeit unintentionally, that taxpayers could not dispute any additional taxes the department might determine could be due after a follow-up audit of the voluntary disclosure. We immediately raised some questions about the application of that provision. And shortly thereafter, the new agreements provided that the right to protest was indeed limited, but only to "challenge an assessment issued for nonpayment of taxes shown on your return or for a mathematical error discovered during the processing of your return filed under this agreement." That is a helpful clarification. But the bottom line is: read the agreements carefully. You might not have much of an opportunity in the future to modify what they say, but at the very least, it's important for you and your clients to understand them fully.
- **Consider Refund Issues.** One problem with the new voluntary disclosure program is that it does not allow taxpayers to obtain traditional refunds if they overpay on their disclosure payment.⁵ It's difficult to understand the rationale behind that provision. The department almost always conducts follow-up audits. If the audit results in a refund for the taxpayer, why should it be disallowed? Whatever the case, that is the rule, so practitioners would be wise to counsel clients so there are no surprises later.

Conclusion

One reason why New York's voluntary disclosure program has worked so well in its first year is because of the transparency Comiskey and others within the department have brought to the process. If practitioners raise concerns, they respond to them. If well-intentioned know-nothings like Noonan and Endres raise questions about the program in a public forum like this, department officials respond publicly and in a thoughtful manner. That type of transparency helps practitioners and taxpayers feel that their concerns are being addressed and that those in charge are thinking about and trying to respond to their concerns. So while most taxpayers probably still wish they could enter the voluntary disclosure program on an anonymous basis, the department's willingness to engage in debate and discussion on that and other issues associated with the program goes a long way to making the program work.

FOOTNOTES

¹ See Timothy P. Noonan and Joseph N. Endres, "Identifying and Resolving a New York Tax Problem Just Got Tougher," *State Tax Notes*, Sept. 29, 2008, p.899, *Doc 2008-19756* , or *2008 STT 190-3* ; William J. Comiskey, "New York's New Voluntary Disclosure Program," *State Tax Notes*, Oct. 20, 2008, p. 185, *Doc 2008-21685*, or *2008 STT 204-14* .

² See William J. Comiskey, "New York's Voluntary Disclosure and Compliance Program Strikes Gold," *State Tax Notes*, Sept. 7, 2009, p. 669, *Doc 2009-19210*, or *2009 STT 171-21* .

³ According to the department's Web site, "If a taxpayer applies but does not enter the . . . program, the information provided by the taxpayer cannot be used by the Department for any purpose and will not be shared with any agency."

⁴ N.Y. Tax Law section 1700(4).

⁵ N.Y. Tax Law section 1700(6) allows for refunds only if "the commissioner on his or her own motion redetermines the amount of tax due."