The Supreme Court Deals IRS a Losing Hand in FBAR Non-Willful Penalty Case

by Robert Horwitz

On February 28, 2023, the Supreme Court issued its opinion in *Bittner v. United States*, ___ U.S. ___, 143 S.Ct. 713, 2023 WL 2247233, holding that the non-willful FBAR penalty is applied per annual report and not per account. For the past few years, the IRS has taken the position that it could impose a separate $10,000 non-willful FBAR penalty based on the number of foreign accounts a U.S. person failed to properly report. The Ninth Circuit rejected the Government's argument and held the maximum penalty per year is $10,000, *United States v. Boyd*, 991 F. 3d 1077 (2021), while the Fifth Circuit held the $10,000 penalty could be imposed per account. *United States v. Bittner*, 19 F. 4th 734 (2021).

The Supreme Court split 5-4, with Justice Gorsuch penning the majority opinion and Justice Barrett penning the dissent, in which she was joined by Justices Thomas, Kagan and Sotomayor. The majority opinion posed the question before it (and the importance of the answer) as

> Does someone who fails to file a timely or accurate annual report commit a single violation subject to a single $10,000 penalty? Or does that person commit separate violations and incur separate $10,000 penalties for each account not properly recorded within a single report?
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> The answer makes a difference, especially for immigrants who hold accounts abroad and Americans who make their lives outside the country. On one view, penalties accrue on a per-report basis. So, for example, a single late-filed report disclosing the existence of 10 accounts may yield a maximum fine of $10,000. On another view, penalties multiply on a per-account basis, so the same report can invite a fine of $100,000 even if the individual's foreign holdings or total net worth do not approach that amount.

The majority began by discussing the Bank Secrecy Act (BSA). The BSA doesn't make it illegal to hold foreign financial accounts and doesn't tax those accounts. It "simply requires those who possess foreign accounts with an aggregate balance of more than $10,000 to file an annual report on a form known as an FBAR." The FBAR helps the government trace funds that may be used for illicit purposes and to identify unreported income.

31 U.S.C. §5314 authorizes the Treasury Secretary to require certain persons to keep records and file reports when they make a transaction or maintain a relationship with a "foreign financial agency." The statute does not speak of accounts or their number; instead, the "relevant legal duty is to file a report." Thus, either a report is filed "in the way and to the extent the Secretary prescribes" or it is not.

Under 31 U.S.C. §5321(a)(5), the Secretary can impose a civil penalty of up to $10,000 for "any violation" of §5314. According to the majority, in all cases non-willful penalties accrue on a per report, not a per account, basis. Penalties for willful FBAR violations are imposed under §5321(a)(5)(C)(i). The penalty for willful failure to report an account or any required

information about an account is the greater of either $100,000 or 50% of the amount in the account at the time of the transaction.

The majority rejected the Government's argument that it should infer that Congress intended the non-willful penalty to be applied in a manner analogous to the application of the willful penalty. According to the majority, under traditional rules of statutory construction when a statute contains particular language in one provision that is missing from another provision "the difference in language conveys a difference in meaning."

According to the majority the reasonable cause exception to the non-willful penalty was further evidence that "when Congress wished to tie sanctions to account-level information, it knows how to do so." Congress did not state that "the government may impose non-willful penalties on a per-account basis." The majority stated that the "dissent founders on the same shoals" in its argument based on the reasonable cause exception. "The fact that a person has a duty to file a report or provide certain information in a report does not tell us whether penalties for non-willful violations accrue per report or multiply per account without regards to the individual's net worth or foreign holdings."

The majority then reviewed guidance issued by the IRS, which stated that the maximum penalty for failing to file a report was $10,000. While "the government's guidance documents do not control our analysis and does not displace our independent obligation to interpret the law" the Court has stated that "courts may consider the consistency of an agency's views when we weigh the persuasiveness of any interpretations it offers in court."

Turning to the history of the non-willful penalty, the majority found that it undermines the Government's theory. It noted that the language for imposition of the non-willful penalty "bears scant resemblance to the language it uses when authorizing per-account penalties for certain willful penalties in 1986." BSA required the maintenance of certain records and the filing of reports. There was no evidence in the legislative history that Congress meant to penalize a person for every non-willful mistake

The majority also found support in the regulations, under which a person with 25 or more accounts does not have to list each one or provide details about every account.

According to the majority, the Government's position would lead to absurd results. A person with one account with $10 million who non-willfully fails to file a report could be liable for a maximum penalty of $10,000 while a person with 10 accounts having an aggregate value of $10,001 could face penalties of up to $100,000.

The majority's reaction to the Government's argument that the Secretary could require separate reports for each account was "so what." This does not answer the question before the court of whether the penalty is applied per report or per account.

The majority looked to the "rule of lenity" to support its position. This rule requires statutes imposing penalties to be strictly construed. It requires the Court to favor a per report over a per account approach, so penalties are not imposed "unless the language of the statute plainly imposes it." It rejected the Government's assertion that the rule of lenity under

Commissioner v. Aker, 361 U.S. 87 (1959), applies only to penalties imposed under the Internal Revenue Code. The rule of lenity protects due process's "promise that a 'fair warning should be given to the world in language that the common would will understand, of what the law intends to do if a certain line is passed." The Government's theory was seen as posing a serious fair notice problem, especially since its guidance all speaks of the penalty being applied "per report" and prior to 2008 and 2009 many tax professionals were unaware of the FBAR requirements.

Noting that §5321 contains civil penalties and §5322 contains criminal penalties for violations of the FBAR requirements, the majority reasoned if the Government was correct, a person with several foreign accounts who willfully failed to file an FBAR would have separate criminal violations for each account. "In these circumstances, the role of lenity, not to mention a dose of common sense, favors a strict construction." The majority pointed out in Bittner's case, if his conduct had been willful, under the Government's theory he would face total criminal penalties of 1,360 years in prison and fines of $68 million.

The majority ended its opinion:

> Best read, the BSA treats the failure to file a legally compliant report as one violation carrying a maximum penalty of $10,000, not a cascade of such penalties calculated on a per account basis. Because the Fifth Circuit thought otherwise, we reverse its judgment and remand the case for further proceedings consistent with this opinion.

The dissent disagreed, stating that "The most natural reading of the statute establishes that the failure to report a qualifying foreign account constitutes a separate violation, so the Government can lay penalties on a per account basis." It argued that §5321(a)(5)(A) allows imposition of a non-willful penalty for "any violation" of §5314, which requires U.S. citizens to "file reports" containing such information as the Secretary prescribes. Sec. 5314 "indicates" its reporting requirement attaches to each individual account. Under it, a report is triggered by maintaining a "relationship with a foreign financial agency." Each account is a separate relationship and each failure to report an account violates reporting requirements. Additionally, §5314(a)(1)-(3) list certain required information that is account specific and the record keeping requirements are also account specific.

The dissent then looked to the reasonable cause exception for a non-willful violation to support is reading. For the exception to apply, the violation must be due to reasonable cause and "the balance in the account at the time of the transaction was properly reported." According to the dissent, "this language suggests that the underlying violation of §5314 is similarly tied to a specific account.… The willful penalty provisions sing the same tune." Noting that under normal rules of statutory construction identical words in different parts of the same statute are presumed to have the same meaning, the dissent reasoned that

> If a violation of §5314 has account-specific connotations in the reasonable cause and willful penalty provisions, it follows that a "violation" of §5314 has account-specific connotations when it comes to nonwillful penalties too.

The dissent found that the implementing regulations support its view since they require the reporting of each foreign financial account annually. According to the dissent, the majority erred in conflating "reports" with "forms." The forms contain the reports, which are for each account. The dissent claimed the majority misread both §5314 and §5321 and the majority was wrong in assuming the account specific language in the willful penalty provisions meant that the non-willful penalty is not account specific, pointing out that both the willful penalty and the reasonable cause exception are account specific.

The dissent rejected the majority's reliance on administrative guidance materials since they don't add "to the interpretive enterprise when the traditional tools of construction supply an answer." That the Secretary allows a person with multiple foreign accounts to not list each account individually doesn't help the majority and the fact that a person with multiple accounts adding up to $10,001 would be subject to greater penalties than a person with one account with $1 million is because "a person who violates the law many times might naturally pay a steeper price than a person who violates it just once."

The dissent noted that Bittner lost his reasonable cause argument because, while he correctly reported the account balances on his late-filed FBARs, the district court found he did not act with ordinary business care and prudence in ascertaining his reporting obligations.

The dissent ended: "The most natural reading of the. BSA and its implementing regulations establishes that a person who fails to report multiple accounts on the prescribed reporting forms violates the law multiple times, not just once."

What can we learn from the *Bittner* opinion? Both the majority and the he dissent present arguments that while persuasive are open to attack. This may reflect a poorly drafted statute. Or that Congress, similar to masters of the language like Shakespeare, Yeats, Dylan and Method Man, write complex lines fraught with multiple layers of meaning. No, I think our elected representatives are have a difficult time drafting clear, concise statutes.

Speaking of our public servants, was it really necessary to assess $2.72 million in non-willful penalties. After all, Bittner voluntarily filed late FBARS after he returned to the United States from his long sojourn in Romania and disclosed all his foreign accounts. Sure, under the Government's construction of the statute he was potentially liable for multiple non-willful penalties, but was no one in the IRS capable of exercising judgment when the decision was made to assess the maximum amount of penalties that the IRS believed could be assessed? During oral argument, however, one of the Justices suggested the IRS could have pursued a willful penalty.

Which leads to my next point. In *Moore v. United States*, Case No. C13-2063RAJ (W.D. Wash. 2015), the plaintiff challenged the assessment of FBAR non-willful penalties for four years. The district court noted that the facts in the case before it were similar to those in *United States v. Williams*, 489 Fed. Appx. 655 (4th Cir. 2012), where the court held the taxpayer liable for willful FBAR penalties. The *Bittner* opinion may lead the IRS to assert willful FBAR penalties in cases where it previously may have been inclined to assess multiple nonwillful penalties. The IRS has made a lot of money for the Government through FBAR enforcement

since the first OVDP in 2009. There is no reason to believe it won't continue to pursue FBAR penalties where it feels they are justified.

Taxpayers against whom multiple FBAR penalties for a single year were assessed should request abatement of the penalties, or if they have paid the penalties, request a refund.