

Supreme Court Rules for Taxpayers on Non-Willful FBAR Penalties

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Tax Alert

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Taxpayers who hold foreign accounts finally received clarity as the Supreme Court ruled that the \$10,000 non-willful penalty for failure to file a FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR) applies on a per form, not per account, basis.

Background

The taxpayer in the case is Alexandru Bittner (Bittner), who was born in Romania and moved to the United States in 1982. He was naturalized in 1987, making him a dual citizen. Some years later, he returned to Romania, where he became a successful businessman and investor, earning millions of dollars. He invested the money in banks around the world, including accounts in Romania, Switzerland and Liechtenstein.

But Bittner, like many US taxpayers—especially those living abroad—did not know that he had to report his interests in certain foreign accounts.

Reporting Requirements

As part of the Bank Secrecy Act (BSA), every US person with a financial interest in, or signature or other authority over, one or more foreign financial accounts with an aggregate value of more than \$10,000 in a calendar year must report the account to the Treasury Department. For purposes of the FBAR, a US person includes a citizen, resident, corporation, partnership, limited liability company, trust and estate.

Typically, a foreign financial account is any account at a financial institution located outside the US. This includes, among other things, bank accounts, brokerage accounts and mutual funds (some exceptions apply). And, you have an obligation to report if you meet the criteria even if the account did not produce any taxable income.

You do this by filing a FinCEN Form 114 with the FBAR. One FBAR can be used to report multiple accounts.

The FBAR is due each year on April 15, unless that date falls on a weekend or holiday. This is the case in 2023, making the 2022 tax year due date April 18, 2023. Your FBAR is, however, separate from your tax return and is filed not with the IRS, but with FinCEN, or the Financial Crimes Enforcement Network. FinCEN is a bureau of the Treasury Department whose mission is to combat money laundering, promote national security and safeguard the financial system from illicit use. If you can't file by the deadline, you can get an automatic extension to October 15.

It is important to file because failure to report can result in a penalty. The size of the penalty depends on whether the failure is considered to be non-willful or willful. The maximum penalty for a non-willful violation is \$10,000. The maximum civil penalty for a willful failure is the greater of \$100,000 or 50% of the value of the account—willful criminal violations can also result in jail time.

Bittner's Mistakes

When Bittner returned to the US, he became aware of the reporting requirements, he says, for the first time. In an effort to get compliant, he hired a tax professional to assist him in preparing FBARs for those prior years. Those FBARs were later found to be inaccurate and he hired another tax professional to prepare revised, correct FBARs.

As a result, Bittner ended up on the IRS' radar. In June 2017, the IRS assessed penalties against him for failing to report the accounts for the tax years 2007-2011. In total, there were 272 accounts that had not been properly and timely reported for those five years. As a result, the government initially sought \$2,720,000 in penalties—\$10,000 for each account.

Bittner disagreed, claiming, among other things, that any penalty should apply per year, not per account. Using his penalty calculations, he would only owe \$50,000—\$10,000 for each of 2007, 2008, 2009, 2010 and 2011. He took the matter to court.

In 2020, the district court ruled in Bittner's favor, finding that the maximum penalty applied per FBAR, not per account. On appeal, the US Court of Appeals for the Fifth Circuit reversed the district court, finding that the penalty applied per account, not per FBAR. The Fifth Circuit's decision contrasted with a similar-in-time Ninth Circuit decision, *United States v. Boyd*.

As a result of the conflicting decisions, the Supreme Court agreed to hear the case and oral arguments began on November 2, 2022.

What the Ruling Means for Taxpayers

On February 28, 2023, the Supreme Court held that the BSA's \$10,000 maximum penalty for the non-willful failure to file a compliant FBAR should be calculated on a per report, rather than a per account, basis. The opinion made clear that 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." That favors the taxpayer—in this case, to the tune of more than \$2 million.

The decision was a close vote, 5-4, with Justice Barrett writing in the dissent, "The most natural reading of the statute establishes that each failure to report a qualifying foreign account constitutes a separate reporting violation, so the Government can levy penalties on a per-account basis. Nevertheless, the Supreme Court reversed the Fifth Circuit and remanded the case back to district court.

The court did not weigh in on the penalty structure for willful violations of the BSA—those remain subject to heavy fines and potential jail time.

Moving forward, without Congressional intervention, the penalty landscape will look very different. The maximum penalty for a non-willful violation is now, after *Bittner*, \$10,000 per form.

What is not clear is what this means for taxpayers who have paid civil fines for non-willful violations on a per account basis in the past. The ruling also raises the question of whether the IRS will be more aggressive in characterizing violations as willful now that the differences in penalty calculations will be more significant.

We will continue to monitor how the IRS reacts to the ruling and will provide further updates.

You can read the opinion here.

If you have questions or would like additional information, please contact Kelly Phillips Erb (erbk@whiteandwilliams.com; 212.864.7186).

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