ALM | LAW.COM

New York Law Journal

US Supreme Court Gives Taxpayers an FBAR Win

By Jeremy H. Temkin
March 16, 2023

For over a decade, the Internal Revenue Service and the U.S. Department of Justice have devoted substantial resources to cracking down on taxpayers who fail to disclose their offshore accounts on Reports of Foreign Bank and Financial Accounts (FBARs). Taxpayers who willfully fail to comply with their FBAR reporting obligations are exposed to imprisonment and other criminal sanctions or, if they are fortunate enough to avoid prosecution, a civil penalty equal to 50% of the highest balance of their undisclosed accounts. On the other hand, taxpayers whose failure to report their offshore accounts is "due to negligence, inadvertence, or mistake or … a good faith misunderstanding of the" legal requirements are subject to "nonwillful" penalties of $10,000 per violation. The circuits have, however, split over whether taxpayers are subject to a $10,000 penalty for each unreported account or a single $10,000 penalty per year.

Last year, the U.S. Supreme Court agreed to resolve a split between the U.S. Court of Appeals for the Fifth Circuit, which agreed with the government that the $10,000 penalty applies on a "per-account" basis, and the Ninth Circuit, which adopted the taxpayer-friendly "per-form" approach. See Jeremy H. Temkin, "**Penalties Go to the Supreme Court: Dueling Statutory Interpretations**," N.Y.L.J. (July 20, 2022). On Feb. 28, the court issued a 5-4 decision in *Bittner v. United States*, No. 21-1195, 143 S. Ct. 713, that cut across ideological lines and, in a victory for taxpayers, limited the IRS to a single $10,000 penalty regardless of how many accounts should have been reported in a given year.

Jeremy Temkin

Background

The FBAR reporting requirement derives from the Bank Secrecy Act of 1970 (BSA), which recognized that "certain reports … are highly useful" in a wide range of matters including "criminal, tax, or regulatory investigations." 31 U.S.C. Section 5311. The BSA directs the Secretary of the Treasury to require taxpayers to file reports when they "maintain a relation" with a "foreign financial agency." 31 U.S.C. Section 5314(a). The Secretary exercised this statutory authority by, among other things, requiring that "each United States person having a financial interest in, or signature or other authority over, a bank, securities, or other financial account in a foreign country" file an FBAR for "each year in which such relationship exists." 31 C.F.R. Section 1010.350(a). By statute, an individual who fails to file timely and accurate FBARs is subject to a civil penalty of up to $10,000, unless that violation is the result of willful conduct (in which case the maximum penalty rises to the greater of $100,000 or 50% of the value of the account) or is due to reasonable cause (in which case no penalty will be imposed). 31 U.S.C. Section 5321(a)(5).

In *United States v. Boyd*, 991 F.3d 1077 (9th Cir. 2021), the taxpayer failed to file a timely FBAR for 13 accounts that she held in the United Kingdom. The Ninth Circuit held that the BSA authorized one $10,000 penalty per untimely FBAR, regardless of the number of accounts that should have been reported on the form. The Fifth

JEREMY H. TEMKIN *is a principal in Morvillo Abramowitz Grand Iason & Anello.* EMILY SMIT, *an associate of the firm, assisted in the preparation of this article.*

Circuit rejected this approach in the case of Alexandru Bittner, who failed to timely disclose 272 foreign accounts between 2007 and 2011. Concluding that the maximum $10,000 penalty applied on a per-account basis, the Court of Appeals upheld a $2.72 million penalty. See *United States v. Bittner*, 19 F.4th 734 (5th Cir. 2021). In granting certiorari in *Bittner*, the Supreme Court agreed to resolve the question of what constitutes a violation of the FBAR reporting requirement giving rise to the $10,000 nonwillful penalty.

Briefs and Arguments

In the Supreme Court, Alexandru Bittner argued that the BSA instructs the Secretary to require parties to "file reports," and that, "under every ordinary interpretive metric," the statute is violated by the failure to file an annual report. Petitioner's Brief at 17. According to Bittner, "nothing in Section 5314 imposes an independent duty to report each account." Rather, "the existence of an account … is merely the triggering condition that activates the reporting requirement." At oral argument, Justice Sonia Sotomayor challenged this reading of the statute as equating the required "report" with a form as opposed to a requirement that individuals disclose their qualifying foreign financial relationships (i.e., accounts). See Transcript of Oral Argument, *Bittner v. U.S.*, No. 21-1195 (Nov. 2, 2022) ("Tr.") at 34-35. Bittner pushed back on this reading of the text, reiterating his view that the only statutory duty is to file reports required by the Secretary, and the reference to accounts describes the conduct that triggers the obligation to file reports.

Bittner also argued that the overall structure of Section 5321(a)(5) supported his per-form approach. Specifically, Bittner noted that both Section 5321(a)(5)(B)(ii)(II)—which creates a reasonable cause exception to the imposition of penalties for nonwillful violations—and Section 5321(a)(5)(D)(ii)—which imposes heightened penalties for willful violations—contain language focusing on specific accounts. In Bittner's view, given that specificity, "Congress would not have vaguely referenced Section 5314 [to define what constitutes a violation] if it truly intended a draconian scheme where parties accidentally commit dozens of violations for failing to file a single form." Petitioner's Brief at 26.

By contrast, relying on the principal that the same phrase is presumed to have been used consistently throughout a given provision, the government argued that the unspecified "violation" referenced in Section 5321(a)(5)(A) must be interpreted in light of the "account-specific" use of the term "violation" in the reasonable cause and willful penalty provisions. Respondent's Brief at 20-26. The government further supported its argument that Congress must have intended that each failure to report an account is a separate violation by contending that Section 5314 defines the subject matter of the required reports in account specific terms.

At argument, the justices explored this divergence of views regarding the significance of the use of the word account in other portions of Section 5321(a)(5). Thus, Justice Elena Kagan pressed Bittner to address the government's argument that the neighboring provisions demonstrate "exactly what Congress was thinking of," Tr. at 11-13, while Justice Neil Gorsuch challenged the government's reading, noting that "the one place where you need it you don't seem to have it."

Majority Opinion

Almost four months after the argument, the court issued a 5-4 decision in which Justice Gorsuch—writing for himself, Chief Justice John Roberts and Justices Samuel Alito, Brett Kavanaugh, and Kentanji Brown Jackson—agreed with Bittner's view that the statute is violated on a per-form basis, while Justice Amy Coney Barrett's dissent—which was joined by justices Clarence Thomas, Sotomayor and Kagan—sided with the IRS's per-account interpretation reading of the BSA and its implementing regulations.

The majority opinion first addressed the interplay between Sections 5314 and 5321, noting that the former "delineates an individual's legal duties under the BSA," while the latter "outlines the penalties that follow for failing to discharge those duties." *Bittner,* 143 S. Ct. at 719. Focusing on a point that Justices Thomas and Jackson had raised at oral argument, see Tr. at 13-14, 48-51, Justice Gorsuch stressed that "Section 5314 does not speak of accounts or their number. The word 'account' does not even appear. Instead, the relevant legal duty is the duty to file reports." *Bittner,* 143 S. Ct. at 719. Agreeing with Bittner's "triggering condition" approach, the majority concluded that "[t]he statutory obligation is binary. Either one files a report 'in the way and to the extent the Secretary prescribes,' or one does not." According to Justice Gorsuch, Section 5321(a)(5) does not speak of accounts, but "pegs the quantity" of penalties to the "quantity of 'violation[s].'" Id. at 720. Relying on the canon expressio unius est exclu-

sio alterius, the majority adopted Bittner's view that Congress's use of the word "account" in defining the reasonable cause exception and fixing the penalty for willful violations weighs in favor of a per-form penalty for nonwillful violations.

Pursuing a point that Justice Alito had raised at argument regarding the IRS's lack of consistent messaging, see Tr. 65-66, the majority also pointed to several documents issued by the government that "seemed to tell the public that the failure to file a report represents a single violation exposing a [nonwillful] violator to one $10,000 penalty." *Bittner,* 143 S. Ct. at 722; see also Brief for American College of Tax Counsel as Amicus Curiae at 17-24.

Besides the concern with administrative guidance, the majority also took issue with anomalies that would result from adopting the government's view. Picking up on a concern raised at argument by Justice Jackson, see Tr. 48-50, the court noted that, under the government's view, a taxpayer who fails to report a single $10 million account is subject to a single $10,000 nonwillful penalty, while another taxpayer who failed to report a dozen accounts with an aggregate balance of $10,001 would be subject to $120,000 in nonwillful penalties. *Bittner,* 143 S. Ct. at 723.

Finally, in a portion of his opinion joined only by Justice Jackson, Justice Gorsuch invoked the rule of lenity, which provides that "statutes imposing penalties are to be 'construed strictly' against the government and in favor of individuals." Id. at 724 (citing *Commissioner v. Acker,* 361 U.S. 87, 91 (1959)). Justice Gorsuch rejected the government's attempt to distinguish *Acker* on the grounds that it "involved a penalty provision in the Internal Revenue Code, … while this case involves a penalty provision in the BSA," finding that that "[t]he rule of lenity is not shackled to the Internal Revenue Code or any other chapter of federal statutory law." Rather, Justice Gorsuch concluded that the principle was especially applicable both because it exists to protect a defendant's due process rights and because the question of what constitutes a "violation" of the BSA has implications in criminal as well as civil cases.

Dissenting Opinion

In her dissent, Justice Barrett argued that because the subject matter of the required reports is a foreign bank account and these accounts are what trigger the filing requirement, each failure to report an account must be a violation of the reporting requirement. (Barrett, J., dissenting). According to Justice Barrett, this interpretation is further underscored by the enumerated list of account-specific information the reports must contain. The dissenters also adopted the government's statutory construction that, given the "account-specific connotations" of a "violation" of Section 5314 in the reasonable cause and willful penalty provisions, the identical word used in the provision for nonwillful violations must have the same meaning.

Justice Barrett's dissent also rejected Bittner's argument that the reference to accounts in Section 5314 merely describes the conduct that triggers the obligation to file reports. Instead, focusing on the implementing regulations, the dissent concluded that the distinction between the form used to report accounts and the reports themselves underscores that FBARs are not the "reports" required by Section 5314, but rather the procedural mechanism used to implement the duty to report each foreign account.

Finally, Justice Barrett also dismissed the majority's application of the expressio unius canon, noting that "[b]ecause the penalty amount [for a nonwillful violation] does not depend on the balance in an account, Congress had no reason to use account-specific language."

Conclusion

As *Bittner* demonstrates, parties can often disagree as to the "plain meaning" of a statutory text. When that happens, the "textualists" on the court are called upon to resolve competing readings of a statute, which can result in a unique alignment of the justices. Last term, Justices Thomas, Sotomayor, Kagan and Barrett did not join in dissenting in a single 5-4 decision. See The Supreme Court-The Statistics, 135 Harv. L. Rev. 491, 497 (2021), available at **//harvardlawreview.org/wp-content/uploads/2021/11/135-Harv.-L.-Rev.-491.pdf.** Thus, in addition to handing taxpayers a victory by limiting their exposure to civil penalties for nonwillful failures to disclose foreign accounts, *Bittner* demonstrates that the "plain meaning" of a statutory text is often far from "plain" and that the line-up of justices in a given case can be unpredictable.