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Legal Sidebar

Supreme Court To Address Foreign Account Reporting Penalties

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Federal law requires U.S. persons with a financial interest in or signature or other authority over foreign financial accounts totaling more than $10,000 to report these accounts by filing a Report of Foreign Bank and Financial Accounts, commonly known as an FBAR, each year. The IRS may levy civil penalties of up to $10,000 for each non-willful violation. Two U.S. Courts of Appeals recently adopted conflicting interpretations of whether this maximum penalty applies to each unreported account or to each unfiled annual FBAR form. In one case, more than $2 million in penalties may hinge on that interpretive question. At the request of both the defendant in that case and the U.S. Solicitor General, the U.S. Supreme Court agreed to review the case and resolve the conflict during its October 2022 term. This Legal Sidebar discusses the relevant penalty provisions and the interpretive approaches of the divergent court rulings.

Reporting Requirements

Congress enacted the Bank Secrecy Act (BSA) in part to address the serious and widespread use of foreign financial institutions to evade domestic criminal, tax, and regulatory requirements. The BSA requires U.S. citizens, residents, and entities to report—independent of any tax obligations—certain foreign financial transactions, relationships, and accounts. One provision of the BSA, 31 U.S.C. § 5314, establishes the reporting requirements, empowering the Secretary of the Treasury to adopt implementing regulations.

In 1986, Congress amended the BSA and gave the Secretary of the Treasury authority to impose civil penalties for willful violations of Section 5314. For violations "involving a failure to report the existence of an account" or related information, the Secretary could impose a penalty no greater than "an amount (not to exceed $100,000) equal to the balance in the account at the time of violation; or $25,000."

In the American Jobs Creation Act of 2004, Congress expanded the available penalties, allowing the Secretary to impose penalties for both willful and non-willful violations. The civil penalties section as amended (31 U.S.C. § 5321(a)(5)) provides that the Secretary may impose a penalty "on any person who violates, or causes any violation of section 5314." For non-willful violations, "the amount of any civil penalty imposed . . . shall not exceed $10,000." (In practice, this value is adjusted for inflation, but the court rulings discussed below use the original statutory values in discussing the interpretive question.) If any violation is due to reasonable cause and "the amount of the transaction or balance in the account at the time of the transaction was properly reported," no penalty shall be imposed.

For willful violations, the maximum penalty is "the greater of $100,000 or 50 percent of the amount determined under subparagraph (D)." Subparagraph (D) provides that, "in the case of a violation involving a failure to report the existence of an account" or related information, the relevant amount is the balance in the account at the time of violation. The maximum penalty for a willful violation is thus the greater of $100,000 or 50% of the balance of the account at the time of violation. The reasonable cause exception does not apply to willful violations. The IRS must assess any penalty, willful or non-willful, within six years of the violation.

The IRS currently interprets the $10,000 maximum penalty for non-willful violations and the $100,000 element of the maximum penalty for willful violations as applying on a per-account basis, to each unreported or improperly reported foreign account. Several defendants accused of non-willful violations have challenged the IRS's position, arguing that the maximum penalty for non-willful violations applies on a per-form basis, so that the maximum penalty for non-willfully failing to file an FBAR in any particular year is $10,000, regardless of the number of foreign accounts the regulations required the defendant to report.

United States v. Boyd

In *United States v. Boyd*, a divided panel of the U.S. Court of Appeals for the Ninth Circuit adopted the per-form interpretation. Defendant Jane Boyd filed an otherwise-accurate FBAR for the year 2010 more than a year late. The IRS determined that Boyd committed thirteen non-willful FBAR violations, one for each of thirteen accounts she did not report when required. It assessed a penalty of $47,279. Boyd argued that she committed only a single violation by failing to file the 2010 FBAR on time, so the maximum statutory penalty was $10,000. The district court ruled for the IRS.

The Ninth Circuit majority, however, agreed with Boyd. It stated that the general provisions of Section 5314 can only be violated by violating the implementing regulations, quoting an observation from the Supreme Court's 1974 decision in *California Bankers Association v. Schultz*, in which the Court rejected a constitutional challenge to the BSA. The Ninth Circuit noted that one regulation requires that foreign accounts be reported on the FBAR and another that the FBAR be filed by a deadline. The court held that Boyd's accurate but tardy FBAR only violated this second regulation, so she committed only a single non-willful violation.

The government argued that the phrasing of references to violations and accounts in the civil penalties statutory section, including the reasonable cause exception and the willful penalty provision, demonstrated congressional intent to impose maximum penalties on a per-account basis. Those provisions, according to the government, showed that Congress understood violations of Section 5314 in terms of the failure to report a particular account. The court rejected this approach and interpreted the absence of any similar reference to accounts in the non-willful penalty provision as an intentional omission by Congress, indicating that the maximum penalty there was not tied to accounts.

Judge Ikuta dissented and would have adopted the per-account interpretation. She argued that the term *violation* should be read consistently throughout the civil penalties section, rejecting the majority's intentional omission argument. Judge Ikuta also disagreed with the majority's interpretation of the applicable regulations, contending that the duty to file an FBAR does not subsume the duty to report individual accounts.

United States v. Bittner

Months later, in *United States v. Bittner*, the U.S. Court of Appeals for the Fifth Circuit declined to follow *Boyd* and instead adopted the per-account interpretation. Alexandru Bittner was born in Romania and became a naturalized citizen of the United States in 1987. From 1990 to 2011, he returned to Romania and became a successful businessman with numerous financial accounts in several European countries. Bittner learned of his FBAR obligations on his return to the United States and filed forms at that time. The IRS assessed $2.72 million in penalties for 272 non-willful violations, based on his failure to report between 51 and 61 accounts in each of the five years for which penalties could still be levied. The district court ruled for Bittner and held that the maximum penalty applied on a per-form basis, so the maximum penalty was $50,000.

The Fifth Circuit reversed on this point. That court rejected both the district court's and the *Boyd* majority's reliance on *Schultz*, noting the differences in subject matter and the intervening statutory amendments. The Fifth Circuit also focused on the statutory language rather than the Treasury regulations, noting that, while Congress specifically referred to violations of regulations elsewhere in the civil penalties section, it did not do so in the account-reporting penalty provisions.

The Fifth Circuit, citing Judge Ikuta's dissent in *Boyd*, held that Section 5314 imposes both a substantive obligation to report every covered account and a procedural obligation to file the appropriate reporting form. The maximum penalties provision, the court determined, is most naturally read as referring to violations of these duties rather than the particular requirements of the implementing regulations. Otherwise, the court explained, the Secretary could expand the scope of potential penalties by adopting more complex reporting requirements.

The court also relied on the principle that the use of the term *violation* throughout the civil penalties section should be read consistently. The court thus held that because *violations* are textually linked to *accounts* in both the willful penalty provisions and the reasonable cause provision, the use of *violation* in the non-willful maximum penalty should be read similarly, compelling the per-account interpretation.

The interpretive split between the Fifth Circuit and Ninth Circuit is also reflected in decisions of U.S. district courts outside those circuits. District courts in New Jersey and Connecticut have adopted the per-form view, while two district courts in Florida have adopted the per-account approach.

Supreme Court Review and Considerations for Congress

Bittner filed a petition for a writ of certiorari with the Supreme Court. The Chamber of Commerce of the United States, the American College of Tax Counsel, and the Center for Taxpayer Rights filed amicus briefs in support of Bittner's petition. Together, these filings emphasize the distinct circuit split, potential discouragement of voluntary compliance, the settlement pressure imposed by large potential penalties, alleged conflicts between the IRS's current position and previous IRS publications, and the alleged arbitrariness of leveraging penalties based on the number of foreign accounts disconnected from the amount of funds within those accounts. In response, the Solicitor General also urged the Court to accept the case, arguing that the circuit split should be resolved in favor of the per-account interpretation.

On June 21, 2022, the Supreme Court granted Bittner's petition. While the Court is expected to hear the case in the October 2022 term, Congress could intervene in the interpretative dispute by amending the BSA provisions at issue to clearly adopt a per-form or a per-account maximum penalty. No such bill has been proposed. The proposed Stop Tax Havens Abuse Act, introduced in the House and Senate, includes an unrelated alteration that would affect the calculation of account balances when used to determine maximum penalties for willful violations.

Author Information

Alexander H. Pepper
Legislative Attorney

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