Supreme Court’s FBAR Ruling Skips Crucial Legal Question for Now (1)

The majority and dissenting opinions in Bittner v. United States relied on traditional canons of statutory construction to reach opposite conclusions, but it left a key issue unanswered—the appropriate standard as to mens rea, say Holland & Knight LLP's James P. Dawson, Chad M. Vanderhoef, and Alexander R. Olama.

The US Supreme Court on Feb. 28 ruled that the Bank Secrecy Act's maximum $10,000 penalty for non-willfully failing to file a Report of Foreign Bank and Financial Accounts, known as FBAR, applies on a per-report—and not a per-account—basis. The court then remanded the case for further proceedings consistent with its opinion.

The questions answered by the decision in Bittner v. United States—and the questions left unanswered—will impact FBAR controversies going forward.

More Willful Penalty Cases

The court's 5–4 decision, which reversed the US Court of Appeals for the Fifth Circuit, seems straightforward and might make one wonder how this could impact future FBAR controversies.

As a result of this one opinion in Bittner, the US went from potentially collecting $2.72 million to $50,000. If this result is extrapolated to consider the full extent of lost revenue among hundreds, or even thousands, of current and future cases, is the government really going to be content with $10,000 per year per person? It's not unreasonable to conclude taxpayers and practitioners are likely to see significantly more willfulness cases.

Furthermore, it's reasonable to expect the government to pursue more aggressive arguments regarding account control and authority to maximize the number of persons subject to the reporting requirements. Examples of these additional individuals include those with signatory authority, those holding a power of attorney, and identified beneficiaries. Accordingly, the willfulness standard takes on elevated importance.

Blurry Line Between Willful and Nonwillful

In the first footnote of the majority opinion, the court sidestepped a question about criminal intent that could impact all FBAR controversies: "What, if any, mens rea the government must prove to impose a 'nonwillful' penalty is not before us."

The high court offered no opinion as to whether a subjective or objective standard is appropriate to establish willfulness. Unfortunately, the standard for willfulness has been diluted to the point where it operates as a de facto strict liability penalty. Although willfulness is a question of fact, several courts have disposed of this issue on summary judgment simply because of a defective schedule B attached to an individual's income tax return.
The IRS hasn't yet explained what it views as the line between willful and nonwillful conduct for FBAR purposes. The Internal Revenue Manual is silent as to the distinction; so is the case law. If the IRS continues to argue for strict liability, then until the definition of willfulness is clarified, the distinction between nonwillful and willful will be eviscerated.

As one district court put it: “Imputing constructive knowledge of filing requirements to a taxpayer simply by virtue of having signed a tax return would render the distinction between a non-willful and willful violation in the FBAR context meaningless. Because taxpayers are required to sign their tax returns, a violation of the FBAR filing requirements could never be non-willful. Yet, the statute provides for non-willful penalties. Applying the USA's suggested reasoning would lead to a draconian result and one that would preclude a consideration of other evidence presented.”

*Bedrosian Case*

Taxpayers and their counsel may not need to wait long for the court to address the unanswered Footnote 1 question because the taxpayer in *Bedrosian v. United States*, another FBAR case, has petitioned the court to take up this exact issue of the willfulness standard.

Should the justices decide to consider the arguments raised in *Bedrosian*, mens rea will be front and center. *Bedrosian* urges the justices to accept its petition and find that willfulness should be determined according to a subjective standard instead of the objective standard used by several courts. Many FBAR litigants have, to no avail, argued that willfulness should be analyzed under the *Cheek* standard, which is a voluntary, intentional violation of a known legal duty.

A brief from the Center for Taxpayer Rights supporting *Bedrosian* includes a complete discussion of mens rea and the lowering of the bar of the willfulness standard.

The Supreme Court in *Bittner* noted that the government’s prior guidance with its litigating position was inconsistent. Although the administrative guidance wasn't controlling, it did impact the persuasiveness of the government's interpretation of the statute. Could the same occur in *Bedrosian* with respect to the IRS' prior interpretation of willfulness?

The IRS issued guidance in 2006 in the form of chief counsel advice declaring that the definition of willfulness is the same for Section 5321 (civil penalty) and Section 5322 (criminal penalty). This IRS proclamation led most practitioners to assert that willfulness was determined on a subjective standard, since there is no question that the *Cheek* standard is used for Section 5322 violations. Further, the IRS in other guidance explained that the civil fraud burden of proof (clear and convincing evidence) was necessary to establish willfulness. The IRS has deviated significantly from these positions throughout the evolution of FBAR litigation.

It remains to be seen whether the high court will view the US’ inconsistencies in the same manner as it did in *Bittner*. Regardless, if the court grants certiorari to Bedrosian, the result will be felt in most, if not every, FBAR penalty assertion.

**Conclusion**

The majority and dissenting opinions in *Bittner* relied on traditional canons of statutory construction to reach opposite conclusions. But the *Bittner* decision left a key issue unanswered—the appropriate standard as to mens rea. Hopefully, the majority's decision to expressly include Footnote 1 foreshadows the court granting certiorari to Bedrosian in order to address that standard.
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We'd love to hear your smart, original take: Write for us.

(Clarifies the penalty for nonwillful failure to file FBAR in the first paragraph.)

Documents

Bittner v. United States

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