Recent Developments in FBAR Jurisprudence

By Usman Mohammad and Michael Gelb

Failing to report foreign bank accounts on a Report of Foreign Bank and Financial Accounts (FBAR) form can carry severe financial consequences. The civil penalty for non-willful violations of the FBAR reporting requirement is $10,000. The civil penalty for willful violations of the FBAR reporting requirement is the greater of $100,000 or 50% of the account balance. In order to properly advise taxpayers regarding those consequences, tax professionals should be aware of recent court developments regarding FBAR penalties.

Recent Developments Regarding Non-Willful FBAR Penalties

Tax professionals should be aware that even non-willful violations of the FBAR reporting requirement may result in substantial penalties if the taxpayer has multiple foreign accounts and resides in a jurisdiction that applies the non-willful penalty on a per-account basis.

The federal courts are currently split on the issue of whether the non-willful FBAR penalty applies to each unfiled FBAR form or to each unreported foreign account. This distinction is significant—if the penalty applies on a per form basis, then the penalty is capped at $10,000 per year, because only one FBAR form is required to be filed each year, no matter the number of foreign accounts to be reported. If, however, the penalty applies on a per account basis, then a taxpayer with multiple accounts can be liable for multiple $10,000 non-willful FBAR penalties in a single year.

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In 2021, the Ninth Circuit held that the non-willful FBAR penalty applies on a per form basis *[United States v. Boyd,* 991 F3d 1077 (9th Cir. 2021)]. Federal district courts located within the Second and Third Circuits have held the same *[United States v. Giraldi,* 2021 WL 1016215 (D.N.J. Mar. 16, 2021); *United States v. Kaufman,* 2021 WL 83478 (D. Conn. Jan. 11, 2021)]. The Fourth Circuit has suggested the same in dicta *[United States v. Horowitz,* 978 F.3d 80, 81 (4th Cir. 2020)].

In late 2021, however, the Fifth Circuit disagreed with the decision in Boyd *[United States v. Bittner,* 2021 WL 5570729 (5th Cir. Nov. 30, 2021)] and held that the non-willful FBAR penalty applies to each unreported foreign account. Federal district courts located in the Eleventh Circuit have held the same [e.g., *United States v Solomon,* 2021 WL 5001911 (S.D. Fla. Oct. 27, 2021)].

Recent Developments Regarding Willful FBAR Penalties

Tax professionals should also be aware that many federal courts have held that a taxpayer's Form 1040 tax return is a significant factor in determining whether the taxpayer's failure to report their foreign accounts on an FBAR was willful.

The current version of Form 1040, Schedule B, which is used to report interest and dividends, includes a question in Part III asking if the taxpayer has an interest in any foreign bank account. Part III then states the following if the taxpayer answered "yes" to having a foreign account:

> If 'Yes,' are you required to file FinCEN Form 114, Report

of Foreign Bank and Financial Accounts (FBAR), to report that financial interest or signature authority? See FinCEN Form 114 and its instructions for filing requirements and exceptions to those requirements.

Because of the language in Schedule B, a majority of courts now holds that a signed Form 1040 tax return with a Schedule B will be treated as creating constructive knowledge of the FBAR filing obligation, even if the taxpayer alleges that they did not read their tax return. Constructive knowledge of the FBAR filing obligation is significant, because a willful FBAR violation can be established by showing knowledge of the FBAR filing obligation, coupled with either a knowing, reckless, or willfully blind failure to comply with the obligation.

There are, however, a few recent court decisions that are more favorable to taxpayers with respect to the impact of Schedule B in willful FBAR cases. Several courts have held that signing a tax return with a Schedule B does not put a taxpayer on constructive notice of the FBAR filing obligation [e.g., *United States v. Schwarzbaum,* 2020 WL 1316232 (S.D. Fla. Mar. 20, 2020); *United States v. Flume,* 2018 WL 4378161 (S.D. Tex. Aug. 22, 2018)]. Moreover, even among the courts that agree that Schedule B creates constructive notice of the FBAR filing obligation, some of those courts nonetheless hold that merely signing a tax return with an incorrect Schedule B does not automatically make an FBAR violation willful, as that would change the willfulness standard to strict liability. Thus, according to these courts, the government must show something more in addition to a tax return with an incorrect Schedule B in order to show a willful FBAR violation [e.g., *Jones v. United States,* 2020 WL 4390390 (C.D. Cal. May 11, 2020); cf. *United States v. De Forrest,* 463 F. Supp. 3d 1150, 1158 (D. Nev. May 31, 2020)].

Unfortunately, other courts have magnified the impact of Schedule B in willful FBAR cases. In *United States v. Gentges* [531 F. Supp. 3d 731, 750 (S.D.N.Y. 2021)], the court upheld willful FBAR penalties and rationalized that when a taxpayer signs a Form 1040 tax return with an incorrect Schedule B, it constitutes "per se evidence of reckless disregard toward the FBAR obligation." Moreover, in *Norman v. United States* [942 F.3d 1111, 1115 (Fed. Cir. 2019)], the court suggested that because of the constructive notice of the FBAR obligation created by Schedule B, and because willfulness for purposes of the civil FBAR penalty includes recklessness, the only circumstance in which a taxpayer's failure to file an FBAR could be non-willful is if the taxpayer did not know, and had no reason to know, about the existence of his foreign bank account.

But not every tax return will include a Schedule B, which should minimize the impact of the tax return in an FBAR penalty case. In *United States v. Hughes* [2021 WL 4768683 (N.D. Cal. Oct. 13, 2021)], the court recognized that a taxpayer cannot have constructive knowledge of the FBAR filing obligation when she signs a tax return that does not include a Schedule B, because it is the foreign account questions in Schedule B that triggers inquiry notice of the FBAR obligation.

These cases demonstrate that the landscape for FBAR penalties is still evolving, and that the federal courts remain split on a number of FBAR-related issues. In order to properly advise taxpayers, tax professionals should stay abreast of FBAR rulings in the jurisdictions in which their clients reside. ■

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