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BLOG

FinCEN Amends Willful FBAR Regulations

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On December 23, 2021, the United States ("U.S.") Department of the Treasury's Financial Crimes Enforcement Network ("FinCEN") announced amendments to the Bank Secrecy Act ("BSA") penalty regulations to remove certain civil penalty language (previously, 31 C.F.R. § 1010.820(g)), despite FinCEN's previous failure to modify the regulations after the enactment of the American Jobs Creation Act of 2004 ("American Jobs Creation Act"), Pub. L. No. 108-357, § 821, 118 Stat. 1418 (2004).

The changes made pursuant to FinCEN's announcement accordingly rescind section 1010.820(g) and cause paragraphs (h) and (i) in section 1010.820 to be redesignated as paragraphs (g) and (h), **effective as of December 23, 2021**.

Background

The BSA requires financial institutions to program recordkeeping and reporting requirements aimed at tackling money laundering, terrorist financing, and other tax or financial crimes. Regulations implementing the BSA have set forth filing requirements for a Foreign Bank Account Report ("FBAR"), which generally require each U.S. person having a financial interest in, or signature or other authority over, a bank, securities, or other financial account in a foreign country to report such relationship for each year in which such relationship exists. Persons who fail to file an FBAR (or who file an incomplete or incorrect FBAR) may be subject to a civil monetary penalty, the amount of which depends on the willful or non-willful nature of the violation.

Conflicting Statutory and Regulatory Sections

Section 5321 has historically contained civil monetary penalties for BSA violations. In October 1986, Congress amended the provision to add section 5321(a)(5), authorizing a civil monetary penalty for willful violations of 31 U.S.C. § 5314. Specifically, section 5321(a)(5)(B) gave the Secretary of the Treasury ("Secretary") the discretion to impose civil penalties for willful FBAR violations to the greater of (i) the amount of the transaction or an amount equal to the balance in the account at the time of the violation (but not to exceed $100,000) or (ii) $25,000. These penalty limitations were incorporated into the regulations at 31 C.F.R. § 1010.820(g).

The American Jobs Creation Act, however, amended section 5321(a)(5), revising the manner in which the penalty is calculated and increasing the maximum amount that could be assessed for willful violations of section 5314.

Specifically, newly added section 5321(a)(5)(C) provided that the maximum penalty for willful FBAR violations "shall be increased to the greater of $100,000 or 50 percent" of the amount of the transaction or the balance in the account at the time of the violation. Although Congress amended section 5321(a)(5) by increasing the potential penalties for willful FBAR violations, the Secretary made no such corresponding regulatory changes to section 1010.820(g). These conflicting statutory and regulatory sections created controversy between the Internal Revenue Service and taxpayers over which section to follow, especially when substantial penalties were at issue.

Courts' Historical Approach to Addressing the Conflicting Statutory and Regulatory Sections

Several courts have addressed the conflicting statutory and regulatory sections, with varying results. For example, in *United States v. Colliot*, Case No. AU-16-cv-01281-SS, 2018 U.S. Dist. LEXIS 83159, at *5-6 (W.D. Tex. May 16, 2018), the Court found that, notwithstanding the American Jobs Creation Act, section 5321(a)(5) set a "ceiling for penalties assessable for willful FBAR violations, but it [did] not set a floor." The Court reasoned that section 5321(a)(5) instead merely vested the Secretary "with discretion to determine the amount of the penalty to be assessed so long as that penalty [did] not exceed the ceiling set by" section 5321(a)(5)(C). *Id.* at *7. Accordingly, the Court in *Colliot* stated that section 1010.820 operates only to cabin the Secretary's discretion by capping penalties at $100,000 and, thus, is not inconsistent with the Secretary's discretion under section 5321(a)(5) "to determine the amount of penalties to be assessed." *Id.*

In *United States v. Wadhan*, 325 F. Supp. 3d 1136 (D. Colo. 2018), the Court similarly reasoned that both provisions could be interpreted such that they do not conflict. *Id.* at 1139. The Court also highlighted that the "Secretary made regular adjustments to another regulation, 31 C.F.R. § 1010.821, that adjusted penalties to account for inflation." *Id.* at 1140. The Court emphasized that, despite these regular adjustments, the Secretary declined to adjust section 1010.820(g), suggesting that the Secretary "was aware of the penalties available under 31 U.S.C. § 5321(a)(5)(C) and elected to continue to limit the [Secretary's] authority to impose penalties to $100,000 as specified in 31 C.F.R. § 1010.820." *Id.*

By contrast, many courts have ruled that section 5321(a)(5)(C), as amended by the American Jobs Creation Act, conflicted with section 1010.820(g), thus invalidating section 1010.820(g). *See, e.g.*, *Kimble v. United States*, 141 Fed. Cl. 373 (2018); *Norman v. United States*, 942 F.3d 1111 (Fed. Cir. 2019), *aff'g* 138 Fed. Cl. 189 (2018); *United States v. Horowitz*, 361 F. Supp. 3d 511 (D. Md. 2019), *aff'd*, 978 F.3d 80 (4th Cir. 2020); *United States v. Garrity*, No. 3:15-CV-243(MPS), 2019 U.S. Dist. LEXIS 32404, 2019 WL 1004584 (D. Conn. Feb. 28, 2019); *United States v. Jung Joo Park*, 389 F. Supp. 3d 561 (N.D. Ill. 2019); *United States v. Schoenfeld*, 396 F. Supp. 3d 1064 (M.D. Fla. 2019); *United States v. Rum*, Case No. 8:17-cv-826-T-35AEP, 2019 U.S. Dist. LEXIS 180339, 2019 WL 5188325 (M.D. Fla. Sept. 26, 2019), *aff'd*, 995 F.3d 882 (11th Cir. 2021).

While most of the above-referenced cases simply reiterated the argument initially raised in *Kimble*, the decision in *United States v. Kahn*, 5 F.4th 167 (2d Cir. 2021), *aff'g* Case No. 17-cv-7258, 2019 U.S. Dist. LEXIS 230491, 2019 WL 8587295 (E.D.N.Y. Sept. 23, 2019), was a split panel decision. The majority reasoned that, while section 1010.820(g) mirrored the language of section 5321(a)(5) prior to 2004 because it gave the Secretary the discretion to determine the amount of a penalty insofar as the penalty did not exceed $100,000, the two provisions were no longer "harmonious" after the American Jobs Creation Act because of section 5321(a)(5)(C)'s new mandate that the maximum penalty for a willful FBAR violation "shall be increased" to $100,000 or 50% of the balance of the account at the time of violation. *Id.* at 174; *see id.* ("The word 'shall,' in a statute, indicates a command; what follows the word 'shall' is 'mandatory, not precatory.'") (quoting *Mach Mining, LLC v. EEOC*, 575 U.S. 480, 486 (2015)); *Norman*, 942 F.3d at 1118 ("It is well-settled that subsequently enacted or amended statutes supersede prior inconsistent regulations."). The majority concluded that the American Jobs Creation Act "plainly amended" section 5321(a)(5), *Kahn*, 5 F.4th at 174, thereby rendering any adherence to section 1010.820(g) in contravention of "both the language of . . . and the 'manifest congressional design' embodied in" the statute, *id.* at 175.

However, the dissent strongly disagreed, stating that section 5321(a)(5) "nowhere mandates that the Secretary impose a higher fine" and, in fact, section 5321(a)(5)(A) "gives the Secretary discretion to impose no fine at all." *Id.* at 177 (Menashi, J., dissenting). The dissent further stated that, while section 5321(a)(5) "*allows* the Secretary to impose a penalty in excess of the $100,000 regulatory cap," the statute does not "*require* that the Secretary subject violators to an increased penalty." *Id.* at 179 (emphases in original). When the statute is read in context, the dissent

continued, “the language that the maximum penalty ‘shall be increased’ does not mandate that the Secretary take or refrain from taking any action with respect to a violator’s exposure to a penalty” but, rather, merely increases the maximum penalty limit that the Secretary can impose at his discretion for a willful FBAR violation. *Id.* at 181. Moreover, the dissent cited *United States ex rel. Accardi v. Shaughnessy*, 347 U.S. 260 (1954), for the principle that agency regulations are permitted to limit an agency’s discretion beyond the statutory constraints. *Id.* Thus, the dissent reasoned, section 1010.820(g)’s limitation that a penalty for a willful FBAR violation not exceed $100,000 “represents a due exercise of the Secretary’s [delegated rulemaking] authority that limits her discretion beyond the statutory constraints.” *Id.* at 180.

Given the previous challenges and the dissent in *Kahn*, one could view the December 23, 2021, regulatory announcement as an attempt to buttress the Government’s position that the regulatory limitation should not apply. It will be interesting to see if the regulations continue to be at issue in willful FBAR cases in the future.

Winston & Strawn will continue to monitor any further developments. For further information, please contact the authors or your Winston relationship attorney.

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