

2 Rulings Highlight IRS' Uncertain Civil Fraud Penalty Powers

By **Michael Landman** (September 30, 2025)

The IRS' ability to administratively assess civil fraud penalties continues to be called into question following the U.S. Supreme Court's 2024 decision in *U.S. Securities and Exchange Commission v. Jarkesy*.

On Aug. 21, in *Silver Moss Properties LLC v. Commissioner*, the U.S. Tax Court upheld a post-Jarkesy challenge to a civil fraud penalty asserted by the IRS in response to a refund action that the taxpayer brought in Tax Court.[1]



Michael Landman

On Sept. 19, the U.S. District Court for the Northern District of Texas went the other way in *U.S. v. Sagoo*, holding that the IRS' assessment of a civil fraud penalty violated a taxpayer's Seventh Amendment right to a jury trial.[2]

Though these two cases arose in different contexts and under different statutes, their apparent conflict raises uncertainty regarding the manner in which the IRS can assess civil fraud penalties. This conflict provides opportunities and potential pitfalls for taxpayers facing the possibility of a civil fraud assessment.

Section 6663 of the Internal Revenue Code allows the IRS to assess a 75% fraud penalty on top of any amount of tax owed if it is determined that any portion of an underpayment is attributable to fraud.[3] Similarly, the Bank Secrecy Act authorizes the IRS to assess civil fraud penalties for, among other things, willful failure to report a foreign bank account.[4]

Taxpayers facing such penalties have cited *SEC v. Jarkesy* in support of their argument that any administrative assessment of these penalties violates the Seventh Amendment's right to a jury trial.[5]

SEC v. Jarkesy and Its Impact on IRS Assessment of Civil Fraud Penalties

The Seventh Amendment provides the right to a jury trial for all "suits at common law." [6] In *SEC v. Jarkesy*, the Supreme Court held that the SEC violated an investment adviser's Seventh Amendment right to a jury trial when it imposed a civil fraud penalty via an administrative proceeding before an SEC administrative law judge.[7]

The court noted that the imposition of a civil fraud penalty was based on allegations akin to a common-law fraud claim. The court concluded that a "defendant facing a fraud suit has the right to be tried by a jury of his peers before a neutral adjudicator." [8]

Following *Jarkesy*, a taxpayer brought a challenge to the IRS' claim for a civil fraud penalty in the *Silver Moss* case, arguing that it too violated the Seventh Amendment's right to trial by jury.[9]

In *Silver Moss*, the Tax Court distinguished *Jarkesy* on two grounds.

First, the court noted that the taxpayer had initiated the suit that gave rise to the civil fraud penalty claim and had done so via a procedure — a claim in Tax Court — for which there is no right to a trial by jury.[10]

Implicit in the court's holding is that, had the taxpayer wished for a trial by jury, it could have brought suit in federal district court pursuant to Title 28 of the U.S. Code, Section 1346(e).[11]

Second, the court held that the imposition of a civil fraud penalty for underpayment of taxes relates to the public rights exception to the Seventh Amendment.[12]

In this respect, the court distinguished the claims brought by the SEC against the investment adviser in *Jarkesy*, akin to fraud claims that could be brought by private parties, from a claim against a taxpayer for willful underpayment of taxes, which has no analogous private cause of action.[13]

Undeterred by *Silver Moss*, which was a Tax Court decision, taxpayers in federal court have continued to cite to *Jarkesy* for the proposition that the IRS violates the Seventh Amendment when it imposes a civil monetary penalty without providing for the right to trial by jury.[14]

On Sept. 19, one of those taxpayers was successful.[15] *Sagoo* involved an action brought by the U.S. in the Northern District of Texas. The U.S. sought to reduce to judgment a civil monetary penalty that the IRS had assessed the taxpayer, Sharnjeet K. *Sagoo*.

Sagoo allegedly failed to report her financial interests in certain foreign bank accounts for three years and was assessed penalties — commonly referred to as FBAR penalties — in excess of \$1 million for her willful failure to do so.

Sagoo moved to dismiss, arguing that the IRS' imposition of a civil monetary penalty based on a claim of fraud violated her Seventh Amendment right to a trial by jury.

Contrary to the position it took in *Silver Moss*, the government conceded *Sagoo*'s Seventh Amendment right to have a jury determine whether she was liable for the assessed civil fraud penalties.[16]

According to the court's decision, the government instead argued that *Sagoo*'s Seventh Amendment right to a jury trial was satisfied by the fact that she had "access to a jury trial to determine de novo her liability for the willful FBAR penalties assessed against her." [17]

The court rejected the government's argument, holding that an "after-the-fact jury trial does not protect an individual's Seventh Amendment right." [18] In other words, the IRS' imposition of the assessment violated the Seventh Amendment right, and the constitutional violation could not be cured by subsequent access to a jury trial where the taxpayer could dispute that assessment.

The court in *Sagoo* did not cite *Silver Moss* or otherwise engage in discussion of whether the IRS' imposition of civil monetary penalties falls within the public rights exception articulated in *Silver Moss*. And the court did not draw any distinction between the imposition of a fraud-based penalty under the Bank Secrecy Act and the imposition of fraud-based penalties under the Internal Revenue Code.

Accordingly, taxpayers can likely use *Sagoo* as support for the argument that any attempt by the IRS to administratively impose a fraud penalty violates the Seventh Amendment.

Practical Effects of SEC v. Jarkesy Where Civil Fraud Penalties Are at Issue

While *SEC v. Jarkey* and *Sagoo* may be viewed by taxpayers — and tax practitioners — as something that can be used to their advantage to argue for lesser or no fraud-related penalties during a civil examination, it is important to be wary of the potential consequences of pushing those cases too far.

If it is true that the IRS needs to provide a right to trial by jury before seeking fraud-based penalty assessments, and if taxpayers stand on such a right, there is a risk that the IRS will bring more criminal cases.

Under the IRS' internal guidelines, the Internal Revenue Manual, civil fraud penalties may only be asserted "when there is clear and convincing evidence to prove that some part of the underpayment of tax was due to fraud."^[19] And such evidence must include "an affirmative act of fraud."^[20]

This means that civil fraud penalties are only at play when there is the possibility that a taxpayer's conduct is considered by the IRS to potentially warrant criminal investigation or prosecution.

Under the Internal Revenue Manual, revenue agents conducting examinations must suspend their examination (i.e., audit) and refer the matter to IRS Criminal Investigation, or IRS-CI, if "it is determined that a potential fraud case has firm indications of fraud/willfulness and meets criminal criteria."^[21]

If the revenue agent knows that the only way the IRS can recover the 75% civil fraud penalty would be to afford the taxpayer a trial by jury, that agent — or the IRS as an institution — may be more inclined to push for IRS-CI to take the case.

Ultimately, it will remain up to IRS-CI to determine whether or not to open a criminal investigation. In the past, the availability of large civil fraud penalties could justify the decision to decline criminal prosecution and pursue certain matters civilly. Now, provided that the court's ruling in *Sagoo* withstands the inevitable appeal, IRS-CI will face increasing pressure to take criminal referrals as the most efficient way of seeking fraud-based penalties while affording taxpayers their Seventh Amendment rights.

Ultimately, it is too soon to determine whether *Sagoo* will have a lasting impact on how civil fraud penalties are handled by the IRS. But it will be important to carefully watch how the IRS reacts to this decision in deciding how to proceed against taxpayers for whom it believes it has the ability to seek a fraud-based penalty.

Michael C. Landman is a partner at Bird Marella Rhow Lincenberg Drooks & Nessim LLP. He previously served as a trial attorney in the U.S. Department of Justice's Tax Division.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] *Silver Moss Props. LLC v. Comm'r of Internal Revenue*, No. 10646-21, 2025 WL 2416867, at *10 (T.C. Aug. 21, 2025).

[2] U.S. v. Sagoo, No. 4:24-CV-01159-O, 2025 WL 2689912, at *4 (N.D. Tex. Sept. 19, 2025).

[3] 26 U.S.C. § 6663.

[4] 31 U.S.C. § 5321(a)(5) (authorizing \$100,000 per violation or 50% of the value of the undisclosed foreign financial account).

[5] U.S. Const. amend. VII.

[6] Id.

[7] SEC v. Jarkesy, 603 U.S. 109, 140 (2024).

[8] Id.

[9] Silver Moss, 2025 WL 2416867, at *3. The procedural posture differed slightly from that in Jarkesy. In Silver Moss, the U.S. asserted its right to a civil fraud penalty in its answer a taxpayer's petition for a refund brought in Tax Court. Silver Moss, 2025 WL 2416867, at *2. Tax Court is a federal trial court constituted by Congress under Article I of the U.S. Constitution.v 26 U.S.C. § 7441.

[10] Id.

[11] A taxpayer typically can choose whether to challenge a tax due and owing in Tax Court or in U.S. District Court. However, in order to challenge the tax in U.S. District Court, the taxpayer must first pay the amount in dispute and then seek a refund for that amount. See <https://www.taxpayeradvocate.irs.gov/news/tax-tips/taxtips-filing-a-petition-with-the-united-states-tax-court/2025/09/> (last visited September 28, 2025, at 10:30 p.m.).

[12] Id. at *4 (citing *Atlas Roofing Co. v. Occupational Safety and Health Rev. Comm'n*, 430 U.S. 442, 455 (1977)) ("Congress may assign the adjudication of public rights to an administrative agency absent a jury without violating the Seventh Amendment.").

[13] Id. at *5.

[14] See Sagoo, 2025 WL 2689912, at *4.

[15] Id.

[16] Id. at *3 n.7.

[17] Id. n.9.

[18] Id.

[19] IRM 25.1.6.2(3) (06-10-2021).

[20] Id. appl. note.

[21] IRM 25.1.3.3 (11-17-2023).