A Critical View of Bank and the Money Laundering Statutes

John K. Villa
A CRITICAL VIEW OF BANK SECRECY ACT ENFORCEMENT AND THE MONEY LAUNDERING STATUTES

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By pleading guilty to a series of Bank Secrecy Act (BSA) offenses in February of 1985, the Bank of Boston heralded a new chapter in the enforcement of the BSA against federally insured financial institutions. This era is characterized by the realization that federal law enforcement authorities can obtain unexpectedly large volumes of information about currency movements by aggressively enforcing the BSA against financial institutions and their officers and employees. While this approach is unquestionably effective in the short run, it succeeds at the expense of damaging the close relationship that has historically existed between financial institutions and federal law enforcement authorities.

There are several reasons for the government's new approach to BSA enforcement. First, the flood of Currency Transaction Reports (CTR's) that followed the Bank of Boston prosecution revealed that the threat of criminal charges, or merely of being publicly identified with money laundering, was a surprisingly potent motivation for financial institutions. Second, public concern over this nation's drug problem, heightened by the deaths of several prominent athletes, gave legislators greater license to take harsh action against anyone identified with money laundering—an activity that many associate with drug dealers. Third, financial institutions failed to comply

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3. Internal Revenue Service Form No. 4789. Financial institutions are required to provide the requested information pursuant to 31 C.F.R. §§ 103.22, 103.26–27 (1987).

strictly with the BSA prior to February 1985 and were, therefore, vulnerable to legitimate criticism.

Nevertheless, the perception by some in the government that the financial services industry blithely ignored the BSA prior to 1985, and that harsh penalties are, therefore, required to motivate compliance, is inaccurate. In fact, the industry performed precisely as regulated industries historically have acted: the industry reflected the priorities of its regulators, most of whom had little interest in the BSA because it has minimal impact on the principal supervisory goal of preserving the safety and soundness of the financial institutions. Once the regulators emphasized compliance with the BSA, financial institutions quickly followed suit.

In light of that experience, there is no warrant for concluding that harsh penalties and criminal charges based upon "flagrant organizational indifference" are necessary to motivate the financial services industry. Such an approach may actually be counter-productive because it fails to distinguish between deliberate intent to violate the law and indifference to legal requirements, thus, disregarding notions of "proportionality" or "just desserts" that have long been basic to our jurisprudence. Unfortunately, the momentum of current initiatives shows no sign of abating. Unless the government takes steps to reverse the adversarial posture that it has adopted toward financial institutions, the long-term relationship between the government and the banking industry will continue to decline, to the detriment of all.

This Article will chronicle the significant points in Bank Secrecy Act enforcement and will analyze the roles that Congress, the Department of the Treasury (Treasury), and the Department of Justice (Justice Department) have played in this process. The major issues that appear on the horizon will then be surveyed, focusing principally on the new laundering statutes.

6. See infra text accompanying note 71.

A. The Bank Secrecy Act

The federal law now commonly referred to as the BSA was enacted in 1970 as part of the Bank Records and Foreign Transaction Act (BRFTA).9 As explained in its declaration of purpose,10 the BRFTA was a response to rising congressional concern over the use of foreign banks to "launder" the proceeds of illegal activity and to evade federal income taxes.11 Title I of the BRFTA, which imposes recordkeeping requirements on financial institutions, has now been assimilated into the text of title 12 of the United States Code, which imposes regulatory duties on federally insured financial institutions.12 Title II of the BRFTA, originally referred to as the Currency and Foreign Transactions Reporting Act, has survived in chapter 53, title 31 of the United States Code.13 The provisions of title II are now commonly referred to as the BSA.

The BSA was controversial because it infringed on the traditionally confidential relationship between the bank and the customer.14 Probably for this reason, the Secretary of the Treasury, who is charged with enforcing the BSA, promulgated regulations which pointedly did not exercise the full scope of his statutory authority. In particular, the regulations did not require that individuals file CTR's regarding their own currency transactions, although the statute would have permitted it.15 Instead, the regulations required only that financial institutions file CTR's for their customers' transactions.16

This self-restraint did not insulate the BSA from attack; in the six years following its passage, it was challenged twice in the United States Supreme Court. In California Bankers Association v. Schultz17 and United States v.

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Miller,\textsuperscript{18} the Court upheld the major provisions of the BSA. Had it not been for the Secretary's voluntary limitations on the reach of the regulations, however, there is reason to believe that the BSA would have been held unconstitutional as infringing upon the customers' privilege against self-incrimination.\textsuperscript{19}

\textbf{B. Early Enforcement Efforts}

Although the \textit{California Bankers Association} and Miller decisions dispelled the cloud that had obscured the BSA since its enactment, very little enforcement activity occurred prior to the early 1980's. Until that time, prosecutions under the BSA\textsuperscript{20} were generally limited to charges against individuals who transported monetary instruments into or out of the United States without reporting them on a Report of International Transportation of Currency (known as CMIR).\textsuperscript{21}

Beginning in the early 1980's, however, federal prosecutors became increasingly aware of the volume of cash related to illegal drug transactions that was flowing into the banking system, particularly through financial institutions in the southeastern United States. They responded with a federal law enforcement task force known as "Operation Greenback," which targeted large-scale money laundering for drug sellers and resulted in a significant number of prosecutions, including several involving financial institutions.\textsuperscript{22} The publicity resulting from Operation Greenback prompted other federal prosecutors to utilize the BSA. Still, only a trickle of cases for failure to file CTR's was brought between 1982 and 1984;\textsuperscript{23} the statute was still regarded as one to be used against customers who circumvented the CTR filing requirements by paying off bank employees or by using false names.

\begin{itemize}
\item \textsuperscript{18} 425 U.S. 435, 444-45 (1976).
\item \textsuperscript{19} In \textit{California Bankers Ass'n}, 416 U.S. at 71-75, the Supreme Court upheld, by a vote of six to three, the Secretary's regulations against a challenge that they infringed on the bank customers' fifth amendment privilege against self-incrimination. Justices Powell and Blackmun concurred, but expressed doubts about the constitutionality of the reporting requirements should the Secretary impose on individual customers the obligation to file reports on their transactions, as he was empowered to do by statute. \textit{Id.} at 78-79. If the Secretary had gone further with the regulations, and Justices Powell and Blackmun had joined the dissenters, then the constitutionality of the Act would have been rejected by a vote of five to four.
\item \textsuperscript{20} See, e.g., United States v. Rodriguez, 592 F.2d 553 (9th Cir. 1979); United States v. Granda, 565 F.2d 922 (5th Cir. 1978).
\item \textsuperscript{21} A Report of International Transportation of Currency, Customs Form No. 4790, is required to be filed pursuant to 31 U.S.C. \textsection 5316 (1982 & Supp. III 1985).
\item \textsuperscript{22} A description of Operation Greenback is contained in \textit{PCOC REPORT supra} note 5, at 26-27.
\end{itemize}
In 1984, the newly appointed President’s Commission on Organized Crime held a series of sensational hearings at which financial institutions were roundly accused of engaging in money laundering.\textsuperscript{24} The hearings resulted in the \textit{Interim Report to the President and the Attorney General}.\textsuperscript{25} The report contained a number of recommendations for statutory changes. The Commission’s proposals included an increase in the civil and criminal penalties imposed for BSA violations\textsuperscript{26} and proposed legislation that was the precursor to the current statutory prohibition of the laundering of monetary instruments.\textsuperscript{27}

Almost simultaneously, Congress revisited the BSA when, as part of the Comprehensive Crime Control Act of 1984,\textsuperscript{28} it raised the civil money penalties for BSA offenses from $1,000 to $10,000 for each violation.\textsuperscript{29} Because the BSA was still viewed as a weapon against drug dealers, however, this statutory change was largely ignored by the financial services industry.

The turning point in BSA enforcement occurred with the guilty plea of the Bank of Boston in February 1985. The spectacle of a major, well-respected bank pleading guilty to criminal charges generated remarkable media attention\textsuperscript{30} and was the subject of highly publicized congressional hearings.\textsuperscript{31} Although many in the banking community, both in and out of government, privately stated that they felt that the Bank of Boston had been unfairly held up to public ridicule, it was impossible publicly to come to the defense of an institution that had pled guilty to criminal offenses.

Many financial institutions reacted to the Bank of Boston case by directing internal auditors to review BSA compliance. All too often those auditors discovered that compliance with the BSA had been haphazard at best and that a significant number of transactions had not been reported on CTR’s. In most cases, the cause of reporting failures was that financial institutions historically viewed the BSA as directed toward large, suspicious cash

\textsuperscript{25} PCOC REPORT \textit{supra} note 5.
\textsuperscript{26} Id. at 73.
\textsuperscript{27} See 18 U.S.C. § 1956 (Supp. IV 1986); see also PCOC REPORT \textit{supra} note 5, at 67-69.
transactions. They devoted little attention to the transactions of established customers that might also require reporting.

To their dismay, financial institutions also found a confusing body of regulations governing CTR filing requirements. In broad terms, the regulations required filing of CTR's for all cash transactions exceeding $10,000 by non-exempt customers. The Treasury regulations, however, apparently drew irrational distinctions between the types of customers who were eligible for exemption by the financial institution and those who were not. Erroneous advice by federal officials contributed to the problems. Customs officers, bank examiners, and even federal prosecutors reviewed exempt lists that were riddled with obviously ineligible customers, yet they voiced no objection. In addition, there was confusion over the relationship between the filing requirements of the CMIR, which requires information about international transportation of currency or monetary instruments, and those of the CTR. Many financial institutions incorrectly assumed that due to similarities between the two forms, they would not be required to file a CTR if they filed the CMIR.

Fearing that they would be the next prosecutorial target for their filing failures, financial institutions began a massive campaign to comply with the BSA and filed a virtual flood of CTR's. Some of the financial institutions that discovered significant filing failures approached the Treasury to disclose their mistakes and to resolve the problem in hopes of avoiding a criminal investigation. The Treasury publicly settled with several dozen banks and announced more than a dozen civil money penalty settlements that exceeded $100,000. Other institutions that disclosed significant filing failures reportedly have not been fined.

Although there are good arguments that civil money penalties should not be imposed where the failure to file had been a mere oversight or the result of a misunderstanding, shock waves from the Bank of Boston case apparently convinced many financial institutions to forego that defense and settle rather
than to take the risk that they would be prosecuted or even sued to enforce a
civil money penalty assessment. Most financial institutions, being particu-
larly cognizant of their public image, concluded they could not risk the
stigma of being charged with a violation that smacked of money laundering.

After a substantial amount of media attention, the publicity surrounding
the civil money penalty settlements peaked in late 1985. References to
money laundering in press accounts of these increasingly routine settlements
have gradually receded and have now vanished.


Congress returned to the issues of the BSA and money laundering in the
Anti-Drug Abuse Act of 1986, which includes subtitle H of title I, referred
to as the Money Laundering Control Act of 1986 (MLCA). The MLCA
contains amendments to the BSA and two new laundering statutes. The
BSA amendments give the Treasury much greater negotiating leverage in
civil settlement cases by increasing the maximum civil penalty for each viola-
tion to the greater of $25,000, or the amount of the transaction, while not
exceeding $100,000. In addition, Congress enacted a new penalty for
“negligent” violations, permitting up to a maximum of $500 per violation.

The MLCA also added a new section to the BSA, which is known as the
“antistructuring statute.” Section 5324(1) and (2) of the antistructuring
statute prohibit an individual from causing a financial institution either to
fail to file a required report or to file a false report. Congress presumably
intended these provisions to address the growing body of cases which have
held that because the regulations promulgated under the BSA do not impose
a duty on individuals to inform the bank of a reportable transaction, such a
duty cannot be imposed in a criminal prosecution without violating the fair
warning requirements of the due process clause of the fifth amendment.

The most controversial portion of section 5324 of the antistructuring stat-

v. One (1) Lot of Twenty-Four Thousand Nine Hundred Dollars ($24,900) in United States
Currency, 770 F.2d 1530, 1533-34 (11th Cir. 1985).
37. See, e.g., Nash, U.S. Penalizes Crocker Bank Over Reporting, N.Y. Times, Aug. 28,
1985, at A1, col. 2.
§§ 5321(a)(1), (4), (b), 5324 (West Supp. 1987).
43. Id. § 5321(a)(6).
44. Id. § 5324.
45. Id. § 5324(1)-(2).
46. See, e.g., United States v. Anzalone, 766 F.2d 676, 682 (1st Cir. 1985).
ute is subsection (3) which prohibits the "structuring" of transactions to evade reporting requirements, although the act of "structuring" is left undefined.\textsuperscript{47} It appears that the prohibition against structuring was intended to criminalize the division of a single quantity of cash which exceeds the exempt limit into two or more unreportable sums for deposit in different institutions. If that is, in fact, the statute's objective, it goes considerably beyond the bounds of most criminal statutes.\textsuperscript{48}

Although it is not yet generally recognized, the statutory changes which will have the greatest impact on financial institutions are the MLCA's two new laundering statutes.\textsuperscript{49} Broadly speaking, section 1956 of title 18 of the United States Code prohibits knowing involvement in a wide range of transactions involving the proceeds of criminal activity either (1) with the intent to promote unlawful activity\textsuperscript{50} or (2) with the knowledge that the transaction is designed either to conceal some aspect of the funds, such as its ownership, control, or source, or to avoid the currency transaction reporting requirements.\textsuperscript{51} Another subsection of section 1956 prohibits the transportation of monetary instruments in foreign commerce with the same intent or knowledge.\textsuperscript{52} Section 1957 of title 18 of the United States Code prohibits knowingly engaging in virtually any typical banking transaction involving a financial institution in "criminally derived property" with a value exceeding $10,000.\textsuperscript{53} The penalty for violation of section 1956 is a fine of $500,000 or twice the value of the monetary instrument or funds involved in the transaction or transportation, whichever is greater, and/or imprisonment for not more than twenty years.\textsuperscript{54} The penalty for violation of section 1957 is a fine of not more than twice the criminally derived property involved and/or im-

\begin{thebibliography}{54}
\bibitem{48} To analogize from tax law, a seller of goods who bargained for and actually received one-quarter of the purchase price at the time of sale and the remaining three-quarters the next year in order to spread his taxable profit over the two-year period would ordinarily not be accused of tax evasion, let alone criminal conduct. The Internal Revenue Code recognizes that in the absence of a sham transaction, a taxpayer who actually structures his business transactions to receive the income in future years will be taxed accordingly. See 26 U.S.C. § 453 (1982 & Supp. III 1985) (installment method). It is, therefore, surprising that Congress would take such a diametrically opposite approach in the antistructuring provisions of the BSA and criminalize such preplanned activity.
\bibitem{50} Id. § 1956(a)(1)(A).
\bibitem{51} Id. § 1956(a)(1)(B).
\bibitem{52} Id. § 1956(b).
\bibitem{53} Id. § 1957. There is no requirement that the transaction involve more than $10,000 in cash or currency, only that a monetary transaction occur as defined in subchapter II, chapter 53 of title 31, which could be satisfied by a monetary instrument. Id.
\bibitem{54} Id. § 1956. There are also civil penalties which extend to the greater of the value of the monetary instrument or funds involved in the transaction or $10,000. Id. § 1956(b).
\end{thebibliography}
prisonment of not more than ten years.\textsuperscript{55}

Although both statutes leave crucial terms undefined—including, most significantly, the concept of "proceeds"\textsuperscript{56}—their thrust is quite clear. These statutes, for the first time, make it a crime to do business with or conduct financial transactions for any person who derives his monies from certain specified unlawful activities. The reach of section 1956 is restricted to some extent by the fact that violation of the statute requires intent to promote the illegal activity or knowledge of an illegal purpose for the transaction by another person.\textsuperscript{57} By contrast, mere knowledge of the illegal source of the funds establishes a violation of section 1957. Thus, section 1957 leaves financial institutions subject to prosecution for conducting routine transactions in the accounts of tainted customers.\textsuperscript{58}

\textbf{D. The Bank of New England Case}

The most significant recent event concerning the BSA occurred in \textit{United States v. Bank of New England, N.A.},\textsuperscript{59} where the Bank of New England was convicted of committing thirty-one felonies arising out of its failure to file CTRs. Over a period of more than a year, a customer of the bank, James McDonough, withdrew more than $10,000 in cash from a single account at one branch of the bank on numerous occasions.\textsuperscript{60} On each occasion, McDonough presented multiple checks to a single bank teller and received in return a lump sum of cash in excess of $10,000.\textsuperscript{61} The jury acquitted McDonough as well as two bank tellers who were indicted along with the bank.\textsuperscript{62} The bank was convicted, however, and fined a total of $1.24 million.\textsuperscript{63}

The BSA provision under which the Bank of New England was convicted imposes criminal penalties on one who "willfully violat[es]" the CTR filing requirement.\textsuperscript{64} Courts interpreting this standard have held that the government must prove the highest level of scienter, or specific intent, imposed by our criminal law.\textsuperscript{65} In particular, "the defendant [must] have actually
known of the currency reporting requirement and have voluntarily and intentionally violated that known legal duty in order to be convicted of the crime.""}66

In Bank of New England, the trial court gave controversial instructions on the issues of corporate “knowledge” and corporate “willfulness.”67 The trial court instructed the jury that the bank could be found to have the requisite specific intent even in the absence of classic respondeat superior liability where an employee, acting within the scope of his duties and for his master’s benefit, intentionally violates the law.68 The jury was told that in order to determine the knowledge of “the bank as an institution,” it could “sum” up the knowledge of its separate employees.69 If the “sum” of that collective knowledge constituted knowledge of the applicable facts and law, the bank could be deemed to have knowledge of its duties.70 Furthermore, the bank could be guilty of a willful violation of those duties if it exhibited “flagrant organizational indifference” to the reporting requirements.71 Thus, the trial court’s instructions permitted a collective entity to be found guilty of a serious federal felony requiring specific intent in the absence of any individual employee, officer, or agent having the requisite intent.

On review of the bank’s conviction, the United States Court of Appeals for the First Circuit upheld these instructions.72 The court reasoned that “the knowledge obtained by corporate employees acting within the scope of their employment is imputed to the corporation.”73 According to the court, corporations divide aspects of particular duties and operations into smaller components and the “aggregate of these components constitutes the corporation’s knowledge of a particular operation.”74 Moreover, the First Circuit held that the corporate “indifference” standard reflected in the instructions was appropriate because, with respect to federal regulatory statutes, the

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66. Warren, 612 F.2d at 890 (emphasis in original).
68. Id. at 855.
69. Id.
70. Id. The instructions stated that, “if Employee A knows one facet of the currency reporting requirement, B knows another facet of it, and C a third facet of it, the bank knows them all.” Id.
71. Id.
72. Id. at 859.
73. Id. at 856.
74. Id.
courts have defined willfulness as "‘a disregard for the governing statute and an indifference to its requirements.’"\textsuperscript{75} The Supreme Court declined to review the First Circuit’s decision.\textsuperscript{76}

Contrary to the implications of the First Circuit’s opinion, the jury instructions in \textit{Bank of New England} reflect a significant expansion of traditional principles of corporate criminal liability. Neither the BSA itself nor previous court decisions support the imposition of criminal liability for a specific intent crime based on the collective knowledge of corporate employees. More fundamentally, equating “willfulness” with “flagrant organizational indifference” represents an erosion of the level of scienter that is prescribed by the BSA. The cases on which the First Circuit relied arose in the context of “public safety” regulations, such as those governing railroads and trucking, for which the courts have traditionally imposed a lower standard of criminal intent than in specific intent crimes such as tax evasion.\textsuperscript{77}

The latter category of offenses has always been understood as involving moral turpitude and, accordingly, some kind of “evil motive is a constituent element of the crime.”\textsuperscript{78} Indeed, when holding that the willfulness standard for “public safety” violations can be met by mere indifference or negligence, the courts have been careful to emphasize that more is required under statutes where “‘willfully’ is . . . used to mean with evil purpose, criminal intent or the like.”\textsuperscript{79} Applying standards developed primarily in civil, public safety cases to the specific intent crimes arising out of failures to file CTR’s poses a

\textsuperscript{75}. \textit{Id.} (quoting TransWorld Airlines, Inc. v. Thurston, 469 U.S. 111, 127 & n.20 (1985)). In \textit{Thurston}, the Supreme Court held that a showing of “reckless disregard” to the requirements of the law is enough to establish “willfulness” for purposes of double civil damages under the Age Discrimination in Employment Act (ADEA). 469 U.S. at 126; \textit{see also} 29 U.S.C. § 626(b) (1982). Under that statute, “evil motive or bad purpose” is not required and the employer need not have “intended to violate the Act.” \textit{See} 469 U.S. at 126-27 & n.19. Although the Supreme Court has held that this definition of willfulness had been used in various civil and criminal contexts, \textit{id.}, its use with respect to civil damages under the ADEA provides dubious support for applying an indifference standard to crimes, such as those arising under the BSA, where specific intent to violate the law is required.


\textsuperscript{77}. That line of cases began with \textit{United States v. Illinois Central Ry.}, 303 U.S. 239 (1938), in which the Court considered violations of a federal statute imposing civil penalties on “knowing and willful” violations of rules governing the incarceration of cattle in railroad box cars. The Court concluded that, with respect to a corporation, the statute’s intent requirement could be met by “mere indifference, inadvertence or negligence of employees.” \textit{Id.} at 244; \textit{see also} \textit{Riss & Co. v. United States}, 262 F.2d 245, 248 (8th Cir. 1958) (criminal statute limiting maximum driving time by truckers); \textit{United States v. Sawyer Transp., Inc.}, 337 F. Supp. 29, 30 (D. Minn. 1971) (criminal statute regarding falsification of truck drivers’ logs), \textit{aff’d}, 463 F.2d 175 (8th Cir. 1972); \textit{United States v. T.I.M.E.-D.C., Inc.}, 381 F. Supp. 730, 740 (W.D. Va. 1974) (criminal statute regarding truck driving while impaired).


\textsuperscript{79}. \textit{Illinois Central Ry.}, 303 U.S. at 242.
substantially enhanced risk of criminal liability for financial institutions genuinely attempting to comply with the BSA.

II. CONGRESS, THE TREASURY, AND THE JUSTICE DEPARTMENT

A. Recent Legislative Changes

The BSA, as well as the more recent laundering statutes, implicitly reflect a congressional judgment that law enforcement goals can be achieved more effectively by severely punishing federally regulated financial institutions than by developing cooperative programs with the banking industry. The wisdom of this approach is open to serious question because financial institutions historically have been close allies with the law enforcement community, and have cooperated with federal law enforcement authorities almost to a fault. Moreover, in its headlong rush to be tough on the banks, Congress adopted legislative changes that have created insoluble problems for financial institutions without any corresponding benefit to law enforcement interests.

A case in point is section 1957 of title 18 of the United States Code. Before analyzing the flaws in the statute, it is worth observing that the statute presents a clear departure from traditional concepts of criminal behavior. Although the criminal law has long forbidden the receipt of stolen goods, it has not generally prohibited a person from doing business with or for another simply because unlawful conduct served as the source of the funds for the transaction. One has the right to sell his house to a gangster as freely as to a clergyman as long as the parties perform the transaction at arm's length with no intent to assist the gangster in the commission of a crime.

Section 1957, by contrast, reflects a new approach and one that seems likely to exact unanticipated social costs. One who suspects a person of offering stolen goods for sale may protect himself by merely declining to purchase the suspect goods. The social cost of declining that purchase is minimal. If, on the other hand, it is a crime to do any business at all with one who deals in the proceeds of illegal activity, then those who are merely suspected of crimes will find that they cannot engage in everyday commerce; fearing criminal liability, no one will risk dealing with them. The impact on the suspected individual can be severe because no knowledgeable person will

transact business with him, yet there may be no means by which the suspected individual can clear himself. The social cost of imposing such a stigma on individuals—especially those who have not been convicted of, let alone charged with, any crime—should present grave civil liberties concerns even for the most ardent law-and-order legislator. It is disappointing to find that Congress did not seriously debate these important issues at the time it enacted section 1957.82

Putting to one side the serious policy questions presented by section 1957, the statute itself is riddled with ambiguities that present enormous problems for financial institutions. As bank officers confront these ambiguities, they may well choose to read the statute broadly—thus minimizing their own risk of criminal prosecution—which would cause the statute to have an even greater impact than Congress expected. A direct result of loose draftsmanship will, therefore, cause the denial of financial services to some innocent customers by justifiably cautious bankers.

Section 1957 prohibits conducting transactions that involve "criminally derived property."83 Yet, neither section 1957 nor section 1956 define these "proceeds" concepts, thus, inviting a wide range of interpretation. Do the statutes only apply to the direct fruits of illegal activity or do they also apply to the products of those fruits which are reinvested and thereby change form? If $25,000 in illegal proceeds are placed into a bank account containing $75,000 in legal monies, does every check subsequently written on that account consist of 25% illegal proceeds? If a bank lends a customer $50,000 and subsequently learns that an unlawful activity created his source of funds, can it accept repayment of the loan? If an individual has legal and illegal sources of income, can a bank transact any business with him without fear of prosecution?

Even with adequate definition of the key statutory terms, there is little chance that financial institutions could apply them accurately. Financial institutions are ill-equipped to decide whether a particular customer obtains his funds from illegal sources. It typically takes a trained federal prosecutor, using experienced investigators and the unparalleled power of a federal grand jury, months or even years to identify criminal activity. An inexperi-

82. The only direct discussion of this issue appears in the transcript of the mark-up session on § 1957 where Representative Lundgren stated: "And I just think it is not a bad thing for us to send a message to even a small community, if you got a local [drug]trafficker and everyone knows he is a local trafficker, you don't do business with that person as you do business with everybody else." Transcript at 17. Representative Shaw later discussed the issue and stated that he wanted to "make the drug dealers' money worthless." Transcript at 23. There was no discussion of this issue on the floor of the House or the Senate.
enced banker applying an unintelligible statute like section 1957 has little hope of making a correct decision while a customer transaction is pending. If the financial institution incorrectly decides to terminate business activities with the suspected customer, a major civil lawsuit is inevitable.

The impossible choices that face many financial institutions demonstrate that Congress has simply dropped the problem in the lap of the financial services industry and walked away. None of the options are attractive, but some financial institutions will ultimately decide that unless a customer clearly and openly engages in illegal activity, they will not terminate business contacts with him. While this may be a realistic solution, it is not a happy one. It means that many financial institutions will, for the first time, knowingly operate on the fringe of the criminal law.

The problems in interpreting and applying section 1957 have not been generally recognized because the statute is new and there are no reported section 1957 prosecutions. Prosecution of a major bank or senior bank officer for violating section 1957 undoubtedly will create a furor similar to that which followed the Bank of Boston case. At that point, financial institutions will realize, for the first time, that there are no ready solutions to the difficulties posed by these new statutes.

B. Treasury Department Initiatives

Given the political realities, the flaws in the BSA prior to October 1986, and an apparent shortage of staff, the Treasury has made a creditable effort to reconcile legitimate law enforcement goals with the maintenance of a constructive relationship with the financial services industry. Two criticisms can be leveled at the Treasury. First, the CTR regulations in section 103 of title 31 of the Code of Federal Regulations are unnecessarily confusing. Second, the Treasury has not adequately encouraged financial institutions to voluntarily disclose their CTR violations. The first problem results from the Treasury's failure to direct adequate resources to this issue in the years preceding 1985. The second problem probably results from a lack of resources, an unwieldy statutory scheme, and an adverse political climate.

84. Financial institutions will almost certainly receive no assistance from law enforcement officials in making the decision whether to do business with a particular customer. In many instances, law enforcement authorities are unaware of the nature of the customer's business at the time that the financial institution seeks advice. In those cases in which they are aware of the illegal nature of the customer's business, they would likely refuse to provide substantive information because it would interfere with an existing investigation, disclose information subject to strict rules governing grand jury secrecy, see Fed. R. Crim. P. 6(e)(2), or subject the law enforcement authorities to civil liability from the customer.

The regulations governing CTR filing reporting requirements historically have drawn apparently irrational distinctions between the types of customers that financial institutions can exempt. For example, if the goal is to detect criminal activity, then there is no apparent reason to allow financial institutions to exempt bars, restaurants, and race tracks from CTR reporting requirements and, at the same time, prohibit financial institutions from exempting churches, schools, and hospitals. The line which the Treasury drew was to permit financial institutions to exempt businesses that customarily dealt in large amounts of cash regardless of the potential for abuse. An equally reasonable and perhaps more sensible rule might have been to permit financial institutions to exempt businesses that traditionally had little risk of criminal activity. Even accepting the Treasury's distinction, however, it was difficult to justify permitting financial institutions to exempt a retail seller of goods but not a provider of services.

Most financial institutions would probably prefer fewer, but clearer, exemptions to more liberal exemption criteria that are difficult to interpret and apply. The Treasury's rules fail to meet that goal and have contributed considerably to the confusion over BSA compliance. While the current regulations are improving, they leave many questions unanswered.

Another source of confusion is the fact that the filing requirements for CTR's and CMIR's are inconsistent. In some instances, financial institutions that filed one form have been fined for not filing the other, despite the fact that they contain the same basic information and that the Treasury records the information from both of them in the same data bank. Some financial institutions that have unwittingly violated these provisions and have therefore been assessed civil money penalties in situations where the information loss to the government was minimal.

A second criticism of the Treasury is that it devotes too much of its available resources to extracting civil money penalties from financial institutions who come forward and voluntarily disclose past BSA violations. While

86. Id. § 103.22(b)(2)(ii).
87. Id. § 103.22(b)(2)(i).
88. Indeed, a number of financial institutions have concluded that the problems of interpreting and applying the Treasury's exemption criteria are greater than the cost of eliminating all exemptions and filing CTR's for all transactions, exempt or not. These institutions have discarded their exempt lists, a decision that has resulted in a substantial increase in CTR filings for an already overburdened system. This practice, which some have dubbed "malicious compliance," is the most convincing rejection of the entire exemption process.
89. It is also possible, however, that significant changes in the regulations, even to achieve clarification, would cause more problems than they would solve in light of the necessity to reeducate compliance personnel who are now finally familiar with the BSA.
90. See supra notes 33-34 and accompanying text.
there does not appear to be any public information regarding the total amount of resources devoted to the voluntary disclosure cases, the Treasury’s small staff—in what is now known as the Office of Financial Enforcement—seems to devote much of its time to the voluntary disclosure cases. At the same time, the Treasury rarely disturbs the vast majority of financial institutions that do not voluntarily disclose past BSA violations. This strategy has the unfortunate effect of punishing the good corporate citizens who come forward while ignoring the financial institutions that elect not to disclose their past violations. It is difficult to conceive of a more counterproductive approach to a regulatory scheme that must, after all, rely upon voluntary compliance to be effective.

There are probably several reasons for the Treasury’s approach. The first, and probably most significant, is that there are so few Treasury personnel and so many voluntary disclosure cases, often involving relatively large financial institutions, that the Treasury has no resources to pursue the nonvolunteers. An important second reason is that the Treasury once lacked the statutory authority to compel financial institutions to disclose BSA violations. This omission was corrected in the MLCA in 1986,92 yet the Treasury still has not fully exercised its authority.93 The third, and more debatable reason for aggressively pursuing those financial institutions that voluntarily disclose, is that congressional overseers are anxious to see a tough enforcement posture by the Treasury against the largest banks, which are the institutions that typically make voluntary disclosures. Thus, even though a “get tough” approach is remarkably shortsighted in the overall regulatory strategy, Congress seems to favor it and it appears to have influenced the Treasury’s actions, especially in the year following the Bank of Boston prosecution.

A review of the Treasury’s enforcement of the BSA reveals that it has performed reasonably well under very difficult circumstances, including insufficient staff, a poorly drafted statute (until the MLCA), and unenlightened congressional oversight. By avoiding unnecessary bank bashing, the Treasury has managed to retain credibility with the financial services industry as a responsible regulator. One must, however, conclude that to the extent that the Treasury had hoped for an effective voluntary disclosure program which would have encouraged financial institutions to come forward with past violations, it has failed. Without any incentive to do so, most financial institutions have simply avoided conducting historical reviews, or if they have

93. The Treasury promulgated regulations implementing the summons authority in June 1987, codified at 31 C.F.R. §§ 103.61-.67 (1987), but has not yet exercised its authority under those rules.
performed them, they have not submitted them to the Treasury. While the threat of future sanctions has encouraged most institutions to achieve a high level of current compliance, the dubious benefits of voluntary disclosure of past errors to the Treasury have not been great enough to induce such disclosures.

C. Justice Department Activities

Criminal prosecutions under the BSA have, with a small number of significant exceptions, been unremarkable. In large part, the Justice Department has prosecuted bankers or customers for engaging in flagrant and intentional violations of the BSA by failing to file CTR's or filing false CTR's with the intent to mislead the government. The small number of more important prosecutions have been brought against major banks whose criminal liability results from some theory of "organizational indifference" to the BSA. The first such significant prosecution appears to have been against the Bank of Boston, followed more recently by Bank of New England.

The conviction of the Bank of New England may have produced one of the most important modern decisions on the issue of corporate criminal liability. If taken to its limits, the decision undoubtedly could lead to scores of indictments of federally insured financial institutions for BSA violations, as well as for violations of the new laundering statutes. Bank of New England gives the Justice Department a significant new weapon against financial institutions. Under the "flagrant organizational indifference" standard, vast numbers of financial institutions are subject to prosecution for lack of BSA compliance prior to the Bank of Boston prosecution in February 1985, which jolted their compliance officers to life. Even more chilling for financial institutions is the prospect of the Justice Department applying the "collective knowledge" concept in section 1957 prosecutions to convict financial institutions of laundering violations when neither the financial institution nor any of its employees or officers had any criminal culpability whatsoever.

94. There have been no civil Bank Secrecy Act suits.
95. See, e.g., United States v. Heyman, 794 F.2d 788 (2d Cir. 1986).
96. Because the First National Bank of Boston pled guilty rather than going to trial, it is difficult to ascertain all of the facts of the offense. The reports surrounding the plea, however, did not suggest that the institution was engaged in deliberate noncompliance. See sources cited supra notes 30-31.
98. See supra notes 71, 75, and accompanying text.
99. See supra notes 69-74 and accompanying text.
100. Because the required scienter for violation of § 1957 is merely that the person conduct
Any critique of the Justice Department’s enforcement of the BSA and the laundering statutes should be deferred until it becomes clear how these powerful new tools will be used. If these theories are used against morally neutral conduct—and they clearly have that potential—then it will erode the industry’s respect for the processes of administering justice. As Professor Packer has observed, the application of criminal sanctions to morally neutral behavior has the effect of decriminalizing the criminal law and subtly changing people’s attitude toward criminality.101 While this concept is typically applied to criminal activity by individuals, it also applies to corporate behavior. If financial institutions perceive that the government is arbitrarily prosecuting banks for violating statutes which the banks are attempting to obey, then some banks will for the first time divert effort from attempting to obey the law to attempting to escape detection of the inevitable violations. The short term gains from an aggressive use of these tools will not outweigh the long term damage between those financial institutions and federal law enforcement.

III. CURRENT ENFORCEMENT PROBLEMS

The first round of BSA enforcement has concluded with fears of prosecution that have brought the financial services industry into substantial compliance. The question for the future is whether the relationship between the financial services industry and federal law enforcement authorities will continue to be strained or will begin to improve. To answer that question, one must consider the important issues that will arise in the next several years under the BSA and the new laundering statutes.

The first issue is whether Congress will amend section 1957 of title 18 of the United States Code, so that the financial services community will have some notion of the statute’s reach. Because of the severe penalties for violations of the statute102 and the fact that it embodies a relatively new concept in our criminal law, it would be extraordinarily painful for the government to define critical elements of the statute through criminal prosecutions. Even if the prosecutions that are ultimately brought interpret the statute

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102. See supra note 55 and accompanying text.
reasonably, the statute’s reach will not be clear for a number of years, if ever. In the interim, financial institutions that attempt good faith compliance with this provision will inevitably err on both sides: those that construe the statute too narrowly will become the target of grand jury investigations and possibly prosecuted, while those who construe it too broadly will be sued by customers with whom they unjustifiably refuse to do business. Financial institutions should not be forced to run that gauntlet; the statute should be clarified.

The second issue is whether the government—specifically the Justice Department—will develop a “safe harbor” concept for section 1957. Even if the statute is amended to address its ambiguities, a financial institution that merely suspects a customer of engaging in criminal activity has difficult choices. It can continue to do business with the customer and expose itself, and its individual officers and employees, to criminal liability for violating section 1957 if the customer is ultimately shown to have engaged in illegal activity and the suspicious incidents are deemed sufficient to give the bank knowledge of his activities (which always seems easier in hindsight). Alternatively, the bank can refuse to conduct business with the customer, running the risk that the customer was innocent, or at least cannot be proven guilty, and will sue.

Mr. Rusch is correct in observing that a financial institution that identifies a customer involved in conducting a suspicious transaction may report that fact to the government on a criminal referral form, and if the referral falls within certain guidelines specified in the Right to Financial Privacy Act, the financial institution cannot be held liable for making the referral or for failing to inform the customer of it. This is good as far as it goes. The real question, however, is whether federal law provides protection for the financial institution that decides not to continue doing business with this suspicious customer in order to protect itself and its personnel from criminal prosecution under sections 1956 and 1957. Evidently, there is no protection. In a case arising in Maine prior to the effective date of these statutes, a bank learned this lesson the hard way when it abruptly terminated its relationships with a customer after being told, incorrectly, by a federal agent that its customer was an underworld figure. The customer sued and recovered a

104. See Rusch, supra note 34, at 482 n.73.
$12.5 million verdict against the bank.106

One would think that if the financial institution were in doubt and filed a criminal referral on the customer,107 it would have advanced law enforcement goals and should, therefore, be relieved of the threat of prosecution even if it continued to do business with that customer. That is not the case. In fact, a prosecutor might use the making of a referral against the financial institution as an admission to show that it knew of the possibility that the customer engaged in illegal activities. This will discourage referrals. Because the possibility of a civil suit against the bank often seems more likely than prosecution for a laundering violation, the bank will probably decide to continue doing business with a current customer unless the evidence of illegal activity is very strong. If it continues to do business, then it may also decide against filing a criminal referral to avoid later being charged with knowledge of criminal activity. The result is that the likelihood of a referral declines and, consequently, the government is deprived of significant law enforcement information.

A more rational solution would be to adopt a safe harbor rule providing that if a bank files a reasonable and good faith referral on a customer, then it will not be prosecuted for further dealings of the same kind with that customer. This would encourage the prompt submission of referrals and allow the financial institutions to believe that law enforcement authorities are working with them rather than against them.

The third issue will be the extent to which the Justice Department uses the "flagrant organizational indifference" and "collective knowledge" standards from the Bank of New England decision.108 These concepts could be used to prosecute many financial institutions for their total ignorance of the BSA prior to February 1985,109 yet no useful purpose would be served at this point by such prosecutions. Similarly, the financial services industry has totally failed to appreciate the dangers inherent in section 1957 in the year after it was enacted and might therefore be vulnerable to the same "indifference" theory of prosecution in the future.


107. All of the regulatory agencies require that the financial institutions subject to their respective jurisdictions file criminal referrals, or reports of suspected crimes, with the agency and the Justice Department. See, e.g., 12 C.F.R. § 21.11 (1987) (Office of the Comptroller of the Currency referral regulations).

108. See supra notes 70, 97-100, and accompanying text.

IV. CONCLUSION

No thoughtful commentator can look at the Bank Secrecy Act and laundering statutes without concluding that they will continue to present unique policy questions for Congress, the Justice Department and the Treasury. The ultimate verdict on whether these powerful statutes are used properly, and effectively, will depend upon whether those charged with drafting and administering these laws carefully define their long-term goals and enlist the help of the financial services industry to achieve those goals.