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2012 Saw an Increase in Enforcement Against Banks

Investigations targeted illicit transactions of funds.

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Last year saw a sharp increase in investigations targeting the illicit flows of funds through financial institutions. In three prominent enforcement actions in 2012—against ING, Standard Chartered Bank and HSBC—prosecutors and regulators extracted massive fines for conduct ranging from intentional concealment of illicit transactions to ineffective monitoring. The crackdown focused not just on how these banks facilitated transactions by parties subject to U.S. trade sanctions, but also on how they failed to conduct due diligence on customers and foreign financial institutions who made suspicious transfers.

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The statutory bases for investigation and prosecution of this conduct have long existed in federal and state law.[1] The U.S. Department of Justice and Department of the Treasury's Office of Foreign Assets Control (OFAC) have targeted violations of trade sanctions laws and regulations that prohibit transactions with individuals and companies in Cuba, Iran, North Korea, the Sudan and Syria, among others. In addition, the federal government has long pursued cases involving money laundering—transactions intended to conceal the origin or nature of illicit proceeds or to avoid report-

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ing requirements.[2] Recently, however, the federal government has signaled an increased focus on these crimes, including through the creation in 2010 of a Money Laundering and Bank Integrity Unit within the DOJ. The unit, staffed at its inception with 14 prosecutors, investigates and prosecutes complex national and international cases, and focuses exclusively on financial institutions.[3]

In addition, New York state recently has become more active in this area. The New York County District Attorney's Office was a party to each of the three prominent enforcement actions of 2012. In addition, in 2011 the New York State Department of Financial Services was created to regulate New York state-chartered banks and many local branches of foreign banks, as well as other providers of financial services, and this department was out in front of other regulators in the Standard Chartered settlement. New York regulators can reach much of the conduct that federal laws prohibit because New York banking laws require banks to maintain accurate books and records and prohibit the making of false entries and lying to regulators.[4] Any violation can be a ground for revoking a bank's New York state license.[5]

This article will review the 2012 enforcement actions against ING, Standard Chartered, and HSBC, which are powerful examples of how financial institutions are subject to steep penalties not only for knowing violations, but also for ignoring warning signs. Increasingly, prosecutors and regulators are demanding that financial institutions scrutinize their clients' identities, determine who the beneficial parties are, and act vigilantly if there is even a suspicion of an illegal purpose behind a transaction.[6]

ING: Knowing and Willful Conduct

The enforcement actions of the DOJ and the New York County District Attorney's Office against ING Bank, which were settled pursuant to deferred prosecution agreements in June 2012, are illustrative of knowing and willful trade sanctions violations.[7] According to the criminal Information and Factual Statement accompanying the deferred prosecution agreements, for years ING branches in Havana, Curacao, France, Romania and Belgium, as well as the bank's headquarters in the Netherlands, processed transactions through U.S. banks on behalf of clients in Cuba and Iran in circumvention of U.S. sanctions laws and regulations.[8] The bank routinely concealed the fact that sanctioned foreign entities were the true parties in interest by "stripping" potentially identifying information (such as addresses) from payment instructions; bank employees were even threatened with possible termination for revealing sanctioned parties in payment messages. Front accounts, maintained explicitly to enable prohibited transactions, also insured that such transactions would not be questioned and/or blocked by the U.S. banks that cleared the transactions.[9]

The Factual Statement went on to describe how ING's compliance and legal departments were aware of, and sanctioned, much of this conduct. For example, in 2004, when warned internally that the bank should not carry out U.S. dollar transactions from entities in Cuba and Iran, a senior ING attorney responded: "We have been dealing with Cuba…for a lot of years now and I'm pretty sure that we know what we are doing in avoiding any fines."[10]

Under the deferred prosecution agreements, ING was required to pay a total fine of $619 million—half to the DOJ and half to the New York County District Attorney's Office—which was then the largest fine imposed against a financial institution for trade sanctions violations.[11] In addition, ING was required to implement new anti-money laundering policies and procedures, including taking a "risk-based sampling of U.S. dollar payments" to detect any suspect transactions.[12] Because of the bank's extensive cooperation, significant remedial measures, and acceptance of responsibility, the deferred prosecution agreement's term is just 18 months, far less than other recent deferred prosecution agreements entered into by the DOJ. Nevertheless, the fine amount alone sent a powerful message that regulators are serious about sanctions violations in the financial services sector.

Standard Chartered: N.Y. Regulator Steps Up

The Standard Chartered settlement in August 2012 involved allegations similar to those in the ING settlement. This enforcement action was unusual, however, in that New York banking regulators took the lead, threatening to revoke the English bank's New York license because of state law violations.

The order issued by the New York Superintendent of Financial Services described a scheme

whereby Standard Chartered helped financial institutions in Iran that were subject to U.S. sanctions conceal tens of thousands of illegal transactions worth a total of at least $250 billion. Among the subterfuges used by the bank were stripping information from wire transfer messages and replacing the unwanted data with false entries so that the true parties in interest could not be identified. There was even an operating manual providing "step by step wire stripping instructions." As with ING, this conduct was sanctioned and even directed by the bank's legal counsel and top executives.[13]

Faced with the prospect of losing its license to operate in New York, Standard Chartered agreed to pay $340 million to the Department of Financial Services and to hire a monitor for a two-year term to monitor money laundering risk controls at the bank's New York branch.[14] Subsequently, the New York County District Attorney's Office and federal authorities settled with Standard Chartered for an additional $327 million, setting a new combined record of $667 million.[15]

HSBC: Willful Failures in Controls

In July 2012, the U.S. Senate Committee on Homeland Security and Governmental Affairs held hearings entitled "U.S. Vulnerabilities to Money Laundering, Drugs, and Terrorist Financing: HSBC Case History."[16] Though HSBC was accused of some deceptive tactics, the Senate hearing focused in larger part on HSBC's negligence and failure to monitor. For instance, an HSBC branch in Mexico, despite being warned of the presence of drug cartels and the high risk that gangs would seek to move drug proceeds, treated Mexico as a low-risk country and ignored red flags. The branch ultimately transferred more than $7 billion in physical dollars to the United States.[17] In addition, HSBC heedlessly supplied a private Saudi bank, the founder of which was later revealed to be a benefactor of Al Qaeda, with about $1 billion in U.S. dollars,[18] and worked with Bangladeshi banks with links to terrorist financing.[19] Also, HSBC cleared suspicious bulk dollar travelers checks for foreign banks—including $500,000 worth of checks every day, signed with an identical signature—purportedly representing the daily proceeds from two dozen Russian used car dealerships.[20]

Several months after the hearings, the settlement between prosecutors and HSBC continued to focus on the bank's failure to maintain effective money laundering controls. The bank paid $1.26 billion in fines pursuant to a five-year deferred prosecution agreement with the DOJ, as well as civil penalties totaling $665 million to the Office of the Comptroller of the Currency and the Federal Reserve. But what was striking about the settlement was not simply the fine amounts but the emphasis on the bank's *allowing* money laundering to occur—i.e., on omissions rather than affirmative conduct. The bank's violations included failing to implement an adequate anti-money laundering/Bank Secrecy Act program, failing to conduct due diligence on its affiliated financial institutions around the world, including in Mexico, failing to monitor trillions of dollars in wire transfers from customers in countries it classified as "standard" or "medium" risk, and failing to provide adequate staffing and other resources to maintain an effective anti-money laundering program.[21] These "willful failures" were charged criminally under the Bank Secrecy Act in two counts of a four-count Information against HSBC (which will be dismissed if the deferred prosecution agreement's terms are met).[22] Two of the four counts against HSBC, in other words, are predicated on conduct that could be seen a little more than mere negligence. The idea that a "willful failure" to implement a program or monitor or conduct due diligence can be charged criminally is unsettling, and there is a risk that such a theory could be used in cases involving alleged money laundering that is far less widespread than it was in the case of HSBC.

To take an example outside the financial services sector, in October 2012 it was reported that federal prosecutors in Los Angeles were threatening to indict the Las Vegas Sands Corporation on money laundering charges in connection with its casino business.[23] The government's investigation appeared to feature a Chinese narcotics trafficker who was in custody and an electronics executive who, in an unrelated case, had pleaded guilty to a kickback scheme. As to each customer, the issue appeared to be not whether the casino was suspicious but whether it was *suspicious enough*. The casino, meanwhile, argues that it had done nothing wrong and even sent a private investigator to make sure that the alleged narcotics trafficker was a "legitimate businessman."[24] Nevertheless, in late January 2013, *The Wall Street Journal* reported that

in response to government scrutiny, Las Vegas Sands had "stopped executing international money transfers and is overhauling its compliance procedures," including improving its background checks on customers.[25]

What the Future Holds

From the enforcement actions against ING, Standard Chartered and HSBC, three trends are readily identifiable. First and most important, at both the state and federal levels, law enforcement is now focusing on illicit transfers of funds. Last July, David S. Cohen, the Undersecretary for Terrorism and Financial Intelligence at the Treasury Department, noted that terrorists, proliferators, drug lords and organized crime figures all "must, at some point, rely on the financial system to move or launder the funds supporting or derived from their operations."[26] FBI Assistant Director Janice K. Fedarcyk commented: "By cracking down on money laundering, we put teeth in the truism that crime doesn't pay."[27] Messages such as these are backed up by more and more resources targeting the illicit flow of funds.

Second, the government's targets are not limited to intentional violators of the law. Willful failure to comply with AML rules—failure to be alert to and report suspicious transactions, failure to have effective training procedures for staff, failure to keep careful records, and failure to verify customer information—can be grounds not only for government investigation, but also for a criminal charge under the Bank Secrecy Act. The head of the DOJ's Asset Forfeiture and Money Laundering Section recently commented that there will be more complex Bank Secrecy Act cases, not only against banks but also against "the broader spectrum of financial institutions."[28] As the HSBC and Sands cases show, the government will seek to stop not only intentional conduct, but also conduct that borders on negligence.

Third, the laws cast a wide net. Not just large banks and casinos, but smaller businesses as well are subject to the standards of due diligence and accurate reporting; they, too, are expected to act vigilantly when there is any suspicion of an illegal purpose behind a transaction.[29] Particularly given the government's increased resources in this area, it would not be at all surprising to see prosecutors and regulators targeting smaller businesses such as smaller banks and credit unions, registered brokers and dealers, insurance companies, and casinos and other gambling establishments.

In view of the risks, businesses large and small are well-advised proactively to evaluate the strength of their money laundering and OFAC compliance programs and make adjustments and improvements as needed. Given the risks, the cost of implementing or improving a compliance program will be money well spent.

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1. See, e.g., the Bank Secrecy Act (1970), the Money Laundering Control Act of 1986, the U.S. Patriot Act (2001), the Trading with the Enemy Act (1917), the International Emergency Economic Powers Act (1977), and 31 C.F.R. §515.201 ("Transactions involving designated foreign countries or their nationals"). In addition, New York State Penal Law §§175.05 and 175.10 make it a crime to make or cause to be made false entries in business records or to prevent the making of true entries or cause the omission of a true entry, when such conduct is done with the intent to defraud.

2. 18 U.S.C. §1956(a).

3. See Assistant Attorney General Lanny A. Breuer, Keynote Address at Money Laundering Enforcement Conference, Washington, D.C., Oct. 19, 2010, available at www.justice.gov/criminal/pr/speeches; "DOJ targets banks, others in new money laundering offensive," Reuters, Aug. 31, 2012, available at http://www.reuters.com/article/2012/08/31/us-usa-moneylaundering-doj-idUSBRE87U11020120831.

4. NYBL §§200-c, 672.1.

5. NYBL §40.

6. See, e.g., the Bank Secrecy Act §326 (requiring customer identification and verification) and 31 C.F.R. §103.103(18) (requiring the reporting of suspicious transactions).

7. See criminal Information 1:12-cr-00136-PLF (D.C.D.C. June 12, 2012), and accompanying Factual Statement at Exhibit A.

8. Information at ¶¶ 6-7. ING's contemporaneous Settlement Agreement with the Treasury Department, dated June 11, 2012, stated that this activity "had been in place for about 40 years" (¶ 9).

9. Information ¶ 25, Ex. A ¶¶ 20-30, 38-42.

10. Ex. A ¶ 53.

11. Half of the fine went to the New York Country District Attorney's Office and half to the Department of Justice, to settle both state and federal claims.

12. Information ¶¶ 5-6.

13. See Order dated Aug. 6, 2012, ¶¶ 1, 3-4, 7-8, 19-21, 24-29, 30-31, 33-40, 48-49.

14. Press Release, Benjamin M. Lawsky, Superintendent of Financial Services, Aug. 14, 2012.

15. See Dec. 10, 2012 Press Release of New York County District Attorney Cyrus R. Vance Jr., available at http://manhattanda.org/press-release/standard-chartered-bank-reaches-327-million-settlement-illegal-transactions.

16. See Written Statements, July 12, 2012, http://www.senate.gov.

17. Written testimony of Sen. Carl Levin, July 17, 2012; "HSBC to Pay $1.92 Billion to Settle Charge of Money Laundering," *The New York Times*, Dec. 10, 2012, dealbook.nytimes.com; Sen. Tom Coburn Opening Statement, July 17, 2012, pp. 1-2; "HSBC's Mexico nightmare on money laundering," Financial Times, July 18, 2012.

18. Levin testimony, supra note 17, at 4-5.

19. "HSBC investigated for laundering terrorist and cartel money," Examiner.com, July 17, 2012,

20. Levin testimony, supra note 17, at 5.

21. See Attachment A to criminal Information 12-cr-763-JG (E.D.N.Y. Dec. 11, 2012), ¶ 10, 13-15, 25-26. The other two counts charged HSBC with trade sanctions violations.

22. 31 U.S.C. §§5318(h), 5318(i), and 5322(b).

23. Justin Scheck et al., "Sands and U.S. Discuss Deal," *Wall Street Journal*, Oct. 29, 2012, at B1.

24. Id.

25. "Casino Halts Overseas Transfers for High Rollers," *Wall Street Journal*, Jan. 25, 2013, at B1.

26. Testimony of David S. Cohen before Permanent Subcommittee on Investigations, Senate Committee on Homeland Security and Governmental Affairs, July 17, 2012.

27. Department of Justice Press Release, June 14, 2012, "Check Cashers in Brooklyn, Philadelphia and Los Angeles Charged for Alleged Violations of Anti-Money Laundering Laws."

28. Aruna Viswanatha and Brett Wolf, "DOJ targets banks, others in new money laundering offensive," Reuters, Aug. 31, 2012, available at http://www.reuters.com/article/2012/08/31/us-usa-moneylaundering-doj-idUSBRE87U11020120831.

29. 31 U.S.C. §5312(a).

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