The Metropolitan
Corporate Counsel®
National Edition
www.metrocorpcounsel.com
Volume 22, No. 7

July/August 2014

The Bank Secrecy Act: A Trap For The Unwary Businessman

Jeff Kern
Sarah Aberg

Sheppard Mullin Richter & Hampton LLP

Jeff Kern

Sarah Aberg

Introduction

Rising rents, confusing healthcare laws, and competition from mega-chains are not the only challenges confronting small business owners these days. To this list, add the U.S. government. Small businesses that take in large amounts of cash now have to be extra careful how they bank these proceeds thanks to increasingly aggressive enforcement of the Bank Secrecy Act by the Department of Justice.

The Bank Secrecy Act ("BSA") is the common title of the Currency and Foreign Transactions Reporting Act of 1970, which Congress passed to assist federal law enforcement agencies to detect money laundering. It has been amended several times, including in 2001 shortly after the September 11 terrorist attacks through Congress's enactment of the PATRIOT Act. The thrust of the BSA is that it requires domestic financial institutions to assist federal agencies to detect and prevent money laundering. Specifically, the act requires financial institutions to keep records of cash purchases of negotiable instruments, file reports of cash transactions exceeding $10,000, and to report suspicious activity that might signify money laundering, tax evasion, terrorism, narcotics trafficking or currency offenses.

It is the $10,000 threshold that has proven most problematic for some unfortunate business owners. Financial institutions are required to file a currency transaction report ("CTR") with the Internal Revenue Service every time a customer makes deposits or withdrawals in amounts greater than $10,000.[1] In connection with this requirement, banks require customers engaging in such transactions to present identification, answer questions and to remain in the bank while the teller completes the CTR. Bank customers may not "structure" transactions (i.e. break down a single sum of currency exceeding $10,000 into smaller sums) for the purpose of thwarting this reporting process.[2] Hence, the practice of breaking down a single transaction into two or more separate ones to sidestep this requirement is known as "structuring."

While some cash-basis business owners are aware that there is something significant about the $10,000 threshold, they may not completely understand this significance. And for these business owners, not knowing could result in the loss of hard-earned profits, or worse, criminal prosecution and a trip to federal prison.

Caught In A Trap

Take, for instance, the real-life example of the owner of a Broadway ticket brokerage who has a banner weekend, raking in about $24,000 in cash. On Monday morning, after counting his proceeds, he decides to bank only $8,000 because he figures that when the theaters reopen the next day, the high demand for tickets will continue and he will need most of that cash to replenish his stock of choice seats. On Tuesday, to his dismay, the demand doesn't materialize, so he deposits another $8,000, and holds onto the rest, hoping that his prospects will brighten on Wednesday. When the drought continues, he reluctantly deposits the remaining $8,000 Wednesday afternoon. This scenario is typical of the ticket brokerage industry and repeats itself numerous times over the next six months to the point where the broker's "structured" deposits total over $300,000.

Banks typically utilize software and electronic surveillance systems that flag deposit patterns such as this one that suggest that the depositor is deliberately avoiding the reporting requirements attendant to the $10,000 threshold. Eventually, if enough of these deposits are flagged, the bank is required under the BSA to file a Suspicious Activity Report or "SAR" with

***Jeff Kern** is Special Counsel in the firm's White Collar Defense and Corporate Investigations Practice. His practice encompasses securities regulation, compliance, and litigation as well as internal investigations and white collar defense. He represents broker-dealers and associated individuals who are the focus of SEC, FINRA and other regulatory investigations as well as individuals accused of fraud, money laundering, tax evasion and other financial crimes. He has particular expertise with SRO litigation, internal investigations and investigative testimony. **Sarah Aberg** is an Associate in the firm's White Collar Defense and Corporate Investigations Practice Group. Her practice encompasses financial and securities regulation, focusing on compliance, internal investigations, civil enforcement proceedings and white collar defense. She represents global and local financial institutions, securities dealers and associated individuals defending investigations and litigations by DOJ, SEC, FINRA and state and local regulators and prosecutors. **Christopher Bosch,** a third-year student at Fordham Law School, assisted in the preparation of this article.*

Please email the authors at jkern@sheppardmullin.com or saberg@sheppardmullin.com with questions about this article.

the government disclosing the deposit pattern. The SAR could end up triggering an investigation by a local U.S. Attorney's Office.

To the assistant U.S. attorney tasked with reviewing the ticket broker's banking activity, the deposits made during the six-month period look like a textbook case of structuring. At this point, she has no insight into what motivated the series of sub-$10,000 deposits. All she has to go on are bank records that strongly suggest that the ticket broker was consciously trying to avoid making deposits that exceeded this amount. As a result, an AUSA in this situation may move forward with obtaining a seizure order for these proceeds and initiating a civil forfeiture action or worse, conducting a full-fledged criminal investigation.

Whether pursued civilly or criminally, structuring consists of three distinct elements: the defendant (1) engaged in acts of structuring (such as breaking down a single sum of currency exceeding $10,000 into smaller sums and depositing those smaller sums with a bank so that the bank's reporting obligation is not triggered); (2) with knowledge that the financial institution(s) involved were legally obligated to report currency transactions in excess of $10,000; and (3) with the intent to evade these reporting requirements.[3] In a civil forfeiture proceeding, the government's burden of proof is by a preponderance of the evidence while in a criminal prosecution the threshold is the familiar proof beyond a reasonable doubt.[4]

In our ticket brokerage example, the owner broke up his deposits for legitimate business reasons, and thus the government would not be able to establish the third element, involving intent to evade the subject reporting obligation. However, because the government has no knowledge of the depositor's intent, it would likely proceed on the presumption that the structuring was done for illicit purposes. In fact, the government can file a facially sufficient complaint by taking advantage of favorable case law that allows it to make out the intent element by demonstrating the defendant engaged in a pattern of "structuring" conduct.[5] Later, if there is a civil or criminal trial, the government can rely on the same presumption in order to prevail in its forfeiture action or secure a conviction. In effect, this case law obviates the need to establish the element of intent and renders structuring a strict liability offense.

In our example, the fact that the ticket broker was not acting to avoid the subject reporting requirements is initially immaterial because the first opportunity he will have to proclaim his innocence is well after the AUSA has obtained a seizure order from a federal magistrate, has served it on the bank, and has taken control of the funds on behalf of the government under the Civil Asset Forfeiture Reform Act of 2000 (CAFRA) (effective August 23, 2000, codified at 18 U.S.C. § 983 *et seq.*). CAFRA covers administrative and judicial forfeitures under all civil forfeiture provisions of federal law and provides the government with the authority to address the structuring activity even before it is required to prove a single element of the offense. Under CAFRA, if the government believes a person or a business has structured transactions in violation of 31 U.S.C. § 5324, it can seize any assets involved in the transactions and any property traceable to the violation on the mere suspicion of structuring.[6] It need only demonstrate probable cause to obtain the seizure warrant and gain control of the structured funds.[7]

This means, as set forth above, that the government can seize assets without the defendant's knowledge. Often, the first time a defendant learns of the seizure is when a federal law enforcement agent comes to the business to serve the defendant with a copy of the seizure order and to extract damning statements about the reasons for the structured deposits. The hope is to provide the assigned AUSA with firsthand evidence that will make it even easier to establish illicit intent. In our example, the ticket broker explained to the field agent that while he was aware that "forms had to be filled out" in connection with large deposits, he was not aware that it was illegal to make smaller deposits. The AUSA later claimed that this statement was proof of the broker's intent to evade the reporting requirement.

Our ticket brokerage example involves the straightforward situation of the business owner himself making the deposits at issue. But consider another variation on the structuring theme. On an April morning in 2012, another small business owner is starting his day's work in his Los Angeles-based wholesale apparel company while three thousand miles away, a suspected drug-money launderer is arrested in Englewood, New Jersey during a traffic stop. Though the suspected money launderer and business owner have never met, and the business owner has never been involved in narcotics trafficking or any other criminal activity, the business owner's fortunes are about to be inextricably tied to those of the suspect.

Like many other clothing entrepreneurs, the owner of the apparel business primarily conducts his business in cash. To facilitate collections, he permits some of his customers to pay invoices by making cash deposits directly into his company's bank account. The business owner reconciles these deposits to outstanding invoices, paying little attention to anything beyond ensuring the payments matched the invoices. Therefore, when he noticed a $8,162 cash deposit into his company's account, he marked the corresponding invoice as "paid" and did not give it any additional thought.

Unfortunately for the business owner, a bank receipt reflecting a $8,162 deposit to a Manhattan bank the day before was found in the suspect's car. The name of the apparel business was written at the top of the receipt because, unbeknownst to the owner, his customer had traded the invoice, and the debt it represented, with the suspected money-launderer in a so-called black market peso exchange.[8] Based solely on this single deposit, the government persuaded a federal magistrate to issue a seizure warrant for *every* cash deposit made into the business owner's bank account between May 2011 and May 2012[9] in all, $425,000 of the business owner's money. The government's theory: because every cash deposit into the account was less than $10,000, the deposits were structured and were thus subject to forfeiture, notwithstanding that each deposit matched a paid invoice. Imagine the bewilderment of the clothing merchant when he learned that $425,000 of his hard-earned money was seized by a prosecutor at the opposite end of the continent based on the arrest of someone he had never met.

Both these examples reflect the increasingly aggressive and enterprising approach taken by the Justice Department with respect to the BSA. In the first example, it was the U.S. Attorney for the Eastern District of New York that initiated the seizure despite the fact that the ticket broker was located in Manhattan, all the subject deposits took place in Manhattan and the broker had never transacted any business within the geography comprising the Eastern District. The U.S. Attorney's Office claimed jurisdiction over the funds based on the fact that the broker's bank had branches in Brooklyn. In the second example, it was the U.S. Attorney for the District of New Jersey that made the seizure, even though the business and its bank was based in Los Angeles and the deposit occurred in Manhattan. Here, the claim of jurisdiction was based on the recovery of the deposit slip in New Jersey. Thus, in both examples, neighboring prosecutor's offices used expansive and self-serving jurisdictional interpretations to take for themselves a revenue-generating case that, by logic and common sense, should have been the rightful prosecutorial province of the Manhattan U.S. Attorney's Office.

Under CAFRA, the government is permitted to keep the assets it successfully forfeits.[10] This feature provides a concrete incentive for the government to seize and forfeit as many assets as possible, a mission made easier by CAFRA's expansive provisions and the favorable treatment accorded these provisions by courts called upon to interpret them. The Justice Department has not been shy about leveraging the advantages provided by CAFRA. More and more U.S. Attorney's offices are setting up specialized civil forfeiture units, often staffing them with retired IRS agents working on a contract basis. This allocation of resources is paying off handsomely. In 2013 alone, the government seized over $2 billion in cash and assets as a result of its forfeiture efforts.[11] This amount has grown steadily since 2001, when the amount seized was approximately $439 million.[12]

The funds successfully forfeited to the government are deposited into the Asset Forfeiture Fund ("AFF"). The Justice Department uses the AFF to cover the operating costs of the Asset Forfeiture Program ("AFP"). These costs include

> asset management and disposition expenses; equitable sharing payments to participating state, local, and foreign governments; Automatic Data Processing (ADP) equipment expenses; contract service payments; and payments of innocent third-party claims. All salaries and employment related expenses, liabilities, and imputed financing costs of DOJ AFP participants are reported in the financial statements of the participants' reporting entities. Salaries and employment related costs of administrative personnel of the AFMS [the Asset Forfeiture Management Staff], AFMLS [the Asset Forfeiture and Money Laundering Section, Criminal Division], EOUSA [the Executive Office for United States Attorneys], and USMS [the United States Marshals Service] are charged to the AFP as program operating costs.[13]

In addition to covering the operating costs of the AFP, Justice is also permitted to distribute AFF assets such as vehicles, electronic equipment and machinery to state and local law enforcement. In 2013, the value of these distributed assets was over $5 million. There is little limitation on how the federal government may use these funds, and in fact the Department of Justice itself has stated that the attorney general "has complete authority to dispose of forfeited property . . . however he or she deems suitable."[14]

Given that administrative costs and salaries for employees, attorney and marshal services are paid directly from the fund, a steady increase in seized and forfeited funds is not surprising – especially in the current fiscal climate. Justice has implicitly communicated its encouragement of the practice as reflected in the most recent version of the Asset Forfeiture Policy Manual.[15] The 2012 version of the manual stresses the importance of exercising restraint in seizing property of an ongoing business, while the 2013 version does not.[16] Indeed, the latest version of the manual explicitly encourages the use of asset forfeiture as "one of the most effective weapons in the law enforcement arsenal."[17] While there can be little doubt that forfeiture is indeed an effective and legitimate law enforcement tool, what is equally undisputed is that the government has created a business model out of its forfeiture powers and is utilizing that model to create revenue streams to finance its operations.

A Rock And A Hard Place

This development was evident in the two examples discussed above. In both cases, the U.S. Attorney's Office followed up the seizure by filing a civil forfeiture action in federal district court to gain permanent control of the seized funds. Once the government filed the civil complaint, both defendants were faced with the choice of either litigating against the government or negotiating a settlement. For defendants in this situation, this choice is fraught with difficulty because, unlike most other civil defendants, the target of a civil forfeiture action has already been separated from his property. Thus, the defendant must simultaneously go on the offensive to recover his money from the government while maintaining a defensive posture with respect to the government's allegations.

The primary instinct of a truly innocent business owner in this situation would be to right the wrong that has been perpetuated against him by his own government and aggressively pursue the return of his property. But doing so is often a high-risk/low-return proposition. Because this is civil litigation, the defendant is required to file an answer to the government's complaint in order to receive his day in court. Filing an answer means committing to a specific version of events that the government could use in a subsequent criminal case or to develop investigative leads. In that connection, not resolving the case through a quick settlement may cause the government to intensify its investigation which, in turn, may entail interviews with customers, bank employees, competitors, neighbors and family members. Worse, further investigation by the government may lead to a grand jury presentation and a subsequent indictment. In addition, the costs to mount a defense are likely to quickly add up precisely when cash shortfalls are already an issue due to the initial seizure. The risk that funds will never be recouped is extremely high.

Litigating against the government does have potential upsides, particularly for the innocent business owner who has the ability to provide legitimate rationales for his deposit practices at trial. Theoretically, this ability would thwart the government's efforts to carry its burden of proof and would result in the return of the seized funds. However, getting to that point is not easy. Among other things, it entails the expenditure of substantial attorney fees and related litigation costs that would substantially dilute the value of any subsequent recovery. Moreover, given the typically slow pace of litigation, it could take several years for the case to go to trial, during which time the defendant will be without the use of any of the seized funds.

Lesser Of Two Evils

In light of these considerations, the two business owners in our examples, like most similarly situated defendants, elected to put aside their indignation and enter into settlement negotiations with the U.S. Attorney's Office. The dynamics for these negotiations are rarely favorable for the defendant business owner. The longer the negotiations drag on, the more expensive they become and the more these costs eat into any subsequent recovery. Similarly, the longer the negotiations, the longer the business owner is without the benefit of the seized funds. AUSAs handling forfeiture actions are acutely aware of these dynamics and, knowing that business owners are anxious to get their money back and are rapidly incurring legal bills, are typically content to sit back and wait for defendants to cry uncle and agree to permanently surrender a large portion of the seized funds.

That's essentially what happened to the ticket broker and clothing entrepreneur. In both cases, the assigned prosecutors were unmoved by evidence that each business owner had acted without intent to violate the BSA and in accordance with legitimate business needs. Instead, they both held their cards close to the vest, insisted that the business owners had only themselves to blame, and stated that if they did not want to accept the government's settlement offers, they were welcome to roll the dice at trial. While counsel for both managed to substantially reduce the amount of money demanded by the government, eventually both business owners became worn down financially and emotionally and elected to

resolve the forfeiture action by forking over profits that had been rightfully earned.

Best Practices

Suffice it to say, becoming ensnared in a government structuring case is not good for business. In this context, as in other precincts of life, an ounce of prevention is worth a pound of cure. Counsel with small business clients would do well to advise the following:

Self-Education: The first thing a business owner should do is educate himself with respect to the core requirements of the BSA. As stated above, it's not enough just to know that $10,000 is a significant threshold. A business owner should know that breaking down deposits (or withdrawals for that matter) in increments of less than $10,000, if done enough times, will eventually draw the government's scrutiny. The FINCEN link on the U.S. Treasury Department website is good place to start: http://www.fincen.gov/statutes_regs/bsa/.

Engage the Bank: Banks are also fertile sources of information. In fact, when opening an account at a new bank, business owners should ask to meet with the branch management. During this meeting, the owner should educate bank staff about the nature of the business, cash flow, banking habits, and any potential issues that may arise with respect to its cash operations. This show of transparency will likely make bank staff less suspicious should an unusual situation arise and, therefore, less likely to file a SAR. The owner should also ask questions about what the bank's reporting obligations are, how the bank goes about satisfying these obligations, and to provide any other information that will help the owner stay compliant with the law.

Exercise Good Judgment: If there's a choice between making a deposit over $10,000 or breaking down the cash on hand into smaller increments, business owners should always err on the side of the former, even if it means having to take the extra time to complete the required forms and exposing some personal or business information to bank staff. Foregoing a little privacy is better than forfeiting a lot of money.

Plan Ahead: If there does come a time when a business owner needs to make structured deposits for valid business reasons, he or she should discuss this need with branch management and request that the bank document that the discussion took place. In addition, the business owner should also memorialize the rationale for making structured deposits and keep reliable records of the cash flow related to the deposits so as to be able to justify the deposit activity if called upon later.

Speak No Evil: In the unlikely event that a federal agent shows up to ask questions about a business's banking, business owners should resist the impulse to explain their conduct in the hope that the government will return any seized funds. Instead, they should politely decline to answer any questions, request the agent's business card, and tell him or her that counsel will be in contact.

Conclusion

The BSA is a comprehensive legislative scheme that imposes various reporting requirements on financial institutions and their customers. While the thrust of the BSA is to combat money laundering, drug trafficking, terrorism, and tax evasion, it often ensnares unsuspecting business owners unfamiliar with its reporting requirements and its proscription on structuring. Due to the vigorous enforcement of the BSA by an enterprising and resource-challenged federal government enamored of its powerful seizure tools, these business owners are often forced to relinquish legitimately earned profits in order to extricate themselves from the government's vise. The best way for business owners to avoid this plight is to become fluent in the BSA's reporting requirements and proactively address situations where business needs or efficiency require bank deposits in amounts less than $10,000.

---

1. *See* 31 U.S.C. § 5313(a); 31 C.F.R. §§ 1010.306, 1010.311.

2. *See* 31 U.S.C. § 5324(a)(3).

3. *See, e.g., United States v. MacPherson*, 424 F.3d 183, 189 (2d Cir. 2005); *United States v. Sutton*, 387 F. App'x 595 (6th Cir. 2010). Note that the statute directs that a person must structure the transactions for the purpose of evading the specific reporting requirements of 31 U.S.C. § 5313(a). *See* 31 U.S.C. § 5324(a); *Dollar Bank Money Market Account No. 1591768456*, 980 F.2d 233, 237 (3d Cir. 1992).

4. 18 U.S.C. § 983(c)(1).

5. *See MacPherson*, 424 F.3d at 190-93, 195.

6. 31 U.S.C. § 5317(c)(2); 18 U.S.C. § 981(a)(1)(A).

7. *See* 18 U.S.C. § 981(b)(2); Fed R. Crim. P. 41(d). Sometimes, not even a warrant is required, as the statute permits seizure without a warrant if (1) there is probable cause to believe the property is subject to forfeiture and (a) it is seized pursuant to a lawful arrest or search, or (b) a Fourth Amendment warrant requirement exception applies, or (2) the property was lawfully seized by a state or local law enforcement agency and transferred to a federal agency. *See* 18 U.S.C. § 981(b)(2)(B)-(C).

8. Drug traffickers often use black market peso exchanges to launder narcotics proceeds. The traffickers convert proceeds from their drug sales (accumulated in U.S. dollars) into pesos by "selling" the dollars to businesses that import U.S. goods. The exchange is attractive to the businesses because the peso-dollar exchange rate is much cheaper than a bank's rate of exchange.

9. There was no explanation as to why this particular period was chosen; however, it could very well be indicative of the government's desire to simply keep the proceeds, because they have one year from the date of the offense to seize fungible assets related to the office (i.e. cash), otherwise the cash must be directly traceable to the offense. *See* 18 U.S.C. § 984.

10. Marian R. Williams et al., "Policing for Profit: The Abuse of Civil Asset Forfeiture" 6 (2010), *available at* http://www.ij.org/images/pdf_folder/other_pubs/assetforfeituretoemail.pdf.

11. U.S. Dep't of Justice, Total Net Deposits to the Fund by State of Deposit as of September 30, 2013, http://www.justice.gov/jmd/afp/02fundreport/2013affr/report1.htm.

12. *See* historic reports on the United States Department of Justice website, available at *Historic Reports: Annual Report of the Department of Justice Asset Forfeiture Program*, U.S. Dep't of Justice, http://www.justice.gov/jmd/afp/02fundreport/HistoricReports.htm (last updated January 2014); *Reports to Congress*, U.S. Dep't of Justice, http://www.justice.gov/jmd/afp/02fundreport/index.htm (last updated January 2014). There was a spike to $4.2 billion in 2012 due to five major fraud cases resulting in "extraordinary forfeiture income of $3,311.9 million." Office of the Inspector Gen. Audit Div., U.S. Dep't of Justice, Asset Forfeiture Fund and Seized Asset Deposit Fund Annual Financial Statements Fiscal Year 2012, at 6 (2013), http://www.justice.gov/oig/reports/2013/a1307.pdf.

13. Office of the Inspector Gen. Audit Div., U.S. Dep't of Justice, Audit of the Assets Forfeiture Fund and Seized Asset Deposit Fund Annual Financial Statements Fiscal Year 2013, at 4 (2014), http://www.justice.gov/oig/reports/2014/a1408.pdf.

14. Criminal Div. Asset Forfeiture and Money Laundering Section, U.S. Dep't of Justice, Asset Forfeiture Policy Manual 2013, at 96 (2014), http://www.justice.gov/criminal/afmls/pubs/pdf/policy-manual-2013rev.pdf.

15. The DOJ publishes annual updates of the Manual.

16. Specifically, the 2012 version states that "AFMLS and the USMS recommend restraining a business in the least restrictive manner needed to preserve the Government's interest. Seizure of a business, and operation or closure of the business by the Government, should only be carried out where all other options have been considered and rejected." U.S. Department of Justice, Criminal Division, Asset Forfeiture and Money Laundering Section Asset Forfeiture Policy Manual 2012 8, http://www.justice.gov/criminal/afmls/pubs/pdf/pm-2012.pdf. This cautionary language has been deleted from the 2013 version of the Manual.

17. U.S. Department of Justice, Criminal Division, Asset Forfeiture and Money Laundering Section Asset Forfeiture Policy Manual 2013 42, http://www.justice.gov/criminal/afmls/pubs/pdf/policy-manual-2013rev.pdf.