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# Jimmy Gurule delivered the keynote address at the Korea Banking Risk Dialogue 2014 in Seoul, South Korea on July 2

Jimmy Gurule

*Notre Dame Law School*, [Jimmy.Gurule.1@nd.edu](mailto:Jimmy.Gurule.1@nd.edu)

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**THE U.S. CRIMINAL PROSECUTION OF BNP PARIABAS AND THE IMPLICATIONS FOR ASIA**  
**Professor J. Gurule**  
**Korea Banking Risk Dialogue 2014**  
**July 2, 2014**

The Obama administration has taken an aggressive posture regarding the imposition of sanctions against banks for non-compliance with U.S. economic sanctions and bank secrecy laws. Since 2009, at least 21 banks have entered into deferred prosecution agreements (DPAs) with the U.S. Department of Justice (DOJ) and penalized approximately \$4.9 billion for doing business with countries sanctioned by the United States including Iran, Sudan, Syria, Myanmar, and Cuba. Further, the monetary penalties imposed against eight of these banks were in the hundreds of millions of dollars, with HSBC topping the list with a \$1.9 billion penalty. However, the stakes have been raised even higher as the result of recent action by the U.S. Department of Justice (DOJ) to criminally prosecute BNP Paribas, France's largest bank, for violating U.S. economic sanctions, signaling a fundamental policy shift away from entering into DPAs with offending banks.

**(A) Deferred Prosecution Agreements**

Despite being aware of the ban on providing financial services to Iran, Lloyds, Credit Suisse, Barclays Bank, ABN Amro, ING, Standard Chartered, and HSBC Group admitted to willfully violating the International Emergency Economic Powers Act ("IEEPA") and the Trading with the Enemy Act ("TWEA") by facilitating financial transactions on behalf of Iran as well as other sanctioned countries and entities.<sup>1</sup>

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<sup>1</sup> See Deferred Prosecution Agreement, United States v. Lloyds TSB Bank, No. CR-09-007 (D.D.C. Jan. 9, 2009) (agreed to pay a \$350 million penalty); Deferred Prosecution Agreement, United States v. Credit Suisse AG, No. CR-09-352 (D.D.C. Dec. 16, 2009) (agreed to pay a \$536 million penalty); Deferred Prosecution Agreement, United States v. Barclays Bank PLC, No. CR 10-218 (D.D.C. Aug. 16, 2010) (agreed to pay a \$298 million penalty); Deferred Prosecution Agreement, United States v. ABN AMRO Bank, N.V., No. CR 10-124 (D.D.C. May 10, 2010) (agreed to pay a \$500 million penalty); Deferred Prosecution Agreement, United States v. ING Bank, N.V., No. CR 12-136 (D.D.C. June 12, 2012) (agreed to pay a \$619 million penalty); Deferred Prosecution Agreement, United States v. Standard Chartered Bank, No. CR 12-1467 (D.D.C. Dec. 10, 2012) (agreed to forfeit \$227 million to the DOJ as well as a \$100 million civil penalty); Deferred Prosecution Agreement, United States v. HSBC Bank USA, No. CR 12-763 (E.D.N.Y. Dec. 12, 2012) (agreed to pay \$1.9 billion penalty). The deferred prosecution agreements also alleged that the banks provided banking services to other sanctioned countries, including Cuba, Libya, Sudan, and Burma.

Most recently, the Treasury Department sanctioned Clearstream Banking, a Luxembourg bank, for doing business with Iran.<sup>2</sup> In the case of the HSBC Group, the bank:

knowingly and willfully engaged in practices outside the United States that caused HSBC Bank USA and other U.S. financial institutions to process payments on behalf of banks and other entities located in Cuba, Iran, Libya, Sudan, and Burma, in violation of U.S. sanctions. HSBC Group Affiliates ensured that these transactions went undetected in the U.S. by altering and routing payment messages in a manner that hid the identities of these sanctioned entities from HSBC Bank USA and other U.S. financial institutions. The total value of these transactions during this period was approximately \$660 million.<sup>3</sup>

In each case the offending banks were permitted to enter into a deferred prosecution agreement in which the DOJ agreed not to pursue criminal prosecution in exchange for the payment of a fine and a promise from the bank to comply with existing federal regulations that prohibit doing business with Iran and other sanctioned countries. The larger monetary penalties assessed by the DOJ ranged from approximately \$300 million to \$1.9 billion.

It should be noted, however, that bank misconduct has not been limited to non-compliance with U.S. economic sanctions. For example, between 2006 and 2010, HSBC Bank USA violated the BSA and implementing regulations by “ignor[ing] the money laundering risks associated with doing business with certain Mexican customers and fail[ing] to implement a BSA/AML program that was adequate to monitor suspicious transactions from Mexico.”<sup>4</sup> Moreover, HSBC Mexico had their own AML failures, resulting in “at least \$881 million in drug trafficking proceeds, including proceeds of drug trafficking by the Sinaloa Cartel in Mexico and the Notre del Valle Cartel in Colombia . . . laundered through HSBC

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<sup>2</sup> See also Press Release, U.S. Treasury Dep’t, *Treasury Department Reaches Landmark \$152 Million Settlement with Clearstream Banking* (Jan. 23, 2014) available at <http://www.treasury.gov/press-center/press-releases/Pages/jl2264.aspx>.

<sup>3</sup> Memorandum and Order, *U.S. v. HSBC Bank USA, N.A., et al.*, 2013 WL 3306161 (E.D.N.Y. July 1, 2013).

<sup>4</sup> United States v. HSBC Bank USA, Case No. 1:12-cr-00763-ILG, Document 3-3, ¶ 61 (E.D.N.Y. Dec. 11, 2012), available at <http://www.justice.gov/opa/documents/hsbc/dpa-attachment-a.pdf>.

Bank USA without being detected.”<sup>5</sup> The bank’s behavior was made even more egregious by HSBC Holdings, the parent company, admitting that it “was aware of the significant compliance problems at HSBC Mexico, yet did not inform HSBC Bank USA of these problems and their impact on HSBC Bank USA’s AML program.”<sup>6</sup>

The AML compliance program at HSBC Bank USA was deficient in several ways. First, the bank engaged in correspondent banking, which is considered “high risk,” “because the U.S. bank does not have a direct relationship with, and therefore has no diligence information on, the foreign financial institution’s customers who initiated the wire transfers.”<sup>7</sup> Because of this high risk, the BSA imposes a duty of due diligence for all foreign financial institutions. However, HSBC Bank USA failed to conduct this due diligence, which was memorialized in a formal policy set forth in the bank’s AML Procedures Manual.<sup>8</sup> Second, HSBC Bank USA also failed to adequately monitor wire transfers from Mexico correspondent accounts. The bank had an internal Customer Account Monitoring Program (“CAMP”) for categorizing foreign countries based on the perceived risk of money laundering originating in those countries.<sup>9</sup> However, despite numerous warnings about the serious risks associated with Mexican correspondent accounts, HSBC Bank USA “rated Mexico as standard risk, its lowest AML category.”<sup>10</sup> As the result, more than 316,000 financial transactions that were worth more than \$670 billion were excluded from monitoring from HSBC Mexico.<sup>11</sup>

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<sup>5</sup> *Id.* at ¶ 9.

<sup>6</sup> *Id.*

<sup>7</sup> *Id.* at ¶ 13.

<sup>8</sup> *Id.* at ¶ 15.

<sup>9</sup> *Id.* at ¶ 16.

<sup>10</sup> *Id.* at ¶ 18-19.

<sup>11</sup> *Id.* at ¶ 19.

Additionally, HSBC Mexico's CEO was told by Mexico's financial intelligence unit that Mexican law enforcement possessed credible evidence of a Mexican drug lord saying that "HSBC Mexico was the place to launder money."<sup>12</sup> In fact, by 2008, "drug traffickers [had] designed specially shaped boxes that fit the precise dimensions of the teller windows" to enable them to make large deposits of bulk cash with the bank.<sup>13</sup> HSBC Group knew of these problems, but failed to inform HSBC Bank USA or warn them to increase compliance monitoring of certain wire transfers.<sup>14</sup> Ultimately, approximately \$881 million in illicit drug proceeds were laundered through the U.S. financial system because of HSBC's AML violations, which resulted in the imposition of a \$1.9 billion penalty.

Other prominent global banks have been implicated in large-scale schemes to facilitate the laundering of criminal proceeds. In January 2014, almost a year after the HSBC settlement, JP Morgan Chase was penalized over \$2 billion for turning a blind eye to the Ponzi scheme run by Bernard L. Madoff.<sup>15</sup> The bank served as Madoff's primary bank for more than two decades. The Ponzi scheme was conducted almost exclusively through various accounts held at JP Morgan Chase. On two occasions, in 2007 and 2008, JP Morgan's own computer system raised "red flags" about Madoff's transactions, but both times, JP Morgan's employees "closed the alerts."<sup>16</sup> In October 2008, JP Morgan alerted authorities in Britain to concerns that Madoff's investment returns were "so consistently and significantly ahead of its peers" that the results "appear too good to be true."<sup>17</sup> However, JP Morgan

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<sup>12</sup> *Id.* at ¶ 37.

<sup>13</sup> *Id.* at ¶ 50.

<sup>14</sup> *Id.* at ¶ 44.

<sup>15</sup> Deferred Prosecution Agreement, United States v. JP Morgan Chase Bank, N.V., No. 14-cr-00007 (S.D.N.Y. Jan. 8, 2014).

<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

never reported a similar warning to the Treasury Department, a violation of the BSA.<sup>18</sup> As the result of JP Morgan’s failure to carry out its AML obligations and “repeatedly” ignoring warning signs of money laundering, Madoff was able to launder billions of dollars in Ponzi proceeds. Ultimately, the Department of Justice imposed a \$1.7 billion penalty against the bank stemming from two felony violations of the BSA for failing to alert authorities to suspicious financial transactions.<sup>19</sup> The bank also agreed to pay \$350 million to the Office of the Comptroller of the Currency.<sup>20</sup>

### **(B) Fundamental Shift in DOJ Policy**

Despite the imposition of hefty monetary penalties for violations of the BSA and economic sanctions there has been strong vocal criticism of the DOJ for failing to shut down the offending banks or charge any bank official with criminal wrongdoing. At a Senate Banking Committee hearing last year, Senator Elizabeth Warren grilled two federal regulators on whether banks and bank officials should face more severe penalties. Senator Warren stated:

The U.S. government takes money laundering very seriously for a good reason. And it puts strong penalties in place. . . . It’s possible to shut down a bank . . . . Individuals can be banned from ever participating in financial services again. And people can be sent to prison. In December, HSBC admitted to . . . laundering \$881 million that we know of . . . . They didn’t do it just one time . . . . They did it over and over and over again . . . . They were caught doing it. Now, HSBC paid a fine, but no individual went to trial. No individual was banned from banking and there was no hearing to consider shutting down HSBC’s activities in the U.S. . . . . You’re the experts on money laundering. I’d like your opinion. What does it take? How many billions of dollars do you have to launder for drug lords and how many sanctions do you have to violate before someone will consider shutting down a financial institution like this?<sup>21</sup>

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<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> Patterns of Abuse: Assessing Bank Secrecy Act Compliance and Enforcement, Hearing before the S. Comm. on Banking, Hous. & Urb. Aff., 113<sup>th</sup> Cong. (2014) (statement of Sen. Elizabeth Warren).

Senator Warren proceeded to explain the injustice of the situation. She stated that “[i]f you’re caught with an ounce of cocaine, you’re going to jail . . . . But if you launder nearly a billion dollars for international cartels and violate sanctions you pay a fine and you go home and sleep in your bed at night.”<sup>22</sup>

Similar sentiments were expressed by U.S. District Court Judge Jed S. Rakoff, rejecting the so-called “too big to jail” excuse for not prosecuting banks implicated in money laundering and related financial crimes. “To a federal judge, who takes an oath to apply the law equally to rich and to poor, this excuse—sometimes labeled the ‘too big to jail’ excuse—is disturbing, frankly, in what it says about the [Department of Justice’s] apparent disregard for equality under the law.”<sup>23</sup> Further, foreshadowing possible criminal charges against banking giants Credit Suisse and BNP Paribas, France’s largest bank, Attorney General Eric Holder offered an ominous warning, stating, “There is no such thing as too big to jail.”<sup>24</sup> He further stated:

Some have used that phrase to describe the theory that certain financial institutions, even if they engage in criminal misconduct, should be considered immune from prosecution due to their sheer size and their influence on the economy. That view is mistaken. And is a view that has been rejected by the Department of Justice.<sup>25</sup>

Preet Bharara, the U.S. Attorney in Manhattan, has also signaled a change in course away from DPAs, opening a criminal investigation into fraud at Citigroup’s Mexican affiliate and other American banks. In a recent speech, Mr. Bharara warned, “You can expect that before too long a significant financial institution will be charged with a felony or be made to plead guilty to a felony, where the

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<sup>22</sup> *Id.*

<sup>23</sup> Judge Jed S. Rakoff, *Why Have No High Level Executives Been Prosecuted in Connection with the Financial Crisis?* (Nov. 12, 2013), available at <http://www.nybooks.com/articles/archives/2014/jan/09/financial-crisis-why-no-executive-prosecutions/?pagination=false>.

<sup>24</sup> Kevin Johnson, *U.S. to Banks: “No such thing as too big to jail,”* USA Today (May 5, 2014).

<sup>25</sup> *Id.*

conduct warrants it.”<sup>26</sup> Finally, if the Department of Justice is intent on prosecuting banks, rejecting the notion that some banks are “too big to jail,” there is good reason to believe that the criminal prosecution of banks officials who engaged in willful blindness and permitted the bank to be used to facilitate money laundering and violate economic sanctions is likely forthcoming.

On June 30, 2014, BNP Paribas entered a plea agreement with the DOJ admitting to violating IEEPA and TWEA, and agreed to pay a \$8.9 billion fine for willfully violating U.S. economic sanctions with Iran. The size of the fine against BNP is unprecedented and almost five times the size of the fine imposed against HSBC. Further, pursuant to the plea agreement the French bank is banned from clearing U.S. dollar transactions for its clients for one year. The restriction on BNP’s ability to conduct financial services in the U.S. is also unprecedented. Additionally, since the pending DOJ investigation was revealed in February 2014, the bank’s market value has dropped by 15 percent, erasing around 11 billion euros (\$15 billion).

### **(C) The SAR Reporting Requirement<sup>27</sup>**

The critical question raised by the DOJ’s fundamental shift in its bank secrecy enforcement policy is what can banks do to avoid either the imposition of a hefty monetary penalty or criminal prosecution? The failure to file SARs, or file them on a timely basis, is the “Achilles heel” of bank AML compliance programs. Virtually every bank that that has been sanctioned by the Financial Crimes Enforcement Network (“FinCEN”) or the DOJ for violations of the BSA or economic sanctions has been penalized for failing to file SARs. In the Iranian economic sanctions cases, the offending banks stripped the identifier information from electronic funds transfers eliminating any reference to Iran or Iranian-controlled entities to prevent U.S.-based banks from freezing those transactions and filing SARs. In the

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<sup>26</sup> *Id.*

<sup>27</sup> The discussion of the SAR reporting requirement is taken in large part from Jimmy Gurule, UNFUNDING TERROR: THE LEGAL RESPONSE TO THE GLOBAL THREAT OF TERRORISM, 156-59 (2008).



other cases, the failure to file SARs was not merely negligent or inadvertent, but under circumstances demonstrating a blatant disregard of or indifference to the legal duty imposed on banks to file SARs. Moreover, these banks were not sanctioned for failing to file a SAR for every possible suspicious transaction. The BSA does not impose such an onerous obligation. Instead, these cases were extreme and egregious in nature and revealed a lack of minimum standards due diligence. In short, these banks were penalized for not undertaking their legal duty and obligation to detect and report suspicious transactions in a serious and responsible manner.

The centerpiece of the federal regulatory regime established by the BSA, and amended by the USA PATRIOT Act, is the requirement that financial institutions establish, implement, and maintain a program to detect and prevent money laundering and terrorist financing. More specifically, the BSA imposes a legal duty on financial institutions to establish an AML/CTF program that includes the following minimum requirements: “(A) the development of internal policies, procedures and internal controls, (B) the designation of a compliance officer, (C) an ongoing employee training program, and (D) an independent audit function to test programs.”<sup>28</sup> The internal policies and procedures should be based upon an assessment of money laundering and terrorist financing risks associated with services offered and customers and geographic areas served. For example, the AML/CTF program should analyze the extent to which the bank customer conducts financial transactions in jurisdictions that have been identified as posing a high risk of money laundering or terrorist financing. The risk-based program should also consider whether certain customers and accounts, such as correspondent accounts, pose a heightened risk of money laundering and terrorist financing.

The AML/CTF plan also should establish written policies and procedures for identifying and reporting SARs. The SAR filing requirements impose an obligation on financial institutions to report

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<sup>28</sup> 31 U.S.C. § 5318(h)(1) (2000 & Supp. I 2004); *see also* 12 C.R.F. § 326.8(c).

transactions that the institution “knows, suspects, or has reason to suspect” are connected to criminal activity.<sup>29</sup> Moreover, a transaction is suspicious if it

- (i) involves funds derived from illegal activities or is conducted to disguise funds derived from illegal activities;
- (ii) is designed to evade the reporting or record-keeping requirements of the BSA (e.g., structuring transactions to avoid currency transaction reporting); or
- (iii) Has no business or apparent lawful purpose or is not the sort in which the particular customer would normally be expected to engage, and the bank knows of no reasonable explanation for the transaction after examining the available facts, including the background and possible purpose of the transaction.<sup>30</sup>

Some financial institutions are further required to file a SAR if there is reason to suspect that the transaction was intended to facilitate criminal activity, including acts of terrorism.<sup>31</sup> Generally, banks must file SARs involving or aggregating at least \$5,000.

#### **“Know your customer”**

Essential to any effective AML/CTF program is the principle of “know your customer” (“KYC”), which “has been the backbone of anti-money laundering and counter terrorist financing measures” by financial service providers.<sup>32</sup> Moreover, a bank cannot determine whether a particular transaction is suspicious and should be reported to the Treasury Department in a vacuum. Thus, KYC is absolutely critical to an effective SAR filing regime. Under the BSA, financial institutions, including foreign banks with U.S. branches, are required to implement reasonable procedures for identification and verification of customers opening an account. At a minimum, financial institutions are required to implement procedures for:

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<sup>29</sup> 31 C.F.R. § 103.18(a)(2); *see also* 31 U.S.C. § 5318(g) (2000 & Supp. IV 2004).

<sup>30</sup> 31 C.F.R. § 103.18(a)(2)(i)-(iii).

<sup>31</sup> *See* 31 C.F.R. § 103.17(a)(2)(iv) (futures commission merchants and introducing brokers in commodities); 31 C.F.R. § 103.19(a)(2)(iv) (brokers or dealers in securities); 31 C.F.R. § 103.20(a)(2)(iv) (money services businesses); and 31 C.F.R. § 103.21(a)(2)(iv) (casinos).

<sup>32</sup> Financial Action Task Force, *Combating the Abuse of Alternative Remittance Systems: International Best Practices*, at 7 (June 20, 2003), *available at* <http://www.fatf-gafi.org/dataoecd/32/15/34255005.pdf>.

(A) Verifying the identity of any person seeking to open an account to the extent reasonable and practicable; (B) maintaining records of information used to verify a person's identity, including name, address, and other identifying information; and (C) consulting lists of known or suspected terrorists or terrorist organizations provided to the financial institution by any government agency to determine whether a persons seeking to open an account appears on any such list.<sup>33</sup>

**(D) Non-Compliance with the SAR Reporting Requirement**

The obligation to file SARs is not a new requirement for financial institutions. Thus, if banks are well aware of their duty to file SARs, what is the explanation for bank non-compliance with the SAR filing requirement? There are three contributing factors: (1) lack of adequate employee training; (2) lack of clear and expeditious procedures for determining whether a suspicious transaction should be reported to the Treasury Department; and (3) senior management's failure to fully embrace and communicate the importance of SAR reporting.

**(i) Employee training**

The proper and timely filing of SARs depends on the ability of bank employees to identify funds suspected of being derived from illegal activities or transactions that do not appear to have a lawful purpose. Employee training should be robust and comprehensive, and not limited to a short on-line training course. Bank employees should be trained on the "red flags" of money laundering and terrorist financing. Further, employee training should involve an examination of actual money laundering cases or case studies. Employees should also be afforded regular refresher training. Finally, the Treasury Department should regularly update AML compliance officers of new money laundering trends and fraud schemes involving banking services, and the compliance officer should share that information with bank employees.

**(ii) Clear and Expeditious Decision-Making Process**

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<sup>33</sup> 31 U.S.C. § 5318(l)(2)(2000 & Supp. IV 2004).

The bank should have internal procedures which clearly and concisely detail the process for resolving whether a transaction initially flagged as suspicious should be reported to the Treasury Department. The internal procedures should identify the persons in the chain of command for determining whether a financial transaction is truly suspicious and should be reported or whether the flagged transaction was merely a false-positive alert. These procedures should also identify the person responsible for making the final decision on whether to file a SAR. Moreover, the internal procedures should include objective criteria for determining whether to file a SAR. For example, a SAR should be filed if there is clearly no business or apparent lawful purpose or the transaction is not the sort in which the particular customer would normally be expected to engage, and the bank knows of no reasonable explanation for the transaction after examining the available facts, or the transaction constitutes a “red flag” of money laundering and a legitimate explanation for the transaction has not been determined. Finally, the internal SAR filing procedures should be streamlined and permit an expeditious resolution of the matter to ensure that bank customers are not unfairly inconvenienced.

**(iii) Senior Management Must Emphasize and Communicate The Importance of SAR Filing**

Perhaps the most significant reason for non-compliance is that bank employees simply do not believe that SAR filling is important. If the bank CEO and other senior management officials have never expressly communicated the importance of identifying and reporting SARs, it is easy to see why bank employees would have this impression. Silence on the subject may be interpreted by bank employees to mean that SAR filing is not an issue of concern for bank management. Further, bank employees may not fully understand that the BSA imposes a legal duty on banks to file SARs. They may mistakenly believe that filing suspicious transactions is discretionary or merely encouraged by the BSA. To the contrary, SAR filing is legally mandated and a willful failure to file SARs could result in the imposition of costly monetary penalties and criminal prosecution. Further, bank employees may be operating under the assumption that what they don't know won't hurt them. However, willful blindness is the legal

equivalent of knowledge and could support a criminal prosecution for failure to file SARs. In order to prevent the bank from being criminally prosecuted for failing to file SARs under the DOJ's new criminal enforcement policy, senior bank management must emphasize and communicate the importance of identifying and reporting suspicious transactions. Establishing a culture of BSA/AML compliance must start at the top.

## **CONCLUSION**