



## WHITE-COLLAR CRIME

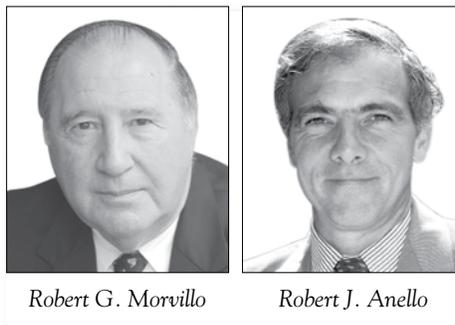
BY ROBERT G. MORVILLO AND ROBERT J. ANELLO

### 'Show Me the Money'

The U.S. Department of Justice encourages its assistants and agents to follow the money in investigating and prosecuting a broad array of federal crimes.<sup>1</sup> Law enforcement has the capability to trace the movement of cash, both before and after commission of a crime, in order to uncover sophisticated white-collar schemes as well as illegal narcotic trafficking.

In some situations, illustrated by former Governor Eliot Spitzer's latest travails, the movement of funds may point to state offenses such as prostitution. The Internal Revenue Service (IRS) defines its role in such investigations as simple and straightforward: "Our job is to follow the money, track and document the flow of funds, and thereby help prove the underlying criminal activity."<sup>2</sup>

Modern laws covering structuring and money laundering are among the weapons in the government's arsenal that not only provide a method for following the money, but also can provide an independent basis for prosecution. The government has at its disposal a number of ways to follow the money even before any illegal activity has occurred. Financial transactions made in anticipation of engaging in illegal acts often are flagged for the government by financial institutions through their filing of Currency Transaction Reports (CTRs) and Suspicious Activity Reports



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(SARs). In addition, the frequently used money laundering statutes contained in §§1956 and 1957 of Title 18 allow the government to trace the proceeds of illegal activity after the allegedly nefarious acts have occurred. The federal government has become increasingly sophisticated in its use of these reports and laws to track the movement of money to determine if someone is up to no good.

#### How Government Monitors Activity

Since 1970, banks and other financial institutions have been required to monitor their customers' activities and file Suspicious Activity Reports with the Treasury Department.<sup>3</sup> SARs are used to report unusual transactions, such as odd patterns of cash withdrawals or wire transfers. These reporting requirements have expanded greatly since the passage of the Patriot Act vested broader investigatory powers in the government after Sept. 11. The number of filings made to the Treasury Department has been growing every year. In 2006, the last full year for which statistics are available, more than 1 million suspicious-activity reports were filed, according to a division of the Treasury Department. In 2001, the number

was only about 205,000.<sup>4</sup> Banks are immune from liability for the reporting of otherwise confidential customer information under the "safe harbor" provisions of the law.<sup>5</sup>

Facing potentially stiff penalties for noncompliance with these reporting requirements,<sup>6</sup> major banks and other financial institutions have installed sophisticated software to detect anomalies among millions of daily transactions. These programs rank the risk levels of the bank's customer base on a scale of zero to 100, based on complex formulas that include the credit rating, assets, and profession of the account holder. In addition, financial institutions set parameters for the types of activities that should be flagged. When such activity occurs, the institution is alerted and can follow up on the activities in question.<sup>7</sup>

The regulations provide that a financial institution is required to file an SAR where a transaction, which includes a "deposit, withdrawal, transfer between accounts, exchange of currency, loan, extension of credit, or purchase or sale of any stock, bond, certificate of deposit, or other monetary instrument or investment security," occurs and the bank knows or suspects that: (i) the funds come from illegal activity or disguise funds from illegal activity; (ii) the transaction is structured to evade reporting requirements or appears to serve no known business or apparent lawful purpose; or (iii) the financial institution is being used to facilitate criminal activity.<sup>8</sup>

A financial institution has 30 days from discovery to file an SAR with "the appropriate federal law enforcement agencies and the Department of the Treasury."<sup>9</sup> The Treasury

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Department's Financial Crimes Enforcement Network reviews the data received and forwards it as necessary. Ultimately, it is available to law-enforcement agencies nationwide and frequently is "scoured" by federal prosecutors for potential leads. Noting that the initial impetus for the Patriot Act was the war on terrorism, observers comment that currently "[t]errorism has virtually nothing to do with it." Rather, "[t]he vast majority of SARs filed today involve garden-variety forms of white-collar crime."<sup>10</sup>

## Structuring

• **Financial Transactions Made Before Any Illegality.** The Bank Secrecy Act enacted in 1970 requires a financial institution to file a currency transaction report (CTRs) when it is involved in a cash transaction for the payment, receipt, or transfer of \$10,000 or more.<sup>11</sup> The purpose of this legislation is to assist the government in "ferreting out criminal activity" that would be revealed through the investigation of large and unusual currency transactions.<sup>12</sup> In the past, this reporting requirement often was avoided by customers who simply moved their money by multiple transactions under the \$10,000 threshold.

In 1986, as part of the Money Laundering Control Act, Congress made it illegal for a person to engage in a series of cash transactions designed to avoid the filing of CTRs. This crime, set forth in 31 U.S.C. §5324 is called "structuring" or "smurfing." According to the Internal Revenue Manual, structuring occurs when a person conducts or attempts to conduct one or more transactions in currency, in any amount, at one or more financial institutions, on one or more days for the purpose of evading the reporting requirements requiring the filing of CTRs.<sup>13</sup>

As originally enacted, §5324 included a willfulness requirement. In *United States v. Scanio*, the U.S. Court of Appeals for the Second Circuit construed the willfulness element to require proof that a defendant, with knowledge of the reporting requirement imposed by law, structured a currency transaction "intend[ing] to deprive the government of information to which it is entitled."<sup>14</sup> The Supreme Court

rejected this interpretation, however, ruling that structuring was "willful" only if the government further proved that the defendant acted with knowledge that his conduct was unlawful. "Undoubtedly there are bad men who attempt to elude reporting requirements in order to hide from government inspectors such criminal activity as laundering drug money or tax evasion. But currency structuring is not inevitably nefarious."<sup>15</sup>

Subsequently, Congress amended the statute to eliminate the willfulness requirement. The Second Circuit noted that the net result of this action by Congress "was to confirm federal antistructuring law 'to the *Scanio* interpretation."<sup>16</sup> Accordingly, in bringing a structuring case, the government is required to prove that: (1) the defendant in fact engaged in the acts of structuring; (2) he or she did so with knowledge that the financial institutions involved were legally obligated to report currency transactions in excess of \$10,000; and (3) he or she acted with intent to evade that reporting requirement.<sup>17</sup>

More recently, the Second Circuit has rejected arguments that a structuring violation requires proof that the money at issue was criminally derived. "The antistructuring law may well have been intended to prevent criminals from concealing their illicit profits, but that is not the limit of its reach. Section 5324 makes no reference to the source of the monies at issue or to the reason why a person seeks to avoid CTR filing. Its singular focus is on the method employed to evade that filing requirement, i.e., structuring."<sup>18</sup>

A violation of 31 U.S.C. §5324 is punishable by up to five years' imprisonment. Like money laundering cases, calculations under the federal sentencing guidelines consider the amount of money actually structured. Accordingly, the amount of imprisonment recommended under the guidelines increases with the amount of funds structured in violation of the statute.

## Money Laundering

• **Financial Transactions Made After the Alleged Illegality.** Section 1956 of the federal money-laundering laws enacted in 1986 prohibit engaging in financial transactions

involving "dirty" money that constitutes the proceeds of illegal activity. This specific intent money laundering statute focuses on those actions designed "to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of" illegal conduct. To establish a §1956 violation, the statute requires proof that the defendant had one of the enumerated purposes, such as the promotion or concealment of an unlawful activity, when engaging in the financial transaction at issue.<sup>19</sup>

Section 1957, on the other hand, criminalizes a broader range of conduct, including certain monetary transactions in criminally derived funds. The government need not prove that the defendant had the specific intent to engage in an enumerated purpose. Rather, it need only show that the defendant knew that the money was criminally derived.<sup>20</sup> In addition to the intent requirement, there are two additional distinctions between §§1956 and 1957. First, §1957 has a \$10,000 threshold requirement for each transaction, which does not exist under §1956. Second, unlike §1956, §1957 requires that the transaction be conducted through a financial institution.<sup>21</sup> The Supreme Court has recognized that both §1956 and §1957 are "after-the-fact" offenses committed with the proceeds generated by consummated specified unlawful activity.<sup>22</sup>

The money laundering laws also contain a conspiracy provision making it criminal to conspire to violate any of the crimes contained in either §1956 or §1957.<sup>23</sup> Because this conspiracy can be accomplished even before the putative launderers or their cohorts engage in criminal conduct, creative use of this statute might ensnare those who are still in the early planning stage. The Supreme Court has ruled that the government need not charge or prove an overt act to obtain a conviction under the money laundering conspiracy statute.<sup>24</sup> A violation of 18 U.S.C. §1956 is punishable by up to 20 years imprisonment, while a conviction under §1957 is punishable by up to 10 years in prison. Under the federal sentencing guidelines, the more money laundered, the longer the sentence.

The reach and application of the money

laundering statutes currently is under consideration by the Supreme Court.<sup>25</sup> These cases challenge the government's frequent use of money laundering charges as an "add on" to other charges in white-collar cases. This action, frequently criticized by the defense bar, not only allows the government to tack on money laundering charges to other substantive crimes, but gives prosecutors leverage in negotiating plea settlements.<sup>26</sup> In amicus briefs recently filed in these cases, the National Association of Criminal Defense Lawyers notes a trend among courts to very broadly construe the money-laundering statute, thereby improperly expanding the scope of the law.<sup>27</sup> The Court's decisions in these cases may impact the government's ability to bring money laundering charges, but likely will have no impact on its ability to "follow the money" under the Bank Secrecy Act and antistructuring laws.

## The Spitzer Case

Eliot Spitzer's recent resignation over allegations that he was involved in a prostitution ring demonstrates the effectiveness of the reporting and investigative structure that has developed by following the money. The government reportedly was drawn to Mr. Spitzer's alleged wrongdoing not by virtue of his involvement in the prostitution ring, but by the financial transactions he conducted to pay for his dalliances.

Mr. Spitzer allegedly made a number of unusual cash transfers from his bank account to shell corporations established by the escort agency.<sup>28</sup> According to the Washington Post, bank officials first became suspicious of Mr. Spitzer because he appeared to be structuring transactions to avoid the \$10,000 CTR requirement.<sup>29</sup>

The bank filed a suspicious activity report with the Treasury Department. Investigators in a Long Island branch of the IRS took note when they saw Mr. Spitzer's name while conducting a standard review of SARs. Upon further investigation by IRS and FBI agents, the government learned that the recipients of the governor's financial transactions were alleged shell companies, QAT Consulting Group and QAT International, associated with

the Emperors Club VIP escort service.<sup>30</sup> Peter Djinis, a former head of regulatory programs at the Treasury Department's Financial Crimes Enforcement Network, observed that "[t]he huge irony here is that probably if [Mr. Spitzer] had not engaged in structuring activity, the call-girl enterprise never would have been discovered or prosecuted."<sup>31</sup>

Mr. Spitzer's conduct may expose him to criminal liability under federal money laundering and related statutes. The laws against structuring financial transactions with an intent to avoid the reporting requirements do not require any showing that the money used by Mr. Spitzer was "dirty" or otherwise tainted. Indeed, the structuring laws worked as intended in this case in allowing the government to ferret out wrongdoing by following the "clean" money trail.

Further, even though the money used by Mr. Spitzer to pay the shell corporations controlled by Emperors' Club VIP apparently was "clean," observers have said that Mr. Spitzer may be liable under the money laundering statutes themselves to the extent that he knew those shell corporations were used to disguise the source or use of the money he paid. New York University Legal Ethics professor, Stephen Gillers, said that if Mr. Spitzer faces any criminal liability, it might be for conspiracy in a money laundering scheme under 18 U.S.C. §1956(h). "When he wired cash to these shell corporations, the government's position may be that he knew that this money wasn't going to be declared and that the corporation's intent was to avoid tax liability and convert illegal proceeds into the appearance of legitimate income, which is laundering."<sup>32</sup>

Indeed, the complaint filed against the Emperors' Club defendants in early March contains a count alleging violations of the money laundering conspiracy statute, §1956(h). The complaint alleges that the defendants opened bank accounts in the names of QAT Consulting Group Inc. and QAT International Inc.—the same accounts to which Mr. Spitzer transferred money—for the purpose of receiving proceeds from the Emperors' Club prostitution business.<sup>33</sup>



1. Scott J. Golde and Winston E. Calvert, "A Practitioner's Guide to the Federal Money Laundering Statutes," *Journal of the Missouri Bar* (September-October 2006).

2. Press Release, Department of Justice, "Three Defendants Indicted in Case Involving Bribery, Conspiracy, Money Laundering, and Obstruction Offenses Related to Contracts in Iraq and Kuwait," (Aug. 22, 2007) (comments of Eileen Mayer, Chief of IRS Criminal Investigation Division explaining her department's role in federal investigations).

3. 12 C.F.R. §21.11.

4. Greg Saitz, "No Matter the Amount, Banks Follow the Money," *Newhouse News Service* (March 20, 2008).

5. 31 U.S.C. §5318(g)(3).

6. Failure to file may lead to civil and criminal penalties. A civil penalty, not to exceed the greater of the amount involved in the transaction (limited at \$100,000) or \$25,000, may apply for each willful violation. A willful violation of the reporting requirements may also result in criminal penalties, including a fine as great as \$250,000 or five years imprisonment. See Internal Revenue Service, "Suspicious Activity Reports" (available at <http://www.irs.gov/businesses/small/article/0,,id=154555,00.html>).

7. Mark Hosenball and Michael Isikoff, "Unintended Consequences," *Newsweek* (March 24, 2008).

8. 12 C.F.R. §21.11(c).

9. *Id.* at (d), (c).

10. *Id.*

11. 31 U.S.C. §5313(a) (defining cash as "United States coins or currency").

12. *California Bankers Ass'n v. Shultz*, 416 U.S. 21, 38 (1974) (citing legislative history).

13. Internal Revenue Manual 4.26.13.2.1 (6-1-06).

14. *United States v. Scanio*, 900 F.2d 485, 491 (2d Cir. 1990).

15. *Ratzlaf v. United States*, 510 U.S. 135, 137 (1994).

16. *United States v. MacPherson*, 424 F.3d 183, 189 (2d Cir. 2005) (citations omitted).

17. *Id.*

18. *Id.* at 193.

19. 18 U.S.C. §1956(a)(1-2).

20. 18 U.S.C. §1957.

21. U.S. Treas. Dept. & U.S. Dept. of Justice, "The National Money Laundering Strategy for 2000" (2000).

22. *United States v. Cabrales*, 524 U.S. 1, 7 (1998).

23. 18 U.S.C. §1956(h).

24. *Whitfield v. United States*, 543 U.S. 209 (2005).

25. Elkan Abramowitz and Barry Bohrer, "Federal Money-Laundering Statutes: Course Correction?" *New York Law Journal* (Nov. 6, 2007).

26. Teresa E. Adams, "Tacking on Money-Laundering Charges to White-Collar Crimes: What Did Congress Intend, and What Are the Courts Doing?" *Ga. St. U. L. Rev.* (Winter 2000).

27. Abramowitz and Bohrer, "Federal Money-Laundering Statutes: Course Correction?"

28. Luke Mullins, "Why Spitzer's Banking May Have Tripped Him Up," *U.S. News and World Report* (March 12, 2008); William K. Rashbaum, "Revelations Began in Routine Tax Inquiry," *The New York Times* (March 11, 2008).

29. Keith B. Richburg, Susan Schmidt and Carrie Johnson, "FBI Watched Spitzer Before February Incident," *The Washington Post* (March 12, 2008).

30. Keith B. Richburg, Susan Schmidt and Carrie Johnson, "FBI Watched Spitzer Before February Incident"; William K. Rashbaum, "Revelations Began in Routine Tax Inquiry."

31. Mullins, "Why Spitzer's Banking May Have Tripped Him Up."

32. Dan Slater, "Beyond the Court of Public Opinion, Is Spitzer Legally Vulnerable?" *The Wall Street Journal Online Blog* (March 11, 2008).

33. Sealed Complaint, *United States v. Brener, et al.*, 08 MAG 0463 (March 5, 2008).