



United States Department of the Treasury
Financial Crimes Enforcement Network

FinCEN Advisory

Subject:
**Court Interprets
“Safe Harbor”
Provision**

Date:
**August
1996**

Advisory:
Vol 1, Issue 5

This advisory is provided to inform financial institutions of the recent court decision concerning the “safe harbor” provision of the Bank Secrecy Act as applied to reports of suspicious transactions.

Protection of financial institutions from liability to customers is an essential part of the United States’ program for reporting suspicious activities. Congress created that protection in 1992 when it added a safe harbor from civil liability for reporting institutions [31 U.S.C. 5318(g)(3)] to the Bank Secrecy Act (BSA). Now, in *Merrill Lynch v. Green* (S.D. Fla No. 952207), a recent decision applying the protection, a federal court provides strong support for the statute, in a situation where a securities firm voluntarily reported a suspicious transaction.

In late 1992, Merrill, Lynch, Pierce, Fenner, & Smith (Merrill Lynch) reported to federal agents the existence of suspect funds held in one of its customer’s accounts. The funds were seized and approximately half the funds were later forfeited by the customer, an alleged narcotics and gold smuggler, under the customer’s settlement with the government.

In 1995, the customer (after beginning and voluntarily dismissing a federal civil action) sought arbitration, before the National Association of Securities Dealers (NASD), of a claim that Merrill Lynch was liable for compensatory and punitive damages because it reported its suspicions without his knowledge and cooperated with the government. Merrill Lynch sought to enjoin the arbitration because of the BSA’s statutory civil liability safe harbor. The court issued a preliminary injunction staying the arbitration on March 29, 1996, and made that order permanent on June 14, 1996.

The court’s orders confirm the broad scope of the protection against civil suits afforded by the safe harbor provision in 31 U.S.C. 5318(g)(3).

In its order granting the preliminary injunction, the court stated that the brokerage firm “is entitled to immunity for its initial disclosure regarding the (defendant’s) account under the safe harbor provision of the Bank Secrecy Act, found at 31 U.S.C. 5318.” The Court stated further:



"The statute prohibits financial institutions who voluntarily report a suspicious transaction to the government from notifying the persons involved in the transaction. Merrill Lynch complied with this provision by abstaining from notifying Green . . . of its own suspicions regarding the account and of the ongoing investigation by various American and British agencies."

Finally, the Court concluded, "[w]ithout presently determining its full breadth and scope, [that] the statute [confers] broad protection upon financial institutions." In its later judgment making the injunction permanent, the court reiterated the broad scope effect of the safe harbor:

"Pursuant to the statute [Merrill Lynch] was authorized to abstain from notifying defendant of its suspicions regarding the accounts and of the ongoing investigation by law enforcement authorities. The safe harbor provision confers broad protection upon financial institutions, such that the protective mantle of 31 U.S.C. 5318 immunizes the plaintiff from claims raised by the defendant."

As the Financial Crimes Enforcement Network (FinCEN) prepares rules to expand the obligation to report suspicious activity to securities brokers and dealers and other non-bank financial institutions, it intends to write the statutory safe harbor into those rules as well. All of this translates into the fact that the court supports the premise that the statute provides broad protection for financial institutions whether they file by regulation, or voluntarily, on a form, in person or even over the telephone and that there is no obligation to notifying the customer(s) involved.

Background

The Congress and the Treasury have carefully crafted anti-money laundering laws and regulations to focus on the reporting of suspicious transactions by financial institutions. That focus recognizes that it is representatives of financial institutions, rather than law enforcement, who see the money launderers first; illicit proceeds are almost always moved through some form of financial institution. The focus also recognizes that the commercial precautions and expertise financial institutions use to protect themselves from fraud, theft, and misuse, equips those institutions to recognize what is or is not suspicious.

For a suspicious transaction reporting regime to be effective, however, financial institutions and their customers must be able to rely upon the confidentiality of the reports, and financial institutions must be protected from civil liability to persons about whom reports are made. FinCEN and the five federal financial supervisory agencies (Federal Deposit Insurance Corporation, Federal Reserve Board, National Credit Union Administration, Office of the Comptroller of the Currency, and the Office of Thrift Supervision) that

now require reporting of suspicious activity reports by depository institutions, confirmed the importance of these protections in final rules issued earlier this year.

It is noteworthy that the emerging international consensus on fighting money laundering couples the requirement of suspicious transaction reporting with firm assurances of confidentiality and protection of reporting institutions against liability to their customers. This is reflected, for example, in the 40 Recommendations of the Financial Action Task Force of the G-7 nations (the United States, The United Kingdom, Germany, France, Italy, Japan and Canada); the European Community's Directive on prevention of the use of the financial system for the purpose of money laundering; and the Model Regulations Concerning Laundering Offenses connected to Illicit Drug Trafficking and Related Offenses of the Organization of American States.

We recognize the extreme importance of the safe harbor provision and support financial institutions' interests in protecting themselves from liability to customers as it relates to the reporting of suspicious activities. We are in the process of reviewing additional decisions related to the safe harbor provision and will keep you informed of relevant legal developments.



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