Suspicious Activity Reports: Deciding When a Good Faith Suspicion Is Good Enough

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In August, Standard Chartered learned an expensive lesson in reporting when a New York regulator ordered a $340 million penalty for a number of alleged state charter violations and unauthorized foreign transactions in violation of the Bank Secrecy Act (BSA). In today's regulatory climate, noncompliance implications can expose a financial institution to significant liabilities.

The BSA requires financial institutions to report to government agencies suspect transactions that raise a potential violation of law. These reports, as covered in 31 U.S.C. §5318(g) of the BSA, can either be ordered by the Secretary of Treasury or filed voluntarily by a financial institution in good faith. To gain a better understanding of when a bank's good faith suspicion may be good enough, let's take a look at Circuit Court decisions that continue to shape the legal landscape.

First, in *Lopez v. First Union National Bank of Florida*, 129 F.3d 1186 (11th Cir. 1997), Patricia Lopez sued First Union after it surrendered financial records in response to a federal regulator's "verbal instructions." The Eleventh Circuit Court made two important holdings in the case: verbal instructions from an enforcement entity do not constitute a sufficient basis for ordering the production of records and in the absence of proper notice, a bank must have a good faith suspicion that a law or regulation had been violated before records can be released.

Next, the Second Circuit in *Lee v. Bankers Trust Company,* 166 F.3d 40 (2d Cir. 1998), ruled differently regarding this good faith standard. Bankers Trust filed a Suspicious Activity Report (SAR) against a former employee, Let Lee, after suspecting that he had engaged in questionable banking activity during his employment. Lee, however, denied any questionable/illegal banking activity and alleged the bank filed the SAR to protect its own interests. Subsequently, the Court endorsed Bankers Trust's actions, noting that a bank is immune from liability under §5318(g)(3) even if the SAR was filed "in an excess of caution."

In *Stoutt v. Banco Popular de Puerto Rico,* 320 F.3d 26 (1st Cir. 2002), the bank filed a Criminal Referral Form (CRF) containing customer disclosures that formed the basis of a federal grand jury indictment. Despite the charges being dismissed, the First Circuit found that the voluntary disclosures made by the bank did not require the good faith suspicion standard established in *Lopez*. The Court held that a financial institution retained immunity when disclosing "any possible violation of law," as stated in §5318(g)(3)(A).

As more district court decisions continue to weigh in on the disclosure of private banking records, banks must be vigilant and consult counsel when deciding when a good faith suspicion is good enough.