Obtaining Records from a Foreign Bank

Note on the Decision of the Federal Court, Washington, DC, of March 18, 2019

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Article

ABSTRACT

A federal court in the United States granted a motion to compel two Chinese banks to comply with subpoenas served on their US branches, demanding records of transactions occurring in China. The same court also granted a motion to compel a third Chinese bank that has no US branches to comply with a similar subpoena for foreign records, holding that, because the bank maintains a correspondent account at a US bank, it is required by law to comply with such a demand for records. Those orders have now been affirmed by a federal appellate court in Washington, DC. This article explains the background of the case, the content of the court decision, and its importance.

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In the United States, the FBI is investigating a Chinese company that served as a front for a North Korean entity involved in North Korea's nuclear weapons program. The investigation concerns possible violations of the federal money laundering statute,[1] the International Emergency Economic Powers Act (IEEPA),[2] and the Bank Secrecy Act.[3] To obtain records of the Chinese company's financial transactions, the Government served grand jury subpoenas on two Chinese banks that have branches in the United States and a third subpoena on another Chinese bank that has no branches in the U.S. but maintains a correspondent account at a U.S. bank. All three subpoenas sought records of transactions occurring in China. After the banks resisted complying with the subpoenas, the US Government filed motion to a federal court in Washington, D.C. to enforce them. The following sections will explain what a subpoena is and which types of subpoenas are relevant in the case (I.), which main legal issues the federal court decided in its enforcing decision (II.), and why the decision is important, in particular in view of being an alternative to the mutual legal assistance path (III.).[4]

I. Background: Subpoenas

A grand jury subpoena is a judicial instrument by which the US Government, acting through the office of the federal prosecutor who advises the investigating grand jury, demands records from financial institutions who possess records relevant to an ongoing criminal investigation.[5] Grand jury subpoenas are issued unilaterally by the grand jury without prior judicial approval, but if the entity on which the subpoena is served resists compliance, the Government must resort to a federal court to enforce compliance.

Such subpoenas are routinely served on domestic financial institutions in the United States. When records are sought from a foreign financial institution that has branches in the USA, the subpoena may be served on any one of the branches, demanding records that the parent bank maintains in its home country. Such grand jury subpoenas are called "*Bank of Nova Scotia* subpoenas" after the case that upheld the use of such subpoenas in criminal investigations.[6]

When records relevant to a criminal investigation are held by a foreign bank that does not maintain any branches in the United States, the Government generally must obtain the records through a bilateral agreement such as a Mutual Legal Assistance Treaty (MLAT). As will be discussed below, however, a provision of the USA Patriot Act, enacted in the wake of the terrorist attacks on September 11, 2001, authorizes the Government to serve a subpoena for foreign records on any foreign bank that maintains a correspondent account in the United States at a US bank, even if the foreign bank has no branches in the United States. The statute is 31 U.S.C. § 5318(k) and such subpoenas are accordingly called "Section 5318(k) subpoenas."[7]

In the cases at issue, the two Chinese banks that have branches in the USA were therefore served with *Bank of Nova Scotia* subpoenas, and the third bank, which has no US branches, was served with a Section 5318(k) subpoena.

II. Enforcing Compliance with the Subpoenas

All three banks resisted the subpoenas, arguing that the proper procedure for requesting foreign bank records would be to make a request under the Mutual Legal Assistance Agreement (MLAA) between the USA and China. But after waiting nearly a year – during which time the US Department of Justice sent two delegations to China in an unsuccessful attempt to gain China's compliance with numerous outstanding MLAA requests in other cases – the US Government filed motions in a federal court in Washington, D.C. to compel compliance with the three subpoenas.

In ruling on the motions, the court had to determine two issues:

- whether the subpoenas were enforceable, and
- whether enforcement of the subpoenas would be proper as a matter of international comity.

1. Enforceability

Regarding the issue of enforceability, the court held that it had jurisdiction to enforce the subpoenas for two reasons: the two Chinese banks with branches in the USA had agreed to submit to the jurisdiction of the US courts as a condition of their being granted permission to open US branches; and all three banks maintained the "minimum contacts" with the United States necessary to justify the exercise of jurisdiction in terms of the Due Process Clause of the Fifth Amendment.[8]

In the context of the latter point, another question was whether the Washington court was locally competent to enforce the subpoenas. The banks objected that although the subpoenas were issued in the course of an investigation based in Washington, D.C., they were served on their representatives in New York, which is where they conducted business in the United States. Thus, they argued that the Washington court had no authority to enforce the subpoenas. But the court held that the subpoenas were issued in the course of an investigation that was national in scope and thus could be enforced in any court.[9]

Beyond the question of jurisdiction, the third Chinese bank that received the Section 5318(k) subpoena had an additional objection to its enforceability: it argued that the subpoena exceeded the scope of the statute. Under Section 5318(k) any foreign bank maintaining a correspondent account in the United States must, as a condition of maintaining such an account, comply with a subpoena for records "maintained outside the United States relating to the deposit of funds into the foreign bank."[10] The bank argued that this meant it was required only to provide records of transactions occurring *in the correspondent account*. The court, however, held that a Section 5318(k) subpoena may request *any records* pertaining to the customer whose money flowed through the correspondent account.

The court reasoned that the purpose of a Section 5318(k) subpoena is to determine the source of the money that funded the later movement of money through the correspondent account in the USA. That would include ledgers, account statements, and records of cash deposits and wire transfers showing the source of the money deposited into the Chinese bank *in China*. Thus, the request that the bank produce such records fell within the scope of the statute.[11]

2. International comity

Turning to the comity issue, the court acknowledged that just because a subpoena served on a foreign bank is enforceable does not mean that it should be enforced. On the latter point, the court referred to several criteria: among other things, a court must consider the importance of the records to the investigation, the lack of alternative means of obtaining them, the competing national interests of the two countries involved, and the potential hardship that might befall the record custodian if its compliance with the subpoena were contrary to local law.[12]

Considering all of these factors, the court determined that "international comity is not a reason to refrain from compelling compliance with the subpoenas."[13] Most importantly, according to the court, the investigation in question concerned the national security of the United States but involved no competing national interest of equal importance to China. Moreover, based on the Government's past experience, the court determined that the MLAA process was unlikely to be a satisfactory alternative means of obtaining the

records, and that, while the Chinese banks might suffer sanctions at home if they complied with the subpoenas, such consequences were speculative.[14]

Accordingly, the court granted the motions to compel, but the banks nevertheless refused to comply and stated that they intended to appeal. Thus, in a separate order,[15] the court granted the Government's motion to hold all three banks in civil contempt, directing them to pay $50,000 per day in penalties until they complied but suspending the imposition of the penalties until the conclusion of the banks' appeals.[16]

Finally, on August 6, 2019, the federal court of appeals sitting in Washington, DC affirmed the orders of the lower court in all respects.[17]

III. Importance of the Federal Court's Decision

As mentioned under I., a *Bank of Nova Scotia* subpoena is a subpoena for foreign bank records that is served on the US branch of a foreign bank that is holding the requested records abroad. While rarely used – because Government policy favors using mutual legal assistance agreements as a first resort – such subpoenas will be enforced if the foreign bank does enough business in the United States to satisfy the "minimum contacts" requirement or, as in this case, if the bank has consented to the jurisdiction of the US courts as a condition of being granted permission by the Federal Reserve to open branches in the USA.

Two of the subpoenas in this case were *Bank of Nova Scotia* subpoenas. Thus, the court's order upholding the subpoenas and compelling compliance with them on pain of contempt is an important reaffirmation of the US Government's right to use such instruments to obtain foreign bank records *even when there is a mutual legal assistance agreement between the United States and the foreign Government*. In short, the court holds that, while resorting first to such mutual agreements is favored as a matter of international comity, the fact that such agreements nominally exist on paper is not a bar to exercising alternative means of obtaining records relevant to a criminal investigation if experience shows that the agreements have been ineffective.

The third subpoena was different: contrary to the *Bank of Nova Scotia* subpoena that could be served because the Chinese banks had at least one branch in the US, the third Chinese bank had no such branches. Hence, Section 5318(k) was enacted to close that gap. The key point of the court decision is the following: the rationale for Section 5318(k) is that, even if a foreign bank does not have a US branch, it is nevertheless availing itself of access to the US financial system by maintaining a correspondent account at a US bank (what is its only business in the USA). Thus, the USA may, as a condition of allowing a foreign bank to have such access, require it to comply with a subpoena for foreign bank records. Indeed, the penalty for non-compliance includes barring the foreign bank from maintaining any such correspondent account, thus freezing the bank out of the US financial system.

Section 5318(k) subpoenas are rarely used; the Justice, Treasury, and State Departments are quite skittish about what they consider to be an option of last resort and do not readily grant requests from law enforcement agencies to issue such subpoenas. But this case illustrates that permission can be obtained in some cases.

IV. Conclusion

The United States has a strong national interest in preserving the integrity of its banking system and preventing its misuse by foreign banks and entities engaged in criminal activity. Because of the role that US

banks serve in processing international financial transactions, the threat of such abuse is both constant and real.

At the same time, the role that US banks play in international finance gives the USA a tool to enforce compliance with its judicial requests for bank records that may not be available to other countries. It gives the US Government the option of telling a foreign bank, "either comply with our requests for financial records or face exclusion from the US financial system." Because most foreign banks could not process dollar-denominated transactions without access to a correspondent account at a US bank, a US demand stated in these terms is likely to compel compliance.

Accordingly, while the US financial system is at great risk of being used to launder the proceeds of foreign crime and to finance acts of terrorism, the USA is not without tools to obtain the records it needs to bring criminal prosecutions against the perpetrators of such acts. And as the cases presented in this article illustrate, the USA is not reluctant to use these tools when other methods – such as mutual legal assistance agreements – prove to be of no avail.

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1. 18 U.S.C. § 1956-57.↩
2. 50 U.S.C. § 1705.↩
3. 31 U.S.C. § 5311, et seq.↩
4. An earlier version of this article appeared in Money Laundering and Forfeiture Digest, which is available by subscription on <www.AssetForfeitureLaw.us>.↩
5. A grand jury is a body of 23 citizens authorized to conduct criminal investigations and issue compulsory process demanding witness testimony and the production of records. While advised by a prosecutor and supervised by the court, it is an independent body. No criminal indictment may be returned unless approved by a grand jury.↩
6. In Re Grand Jury Proceedings, United States v. Bank of Nova Scotia, 691 F.2d 1384 (11th Cir. 1982).↩
7. Section 5318(k) is part of the Bank Secrecy Act, 31 U.S.C. § 5311, et seq.↩
8. *In Re Grand Jury Investigation*, ___ F. Supp.3d ___, 2019 WL 2170776 (D.D.C. Mar. 18, 2019) (Order Granting Motion to Compel).↩
9. *Id*.↩
10. 31 U.S.C. § 5318(k)(3)(A)(i).↩
11. In Re Grand Jury Investigation, 2019 WL 2170776.↩
12. *Id*.↩
13. *Id*.↩
14. *Id*.↩
15. *In Re Grand Jury Investigation*, 2019 WL 2182436 (D.D.C. Apr. 10, 2019) (Contempt Order).↩
16. The *Washington Post* published a lengthy news article on this case on June 25, 2019: "Chinese bank involved in probe on North Korean sanctions and money laundering faces financial 'death penalty'," https://www.washingtonpost.com/local/legal-issues/chinese-bank-involved-in-probe-on-north-korean-sanctions-and-money-laundering-faces-financial-death-penalty/2019/06/22/.↩
17. *In Re: Sealed Case,* ___ F.3d ___, 2019 WL 3558735 (D.C. Cir. Aug. 6, 2019).↩

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