

THE INADEQUATE UTILIZATION OF THE ACCOUNTING PROFESSION IN THE UNITED STATES GOVERNMENT'S FIGHT AGAINST MONEY LAUNDERING*

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INTRODUCTION

Money laundering is a very serious worldwide problem that requires immediate solutions.¹ The true magnitude of the money laundering problem is impossible to ascertain simply because it increases dramatically on a daily basis.² While recent studies reveal that money laundering is a “\$500 billion problem worldwide,”³ some experts estimate it to be a trillion dollar problem.⁴

* This article was presented in the New York University School of Law seminar “Developing Issues in Financial Reporting: The Latest Developments in Accountants’ Responsibilities.” I am extremely grateful for the invaluable support and feedback I received from the audience, including New York University School of Law professors Abraham Stanger and Stanley Siegel.

I am honored to present this work as my contribution to the Accounting Subgroup of the United States Treasury Department Bank Secrecy Act Advisory Group, which invited me to join its team and assist in developing anti-money laundering rules and regulations.

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1. See generally *Taking the Profit Out of Drug Trafficking: The Battle Against Money Laundering: Hearing Before the Subcomm. on Crime of the House Comm. on the Judiciary*, 105th Cong. 118-27 (1997) (statement of Brendan T. Hewson, Senior V.P., Int’l Investigations, NationsBank) [hereinafter Hewson Testimony], microformed on CIS No. 99-H521-48 (Cong. Info. Serv.).

2. See *id.*

3. *H.R. 4005—Money Laundering Deterrence Act of 1998 & H.R. 1756—Money Laundering and Financial Crime Strategy Act of 1997: Hearing Before the House Comm. on Banking and Fin. Services*, 105th Cong. 12 (1998) (statement of Sen. Charles E. Grassley), microformed on CIS No. 99-H241-6 (Cong. Info. Serv.).

4. FIN. CRIMES ENFORCEMENT NETWORK, U.S. DEP’T OF THE TREASURY, PROPOSED ADDENDUM TO AICPA AUDIT RISK ALERT: SECURITIES INDUSTRY DEVELOPMENTS—MONEY LAUNDERING RISK AND RELATED REGULATORY DEVELOPMENTS 2 (1998) [hereinafter PROPOSED ADDENDUM TO AICPA]. Due to the very nature of the crime, it is extremely difficult to ascertain the true magnitude of the money laundering problem. The latest attempt made by the G-7 Economic Summit Group’s Financial

The United States has tried to stop money laundering, or at least decrease its dimensions, by enacting a range of anti-money laundering laws.⁵ These laws, however, are generally ineffective, and the majority of money laundering activities remain undetected.⁶ The United States must make more effective efforts in its war against money laundering. Otherwise, money laundering will “erode the integrity of our nation’s and the world’s financial institutions.”⁷

Action Task Force (FATF) to quantify the extent of the money laundering problem was unsuccessful. FIN. ACTION TASK FORCE, FATF-VIII MONEY LAUNDERING TYPOLOGIES EXERCISE: PUBLIC REPORT 2 (Feb. 5, 1997) [hereinafter FATF-VIII], available at <http://www.treas.gov/fincen/fatfnet.html> (stating that “the vast majority of FATF members lack sufficient data to support any credible estimate”). Consequently, it is not surprising that no country has been able to generate any extensive statistical data on money laundering. See *id.* While efforts to “get a grasp” on the money laundering problem continue, many have begun to question the “practicability of continuing attempts to estimate.” *Id.* Even without statistical evidence, however, all commentators seem to agree that any data, once generated, will represent only the tip of the money laundering iceberg. *Id.*

5. E.g., Annunzio-Wylie Anti-Money Laundering Act, Pub. L. No. 102-550, 106 Stat. 4044 (1992) (codified in scattered sections of 12 U.S.C., 18 U.S.C., and 31 U.S.C.); Money Laundering Control Act of 1986, tit. 1, subtit. H, Pub. L. No. 99-570, 100 Stat. 3207 (codified as amended 18 U.S.C. §§ 1956-1957; 31 U.S.C. §§ 5314-5326 (1988 & Supp. IV 1992)); Bank Secrecy Act, Pub. L. No. 91-508, 84 Stat. 114 (1970) (codified as amended at 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959, and 31 U.S.C. §§ 5311-5330). One author notes that “[t]he Bank Secrecy Act of 1970 is the commonly used name for a statute that was originally known as the Financial Record-keeping and Currency and Foreign Transactions Reporting Act of 1970.” Peter E. Meltzer, *Keeping Drug Money from Reaching the Wash Cycle: A Guide to the Bank Secrecy Act*, 108 BANKING L.J. 230, 230 n.2 (1991).

6. See *Private Banking and Money Laundering: A Case Study of Opportunities and Vulnerabilities: Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Governmental Affairs*, 106th Cong. 85-87 (1999) (statement of Raymond W. Baker, Guest Scholar in Economic Studies, The Brookings Institution, Washington, D.C.) [hereinafter Baker Testimony], microformed on CIS No. 00-S401-17 (Cong. Info. Serv.); *Private Banking and Money Laundering: A Case Study of Opportunities and Vulnerabilities: Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Governmental Affairs*, 106th Cong. 107 (1999) (statement of Sen. Carl Levin) [hereinafter Levin Testimony], microformed on CIS No. 00-S401-17 (Cong. Info. Serv.); *Private Banking and Money Laundering: A Case Study of Opportunities and Vulnerabilities: Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Governmental Affairs*, 106th Cong. 1113 (1999) (statement of Ralph E. Sharpe, Deputy Comptroller for Community and Consumer Policy, Office of the Comptroller of Currency, Department of the Treasury, Washington, D.C.) [hereinafter Sharpe Testimony], microformed on CIS No. 00-S401-17 (Cong. Info. Serv.); Hewson Testimony, *supra* note 1, at 123; Joseph Kahn, *Money Laundering Prompts U.S. Drive for a Tougher Law*, N.Y. TIMES, March 2, 2000, at A1 (describing Clinton Administration’s criticism of current laws that “do not provide enough authority to fight money laundering”).

7. *Basic Facts About Money Laundering and FinCEN*, FINCEN ADVISORY (U.S. Dep’t of the Treasury, Fin. Crimes Enforcement Network, Washington, D.C.), Mar. 1996, at 2 [hereinafter FinCEN Advisory].

Due to the nature of their profession, accountants are well positioned to detect and report money laundering activities. They already carry out similar responsibilities with a great degree of success⁸ and have access to their clients' business operations and records.⁹ Contrary to the public's perception,¹⁰ however, laws do not place affirmative¹¹ anti-money laundering obligations on accountants. Presently, the only affirmative obligation on accountants requiring them to address their clients' illegal acts is overly broad and fails to specifically combat the money laundering problem.¹² Ironically, governments of other countries require American accounting firms to fight money laundering outside the United States.¹³ Several of these countries already successfully utilize accountants' valuable skills in the fight against money laundering.¹⁴

In order for the United States government to wage a more successful war against money laundering, Congress should enact rules and regulations that make accountants responsible for detecting and reporting money laundering activities during their audits.¹⁵ These af-

8. *Infra* notes 85-92 and accompanying text.

9. *Infra* notes 72-74 and accompanying text.

10. See TED J. FIFLIS, ACCOUNTING ISSUES FOR LAWYERS 653-61 (1991) (discussing public's perception that quality of auditor performance is lower than it actually is due to assumption that fraudulent financial reporting is involved in every instance of business failure); VINCENT M. O'REILLY ET AL., MONTGOMERY'S AUDITING 19 (11th ed. 1990).

11. This article differentiates general anti-money laundering laws that criminalize money laundering from affirmative anti-money laundering laws that require certain parties to "police" money laundering activities. An example of an affirmative money laundering law would be a requirement that a bank, upon becoming aware that its customers are involved in money laundering, report this knowledge to the government.

12. See Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended at 15 U.S.C. § 78a).

13. *Infra* notes 140-41 and accompanying text.

14. *Infra* notes 128-39 and accompanying text.

15. The proposition of this article extends to accountants' audits of companies registered subject to the 1934 Securities Exchange Act. During these audits, auditors owe a special duty of loyalty to the investing public and not to their clients. *United States v. Arthur Young & Co.*, 465 U.S. 805, 817 (1984). This special relationship between accountants and the investing public does not necessarily exist when accountants are engaged to perform other types of work for their clients. Affirmative anti-money laundering responsibilities could, theoretically, be placed on those accountants performing other types of engagements, and although this complex proposition is ripe for further investigation, it is outside the scope of this article and will not be addressed. Furthermore, throughout this article, the terms auditor and accountant are used interchangeably and should be understood to denote a professional accountant who offers auditing services to companies registered under the Securities Exchange Act of 1934. Finally, although there is no statistical information on the extent of the money laundering problem in any segment of an industry, *supra* note 4, there

firmative anti-money laundering responsibilities would be very similar to those already placed on financial institutions.¹⁶

Part I of this article provides a general background on money laundering. Part II discusses why laws should place affirmative anti-money laundering responsibilities on accountants. Part III proposes specific changes to the current anti-money laundering laws. Part IV addresses potential problems with these recommendations and suggests a number of corresponding solutions. Part V discusses the urgent need for congressional involvement in enacting legislation that would require the accounting profession to assume additional anti-money laundering responsibilities.

I

BACKGROUND

A. *Definition of Money Laundering*

The term “money laundering” describes the process of concealing the true owners of illegally obtained funds.¹⁷ This process gives legitimacy to criminal funds by “washing” them through various institutions “so [that] they can be used without detection of the illegal activity that produced them.”¹⁸ Each phase of money laundering, also known as a “washing cycle,” removes a “layer of the taint or criminal staining from those funds.”¹⁹

Generally, the money laundering process consists of three phases: placement, layering, and integration of money.²⁰ The first phase,

are numerous examples of audited enterprises that have been tainted by money laundering. *E.g.*, Michael Allen, *Fridge Connection: A Tangled Tale of GE, Appliance Smuggling and Laundered Money*, WALL ST. J., Dec. 21, 1998, at A1 [hereinafter Allen, *Fridge Connection*] (explaining techniques used by drug dealers to launder money through foreign trade); Michael Allen & Paul Beckett, *Bank's Monitoring System Is Scrutinized*, WALL ST. J., Aug. 27, 1999, at A2 [hereinafter Allen & Beckett, *Bank's Monitoring System*] (discussing money laundering scandals of Mexican banks that do business, and are audited, in United States); Paula Dwyer, *How to Wring Out Money Launderers*, BUS. WK., Nov. 22, 1999 (discussing Citibank's involvement in money laundering); Victor Kamber, *Transparency Can Save BoNY from Being the Ugly American of Banking*, FUTURE BANKER, June 2000, at 38s (discussing Bank of New York's involvement in money laundering); Julia Preston, *Mexicans Belittle Drug-Money Sting*, N.Y. TIMES, May 20, 1998, at A6 (discussing indictment of Mexican banks for money laundering); Jay Solomon, *Money Laundering Is Cited in Probe of Bank Bali Affair*, WALL ST. J., Nov. 1, 1999, at A45 (noting role of Price-waterhouseCoopers audit inquiry into allegations of money laundering).

16. *Infra* notes 142-150 and accompanying text.

17. Hewson Testimony, *supra* note 1, at 120.

18. *Id.* at 115-16.

19. *Id.* at 119.

20. Meltzer, *supra* note 5, at 231.

placement, occurs when funds derived from criminal activity are introduced for the first time to a legitimate financial institution.²¹ During the second phase, layering, funds are transferred to and from various financial institutions in order to make it difficult for authorities to trace those funds to the location of their initial deposit.²² Finally, the integration phase legitimizes the “dirty” funds by transferring them to legitimate business enterprises.²³

B. Dangers of Money Laundering

Money laundering has “devastating social and economic consequences.”²⁴ Corruption is one such consequence.²⁵ Criminals who possess large amounts of “dirty” funds are often willing to pay as much as eight percent of those funds to anyone who is in a position to launder their money.²⁶ This causes many otherwise law-abiding employees of the government and private enterprises to commit criminal acts of money laundering.²⁷

The increase in underlying crimes is another consequence of money laundering. The ability to dispose of illegally obtained funds without being noticed gives criminals an extra incentive to repeat their crimes. Whether these underlying crimes are drug trafficking, robberies, or extortion, they disturb the lives of millions and the economies of many countries, including our own.²⁸ The ease of laundering illegally obtained funds causes an increase in the amount of drugs sold on the streets, and, consequently, in the burden on law enforcement and healthcare. The government must spend money policing the streets and treating drug addiction, using funds that would otherwise be avail-

21. *Id.*

22. *Id.*

23. *Id.*

24. FinCEN Advisory, *supra* note 7, at 2.

25. See Baker Testimony, *supra* note 6, at 80-87, 1053-60 (discussing influence of money laundering on corruption); Julie Fendo, Comment, *Attacking the Tools of Corruption: The Foreign Money Laundering Deterrence and Anticorruption Act of 1999*, 23 FORDHAM INT'L L.J. 1540, 1550-54 (2000) (describing how money laundering corrupts “government officials of various countries”); see also U.S. DEP'T OF STATE, INTERNATIONAL NARCOTICS CONTROL STRATEGY REPORT (1995), available at <http://dosfan.lib.uic.edu/ERC/law/INC/1995/11.html> [hereinafter STRATEGY REPORT] (discussing effect that money laundering has on corruption).

26. *Current Trends in Money Laundering: Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Governmental Affairs*, 102d Cong. 41 (1992) (statement of Ron Eatinger, Chief, Criminal Investigations Division, Internal Revenue Service, Houston, Tex.), microformed on CIS No. 92-S401-33 (Cong. Info. Serv.).

27. See STRATEGY REPORT, *supra* note 25.

28. See *id.*; see also FinCEN Advisory, *supra* note 7, at 3.

able for important social programs. The government is thus forced to decide between cutting back on those other socially beneficial programs and generating additional funds through increased taxation of its citizens. As this example illustrates, those not directly affected by drug trafficking suffer from its indirect consequences.

C. An Overview of United States Anti-Money Laundering Initiatives

The United States government has imposed affirmative anti-money laundering guidelines primarily on banks and other similar financial institutions²⁹ because of their constant dealings with money and their historical involvement in money laundering schemes.³⁰ For example, in 1970 the United States enacted the Bank Secrecy Act (“Secrecy Act”),³¹ which requires financial institutions to file a Currency Transaction Report (CTR) with the government every time a customer executes one or more cash transactions totaling greater than

29. For example, 31 C.F.R. § 103.11 (1999) lists the following institutions obligated to file Currency Transaction Reports:

- (c) *Bank*. Each agent, agency, branch or office within the United States of any person doing business in one or more of the capacities listed below:
 - (1) A commercial bank or trust company organized under the laws of any State of the United States;
 - (2) A private bank;
 - (3) A savings and loan association or a building and loan association
 - ...
 - (6) A credit union organized under the law of any State or of the United States;
 - ...
- (f) *Broker or dealer in securities*. A broker or dealer in securities, registered or required to be registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934.

In order to simplify the references within this article, the article will refer to these institutions in aggregate as “financial institutions.”

30. See Sharpe Testimony, *supra* note 6, at 1113-14 (outlining current and proposed laws designed to shield banking industry from money laundering); see also, e.g., Allen & Beckett, *Bank’s Monitoring System*, *supra* note 15, at A2; Kathleen Day, *Federal Bank Oversight Faulted: Testimony, Treasury Report Hit Anti-Money Laundering Effort*, WASH. POST, Nov. 11, 1999, at E2 (discussing vulnerability of banking to money laundering); Preston, *supra* note 15, at A6 (discussing Mexican banks’ money laundering scandals).

31. Bank Secrecy Act, Pub. L. No. 91-508, 84 Stat. 114 (1970) (codified as amended at 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959, and 31 U.S.C. §§ 5311-5330).

\$10,000.³² The Secrecy Act imposes serious penalties for failure to follow its requirements.³³

The Secrecy Act also authorizes the Secretary of the Treasury to issue rules and regulations requiring financial institutions to keep records and file reports, which are highly useful to governmental investigations.³⁴ The Treasury Department has delegated the responsibility to enforce the Secrecy Act to the Financial Crimes Enforcement Network (“FinCEN”),³⁵ and has charged this agency to “formulate, oversee and implement policies to prevent and detect money laundering.”³⁶

The Money Laundering Control Act of 1986 (the “Control Act”) was enacted to reinforce the Secrecy Act.³⁷ The Control Act criminalizes the structuring of transactions to avoid the scope of CTR.³⁸ It also sets out three new criminal offenses: (1) participation in financial transactions that involve proceeds from specified unlawful activities; (2) international transportation of criminal proceeds; and (3) involvement in monetary transactions in property derived from proceeds obtained from criminal offenses.³⁹ To win a conviction under the Control Act, the prosecution must establish that the defendant knowingly dealt with funds derived from criminal activity.⁴⁰

The Annunzio-Wylie Anti-Money Laundering Act (“Annunzio-Wylie Act”), enacted into law in 1992,⁴¹ requires banks to obtain identification from all parties with whom they transact funds, regardless of whether the customers have accounts with those banks.⁴² The Annunzio-Wylie Act also enables the government to revoke foreign banks’ licenses to operate in the United States if any one of their branches is convicted of money laundering.⁴³ To avoid this and other penalties,

32. 31 C.F.R. § 103.22(b) (1999).

33. Failure to file a CTR is punishable by criminal fines, in an amount up to \$250,000, or five years in prison, or both. 31 C.F.R. § 103.49(b) (1999).

34. 31 C.F.R. § 103.20 (1999).

35. 12 C.F.R. §§ 208.62(c), 353.3(a) (2000). See U.S. Dep’t of the Treasury, Fin. Crimes Enforcement Network, *Frequently Asked Questions*, at <http://www.treas.gov/fincen/faqs.html>.

36. FinCEN Advisory, *supra* note 7, at 3.

37. See 18 U.S.C. §§ 1956, 1957 (1994).

38. *Infra* note 93 and accompanying text.

39. *Id.*

40. 18 U.S.C. §§ 1956(a), 1957(a) (1994).

41. Annunzio-Wylie Anti-Money Laundering Act, Pub. L. No. 102-550, 106 Stat. 4044 (1992) (codified in scattered sections of 12 U.S.C., 18 U.S.C., and 31 U.S.C.).

42. *Id.* at § 1511.

43. *Id.* at § 1502.

the Annunzio-Wylie Act requires banks to take several steps to prevent the occurrence of money laundering.⁴⁴

In addition, the United States Treasury Department's anti-money laundering regulations require financial institutions to actively participate in a fight against money laundering⁴⁵ by establishing an internal anti-money laundering infrastructure that facilitates the detection and reporting of money laundering activities.⁴⁶ For example, these regulations require institutions both to designate an anti-money laundering officer responsible for the supervision and coordination of the institution's anti-money laundering efforts, and to develop anti-money laundering policies and procedures. Among other things, these policies and procedures give employees guidance on how to file a CTR.⁴⁷

Financial institutions are also required to implement Know Your Customer (KYC) policies and procedures,⁴⁸ designed to enable institutions to identify customers' potential money laundering activities.⁴⁹ The KYC regulations require financial institutions to acquire detailed information on their customers, including sources of funds, subsidiary businesses, reasons for opening accounts, and expected types of account activities.⁵⁰ Financial institutions are then required to utilize this information when monitoring their customers' account activities for possible signs of money laundering.⁵¹

Finally, financial institutions are also required to file a Suspicious Activity Report (SAR) with the government each time they suspect that a customer has laundered money.⁵² The SAR regulations provide examples of suspicious customer activities. For instance, a financial institution is required to file a SAR if a customer continually transfers funds between different accounts or banks without an apparent business reason,⁵³ withdraws amounts that are just below the reporting

44. *Id.* at § 1515.

45. *See* 31 C.F.R. § 103.21 (1999).

46. 31 U.S.C. § 5318(h) (1994).

47. *Id.* (authorizing and giving guidance on anti-money laundering programs, and discussing required policies, compliance officers, training programs, and independent audit procedures).

48. *See* Suspicious Transactions Reporting Requirements, 61 Fed. Reg. 4326, 4329 (Feb. 5, 1996) (to be codified at 31 C.F.R. pt. 103) (stating that institution must utilize "knowledge of its customer" in determining whether or not activity is suspicious).

49. *See id.*

50. *See id.*

51. *See id.*

52. 12 C.F.R. §§ 208.62, 211.8, 353.3 (2000); 31 C.F.R. § 103.21 (1999); 31 U.S.C. § 5318(g)(1) (1994).

53. 12 C.F.R. § 208.62(c)(4)(i)-(iii) (2000); 12 C.F.R. § 353.3(a)(4)(i)-(iii) (2000); 31 C.F.R. § 103.21(a)(2)(i)-(iii) (1999).

threshold, or attempts to modify transactions subsequent to learning of the reporting requirements.⁵⁴

Unfortunately, the United States anti-money laundering legislation has not proven to be very effective in stopping the spread of money laundering.⁵⁵ The magnitude of the money laundering problem is greater than ever, and continues to increase dramatically.⁵⁶ In light of the ineffectiveness of the current crusade against money laundering, the historical exclusion of the accounting profession from the list of professions charged with anti-money laundering obligations should be reevaluated.

II

REASONS TO CHANGE THE CURRENT ANTI-MONEY LAUNDERING INFRASTRUCTURE AND PLACE AFFIRMATIVE ANTI-MONEY LAUNDERING OBLIGATIONS ON ACCOUNTANTS

A. *The Nature of the Public Accounting Profession*

Since its inception, the public accounting profession has provided assurance to federal, state, and local governments, as well as to individual investors, that audited enterprises comply with various rules and regulations.⁵⁷ There are four main reasons why accountants have been trusted with this responsibility. For these same reasons, accountants should be trusted with affirmative anti-money laundering responsibilities.

First, accountants operate independently from their clients⁵⁸—they are not agents or advocates.⁵⁹ When public accounting firms perform audits, they are under a professional obligation to protect the interests of investors, the government, and other third parties.⁶⁰ Courts have consistently stressed these obligations. In *United States v. Arthur Young & Co.*,⁶¹ the Supreme Court emphasized the indepen-

54. 12 C.F.R. § 208.62(c)(4)(i)-(iii) (2000); 12 C.F.R. § 353.3(a)(4)(i)-(iii) (2000); 31 C.F.R. § 103.21(a)(2)(i)-(iii) (1999).

55. See Baker Testimony, *supra* note 6, at 1057 (illustrating shortcoming of U.S. anti-money laundering efforts); Levin Testimony, *supra* note 6, at 107 (declaring ineffectiveness of U.S. efforts to combat money laundering); Hewson Testimony, *supra* note 1, at 123 (noting that law enforcement has been unable to stop money laundering).

56. See FATF-VIII, *supra* note 4, at 2.

57. D.R. CARMICHAEL & JOHN J. WILLINGHAM, AUDITING CONCEPTS AND METHODS: A GUIDE TO CURRENT AUDITING THEORY AND PRACTICE 2-3 (5th ed. 1989).

58. *Id.* at 44-45.

59. *Id.* at 42-43.

60. *United States v. Arthur Young & Co.*, 465 U.S. 805, 817-18 (1984) (citations omitted).

61. *Id.*

dent nature of accountants from their clients, stating: “The independent public accountant . . . owes ultimate allegiance to the corporation’s creditors and stockholders, as well as to the investing public. This public watchdog function demands that accountants maintain total independence from the client at all times and requires complete fidelity to the public trust.”⁶² The court added that to hold otherwise “would be to ignore the significance of the accountant’s role as a disinterested analyst charged with public obligations.”⁶³

Second, the accounting profession is highly regulated.⁶⁴ It is governed largely by the Generally Accepted Auditing Standards adopted by the American Institute of Certified Public Accountants (AICPA).⁶⁵ These standards guide accountants in ascertaining their clients’ compliance with rules and regulations.⁶⁶ The AICPA has also developed a Code of Professional Conduct⁶⁷ which outlines accountants’ ethical obligations. Various governmental agencies, such as the Securities and Exchange Commission (SEC), also prescribe standards that govern the conduct of public accountants.⁶⁸ The AICPA issues its own interpretations of these standards to ensure consistency in their application.⁶⁹ Accountants must follow each of these standards,⁷⁰ or face penalties imposed by the AICPA and other authorities for unwarranted deviations.⁷¹ If the U.S. government places the affirmative anti-money laundering responsibilities on accountants, it can rely upon the regulatory infrastructure surrounding accountancy to ensure compliance with these responsibilities.

Exposure to a client’s records and day-to-day operations is the third reason why an accountant is well positioned to successfully combat money laundering. In order to perform an annual audit properly, accounting firms must both obtain a detailed understanding of their clients’ businesses and test clients’ operations and controls.⁷² Auditors require that clients’ back office operations, from bank reconciliations to valuations of inventory, function at a level where they will not

62. *Id.* at 817-18.

63. *Id.* at 818.

64. *See* CARMICHAEL & WILLINGHAM, *supra* note 57, at 36.

65. *Id.* at 12, 37.

66. *See id.*

67. Am. Inst. of Certified Public Accountants, *AICPA Code of Professional Conduct*, available at <http://www.aicpa.org/about/code/index/htm>. *See also* CARMICHAEL & WILLINGHAM, *supra* note 57, at 39, 41-49.

68. CARMICHAEL & WILLINGHAM, *supra* note 57, at 16, 38, 52.

69. *See id.* at 12-16.

70. *See id.*

71. *Id.* at 49.

72. *Id.* at 76-77.

cause the financial statements to be materially misstated.⁷³ In order to gain this comfort, accountants must test all major business areas and records.⁷⁴ Thus, if the profession were required to specifically look for money laundering during audits, there would be a high likelihood of the detection of at least some, if not all, money laundering activities existing within the audited enterprise.

Even under the present regulatory scheme, in a number of instances auditors have been successful in discovering their clients' illegal acts, including money laundering.⁷⁵ The Bank of Credit and Commerce International (BCCI) scandal exemplifies the role independent public accountants have played in uncovering money laundering activities.⁷⁶ In the course of their audit, Price Waterhouse (PW), BCCI's auditors, discovered that BCCI was involved in extensive money laundering, bribery, fraud, and other illegal activities.⁷⁷ PW

73. See AM. INST. OF CERTIFIED PUBLIC ACCOUNTANTS, STATEMENT ON AUDITING STANDARDS NO. 47, AUDIT RISK AND MATERIALITY IN CONDUCTING AN AUDIT 2 (1983) ("Financial statements are materially misstated when they contain errors or irregularities whose effect, individually or in the aggregate, is important enough to cause them not to be presented fairly in conformity with generally accepted accounting principles.") (citations omitted).

74. See CARMICHAEL & WILLINGHAM, *supra* note 57, at 76-77.

75. See, e.g., Allen, *Fridge Connection*, *supra* note 15, at A1 (auditing of General Electric appliance distributors); Paul Beckett & Michael Allen, *Bank of New York Probed on IMF Aid*, WALL ST. J., Aug. 23, 1999, at A3 [hereinafter Beckett & Allen, *Bank of New York*] (discussing report by PricewaterhouseCoopers revealing \$1.2 billion diverted from Russia's central bank); Kathleen Day, *Citibank Faulted in Probe*, WASH. POST, Nov. 5, 1999, at E1 (auditing of Citibank private banking unit); James C. McKinley Jr., *Police Search the Cash Boxes of Belmont Betting Clerks for Evidence of Money Laundering*, N.Y. TIMES, Sept. 28, 2000, at B7 (auditing race track cash boxes); Lynda Richardson, *Car Dealer Gets 5 Years for Bilking G.M. of More Than \$400 Million*, N.Y. TIMES, Aug. 10, 1996, at A25 (auditing car dealership); *Sentencing in Fraud Case*, N.Y. TIMES, Jan. 29, 1991, at D9 (auditing defense contractor).

76. See Duncan E. Alford, *Basle Committee Minimum Standards: International Regulatory Response to the Failure of BCCI*, 26 GEO. WASH. J. INT'L L. & ECON. 241, 258-290 (1992). See also *BCCI: Dead and Buried*, ECONOMIST, Apr. 15, 2000, at 82 (revising BCCI scandal to highlight continuing vulnerability of financial institutions to money laundering); Steve Lohr, *At the End of a Twisted Trail, Piggy Bank for a Favored Few: World-Class Fraud, How B.C.C.I. Pulled It Off*, N.Y. TIMES, Aug. 12, 1991, at A1 (describing process by which BCCI laundered money and how auditors uncovered fraud).

77. BCCI secretly controlled three American Banks and

The bank carried favor with [] prominent people through charitable donations or consulting fees, including former President Jimmy Carter and former Prime Minister James Callaghan of Britain, to lend B.C.C.I. an aura of influence and respectability.

And the bank maintained secret accounts for a collection of people and institutions that reads like a list of characters and organizations for a spy novel: Saddam Hussein, Abu Nidal, Manuel Noriega, the Central

reported its findings, thus leading to the seizure of BCCI by international regulators.⁷⁸

Furthermore, because of their access to client records and operations, auditors have always been reliable “watch dogs”⁷⁹ not only for third parties, but also for their clients’ management. Management is not always responsible for, or even aware of, illegal acts that take place in a company. Auditors’ detail-oriented approach, combined with their required “professional skepticism,”⁸⁰ frequently puts them in a better position than their clients’ own management to identify unauthorized activities.⁸¹ If placed on accountants, affirmative anti-money laundering responsibilities will inevitably give rise to even more instances of money laundering detection.

Fourth, the imposition of affirmative anti-money laundering responsibilities on accountants will help to prevent, not merely detect, money laundering by their clients.⁸² Once accountants implement proposed anti-money laundering requirements,⁸³ they will be better equipped to identify money laundering activities. These changes will give accountants an elevated sense of responsibility that, when coupled with familiarity with money laundering activities and constant access to companies’ records and operations,⁸⁴ will most certainly discourage potential money launderers. In addition, clients will realize that the chances of the government finding out about their money

Intelligence Agency and an assortment of drug runners and arms merchants.

Lohr, *supra* note 76, at A1.

78. *See id.*

79. *See* United States v. Arthur Young & Co., 465 U.S. 805, 818 (1984) (citations omitted). *See also* FIFLIS, *supra* note 10, at 660.

80. AM. INST. OF CERTIFIED PUBLIC ACCOUNTANTS, STATEMENT ON AUDITING STANDARDS No. 82, CONSIDERATION OF FRAUD IN A FINANCIAL STATEMENT AUDIT 19 (1997) (defining professional skepticism as a “questioning mind and critical assessment of audit evidence”). *See also* FIFLIS, *supra* note 10, at 660.

81. *See, e.g.*, Allen, *Fridge Connection*, *supra* note 15, at A1 (auditing of General Electric appliance distributors); Paul Beckett, *Bank of New York Lapses Seen in Russian Case*, WALL ST. J., Feb. 8, 2000, at A4 (noting Bank of New York’s use of auditors to detect money laundering in wake of scandal); Beckett & Allen, *Bank of New York*, *supra* note 75, at A3 (discovery of fraud by auditors); Day, *supra* note 75, at E1 (auditing of Citibank private banking unit); Day, *supra* note 30, at E2 (noting need for audits to deter money laundering); McKinley Jr., *supra* note 75, at B7 (auditing of race track cash boxes); Richardson, *supra* note 75, at A25 (auditing car dealership); *Sentencing in Fraud Case*, *supra* note 75, at A1 (describing auditors’ discovery that alleged annual shipments of thousands of vehicles overseas per month were false).

82. Hewson Testimony, *supra* note 1, at 117 (noting that “the primary focus of all . . . should be prevention not detection” of money laundering).

83. *Infra* notes 143-51 and accompanying text.

84. *See* CARMICHAEL & WILLINGHAM, *supra* note 57, at 76-77.

laundering activities will increase if accountants are charged with detecting and reporting money laundering. As with any attempt to eliminate criminal activity, some companies will respond by continuing to break the law and absorbing the increased cost. If money launderers choose to continue their illegal activities, the imposition of affirmative anti-money laundering responsibilities on accountants will force them to look for new, more expensive, and complex ways to launder their money. While aiming at its complete extinction, the proposed regulations, at the very least, will reduce money laundering.

Requiring accountants to actively fight money laundering will not force the profession to undergo any profound changes.⁸⁵ The accounting profession is well-trained and has unparalleled experience in successfully executing monitoring and reporting responsibilities. Affirmative anti-money laundering regulations will simply require diversification of these responsibilities.

To illustrate, accountants currently perform a wide range of attestation and compilation services, such as audits and regulatory compliance reviews.⁸⁶ When performing these services, accountants are required both to ascertain whether their clients violate certain securities and financial reporting regulations,⁸⁷ and to report such violations to the designated corporate authority.⁸⁸ Accountants would be required to follow exactly the same process if they were charged with detection and reporting violations of anti-money laundering laws.

A number of major accounting firms already perform services that deal with money laundering. These firms have departments, known as litigation support or forensic accounting departments, that assist law firms in their trial-related work.⁸⁹ This work often involves the investigation of illegal acts, including money laundering.⁹⁰ These departments are familiar with various money laundering techniques,

85. John Mahon, a technical partner at Coopers and Lybrand, Ireland has said, "We do not envisage the extension of the money laundering regulations to auditors and accountants as imposing any great burden on the profession." *Irish Law to Ferret Out Criminal Proceeds*, EUR. ACCT., Aug. 1, 1996, at 3.

86. CARMICHAEL & WILLINGHAM, *supra* note 57, at 531-33 (explaining types of auditing procedures).

87. *See id.* at 76-77.

88. *Id.* at 506-12.

89. For a thorough discussion of the role forensic accountants play in fraud investigations, see Harvey R. Kelly, *Digging Out the Fraud: The Forensic Accountants*, in ACCOUNTING IRREGULARITIES AND FINANCIAL FRAUD 89 (Michael R. Young ed. 2000). *See also* Elizabeth M. Fowler, 'Forensic Accountants' in Demand, N.Y. TIMES, July 16, 1991, at D17.

90. *See* Stefan D. Cassella, *Establishing Probable Cause for Forfeiture in Federal Money Laundering Cases*, 39 N.Y.L. SCH. L. REV. 163, 172 (1994 (noting use of forensic accountants to detect money laundering); *see also* Diane L. Womack, *Foren-*

and the latest anti-money laundering laws and regulations.⁹¹ The fact that these services already exist further reinforces the accounting profession's ability to combat money laundering.⁹²

B. Current Anti-Money Laundering Laws Are Not as Effective as They Should Be

1. Financial Institutions Are Not as Likely as Accountants to Identify Money Laundering

Financial institutions are generally exposed to single, isolated transactions of their customers, and therefore do not always have access to the information necessary to identify and report money laundering activities. For example, if Corporation A would like to deposit \$50,000 of its drug-related proceeds in its bank account without being reported to the government, it can simply make ten \$5,000 deposits in ten different financial institutions.⁹³ Each institution will only know of one deposit. Since there is nothing inherently suspicious about a single \$5,000 cash deposit, none of the financial institutions will file an SAR. In addition, because there is only one deposit made in each financial institution and because each deposit is significantly below the reportable \$10,000 threshold, none of the financial institutions will file a CTR. Consequently, while Corporation A is laundering money through the illegal act of "structuring,"⁹⁴ its money laundering activities will not be detected or reported by the financial institutions.

The ability to see the entire picture and not just single, isolated transactions puts accountants in a much better position than financial

sic Accountants in Criminal Cases, N.Y. L. J., July 22, 1996 at S1 (noting effectiveness of forensic accountants in, inter alia, money laundering cases).

91. See John L. Evans, *International Money Laundering: Enforcement Challenges and Opportunities*, 3 Sw. J. L. & TRADE REG. 195, 212 (1996) (arguing that law enforcement must work with, inter alia, forensic accountants to understand money laundering legislation). See also Lacy McCrary, *Papers Tie Magnet to Crime Lord*, PHILADELPHIA ENQUIRER, Dec. 11, 1998, at B6 (describing 50-page report by forensic accountants that detailed suspicious transactions that "raised the specter of money laundering.").

92. See, e.g., *Tracking Fraud Opens the Books for Accountants*, CHI. TRIB., Dec. 1, 1998, § 8, at 1 (noting that American Institute of Certified Public Accountants (AICPA) has initiated fraud seminars to prepare accountants to understand money laundering); Diana Kunde, *Revenge of the Nerds: Techie Accountants Turn Into Corporate Crime Busters*, CHI. TRIB., Nov. 15, 1998, § 6, at 3 (describing accounting firms' use of forensic accountants to uncover crimes such as money laundering).

93. If a party makes a deposit of \$10,000 or an amount close to it, banks are very likely to deem this deposit suspicious and report it on SAR due to potential "structuring." Structuring means utilizing transactions designed to avoid money laundering reporting requirements. 31 C.F.R. § 103.22(b) (1999); 31 U.S.C. § 5324(a) (1994).

94. 31 C.F.R. § 103.22(b) (1999); 31 U.S.C. § 5324(a) (1994).

institutions to detect and report money laundering activities. Accountants could identify and report Corporation A's money laundering if they were required to do so. Their review of bank reconciliations would reveal that Corporation A made ten deposits in ten different financial institutions in one day, or during a period of several days.⁹⁵ Unless the client has a reasonable explanation, accountants will view these deposits as suspicious⁹⁶ and report Corporation A's activities to the government through the SAR.

Moreover, accountants are in a better position than financial institutions to ascertain the validity of the information received from suspected money launderers. For example, if a broker-dealer company decides to begin laundering money, it can go to a bank with which it has never dealt and open an account for a new "shipping" business. To make its new business appear legitimate, this broker-dealer can even enter into a number of legitimate short-term shipping contracts. Although financial institutions are required by the KYC regulations to know their customers' businesses and purposes for opening accounts⁹⁷ in order to enable them to spot suspicious activities, in reality their ability to do so is very limited.⁹⁸ Generally, financial institutions can only verify the legitimacy of the information the client provides.⁹⁹ If the client has other businesses under different names, this information is likely to remain undiscovered by the financial institutions. Because of their limited resources, financial institutions rarely go beyond verifying the existence and validity of names and addresses.¹⁰⁰ As a result, it is likely that the broker-dealer can operate its money laundering activities under the "shipping" business umbrella without being detected and reported.

In an effort to ascertain whether the new "shipping" business is legitimate, accountants will go much further than financial institutions

95. In *In re Montross*, 209 B.R. 943, 946 (B.A.P. 9th Cir. 1997), the accountant detected money laundering activities by comparing cash receipts and disbursement journals to bank records. In addition, "accountant discovered . . . a separate journal . . . for . . . record[ing] . . . money laundering activity." *Id.*

96. *See id.*

97. *See* Suspicious Transactions Reporting Requirements, 61 Fed. Reg. 4326, 4329 (Feb. 5, 1996) (to be codified at 31 C.F.R. pt. 103); 31 U.S.C. § 5318(h) (1994) (authorizing government to require financial institutions to have anti-money laundering programs, which can include policies, compliance officers, training programs, and independent audit procedures).

98. Fendo, *supra* note 25, at 1547-50 (noting, for example, that "U.S. financial institution that houses the [pass through account (PTA)] has no independent way of knowing the identity of their PTA customers").

99. *See id.*

100. *See id.*

in verifying the information provided by the client. Under professional standards, accountants become intimately familiar with a client's current and historical business records while performing audits.¹⁰¹ Accountants gain a thorough understanding of a client's new business, its economics, and mechanics.¹⁰² They test the existence and completeness of the information received from the client through confirmations of contracts and analysis of selected individual transactions.¹⁰³ Furthermore, accountants' testing of the new business continues during future annual audits.¹⁰⁴ Consequently, accountants are more likely than financial institutions to really get to know their customers, as well as identify and report money laundering activities.

2. *The Law that Does Apply to Accountants Is Ineffective Against Money Laundering*

In an effort to have the accounting profession assist in identifying and reporting illegal acts of companies registered under the 1934 Securities Exchange Act ("1934 Act"),¹⁰⁵ Congress enacted the Private Securities Litigation Reform Act (the "Tort Reform Act") on December 22, 1995.¹⁰⁶ The Tort Reform Act requires accountants to implement procedures which enable them to identify clients' illegal acts that have a "direct" and "material" effect on financial statements.¹⁰⁷ It defines an "illegal act" as an "act or omission that violates any law, or any rule or regulation having the force of law."¹⁰⁸ The AICPA issued requirements that basically parallel those outlined in the Tort Reform Act.¹⁰⁹ As a result, there is a public perception that auditors are re-

101. See CARMICHAEL & WILLINGHAM, *supra* note 57, at 490-92 (describing "continuing auditor" as "an auditor who has audited the immediate past period for the periods [audited]").

102. See *id.* at 86.

103. See *id.*

104. See *id.* at 490-92.

105. 15 U.S.C. § 78j (1994).

106. Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended at 15 U.S.C. § 78a).

107. *Id.* § 301.

108. *Id.*

109. Statement on Auditing Standards No. 54 defines the term illegal acts as "violations of laws or government regulations." AM. INST. OF CERTIFIED PUBLIC ACCOUNTANTS, STATEMENT ON AUDITING STANDARDS NO. 54, ILLEGAL ACTS BY CLIENTS I (1988) [hereinafter ILLEGAL ACTS BY CLIENTS]. Paragraph 17 of SAS No. 54 requires an auditor to assure that the audit committee or others with equivalent authority inside the company are adequately informed with respect to illegal acts that come to auditor's attention. See *id.* at 7. The auditor should also consider the effect of any noncompliance on the financial statements and should modify the auditor's report on those financial statements as necessary in accordance with Statement on Auditing Standards No. 58. See *id.* at 7-8; see generally AM. INST. OF CERTIFIED PUBLIC AC-

sponsible for identifying and reporting all illegal acts committed by their clients,¹¹⁰ including money laundering. There are three reasons, however, why the Tort Reform Act is ineffective against money laundering.

First, although an illegal act of money laundering usually has a *material* effect,¹¹¹ it generally does not have a *direct* effect on the financial statements of the company.¹¹² In the following passage, the AICPA illustrates the difference between direct and indirect effects on financial statements in the context of securities trading:

Entities may be affected by many . . . laws or regulations, including those relating to securities trading Generally, these laws and regulations relate more to an entity's operating aspects than to its financial aspects, and their financial statement effect is indirect. . . . Their indirect effect is normally the result of the need to disclose a contingent liability because of the allegation or determination of illegality. For example, securities may be purchased or sold based on inside information. While the direct effects of the purchase or sale may be recorded appropriately, their indirect effect, the possible contingent liability for violating securities laws, may not be appropriately disclosed.¹¹³

Thus, under the Tort Reform Act, auditors are not required to tailor their auditing procedures to detect money laundering because its effect upon financial statements is generally indirect.¹¹⁴ In light of this nuance, the overwhelming majority of money laundering activities are not discovered by auditors.¹¹⁵ For example, auditors failed to de-

COUNTANTS, STATEMENT ON AUDITING STANDARDS NO. 58, REPORTS ON AUDITED FINANCIAL STATEMENTS (1988).

110. See FIFLIS, *supra* note 10, at 653-61; O'REILLY ET AL., *supra* note 10, at 102.

111. Legal costs that arise from money laundering related prosecutions, as one would expect, are substantial and most of the time material to the financial statements. As a result, these costs require a special disclosure in the footnotes to the financial statements of the reporting institution. In *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 439, 448 (1976), the Supreme Court held that an item is material if "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote" or whether or not to invest in the company. *Id.*

112. See PROPOSED ADDENDUM TO AICPA, *supra* note 4, at 3.

113. ILLEGAL ACTS BY CLIENTS, *supra* note 109, at 2-3.

114. See *supra* notes 106-08 and accompanying text. Theoretically, it is possible to come up with circumstances under which money laundering would have a direct effect on financial statements. The likelihood of that actually occurring, however, is extremely small. In the absence of affirmative obligations, accountants will not consider this possibility to warrant designing auditing procedures to detect money laundering. See generally PROPOSED ADDENDUM TO AICPA, *supra* note 4, at 3 (discussing ineffectiveness of accounting laws in dealing with money laundering issues).

115. See generally PROPOSED ADDENDUM TO AICPA, *supra* note 4, at 3.

tect the money laundering activities of the DeLorean Motor Company.¹¹⁶ In *Allard v. Arthur Andersen & Co.*, the plaintiff, a trustee of the DeLorean Motor Company, argued that Mr. DeLorean was laundering his illegally obtained funds by “siphoning away millions of dollars for himself and others through a fictional Panamanian company that had a post office box in Switzerland.”¹¹⁷ During their audits, however, Arthur Andersen did not discover any traces of money laundering,¹¹⁸ most likely because such activity was unlikely to have had a material and direct effect on DeLorean’s financial statements. For the same reason, it is very likely that Arthur Andersen did not even consider possible money laundering activities when designing their auditing procedures.

Second, even if money laundering were to have a direct effect on financial statements, accountants are not as prepared as they could be to deal with the problem. Accountants are not required to institute internal anti-money laundering infrastructure.¹¹⁹ The availability of such an infrastructure, however, would help accountants become more familiar with various money laundering techniques, the latest anti-money laundering laws, and their personal anti-money laundering responsibilities. This increased knowledge of money laundering related issues would make accountants better prepared to detect and report money laundering.

Finally, even if accountants detect money laundering activities, there is no guarantee that the government will be notified. Under the Tort Reform Act, an accountant, upon discovering information that an illegal act might have occurred or did occur, is required to report the findings to the appropriate level of clients’ management and not to the government.¹²⁰ Only when an accountant is dissatisfied with management’s remediation of the illegal act, does she have an obligation to report the act to the Board of Directors (“Board”) of the company.¹²¹ The Board is then required to notify the SEC within one day of being

116. *Allard v. Arthur Andersen & Co.*, 957 F. Supp. 409 (S.D.N.Y. 1997).

117. Melody Petersen, *DeLorean Jury Rules Against Arthur Andersen*, N.Y. TIMES, Mar. 6, 1998, at D1.

118. *See id.*

119. *Supra* notes 29-56 and accompanying text.

120. The auditor is required to report identified illegal acts to the appropriate level of the client’s management, unless the identified illegal act is “clearly inconsequential.” Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, § 301(b), 109 Stat. 737, 762-64 (codified as amended at 15 U.S.C. § 78a).

121. *Id.* at § 301(b)(2).

notified by the accountant.¹²² The Act requires accountants to directly notify the SEC¹²³ only if the Board does not do so.¹²⁴

Thus, if the auditor is satisfied with the management's "remedial" actions, she is relieved from the obligation to report the illegal act either to the government or to the BOD.¹²⁵ It is, however, very possible that the management might simply create an appearance of taking appropriate remedial actions in order to prevent auditors from reporting their findings. For example, the management could begin its own investigations, establish internal controls designed to prevent the type of identified illegal acts from taking place in the future, or even fire a number of employees. These actions might satisfy the auditors and, as a result, no officials outside the company would ever find out about the occurrence of the illegal act.

C. *Accountants Are Already Successfully Utilized by Foreign Governments in Their Fight Against Money Laundering*

The international community has long recognized the enormous assistance accountants can provide in the war against money laundering.¹²⁶ Since 1996, accountants in the United Kingdom have been charged with affirmative responsibilities to fight money laundering.¹²⁷ British accountants are required to establish know your client procedures.¹²⁸ Unlike their American counterparts, they are also required to report their knowledge or suspicion of their clients' involvement in money laundering to the government.¹²⁹ In order to help accountants deal with their affirmative anti-money laundering responsibilities consistently and effectively, the British Institute of Chartered Accountants has developed thorough interpretations and guidelines for their accountants to follow.¹³⁰

122. *Id.* at § 301(b)(3).

123. *Id.*

124. *Id.* at § 301(b)(3)-(4).

125. *Id.* at § 301(b)(2).

126. *See, e.g., A Roundup of Money Laundering News*, MONEY LAUNDERING L. REP., Aug. 1996, at 8 (regarding guidelines issued by British Institute of Chartered Accountants in effort to combat money laundering); *Irish Law to Ferret Out Criminal Proceeds*, *supra* note 85, at 3 (discussing Irish law placing affirmative anti-money laundering obligations on accountants); Gundi Jeffrey, *Cleaning up Their Act*, ACCOUNTANT, Dec.-Jan. 1998, at 4 (discussing Canadian legislation regulating money laundering and accountants' responsibilities under that legislation).

127. *See A Roundup of Money Laundering News*, *supra* note 126, at 8.

128. *See id.*

129. *See id.*

130. *See id.*

The Netherlands also requires accountants to actively fight money laundering.¹³¹ In 1993, the Netherlands enacted the Disclosure of Unusual Transactions (Financial Services) Act (“Disclosure Act”).¹³² This act requires anyone who provides professional services in the Netherlands to report “unusual transactions” that might constitute money laundering to the appropriate governmental authority.¹³³ The Disclosure Act defines “unusual transactions” in a manner similar to the way “suspicious activities” are defined in the United States.¹³⁴

Many other European countries are on their way to casting a wider net to capture money laundering offenders.¹³⁵ In 1991, the European Community issued the European Directive on Money Laundering (“Directive”) with the purpose of coordinating their efforts in fighting money laundering.¹³⁶ Among other things, this Directive outlined penalties that member countries were to impose on anyone involved in money laundering.¹³⁷ The Directive also required that a regulatory shield from liability be provided to anyone who reports suspected money laundering activities to the government.¹³⁸ On July 13, 1998, the European Union Commission changed its Directive 91/308/EEC to require auditors to report “suspicious activities.”¹³⁹ This change has already affected American accounting firms performing audits on U.S. subsidiaries of companies incorporated within the European Union.¹⁴⁰ The United States accounting firms are required to follow Directive 91/308/EEC and report suspicious activities to the foreign governments.¹⁴¹ Thus, U.S. accounting firms are already assisting foreign governments, and unfortunately, not the United States government, in fighting money laundering.

Money laundering is a global problem that requires global solutions. In order to succeed in its fight against money laundering, the United States should coordinate its anti-money laundering efforts with

131. Konstantinos D. Magliveras, *The Implementation of the 1991 EC Directive on Money Laundering in Germany, Italy and the Netherlands*, 8 INT'L L. PRACTICUM 89, 95 (1995).

132. *Id.* at 96.

133. *Id.* at 97.

134. *See id.*

135. Richard T. Preiss, *Privacy of Financial Information and Civil Rights Issues: The Implications for Investigating and Prosecuting International Economic Crime*, 14 DICK. J. INT'L L. 525, 547 (1995).

136. *Id.*

137. *Id.*

138. *Id.*

139. PROPOSED ADDENDUM TO AICPA, *supra* note 4, at 6.

140. *Id.*

141. *See id.*

those of the rest of the world. It should also capitalize on the combined experiences of foreign countries in addressing money laundering issues.

III

PROPOSED ANTI-MONEY LAUNDERING LAWS

The United States should establish affirmative statutory anti-money laundering obligations on accountants in order to deal more effectively with the money laundering problem. These obligations need not be significantly different from those currently placed on financial institutions.¹⁴² First, independent public accounting firms should be required to institute an anti-money laundering infrastructure designed to facilitate an effective handling of clients' money laundering issues. For example, each accounting firm should be required to have a designated anti-money laundering compliance officer.¹⁴³ Depending on the structure of individual accounting firms, the designated compliance officer may be able to delegate certain day-to-day anti-money laundering responsibilities to individual partners responsible for specific clients. One of these responsibilities would be ensuring that the specific client's SARs are properly filed with the government. Regardless of whether the anti-money laundering officer delegates certain responsibilities to individual partners, she should still be held responsible for the monitoring of each partner's overall compliance. This will ensure consistent and proper handling of all clients' money laundering matters and provide an important quality control.

The anti-money laundering infrastructure should also consist of anti-money laundering policies and procedures that provide guidance to accountants on how to fulfill their individual anti-money laundering responsibilities. For example, these policies and procedures should require lower level employees to report their findings to either managers or partners of the firm. Managers and partners, in turn, should be required to report these findings to the designated money laundering officer. When an employee is not satisfied with his or her management's handling of a money laundering matter, that individual should be obligated to report his or her views to the top management of the firm. This reporting mechanism, although not foolproof, is likely to

142. *Supra* notes 29-56 and accompanying text.

143. This requirement parallels requirements currently set on banks. *See* 31 U.S.C. § 5318(h) (1995). In their European offices, firms such as PricewaterhouseCoopers have already taken affirmative anti-money laundering steps. *See Irish Law to Ferret Out Criminal Proceeds*, *supra* note 85, at 3.

reduce the risk of a partner's personal interests interfering with her reporting responsibilities.

In addition, as part of an effective anti-money laundering infrastructure, public accounting firms should be required to provide adequate training to their employees, as well as periodic examinations. These efforts will facilitate employee familiarity with the latest money laundering trends and requirements. During training sessions, for example, a compliance officer can demonstrate the importance of a thorough review of bank reconciliations as well as procedures designed to identify structured transactions.¹⁴⁴ Periodic examinations of employees' proficiency with anti-money laundering techniques will reveal the effectiveness of these training sessions and hence the level of employees' preparedness to combat money laundering.

Second, accountants should be required to institute formal KYC requirements. The establishment of sound KYC practices is essential to an effective war against money laundering.¹⁴⁵ Public accountants already have a favorable infrastructure in place to fulfill KYC rules currently imposed on financial institutions.¹⁴⁶ However, this infrastructure will need to be further developed to address the unique intricacies of money laundering.

To illustrate, accountants should be required to obtain from their clients the kind of information that would better position them to detect potential money laundering activities. For example, on a scope basis,¹⁴⁷ accountants should be required to gain a detailed understanding of the following: (1) the purposes behind their clients' various bank accounts; (2) the reasons for executing certain wire transfers; and (3) a background of their clients' customers. Accountants should be required to obtain this information even if not already required to do so for the purpose of issuing an opinion on financial statements.¹⁴⁸

Third, to the extent reasonable, accountants should be required to design their audits to detect all money laundering activities that have a material effect on financial statements. When designing their auditing

144. See 31 U.S.C. § 5324(a) (1994); see also text accompanying note 93.

145. See Hewson Testimony, *supra* note 1, at 121.

146. *Supra* notes 57-92 and accompanying text.

147. See O'REILLY ET AL., *supra* note 10, at 635 (describing "scope paragraph," which "notes that evidence about the accounting measurements and disclosures in the financial statements was obtained only on a test basis. To do otherwise would be economically prohibitive"). For a complete discussion of this process of "audit sampling" see generally AM. INST. OF CERTIFIED PUBLIC ACCOUNTANTS, *AUDIT SAMPLING* (1983); ALVIN A. ARENS & JAMES K. LOEBBECKE, *APPLICATIONS OF STATISTICAL SAMPLING TO AUDITING* (1981); HERBERT ARKIN, *SAMPLING METHODS FOR THE AUDITOR: AN ADVANCED TREATMENT* (1982).

148. See Hewson Testimony, *supra* note 1, at 121.

procedures, accountants should not be allowed to concentrate solely on illegal acts that have material *and* direct effects on financial statements, thus ignoring the risk of their clients' involvement in money laundering. For example, it would be unreasonable to require accountants to discover money laundering activities when their clients intentionally act as depositories for money launderers,¹⁴⁹ because, generally, accountants do not have access to the information that would reveal this involvement. However, it would be reasonable to require accountants to discover their clients' structuring of deposits designed to avoid CTR requirements, because accountants have access to bank reconciliations and deposit histories which reveal this type of activity.

Fourth, accountants should be required to file an SAR with the government every time they suspect that their client is involved in money laundering. When filing an SAR and making other related decisions, auditors should be encouraged to consult with their legal counsel as well as with appropriate governmental authorities. This would reduce the likelihood that accountants will misinterpret either certain evidence or an anti-money laundering regulation. In order to prevent cover-ups of money laundering, and hence make the government's follow-up investigation more effective, accountants should be required to take precautions not to "tip off" parties that are involved in the money laundering. Unless accountants believe that management itself is involved in the money laundering, accountants should be permitted to discuss their findings with the client's management.

Finally, accountants should be required to communicate the effectiveness of their clients' internal controls designed to prevent and detect money laundering activities to the regulators. This communication could be incorporated in the Internal Control Letter currently filed by accountants with regulators.¹⁵⁰ For example, accountants should be required to review, evaluate, and comment on the adequacy of an organization's anti-money laundering policies and procedures, training, and supervision. The clients' desire not to be "written up" for their failure to set up necessary anti-money laundering controls will likely force the enterprise to take a proactive role in setting up the proper infrastructure.

149. Any intentional involvement in money laundering activities is criminalized. If the amount laundered exceeds \$100,000 within any twelve month period, the penalty is enhanced. 31 U.S.C. § 5324(c)(2).

150. See generally AM. INST. OF CERTIFIED PUBLIC ACCOUNTANTS, STATEMENT ON AUDITING STANDARDS NO. 78, CONSIDERATION OF INTERNAL CONTROL IN A FINANCIAL STATEMENT AUDIT: AN AMENDMENT TO SAS No. 55. (1995) (outlining "Internal Control" components).

By setting up an internal anti-money laundering infrastructure, utilizing the knowledge of their clients' businesses, actively looking for and reporting money laundering activities, and monitoring their clients' anti-money laundering efforts, accountants will create an unprecedented shield that will protect institutions from becoming infested with money laundering. These relatively simple requirements will contribute tremendously to the government's fight against such a dangerous crime. The accounting profession, unlike any other, has the knowledge, experience, and ability to stop the unprecedented spread of money laundering.

IV

POTENTIAL ISSUES WITH THE PROPOSITION AND SUGGESTED SOLUTIONS

A. *Issues of Confidentiality, Ethics, and Trust*

Historically, disclosure of confidential information to third parties has been criticized as a violation of an accountant's ethical obligation to her client.¹⁵¹ This criticism is based upon the notion that because clients provide accountants with unfettered access to their records and operations, accountants owe a duty of confidentiality to their clients.¹⁵² The unrestricted access to client data is essential to an accountant's ability to verify the accuracy of the information a client submits to the public.¹⁵³ Because an accountant can verify the accuracy of clients' statements to the public, investors and lenders are able to rely on these statements when making their business decisions.¹⁵⁴ This chain of events is essential to the efficient operation of the securities markets.¹⁵⁵ The argument against a duty to "blow the whistle"¹⁵⁶ on a client holds that a client would cease to trust her accountant, thus destroying the efficiency of capital markets.¹⁵⁷

In *United States v. Arthur Young & Co.*, the Supreme Court heard the issue of whether an accountant who reports her client's ac-

151. See *United States v. Arthur Young & Co.*, 465 U.S. 805, 818 (1984) (citations omitted).

152. See *id.* at 818-19.

153. See *id.* at 818.

154. See *id.*

155. See *id.*

156. Marion P. Rosner & Andrew E. Lenlyk, *Whistle Blowing: An Accountant's Duty to Disclose a Client's Illegal Acts*, 506 PLI/Lit 211, 215 (1994).

157. *Latigo Ventures v. Laventhol & Horwath*, 876 F.2d 1322, 1327 (7th Cir. 1989) (holding that "relations of trust and confidence between accountant and client would be destroyed if the accountant were duty-bound to make continuous public disclosure of all of the client's financial adversities.").

tivity to authorities would violate ethical obligations and client trust.¹⁵⁸ The Court held that “no confidential accountant-client privilege exists” in the relationship between accountants and their clients.¹⁵⁹ Unlike an attorney-client relationship, an accountant’s public role and responsibility “transcend[s] any employment relationship with the client.”¹⁶⁰ The Court concluded that accountants owe an overriding duty of loyalty to the investing public—not their clients.¹⁶¹ Allowing accountants to withhold material information from the public would undermine the justification for the very existence of the public accounting profession.¹⁶² It is because of this overriding duty to protect the public that the public accounting profession was created.¹⁶³ Thus, the very concept of ethics and trust between auditors and their clients must contain an understanding of accountants’ superseding duty to the public.¹⁶⁴

Moreover, under present laws, accountants’ ethical obligations to their clients successfully coexist with accountants’ obligations to identify and report clients’ illegal activities.¹⁶⁵ Congress recognized and highlighted the presence of accountants’ superseding obligations to third parties in the overall accountant-client relationship when it enacted a reporting provision in the Tort Reform Act that requires accountants to report their clients’ illegal activities.¹⁶⁶ This “whistle blowing” provision, contrary to the expectations of some commentators,¹⁶⁷ has not jeopardized the healthy functioning of capital markets.¹⁶⁸ The mere inclusion of money laundering in the list of illegal acts that accountants are already required to report will not bring a

158. *United States v. Arthur Young & Co.*, 465 U.S. 805, 818 (1984) (citations omitted).

159. *Id.* at 817 (quoting *Couch v. United States*, 409 U.S. 322, 325 (1973)).

160. *Id.*

161. *See id.*; *see also* CARMICHAEL & WILLINGHAM, *supra* note 57, at 16, 41-45.

162. *See Arthur Young & Co.*, 465 U.S. at 818.

163. *See id.*; *see also* CARMICHAEL & WILLINGHAM, *supra* note 57, at 2-3.

164. *See Arthur Young & Co.*, 465 U.S. at 821.

165. Private Securities Litigation Reform Act of 1995, § 301, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended at 15 U.S.C. § 78a); *see also* ILLEGAL ACTS BY CLIENTS, *supra* note 109, at 5 (describing AICPA process of evaluating and reporting illegal acts by clients).

166. Private Securities Litigation Reform Act of 1995, § 301, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended at 15 U.S.C. § 78a); *see also* ILLEGAL ACTS BY CLIENTS, *supra* note 109, at 5 (describing AICPA process of evaluating and reporting illegal acts by clients).

167. Andrew W. Reiss, *Powered by More than GAAS: Section 10A of the Private Securities Litigation Reform Act Takes the Accounting Profession for a New Ride*, 25 HOFSTRA L. REV. 1261, 1306 (1997).

168. *See United States v. Arthur Young & Co.*, 465 U.S. 805, 818 (1984) (citations omitted).

change to this time-tested ethical paradigm between accountants and their clients.

B. *Administrative Concerns*

Will accountants be effective in administering their anti-money laundering responsibilities? Will there be many false alarms? Will accountants identify all detectable money laundering activities? Appropriate guidance is the answer to all these questions.

It will be extremely important to provide clear guidance to accountants on how they should “comply” with their new anti-money laundering responsibilities. This guidance should contain illustrations of traditional money laundering techniques and samples of anti-money laundering procedures to be utilized during audits. Accountants should be advised to consider a client’s transactions as suspicious if they do not fit the profile of the client’s legitimate business operations. For example, unsupported travel expenses to known drug-trafficking countries can serve as an illustration of the transactions that do not fit the client’s legitimate business operations.

The proposed rules will only be effective if there is adequate guidance to accompany them. The new anti-money laundering rules and the accompanying guidance should be developed in coordination with representatives of the accounting profession, namely the AICPA. The accounting profession could make an invaluable contribution to the lawmaking process by incorporating into this process their technical expertise.

C. *Legal Issues*

The proposed changes to accountants’ responsibilities with regard to clients’ money laundering create additional legal exposure for accountants. Accountants are already overwhelmed with litigation due to the nature of their services.¹⁶⁹ The risk of clients and third parties suing accountants for slander, false incrimination, and other causes of action will increase dramatically.

169. Ronald A. Dye, *Auditing Standards, Legal Liability, and Auditor Wealth*, 101 J. POL. ECON. 887 (1993).

The most profound change [in the audit market] is the increase in the amount of litigation auditors have been subject to . . . “[M]ore suits have been filed against accountants in the past 15 years than in the entire history of the profession.” In 1992 there were estimated to be \$30 billion in lawsuits against auditors.

Id. See CARMICHAEL & WILLINGHAM, *supra* note 57, at 54-64; see also Allard v. Arthur Andersen & Co., 957 F. Supp. 409 (S.D.N.Y. 1997).

Accountants need to be provided with a solid shield against potential litigation that might arise as a result of fulfilling their new anti-money laundering responsibilities. This shield should ensure that if accountants properly carry out their anti-money laundering responsibilities they will not be held liable for the consequences of blowing or not blowing the whistle on their clients. Only with adequate protection will accountants be effective in fighting money laundering.

This issue has been partially addressed. On September 11, 1998, the House of Representatives passed the Money Laundering Deterrence Act of 1998 (“Deterrence Act”).¹⁷⁰ This act would establish a “safe harbor” for auditors who report clients’ suspicious activities to the appropriate governmental authorities.¹⁷¹ The protections provided in the Deterrence Act need to be expanded, however, to include accountants who file formal SARs and take any other actions in good faith and in accordance with the law.

It will be extremely important for auditors to understand what protections the safe harbor will and will not offer. An examination of financial institutions’ prior experiences with the “good faith suspicion” requirement of the applicable safe harbor provision illustrates this point. For example, in *Lopez v. First Union National Bank*,¹⁷² the First Union Bank disclosed information to governmental agencies concerning customer account activities upon verbal instructions from federal law enforcement officials.¹⁷³ A customer prevailed in a suit against the bank for the disclosure of this confidential information.¹⁷⁴ The Eleventh Circuit Court of Appeals held that the requirement of good faith suspicion was not met because, at the time the representative was reporting the customer’s confidential information, he did not have sufficient reason to believe that the customer was involved in money laundering.¹⁷⁵ Even though the bank argued that the govern-

170. Money Laundering Deterrence Act of 1998, H.R. 4005, 105th Cong. (1998).

171. The bill states that:

[A]ny independent public accountant who audits any such financial institution and makes a disclosure described in clause (i), shall not be liable to any person under any law or regulation of the United States, any constitution, law, or regulation of any State or political subdivision thereof, or under any contract or other legally enforceable agreement (including any arbitration agreement), for such disclosure or for any failure to notify the person who is the subject of such disclosure or any other person identified in the disclosure.

Id.

172. 129 F.3d 1186 (11th Cir. 1997).

173. *Id.* at 1188.

174. *Id.* at 1194.

175. *Id.* at 1193.

ment's request on its own warranted a "good faith basis to suspect a possible violation of law or regulation" and, consequently, warranted disclosure, the court held that Congress did not intend the safe harbor to protect disclosures made in response to the "government official's unexplained request or unvarnished instructions for financial records."¹⁷⁶

The *Lopez* case is significant in a number of ways. First, it illustrates the importance of having internal policies and procedures that specifically address situations where the government requests client information. Specifically, client information should only be released upon receipt from the government of a written request for information along with reasons for this request.

More importantly, however, the *Lopez* case provides a valuable lesson to the reporting community—"the more" client information they furnish to the government is not necessarily "the better." Companies should be very conscious of their clients' confidentiality concerns. This means that even in cases where they deem the release of client information to be appropriate, companies should always make sure that only the appropriate, relevant, and necessary information is disclosed. Although it is not always easy to determine what portion of clients' information is appropriate, relevant, and necessary for disclosure, raising this issue and continuously keeping this issue in mind can sometimes by itself lead to proper decisions.

D. How Likely Are Auditors to Report Their Clients' Money Laundering Activities to the Government?

One might argue that auditors are not very likely to report their clients' involvement in money laundering to the government because they fear that their relationships with their clients will be damaged. Because accountants use their audit services to get in their clients' doors and later sell other more profitable services,¹⁷⁷ such as general consulting and merger advisory work, there is often an incentive to "go easy on auditing clients."¹⁷⁸ These other services currently generate over fifty percent of accountants' total revenues.¹⁷⁹ Consequently, if accountants report their clients' money laundering activities, they run the risk of losing the client.

176. *Id.*

177. *Id.*

178. Richard Melcher, *Where Are the Accountants?*, BUS. WK., Oct. 5, 1998, at 144, 146 (discussing profitability of consulting services offered by accountants).

179. *Id.*

This issue can be addressed by enacting laws that would alter the “cost-benefit” analysis of reporting versus not reporting clients’ money laundering activities. As long as the costs of not reporting clients’ money laundering activities outweigh the costs of losing revenues from those clients, accountants will likely comply with the duties placed on them. In order to ensure that this “cost-benefit” analysis will produce the desired result, an overt failure to report a client’s money laundering activities should be treated as a criminal act of aiding and abetting and thus be subject to criminal prosecution and penalties.

During the past few years, the public accounting profession has received a great deal of criticism for not performing up to the expectations placed on it by the public.¹⁸⁰ The imposition of these new responsibilities should strengthen the public perception of the effectiveness and importance of the profession.¹⁸¹ For example, the SEC recently stated that it “expects more” from accountants in light of the latest “bookkeeping disasters” surrounding the mishandling of many important financial issues.¹⁸² Accountants have become subjects of this criticism because they “seem to have allowed more and more of their clients to undercut the trustworthiness of their reported numbers with aggressive, albeit often legal, accounting”¹⁸³ By accepting and effectively carrying out their new anti-money laundering responsibilities, accountants will be able to demonstrate the true importance of their profession.

Whether or not these laws are enacted, it is still in an accountant’s best interest both to ensure that clients are not involved in money laundering and to report clients’ suspicious activities. The damage that accountants will suffer to their reputation as a result of being associated with clients who launder money is many times greater than the cost of losing a particular client’s business. A good reputation is an accountant’s most valuable asset. Without it, no one will rely on the assurance the accountant provides and, consequently, no one will hire her.

E. Who Will Pay for It All?

The additional costs associated with carrying out the proposed requirements will be incorporated by accountants in the overall cost

180. *See id.*

181. *See United States v. Arthur Young & Co.*, 465 U.S. 805, 818 (1984) (citations omitted).

182. Melcher, *supra* note 178, at 146.

183. *Id.* at 144.

structure of audits. Just like all other audit-related costs, the new costs will be passed on in full, or in part, to the clients. Accountants will have to absorb, as they do now, any unbilled or uncollected expenditures. The benefits to both the auditor and the client, however, will outweigh the additional costs.

Accountants will assist management to protect companies from costly money laundering scandals.¹⁸⁴ Generally, scandals arise when a single employee, or a small group of employees, commit money laundering acts without top management's involvement.¹⁸⁵ Subsequent to the government discovery of employee money laundering activities, the company's reputation is severely damaged. This damage translates into lost revenues because fewer people want to transact business with a company that has money laundering problems. The new procedures would enable accountants to detect and report money laundering in its infancy, before the damage ensues.

Accountants will also benefit from the imposition of affirmative anti-money laundering responsibilities. Their increased role in the government's anti-money laundering efforts will put accountants in a better position to offer other related anti-money laundering consulting services. These consulting services have a high profit margin.¹⁸⁶ Revenues generated from these services will compensate for the possible lost billings from annual audits.¹⁸⁷ For example, accountants will be in a better position to help their clients set up necessary anti-money laundering internal control infrastructure, write effective anti-money laundering policies and procedures, and help with employee training.

184. See Allen, *Fridge Connection*, *supra* note 15, at A1 (outlining General Electric's use of auditors to stop further money laundering abuses); Beckett, *supra* note 81, at A4 (noting Bank of New York's increased vigilance to detect money laundering in wake of scandal); Day, *supra* note 75, at E1 (discussing increased attention to internal audits following Citibank's failure to recognize money laundering in accounts); Lohr, *supra* note 76, at A1 (discussing BCCI's use of auditors); McKinley Jr., *supra* note 75, at B7 (auditing race track betting windows); Preston, *supra* note 15, at A6 (describing use of audits to discover money laundering); Solomon, *supra* note 15, at A45 (noting role of PricewaterhouseCoopers in investigating money laundering).

185. See, e.g., Allen, *Fridge Connection*, *supra* note 15, at A1 (noting appliance distributors use foreign trade to launder money); Lohr, *supra* note 76, at A1 (describing corruption at lower levels of company); McKinley Jr., *supra* note 75, at B7 (describing allegations that betting clerks laundered money); Preston, *supra* note 15, at A6 (discussing Mexican banks' money laundering scandals brought about by small group of banks' employees).

186. See Melcher, *supra* note 178, at 146.

187. See *id.*

CONCLUSION

The United States Congress should take immediate action against money laundering. The implementation of the proposed changes to accountants' anti-money laundering responsibilities is a necessary step towards achieving the ultimate goal of stopping money laundering and related crimes. Only timely legislation can effectively combat the war against money laundering:

[T]he fight against money launder[ing] is a fight against all crime [It] is not a battle to protect the fabric of our economy and society, but a full scale war. As in all wars, different methods are used to destroy, deter or undermine the enemy All require one fundamental ingredient—the support of the legislature and its government.¹⁸⁸

Money laundering has reached very dangerous proportions and poses a real and immediate threat to the United States and to the rest of the world. It “challenges the legitimate authority of national governments, corrupts government institutions, endangers the financial and economic stability of nations, and routinely violates legal norms [and] property rights.”¹⁸⁹ The public accounting profession is perfectly positioned to make significant contributions to the war against money laundering. Given the accounting profession's experience in monitoring and reporting client compliance with various rules and regulations, and its access to client business records and activities, the U.S. should follow the lead of many foreign governments and utilize accountants in the fight against money laundering.

188. Hewson Testimony, *supra* note 1, at 126.

189. Money Laundering Deterrence Act of 1998, H.R. 4005, 105th Cong. (1998).

