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Supreme Court Clarifies Federal Bank Fraud Statute in *Loughrin v. United States*
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On June 30, 2014, the U.S. Supreme Court issued its final opinions and concluded its 2013-2014 term. Among the Court's recently decided cases is *Loughrin v. United States*, where the Court clarified that Section 1344(2) of the federal bank fraud statute does not require intent to defraud.[i] The Court's decision impacts federal bank fraud prosecutions, but may also impact bank compliance personnel and in-house counsel.

The Case

In *Loughrin v. United States*, the Supreme Court held, in a unanimous decision, that Section 1344(2) of the federal bank fraud statute does not require the Government to prove that a defendant intended to defraud a financial institution. In *Loughrin*, Petitioner was charged with six counts of bank fraud under 18 U.S.C. § 1344(2) for a check fraud scheme carried out at a Target store. Petitioner stole checks from residential mailboxes, altered them, and then used them to purchase merchandise at Target, which he immediately returned for cash.

The federal bank fraud statute, 18 U.S.C. § 1344 provides:

> Whoever knowingly executes, or attempts to execute, a scheme or artifice – (1) to defraud a financial institution; or (2) to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises, shall be fined not more than $1,000,000 or imprisoned more than 30 years, or both.

While Section 1344(1) clearly requires an intent to defraud a financial institution, the Court said that "to read [Section 1344(2)] following the word 'or,' as somehow repeating that requirement even while using different words, is to disregard what 'or' customarily means." Therefore, the Court concluded that Section 1344(2) does not require an intent to defraud. Instead, all Section 1344(2) requires is: (1) that the defendant intend to obtain any of the moneys [. . .] or other property owned by or under the custody or control of a financial institution and (2) to obtain such bank property "by means of" false or fraudulent pretenses, representations, or promises. Because checking accounts are under the custody or control of a financial institution, check fraud qualifies under the statute.

The Court further clarified that under Section 1344(2), "it is not enough that a fraudster scheme to obtain money from a bank and that he make a false statement;" the statute includes "a relational component" that "the criminal must acquire (or attempt to acquire) bank property 'by means of' the misrepresentation." According to the Court, "the 'by means of' language is satisfied when [. . .] the defendant's false statement is the mechanism naturally inducing a bank (or custodian of bank property) to part with money in its control." However, according to Justice

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Scalia, joined in his concurrence by Justice Thomas, the Court's definition of the "by means of" requirement "does not accord with common usage." According to Justice Scalia, although the "statute must be interpreted, if possible, in a manner that will not make every fraud effected by receipt of a check a federal offense," deciding the proper way to do so is a question that should be left for a future case.

Effect on Bank Fraud Jury Instructions

Currently, the model federal jury instructions on bank fraud include an instruction that the defendant acted with the intent to defraud. The model federal jury instructions for a Section 1344(2) case provide:

> In order to sustain its burden of proof for the crime of knowingly executing a scheme or plan to obtain the money, funds or other property owned by or under the control of a financial institution as charged in Count __ of the indictment, the government must prove the following three (3) essential elements beyond a reasonable doubt.
>
> One: Defendant knowingly executed a scheme to obtain the money, funds or other property owned by or under the control of ____ , a financial institution, by means of material false or fraudulent pretenses, representations or promises as detailed in Count __ of the indictment;
>
> Two: Defendant did so with the intent to defraud; and
>
> Three: ____ , the financial institution was [either] then insured by the United States [or] was chartered by the United States.

In light of the Court's decision in *Loughrin*, these model jury instructions will probably change. In fact, the Court states that by hearing the *Loughrin* case, they intended to "resolve a Circuit split on whether § 1344(2) requires the Government to show that a defendant intended to defraud a federally insured bank or other financial institution."[ii] Therefore, as a result of the Court's decision in *Loughrin*, any provision of federal jury instructions currently requiring intent to defraud a financial institution will be removed. Instead, the jury instructions will likely instruct the jury on the elements of a Section 1344(2) case, while remaining silent on intent to defraud.

Effect on Financial Institutions

By removing the intent to defraud requirement from a Section 1344(2) case, the Court's decision in *Loughrin* lessens the burden on prosecutors and, therefore, makes prosecuting bank fraud easier. Easier prosecutions could also deter bank fraud and lead to less fraud overall, though the actual extent of deterrence, if any, is unclear.

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The Court's decision—particularly, the Court's discussion of the "by means of" requirement—may also affect bank compliance personnel and in-house counsel. Currently, the Bank Secrecy Act requires bank personnel to file a suspicious activity report ("SAR") when banks identify suspicious transactions that may constitute criminal violations. The SARs are meant to report known or suspected violations of law and help the Federal Government identify individuals, groups, or organizations involved in fraud or other financial crimes. If bank personnel uncover a transaction where an individual is attempting to defraud the bank, Section 1344(1) is clearly implicated and a SAR is warranted. However, a violation under Section 1344(2) presents a more complicated scenario. Absent intent to defraud the bank (i.e., when a suspect defrauds a third party using a check drawn on a bank or a credit card issued by a bank), bank compliance personnel may have to determine whether "the defendant's false statement [was] the mechanism naturally inducing a bank (or custodian of bank property) to part with money in its control." In other words, prior to filing a suspicious activity report for a Section 1344(2) violation, bank personnel may have to determine whether there is a sufficient link between the bank property sought and the means of fraud utilized so that there is a "real connection to a federally insured bank."

For example, compare the following scenarios proposed by the Court in *Loughrin*. First, consider a defendant that makes a misrepresentation to the bank itself (i.e., cashing a forged check at a bank teller window). If the bank teller cashes the check, the defendant's false statement (the forged check) is the means by which he induced the bank to part with money in its control. In such a scenario, it is clear that Section 1344(2) has been violated and bank personnel should file a SAR for this transaction. The same is true if the defendant issues a forged check to a third party such as Target. It is practically inevitable that the forged check will make its way to the bank and be the means by which the bank is induced to part with money in its control. Bank personnel should file a SAR for this transaction as well.

The Court's discussion of the "by means of" requirement, however, limits the reach of Section 1344(2) to cases in which there is "a real connection to a federally insured bank," in order to guard against federal penalties for fraud that is not directly committed on a bank. To explain this, the Court offers the following scenario: a fraudster sells something to a customer and misrepresents its value (i.e., the fraudster sells a cheap knock-off as a Louis Vuitton handbag). The customer then uses a valid check to purchase the handbag. In such a case, the fraudster obtained property in the bank's control (the money in the customer's checking account) and made false representations (misrepresenting the value of the handbag). However, according to the Court, such a scenario does not present a Section 1344(2) violation because the "by means of" requirement is not met (i.e., the means by which the bank parted with its property was a valid check and the fraudster's misrepresentation about the value of the handbag never reached the bank). Therefore, in such a scenario, a SAR would not be warranted because Section 1344(2) has not been violated.

The examples above are meant to illustrate that following the *Loughrin* decision bank personnel may have to be more selective in screening which suspicious activity merits a SAR. However,

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the effects of the *Loughrin* decision on bank behavior are likely to be marginal. Although banks may, in light of the Court's decision, screen suspicious activity for the relational component the Court read into the "by means of" language of Section 1344(2), such screening is not likely to be crucial. Until further regulations, banks could continue to use the same reporting standards, leaving the federal government to sort through SARs when deciding which fraudulent activity should be prosecuted under Section 1344(2).

For a summary of some of the Supreme Court's biggest opinions of the term, *see* "A Look at Some of the U.S. Supreme Court's Biggest Decisions of the Term" (PDF).

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[i] The case is *Loughrin v. United States*, No. 13-316, slip op. (U.S. June 23, 2014). The full opinion is available here.
[ii] Compare United States v. Everett, 270 F.3d 986, 991 (6th Cir. 2001) (stating that § 1344(2) does not require intent to defraud a bank), with United States v. Thomas, 315 F.3d 190, 197 (3d Cir. 2002) (requiring intent to defraud a bank), and United States v. Kenrick, 221 F.3d 19, 29 (1st Cir. 2000) (requiring intent to defraud a bank), and United States v. Jacobs, 117 F.3d 82, 92-93 (2d Cir. 1997) (requiring intent to defraud a bank).