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STATE BUSINESS INCORPORATION—2009

HEARINGS

BEFORE THE

COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS UNITED STATES SENATE

OF THE

ONE HUNDRED ELEVENTH CONGRESS

FIRST SESSION

JUNE 18, 2009
EXAMINING STATE BUSINESS INCORPORATION PRACTICES: A DISCUSSION OF THE INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT

NOVEMBER 5, 2009
BUSINESS FORMATION AND FINANCIAL CRIME: FINDING A LEGISLATIVE SOLUTION

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STATE BUSINESS INCORPORATION—2009

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EXAMINING STATE BUSINESS INCORPORATION PRACTICES: A DISCUSSION OF THE INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT

THURSDAY, JUNE 18, 2009

U.S. SENATE,
COMMITTEE ON HOMELAND SECURITY
AND GOVERNMENTAL AFFAIRS,
Washington, DC.

The Committee met, pursuant to notice, at 2:31 p.m., in room SD–342, Dirksen Senate Office Building, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.

Present: Senators Lieberman, Levin, and Carper.

OPENING STATEMENT OF CHAIRMAN LIEBERMAN

Chairman LIEBERMAN. The hearing will come to order. Good afternoon. I was waiting a moment. Senator Levin is on his way. Senator Carper will be here a bit later. Unfortunately, Senator Collins is involved in Appropriations Committee markup deliberations, so she cannot be with us.

Welcome to our hearing on the Incorporation Transparency and Law Enforcement Assistance Act, S. 569, a bill that has been introduced by Senators Levin and McCaskill on this Committee and Senator Grassley of Iowa as well. The bill results from the persistent investigative work of the Permanent Subcommittee on Investigations (PSI) of this full Committee.

I am about to thank Senator Levin before he is here. I was once told that if someone praises you in Washington when you are not in the room, they really mean it. So I am going to do that quickly before he gets here, because I mean it. I do want to thank my very good friend and colleague Senator Levin, who chairs the Permanent Subcommittee on Investigations, for introducing this legislation after an intensive investigative review of State incorporation procedures. The PSI staff has dedicated many hours to this matter, dating back years, and has identified numerous problems that have become law enforcement problem that are caused by the use of shell companies for illicit purposes. And I appreciate very much the work of the leadership of the Permanent Subcommittee on Investigations of this Committee and its bipartisan staff.

Each year, nearly 2 million new corporations and limited liability companies are established in the 50 States and the District of Columbia. That is more than 5,000 new businesses per day, just what we want and are proud of. It is part of the American way, entrepre-

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neurship at its best, generating revenue, creating jobs, and helping people realize their dreams.

But, each year, some of the new businesses are incorporated for improper or illegal purposes—to try, for instance, to use the corporate status to defraud innocent people or to cheat tax authorities, or to hide the true nature of their transactions, or even, as we know, to launder ill-gotten funds.

No one can put a figure on the number of corporations set up for illegitimate purposes, but some analysts have estimated that billions of dollars may flow through such U.S. corporations every year.

Right now, a majority of States require some basic information from those seeking to establish a corporation. Most require the name and address of the company, the name of a registered agent who represents the company, and a list of officers or directors. This information is typically considered a matter of public record.

It has long been customary, however, for States to allow the individuals with actual ownership interest—including the investors who control the corporation or partnership—to remain anonymous to State authorities and, therefore, to the public. This has often become a problem for law enforcement officials who have cause to investigate a company that has aroused their suspicions. The trail goes cold when they search public records and find no record of the people behind the incorporation—the people who may be using the business for illicit purposes.

Senator Levin's bill—and it is, as I said at the outset, Senator Levin, Senator Grassley, and Senator McCaskill particularly—is designed with these law enforcement investigations in mind. It would set a national minimum standard intended to require States to collect and maintain information about a corporation's underlying owners to help law enforcement in its work. The bar is set higher yet for foreign owners, whose identities must be verified by the company's registered agent before the State can process the forms and set up the corporation. This bill gives States the authority to decide whether to keep the beneficial ownership information private or to make it a matter of public record.

So this is a classic transparency requiring laws which includes some new penalties for providing false or insufficient information. It is sunshine legislation in the best sense of the word. But we all know that such legislation has to be weighed against other factors as well, including the privacy rights of those making in this case personal investment decisions and, others would argue, the potential costs of administration and enforcement that would fall on State governments and companies.

Senator Levin's bill, for example, would not require States to verify the accuracy of information provided before granting a new entity its legal status.

The Uniform Law Commission (ULC), which I am pleased to say is represented here today, has drafted an alternative proposal that would leave companies in charge of maintaining the required information. Forty-four out of the 50 States already ask corporations to keep lists of all members or shareholders of record, the real owners, at their principal offices. The ULC's recommendation now seeks to strengthen that practice.

So today, in a matter that really matters, we are going to try to better identify both the problem and to discuss what the best solution to it is. We do have a panel of witnesses very experienced and informed on business incorporations and on corporate investigations. I look forward to their testimony of this full Committee, following the excellent investigation of our Permanent Subcommittee, on this legislation which aims to limit illegal operations, without damaging the smooth flow of commerce for legitimate corporate purposes.

Senator Levin, I spoke in highly laudatory terms of you in your absence. I could repeat those now, but I will just say how much I appreciate your work on this and so much else, and I call on you now for an opening statement.

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. Mr. Chairman, thank you for those comments, and thanks so much for holding this hearing to focus on the fact that we are forming about 2 million U.S. corporations and limited liability companies each year without knowing who is behind them.

My opening statement, Mr. Chairman, is a bit long, and if it gets too long, do not hesitate to let me know, and I will cut off whenever that moment comes.

Chairman LIEBERMAN. It will be a pleasure if that moment comes. [Laughter.]

Senator LEVIN. And I think we have a vote, actually, in a few minutes.

Chairman LIEBERMAN. Go right ahead.

Senator LEVIN. U.S. corporations with hidden owners have created a serious law enforcement and a national security problem. For instance, we are going to hear today from witnesses about U.S. corporations that, it turns out, were established by the military in Iran, a state sponsor of terrorism. We are going to hear about U.S. corporations involved with money laundering, about U.S. corporations that are used to commit tax evasion and more, and they all have one thing in common: Their real owners—the legal term is "beneficial owners"—are hidden from view. Here is one example of what is going on.

In 2004, one of our key law enforcement agencies, Immigration and Customs Enforcement (ICE)—who is here today—uncovered a collection of U.S. companies that were secretly controlled by entities located in Panama. The investigation began when bank reports showed that a single company, formed in Utah, was participating in nearly $150 million in suspicious international wire transfers. Further investigation by ICE uncovered a network of nearly 800 U.S. companies, dispersed among nearly all 50 States, controlled by the same Panamanian entities. These companies were transferring large amounts of money to each other and to high-risk jurisdictions overseas.

The companies claimed they were paying for the import or export of goods, but it turned out no such goods were being shipped. In effect, the money transfers were part of a massive financial shell game in which U.S. companies were being used to disguise the movement of funds and to mask suspicious activity.

When ICE obtained the incorporation records for the 800 U.S. companies, not one identified a company's true owner. After analyzing the available information, ICE found that nearly 200 companies had been formed in Utah and used the same company formation agent in a small office in a Salt Lake City suburb. That company formation agent also served as the company's registered agent within the State to accept service of process. When questioned by ICE, the Utah registered agent indicated that he had formed the companies at the request of another company formation agent located in Delaware, did not have any beneficial ownership information, and believed that all were "shell companies," with no real business operations in the United States.

The Delaware company formation agent was already well known to law enforcement. No less than eight previous investigations had led to its doors, each of which involved millions of dollars in suspected money laundering by U.S. shell companies associated with the same Panama entities. When questioned by ICE in the prior cases, the Delaware company formation agent freely admitted that he knew some of the corporations he formed or caused to be formed were intended to move money out of Russia and some former Soviet republics. He also said that he sometimes sold U.S. companies to the same overseas buyer at the rate of 40 companies per month. When asked about the actual owners of the 200 Utah companies, the company formation agent was unable to provide law enforcement with any names since that information was not required by law.

The end result was that the ICE investigation, like the eight before it, hit a dead end, unable to proceed due to the lack of beneficial ownership information. A hearing exhibit that is in our books summarizes the case.

Now, Michael Chertoff, former Secretary of the U.S. Department of Homeland Security (DHS), wrote the following: "In countless investigations where the criminal targets utilized shell corporations, the lack of law enforcement's ability to gain access to true beneficial ownership information slows, confuses, or impedes the efforts by investigators to follow criminal proceeds. This is the case in financial fraud, terrorist financing, and money-laundering investigations. It is imperative that States maintain beneficial ownership information while the company is active and to have a set time frame for preserving those records."

Here is another aspect of the problem. A few weeks ago, members of my staff conducted an Internet search and found numerous company formation agents advertising the sale of U.S. companies and trumpeting the fact that U.S. companies can be formed without disclosing the names of any company owner. One of the most blatant was Corporations Today, Inc., which advertises its ability to form U.S. corporations in nearly every State with minimal cost and effort. Copies of some of its Internet ads are presented in the two hearing exhibits,[1] and the chart which I am putting up here reproduces one of its advertisements offering the sale of aged corporations, meaning companies which Corporations Today formed

[1] The exhibits referenced by Senator Levin appear in the Appendix on page 107.

years earlier.[1] One of the companies on sale for $6,000 is advertised as coming with 4 years of tax returns and an existing employer identification number (EIN), issued by the IRS.

Why buy an aged corporation? According to Corporations Today, "Obtaining bank loans may be easier when you can show you have history." So is "obtaining corporate credit cards and leases." The quote goes on: "For example, Dell computers lease only to corporations 6 months old or more."

They are selling aged corporations for a price—corporations that have been in business, allegedly, for 6 months or more. So Dell is told, Hey, this corporation has been in business for years, so we are now eligible to lease your product.

So the ad invites fraud. It enables hidden owners to pretend that they have had a corporation operating in the United States for years when they have not. Despite mounting evidence of misconduct by U.S. shell corporations, despite Internet advertisements selling U.S. corporations with promises of unanimity, despite the years of law enforcement complaints, many of our States are reluctant to admit that there is a problem in established U.S. corporations with hidden owners. Too many of our States are eager to explain how quick and easy it is to set up corporations within their borders without acknowledging that those same quick and easy procedures enable wrongdoers to utilize U.S. corporations in a variety of ways both here and abroad.

In 2006, the leading international anti-money-laundering body in the world, the Financial Action Task Force (FATF) on Money Laundering, issued a report criticizing the United States for failing to comply with the FATF standard which requires countries to obtain beneficial ownership information for the corporations formed under their laws. FATF gave the United States 2 years, until July 2008, to make progress towards compliance with the FATF standard. Next week, FATF is scheduled to review U.S. actions on this matter. How can we possibly justify our failure to do what we have committed to do: Obtain beneficial ownership information for the corporations formed within the United States?

Our bill, the Levin-Grassley-McCaskill bill, that is the subject of today's hearing, would assist our law enforcement community instead of thwarting it and would enable the United States to meet its commitment to FATF. Our bill would require States to add a question to their incorporation forms asking for the names and addresses of the beneficial owners of a proposed corporation. States would not be required to verify the information, but penalties would apply to persons who submit false information.

Prospective corporations with foreign owners would also be required to submit a certification from an in-state company formation agency that the agent had verified the owners' identities and obtained photographs for them.

This beneficial ownership information would have to be updated annually. If law enforcement issued a subpoena or a summons to obtain the ownership information, States would supply the data contained on its forms. And I want to emphasize that point because the Chairman made an important point here about privacy. This

[1] The chart referred to by Senator Levin appears in the Appendix on page 95.

beneficial ownership information would be available only when the law enforcement folks issued a summons or a subpoena.

Funds that are already provided to States on an annual basis by the Department of Homeland Security could be used to pay for the minimal cost associated with adding a question to their incorporation forms.

Now, chart 2 summarizes how the bill would work.[1] It is a very simple step. You file a corporation with the Secretary of State. It has the beneficial ownership information. Law enforcement can request it with a subpoena or summons, and the Secretary of State can respond.

Introducing this legislation, Mr. Chairman, was not our first choice. In fact, at the request of the States, we delayed introducing a bill for a year to provide the States with an opportunity to craft their own solution. But when it became clear that the States would not step up to the plate, we then introduced the bill, last time cosponsored by Senator Coleman and at that time, Senator Obama, in the last Congress—and that legislation which was introduced last Congress is identical to the bill which we have introduced in this Congress and which is before the Committee today.

Now, today's hearing is going to discuss not only our bill but an alternative proposal developed by the National Conference of Commissioners on Uniform State Laws (NCCUSL), at the request of the National Association of Secretaries of State. But the NCCUSL proposal fails to cure the problem and would create a host of new ones.

Most significantly, the NCCUSL proposal would not require those seeking to form a U.S. corporation to provide the names of the beneficial owners to the State. In fact, the term "beneficial owner" never appears anywhere in their proposal. Instead, the proposal creates a complex and time-consuming procedure, summarized in the chart which we are putting up now,[2] which requires law enforcement to get the name of a company's so-called records contact person from the State, chase down that individual, ask that individual to ask the U.S. company under suspicion for certain ownership information. If the U.S. company responds, it is still not required to provide its beneficial owners, but what are essentially its owners of record, which could be shell companies here or overseas. In other words, to say that owners of record are going to be supplied after all that effort does not get to the people who really control the corporation because shell companies, either here or abroad, can be the owners of record.

So if a company has been involved in a crime or has been dissolved, the records contact individual will likely come back empty-handed. Instead of getting the beneficial ownership information it needs, law enforcement is going to be chasing its tail, and chasing its tail after the misconduct has occurred, and maybe after the suspect company shut down. And, to add to the futility of this convoluted process, it may not produce any useful information.

Another problem involves timing, Mr. Chairman. Instead of collecting beneficial ownership information at the time that a new corporation is being formed in the United States, as our bill does, the

[1] The chart referred to by Senator Levin appears in the Appendix on page 96.
[2] The chart referred to by Senator Levin appears in the Appendix on page 97.

NCCUSL proposal would allow hidden persons to obtain a U.S. corporation, misuse it, and only after the fact does it set up a process for requesting ownership information. Worse, the proposal would require law enforcement to direct its information request not to a State on a confidential basis, but to the suspect company itself, which would then be alerted to the investigation. Informing suspects of active U.S. law enforcement investigations is not a good way to thwart or punish crime.

There is a long list of endorsers of our legislation, including the Federal Law Enforcement Officers Association, the Fraternal Order of Police, the National Association of Assistant U.S. Attorneys, and more. It has been endorsed by groups combating financial and corporate abuses, including Tax Justice Network, Global Financial Integrity, Citizens for Tax Justice, Public Citizen, and more.[1] There are letters of support we will offer for the record, Mr. Chairman, as well as the balance of my statement. And, again, I thank the Chairman.

Chairman LIEBERMAN. Thank you, Senator Levin, for a very thoughtful statement, which shows the work that you and the staff of the PSI did.

I think it is probably best that we recess now. We will go over and vote. We will come right back. Please do not go too far because we will start quickly.

The hearing stands in recess.

[Recess.]

Chairman LIEBERMAN. Thank you very much for your patience. Senator Levin had urged me to reconvene. He has got a quick meeting of the Armed Services Committee that he is chairing.

So we will go first to Janice Ayala, Deputy Assistant Director, Office of Investigations, U.S. Immigration and Customs Enforcement, U.S. Department of Homeland Security. It takes a while to introduce you these days.

Ms. AYALA. It is a long title.

Chairman LIEBERMAN. Anyway, we appreciate very much your coming, and obviously we want to hear your reaction to this proposed piece of legislation.

TESTIMONY OF JANICE AYALA,[2] DEPUTY ASSISTANT DIRECTOR, OFFICE OF INVESTIGATIONS, U.S. IMMIGRATION AND CUSTOMS ENFORCEMENT, U.S. DEPARTMENT OF HOMELAND SECURITY

Ms. AYALA. Thank you. Chairman Lieberman, distinguished Members of the Committee, on behalf of Secretary Napolitano and Assistant Secretary John Morton, I would like to thank you for the opportunity to testify today on the efforts of ICE to protect the United States from the growing threat of international money laundering. ICE has expansive investigative authority and the largest force of investigators in DHS. We protect national security and uphold public safety by targeting transnational criminal networks and terrorist organizations that seek to exploit vulnerabilities at our borders.

[1] The letters of support submitted by Senator Levin appears in the Appendix on page 271.
[2] The prepared statement of Ms. Ayala appears in the Appendix on page 148.

ICE also investigates individuals and organizations that exploit vulnerabilities in the U.S. financial system to launder illicit proceeds. ICE's financial investigative authorities and unique capabilities enable it to identify, dismantle, and disrupt the financial criminal enterprises that threaten our Nation's economy and security. The combination of Bank Secrecy Act reporting requirements and Anti-Money-Laundering compliance efforts has, historically, forced criminal organizations to seek other means to launder their illicit funds across our borders. However, in the attempts to accomplish this mission, law enforcement is often hindered by the lack of information available as to the true ownership or control of the shell companies that criminals utilize. Further, this impediment limits our abilities to work jointly with our international law enforcement partners and our ability to take quick action where it may be required.

ICE has long recognized the misuse of corporations and limited liability companies formed under State law as a serious threat to the ongoing effort to combat international criminal activities. The lack of corporate transparency has allowed criminal entities a gateway into the financial system and further veils their illicit activity. Investigations can be significantly hampered, or stalled completely, when criminals utilize shell companies. It also impedes our ability to follow criminal proceeds.

Obtaining information on true beneficial corporation owners and limited liability companies and providing the information to law enforcement upon receipt of a summons or subpoena would assist DHS in its endeavor to protect the country.

At this time, I would like to share with you examples of ICE investigations that demonstrate how shell corporations established in the United States have been utilized to commit crimes against individuals across the world.

An investigation was initiated by the New York office against a criminal organization that defrauded investors out of millions of dollars and laundered the fraudulently obtained proceeds. The investigation revealed an enterprise of individuals offering fictitious instruments for investment programs described as "currency leasing trading programs," leading to more than $14 million in fraudulent transactions. These funds were laundered through a network of domestic and foreign bank accounts utilizing shell corporations, many of which had been established in the United States.

The perpetrators operated an Internet Web site which offered investors the opportunity to lease $1 million for a $35,000 fee. Victims were told these funds would be placed into a high-yield international trading program and that they could expect as much as 25 percent biweekly return on their investment.

A co-conspirator established shell corporations in Delaware, Nevada, California, and Massachusetts and companies in Denmark, Sweden, Luxembourg, and the Bahamas, which allowed them to create a complex web of bank and brokerage accounts. Another co-conspirator opened cash management accounts at other brokerage firms to receive the investors' $35,000 fee. Once in this account, the funds were then transferred to secondary accounts and further disbursed to various foreign and domestic accounts and liquidated through the use of checks and debit cards.

The investors never realized the profits they were promised nor received the requested refunds. But they did receive a litany of excuses for the delays and promises that the transactions would be completed.

In the end six individuals were convicted of violating money-laundering, wire fraud, and international transportation of stolen funds statutes. The defendant's use of domestic and foreign shell companies to layer the funds prevented full recovery of the fraudulently obtained funds.

In 2003, ICE established a Federal Foreign Corruption Task Force to conduct investigations into the laundering of proceeds emanating from foreign public corruption, bribery, or embezzlement. Investigations are conducted jointly with representatives of foreign governments to prevent laundered monies from entering the U.S. financial infrastructure, seize identified assets in the United States, and repatriate these funds to the victimized governments.

The following Miami case is another example of how shell companies are utilized for criminal activity. In this investigation, the violators utilized shell corporations to defraud the Government of Trinidad and Tobago out of more than $100 million. The foreign and domestic shell companies enabled them to engage in a bid-rigging scheme and then launder the fraudulently obtained proceeds. The co-conspirators bribed members of a Trinidad and Tobago bid committee for the construction of the Piarco International Airport in order to win a competitive construction bid. The U.S. targets of the investigation operated a construction company and architectural firm in South Florida, which submitted a competitive bid for work in the construction of the airport. A Trinidadian Government assessor believed the bid was too high and requested that a second bid be conducted. Based on this, the targets of the investigation utilized a shell company to submit a second, much higher bid for the work. As a result of this much higher second bid, the contract was awarded to the targets of the investigation.

Once they were paid by the Trinidadian Government, they laundered the proceeds by layering them through a series of shell companies in the Bahamas, Liechtenstein, and the United States. Only through reviews of handwritten notes kept by Bahamian bankers, ICE investigators were able to identify the true beneficiaries of the funds. Six of the eight indicted individuals were found guilty of violating money-laundering and wire fraud statutes; two are awaiting extradition. As part of the sentence, the court ordered approximately $22 million in restitution be paid, but the majority of that ordered restitution has not been realized.

The use of shell companies to engage in illicit activities, including money laundering and financial fraud, presents a number of investigative challenges for law enforcement. Greater transparency in the corporation formation process and providing reasonable access to the information will greatly assist our efforts to combat this threat.

I would like to thank the Committee members for this opportunity to testify and for your continued support of ICE, Customs and Border Protection (CBP), DHS, and our law enforcement mis-

sion, and I will be happy to answer any questions that you may have. Thank you.

Chairman LIEBERMAN. Thanks very much, Ms. Ayala. That was interesting testimony, and I appreciate the case studies.

Next we are going to hear from Jennifer Shasky, who is Senior Counsel to the Deputy Attorney General at the Department of Justice. Welcome.

TESTIMONY OF JENNIFER SHASKY CALVERY,[1] SENIOR COUNSEL TO THE DEPUTY ATTORNEY GENERAL, U.S. DEPARTMENT OF JUSTICE

Ms. SHASKY. Thank you and good afternoon, Chairman Lieberman. I am honored to appear before the Homeland Security Committee to discuss the issue of shell companies. In the time I have this afternoon, I would like to briefly discuss the Department's concerns about the abuse of shell companies and our views on measures designed to address the problem. In using the term "shell company," I am referring to those legal entities that have no significant operations and exist primarily on paper—with any U.S. presence typically consisting of a postal box or a mail drop.

Nearly 3 years ago, the Department discussed the difficulties that U.S. shell companies consistently pose to law enforcement efforts and the critical need for greater transparency in corporate formation in this country. Unfortunately, since the Committee last examined this issue, the problem has not improved.

Increasingly, professional money launderers use shell companies as necessary tools of their trade and schemes to launder money for international criminal organizations and to finance terrorism. Shell companies are intentionally selected for this purpose because they are very easily formed, they provide a level of anonymity in opening domestic and foreign bank accounts, and in the case of U.S. shells, they offer an air of legitimacy. Criminals trade on the good names of our States by sending illicit money through bank accounts fraudulently disguised as legitimate economic trade.

The use of shell companies to facilitate criminal schemes has evolved over time. Initially, in the 1970s and 1980s, criminals opened shell companies in offshore jurisdictions to conceal their ownership of assets. They would then open bank accounts in the United States and abroad in the names of these companies. As banks began to scrutinize offshore shell companies more closely, criminals realized that they could obtain some of the same benefits from U.S. shell companies, with the added benefit that U.S. companies would not receive the same level of scrutiny.

The use of domestic shell companies has continued to evolve. When Congress passed legislation enhancing customer identification requirements, U.S. banks began to require more information from domestic companies. This additional scrutiny resulted in the most recent trend where criminals, both domestic and foreign, are forming shell companies in the United States and then opening bank accounts in the names of those companies in foreign countries where U.S. shells have an aura of legitimacy.

[1] The prepared statement of Ms. Shasky Calvery appears in the Appendix on page 156.

Finally, the criminals use correspondent accounts at U.S. financial institutions to anonymously transfer money abroad to their U.S. shell company. Adding to the complexity, criminals will perpetrate their schemes using so-called shelf or aged companies that were created at some point in the past and are now a valuable commodity for resale because of their history of good standing, their good credit, and often their existing banking relationships. In such cases, the trail very often goes cold, with either the initial company formation agent or the middleman who is brokering a resale, neither of whom know, or often care, who has purchased the shelf company.

U.S. shell companies present severe criminal and national security vulnerabilities for the United States, and all indications are that the scope of the problem is quite broad. So we are particularly heartened to see that, through the leadership of members of the Permanent Subcommittee on Investigations, the discussion among all of the stakeholders has moved beyond the stage of merely recognizing the severity of the problem to developing real and effective solutions. We are convinced that such a solution is possible and can be crafted in a manner that is workable for law enforcement, State governments, and the private sector. We are confident that there is a solution that will benefit everyone but the would-be criminals and the would-be terrorists.

It bears emphasizing here that the Department also strongly believes that Federal legislation is an essential component of any such solution. Without Federal legislation, we cannot practically hope to achieve participation by all 50 States. And with anything short of full participation, the problem will merely shift and continue unabated in the non-participating States.

Of course, the Department also recognizes the importance of refraining from placing undue burdens on the States or the vast majority of legitimate businesses that are trying to establish a legal presence in one or more of our States.

It is with this delicate balance in mind that I would now like to focus my testimony on the four critical issues the Department believes must be addressed in any legislative solution.

First, it is critical for law enforcement to be able to identify the beneficial owner of a legal entity, the living, breathing person who controls the company and its assets. Toward this end, the Department strongly recommends consistently defining "beneficial ownership" across all 50 States to ensure that criminals cannot exploit definitional gaps between differing State systems.

In terms of identification, at formation, beneficial owners should be required to provide their name, their current address, and a legible photo ID to provide law enforcement with a name and a face to further their investigation when the information provided to the State was either false or misleading.

It is important to note here that the Department believes that both U.S. and foreign persons should be required to furnish such information. To require less from U.S. persons would invite fraud as foreign individuals could falsely claim to be a U.S. person or use straw actors to evade the verification.

To make collection of this beneficial ownership information meaningful, law enforcement must be able to obtain it an accurate

and timely manner—the second of our four critical needs. Specifically, law enforcement must be able to obtain through an appropriate legal process all beneficial ownership information for a legal entity in a timely fashion. This means that the information must already be maintained on-site in the state of formation and cannot be something that a corporate agent endeavors to collect from outside the State or even outside the country, only after a request is made by law enforcement.

This leads us directly to our third critical need. Any meaningful legislative solution must also address the point of transfer. When beneficial ownership information is transferred from one person to the next to the next to the next, currently criminals can easily throw investigators off the trail by purchasing shelf companies and transferring the ownership. To combat this practice, the Department strongly recommends legislation that both requires all covered legal entities to provide updated beneficial ownership information anytime there is a change, and also to certify annually that their information is up to date.

Finally, the fourth need: The Department believes it is critical to enact an enforcement regime. Federal criminal penalties in particular are an essential ingredient for law enforcement to target professional money launderers and their clients and the criminal in the extreme underworld. Specifically, the Department recommends crafting Federal criminal penalties targeting those who knowingly provide false information and those who knowingly fail to update that information.

The Department of Justice looks forward to working with this Committee to address the issues identified in this hearing, and I would be happy to answer any questions.

Chairman LIEBERMAN. Thanks very much, Ms. Shasky. I look forward to a few questions of my own that I have for you.

We are honored on the Committee to have with us as our next witness the Secretary of State of North Carolina, Elaine Marshall. Thank you for taking the time to be here, and we welcome your testimony now.

TESTIMONY OF ELAINE F. MARSHALL,[1] NORTH CAROLINA SECRETARY OF STATE, AND CO-CHAIR, COMPANY FORMATION TASK FORCE, NATIONAL ASSOCIATION OF SECRETARIES OF STATE

Ms. MARSHALL. Thank you, Chairman Lieberman, Senator Carper, and Committee Members. I want to thank you from my personal point but also on behalf of the National Association of Secretaries of State (NASS). I am wearing two hats here today: One as North Carolina's Secretary of State since 1997, and also as the Co-Chair of the NASS task force on this issue since 2007.

From the outset, let me say that I am currently opposed to enactment of S. 569 in its current form because of its questionable effectiveness and the huge burden it would place upon North Carolina. NASS has likewise voted twice against the contents of this bill.

[1] The prepared statement of Ms. Marshall with attachments appears in the Appendix on page 172.

The members of NASS and I support the goal of preventing money laundering; however, the terms of S. 569 to us do not appear to achieve that goal with the least amount of burden on legitimate business. The NASS response to this issue in 2007 committed us to a five-part course of action with great success.

First, bearer shares have been eliminated by statute.

Second, the 50-State survey of business formation laws has been completed.

Third, the ULC has risen to the challenge to draft a uniform law with the American Bar Association (ABA) assistance and will be going to full vote in about 30 days. We thank Commissioner Harry Haynsworth and the other commissioners for this undertaking.

Fourth and fifth, items relating to Trading With the Enemy Act and the Specially Designated National List remain incomplete, but not due to our part.

My experience in and out of government is that compliance with the law is much easier to achieve when people understand the problem and can see the value of the proposed remedy. The efficacy of S. 569 is in doubt, especially when contrasted with the fact that the government has easier ways to deal with the problem—the burden on legitimate business, the burden on State government, and the turmoil that will be created. Even FATF acknowledges in its 2005–06 report the lack of clarity or consensus over the beneficial owner concept is a problem. S. 569 will require tremendous additional recordkeeping and impose long-range costs on the States. We believe the ULC approach will be more effective, prudent, and easily managed.

To the extent that much of the information sought by law enforcement already resides within institutions such as the IRS or can be tracked through financial institutions, we respectfully request that Congress redirect its attention to requiring those institutions to share it instead of having State agencies collect it.

From the entity filing standpoint, S. 569 creates a number of practical problems. Will information collected be confidential or public? Some of my colleagues have advised that under their State Constitution they will have a difficult time in having the information be considered confidential. From my standpoint, I strongly desire that the information be designated confidential under our public records law, and I can explain my reasons later, if you desire.

Another issue with the bill is that the formation agent definition may be overly broad, and we estimate that 60 percent of North Carolina's 548,000 filers do not use a formation agent. What is the default activity when no formation agent is involved? Does the Secretary of State determine citizenship, legal permanent residency, or non-U.S. citizenship status? If no formation agent is used, who holds those passport photos? Is this REAL ID business class? Does this bill cover only entities going forward or apply to all existing entities? If it is the larger group, the education requirement then becomes a much more serious challenge, and to be meaningful, it would have to apply to all.

In North Carolina, there is no annual report requirement for our 94,000 nonprofits. Many nonprofits do not have shares or ownership interests at all, so absent "owners," the concept of "control" comes into play for a nonprofit. We currently come into a cross-fire

of that issue far too often with homeowners associations and more. Requiring nonprofits to begin annual reports, or the evergreen requirement of S. 569 will be met with strong resistance by North Carolina churches in particular, who feel church and state separation trumps reporting to any government.

Many of us question the accuracy of self-reported information in this context. Therefore, verification has always been a huge concern for NASS. If the intention is that we do not have to verify the information or compare it to any Federal list, clear language in that regard would be greatly appreciated.

Technology changes for North Carolina would be a minor cost for this act as creating the additional databases and forms would be under $100,000 for us. But please note that in North Carolina I have my own technology staff that can do this in-house at a reduced cost. It would have taken another $150,000 or so to reprogram and re-engineer annual report functions as much of the collected data would be partly public and partly confidential.

The educational training component of either of the two proposals will be significant. We have no ability to determine exceptions without a mailing. There may be a software matching program available to determine the Securities and Exchange Commission (SEC) governed entities as exceptions, but none has surfaced at this point.

A single mailing to our entire existing database with a folded, letter-size, single sheet, perforated edges, mailed at bulk rate is $390,000. This one mailing is more than our entire Secretary of State total mailing budget for the entire agency in a year.

We would seek $200,000 to $250,000 for education, for Web designs, public service announcements (PSAs), printing, Web announcements, and more. We estimate a minimum of a 40-percent staff increase in annual reports, for $170,000 annually, and a 50-percent staff increase in the customer service unit of $226,500 annually. Replacement of one server each year due to burnout adds $60,000 more, for an annual total cost of $450,500.

These proposals represent a cultural change, not just to Secretaries of State but to every business in America. We will be ground zero for the fallout from this cultural change, and we are gravely concerned. Viewing the financial and human asset commitment contrasted with the efficacy of the proposal, it is hard to find significant added value and meaningfulness, and none of us relish or expect success in competing with home State first responders to fund this.

Thank you for this opportunity. My deep thanks to the NASS staff and my colleague Secretaries of State.

Chairman LIEBERMAN. Well, thank you, Madam Secretary. We have a pretty lively debate going here now.

Ms. MARSHALL. We do.

Chairman LIEBERMAN. And we will keep it up.

Next, Adam Kaufmann. Originally, we had hoped, with great excitement, that Robert Morgenthau, the District Attorney—really the iconic, the great District Attorney—could be here. Unfortunately, I know he could not. We are very grateful, Mr. Kaufmann that you are representing him. I know in your own more youthful way—not to say that Mr. Morgenthau is not still youthful—you

bring a lot of experience to the table, so we thank you for being here.

TESTIMONY OF ADAM S. KAUFMANN,[1] ASSISTANT DISTRICT ATTORNEY, CHIEF OF INVESTIGATION DIVISION CENTRAL, NEW YORK COUNTY DISTRICT ATTORNEY'S OFFICE, ON BEHALF OF ROBERT S. MORGENTHAU, DISTRICT ATTORNEY FOR NEW YORK COUNTY, STATE OF NEW YORK

Mr. KAUFMANN. Thank you, Chairman Lieberman, Senator Levin, Senator Carper, and Committee staff. Thank you for the opportunity to be here. I note that I am the proverbial booby prize in my presence here, but I am delighted to be here all the same.

I should also note that Mr. Morgenthau sends his regards to the Committee, his support of the bill, and, to Senator Lieberman and Senator Levin, his personal regards to you two gentlemen as well.

For those of us in law enforcement, these issues with shell companies are not some abstract idea. This is what we do and deal with every day. We see these shell companies being used by criminal organizations, and the record is replete with examples of their use for money laundering, for their use in tax evasion, and for their use in securities fraud. You almost go so far as to say any of those crimes cannot function without the use of shell companies, either domestic or foreign. And, of course, today we are focusing on the problems presented specifically by domestic shell companies.

As I was getting ready for my testimony here today, I reached out to a number of colleagues in law enforcement—prosecutors, cops, agents, detectives—and every one of them had the same response, which was that this is a no-brainer. This is a simple, clear issue for us. These shell companies have to come to an end. They are a problem, and they have to stop. In New York, the police and detectives added, "They got to do something about this." That was the New York take on the problem.

Mr. Morgenthau again and again boils it down to a very simple concept, and the concept is transparency. For 45 years, he has been the top State or Federal prosecutor for Manhattan, and again and again, he talks about transparency and the need for daylight on these systems that allow corruption and criminality to exist. And again and again, we go out and conduct investigations that prove him right.

We see consistently that increasing transparency inures to the benefit of law enforcement and to the detriment of the criminals who use these systems to further their criminal activity. The written record that we submitted contains numerous examples of this. A colleague from Immigration and Customs Enforcement gave some great examples of the use of shell companies in securities fraud. And we just constantly see it.

Where we have seen some changes recently is the use of domestic shell companies relating to terror finance, and I noted in my prepared statement some of the Federal cases. I looked at the Hezbollah, the cigarette smuggling cases where there were domestic shell companies used to channel funds, set up bank accounts,

[1] The prepared statement of Mr. Morgenthau delivered by Mr. Kaufmann appears in the Appendix on page 192.

and get the monies to entities and accounts controlled by Hezbollah.

A case that we recently conducted at the Manhattan District Attorney's office focused on the abilities and influence of Iran in moving money around the world. And one of those cases we completed with the assistance and cooperation of the Department of Justice was the Lloyds Bank matter. But when we were doing those investigations, we found domestic shell companies that had been set up by entities controlled by the Government of Iran for the simple purpose of owning U.S. assets in violation of U.S. sanctions and the International Emergency Economic Powers Act (IEEPA) laws, and we saw them setting up bank accounts and moving money offshore.

These are ongoing matters, but I will tell you that specifically we looked at one New York corporation that was created and owned assets in New York, and we saw funds going from the New York corporation to what we would call an offshore bank secrecy jurisdiction. And we reached out to that bank secrecy jurisdiction to get information. The irony was that we were able to get more information from the bank secrecy jurisdiction located out of the country than we were from the State of New York. And I think that says a lot about where we are as a country in terms of our ability to conduct our affairs.

That problem is one that we should not ignore. We do many investigations with foreign law enforcement, and there is a certain moral authority that I submit to the Committee that the United States should bring to these issues, and it is a moral authority that is now lacking. It is disturbing that the United States should be found noncompliant by the FATF. As disturbing as that may be, 3 years without rectifying that becomes something of an embarrassment for our country.

It is very hard for us to point a finger at Switzerland or Liechtenstein for their bank secrecy policies when they can point back to us—and they do point back to us—and say, "But you have bank secrecy corporations in all of your 50 States. Why are you lecturing to us?"

And not to be glib about it, but I will say that I think that from a national pride perspective, our statement of our standard of transparency should be something more than, "financial transparency in the United States: better than Panama and trying to catch up with Liechtenstein." It is a sad comment on where we are.

Foreign criminals view a U.S. corporate entity as a passport to respectability and legitimacy. In our written record, there is a communication that we received from a Brazilian case where a Brazilian criminal discussed with a U.S. incorporating agent the benefits of getting a U.S. corporation. And they talked about the fact that it did not have to be public, that the owners do not have to be the registered individuals. And once the foreign criminal is able to obtain this U.S. corporate entity, it is an open door to opening bank accounts in the United States, abroad, and becomes the conduit by which they can continue to engage in their criminal conduct. It is a great source of revenue to the agents that are involved in these packages of incorporation, much like the Wyoming example that Senator Levin put up.

I am just going to comment briefly on some of the proposed legislation. I am just about out of time, but I will note that I can say—I say without hesitation or reservation—that from a law enforcement perspective, the bill proposed by NCCUSL would be worse than no bill at all. And there are two very basic reasons for this.

It eliminates the ability of law enforcement to get corporate information without alerting the target of the investigation that the investigation is ongoing. That is the primary reason.

It also sets up a system that is time-consuming and complicated, and, of course, if the Committee wants to hear more, I am happy to go into that or any of the other matters.

I thank you very much for this opportunity.

Chairman LIEBERMAN. Thank you, Mr. Kaufmann. Excellent statement.

Mr. Haynsworth, Chair of the Drafting Committee on the Uniform Law Enforcement Access to Entity Information Act of the Uniform Law Commission. Thanks for being here. Obviously, Mr. Kaufmann at the end posed a tough challenge to you, so we call on you now to respond.

TESTIMONY OF HARRY J. HAYNSWORTH,[1] CHAIR, DRAFTING COMMITTEE ON THE UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT, UNIFORM LAW COMMISSION

Mr. HAYNSWORTH. Thank you, Chairman Lieberman, Senator Levin, and Senator Carper, and thank you for inviting us to be here. I am speaking on behalf of the Uniform Law Commission and the Uniform Act that we have developed over a 2-year period.

This Act is one that has involved law enforcement officials, filing officers, Secretaries of State, practicing lawyers, every conceivable constituency that would have an interest in an Act like this has been involved in this drafting process. And we have had four 2-days drafting sessions and four conference calls that have lasted multiple hours in trying to put something together that we feel is something that can be adopted across the country in a very rapid format, assuming we can get agreement on the fact that this is what we need to do.

Whatever is done, it will have to end up being State legislation. Everything to do with what gets filed in a Secretary of State's office, the content of that access to records, and what records have to be kept by companies is something that is a matter of State law, always has been. So it is going to have to be State law to begin with, and the Uniform Law Commission, that is what we do. We draft statutes that are adopted across the country in a uniform fashion so that you have a uniform standard that applies everywhere. And for this to have any impact, whatever the ultimate outcome, it must be a uniform standard across the country.

The Uniform Law Commission has produced numerous acts that have been adopted in this fashion. I will just mention one: The Uniform Commercial Code, which is one everybody, I think, would be familiar with. And so this would be another example of doing that.

[1] The prepared statement of Mr. Haynsworth with attachments appears in the Appendix on page 200.

The objectives that we sought were: First and foremost, recognizing this is a very important and difficult issue, that law enforcement officials do need to have more effective and more current accurate information about ownership and control of companies.

Second, that you have to have some kind of a system that is workable and does not create more problems than it solves in terms of having unmanageable burdens on the Secretary of State's office, which is what Secretary Marshall was referring to in her concerns about S. 569, and does not cause undue burdens on companies in terms of their operations and recordkeeping they have to keep up with.

That is a really major concern about trying to balance those concerns, plus the privacy concerns that have been mentioned; and also the concerns about foreign investors in the United States and not creating barriers that would unduly restrict their ability to be able to form and operate businesses. And you have to put this in the context that well over 99.5 percent, at least, maybe 99.9 percent of all businesses are legitimate. And so when you put a burden on everybody, you have to be careful that you are not putting an undue burden that creates barriers to formation and operation of legitimate companies. That means 99.9 percent of them.

We think we have accomplished these objectives in a way that our Act will provide more information, will provide it in a workable administrative system. And it will be less burdensome and certainly more cost-effective than S. 569.

The differences between us and S. 569 are significant, but they are not perhaps as broad as a lot of people seem to think. One would have to do with coverage, and we believe that in order to have any kind of effective system, you have got to have it cover every single type of entity that files in the Secretary of State's office for its existence. Otherwise, you have just created an escape hatch. And just corporations and limited liability companies (LLCs) is not going to do the trick. That in and of itself would only cover about 80 percent of the filing entities in this country.

The other thing would be you are also going to skew, once you say one set of entities is going to be subject to a certain kind of regulation but another set is not, immediately you are going to have a migration to that other set. So, it is an escape hatch that has to be closed if you are going to have effective regulation.

Second, it has to cover all existing as well as newly formed entities. Senator Levin talked about the sale of existing entities. Well, if you are going to have any kind of control or effective regulation of that, you have got to cover existing entities and not merely new ones that are formed going forward.

The second difference is what types of records are required to be kept by companies, and currently the differences there would be right now companies only keep what is known as "record ownership." You know who the record owner is, an individual—if it is a trust, you know that it is a trust and who the trustee is. If it is an estate, you know who the administrator of the estate is. If it is a corporation or an LLC, you know that it is a corporation or an LLC. You would know. You would have identification of that entity, etc.

So that is the system that exists here, and it is the system that basically exists throughout the world, this record ownership concept. So if you are going to change anything there, you are changing fundamentally what is the recordkeeping system that you have.

Then the third thing is what gets filed in the office of the Secretary of State, and here what we have proposed, instead of filing all this so-called beneficial ownership information—and I will be glad to answer questions about that. That is an impossibility to come up with something that will work, and no country in the world has come up with something that is workable or is in compliance with what FATF 33 apparently says. That information filed in the Secretary of State's office is just going to be a morass of problems and massive noncompliance would result because of the fact that people cannot even figure out what it is, and to have it filed and to keep it updated. And under S. 569, what would happen is that it would be current only as of day one, and then it is not current until a year later; whereas, what we are providing, it would be current as of the time it is requested. And it must be accurate and it must be current. So there are a lot of things where you actually get more information, more current information, more accurate information the way we have established the bill.

What I would like to suggest is this, going forward, if it is possible: For the Uniform Law Commission (ULC), to be able to work with the Committee in trying to come up with a format that we can agree upon that accomplishes the objectives that are being sought, does provide an effective monitoring system, provides better access, and is one that then we can go out and get it approved by the States in a very reasonable fashion. Of necessity, you are going to have to have a Federal act that says that this Uniform Act is the one that needs to be adopted by the States so you get this uniformity across the country in a very short period of time, and that there needs to be some kind of mechanism for funding the up-front cost of getting this established.

Incidentally, under our system, unlike the system as proposed under S. 569 in terms of what gets filed in the Secretary of State's office and maintaining the records and everything, it would be far less expensive, and I do not think any new employees would have to be hired to be able to monitor the information. What we file is different, but in any case, maintaining it.

Then there needs to be probably a penalty of some kind if States do not adopt it within a given period of time. So the sort of carrot and/or stick approach I think will be necessary.

But I guess my final comment would be you need us, we need you, and let us try to work together.

Chairman LIEBERMAN. Thanks, Mr. Haynsworth.

We have had a really good discussion that the five of you have presented to the Committee, I think very beneficial for us. Before we proceed to the questions, Senator Carper, I know you could not be here when we started. Senator Levin and I made opening statements. Before I start questioning, would you like to make an opening statement?

OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. I would welcome that, and I appreciate that very much. I apologize for missing the first part of the hearing. I led a congressional delegation of four other Senators to Afghanistan and Pakistan last month, and we had an opportunity to sit down today with, among others, Ambassador Richard Holbrooke, and this was the one time that he could meet with our delegation, so I apologize for arriving late. And thank you very much, Mr. Chairman, for the chance to say a few words.

I just want to start off by saying to Mr. Haynsworth we very much appreciate the spirit in which you made your offer there at the close of your testimony, and I hope that is an offer that we will seriously consider and, I hope, accept.

I want to thank our Chairman, and I want to thank my colleague Senator Levin, and each of their staffs for working closely with my own staff as we studied this topic and as you all put this hearing together.

The last time that we met on this issue—I think it was in November 2006—I emphasized the importance of this issue to my own State. As some of you know, business incorporations and related fees account for roughly 25 percent of Delaware's general fund revenues. I continue to be proud that my State of Delaware is a leading home of incorporation for businesses in this country. Delaware continues to be a leader in entity corporations because our State has the expertise to ensure corporate success from annually updating our laws to meeting the changing needs of incorporated interests to a well-respected and a renowned judiciary, some of whom I actually had the privilege of appointing as governor of Delaware.

Delaware has enacted a number of laws to deter the formation of illicit businesses and ensure that law enforcement has better access to the information that they need in order to prevent crimes and to solve those that occur.

For example, Delaware was the first State, I believe, in the Nation to adopt legislation responding to the concerns expressed by law enforcement regarding illicit practices of registered agents. Delaware now regulates commercial registered agents and has successfully removed a number of registered agents from doing business in our State.

Delaware requires every business entity to provide the name, the address, and the phone number of a designated communications contact person who is available to law enforcement. And Delaware has responded to international criticism that the U.S. company law permits companies to issue bearer shares—stock certificates whose record of ownership is not maintained by the issuing company—when we explicitly banned the practice in statute to be consistent with long-established Delaware case law.

There are a number of reasons for us to encourage more transparency and disclosure with respect to ownership of legal entities. But whenever we undertake legislation, we have to find the right balance. In this case, we need to provide law enforcement with the tools that they need in order to prevent and to prosecute crime. Having said that, we must also ensure that we do not put additional burdens on our States or our State budgets, many of which are operating in a deficit.

As I think Mr. Haynsworth alluded to in his comments, I am told that some 99.9 percent of corporate entities in the United States are actually good citizens. We should not burden the vast majority of good citizens with expansive and burdensome paperwork while trying to find less than 0.1 percent of bad actors who are likely to try to evade such disclosures anyway.

Whatever solutions we pursue, it is important that we be careful not to hinder legitimate business activities or invade the financial privacy rights of risk-taking entrepreneurs who have historically found the United States to be the freest economy in the world.

At the last hearing that we held here in November 2006, our Assistant Secretary of State from Delaware, Rick Geisenberger, appeared before this Committee and discussed the issues related to disclosure of beneficial owners of incorporated entities, and, Mr. Chairman, I would just like to ask unanimous consent to offer Mr. Geisenberger's testimony from that hearing into our record today.[1]

Chairman LIEBERMAN. Without objection, so ordered.

Senator CARPER. Thank you. In his testimony, Mr. Geisenberger concluded—and he was not alone. He was joined by, I think, the National Association of Secretaries of State, represented here today by Secretary Marshall—requiring entities that incorporate in any State to disclose who the beneficial owners of a corporation are at a certain point in time would be difficult to implement. The act of defining "beneficial owner" is not easy and could be interpreted quite broadly, in some cases requiring the disclosure of hundreds, even thousands, of names.

After that hearing in 2006, I charged Mr. Geisenberger and the Delaware Secretary of State's office with the task of trying to find a compromise on this issue. As we heard today, the National Association of Secretaries of State represented by Secretary Marshall created a Company Task Force to examine this issue in February 2007. The task force asked the Uniform Law Commission, represented today, as we know, by Mr. Haynsworth, to develop amendments to various uniform and model entity laws to help address these issues. The Uniform Law Commission committee included representatives from, among others, the American Bar Association and other stakeholders from around the Nation.

My understanding—and I am sure the witnesses today can attest to this fact—is that this group has worked diligently, some would say ferociously, for 2 years, to find a compromise that would work, that would both assist law enforcement by providing information that they need without putting an onerous burden on States or on legitimate American businesses.

I look forward to hearing further from our witnesses today and to the questioning that is about to take place so that we can get some further update and maybe even a path forward, maybe even along the lines that Mr. Haynsworth has suggested.

Again, Mr. Chairman, as you know and my colleagues know, this is important to my State, and I think it is important to a lot of States. And my hope is that we can resolve this in a way that does what we need to in terms of enforcing our laws and going after the

[1] Senator Carper submitted a copy of Mr. Geisenberger's Prepared Testimony from November 14, 2006, which appears in the Appendix on page 296.

bad guys, at the same time not adversely affecting the good guys, and particularly the States that have to administer whatever law we come up with.

Thanks very much.

Chairman LIEBERMAN. Thank you, Senator Carper. We will begin now with each Senator having 7 minutes of questioning.

I take it, in listening to the panel, that everyone on the panel agrees that it ought to be easier for law enforcement to obtain information about who owns corporations, but that the question is how to achieve that purpose in the best and, I suppose, most effective and least burdensome way. That is true, Secretary Marshall?

Ms. MARSHALL. Yes, sir.

Chairman LIEBERMAN. And you, too, Mr. Haynsworth.

Mr. HAYNSWORTH. Yes, sir.

Chairman LIEBERMAN. I know the three others testified very strongly in favor of that, and obviously, they are in one form of law enforcement or another.

Your testimony was very thorough, and you raised some very good questions, Secretary Marshall. But I wanted to see if I could draw you out a little bit more on just restating in summary fashion what you think the most significant burdens of this would be that essentially tipped the scale against S. 569 as drafted. Why don't you begin with that first?

Ms. MARSHALL. Well, my colleague Secretaries are incredibly worried that even though the conversation here today has been that there would be no verification, that would be the very next thing that would happen, and that would be a burden way beyond the abilities and staffing of my colleague Secretaries of State. Those States which have a stronger public record law believe that they will have a difficult time in developing a confidential database.

The other is the confusion with the beneficial owner. Our frontline people, while well trained, are not lawyers. They are for the most part high school graduates who are good, hard-working State employees. Even the best of lawyers have difficulty in defining "beneficial ownership" and "direct" benefit. And if that is not possible, the control, defining control of an entity, it would just be very difficult to convey that to the public.

The other issue is that all of our State statutes, to the best of my knowledge, have an evergreen requirement to let folks know when addresses change, and that kind of information. And it really does not happen. Most Secretaries have no enforcement powers in the area of compliance. In my situation, I actually have a law enforcement staff because I am a quasi-Attorney General in some cases. But in corporations, I do not.

So, therefore, to get compliance, the only tool that we really have is dissolution of a corporation, and we really are reluctant to do that because public policy of most States is that we encourage and support business.

So the annual report function was created in a lot of States 10 to 15 years ago to make sure that there is a point every year annually where you kind of force a corporation's hand to give you correct, current information. But it is only as good as the day it was mailed.

Chairman LIEBERMAN. OK. So let me now ask Ms. Ayala, Ms. Shasky, and Mr. Kaufmann to respond, because I think Senator Levin's investigation, the PSI investigation, and your testimony to me—I admit my bias having been a former Attorney General—makes a compelling case for providing you with easier access to the question of who owns corporations.

How do you respond to some of the practical problems that Secretary Marshall has made on behalf of the Secretaries of State?

Ms. AYALA. Well, we understand that there needs to be a balance between our efforts to protect our financial institutions and the homeland and our international reputation with preserving a flexible business environment and not having an undue burden on the States. But sometimes there are many agencies out there or many situations that have conflicting or competing missions. For example, the CBP and ICE, we are charged with ensuring and facilitating the timely movement of trade and people, merchandise, money, and things across our borders, while at the same time making sure that we prevent harmful things and harmful people from entering the border.

Chairman LIEBERMAN. That is a good example.

Ms. AYALA. So this is something that is really not insurmountable, and I am sure that at some point an equitable solution will be reached. But at the end of the day, while we are trying to obtain beneficial ownership information, in order to make sure that we are able to further an investigation, prevent further crime, disrupt and dismantle criminal organizations, and really to try to prevent an additional person from becoming a victim or minimizing the misery of victims that are already here domestically or abroad. And while some people view these—we talked a lot about financial fraud cases and other typical cases in that vein. Also, a lot of the money that is flowing through these businesses or these accounts is also the illegal proceeds of human misery, human trafficking, or potential terrorism funds.

So we really do need to find a solution that while it does not place an undue burden on the States, also provides us with an ability to immediately access this information from an individual that is bound by privacy and confidential laws so that we can react in exigent circumstances.

Chairman LIEBERMAN. Ms. Shasky, do you want to add anything to that?

Ms. SHASKY. Yes, Senator Lieberman. Thank you. Like my colleague from the Department of Homeland Security, I echo the comments that it is very important and the Department recognizes that it is very important that we strike a delicate balance between overburdening the States and the legitimate business owners on the one hand, and addressing very serious criminal and national security vulnerabilities on the other.

I would point out that we are not recommending at the Department that States be asked to verify beneficial ownership information. We do believe that defining beneficial owner is possible. In fact, in our written testimony, we provided references to some samples of both domestic and foreign definitions that are out there. I would point out that S. 569 also accomplishes this objective. And in terms of the characterization of giving easier access to law en-

forcement to this information, it is not just about giving us easier access to identifying the beneficial owner. It is giving us the ability to identify that owner at all.

Chairman LIEBERMAN. Thank you. Mr. Kaufmann, do you have a quick response?

Mr. KAUFMANN. I think they said it all, Senator. I will rest on our opening comments.

Chairman LIEBERMAN. You are resting your case.

Mr. KAUFMANN. Absolutely.

Chairman LIEBERMAN. Co-counsel has made the point. Thank you. Senator Levin.

Senator LEVIN. Thank you, Mr. Chairman, and thanks to all of our witnesses.

Mr. Haynsworth, attached to your testimony is a memo which you wrote in which you say that collection and maintenance of accurate business entity beneficial ownership and control information is a key component of the anti-money-laundering business entity proposals that have been made by the FATF. So, from the FATF perspective, which is the international organization trying to get at money laundering, having access to beneficial ownership information is critically important. Would you agree with that? Your own memo says that.

Mr. HAYNSWORTH. Yes, sir. Yes, that is written into FATF Recommendation 33.

Senator LEVIN. Now, in terms of the definition of "beneficial owner," I am not sure who said that there is a problem. I think, Madam Secretary, you did. The Treasury Department has defined "beneficial owner." It is in the regulations. It is in the law.

Ms. MARSHALL. Yes, sir, but it was the FATF acknowledgment that it was a difficult concept.

Senator LEVIN. All right. But Treasury itself has defined beneficial owner in 31 CFR Section 203, anti-money laundering programs definition, beneficial owner of an account means—and they define it. So it is in law.

I am not sure which of you, because I missed, I am sorry, some of your testimony. I had to be on the floor. Unlike these other new concepts, which were put into the Uniform Law Commission proposal, there is a legal definition of "beneficial owner."

Ms. Marshall, you have given us an idea of the cost of what our bill would be. What would the NCCUSL approach cost?

Ms. MARSHALL. Well, the NCCUSL cost for the technology would remain the same. The additional staffing would not be included in the NCCUSL cost. The mailings certainly, to segregate out exceptions and those kinds of things, would not be necessary.

Senator LEVIN. I am saying what would the cost of the NCCUSL proposal be.

Ms. MARSHALL. It would probably be around $500,000, my staff estimates.

Senator LEVIN. Could you give us that estimate for the record?

Ms. MARSHALL. Yes, sir.

Senator LEVIN. And that is $500,000 for your State?

Ms. MARSHALL. Yes, sir.

Senator LEVIN. OK, and that is the NCCUSL?

Ms. MARSHALL. Yes, sir.

Senator LEVIN. OK. Mr. Haynsworth, our bill requires that filers provide beneficial owner information up front at the time of incorporation. Your proposal requires that States collect the names and contact information of two parties—one is the record contact, and the other is the responsible individual. But other than that, there is no real information collected about ownership and control at that point up front. Is that correct?

Mr. HAYNSWORTH. No, sir, because—if you are talking about what gets filed in the Secretary of State's office, it is a responsible individual. If you are talking about what the company is responsible for maintaining, no, sir, they would have information relating to ownership and control.

Senator LEVIN. And if you want to try to get to that company's beneficial information, under your proposal—if we could get our chart up here showing how many steps it would take to do it.[1]

Law enforcement now wants to find out who the beneficial owners are, so the first thing they have to do is to find a record contact and the responsible individual. These are folks who have never been defined before in law, unlike beneficial owner, but that is the first thing law enforcement has to do.

Then, assuming you find that responsible individual, then law enforcement asks that individual to ask the entity for the names of whom? Under your proposal, it does not say beneficial owner. You make no reference to beneficial owner at any time in your proposal. Instead, you say that person is asked to ask the entity for who are the owners of record.

Mr. HAYNSWORTH. Not only the owners of record, Senator Levin, but it is all the information relating to who the managers are, directors, etc. All the records, documents, anything that would pertain to voting rights, who votes on what.

Senator LEVIN. Everything but the beneficial owner.

Mr. HAYNSWORTH. Well, it depends on how you define beneficial owner.

Senator LEVIN. No. You do not make a reference to beneficial owner in your proposal at all, do you?

Mr. HAYNSWORTH. No, sir.

Senator LEVIN. And yet we have the international organization that is trying to end money laundering in this world that says the most important information for law enforcement to know is the beneficial owner. You make no reference to it whatsoever. Instead, you have this wild chase that you, after the fact, set law enforcement on—find that person that you are creating for the first time, a record contact, ask that person to ask the entity to give you information, none of which has to be the key information of who is the beneficial owner.

So, after that goose chase that you are sending people on, they still do not get the information that is the most important to law enforcement, who is the beneficial owner.

Mr. HAYNSWORTH. They get a great deal of information. It depends on how you are defining beneficial owner.

Senator LEVIN. I am not defining it. The Treasury Department is defining it.

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[1] The chart referenced by Senator Levin appears in the Appendix on page 97.

Mr. HAYNSWORTH. Yes, sir. And when you try to apply that, you see that there are a lot of difficulties in trying to figure out who that is.

Senator LEVIN. Well, there may be a lot of difficulties in trying to find out who all those other folks are, voting rights and owners and everything else. But it all may disappear by the time you get to it, anyway.

Mr. HAYNSWORTH. Well, may I just say one thing, Senator? The only country that I know of that has some regulations that would comply with the FATF 33 recommendation with respect to beneficial ownership information is Great Britain. I think it is important to know that this is the FATF report, June 29, 2007, from FATF on the United Kingdom of Great Britain and Northern Ireland, paragraph 1132, "The UK authorities stated that they had considered the possibility of a system requiring up-front disclosure of beneficial ownership. Consultants were engaged in 2002 and a report produced. Public consultation on the report concluded that there were significant disadvantages and no clear benefits, particularly when taking into account the costs of introducing such measures. Reasons included:

"Disclosure of beneficial ownership would add no information of benefit to the register of members." "Register" would be record ownership. "Those engaged in criminal activities would not provide true information about the beneficial owners.

"Two, disclosure would result in misleading information being included on the register. Because beneficial ownership is, as a matter of law, impossible to define precisely, any information requirement designed to require by law disclosure would have to be complex and detailed. Many ordinary, innocent shareholders would be unable to understand or comply with it."

Paragraph 1133: "In the light of these points, it was concluded by the UK authorities that the existing register of members already provides investigators with as much as any disclosure regime can. The view was taken that attempting to add details of beneficial ownership to the existing register would be harmful to investigations through the resulting misleading information provided by both criminal and innocent shareholders."

Senator LEVIN. OK. Now let us ask Mr. Kaufmann about that misleading information argument, not useful argument that Mr. Haynsworth said.

Mr. KAUFMANN. That is something, Senator Levin, that we have discussed a lot in my office, and I think there are a couple of points about what happens when someone provides false information that are not readily apparent to those who do not prosecute crime for a living. And from the perspective of law enforcement, the very requirement of having someone state beneficial ownership is important because it brings an aspect of daylight onto the activities of these criminal corporate entities. Now, we are not talking about really worrying about the legitimate corporations out there. I am focused on the shell companies, the criminals, the money launders, and the tax cheats.

And so what happens when we ask them to state up front who is the beneficial owner of the company? When someone gives false information in that regard, it is tremendously powerful and persua-

sive evidence of what the criminal law calls "consciousness of guilt." When we have a statement from a person that set up a shell company at the time of the incorporation that lists a nominee or a straw person, it does not matter that it was not verified by the States. None of us are asking for State verification. That would be a burden.

What it does is it creates a record at that moment in time that that person who set up that shell company told a lie. So when we go to prosecute that person in these types of white-collar cases, it always comes down to proving intent. That is the whole ball game in a criminal trial for a white-collar, money-laundering, security fraud, or tax evasion-type of event.

If we have a lie, we can say to a jury, "Let me ask you something. Why would an innocent person have listed a nominee or a straw man or put their grandmother down as the owner?" The answer is an innocent person would not have done that. So, from our perspective, it gives us a very powerful tool to prove the criminal intent of the person that set up the shell company.

The other point, this focuses more on the dirty agent that is setting up shell company after shell company after shell company. And in this regard, we might be looking at, for example, an identity theft ring, and we may see that this identity theft ring went to the same incorporation agent again and again and again to set up shell company after shell company after shell company.

If we have a tool that says to the incorporation agent, "You have to put down the beneficial owner when you create these shell companies," well, if that incorporating agent is again and again and again filing false and misleading information with the State, that gives us from the State perspective a State charge that we can bring against that incorporating agent. And that is going to be a very powerful tool to clean up an industry where I think that there are bad actors out there, and the fact that we cannot necessarily tie them in to being part of the ring, to being an accomplice in the money laundering or the securities fraud. But if we can go after them for their independent conduct of setting up false companies by filing false statements with States, that gives us a tool to go after the bad actors and to encourage the good actors who are out there doing what they are supposed to do and setting up good corporations and making good business happen in this country.

Senator LEVIN. My time is up, but I would just say that we ask banks all the time for who the beneficial owners of accounts are, and they provide that information to us. That is what the Treasury Department definition is for, and we ask for it all the time.

Mr. KAUFMANN. It is the basic cornerstone of all the anti-money laundering (AML) programs for all the banks, not just in this country but around the world.

Senator LEVIN. I wonder if the Justice Department could just quickly say, don't we ask banks for beneficial owners?

Ms. SHASKY. Senator, we do, and we get that information every day. We do believe it is absolutely possible and that there are provisions already defining beneficial owner.

Senator LEVIN. Thank you.

Chairman LIEBERMAN. Thanks, Senator Levin. Senator Carper.

Senator CARPER. I think there is probably one thing—I had not planned on asking this question, but it would seem to me the beneficial owner of an account at a bank might be fairly easy to identify. I think the beneficial owners of corporations change not just every year, not just every month, not just every week, but every day. The folks that own common stock and preferred stock in these companies change sometimes by the minute. So I am not going to pursue that, but I just want to kind of put that out there, if I could.

Again, we appreciate the testimony of all of you here, taking your time and really trying to help us work with a difficult issue and try to come up with something that is, as they say at Fox News, "fair and balanced," and hopefully before we are done, we will do that.

The first question I have would be for the Secretary of State. Ms. Marshall, where are you from in North Carolina, anyway?

Ms. MARSHALL. I live in Raleigh.

Senator CARPER. OK. My wife is from Boone, and I have a sister-in-law in Holly Springs and one——

Ms. MARSHALL. I am one of the elected Secretaries of State, so let them know. [Laughter.]

Senator CARPER. I certainly will. That is great to know. You must be pretty good at it because you have been doing this for a while.

If the States are required to obtain beneficial ownership on every corporation formed in their State, do you think that is enough for law enforcement? And going back to the question of verification, does somebody need to verify who all these people are to determine if they are engaged in legitimate or non-criminal activities? How do we do one step—that is, the disclosure—without at some point in time doing the second step—and that would be the verification.

Ms. MARSHALL. Well, that is a problem for us. I know that it has been stated here that is not going to happen, but truly, as I said in my remarks, for people to believe a law is a good thing to be able to comply with it, they have to understand why. And if incorrect information is just as good as correct information, we are not being fair to ourselves about what we are all about as State office holders.

I understand that when someone provides that information, if they are a third party who is providing incorrect information rather than the Mom-and-Pop's that we deal with all the time, it is just a tremendous burden on all those people for something that they will not be able to see the light at the end of the tunnel as to why this information is being asked, except that government is just too intrusive.

Senator CARPER. You may not know the answer to this question. If you do not, just feel free to say so. But if verification is required, any idea how much more this would require in terms of costs or expenditures or outlays by the States?

Ms. MARSHALL. It is impossible to say. It depends upon what verification you would be doing. In one of our suggestions, we had talked about a notarization. We have a robust notary law in North Carolina, and that is to show that the person who is signing the document actually is that person. We encourage notaries to keep

that photo ID. That would be transferring the verification somewhere else.

If we had to do that, there is no way—I have 50 people in my Corporations Division, 200 all together. I would probably need another 50 people just to be able to do verifications.

Senator CARPER. OK. If I could, maybe a question for Mr. Haynsworth. Do you know your other 49 colleagues from the other 49 States?

Mr. HAYNSWORTH. You mean the Commissioners of Uniform State Laws?

Senator CARPER. Yes.

Mr. HAYNSWORTH. Yes, sir.

Senator CARPER. Have you ever met one from Delaware?

Mr. HAYNSWORTH. I have met several from Delaware, yes.

Senator CARPER. How long have you been a commissioner?

Mr. HAYNSWORTH. I have been a commissioner for 18 years now, but I have worked with Delaware lawyers who happened to be commissioners——

Senator CARPER. Michael Houghton is an attorney from Delaware. I do not know if you have ever——

Mr. HAYNSWORTH. I know Mr. Houghton very well. Yes, sir.

Senator CARPER. I appreciate the time that you and others on your committee have spent on trying to find a workable compromise on this issue. We all appreciate that. I think we have a chance here to advance the ball and to help law enforcement while also not overburdening our States and our State systems.

How is your proposal less of a burden on the State framework than what is being proposed by my colleague from Michigan?

Mr. HAYNSWORTH. Well, one difference would be that what gets filed in the Secretary of State's office is much less prolific, if I can use a word like that. You file the name of the responsible individual, which has to be somebody who is directly involved in the management of the company. So that is somebody law enforcement can go to directly and find out what is going on here, what is this company about, who is involved in it, and all that. And the other is the name of the record contact, and that is the person that has to be able to get all this information about the ownership, control, management, and all the records the company has with respect to that. So that is what gets filed in the Secretary of State's office, not all this beneficial ownership information or any other kind of ownership information, because that has never been filed, in any substantial amount, in Secretaries of State offices. So in that sense, it is much less burdensome.

In terms of the companies, they keep a lot of information that relates to the ownership, who the individuals are that own, who the trustees are, other corporations, entities, whether they are foreign or domestic, contact information for all those people. And you get all that information. And then law enforcement could take that information, and if it is a foreign entity, they know where to go to that entity, foreign state entity or even an in-state entity, that entity has to have a records contact person that would provide the information about who owns that entity.

And companies do not keep that kind of information themselves. If you are a company, you have the information that it is a trust,

but you do not know who the beneficiaries are. You have the information about that it is a company, formed in Delaware or wherever it may be, but you do not know who the owners are. And you have really no way of getting that information.

And then if it is going to be inaccurate—say it is an entity. That entity has a change of ownership. Well, immediately, unless they alert the company that is keeping this information, how are they going to know about it? They have no way of knowing about it.

So you are just creating the possibility that there is just going to be all this misinformation out there and inaccurate information, and most of this will be totally unintentional. So law enforcement, instead of having a benefit, it is going to actually be more difficult for them to find out the information than if they could go directly to this record contact and responsible individual, get as much information as they can, and then trace back. And if they are worried, the ultimate individual beneficial owner, they will find out instantly, and in most situations there is not going to be a beneficial owner in control.

I will give you one example. You have three individuals, and they own an equal amount of stock—we will make it simple—an equal amount of stock in a corporation. And they each elect one director, and that is it.

Now, is there somebody in control? There is nobody that is in control because no one individual can control anything. You have 10 owners of a company, and they have an agreement that it takes unanimous consent to do anything. Nobody has control.

Ms. SHASKY. Senator, if I may, I would suggest to you that in a criminal organization—

Senator CARPER. This is a place where we actually work under unanimous consent, and sometimes—I would agree—we do not know who is in control here either. [Laughter.]

Chairman LIEBERMAN. Well, you remember what Alexander Haig said.

Senator CARPER. I do remember.

Chairman LIEBERMAN. He said, "I am in control here."

Senator CARPER. Go ahead, Ms. Shasky.

Ms. SHASKY. Senator, I would submit to you that in a criminal organization everyone knows who is in control, and this will not be an issue of determining who is in control. What we are concerned about here from the law enforcement perspective are the criminals and the criminal organizations, and so what we are asking is that when criminals use shell companies, they provide the name of the beneficial owner. That is the person who is in control, the criminal in control, as opposed to the NCCUSL proposal where they are suggesting that instead two nominees are provided—two nominees between law enforcement and the criminal in control.

Thank you.

Senator CARPER. Ms. Marshall, I saw you shaking your head a little bit there when Ms. Shasky was speaking. I do not know if you wanted to say anything on that. If you do, fine. If you do not, that is all right. But in your testimony, you state that a number of States—Wyoming was one, I think Delaware is certainly another—have passed significant legislation that is designed to combat some of the problems that we have gathered here to talk about today.

And if you can help us with this, I would appreciate it. Are you in a position to give us an idea of some of the laws that the States have passed in the last several years?

Ms. MARSHALL. Yes. You will find in your materials statements from both Nevada and Wyoming. Both of those States were held out as poster children back in the fall of 2006 regarding some of these activities of registered agents——

Senator CARPER. Held out in a good way?

Ms. MARSHALL. In a bad way. And they took that message very seriously to heart, with both States doing a fairly major overhaul in their legislation during 2007.

For example, Wyoming now requires each company must have a registered agent, human being, in the State at a physical location. No drop boxes are allowed. The registered agent must keep information about the key players of the company represented, must have information about a contact person for each company. They have greatly increased their law enforcement authority. They have provided a felony provision for filing false documents.

The State of Nevada has eliminated the bearer shares. They have a strict prohibition on the bearer shares. The authority is given to the Secretary of State to investigate forged or fraudulent filing complaints and to correct documents when they are deemed forged or fraudulent. The Secretary now requires information on owners of record be provided upon demand, requires answers to interrogatories in the course of criminal investigation, and if information is not received in 3 days, then certain other things begin to happen.

Those are just highlights of what these different States have done. And Delaware, of course, has done the Registered Agent Act requiring an in-state registered agent with materials, and they can go out and audit. They can revoke their ability to be a registered agent. They can do criminal prosecutions, as I understand it.

Senator CARPER. Thank you. Mr. Chairman, my time has expired. Will there be another round?

Chairman LIEBERMAN. Yes, indeed.

Senator CARPER. OK. Thanks so much.

Chairman LIEBERMAN. Thank you.

Ms. Shasky, let me start with you. In your opening statement, you listed four principles or components that from the perspective of the Department of Justice you would like to see in legislation that improved corporate transparency practices as we have described them. I wanted to ask you to what extent you believe S. 569, which is the subject of this hearing, fulfills those four objectives.

Ms. SHASKY. Absolutely. First of all, the Department would like to thank Senator Levin for his leadership in this area in working with his fellow Committee members in developing this legislation. The Department strongly supports any Federal legislation that would bring transparency to this area. Nonetheless, we do feel the bill needs some amendments to align with the four principles outlined in my opening statement.

We are most supportive of the fact that the bill does require beneficial ownership information. This is key. And the bill does have that requirement in it. We would add to that, requesting, in addi-

tion to the name of the beneficial owner and the current address, that the beneficial owner be asked to provide a photo ID. The bill allows for this with foreign beneficial owners but not domestic. So we would make that change so that both domestic and foreign beneficial owners provide a copy of the photo ID. We are afraid that to do otherwise would merely invite fraud. We would expect that foreign criminals would claim falsely to be U.S. persons or to use straw actors, if we had that difference there.

In addition, S. 569 requires an annual certainly of who the beneficial owners of a company are, unless the State does not have that requirement, in which case it would require an update to the beneficial ownership every time there is a change.

We would suggest and recommend from the Department perspective that both of these things be required, so anytime there is a change in beneficial ownership information, it should be updated, and then annually it should just be verified.

Now, I would point out that we do recommend exempting companies that are already regulated by State or Federal regulatory bodies and need to provide beneficial ownership information as a result of that. So like the company that Senator Carper mentioned that is listed on the stock exchange with a securities commission, they would be exempted from this bill.

Finally, we would recommend slightly strengthening the Federal penalties contained in S. 569 to target those who would act willfully blind in failing to update information. So we look forward to continuing to work with Senator Levin and the Committee and the staff to bring S. 569 on par with the four principles outlined in my opening statement.

Chairman LIEBERMAN. So would it be fair for me to conclude that generally the Department of Justice is supportive of this legislation with the amendments or additions that you just described?

Ms. SHASKY. I think it would be fair, Senator, to say the Department is supportive of all attempts to craft Federal legislation bringing transparency, but, unfortunately, the Administration has not yet taken a position on the bill.

Chairman LIEBERMAN. Understood.

Ms. Ayala, from the vantage point of Immigration and Customs Enforcement, again, your testimony is very forward-leaning about certainly the purpose of S. 569. Is there anything particular you would add or subtract from it?

Ms. AYALA. Again, I also would like to thank you and I certainly appreciate your efforts in bringing so much attention to this problem and engaging all the stakeholders in looking for a solution, and we hope that at the end of the day any legislation that is passed will enable law enforcement to immediately obtain this information and to be able to obtain it from one central point at each State and that it is consistently obtained. That way we are not in a position of looking around and spending time, maybe weeks, exhausting so many individuals in our investigative efforts and, like you said, run around on a wild goose chase and waste our time in general.

But we also would like to see that this information is updated because that is very important for us, not only to make sure that we are focusing in a correct time frame as to who owned the company, but to also not waste the time of a legitimate company or a

beneficial owner that might have owned the company beforehand and have to bother with that person or look at that person as a target of investigation.

I know that the Secretary has received a letter from this Committee, and they are formulating a response as to their position.

Chairman LIEBERMAN. Good.

And, Mr. Kaufmann, I will finally give you the chance to help us write some good legislation.

Mr. KAUFMANN. I think the concept of beneficial ownership is one that is well established in the law. I think that the Congress has made great strides in increasing transparency through the Bank Secrecy Act and the USA PATRIOT Act to make sure, for example, that banks know who their customers are. I see this bill as being a simple answer.

I also think it would strengthen the bill to make parallel provisions for requiring identification from both domestic and foreign registrants of corporations.

I guess I am a little bit confused as to the perception that I am hearing that this will be so unduly burdensome. As we have looked at this, it seems to be simply a question who is the owner of this company, and I do not see the tremendous volume or burden that that imposes.

One fundamental disconnect from what I am hearing from my left and my right, and I do not say this facetiously at all, but some of the concepts that are being put forth—and we are trying to achieve a balance here—but they are not rooted in the reality that we see in how we investigate criminal organizations. And I think that Ms. Shasky said it well. In a criminal organization, there is no doubt who is in control. When we are investigating a criminal organization, we cannot go to the person designated by the company to contact them because it is akin to picking up the phone and telling the criminal that he or she is under investigation. So the fundamental flaw in the NCCUSL structure is that we have to go to the target of the investigation to obtain the information that we seek to further the investigation.

What S. 569 does is it puts that information with the State so we can get it without going to the target and alerting the target to the fact that we are investigating them.

Chairman LIEBERMAN. Very helpful answers.

A vote has gone off. I am going to go over and vote. I, unfortunately, cannot return so I am going to leave it to my senior colleague to conduct the rest of the hearing and determine, together with Senator Carper, whether at any point you want to recess and come back. And I do want to assure the witnesses with the long knowledge of Senator Levin, I can assure you he believes not only in equal protection but in due process. So you will be all right. [Laughter.]

Senator Levin, it is all yours.

Senator LEVIN [presiding]. Thank you, Mr. Chairman.

Ms. Ayala, when you said that it is important that law enforcement be able to obtain this information, you were referring, I believe, to the beneficial ownership. Is that correct?

Ms. AYALA. Yes, Senator.

Senator LEVIN. So just to be real clear as to where the witnesses are, do you believe that it is important that beneficial ownership information be collected? Ms. Ayala, first.

Ms. AYALA. Yes, Senator.

Senator LEVIN. Ms. Shasky.

Ms. SHASKY. Absolutely, sir.

Senator LEVIN. We know where the other three witnesses are, and I want to just focus on you two.

Where should the ownership be kept, in the United States or in a foreign jurisdiction? First, Ms. Ayala.

Ms. AYALA. It should be kept in the United States where it is easily accessible.

Senator LEVIN. OK. Ms. Shasky.

Ms. SHASKY. Senator, that is not even a close question. It should be in the United States.

Senator LEVIN. All right. And when should the ownership information be collected—when the company is formed or after it is being investigated for suspicious activity? First, Ms. Ayala.

Ms. AYALA. When it is formed.

Senator LEVIN. Ms. Shasky.

Ms. SHASKY. When it is formed.

Senator LEVIN. And is it important to be able to determine beneficial ownership and other basic corporate information without tipping off the corporation that an investigation is going on?

Ms. AYALA. Yes, it is absolutely necessary in order to preserve evidence and make sure that illegal funds are not being moved or to convolute our investigative process.

Senator LEVIN. OK. Ms. Shasky.

Ms. SHASKY. Senator, our job would certainly be much easier if all we had to do is ask the criminal to provide us with the evidence. So it is imperative that not be the case here.

Senator LEVIN. All right. Now, you both have testified in terms of your agency's position in terms of this specific bill, and I think, Ms. Shasky, what you said is that there are four principles you laid out, which are fine with me. You have also indicated a number of ways which I would say would strengthen the bill, would make it a tougher bill: A photograph for domestic as well as foreign beneficial owners; a regular update when there is a change in the beneficial ownership, not just each year; and the other two, I think, qualified as toughening or strengthening, which would make the bill probably more objectionable, I would think, although I am not going to speak for the Secretary, but, Ms. Marshall, would you say those suggestions would make the bill more objectionable?

Ms. MARSHALL. Yes, sir.

Senator LEVIN. All right.

Ms. MARSHALL. If it is a government-issued ID with a person's name on it, that is one matter. If it is a photo, we have no idea if it would match up to the name. Would we be in a position of rejecting photos? Suppose it is a photo of someone with heavily draped head wear and all we see are eyes? Do we reject those, when that is what that person wears for religious reasons? On and on and on.

Senator LEVIN. Well, I doubt that the Justice Department would suggest you reject any photo. I think they just want you to file it. But I will let them speak for themselves.

Let me also ask you, Mr. Kaufmann, specifically in terms of the bill, do you and does your office support the bill?

Mr. KAUFMANN. Yes, sir, absolutely.

Senator LEVIN. OK. As to the FATF question, the beneficial owner standard in FATF has been there for 20 years, by the way. It has been in U.S. law since the USA PATRIOT Act of 2001, and it is also in other securities, tax, and anti-money-laundering bills. So this is a concept which has been defined in a number of ways and a number of laws.

Finally, in terms of FATF, we have 27 countries that now require the beneficial ownership information. We are not sure what the status of all their compliance is, but we know they have all committed to it. And that is the question, whether we are going to commit to it as a country, the way other countries have committed to it.

When you said, Mr. Haynsworth, that this has to apply to all the States, I think that is clearly true.

Mr. HAYNSWORTH. Yes, sir.

Senator LEVIN. Uniform law does not have to be adopted by all the States.

But the bill does not change State law. It adopts a Federal requirement that the States ask the question on the incorporation form about beneficial ownership. Are you suggesting that under the Commerce Clause of the U.S. Constitution, given what corporations do across boundaries of States, we do not have the jurisdiction in Congress to require States to ask the question on their incorporation forms? Is that what you are saying?

Mr. HAYNSWORTH. No, I am not. What I am saying, Senator, is for the States to be able to do that, there would have to be enabling legislation in the State to make that occur.

Senator LEVIN. Well, if there is a Federal law that requires them to do it, are you suggesting they are not all going to do it?

Mr. HAYNSWORTH. Well, what I am suggesting is that you are likely to end up with very different interpretations of what that means, and you are going to end up with 53—because you have to include DC——

Senator LEVIN. We have a Treasury Department definition. We have one line. You must ask for the beneficial ownership as defined in 31 CFR. That is not complicated. Your proposal is a heck of a lot more complicated and convoluted than that. I do not see how 50 States can come up with 50 definitions if we say the definition already in Federal law is the definition in our law, and we incorporate it by reference.

Mr. HAYNSWORTH. Yes, sir, but there would still have to be State legislation that says that the States will——

Senator LEVIN. Comply with Federal law? Really?

Mr. HAYNSWORTH. No. That what would be filed in the Secretary of State's office and what would be required to be in those filings, that is a matter of State law.

Senator LEVIN. Thank you. Senator Carper.

Senator CARPER. Thank you. Secretary Marshall, it is my understanding that the funding from the bill that Senator Levin has introduced will come from homeland security grants that States currently receive. Is that correct?

Ms. MARSHALL. That is correct.

Senator CARPER. If you had to prioritize the way that your State, North Carolina, homeland security grants would be spent, any idea where this bill's requirements might rank?

Ms. MARSHALL. I think very low. I mean, I think the anticipation on homeland security money is that it is already inadequate to do what all our first responders, all our medical folks, all our emergency preparedness folks would like for it to do. And it is not a very enticing place that we would like to be competing with them for bulletproof vests, respirators, and training, the types of things that they are using that money for.

I cannot speak for that grantmaking entity, but this is certainly very different than the kind of things that they are entertaining grant requests for.

Senator CARPER. OK. We have about 5 minutes to get over to vote on a big piece of legislation, so I am going to ask a couple of questions to be answered for the record.

One of the questions I want to say—and I do not have time, unfortunately, to listen, to hear you out, but, Mr. Haynsworth, at the conclusion of your statement basically you said let us just keep working at this and see if there is not some way that we can meet the legitimate concerns of law enforcement and be respectful of the concerns of States.

I think we have been working on this for a while, and I would like to—I am one who does not give up very easily on almost anything that I think is important. And I am not inclined to give up here either. But you made an offer, I think, in good faith that we should maybe redouble our efforts and see if we cannot come close to where we want and need to be.

Do you think you are speaking for one person, or do you think you are speaking for all the commissioners?

Mr. HAYNSWORTH. I am speaking for the Uniform Law Commission, and I am certainly speaking for my committee and what we are trying to do. And one thing, Senator, I might just mention is that we have one shot at this in order to get it right and to get it then adopted by the States in a way that makes sense. And one of the things I have been reading about a little bit is this PASS ID legislation that is aimed at trying to correct some problems with overburdensome regulations imposed by Congress under the REAL ID.

Senator CARPER. Yes, we are familiar with it.

Mr. HAYNSWORTH. All right, sir. Well, I think you were one of those.

Senator LEVIN. We are really familiar with it.

Mr. HAYNSWORTH. But, I mean, we have to avoid that at all costs because of the Federal-State relations and trying to make something that really does work and does achieve the purposes that we are all trying to achieve.

Senator CARPER. All right. I think we are out of time.

Senator LEVIN. Thank you, Senator Carper. Thanks to all of our witnesses.

Senator CARPER. And we will have some more questions to submit for the record, if we could.

Senator LEVIN. I will just close with a quick comment, which is that we are going to have to end the misuse of U.S. corporations, and there is only one way to do it, and that is to require those corporations to disclose beneficial ownership. There is no other way to do it. Otherwise, it is a three-step wild goose chase after the horse is out of the barn, I guess, to mix metaphors. We have horses and geese, but the point I think is pretty clear.

We very much appreciate the testimony, and we will stand adjourned, with Senators being able to file questions for the record. Again, we thank you all, and we will stand adjourned.

[Whereupon, at 4:55 p.m., the hearing was adjourned.]

BUSINESS FORMATION AND FINANCIAL CRIME: FINDING A LEGISLATIVE SOLUTION

THURSDAY, NOVEMBER 5, 2009

U.S. SENATE,
COMMITTEE ON HOMELAND SECURITY
AND GOVERNMENTAL AFFAIRS

The Committee met, pursuant to notice, at 10:04 a.m., in room SD–342, Dirksen Senate Office Building, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.

Present: Senators Lieberman, Levin, Carper, McCaskill, Burris, Ensign, and Bennett.

OPENING STATEMENT OF CHAIRMAN LIEBERMAN

Chairman LIEBERMAN. Good morning. The hearing will come to order. This is our Committee's second hearing on the Incorporation Transparency and Law Enforcement Assistance Act, S. 569, which was introduced by Senators Levin and McCaskill, who are Members of the Committee, and by Senator Grassley, who is, of course, the ranking member of the Finance Committee.

This legislation, which is the result of work done by Senator Levin's Permanent Subcommittee on Investigations (PSI), seeks to increase the transparency of business formation practices as a way to reduce what is estimated as billions of dollars in fraud that is perpetrated by shell corporations.

Each year nearly two million new corporations and limited liability companies (LLCs) are established in the 50 States and the District of Columbia. That comes to more than 5,000 new businesses every day. This is really the American way, entrepreneurship at its best, generating revenue and creating jobs, people taking risks and building on innovations.

But each year a relatively small number of those businesses—but nonetheless a significant number—are incorporated for improper or illegal purposes to try to use registered corporations to defraud innocent people, to cheat tax authorities, to hide true transactions or to launder ill-gotten funds.

Right now a majority of States require basic information from those seeking to establish a corporation. Most require the name and address of the company, the name of a registered agent who represents the company, and a list of officers and/or directors. This information typically is considered a public record, but most States allow individuals with actual ownership interest, including the investors who control the corporation or partnership, to remain anonymous to State authorities and therefore to the public, and this is the problem.

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This is a problem for law enforcement, of course. Senator Levin's bill offers one solution to this problem, which is to set a national minimum standard for State incorporation practices that require States to collect, maintain and update so-called beneficial ownership information. But there are critics of this method who argue that this well-intended desire for more sunshine should be weighed against other factors, including the privacy rights of those making personal investment decisions and the cost of administration and enforcement that would fall on companies and State governments.

Our goal today is to hear from witnesses who are expert in various aspects of this problem so that we can make a judgment now about how best to proceed to deal with what everyone acknowledges is a problem. On the first panel we will hear from the Treasury Department, which administers anti-money laundering laws and leads U.S. efforts to stop the flow of terrorist financing. Treasury has worked tirelessly on corporate transparency issues, engaging with stockholders to consider all the possible approaches to improving practices in this area.

We're also going to hear from the Department of Justice, which has first-hand experience, of course, in the challenges of law enforcement as they try to combat the use of corporations for nefarious purposes.

Our second panel of witnesses represents the business and legal communities which have distinct concerns about obviously the smooth flow of commerce for legitimate corporate purposes. We are also going to hear from a representative of the Federal Law Enforcement Officers Association and an expert on tax havens, both of whom support the general approach taken by the bill. So this is an interesting and important matter on which we hope to shed some light this morning.

Senator Ensign, it is a pleasure to have you sitting in for Senator Collins today. I know she is particularly happy you are sitting in for her and I welcome you and your opening statement at this time.

OPENING STATEMENT OF SENATOR ENSIGN

Senator ENSIGN. Thank you, Mr. Chairman. I think this is a very important piece of legislation because it affects a number of different issues, not the least of which is its impact on the small business community, which serves as the backbone of our economy.

Corporate law has long been within the State's domain. By forcing States to amend their individual laws on corporate formation, Congress is effectively imposing a Federal standard on business creation, ignoring the particularities of each State's business culture. With such a new Federal standard, there is no incentive to choose one State over another when deciding where to form a business.

I believe that this will hurt many business-friendly States like my home State of Nevada. Businesses choose Nevada as their State of incorporation because of our State's regulatory climate, tax situation, and flexibility for companies to run their businesses how they see fit. This week I received comments from the Nevada Sec-

retary of State for this hearing and I would like at this time to submit his statement and letter to me for the record.[1]

Chairman LIEBERMAN. Without objection, so ordered.

Senator ENSIGN. If enacted, S. 569 would require my State to add additional staff, undertake an extensive rewrite of the e-Secretary of State processing system and deploy a new system, maintain a separate, non-public database, and deal with other operational infrastructure needs.

And this is a Democrat Secretary of State. According to their office, the estimated cost for initial implementation could reach as high as $10 million, with ongoing operating costs of $1 million annually. These are costs that my home State of Nevada simply cannot afford at this time.

As a former small business owner, I know firsthand how difficult it is to start and to grow a business. It is certainly more difficult in today's economic environment. Every dollar spent on the burdensome requirements under this bill is one less that can be reinvested in the business. Too often in Washington we see unintended consequences of bills that, while they have a valuable purpose, turn out to be overreaching in their application. I fear that this is the case with this bill.

It will result in significant regulatory and compliance costs that may have a chilling effect on the creation of new businesses and new jobs at a time when our economy can least afford it. The term "beneficial ownership" as defined in the bill is simply too broad. Rather than qualifying it by some clear cut standard, the language in the bill is borrowed from the Treasury Department's use of the term to determine the proper taxpayer on a bank account.

Because of the number of different entities involved, this is not a workable comparison for corporations and LLCs. It leaves open the possibility to interpret the definition differently. Rather than risk the harsh penalties associated with non-compliance, entrepreneurs will be encouraged to register their businesses only after consulting with certain professionals, such as attorneys and accountants. The expense associated with this new registration process will simply be too great for many smaller startup businesses to bear, resulting in less business activity and less job creation.

Mr. Chairman, we are not the first economic power to consider the regulatory system proposed under this bill. In fact, efforts to enact a similar regulatory scheme have failed in other jurisdictions, most notably in the United Kingdom. I understand that one of the witnesses in the Committee's last hearing on this topic mentioned this. The United Kingdom considered a system requiring upfront disclosure of beneficial ownership as defined in a manner consistent with the definition in the bill before us. The U.K. authorities rejected this approach, concluding that "there were significant disadvantages and no clear benefits, particularly when taken into account the cost of introducing such measures."

As a basis for their conclusion, these authorities noted "that those engaged in criminal activities would not provide true information about beneficial owners" and that "disclosure would result in misleading information being included in the register."

[1] The letter submitted by Senator Ensign appears in the Appendix on page 435.

According to these authorities, requiring further details of beneficial ownership "would be harmful to investigations through the resulting misleading information provided by both criminal and innocent shareholders." Mr. Chairman, it is my hope that we can continue to work together on this very important issue to ensure that the needs of law enforcement are adequately met while not overburdening our States or our business communities. I thank you for this hearing.

Chairman LIEBERMAN. Thanks very much, Senator Ensign, for that thoughtful opening statement. Normally we would just have the Chairman and Ranking Member give opening statements, but two of our colleagues here, and very valued Members of the Committee, have been involved in this matter quite a bit and I think it would be helpful to the Committee, if they are so inclined, to ask Senator Levin and then Senator Carper also to deliver some opening comments.

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. Thank you, Mr. Chairman. Last hearing we went into a number of examples of how the hidden secret ownership of corporations in this country denies law enforcement critical tools and this hidden ownership is a significant security risk to our country because it frustrates law enforcement in this country.

Just a number of examples. Viktor Bout, who is a Russian, one of the most notorious arms traffickers in the world, is featured in a book called "Merchant of Death." Last year the United States indicted him for conspiracy to kill U.S. nationals, the acquisition and use of anti-aircraft missiles, and providing material support to terrorists. To carry out his activities, he is known to use a network of shell companies around the world, including companies formed in countries like Liberia, Moldova, as well as here.

Now the first chart, which we have up in front of us here, lists the names of 10 Texas and Florida companies alleged to have been used by Viktor Bout over the years.[1] It also includes two Delaware companies that were alleged in a 2002 Interpol notice, based on information from Belgium, to have been used by Viktor Bout to transfer $325 million to carry out his activities. The chart does not include another company, Garland Global Corporation, which Romania believes may also be related to Viktor Bout, but whose beneficial owners are unknown.

In July 2009, Romania filed a formal request with the United States for the names of the company's owners and other information, but it is unlikely the United States can supply the names since as this Committee has heard before, our 50 States are forming nearly two million companies each year and in virtually all cases, doing so without obtaining the names of people who will control or benefit from those companies.

The end result is that a U.S. company may be associated with an alleged arms trafficker and supporter of terrorism, but we are stymied in finding out in part because our States allow corporations with hidden ownership. Here is another aspect of the problem. Last month my staff went on the Internet and typed in "shell

[1] The chart submitted by Senator Levin appears in the Appendix on page 368.

company" as a search term. The first entry that came up was for aged shell companies and provided a link to the Web site of a company called Go Risk-Free, which offers corporations for sale in all 50 States.

Chart two, which is in front of us,[1] shows how Go Risk-Free promises "if you need a company that is in a certain State or age, contact us and we will help you find it." On the date that we checked, Go Risk-Free had over 200 companies available for sale. The price starts at $3,500. The first was a Nevada company incorporated in October 1928, 80 years ago. A secret buyer of this company can pretend to have had a U.S. business in operation for decades, could use that shell company to convince a bank to open an account or issue a credit card and go from there.

These sales seemingly have no purpose other than to create a misleading impression. The potential for criminals to buy these types of companies without ever divulging their names or interest is a threat to our security and to our well being.

At the Committee's hearing in June, we were told about a New York corporation that was secretly owned by members of the Iranian military. Our government learned of that ownership interest not from New York State records, but because another country had the beneficial ownership information that we didn't. We heard about a network of 800 U.S. companies across the country that had attracted law enforcement attention because they were transferring suspect funds to each other and in and out of high-risk jurisdictions.

When the Department of Homeland Security, Immigration and Customs Enforcement (ICE), tried to find out the company's owners, all they could learn was that they were associated with a group of shell companies in Panama. ICE eventually dropped its investigation, in part because not one of the 800 company formation documents had any information on the true owners. Now, these are only a few examples of U.S. companies being used to engage in a wide range of wrong doing from money laundering to tax evasion to drug trafficking and worse.

Right now we require people to provide more information to obtain a driver's license than to acquire a U.S. corporation. Most of our States allow hidden owners to buy companies online, within 24 hours of a request in two States. For an extra $1,000, hidden owners can form a U.S. company within a single hour.

In 2006, the leading international anti-money laundering body in the world, the Financial Action Task Force (FATF) on money laundering, issued a report criticizing the United States for failing to comply with the FATF standard requiring countries to obtain the true owners, the beneficial owners of the corporations formed in their countries.

FATF set a goal of 2 years, until July 2008, for the United States to strengthen its compliance with the FATF standard. We are now more than a year past due with no progress to speak of. That is why we introduced the bill which is the subject of today's hearing. Beneficial ownership information would be available to law enforce-

[1] The chart submitted by Senator Levin appears in the Appendix on page 367.

ment presenting a subpoena or a summons. That information would be available to the public only if State law so provided.

The minimal cost of adding a question to State incorporation forms could be paid for with funds already provided to the States on an annual basis by the Department of Homeland Security (DHS). Our bill does not require any State law to be passed. Nevada or other States will still have their business-friendly tax and regulatory laws in place.

A host of law enforcement groups have endorsed our bill, including the Federal Law Enforcement Officers Association, which we will hear from today. It has also been endorsed by groups combating financial crime, corruption, and tax evasion, including the Tax Justice Network USA, Global Financial Integrity, Citizens for Tax Justice, and many more. By the way, an identical version of the bill was co-sponsored by President Obama last year when he was a senator.

One final point, we have been fighting offshore secrecy laws for years. These laws enable wrongdoers to secretly control offshore corporations. Now we made a little progress on that front. More is hopefully coming. But one of the impediments that we run into in combating offshore secrecy is the point made by offshore jurisdictions that the United States, itself, promotes corporate secrecy. A report issued by Tax Justice Network earlier this week asserts that Delaware provides more corporate secrecy than Switzerland demonstrates that we have got to get our own house in order and comply with FATF's international standards on beneficial ownership if we are going to continue to make progress on offshore tax havens whose secrecy is a real problem and a real deterrent to law enforcement.

Corporations were intended to shield owners from personal liability for corporate acts, not to hide ownership. But today the corporate form is being corrupted and is serving those who use the corporate veil to hide their identities while committing crimes or dodging taxes and robbing our treasury and taxpayers of billions of dollars each year. It is past time to stop this misuse of the corporate form and if we want to end inappropriate corporate secrecy offshore, we have to stop it here at home when it comes to law enforcement and the needs of law enforcement.

So I thank you again, Mr. Chairman, for this opportunity to give an opening statement.

Chairman LIEBERMAN. Thanks very much, Senator Levin. Senator Carper, good morning.

OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. Good morning and thanks very much for holding this hearing and giving us, Senator Levin and I, an opportunity to speak as well.

I know not everyone was anxious to hold this second hearing. I am glad that we have. I am encouraged, having talked to a couple of our witnesses today, that it has actually helped provide an opportunity for us to find a path forward—I think maybe to a compromise that will actually address the concerns that Senator Levin has stated and I think all of us share about combating money laundering and tax evasion, but at the same time meets, I think, the

very legitimate concerns that Senator Ensign spoke to with respect to undue burdens that we would place on States, including our own State, and frankly all 49 other States as well.

Let me just say that as currently drafted, the bill exempts publicly-traded corporations and businesses they form. Meanwhile, the bill applies to more than 10 million small businesses in the United States, placing them at a competitive disadvantage to their larger brethren.

I just want to know, is this really the best possible way to address money laundering? Since the bill notably exempts partnerships and several other business forms, including sole proprietorships, won't criminals just find another entity under which to conduct their criminal enterprises?

I know that some of us are confused as to why we're discussing this issue in this Committee and not before the Banking Committee, which has jurisdiction over money laundering policies. The reason is that the bill permits States to redirect their Federal homeland security dollars to comply with its provisions and we need to ensure that we have very good reasons to deprive police, firefighters, and first responders with very limited Federal funds before we move forward.

Recent press articles and reports have unfairly singled out the United States, and notably my State, for its corporate laws. A report by the Tax Justice Network which is represented on our second panel today and notably funded by the Ford Foundation in Michigan, asserts that the United States and the subjurisdiction of Delaware are the most secretive jurisdictions in the world.

The report actually rates the transparency of the United States above other jurisdictions, but because the report applies a weighting factor that is based on the size of the U.S. economy, the formula results in the United States receiving the highest secrecy index in the world. Without such a weighting, the United States would be tied with 16 other jurisdictions for 15th place.

Let me be very clear that the report provides no evidence to support its assertions. In fact, Delaware State company formation laws are essentially identical to laws on the books in Michigan, Connecticut, Missouri, and many other States. Of the 12 criteria used by this report's authors to establish the secrecy's rankings, six are matters purely of Federal law or compliance and one of the criteria was based on whether the jurisdiction answered a survey which Delaware's Secretary of State asserts it never received.

Even more troubling, no other State in the United States was included in the survey. It appears even to the most casual observer that this report may have been contrived to achieve a particular result. In fact, Delaware is doing a number of things to deter criminal enterprises. It has enacted laws that provide law enforcement with better access to the information they need to prevent and solve crimes.

Let me just give a couple examples. Delaware was the first State in our Nation to adopt legislation responding to the concerns expressed by law enforcement regarding elicit practices of registered agents. Delaware now regulates commercial registered agents and has successfully removed a number of registered agents from doing business in our State.

Delaware requires every business entity to provide the name, address, and phone number of a designated communications contact person who is available to law enforcement. And Delaware responded to international criticism that U.S. company law permits companies to issue bearer shares, stock certificates whose records of ownership are not maintained by the issuing company, when we explicitly banned the practice in statute to be consistent with long-established Delaware case law.

We have heard from a number of diverse interests with respect to this bill, the National Association of Secretaries of State, the U.S. Chamber of Commerce, the National Association of Manufacturers, the National Conference of State Legislatures, and the American Bar Association. Others also have raised legitimate concerns with S. 569.

We will hear from the Treasury Department in testimony today, even the international community has been unable to comply with FATF recommendations on beneficial ownership, and therefore, unable to find a suitable way to date to address these complex issues.

We heard from the Uniformed Law Commission at the last hearing and they worked on an approach that is designed to balance all the interests, providing greater transparency, respecting State privacy and mitigating the negative impacts on the economy and on small businesses. There are a number of reasons for us to encourage more transparency and disclosure with respect to ownership of legal entities. However, I fear that S. 569 would impose undue burdens on State authorities and on legitimate businesses, especially our struggling small businesses, at a time when the U.S. financial system and our domestic economy are under severe stress.

I believe that there is a balance that can be achieved by working together. We should start by respecting the job that our governors and secretaries of State are doing in their individual States and through the Uniform Law Commission. I also appreciate the work that has been done since our last hearing by the Department of Treasury and the Department of Justice. Together, I am confident we can achieve an approach that works for all stakeholders.

And again, Mr. Chairman, I want to thank you for holding this hearing and I would just say, I want us to work hard to get this right. I think together we can find an approach that works for all of us and that is what my intent is to do.

Chairman LIEBERMAN. I appreciate that very much, Senator Carper, and I share that goal as well. I thank the two witnesses, who I introduced, on the first panel. So we will go immediately to David Cohen, Assistant Secretary of Treasury for Terrorist Financing and Financial Crime. Thanks very much for being here. Thanks for your good work and we welcome your testimony now.

TESTIMONY OF HON. DAVID S. COHEN,[1] ASSISTANT SECRETARY FOR TERRORIST FINANCING, U.S. DEPARTMENT OF THE TREASURY

Mr. COHEN. Thank you, Chairman Lieberman, distinguished Members of the Committee. Thank you for inviting me to testify today on finding a legislative solution to enhancing access to bene-

[1] The prepared statement of Mr. Cohen appears in the Appendix on page 377.

ficial ownership information, a key step in combating the abuse of legal entities by those engaged in financial crime.

I would like to begin by thanking Senator Levin for his leadership over the years on this important topic. I would also like to extend my appreciation to colleagues across the government, State and Federal, and in the private sector, with whom we have worked to understand the challenge of beneficial ownership and develop effective solutions.

At the outset, it is important to recognize a number of key considerations. First, the ability of elicit actors to form corporations in the United States without disclosing their true identify presents a serious vulnerability and there is ample evidence that criminal organizations and others who threaten our national security exploit this vulnerability.

Years of research and law enforcement investigations have conclusively demonstrated the link between the abuse of legal entities and weapons of mass destruction (WMD) proliferation, terrorist financing, sanctions evasion, tax evasion, corruption, and money laundering for virtually all forms of criminal activity. This abuse is particularly prevalent with respect to legal entities created in the United States. We know that elicit actors use the presumed legitimacy of U.S.-based entities to gain access to the international financial system and disguise the source of their funds or the purpose of their transactions.

Second, information on the true beneficial ownership of a legal entity at the time of formation, as its ownership changes over time and when it opens accounts it is critical to stopping the exploitation of legal entities. Third, the challenge of enhancing access to beneficial ownership information is complex and requires a global solution. Treasury is working domestically and internationally to address this challenge.

Fourth, we are keenly aware of the need to preserve an efficient entity formation process and not to create unnecessary impediments to accessing the financial system for legitimate businesses. And finally, we believe even incremental progress in this area to enhance access to beneficial ownership information is likely to yield substantial results.

Taking account of these key considerations, Treasury has developed a comprehensive approach to the issue of beneficial ownership that includes the following elements. We favor legislation that requires a submission of beneficial ownership information at the time of company formation, the obligation to keep that information updated, and the availability of that information upon proper request by law enforcement.

Treasury is also working with the Federal financial regulators to consider guidance and possibly new regulations for U.S. financial institutions that will clarify when and how financial institutions should identify and verify beneficial ownership while conducting customer due diligence.

Internationally, we are working with our counterparts in the Financial Action Task Force to ensure that its standards evolve in a way in which compliance is both achievable and effective. The Administration believes that S. 569 provides a good platform on which

to construct the legislative solution we favor, provided that it is amended and modified to address certain key issues.

We are fully committed to working with the Congress and our interagency partners to craft amendments that will strengthen S. 569 in the following ways. First, we believe the definition of beneficial ownership should be modified. Under S. 569, the ambiguity and breadth of the definition, coupled with burdensome disclosure requirements, makes compliance uncertain, time consuming, and costly. We believe the definition of beneficial ownership should be straightforward and simple in application to work for the full range of covered legal entities.

Second, we do not believe the bill should impose anti-money laundering (AML) obligations on company formation agents. As drafted, S. 569 would require Treasury to impose AML program requirements on a new class of financial institutions, so-called company formation agents, which raises substantial legal, policy, and practical challenges.

We believe that the bill should not attempt to regulate company formation agents under the Bank Secrecy Act, but instead should establish clear and significant Federal, criminal, and civil liability for persons who fail to provide accurate beneficial ownership information as required by law.

Third, the bill should establish robust documentation requirements. As currently drafted, S. 569 does not impose any documentation requirements for beneficial owners who are U.S. persons. In our view, S. 569 should require documentation for all beneficial owners, foreign and domestic, to be held within the State and made available upon proper demand by law enforcement.

Fourth, we believe that further study of the vulnerabilities associated with the transfer of legal entities is required. S. 569 allows for businesses to update their beneficial ownership information in an annual filing with the State. This time gap introduces a significant vulnerability for abuse upon the transfer of a legal entity and requires further study.

Fifth, we believe the bill should not draw on State homeland security grant funds to carry out the obligations imposed by the law. These funds are already relied upon by States to finance first responders in preparing for and responding to emergency situations. Treasury is committed to working in earnest and expeditiously with the Congress, our interagency partners, and other interested parties to address these concerns and develop legislation that will enhance the availability of beneficial ownership information in an effective and workable manner.

I would like to thank the Committee for inviting me to testify today and I look forward to answering your questions.

Chairman LIEBERMAN. Thanks very much, Mr. Cohen. That gets us off to a good discussion and I am sure we will have a lot of questions for you.

Next is Jennifer Shasky, who is Senior Counsel to the Deputy Attorney General at the U.S. Department of Justice. Good morning.

TESTIMONY OF OF JENNIFER SHASKY,[1] SENIOR COUNSEL TO THE DEPUTY ATTORNEY GENERAL, U.S. DEPARTMENT OF JUSTICE

Ms. SHASKY. Good morning. Thank you, Chairman Lieberman, distinguished Members of the Committee. I am honored to appear before the Homeland Security Committee to discuss S. 569, which addresses the need for greater transparency in corporate formation in the United States.

While those of us in the law enforcement community understand that the topic of corporate transparency does not readily evoke images of the criminal and extremist underworld and can often seem quite esoteric, it is important to recognize that some of the worst actors seek to exploit the lack of corporate transparency in this country to harm our national and economic security.

For example, as Senator Levin already pointed out, Viktor Bout, the infamous arms merchant and war profiteer designated by the U.S. Department of Treasury, Office of Foreign Assets Control, used U.S. shell companies to further his illegal arms trafficking activities.

The Sinaloa Cartel, one of the major Mexican drug trafficking organizations that figures prominently in our discussions of transborder security. The Sinaloa Cartel is believed by U.S. law enforcement to use U.S. shell companies to launder its drug proceeds. Semion Mogilevich was recently named to the Federal Bureau of Investigation's 10 most wanted fugitives list. Semion Mogilevich and his criminal organization are charged with using U.S. shell companies to hide their involvement in fraudulent investment activities and to launder money.

Yet each of these examples involves the relatively rare instance in which law enforcement was able to identify the perpetrator misusing U.S. shell companies. Far too often, we are unable to do so. Take for example the instance in which a foreign partner notified U.S. law enforcement after uncovering a plot to send military cargo which had been mislabeled as farm equipment to Iran.

Why contact us you might ask? Because in this instance, the seller listed in the shipping documentation was a U.S. shell company. Unfortunately, through this case and others, our foreign partners have learned that in most instances, U.S. law enforcement cannot identify the individuals who own and misuse U.S. legal entities, or in the alternative, the significant investigative delays associated with identifying the perpetrator result in criminal participants staying several steps ahead of law enforcement, the trail turning cold, or the case being terminated for statute of limitations or other delay-related reasons.

The Administration believes that S. 569 is an important step in the right direction on this issue and provides a useful platform on which to construct an effective legislative solution. We have a number of recommendations that should strengthen S. 569 and are fully committed to working with the Congress and our inter-agency partners to craft legislative texts to amend the bill in order to address our concerns.

[1] The prepared statement of Ms. Shasky appears in the Appendix on page 388.

We also recognize, however, that no legislation can provide the perfect solution to this problem. Whatever legislation we enact will have some costs to legitimate business and will have some weaknesses that criminals can exploit. Despite this fact, the Administration is committed to taking what is has learned from studying this problem and working with Congress to craft a legislative solution that has maximum effectiveness with minimum burden on legitimate business.

As noted in the department's previous testimony, the first and most critical issue facing law enforcement is the ability to identify the living, breathing, beneficial owner of a legal entity: A natural person. As currently drafted, S. 569 takes a significant step forward on this point by including a definition of beneficial ownership that would apply across all 50 States and ensure that criminals cannot exploit definitional gaps between differing State systems.

The Administration would like to work with Congress and this Committee to amend and further refine that definition to address concerns in the business community that compliance will be uncertain, time consuming, and costly. We believe the interests of law enforcement can be met while also ensuring that the definition is sufficiently straightforward and limited in application to work for the full range of covered legal entities.

Once a more limited application is achieved, the Administration recommends that S. 569 also be strengthened to require a credible and legible photocopy of government-issued identification for each beneficial owner to be held within the State. The provision and retention of such information is critical to any meaningful effort to promote transparency by assuring that law enforcement will have a name and a face for all beneficial owners. Currently S. 569 requires beneficial owners to provide their names and addresses to the State, a requirement that should remain in place. However, the bill only requires foreign beneficial owners to take the additional step of providing legible photo identification.

The Administration recommends this requirement be extended to all beneficial owners. Recognizing the challenges, both fiscal and technological, that come with this effort, we believe it would be sufficient for the photo identification to be maintained in the State and not necessarily with the State.

Another issue encountered by law enforcement is the criminal misuse of so-called shelf or aged companies, also previously addressed by Senator Levin. We often see companies transfer through several middlemen before ultimately reaching the criminal perpetrator. In such cases, the investigation often leads to a formation agent who has long ago sold the company with no record of the purchaser and no obligation to note the ownership change.

While S. 569 partially addresses this problem, the Administration recommends further study of the vulnerabilities associated with the transfer of legal entities, including identifying potential solutions for updating beneficial ownership information with every change. Additionally, the Administration recommends eliminating the expansion of anti-money laundering obligations to company formation agents, a significant administrative and regulatory burden in favor of broader civil and criminal Federal liability for non-compliance.

Specifically, we believe the Federal penalties in S. 569 should be amended to include criminal and civil liability for persons obligated to hold beneficial ownership information if they fail to meet their statutory obligations, including to maintain the confidentiality of subpoenas and other legal process, thereby eliminating the so-called tipoff problem.

Finally, while the Administration does not have an affirmative position on which funding mechanism should be used to carry out the obligations imposed by the bill, we note with concern that S. 569, as currently drafted, authorizes the use of State homeland security grant funds since these funds are already relied upon by the States to fund first responders.

I would like to conclude by expressing the gratitude of the Department of Justice for the continuing support that this Committee has demonstrated in assisting law enforcement to protect our people, businesses and institutions from those who would do us harm. I would be happy to answer any questions you have.

Chairman LIEBERMAN. Thanks very much for your testimony, Ms. Shasky. We will have 7-minute rounds of questioning.

I take it, just to clarify the point, although you said it pretty clearly, that both of you have testified that the Administration supports S. 569, but with the amendments that you both have described; is that correct?

Mr. COHEN. Mr. Chairman, I think the way we would phrase it is that with the amendments and modifications that Ms. Shasky has identified that we believe would strengthen the legislation, we would be in a position to support the bill.

Chairman LIEBERMAN. OK, that is what I thought you had said. Let me ask you briefly, Mr. Cohen, because this is obviously the Homeland Security Committee, you are assistant secretary for, among other things, terrorist financing. If you can tell us to what extent this problem of shell corporations has frustrated investigations that you have done in regard to terrorist financing?

Mr. COHEN. Yes, Mr. Chairman. It has frustrated investigations and I think Ms. Shasky's testimony and other testimony that this Committee and Senator Levin's Subcommittee have received have illustrated a number of instances where investigations have been frustrated. The difficulty, of course, is that if there is a lead on a business that may be involved in any matter of crime, including terrorist financing, that when you try to get behind that—and what we do at the Treasury Department is try to map out these networks, map out who is involved in raising the money and moving the money. If you then go and try and figure out who the actual people are who are involved and there is no access to the beneficial ownership information, that can, of course, stymie the investigation.

It is also, I should add, a problem that some of our international partners have encountered as they try to undertake similar efforts.

Chairman LIEBERMAN. In the United States or in their home countries?

Mr. COHEN. It is particularly a problem with U.S. corporations.

Chairman LIEBERMAN. Yes. But there have been specific cases where you have been pursuing, for instance, a terrorist financing

investigation and this shell corporation problem has frustrated what you have been trying to do.

Mr. COHEN. It has. I do not want to overstate the problem. I think what we see is a significant vulnerability and we have seen some exploitation of that vulnerability. But it is a problem that we have identified.

Chairman LIEBERMAN. In the testimony that you both offered, in different ways you said something really interesting to me, which is that the Administration's position is that the law enforcement community particularly can get the information that you need even if a company's beneficial ownership information, including particularly photo identification, is held by a third party in the State rather than in the State Secretary of State's office.

That is interesting and I wanted to ask you to just go into that in a little more detail. How would such a revised procedure work? In other words, who would hold the information, particularly the photographic documentation?

Mr. COHEN. I think in our conception of a modified bill, that information would be held with the State either by someone who is in the corporation if the corporation is, in fact, operating in the State, or if the corporation is not operating in the State of its incorporation, then there would be a designated person in the State who would be holding that information. That person in the instance of an out-of-state corporation or foreign corporation would need to identify himself or herself to the Secretary of State's office and certify that they have the credible and legible documentation information.

So it differs on whether the corporation is operating in the State or is operating outside the State, but in either instance, there would be a person in the State who has that information.

Chairman LIEBERMAN. And the law, if you were drafting it, would say that the individual holding the information would have an obligation to present it upon request?

Mr. COHEN. Yes, sir.

Chairman LIEBERMAN. Request of law enforcement?

Mr. COHEN. Exactly.

Chairman LIEBERMAN. Again, in your ideal version of a bill on this, what would States be required to ask on their incorporation forms and how would law enforcement access the necessary information without tipping off a subject of an investigation of a potential criminal?

Mr. COHEN. The States would be required to obtain the name and address of the beneficial owner as defined—and we can talk about the definition of beneficial ownership. The concern about tipping off is a very serious one and the legislation that we have in mind would contain a very clear prohibition on tipping off, whether it is by someone in the State Secretary of State's office or this third party who may be holding the documentation. They would be prohibited from notifying the subject of the investigation that a subpoena has been received.

There are other places in the Federal criminal code where there are similar prohibitions on tipping off and I think we would model on those provisions.

Chairman LIEBERMAN. Ms. Shasky, do you want to add anything to that?

Ms. SHASKY. No, I think he has covered it adequately, thank you.

Chairman LIEBERMAN. From what you have said, I gather that the Administration does not favor making homeland security grant funds available to the States for the purposes of this legislation. Obviously, that provision, I presume, was put in the legislation because we did not want to create an unfunded mandate on the States.

So it leaves naturally for me to ask, do you have any suggestions for how we can help the States pay for the changes in these procedures, or frankly whether we should help them pay for those changes? Ms. Shasky.

Ms. SHASKY. Sure, we definitely do not support an unfunded mandate.

Chairman LIEBERMAN. Yes.

Ms. SHASKY. We believe it is important to provide both the capacity and the incentive to States that will enable them to carry out the legislation. However, we would just note our concern, quite frankly, in using the State homeland security funds as the mechanism since they are used by first responders. The States are already relying on those funds for the first responders.

We look forward to exploring this issue further with the Committee in trying to identify, quite frankly, some appropriate sources of funding.

Chairman LIEBERMAN. So in other words, you do not support the unfunded mandate, but you do not support the use of the homeland security grant funds because you believe there are more priority claims on them, namely from first responders, correct?

Mr. COHEN. I think that is correct.

Chairman LIEBERMAN. Thanks. My time is up. Senator Ensign.

Senator ENSIGN. Thank you, Mr. Chairman. Does the Administration have a definition yet, or when can we expect a definition on beneficial ownership?

Mr. COHEN. We do not have legislative language that we are prepared to present this morning. We are working with the Justice Department and others in the Administration to craft language on beneficial ownership. I think the principle that is guiding our work in this area is as you said, Senator Ensign, that the definition ought to be clear cut. It ought to be simple and straightforward and a definition that can be easily applied by the two million or so people a year who form corporations without needing to consult an attorney, consult an expert—that the entrepreneur sitting at their kitchen table can look at this definition and figure out who the beneficial owners are and submit the form.

Senator ENSIGN. I just want to encourage you that when you are coming up with the suggestions for us that you do consult with some of those small businesses that are going to be forming, to ensure that we are not putting that kind of burden on them. These businesses will say that I have all my money invested in what I have been doing. I just cannot spend more money on accountants and lawyers to make sure that this thing is done right. And a lot of these people are just common sense, street smart people. They do not have a college degree. You have to take it down basically

to their educational level for a lot of these small businesses and make sure that we are not putting a burden on them.

Because frankly, job creation is something I think that all Americans can agree we need right now. So I just want to make sure we are not placing undue burdens on these businesses and I look forward to seeing that definition when you get it.

If law enforcement came in and said that they want this information, who is tasked with verifying that person is who they said they are? Is it law enforcement? Is it the Secretary of State's office? Because I think that this is one of the concerns that the Nevada Secretary of State relayed to us. Who is going to be in charge of verifying? Because that would be additional costs from the one's I mentioned earlier.

Ms. SHASKY. In our conception, Senator, it would be law enforcement that would hold that responsibility.

Senator ENSIGN. So you would just get the information from the Secretary of State's office and then it would be up to you to determine whether that was right or not?

Ms. SHASKY. That is right. We are merely asking the State to collect the information, not to verify it.

Senator ENSIGN. I see. Have you all done cost studies at all, like what Secretary of State has submitted to us? [1] Because there is one thing to say that this thing is not an unfunded mandate, but as we have seen a lot of times, it turns out to be a lot more expensive than what the estimate are.

Have you done extensive studies on how much it is going to cost each State? Because, for instance, Delaware and Nevada, we incorporate a lot more companies than other States do. How would you divvy up the money, which is always a problem up here?

Mr. COHEN. I do not believe that we have conducted any detail analysis on the cost of implementation. I think what Ms. Shasky was testifying to on the question of unfunded mandate is not that we think this is a costless endeavor, but quite the contrary. We recognize that there are costs associated with the implementation of this legislation if it were to be enacted and we are committed to working with the Congress to find a way to resolve that issue for the States, not that we think that this is something that is free.

Senator ENSIGN. Any comments, Ms. Shasky?

Ms. SHASKY. I agree wholeheartedly with my colleague from the Treasury Department. Again, we are committed to working with Congress to identify appropriate funding mechanisms.

Senator ENSIGN. Just to summarize, these are my major concerns. One is that we do not hurt small business. Two is that we do not have an unfunded mandate to the States, which we do a lot up here, especially in the past. We do less of it now, but we still do some up here. There are promises.

And then third is the fairness of the distribution of the funds. Sometimes we will do a formula and we have to make sure that it is not just done on population, but it is actually done on the need for that State based on the numbers. Some of our States have tried to enact laws that were friendly and made it easier to get into busi-

[1] The prepared statement of Nevada Secretary of State Ross Miller submitted by Senator Ensign appears in the Appendix on page 435.

ness. My State is one of those. We think that we have done a pretty good job of balancing that.

I do think that law enforcement has legitimate concerns; there is no question about that. But we have to be very careful that the law of unintended consequences does not make things so burdensome in the future that when we correct one problem that we are making other problems much more severe.

Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator Ensign. As is our custom in this Committee, we call Members in order of their arrival and for the information of my colleagues, that will be Senators Levin, Bennett, Carper, McCaskill, Burris.

Senator Levin.

Senator LEVIN. Thank you, Mr. Chairman. I thank both of our witnesses. Their testimony is very helpful, very supportive.

I look forward to the definition on beneficial owners. We use the Treasury definition in our bill. We thought the Treasury would love that. It turns out Treasury does not particularly like its own definition and if you can simplify it, great. I think there could be some improvements in your definition, frankly. Make it clear that we are not going after single stockholders and those kind of straw man issues which have been raised by opponents. So we do look forward to your giving us the legislative language for whatever improvements and strengthening that you think is appropriate.

One of the issues here in terms of beneficial owners however is that as Ms. Shasky pointed out, I think very powerfully, what we need are the living, breathing, natural persons. We are not looking for some shell corporation to be called the owner. Would you agree with that?

Mr. COHEN. Yes, Senator.

Senator LEVIN. Now the National Conference of Commissioners on Uniform State Law (NCCUSL), in their proposal just requires a records contact and that records contact could simply be an owner of record, which could be a shell corporation, putting us right back into a circle which leads absolutely nowhere in terms of finding the beneficial owners.

Would you agree that the approach of NCCUSL in this regard is not acceptable, Ms. Shasky, first of all?

Ms. SHASKY. Yes, Senator. To allow companies to provide anything less than the beneficial owner information merely provides criminals with an opportunity to evade responsibility and put nominees between themselves and the true perpetrator.

Senator LEVIN. Do you agree with that?

Mr. COHEN. I do, Senator.

Senator LEVIN. The letter which we received, I should say Senator Dodd received an undated letter, but it came after the September 22 letter, because the Secretary of the Treasury refers to the Dodd letter of September 22.[1] But that letter, which is a very helpful letter, in one place suggests that the legislative proposal would be built upon the NCCUSL approach. And I take it from conversations both with Secretary of the Treasury Timothy Geithner

[1] The undated letter to Senator Dodd submitted for the Record by Senator Lieberman appears in the Appendix on page 433.

and from what you have said here today that is not accurate, that it would not be built on that proposal. Can you clarify that?

Mr. COHEN. Certainly, Senator. I think what Secretary Geithner was driving at in the letter is that the NCCUSL proposal has some ideas in it that we think are useful and worthy of developing, not that the Department of Treasury supported the NCCUSL legislation.

I think the idea is that we will draw from the NCCUSL legislation. We will draw from other ideas that are out there, use that to inform our steps forward in terms of building on the platform of S. 569.

Senator LEVIN. That their approach to the definition of beneficial ownership is not one of them.

Mr. COHEN. I think that is right. There are other aspects of that bill that have some useful ideas, but not that.

Senator LEVIN. You have also indicated, I believe, this morning, Mr. Cohen, that the documentation information, such as passports and photos, which you believe should be provided even for domestic corporations, which we do not require for domestic corporations in our bill, we made a big effort to keep this simple and not to have a big burden, and that was one of the ways in which we avoided a burden, by saying foreign corporations, of course, you've got to provide photo identification, passport, whatever, but not for domestic corporations.

That was a compromise we made to try to accommodate the very concerns that had been raised about avoiding complexity. But when you testified earlier, because you support that documentation being provided for domestic corporations as well as foreign corporations, you indicated, I think, that your intent was that documentation information could be or should be kept in the hands of a third party in the State rather than kept by the State.

But I also understand that your intent, and correct me if I am wrong, is that the actual information, the basic name of who the beneficial owner is, would be provided with the incorporation form and updated to the State itself and then that would be available from the State to law enforcement; is that correct?

Mr. COHEN. I think you have it exactly right.

Senator LEVIN. OK, because I think there was a little confusion on that point, which I wanted to clarify. If false information is provided on the form, would it be fair to say that even that information might be helpful? We do not require verification, again to avoid the very expense and complication which some of the opponents representing States that do a lot of incorporation have pointed out they want to avoid.

So one of the ways we avoid it is to not require the State to verify the name of the beneficial owner. However, even false information, is it not accurate to say, would be helpful because it could help to prove the intent element that is a part of many crimes that somebody intentionally lied; is that fair, Ms. Shasky, first?

Ms. SHASKY. That is exactly right, Senator, and it is within the jurisdiction of the United States at that point.

Senator LEVIN. And Mr. Cohen?

Mr. COHEN. I agree with that, Senator.

Senator LEVIN. In terms of the mandate issue, we want to avoid a mandate as well, so we provide a possible source of funds, but we do not require that the source be used and we are more than happy to have you folks provide additional sources. We look forward to it being in the Department of Justice budget perhaps or the Treasury budget. But one way or another, we are very happy to do that.

But I would point out that the law enforcement community, very much supports this bill and wants to avoid an unfunded mandate as well so we do not sink the bill with that issue, those first responders, those law enforcement community folks favor this bill and I believe will point out that it will help them much more to be able to find the criminals than they would be losing by a fairly minor loss of any funds that go to the Department of Homeland Security.

So I think we will find out later this morning that the law enforcement community does favor this approach as a possible source, not a required source. But in any event, we would welcome also your suggestions as to alternative sources for what I think will be fairly nominal funds, but important expenditures to go after criminals and so forth.

Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator Levin. Senator Bennett.

OPENING STATEMENT OF SENATOR BENNETT

Senator BENNETT. Thank you, Mr. Chairman. I have never had anything to do with law enforcement, but I have run a small business, a number of businesses, so I come at this with a different kind of aspect. I do not want to get in the way of law enforcement under any circumstances, but I do not understand it, having not any personal experience.

I do see the potential of getting in the way of small business, indeed medium business or even large business. If I may without being offensive, suggest that some people in law enforcement do not understand business any better than I understand law enforcement. And since it is business that is going to be affected by this, we have to be very careful how we do it.

Let me give you some concerns. First question, who is going to have access to this information? Competitors? If I am a competitor and I want to know who the beneficial owner is of my competition, can I go to the State and ask for it and get the information? Or is it exclusively available to law enforcement?

Ms. SHASKY. Senator, we are recommending that it be exclusively available to law enforcement upon the appropriate issuance of process.

Senator BENNETT. So the information sits there, but nobody can get at it until somebody shows up with a subpoena?

Ms. SHASKY. That is correct, Senator.

Senator BENNETT. All right, that lowers my temperature a little bit. [Laughter.]

Many times, not overwhelmingly——

Senator ENSIGN. If the Senator would yield? The one point to make about that is, though, the Secretaries of State will have to

have separate databases for that because right now they have one that is public and they will have to have one that is completely private, which is a big part of their expense is going to be raised.

Senator LEVIN. Yes. Perhaps just on that point, we could ask Secretaries of State whether or not it is not true that already they keep certain information private in a separate database. If I could also, my next time, just to clarify one other point, we do allow in our bill the States, if they want to, could make information available, but we prohibit it in the bill.

Senator BENNETT. You prohibit it, but you make it possible?

Senator LEVIN. Only if the State——

Senator BENNETT. Help me understand that.

Senator LEVIN. We prohibit it. We say only if a State decides that they want to make it available for whatever reason.

Chairman LIEBERMAN. You might call it a State opt-out. [Laughter.]

Senator LEVIN. We are trying to protect the rights of the States here. We are trying not to trample on the rights of the States. People say do not impose these requirements on the States, so all we are saying is just collect the name. It is only available to law enforcement, but we are not going to stop a State from making it available to someone else.

Senator BENNETT. But you force the State to collect it in the first place.

Senator LEVIN. We do.

Senator BENNETT. That is the circumstance that gives me concern. If I form a company, and I think it is going to be marvelously successful over time, and I give shares to my grandchildren, does the State have to have pictures, baby pictures, of my grandchildren and as the grandchildren grow up, are those pictures now false because they do not look anything like the teenagers or whatever?

This whole thing sounds wonderful, but in the reality of the way these small companies are often operated, is there a liability that somebody is going to be sued because the picture does not match what is in the file?

Ms. SHASKY. Senator, we would not recommend a private right of action based on this bill and would instead support very limited and focused, targeted civil and criminal Federal penalties in appropriate circumstances.

Senator BENNETT. Well, again, details come down to what Senator Ensign was talking about. These are definitions. We want to know who the beneficial owner is by definition and my grandchild becomes a beneficial owner by definition, is there a liability if at some point the company gets sold to this company, but there is still a stock certificate somewhere and the Federal Bureau of Investigation (FBI) shows up looking for my grandchildren as being involved in a criminal activity?

You do not need to comment on that because you say it is probably not going to happen, but is one of the things I raise that people get concerned about.

Now let me get to the one that I am most concerned about. A major source of job creation in this country, unique to this country that no other country understands, is the venture capital (VC) world. People in the venture capital world have a variety of ave-

nues through which they can place their money to try to participate in the explosion of technology.

I am not sure I would do this, but there are some VCs that say, we see X number of companies in this particular arena, we are going to invest in every one of them on the assumption that one of them will hit it and we do not know at this point which one it is. All right, somebody invests in that VC not knowing how the VC is going to make the bet among these 10 startups.

One of the startups gets taken over by Mr. Bout. The fellow who invested in the VC is listed as a beneficial owner in that particular enterprise. He finds out that he has that kind of exposure and he says, I am not going to put in any money, I am not going to run that risk.

Help me understand why he should not be concerned.

Mr. COHEN. Senator, I think the answer to that question turns on how the term "beneficial ownership" will be defined in the legislation. I think our ideas, I tried to explain previously, is that it be a simple straightforward definition, and as well, a definition that does not require small holders of an interest in a corporation to be identified. But I think we are looking to set a threshold of ownership at a sufficiently high level that the beneficial owners, the need to be identified to the State, are those who have really a truly significant interest in the corporation.

So I think in your hypothetical I am not sure that the person who invests in the VC firm, which then invests in a corporation in the first instance, would be identified as a beneficial owner and——

Senator BENNETT. Well now, if we go where Senator Levin was going, who is the beneficial owner, the real live breathing person? It is the ABC Venture Capital Company. We have to get behind that veil and find out who owns the company. We go behind the veil and we find several investors, one of which is Senator Ensign's family foundation. Who are the beneficial owners of his family foundation?

Now we get to his kids and his kids are tainted with an investigation that says somehow they are involved. These definitions have to be very important and I just echo what Senator Ensign has had to say about as you are putting them together, do not just talk to law enforcement. Do not talk to me from the law enforcement side because I do not know anything about that from personal experience.

But do not just talk to law enforcement. Talk to people in the business world and have them walk you through scenarios like the ones I have raised because they are going to come up with a whole lot more than I have come up with that are going to say, there will be unintended consequences of enormous complexity down the road from here that will end up causing people to say, I will not invest in this venture capital company or that venture capital company will not invest in these kinds of startups because we are afraid.

The average law enforcement person says, you do not need to be afraid. As long as you do not do anything illegal, we are not coming after you. Yes, well let me tell you how zealous the attorney general in my State is to embarrass me, and I will not go any farther with that one, but I think you all know who I am talking about.

Pay attention to the people who are going to be making this thing work in their real lives.

Chairman LIEBERMAN. Thanks, Senator Bennett. You know, in terms of the practical implications that you are focused on, you mention a picture of your grandchildren. Just for the record, would you indicate how many grandchildren you have been blessed with?

Senator BENNETT. Twenty, Mr. Chairman, and I am a far second with Senator Bunning.

Chairman LIEBERMAN. But a strong second, I would say. Senator Carper.

Senator CARPER. You just asked. My first question would be of Senator Bennett. Senator Bennett, would that be 20 and counting?

Senator BENNETT. I believe we have shut down production at this point. [Laughter.]

But you never can tell.

Senator CARPER. I once asked Senator Bunning, how many grandchildren does he have? It was 30-something, maybe 39. I once asked him, how do you remember all their names? And he said, we use nametags. Whatever works.

A question, if I could, for both of our witnesses. Again, thank you very much for being here and for your input today. I just want to clarify the Uniform Law Commission approach.

My understanding of the Uniform Law Commission model law is that the records contact and the responsible individual must be a real live person. I think in Section 2 it says that the records contact and responsible person must be a live person, not another entity. I just wonder, is there some confusion about the language in the Uniform Law Commission approach?

Mr. COHEN. Senator, I do not think there is any confusion in what the Uniform Law Commission has done with respect to the records contact and responsible individual. They do require a live person. I think one of the concerns that we had with the legislation is that, I think, there is not an obligation for that live person to not be a nominee. And what I think is important in the legislation is that we get at the true beneficial owner and not someone who may be a nominee.

Senator CARPER. I am tempted to say that maybe we could tweak it a little bit and say really live person as opposed to real live person, but I think you get my point. We believe the language is actually pretty straightforward. We are talking about a real live person.

Secretary Cohen, if I could follow up with you. Would it be difficult for law enforcement to identify the corporation formation agents in Delaware?

Mr. CARPER. Senator, I think that law enforcement would have some difficulty in identifying all the corporation formation agents in Delaware. I think as was previously indicated, Delaware has required the registered agents to be known to the State and to have a place of business in the State, but I think that is distinct from the corporate formation agents.

And one of the concerns that we have with the bill as currently drafted is that if the Treasury Department were required to regulate company formation agents, we would have some difficulty in identifying all of the corporate formation agents in Delaware and around the country.

Senator CARPER. As I said earlier, and I will say it again, I think Delaware might have been the first State in our country to adopt legislation responding to concerns expressed by law enforcement regarding illicit practices of registered agents and we now regulate our commercial registered agents. We are not the only State that does that. I think Nevada does that now and I believe Wyoming does it as well.

Assistant Secretary Cohen, a lot of attention has been paid to the Treasury Department's definition of beneficial owner. I think you alluded to this in your comments, but as it is defined in the Treasury Department's anti-money laundering regulations.

Was this definition as drafted intended to apply to corporations? Wasn't the definition really meant to apply to bank accounts, not to corporations? And why are these terms not interchangeable?

Mr. COHEN. I think that's exactly right, Senator. The definition that is currently in the legislation is taken from a regulation that is designed to implement the requirements that when a foreign person is seeking to open a private banking account that the beneficial owner of that private bank account be identified.

In that context, you have presumably a sophisticated person who is opening a private banking account that legislation requires that there is a $1 million minimum in that bank account. So you presumably have a sophisticated person dealing with a private banker and discussing who may be the beneficial owner of that bank account.

The context that we are considering today, of course, is beneficial ownership of a corporation, which is obviously a different question than beneficial owner of a bank account and also one in which, as I indicated previously, we want to facilitate the entrepreneur who may not be the sophisticated foreign person opening a private bank account to be able to understand readily and easily who the beneficial owners are.

So that is why although we like our definition very much, for the foreign private banking account context, we do not think that it can be transferred into this context.

Senator CARPER. And I would agree. A follow-up, if I could. The Treasury Department, as head of the U.S. delegation to the Financial Action Task Force, plays a key role in developing guidelines that govern anti-money laundering efforts within the United States and I think leads the U.S. enforcement internationally through FATF.

Deep concern was expressed at our last hearing, as you may recall, that the United States is not in compliance with the Financial Action Task Force Recommendation 33, which requires countries to obtain beneficial ownership information for the corporations formed under their laws.

What countries are in compliance with FATF Recommendation 33?

Mr. COHEN. Senator, there are a few countries who have been assessed by FATF to be in compliance with Recommendation 33, although the vast——

Senator CARPER. Like 10 or 20?

Mr. COHEN. Something in that neighborhood. The vast majority of countries, both FATF members and non-FATF members, have been found not to be in compliance.

Senator CARPER. Why are more countries not in compliance?

Mr. COHEN. Well they are not in compliance frankly because this is a very difficult recommendation to comply with in the FATF recommendations to obtain beneficial ownership information and there has been efforts in a number of countries and in the European Union to come up with a mechanism to obtain beneficial ownership information at the time of company formation. Frankly, they have not solved this problem effectively.

I think the one jurisdiction that seems to have done this well is Jersey, not New Jersey, but the Island of Jersey, which is obviously——

Senator CARPER. I was going to say, I find that hard to believe. [Laughter.]

But, I will not say that.

Mr. COHEN. But their economy and their business formation business is far different from what a major economy like the United States confronts. And so I think the reality is that most countries have not been in compliance and no country that is even remotely on par with the United States in terms of its economy has been able to solve this problem effectively.

Senator CARPER. Thank you for your responses. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks you, Senator Carper. Senator McCaskill.

OPENING STATEMENT OF SENATOR MCCASKILL

Senator MCCASKILL. Thank you, Mr. Chairman. I completely understand why this legislation is important and why we need to get it passed. Because of my experience in law enforcement and understanding that having a thread to pull is sometimes the difference between success and failure in a huge investigation where if you can't find any threads to pull then you hit that wall. There is no feeling of helplessness that is more acute than when you know there is really bad stuff out there and you cannot find the thread to pull.

I know this legislation, if we do it right, will provide lots of threads for you all to pull. The problem is we have to be careful that the benefits outweigh the cost of compliance, both directly to businesses and indirectly to our economy. And that is the tricky part and that is why this definition is so important and why I think you are really going to have to focus with maybe a broader view than you typically would have.

Because of what you do, you focus laser-like on how you continue the path of investigation to get the evidence you need to bring someone to justice and sometimes—I mean, there is a hyper focus that leaves out some of the things that Senator Bennett and Senator Ensign have talked about. I do think it is important though, when we talk about this definition, that we are talking about someone who is exercising control. I mean, what we are trying to get here is not who benefits from the corporation in terms of its success, but rather who is it that is in control.

While there are many venture capitalist firms that invest in corporations, they generally are not exercising control. Do either one of you have a comment on that in terms of that exercising control that we are trying to get to in this quest for the right definition?

Ms. SHASKY. Senator, I think you are exactly right. That is, at the end of the day, what we are concerned with, finding the natural person or persons who are in control of that company. I provided some examples of instances where we were able to identify the worst actors out there who used U.S. shell companies. But really what happens most of the time is we have a victim who comes to us and reports a very difficult crime. We are very sympathetic, obviously, to the victimization, but the victim does not know who it was that perpetrated the crime and nor do we.

It is these U.S. shell companies that are used as the shield between law enforcement and the victim on one side, and on the other side of the shield the criminal perpetrator. If we cannot get behind that shield and identify who is ultimately exercising control over that company, we are not going to solve those crimes because we are unable to solve those crimes.

Senator MCCASKILL. I think it is important for the record, I understand—I do not think that anyone has asked this directly yet—I could give an answer here, but I think it is more important for you all to give an answer. What is the argument when someone says well, someone who is a criminal is not going to really put down the right name? They are going to make up a name. How do you address that concern that people have that we may be putting a burden on legitimate businesses while the bad guys are merely going to give fictitious information?

Ms. SHASKY. There are two answers to that. There are two results that come from having effective legislation in this area. We do have a thread on which to pull, as you mentioned earlier, and the trail does not go cold. So we have an avenue to go down. Or in the alternative, the criminal chooses not to use U.S. companies to perpetrate his crimes. We have successfully hardened ourselves as a target of criminal perpetrators.

U.S. shell companies are particularly advantageous to criminals because they come with an air of legitimacy. Using a shell company from a small offshore haven, that highlights for law enforcement that there may be a problem and that we need to look there. The United States, as everyone has mentioned, is mostly engaged in legitimate commerce, and therefore, it is very easy for criminals to hide their activities, their criminal activities in the stream of our legitimate commerce. If we harden the target, they will no longer be able to do so.

Senator MCCASKILL. I know you said, Ms. Shasky, that you guys do not keep statistics on the use of shell corporations, but can you talk about it as a trend? Are you confident that this is a growing trend? Are you confident that this is something that is much worse today than it was a decade ago?

Ms. SHASKY. There is no question, Senator, and perhaps the best kind of anecdotal evidence of that is witnessed by myself and my colleagues every day as we train on this topic. We actually train law enforcement and prosecutors, both domestically and abroad, about the problem of U.S. shell companies, how you might inves-

tigate a case that involves this complex problem, what steps you can try to take. But we typically ask your question.

And about a year ago, in fact, we had an audience of about 75 investigators from nine different Federal agencies, as well as Federal prosecutors from around the country, and we asked them just by a show of hands to tell us how many of them have had cases halted because they came to a U.S. shell company and the trail turned cold. They were no longer able to proceed.

And sitting in that audience, it sure seemed to me that every hand in the audience was raised. And, if it was not every hand, it was nearly every hand. This is not a singular experience. This happens time and again. Every time we go overseas to talk to our foreign colleagues, lecture on money laundering, and how to investigate it; after every one of those classes, we have some member of law enforcement approach us to discuss the problem of U.S. shell companies. They ask whether we can do anything to fix it. So it is extensive.

Senator MCCASKILL. I heard both of you say that you are opposed to the method of funding that this bill embraces. I understand that is the company line at this point and I get that. I really would, though, urge you all to whatever extent you can, run it up the chain.

You know, I audited the use of these homeland security monies in my State and it was not good how a lot of this money was used. Suits sitting around in boxes that had never been opened, units in rural areas that had never really been formed, but they were getting money for stuff that probably in the long run is not a high-risk area.

You all know that terrorists cannot succeed unless they move money. If shell corporations are being used to help terrorists move money, then it seems to me that this would be a great use of homeland security monies to the States because money is the weapon of choice as it relates to terrorists activities because we are not talking about putting together armies.

We are not talking about buying weapon systems. We are talking about moving money around the world in ways that are going to kill people. I hope you guys reconsider the position you are taking on the use of these homeland security monies. I think it would be important and I think we have to work on these definitions so we do not have unintended consequences.

But I think this legislation is really important to national security, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator McCaskill. Senator Burris.

OPENING STATEMENT OF SENATOR BURRIS

Senator BURRIS. Thank you, Mr. Chairman, and to our two witnesses. This has been a very interesting hearing, and I am wearing several hats here. I am a former law enforcement person. I am also a former private business owner. I find this very interesting in terms of how we are going to deal with this.

I am looking at several situations in terms of incorporation. I am talking primarily about the State of Illinois now. You can get the S Corp. You can do the C Corp. You can do the LLC. And those

are all registered with the Secretary of State. By the way, I am also a lawyer who did all these incorporations and I am going to deal with the other point in a few seconds here.

Now if someone were to form a general partnership, you all have no access to any type of State records; is that correct?

Mr. COHEN. That is correct, Senator.

Senator BURRIS. I just want to make sure I get the legal basis clear. Because you are talking about documents that are just filed with some entity; is that correct?

Mr. COHEN. [Nodding affirmatively.]

Senator BURRIS. Now having served as a registered agent for several corporations and companies, and in your legislation you talk about the live person that Senator Carper was mentioning, I just wondered why all of that repository of information cannot be placed—I am sure you have all thought about this; I just maybe have not run across your notes—with that registered agent or require every entity to have a registered agent that the documents would be with, pictures, and any change in the corporation would have to be on that registered agent?

That would be a source that law enforcement could go to and there would be penalties for that registered agent for not keeping up with the changes in the corporate structure. For example, Illinois just caught up with this notary requirement. We can notarize stuff. Your law partner would bring it in and you would notarize it. There turned out to be a lot of problems with that, because my church got involved with all these notary frauds with the transfer of real estate and using defunct corporations, corporations that failed to file their annual reports to find out who is now defunct and then reincorporate the corporations and then take over.

As a matter of fact, he took over our church, owned our church and sold off some of our empty land. We were able to get it back because they had a smart lawyer called Roland Burris, but anyway. [Laughter.]

I am just wondering whether or not the registered agent extension would be a solution to the problem that would cause whoever the players are in the corporate structure, that is who you go to if you—I served on a regulated investment company board and we created LLCs—LLCs to own LLCs, to own LLCs. Each one of those LLCs has to have a registered agent.

Any entity that is filed should have an identifying person who then the Secretary of State could send law enforcement to and with a picture or whatever that registered agent would need to have on file, and if that registered agent is not keeping track of the corporate structure, then there would be certain liabilities on him. Is that within your thoughts?

Mr. COHEN. Senator, we have been thinking about different methodologies for how the documentation should be held. I think our current approach is for corporations that are operating within the State, that it is sufficient for that corporation to have the documentation available to law enforcement. If the corporation is not operating in the State, then someone in the State needs to have that documentation.

It could certainly be the registered agent who could serve the dual purpose of being the registered agent for service of process

and other reasons, as well as the person that the corporation has designated to hold the documentation.

Senator BURRIS. Would we have to change State laws to some extent in this regard or would Federal laws be able to strongly suggest ways that they have gotten around the 10th Amendment for States to take certain actions?

Mr. COHEN. I think there is a variety of ways to accomplish this and undoubtedly they will be required to have some changes in——

Senator BURRIS. Even if you had a corporation that was incorporated in Illinois, it still has to have a registered agent and you still look to the registered agent of that corporation, have the responsibility on that entity that is called the agent of that company and that agent should know every player, have a picture of every player, have a document of every change in that entity and therefore you have your strings, as Senator McCaskill was saying, to really pull on.

Mr. COHEN. Senator, I think that is one possible approach. I think we are in the process of discussing with each other, and as many of your colleagues have suggested, reaching out to the business community to formulate of the best approach to these various questions. No, I think your suggestion is a useful one.

Senator BURRIS. Having been a registered agent, having formed corporations—I mean that is what I did in my legal practice normally. And I even served as the registered agent for several companies. The responsibility has been on me to file those annual reports and get in touch with the principals and keep them advised. And even if you are a Delaware corporation, you still are going to have to have a registered agent in Senator Carper's State, wherever you are, whether Nevada or wherever.

The other thing I do not want to see—I am not going to agree with any unfunded mandates here. Let's not put anymore burdens on these State governments, because I have been trying now, Mr. Chairman, to get my bill out of this Committee that deals with giving assistance to those State governments for their transparency on that stimulus money.

Our State comptrollers, our State auditors—S. 1064 has not moved out of this Committee and those State governments are suffering right now with having to do all this accountability on this stimulus money that is coming in, but they have no money themselves and we are holding up a piece of legislation here now that is an unfunded mandate on State governments. They are now trying to keep up with what the transparency accountability is supposed to be in those States with all those billions of dollars coming in and they have no other resources to do it.

So I am hoping, Mr. Chairman, that S. 1064 can get the hold off of it and we can get it out of the Committee, because this is what we are going to do if we pass this legislation; you are going to have something that the States are going to have to do. There is not going to be any money and we are then going to find ourselves with the States struggling and suffering again and having to tell them they have to raise taxes.

So I am not going to be that supportive of any legislation that is going to be without some funds going into those States to carry

on this activity, even though with my law enforcement hat on, I think it is a good idea.

Chairman LIEBERMAN. Thanks, Senator Burris. As you know, I support that legislation. Unfortunately, there have been holds on it.

Senator BURRIS. Yes, and Mr. Chairman, it is now your bill.

Chairman LIEBERMAN. We should reason together——

Senator BURRIS. You and the Ranking Member took over my bill with the—— [Laughter.]

Chairman LIEBERMAN. It wasn't an unfriendly takeover.

Senator BURRIS. It was a great takeover. I loved it because that gave it impetus and I just knew it was going to sail right through. I am wondering what happened.

Chairman LIEBERMAN. We will see, I hope. Mr. Cohen and Ms. Shasky, I thank you very much. I am afraid we have to go on to the second panel because there is a vote called in about 45 minutes and I want to give the four witnesses time to testify and Members time to question them.

I am sure there will be questions that will be submitted to you for the record and I appreciate your testimony. It has been very thoughtful and very forthcoming. I look forward to working with you. Thank you very much.

We will call the second panel now, David Kellogg, Kevin Shepherd, Jack Blum, and John Ramsey. Thank you all very much for being here. Thanks for your patience in sitting through the first panel. I thought it was an interesting, helpful panel and I hope you did too.

This is a group of witnesses from outside the government who have practical experience and have different points of view that will be helpful to the Committee in reaching judgment on this legislation. We have reduced the time to 5 minutes. If you go over a little bit, we are not going to forcibly evict you, I assure you.

The first witness is David Kellogg, President and Chief Executive Officer of Solers, a privately-held company that provides technology services to the U.S. Government, has more than 120 employee-owners—interesting—and involves multiple legal entities.

Mr. Kellogg, we welcome you and invite your testimony now.

TESTIMONY OF DAVID H. KELLOGG,[1] PRESIDENT AND CHIEF EXECUTIVE OFFICER, SOLERS, INC.

Mr. KELLOGG. Thank you, Chairman Lieberman, and distinguished Members of the Committee on Homeland Security and Governmental Affairs, for the opportunity to testify today on the impact on business of S. 569, Incorporation Transparency and Law Enforcement Assistance Act.

Solers believes strong corporate governance and capital formation are a vital part of any vibrant economy. We also agree with the priority of combating terrorism and money laundering. However, I must express my serious concerns with S. 569 because it does not appear to combat money laundering and places additional burdens on American businesses during the worst economic downturn in 75 years.

[1] The prepared statement of Mr. Kellogg appears in the Appendix on page 395.

Founded in 1999, the Solers employee-owners are proud to be part of the effort to make our Nation safer through our primary lines of business, net-centric systems, and mission support services. We have a strong working relationship with the Department of Defense and the intelligence community and our mission at Solers is to find practical and innovative solutions to meet the challenges they face in fulfilling their vital missions.

To achieve these critical missions, Solers relies on our principal asset, our talented staff, which is comprised primarily of engineers and scientists. An important component to attracting and retaining our team is that our employees have the opportunity to own a piece of Solers as shareholders. As a result, Solers is privately-held by its employees, former employees and directors, and is a Virginia C Corporation with about 140 stockholders.

The majority of Solers' staff are owners and we found that they greatly value this benefit. With our employees owning stock in the company, they satisfy the broad definition of beneficial owners under S. 569. Upon review of S. 569, I was struck by several issues that I believe would both impede the effectiveness of the legislation such that it would not be an effective deterrent to illegal activity and at the same time, penalize legitimate law-abiding businesses and their workers.

First, I would like to speak to the difficulty of determining beneficial ownership under S. 569. The bill lacks a clear cut definition of beneficial owner that can be understood and applied by lawyers, let alone by the common business person like myself. For example, as the bill is now written, a beneficial owner could include any number of individuals, including a shareholder, family member of a shareholder, individual who has power of attorney for a shareholder, an accountant employed or retained by the business, a lien holder, a bondholder of the company, a credit card company or financial institution extending credit to the business, and any other individual who may have a legal interest in or entitlement to the company or its assets.

Further, any change in the relationship between any of these entities and the business would require new documents to be compiled and filed with the appropriate legal authorities. With such an overly broad definition, the company would be required to track and file information that is beyond its control. The vagueness and lack of precision in a standard that requires an assessment of when as a practical matter a person exercises control is particularly troubling in a law that carries criminal penalties.

Unquestionably, preventing money laundering, tax evasion and other illegal activities are laudable goals, but S. 569's indiscernible requirement to disclose beneficial owners based on an uncommon and vague definition used in this bill fails to advance these goals.

Criminals will simply ignore S. 569's requirements and legitimate companies will be unable to understand or comply with them. Second, I would like to speak to the privacy rights of investors, business owners and in Solers' case, our employee-owners. S. 569 requires States to amend their incorporation law practices to comply with new federally-mandated standards. This includes providing and documenting the detailed personal information, including home addresses of all beneficial owners.

According to the National Association of Secretaries of State, at least 38 States require compliance with their own internal right-to-know laws and other regulations. Once States collect this data, it is immediately made public. Consequently, this private information is now in the public domain.

I fear that the beneficial owner list of Solers' employee-owners will be used by headhunters and competitors to recruit Solers' staff. Like any other professional services firm, Solers' staff is its most valuable asset and providing a list to professional recruiters and competitors puts Solers at a distinct disadvantage relative to the numerous public companies that have no such requirement.

We urge you to consider a privacy provision for the beneficial ownership information to prevent its use by competitors, recruiters, other parties or activist groups who would use it for their own purposes.

Third, operating in a competitive environment, businesses make decisions and seek to conceal them from their competitors. It is a well-established and legitimate business practice to protect trade secrets. These companies are not interested in breaking the law. They are interested in being a competitive, effective force in their industry.

By passing S. 569, small companies will be placed at a competitive disadvantage in relation to the large public companies, partnerships, sole proprietorships, and even foreign competitors. Venture capital firms invest in new products and small companies. They form a vital cog in the formation of capital for small business. However, this financial backing is typically undisclosed so as to prevent market signaling.

Under S. 569, these financing vehicles will now have to be publicly disclosed, potentially cutting off start-up financing for small businesses that account for 80 percent of the job growth in the United States.

Fourth, S. 569 could also create other unintended consequences, including new and onerous recordkeeping requirements on States. While estimates vary by State, the National Association of Secretaries of State estimate the cost of implementing S. 569 in California could be as high as $17.5 million.

Finally, it is unclear how S. 569, by targeting only private and limited liability corporations, would stem money laundering or terrorist financing. Criminals will not hesitate to exploit the large loopholes and simply form business entities not covered by S. 569, leaving legitimate businesses with an unreasonable burden and criminal penalties for non-compliance. In that regard, S. 569 punishes the whole class because of one student's bad behavior.

I appreciate the opportunity to speak to you regarding this important issue. Again, while we share the goals of protecting the country, we do have disagreement with the methods being employed. I seek to make sure that this legislation actually accomplishes the goal without hurting legitimate business in the process.

Thank you and I look forward to your questions.

Chairman LIEBERMAN. Thanks, Mr. Kellogg. Am I right that you are a Virginia business, Virginia-based?

Mr. KELLOGG. Yes, we are a Virginia corporation.

Chairman LIEBERMAN. Right. Thank you. Next we are going to hear from Kevin Shepherd on behalf of the American Bar Association (ABA) Task Force on Gatekeeper Regulation and the Profession. If I am correct, you are a lawyer who is with the Venable law firm?

Mr. SHEPHERD. Yes, sir.

Chairman LIEBERMAN. Thank you for being here.

Mr. SHEPHERD. Thank you.

Chairman LIEBERMAN. Please proceed.

TESTIMONY OF KEVIN L. SHEPHERD,[1] MEMBER, TASK FORCE ON GATEKEEPER REGULATION AND THE PROFESSION, AMERICAN BAR ASSOCIATION

Mr. SHEPHERD. Good morning, Mr. Chairman and distinguished Members of the Committee. My name is Kevin L. Shepherd. I am a member of the ABA Task Force on Gatekeeper Regulation and the Profession. I am also a former chair of the ABA Real Property, Trust, and Estate Law Section.

I am a co-chair of the Real Estate Practice Group at Venable LLP in Baltimore and Washington and I am also the President of the American College of Real Estate Lawyers. I am here to present the views today of the ABA on S. 569, the Incorporation Transparency and Law Enforcement Assistance Act.

I am very pleased to be here and I just want to say at the outset that the ABA supports all reasonable and necessary efforts to combat money laundering, tax evasion, and terrorist financing. Indeed, we have worked very closely with the Financial Action Task Force (FATF) and the U.S. Department of Treasury in developing risk-based guidance for the legal profession, not only domestically, but internationally.

We are also in the process right now of implementing the FATF guidance for U.S. lawyers. These efforts underscore the ABA's unwavering commitment to work with national and international authorities and constituents in combating money laundering, tax evasion and terrorist financing. The ABA, however, opposes the proposed regulatory approach set forth in S. 569 and any other legislation that would unnecessarily regulate State incorporation practices and impose government-mandated suspicious activity reports on the legal profession.

The ABA's opposition is grounded in three core principles. First, S. 569 would essentially federalize State incorporation practices, meaning the States would have to obtain, keep current, and make available to law enforcement authorities beneficial ownership information on corporations and limited liability companies.

In our view, the imposition of a Federal regulatory regime focused on beneficial ownership information is not workable, would be extremely costly, would impose onerous burdens on State authorities and legitimate businesses, would run counter to formation practices in other countries, including Canada, Mexico, Japan, and China, and will not achieve the laudable goal of assisting Federal law enforcement authorities with pursuing and prosecuting criminal activity.

[1] The prepared statement of Mr. Shepherd appears in the Appendix on page 402.

These impediments, coupled with a simply unwieldy definition of beneficial ownership and the bill's focus only on a limited number of entities, would sow confusion into the formation process that would not enhance law enforcement's goals.

Second, S. 569 would create a new class of financial institutions known as formation agents that would be subject to enhanced anti-money laundering requirements. Because lawyers assist clients in forming corporations, partnerships, trusts, and limited liability companies, the designation of formation agents as financial institutions subject to the AML requirements threatens to sweep in U.S. lawyers and treat them as the functional equivalent of banks.

Third, S. 569 could potentially impose suspicious activity reporting (SAR) requirements on the legal profession, meaning that lawyers would have to report to governmental authorities a suspicion that their clients are engaging in money laundering or terrorist financing activity, and at the same time, the lawyers would be prohibited from telling their clients that they are telling the government about this SAR.

These requirements are in direct conflict with ethical obligations of confidentiality, the attorney-client privilege, and the core relationship of the attorney to the client. They could also undermine the rule of law by dissuading clients from seeking legal counsel from lawyers on proposed courses of conduct.

The ABA believes that a more effective and workable solution would involve collective and collaborative action of State government representatives working with the U.S. Departments of Treasury and Justice. Although the ABA has not taken a position on any such proposal since we favor the State-based approach, we suggest that Congress give this solution an opportunity to be implemented and assessed for its effectiveness before imposing unprecedented Federal regulation of State incorporation practices.

The ABA believes that the effort to designate formation agents as financial institutions is premature and does not take adequate account of the implications for the legal profession. In light of the other initiatives that the legal profession is undertaking on a voluntary basis, such as the development of the good practice guidance I just mentioned, the ABA believes that the imposition of AML requirements on the legal profession is unnecessary.

I would like to speak a moment about the significant efforts of the ABA to respond to the concerns sought to be addressed by S. 569. For the last 2 years, I have been working with my ABA task force colleagues, together with legal professionals from around the world and also with FATF and the Treasury Department, to develop risk-based guidance for the legal profession dealing with client due diligence.

FATF has been working actively with specially designated non-financial businesses and professions, including lawyers, to produce voluntary risk-based guidance for the legal profession to ensure that adequate client due diligence is performed at the outset of the client relationship so as to minimize the risk that lawyers will be used by unscrupulous clients to launder illegally obtained money.

We have been working with members of U.S. specialty bar associations, together with our counterparts from the United Kingdom, in this effort and we have attended numerous meetings with FATF

officials to prepare this guidance. This proposal for legal professionals was released by FATF last October. This was a major achievement for the FATF and resulted directly from the active and extensive participation of the U.S. legal profession in this effort.

Education of U.S. lawyers regarding AML and counterterrorist financing compliance is an important cornerstone of an effective AML compliance program. The ABA, as well as members of other specialty bar associations, continue to be active in this educational area. Through the efforts of members of the ABA Gatekeeper Task Force, as well as others within the ABA, the American College of Real Estate Lawyers, the American College of Mortgage Attorneys, the American College of Trust and Estate Counsel, and other professional organizations in the United States, we have been developing additional voluntary client due diligence guidance in collaboration with members of the Treasury Department.

On a personal note, I have written extensively on this topic in an effort to educate the U.S. legal profession on this important issue: Combating money laundering, tax evasion, and terrorist financing activity while minimizing the impact on our economy and State regulators are critical objectives. The ABA, together with other private and government sector groups, has expended a considerable amount of resources, but has made great headway in developing an effective solution to the identified problem.

We continue to support collaborative State efforts and oppose premature Federal legislation. We look forward to working with you to develop a workable solution and a comprehensive solution that addresses the mutual objectives of all concerned.

I want to thank you for giving us the opportunity to present the views of the ABA on S. 569 and I would be delighted to answer any questions you may have.

Chairman LIEBERMAN. Thank you very much, Mr. Shepherd. Good testimony. Now we go to John Ramsey, National Vice President of the Federal Law Enforcement Officers Association. Welcome and please proceed.

TESTIMONY OF JOHN R. RAMSEY,[1] NATIONAL VICE PRESIDENT, FEDERAL LAW ENFORCEMENT OFFICERS ASSOCIATION

Mr. RAMSEY. Thank you, Chairman Lieberman, and distinguished Members of the Committee. I would like to thank you for the opportunity to testify today. I appear before you today in my official capacity as the National Vice President for the Federal Law Enforcement Officers Association (FLEOA).

On behalf of over 26,000 members of FLEOA, I am memorializing our support for S. 569. The proposed legislation is very important to the FBI, Immigration and Customs Enforcement, and the Internal Revenue Service members, as they are the lead agencies that investigate money laundering and terrorist financing cases, as well as other Federal law enforcement agencies.

Incorporation transparency is an invaluable tool to combat national and international crime and terrorism, hinder the financing

[1] The prepared statement of Mr. Ramsey appears in the Appendix on page 414.

thereof, and frustrate the ability of perpetrators to hide and benefit from the proceeds of these crimes. While criminals cower behind the anonymity of their corporate filings, they continue to exploit the system as a means to commit terrorist financing and money laundering.

Using a registered agent or attorney as the front person for their company, these terrorists and criminals are able to circumvent law enforcement and accomplish the following five things, use shell company bank accounts to launder millions of dollars, use shell companies to attempt to acquire significant ownership interests in a financial institution, purchase real property through their shell companies to be used as stash houses for stockpiles of drugs or weapons, operate money remitter businesses to move their illegal proceeds to offshore accounts, and engage in cyber terrorism attacks by disseminating contaminated e-mails from ostensibly legitimate companies.

By attacking and addressing the above five mentioned points would allow for greater protection of our vulnerabilities with regards to our own homeland security front. We are aware of some of these concerns that have been voiced by industry and at the State level with respect to this bill. Specifically, this bill does not require any State to enact any law with respect to corporations. It merely requires the States to add the relevant question to their existing incorporation forms and make the information available to law enforcement upon presentation of a legally authorized subpoena or summons.

This information is beneficial to law enforcement and homeland security to prevent the misuse of U.S. corporations by criminals and other wrongdoers within or outside of the United States. With regards to cost, beneficial ownership information can be collected via existing electronic incorporation methods and stored in existing electronic databases. Alternatively, such information can be obtained by adding the relevant question and space for a response on existing paper incorporation forms.

The lack of truthful disclosure is not necessarily an obstacle, but merely identifies the direction in which to proceed in order to identify the criminal enterprise and ultimately showing the criminal intent.

Law enforcement's ability to investigate and enforce the provisions of the Bank Secrecy Act has been impeded by terrorist and criminals who hide behind the corporate veil. This costs law enforcement agencies a substantial amount of time and money, for example, long-term surveillance and subpoena service on numerous third parties. It also allows the terrorists and criminals to remain about 10 steps ahead of law enforcement. FLEOA maintains the identity of the real beneficial owners should be made available to law enforcement officers who again make legally authorized requests pursuant to official investigations.

I would like to share with you one example—I would be glad to share more later if you would like—regarding a case. The owner of La Bamba Check Cashing Company, Inc. was sentenced in connection with $132 million in false currency transaction reports. On June 23, 2009, in Miami, Florida, Juan Caro and the company he owned and operated, Maytemar Corporation, doing business as La

Bamba Check Cashing, was sentenced to one count of conspiracy and 15 substantive counts of failing to file currency transaction reports.

He was sentenced to 216 months in prison and ordered to pay a $250,000 fine. The court also ordered the forfeiture of more than $11 million in cash and property. The Maytemar Corporation was also sentenced to probation, which is the only possible sentence for a corporation.

According to the evidence presented at trial, the defendants executed a scheme to assist individuals and entities in South Florida to cash checks in anonymity in exchange for a commission based on the face value of the check. Other defendants working with Mr. Caro identified and recruited customers, mostly local construction companies and subcontractors who were interested in cashing checks at La Bamba through shell companies that the defendants owned or controlled.

In this way, the construction companies participating in the scheme would cash checks payable to the shell companies and get back cash from La Bamba. Thereafter, the defendants would file currency transaction reports (CTRs) with the Treasury Department, falsely stating that the shell company and/or nominee owner had conducted the transaction, concealing the true parties involved in the transaction and the source of the funds.

For this service, La Bamba Check Cashing, Mr. Caro and others earned substantial fees. Through the course of the conspiracy, the defendants in this case filed CTRs with the Treasury Department reflecting transactions in the name of the shell companies. These transactions totaled more than $132 million.

While our membership respects the free spirit of enterprise in our country, we do not want to see the United States adopt the financial safe haven image of other countries around the world. If our country's laws require individuals to register firearms and vehicles, the same should apply for a corporation. The consequences for allowing terrorists and criminals to exploit our corporate filing system are severe.

In the spirit of homeland security and protecting our great nation, we cannot permit this to continue. The content of this bill does not disvalue the American dream, but it addresses the American deception. We should not continue to allow corporate secrecy to be used as a shield to hide corporate misconduct.

We hope your Committee will embrace the importance of S. 569 and work together to move it forward. I would like to thank the Committee Members for my time and would be glad to answer any questions.

Chairman LIEBERMAN. Thank you very much, Mr. Ramsey. And last, Jack Blum is the Chairman of Tax Justice Network USA. I think I am correct that you previously were with Baker and Hostetler?

Mr. BLUM. Yes, that is correct.

Chairman LIEBERMAN. And may have also had service here in the U.S. Senate?

Mr. BLUM. Fourteen years ago.

Chairman LIEBERMAN. It is a pleasure to welcome you back and we look forward to your testimony now.

TESTIMONY OF JACK A. BLUM,[1] CHAIRMAN, TAX JUSTICE NETWORK USA; AND MEMBER, ADVISORY BOARD, GLOBAL FINANCIAL INTEGRITY

Mr. BLUM. Thank you, Mr. Chairman, Senator Ensign, and Members of the Committee. I have a prepared statement. I ask that it be made part of the record.

Chairman LIEBERMAN. Without objection.

Mr. BLUM. What I would like to do is simply focus on the problem and urge all of you not to let the details that we are talking about here prevent addressing the serious problem we have.

The serious problem comes from the fact that incorporation is now available on the Internet to anybody with almost no checking as to who they are. They get the documents not a terribly long time after they fill out their Internet forms and then to try and figure out what is being done with that corporation is well nigh impossible.

The worst part of it is you do not even have to be the individual who is setting it up. You can be another corporation from another jurisdiction which has equally weak controls over who sets up a corporation. So, for example, if I were trying to fund a terrorist operating, let's say in the United States, what I would do would be set up a U.S. company, have that corporation be owned by some entity, for example, offshore, and then in turn have the U.S. corporation open the bank account.

They would be able to do that by providing, let's say officer and director information for the offshore company and the next thing wire money in from wherever and provide a card to whoever wants to use it inside the United States.

At the very minimum, we should be checking under all of the various worldwide sanction lists the identity of individuals who want to open a corporation. We have focused on the problem of the individual small business owner and I am terribly sympathetic to that because in private practice, I have represented some small business owners. The difficulty that a small business owner has is not incorporation. I have had to take them through dealing with regulatory agencies at the State and local level. I challenge anyone who says the problem will be the added burden of incorporation to try to open a restaurant in Maryland.

It turns out that there is a lot more that you have to do and many other hurdles to jump. So I am very focused on how we get at these people who are coming in to abuse the system and misuse the system. I am also terribly concerned about following the trail. Time and again, conmen have used anonymous corporations to block any ability on the part of anyone to figure out who they are.

And it turns out that is both civil and criminal. And here I would say that I would like to see much more information available in discovery and private litigation. The reason is, if a con man moves money to a corporation and there is no information about who is behind it or what is going on, there is no way to pursue the recovery of that money through civil litigation.

It is in the nature of all criminal activity that fraud is least policed and least enforced by the criminal justice system. The cases

[1] The prepared statement of Mr. Blum appears in the Appendix on page 418.

are complicated. If you come in with a client who has been defrauded, they say to you that is a civil matter. Well that is fine, but there ought to be some trail of responsibility and that means being able to identify where the corporation is, who is behind it, not simply get a corporate name and a dead blank from there.

So these are the core issues as far as I am concerned. I think we can get around the problem of identifying beneficial owners with some pretty easy things. Who is putting up the money? What kind of business are you going to be in and where is it located? And with basic information about the live person who is going to direct the money and the bank accounts, who that person is. With that kind of information, law enforcement can move forward and I cannot see that any legitimate business person would be inhibited by having that available.

I will be happy to answer any questions you might have. Thank you for letting me speak.

Chairman LIEBERMAN. Thank you very much, Mr. Blum. I am going to suggest that the Members reduce our time of questioning to 5 minutes as well, so we can get to the vote on the Senate floor.

Mr. Shepherd, you have expressed some significant concerns about the requirements the legislation before us could place on attorneys who help clients complete the information process. You have offered some suggestions, certainly intentions to work together.

I wonder if you would draw it out a little bit more and tell what steps you think should be taken. I am speaking out from the other side to make sure that lawyers and other formation agents are not wittingly—of course, we assume most times—aiding and abetting fraud, tax evasion, or money laundering, for instance, for the use of shell companies.

Mr. SHEPHERD. Yes, Mr. Chairman, I would be happy to answer that question.

First and foremost, we have been meeting with FATF, on behalf of the legal profession, for the last 5 or 6 years. We have asked at every meeting we have had with FATF to show us examples of typologies where lawyers have been used unwittingly in the facilitation of money laundering and terrorist financing.

FATF has been unable to show us one typology globally where lawyers have been used unwittingly. We have asked that repeatedly of FATF. No answer forthcoming on that, so that suggests to us that the problem probably does not exist, otherwise FATF would have provided typologies on that.

Second, we have been very active in developing risk-based guidance for the legal profession with FATF. We did not have to engage with FATF, but we did. We used the financial institution risk-based guidance as a template that was developed in June 2007 between FATF and the financial institution industry. Taking that as a template for the designated non-financial businesses and profession sectors, including lawyers, accountants, and others, we developed risk-based guidance for the legal profession over the course of a year and a half with direct engagement with FATF.

We dealt with some very difficult issues, including beneficial ownership issues, with FATF during that process, but we worked through the issues. Suspicious transaction reporting requirements,

we worked through that very difficult issue for the legal profession. So I think that demonstrates that we are willing to engage with FATF and with governmental authorities both domestically and internationally to grapple and resolve some very difficult issues that face the legal profession.

In fact, what we are doing now is that we have the FATF risk-based guidance for the legal profession in place. We have developed good practices guidance that is given out to various groups, especially bar associations, the ABA, and other constituents as a implementation tool for what the risk-based guidance is all about.

Most lawyers are unfamiliar with the FATF risk-based guidance. What this does, the good practices guidance, is to get it out to all the U.S. lawyers so they can understand and appreciate what the risk-based approach means. It is a cost benefit analysis and I think it is good instruction to the U.S. legal community.

Chairman LIEBERMAN. Thank you. Mr. Kellogg, a question for you. You spoke about the practical problems that this legislation could cause you and your business and I think you made your point and I heard it clearly. I assume that you also recognize that there can be a problem here in terms of the law enforcement and I wonder if you have thought about—and this is what the Committee is striving for—what is the appropriate balance between law enforcement's need for useful information and the understandable concerns of the business community that you have expressed?

Mr. KELLOGG. There has been a fair amount of discussion about law enforcement only having access of this information if they were to provide a subpoena or have some other review prior to going to a State for this information and I think that is a very sufficient and necessary condition to get the information.

One of my concerns from a privacy standpoint is that at least 38 States currently publish all of their incorporation filings, I guess, as a matter of public record and it would certainly be easy for those States to just go ahead and say, we are going to publish this beneficial ownership information along with the State incorporation information.

This is really private information that I think needs to be protected. Now there have been a number of references to having to set up separate databases the States would have to do, and that certainly would be very welcome and I would balance that.

So I think that if you can set up a separate database, that the State will protect the sensitive information and make it available to law enforcement under subpoena or other official requests, I think that would be sufficient.

Chairman LIEBERMAN. Thanks for that answer. My time is up. Senator Ensign.

Senator ENSIGN. Mr. Kellogg, I think it is very important that we had you here and heard your perspective and yours is just one of many perspectives from small businesses. You have one type of setup with employee-owners, but there are other perspectives, I am sure, that are out there as well and that is why I think that it is important to hear from folks like yourself about—we need to hear from many others.

Mr. Blum talked about that it would be very easy to just provide the information on who provides the money. You made the point.

Could you reiterate your point on venture capital and how that could have a chilling effect on all businesses?

Mr. KELLOGG. There has been a fair amount of discussion today about the difference between who exercises control and who actually provides the money and there is actually a difference in most businesses as to who provides the money and who exercises control. Most businesses have a general manager, an operator, some person that actually is in control of the day-to-day operations of the business and the investors and other folks are more passive in that sense.

The problem that I see more than anything else is that there is a real complicating factor from the standpoint of wanting to be able to establish a new business that competes with say an existing business and you want to keep it quiet while you are still in the development phase. I mean, a lot of the times if you are developing a new product or you are developing a new service, you would like to enjoy some level of trade secrecy with that and so you want to bring it to market. And then when you bring it to market, you are going to tell everybody about it at that point, but you would like to have it ready to go and be ready to take on customers, and that is a very legitimate practice. Entrepreneurs and others drive efficiency in the economy by competing with larger businesses and finding new ways to do things.

Some level of secrecy is helpful from the standpoint that if you have good financial backing, people are going to take you a little bit more seriously and potentially compete with you more rapidly.

Senator ENSIGN. Have you or are you aware of any definition of this beneficial ownership that would strike the balance between small business and law enforcement?

Mr. KELLOGG. I am going to beg that I am not a lawyer. I am a common businessman and I am not sure that I want to weigh into saying how are you going to define beneficial owner, so I am going to decline to say that I am an expert in that area.

Senator ENSIGN. One of the reasons we do not necessarily want an expert, because you want the average small business person to be able to understand it. That is one of the reasons that the language needs to be that simple, is because you may not want to hire a lawyer to—no offense to the lawyers with the ABA at the table—but that is one of the things that actually the first panel testified. They want to make the definition simple enough to where you do not have to hire all these consultants and lawyers to be able to set up a simple business shell to be able to get into business.

You want to have the proper entity set up that meets your needs, but you want to make it simple enough and those definitions need to be simple enough where just the average person can understand it without hiring a lawyer. So that is why we need regular people.

Mr. KELLOGG. Well, I would concentrate on who controls it more than the beneficial ownership. I mean, that makes more sense to me in terms if you want to find this real live person.

Senator ENSIGN. Is it a percentage of control?

Mr. KELLOGG. I think that is a hard question to answer because any kind of little threshold, criminals are just going to read whatever it is that the threshold is and try and get around it.

Senator ENSIGN. Mr. Chairman, in the State of Nevada, the Gaming Commission requires certain people to be licensed. These are usually bigger businesses. These are not smaller businesses and they are very expensive to get licensed, by the way.

But it goes to the fact of control. It used to be any key employees, but they have really defined it down now and even a small percentage of ownership does not necessarily mean that you have to be identified as one of the key employees. But it really, over the years—and we may want to even look at some of the definitions in that regard simply because that is going to be more of what Mr. Kellogg is talking about.

As far as actual control of the company, I think that is really what we need to be looking at.

Chairman LIEBERMAN. Thanks, Senator Ensign. It is a good idea. We should look at that. Senator Levin.

Senator LEVIN. Thank you, Mr. Chairman. First let me agree, that is the effort here, is to get to the people who control the company and the definition of beneficial owner should focus on control. I think that is an important point. I think that is a common approach, as a matter of fact.

The Treasury told us this morning, and the Justice Department, that they are going to work on a definition. I think it was fairly clear that the definition is going to focus on that aspect, beneficial ownership not the small shareholders, but who controls the entity. So I think your testimony is very helpful in that regard, Mr. Kellogg, and we thank you for it.

Mr. Ramsey, there is authorization in this bill to allow DHS grant funds to be used for costs that are incurred by the States, adding a line to their forms in order to enable them to collect the beneficial ownership information. Now I am wondering what your reaction to that is in terms of you represent law enforcement personnel. Is that a useful expenditure of DHS grants? Do you view that as something which we should not even authorize? What is your reaction?

Mr. RAMSEY. I do not know if FLEOA would actually take a position on that, but I would say that it appears that the monies would be going toward law enforcement in a matter of you are putting monies into a program that in the long run actually assist law enforcement in its investigations.

Senator LEVIN. That is very helpful. Thank you. And that is, of course, the point of it, and one of the reasons why this bill has been referred to this Committee. But if your organization does have any further thoughts on that, would you just share them with this Committee?

Mr. RAMSEY. Sure.

Senator LEVIN. On that issue. Mr. Shepherd, are you familiar with the NCCUSL proposal?

Mr. SHEPHERD. Yes, I am, Senator Levin.

Senator LEVIN. Would you agree that the proposal does not require corporations to identify the natural persons who are the beneficial owners of a corporation and that instead, it simply requires corporations to identify their owners of record?

Mr. SHEPHERD. The act, Senator——

Senator LEVIN. NCCUSL, their proposal.

Mr. SHEPHERD. The NCCUSL model legislation, yes. It contains two concepts of records contact and responsible individual, both of whom must be natural, breathing, warm people.

Senator LEVIN. That is for the contact person.

Mr. SHEPHERD. That is for the records contact.

Senator LEVIN. But that person then is supposed to disclose who the owners of record are and that owner of record under NCCUSL could be, for instance, another corporation; is that correct?

Mr. SHEPHERD. That is right.

Senator LEVIN. Because there has been some confusion about that. The living, breathing person that we are looking for is the beneficial owner, the person that controls, and under the NCCUSL proposal, there has to be a person to whom you can go, but that person then is required to say who the owner of record is. That owner of record need not be a living, breathing person. It could be a corporation?

Mr. SHEPHERD. Let me just elaborate on that.

Senator LEVIN. But is that correct?

Mr. SHEPHERD. Well I think that requires some clarification, Senator. On the NCCUSL model, legislation went through a series—in a evolutionary process and we introduced a concept of a responsible individual and the purpose of that was to make sure that law enforcement could contact the responsible individual because that person should be informed as to the control, management, and direction of the underlying entity.

Senator LEVIN. Should be.

Mr. SHEPHERD. That is right.

Senator LEVIN. Can they be identified as the record owner of a corporation?

Mr. SHEPHERD. Under the NCCUSL proposal, I think that was certainly the intent, Senator, to do that.

Senator LEVIN. So they could identify a shell corporation in Panama or someplace as the record owner of that company?

Mr. SHEPHERD. That is right, because in some of these situations, you are talking about tier entities.

Senator LEVIN. I think we ought to ask FATF. By the way, there has been a reference to FATF this morning and as to the conversations which Mr. Shepherd had with FATF. I think it would be useful for us to ask FATF for their position on this proposal on the bill, but also give them a chance to comment on Mr. Shepherd's testimony as well.

Mr. Ramsey, there is a question of tipping off a corporation to law enforcement under the NCCUSL proposal. Would you agree that under their proposal there is that problem, that there would be a tip off to the real owner if they want to give it to us, of the law enforcement's interest and that is a problem which we could avoid if we have a confidential disclosure just to the State and that disclosure could only be to law enforcement?

Mr. RAMSEY. Yes sir, I believe that currently law enforcement has to go to the company to gather information, which could actually tip our hand in the investigation. This bill could actually provide a more discreet avenue of obtaining this information, possibly through the Secretary of State's office, without tipping our hand and telling everybody we are in that investigative mode.

Senator LEVIN. Finally, because I'm over my time, Mr. Blum, do you have a comment on the tipoff issue?

Mr. BLUM. I think the tipoff issue is very serious because if you go to the people who are in essence involved with the perpetrators and say, oh tell us who is really behind this, they are likely to move the money very quickly. Money moves with the speed of light and one of the objectives in these criminal cases is to freeze the money and apply it either for the benefit of the victims of a crime or to prevent further use of the money for terrorist or other purposes.

Senator LEVIN. Thank you. My time is up.

Chairman LIEBERMAN. Thanks, Senator Levin. Senator Carper.

Senator CARPER. Thanks. Mr. Shepherd, in your testimony, I think you discussed the fact that the bill before us is prospective in nature and it only covers new corporations that form after the bill's enactment.

I think that leaves maybe 18 million corporations that have already been formed out of compliance with this bill. Could you discuss some problems with that?

Mr. SHEPHERD. Well I think the way I read the bill is that the intent is to cover corporations and LLCs that are formed after the effective date of the bill. The concern is you have an estimated 18 million corporations and LLCs currently in existence. What do we do with them? Are they covered? Are they not covered?

So you are in effect creating a dual formation system or system that will be covered by this bill or not covered by this bill because you have 18 million entities not covered, not subject to these disclosure requirements, and then you have the new ones subject to it. So you are creating a duality that perhaps is unintentional, but I think that is a shortcoming of this legislation.

Senator CARPER. Wouldn't the Uniformed Law Commission approach capture more corporations and hopefully more criminals?

Mr. SHEPHERD. That is right. The NCCUSL proposal covers not only LLCs and corporations, but also partnerships and trusts, plus it contains a transition provision that for a 2-year period the existing entities would be required to comply with the NCCUSL provisions.

Senator CARPER. All right, thank you. Thanks to all of you for being here today and for your testimony. Mr. Kellogg, as a defense contractor, I can imagine that there are potential national security concerns if employee information is made public.

Could you describe how this bill would impact companies in sensitive areas, defense, maybe technology, exports and the like?

Mr. KELLOGG. Well Senator, that is actually one of my concerns. I will tell you that without going into detail, we certainly have been concerned about network vulnerability for a great period of time because we have for official use only, International Traffic in Arms Regulations ITAR-controlled and proprietary information on our computer networks, so there is substantial valuable information that needs to be protected just from a privacy standpoint.

We would be concerned about a list of employees going out publicly from the standpoint that foreign intelligence service potentially would get a list of people in order to target, in order to say the typical routine would be to steal their laptop out of their car

and try and get a recording of their password or user name or some other mechanism in order to be able to get into the network.

And then you would normally try and place a key logger event on a machine and that would start externally sending information out. That is a concern that we have, although I think it is somewhat unique to our industry and there are much larger implications relative to the competitive advantages of smaller private businesses and LLCs relative to their larger competitors of disclosing the ownership information. I think that is a bigger concern.

Senator CARPER. I think those are good to point out. Back to you if I could, Mr. Shepherd, for my last question before time expires. As we discussed in the first panel with Assistant Secretary Cohen, a lot of attention has been paid to the Treasury Department's definition of beneficial owner. It is defined in the Treasury Department's anti-money laundering regulations.

Could you help us better understand why this definition of beneficial owner is difficult to apply in the corporate context?

Mr. SHEPHERD. Yes, Senator. I think there are a number of issues with that. One deals at the outset with the terms used in the definition of beneficial ownership. You have the word "control," it is not defined. You have the definition "indirectly or directly" nowhere to be defined.

The phrase "control, direct, or manage," is nowhere to be defined. So you have these concepts in there and what is troubling about the definition is that you are dealing with corporations and LLCs, totally different vehicles, and when you talk about control in the general sense about voting control, voting power, it is different in a corporation than it is in a LLC.

So I think the definition needs to respect the distinctions between these two legal entities.

Senator CARPER. And one more quick question, if you can respond briefly. Mr. Shephard, you mentioned that the ABA is working with FATF. We discussed the issue on the last panel, but if you could talk a little bit more about FATF's rating on the United States.

Why is the recommendation so difficult for other countries, not just for the United States, to implement?

Mr. SHEPHERD. Yes, Senator. In 2007, the mutual evaluation report prepared by FATF on the United Kingdom indicated that consultants had concluded that the definition of beneficial ownership is incapable from a law interpretation standpoint of precise definition as a matter of law. So even the FATF report included views from consultants that the definition of beneficial ownership was not very clear.

The definition of beneficial ownership in this legislation differs from the FATF definition, but both suffer from some ambiguities. So I think that it is important that FATF recognized the difficulties in applying the definition of beneficial ownership to the various countries. And as you can see from the mutual evaluation reports that I have seen, most countries received a partially compliant grade. Other countries, such as the United States, received a non-compliant.

But again, you receive four different grades under FATF, compliant, largely compliant, partially compliant and non-compliant. The

majority of the countries are partially compliant. That is just one notch above non-compliant. So I think that demonstrates the difficulty that FATF has had and the countries have had, frankly, in complying with Recommendation 33.

Senator CARPER. All right, thanks. Mr. Chairman, I would just say not every committee hearing that we have provides, I think, a roadmap to a common sense compromise where there are legitimate concerns on all sides and a lot of stakeholders refuse to take—I think this has been very constructive. I really want to thank you for scheduling this hearing and for each of our witnesses for coming in and for testifying.

Chairman LIEBERMAN. Well thank you, Senator Carper. I appreciate what you said and I appreciate the spirit of it. Senator Levin.

Senator LEVIN. Just very quickly. Thank you, Mr. Chairman, for your holding again this hearing. Two quick things. One, if the ABA has any suggestions relative to a good definition of beneficial owner, we would welcome that. The Treasury and the Justice Departments are working on it and if you have problems, which I think you do, with the current Treasury one or its application in this circumstance, we would hope the ABA would offer, not just offer, but actually give us a definition that you think is a simple, workable one.

And second, finally, Mr. Kellogg, on your comment about sometimes secrecy is needed in terms of the business needs of new business, there is a way to address that. We do in our bill, which is to say that the information must be kept private unless there is a subpoena. It is up to the State to decide whether or not to release that information and we could tighten that further, I think, following your suggestion, which is that we would say that information is only available by subpoena, but a State could specifically authorize. It would have to take a separate legislative action to do it.

We are trying to protect the rights of States here. We are trying not to intrude on them more than is necessary for Federal law enforcement purposes. So we put this language in saying you cannot make this public without a subpoena, and only to law enforcement. But we had to put it in there to protect States' rights. Hey, if the States want to release it, they can. We could tighten that further to make sure it was a conscious decision on the part of the State to release it, to take into consideration your concerns, to say this cannot be released by the State unless they specifically legislate to do that.

I think you made a legitimate point which we could——

Chairman LIEBERMAN. Forgive me for doing this, but we are about to miss a vote.

Senator LEVIN. I thank you again.

Chairman LIEBERMAN. I would welcome a response for the record. I hope Senator Carper's evocation and invocation is carried forward based on the very helpful testimony of all given. It will be great if we can come to a compromise on this, because we all have the same goal.

The record will be kept open for 15 days to allow for further questions or statements. I thank you very much. I apologize for cutting you off. The hearing is adjourned.

[Whereupon, at 12:33 p.m., the Committee was adjourned.]

APPENDIX

Examining State Business Incorporation Practices:
A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act
Chairman Joseph Lieberman:
June 18, 2009

Good afternoon and welcome to our hearing today on the Incorporation Transparency and Law Enforcement Assistance Act – a bill that results from the persistent work of the Permanent Subcommittee on Investigations.

I want to thank my good friend and colleague Senator Levin, who chairs the subcommittee, for introducing this legislation after an intensive review of state incorporation procedures. The PSI staff has dedicated many hours to this issue, dating back more than nine years. The subcommittee held a hearing in November 2006 and has identified numerous law enforcement problems caused by the use of U.S. shell companies for illicit purposes. I commend them for their work.

Each year, nearly two million new corporations and limited liability companies are established in the 50 states and the District of Columbia. That's more than 5,000 new businesses per day. This is the American way - capitalism at its best: generating revenue and creating jobs.

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But, each year, some new businesses are incorporated for improper or illegal purposes. Criminals may try to use registered corporations to defraud innocent people, to cheat tax authorities, to hide the true nature of their transactions, or to launder ill-gotten funds. No one can put a figure on the number of corporations set up for illegal purposes, but some experts have estimated that billions of dollars may flow through such corporations every year.

Right now, a majority of states require some basic information from those seeking to establish a corporation. Most require the name and address of the company, the name of a "registered agent" who represents the company, and a list of "officers" or "directors." This information is typically considered a public record.

It is also customary, however, for states to allow the individuals with actual ownership interest – including the investors who control the corporation or partnership – to remain anonymous to state authorities. This can become a problem for law enforcement officials who may have cause to investigate a suspicious company. Often, the trail goes cold when they search public records or contact a Secretary of State's office, because the

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state has no record of the real people behind the incorporation – the people who may be using the business for illicit purposes.

Senator Levin's bill is designed with these law enforcement investigations in mind. His bill would set a national minimum standard intended to force states to collect and maintain information about a corporation's underlying owners to help law enforcement in its work. The bar is set higher for foreign owners, whose identities must be verified by the company's registered agent before the state can process the forms and set up the corporation. The bill gives states the authority to decide whether to keep the beneficial ownership information private or to make it a matter public record.

This is a transparency requirement, plain and simple, with stiff new penalties for providing false or insufficient information. Justice Lewis Brandeis famously said, "sunshine is the best disinfectant" - and since PSI held a hearing on this issue in 2006, opening the curtains to let the sun flood in, at least two states have revised their beneficial ownership laws to make them more transparent.

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But a well-intended desire for more "sunshine" must be weighed against other factors, including the privacy rights of those making personal investment decisions, the potential costs of administration and enforcement that would fall on companies and state governments, and the real impact the law would have on both investigations and prosecutions.

Senator Levin's bill, for example, would not force states to verify the accuracy of information provided before granting a new entity its legal status -- a potential loophole that criminals could continue to exploit even if this legislation was adopted.

The Uniform Law Commission, represented by one of our witnesses today, has drafted an alternative proposal that would leave companies in charge of maintaining the required information. Forty-four out of the 50 states already require corporations to keep on file lists of all members or shareholders of record at their principal offices. The Uniform Law Commission's approach would seek to strengthen and update that practice.

So today, we'll try to better identify and understand the problem, as well as discuss the potential solutions. We have an array of witnesses well

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schooled in business incorporations and in corporate investigations. I look forward to their testimony as we try to limit illegal operations, without damaging the smooth flow of commerce for legitimate corporations and corporate purposes.

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OPENING STATEMENT OF SENATOR CARL LEVIN (D-MICH)

BEFORE THE U.S. SENATE

COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

ON

EXAMINING STATE BUSINESS INCORPORATION PRACTICES:

A DISCUSSION OF THE INCORPORATION TRANSPARENCY

AND LAW ENFORCEMENT ASSISTANCE ACT

June 18, 2009

Senator Lieberman, thank you for holding this hearing to focus on the fact that we are forming about 2 million U.S. corporations and limited liability companies each year without knowing who is behind them.

U.S. corporations with hidden owners have created a serious law enforcement and national security problem. We will hear today from witnesses about U.S. corporations established by the military in Iran which is a state sponsor of terrorism; we will hear about U.S. corporations involved with money laundering; about U.S. corporations used to commit tax evasion, and more. They all have one thing in common: their real owners – the legal term is "beneficial owners" -- are hidden from view. Here is one example of what is going on.

In 2004, one of our key law enforcement agencies, Immigration and Customs Enforcement or ICE -- who is here today – uncovered a collection of U.S. companies that were secretly controlled from entities located in Panama. The investigation began when bank reports showed that a single company formed in Utah was participating in nearly $150 million in suspicious international wire transfers. Further investigation by ICE uncovered a network of nearly 800 hundred U.S. companies, dispersed among nearly all 50 States, controlled by the same Panamanian entities. These companies were transferring large amounts of money to each other and to high-risk jurisdictions overseas. The companies claimed they were paying for the import or export of goods, but foreign authorities indicated no such goods were being shipped. In effect, the money transfers were part of a massive financial shell game, in which U.S. companies were being used to disguise the movement of funds and mask suspicious activity.

When ICE obtained the incorporation records for the 800 U.S. companies, not one identified a company's true owner. After analyzing the available information, ICE found that nearly 200 companies had been formed in Utah and used the same company formation agent in a small office in a Salt Lake City suburb. That company formation

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agent also served as the companies' registered agent within the State to accept service of process. When questioned by ICE, the Utah registered agent indicated that he had formed the companies at the request of another company formation agent located in Delaware and believed all were "shell companies" with no real business operations in the United States.

The Delaware company formation agent was already well known to law enforcement. No less than eight previous investigations had led to its doors, each of which involved millions of dollars in suspected money laundering by U.S. shell companies. When questioned by ICE in prior cases, the Delaware company formation agent freely admitted that he knew some of the corporations he formed or caused to be formed were intended to move money out of Russia and some former Soviet republics. He also said that he sometimes sold U.S. companies to the same overseas buyer at the rate of 40 companies per month. When asked about the actual owners of the 200 Utah companies, the company formation agent was unable to provide law enforcement with any names, since that information was not required by law. The end result was that the ICE investigation, like the eight before it, hit a dead end, unable to proceed due to the lack of beneficial ownership information. A hearing exhibit summarizes this case.

Michael Chertoff, former Secretary of the U.S. Department of Homeland Security (DHS), wrote the following:

> "In countless investigations, where the criminal targets utilize shell corporations, the lack of law enforcement's ability to gain access to true beneficial ownership information slows, confuses or impedes the efforts by investigators to follow criminal proceeds. This is the case in financial fraud, terrorist financing and money laundering investigations. ... It is imperative that states maintain beneficial ownership information while the company is active and to have a set time frame for preserving those records."

Here's another aspect of the problem. A few weeks ago, members of my staff conducted an Internet search and found numerous company formation agents advertising the sale of U.S. companies and trumpeting the fact that U.S. companies can be formed without disclosing the names of any company owner.

One of the most blatant was Corporations Today Inc., which advertises its ability to form U.S. corporations in nearly every State with minimal cost and effort. A copy of some of its internet ads is presented in two hearing exhibits. This chart [Chart One] reproduces one of its advertisements offering the sale of "aged" corporations, meaning companies which Corporations Today formed years earlier. One of the companies, on sale for $6,000, is advertised as coming with four years of tax returns and an existing employer identification number (EIN) issued by the IRS. Why buy an aged corporation? According to Corporations Today, "obtaining bank loans may be easier when you can show you have history." So is "obtaining corporate credit cards and leases. For example, Dell Computers lease only to corporations 6 months old or more." This ad invites fraud –

enabling hidden owners to pretend they've had a corporation operating in the United States for years when they haven't.

These are not isolated cases. In the previous hearing we held on this topic, we presented evidence on Nevada First Holdings, a company formation agent which formed thousands of companies, allowed over 1,800 of them to use its address as their business address, provided nominee directors and officers to enable the true company owners to "retain a higher level of anonymity," and instructed its employees to open bank accounts and obtain Employer Identification Numbers from the IRS for companies sold to hidden third parties. That U.S. shell corporations are used in numerous crimes within the United States is well known, as described in reports we obtained in our last hearing from the Justice Department, DHS, IRS, Treasury and others, identifying U.S. corporations with hidden owners as a significant law enforcement problem. What may be less well known is the parade of requests being made by foreign law enforcement trying to track down the owners of U.S. corporations suspected of committing crimes in their countries. Some of those requests are set out in another hearing exhibit.

Despite mounting evidence of misconduct by U.S. shell corporations, despite Internet advertisements selling U.S. corporations with promises of anonymity, despite the years of law enforcement complaints, many of our States are reluctant to admit there is a problem in establishing U.S. corporations with hidden owners. Too many of our States are eager to explain how quick and easy it is to set up corporations within their borders, without acknowledging that those same quick and easy procedures enable wrongdoers to utilize U.S. corporations in a variety of ways both here and abroad.

In 2006, the leading international anti-money laundering body in the world, the Financial Action Task Force on Money Laundering – known as FATF – issued a report criticizing the United States for failing to comply with the FATF standard requiring countries to obtain beneficial ownership information for the corporations formed under their laws. FATF gave the United States two years, until July 2008, to make progress toward compliance with the FATF standard. Next week, FATF is scheduled to review U.S. actions on this matter. How can we justify our failure to do what we have committed to do – obtain beneficial ownership information for the corporations formed within the United States? We can't.

For those who say that if the United States tightens its incorporation rules new companies will be formed elsewhere, it is appropriate to ask exactly where they will go. In compliance with the FATF standard, every country in the European Union is now required to get beneficial ownership information for the corporations formed under their laws. Even many offshore secrecy jurisdictions request this information, including the Bahamas, Cayman Islands, Jersey, and the Isle of Man.

The Levin-Grassley-McCaskill bill that is the subject of today's hearing, S. 569, would assist our law enforcement community instead of thwarting it, and would also enable the United States to meet its commitment to FATF. Our bill would require States to add a question to their incorporation forms asking for the names and addresses of the

beneficial owners of a proposed corporation. States would not be required to verify the information, but penalties would apply to persons who submit false information. Prospective corporations with foreign owners would also be required to submit a certification from an in-state company formation agent that the agent had verified the owners' identities and obtained passport photographs for them. This beneficial ownership information would have to be updated annually. If law enforcement issued a subpoena or summons to obtain the ownership information, States would supply the data contained on its forms. Funds that are already provided to States on an annual basis by the Department of Homeland Security (DHS) could be used to pay for the minimal cost associated with adding a question to their incorporation forms. This chart [Chart Two] summarizes how the bill would work.

Introducing this legislation wasn't our first choice. In fact, at the request of the States, we delayed introducing any bill for a year to provide the States with an opportunity to craft their own solution. But when it became clear that the States would not step up to the plate, I introduced a bill cosponsored by Senator Coleman and then Senator Obama in the last Congress. That legislation is identical to the Levin-Grassley-McCaskill bill before this Committee today.

S. 569 has since been endorsed by a host of law enforcement groups including the Federal Law Enforcement Officers Association, the Fraternal Order of Police, the National Association of Assistant United States Attorneys, and more. It has also been endorsed by good government groups combating financial and corporate abuses, including the Tax Justice Network USA, Global Financial Integrity, Citizens for Tax Justice, Public Citizen, and more. I have submitted their letters of support for inclusion in the hearing record.

Today's hearing will discuss, not only our bill, but also an alternative proposal developed by the National Conference of Commissioners on Uniform State Laws (NCCUSL) at the request of the National Association of Secretaries of State (NASS). Unfortunately, the NCCUSL proposal fails to cure the problem and would create a host of new ones.

Most significantly, the NCCUSL proposal would not require those seeking to form a U.S. corporation to provide the names of the beneficial owners to the State. In fact, the term "beneficial owner" never appears anywhere in the proposal.

Instead, the proposal creates a complex and time-consuming procedure, summarized in this chart [Chart Three], which requires law enforcement to get the name of a company's so-called records contact from the State, chase down that individual, and ask that individual to ask the U.S. company under suspicion for certain ownership information. If the U.S. company responds, it is not required to provide its beneficial owners, but what are essentially its owners of record, which could be shell companies here or offshore. If the company is involved in crime or has been dissolved, the records contact individual will likely come back empty handed. So instead of getting the beneficial ownership information it needs, law enforcement will be chasing its tail after

the misconduct has occurred and maybe after the suspect company has shut down. And to add to the futility of this convoluted process, it may not produce useful information.

Another problem involves timing. Instead of collecting beneficial ownership information at the time a new U.S. corporation is being formed as our bill does, the NCCUSL proposal would allow hidden persons to obtain a U.S. corporation, misuse it, and only after the fact, set up a process for requesting ownership information. Worse, the proposal would require law enforcement to direct its information request, not to a State on a confidential basis, but to the suspect company itself which would then be alerted to the investigation. Informing suspects of active U.S. law enforcement investigations is not a good way to thwart or punish crime.

There are other problems with the NCCUSL proposal as well. For example, it would create confusing new terminology and incorporation requirements, including requiring persons forming a new corporation to supply a "record contact," "responsible individual," "initial public organic record," and "entity information statement." Defining those new terms and requirements would require wholesale changes in State law, instead of using the minimalist approach in S. 569 of simply adding a new question to existing State incorporation forms.

Another problem is that the "responsible individual" referenced in the proposal is defined so loosely that a nominee corporate director or officer in an offshore jurisdiction could qualify as such a party, and deny law enforcement requests for information by invoking offshore secrecy laws. Still another flaw is that the NCCUSL proposal is strictly voluntary, and any State that adopted it would be placed at an immediate competitive disadvantage by requiring more ownership information than its peers.

The fact is that only federal legislation can level the playing field among the States and, by requiring all States to take the same action within the same period of time, ensure that no State suffers a competitive disadvantage from collecting beneficial ownership information. In addition, only federal legislation can impose consistent, nationwide penalties on persons who submit false information to obtain use of a U.S. corporation. Only federal legislation can end the misuse of U.S. corporations, assist our law enforcement in combating this misuse, and bring the United States into compliance with its international commitments within a reasonable timeframe.

The purpose of corporations is not to hide owners and thwart law enforcement; the purpose is to limit financial liability for owners. Our States should not be enabling corporate owners to remain hidden from law enforcement. It is time to stop wrongdoers from turning U.S. corporations into convenient vehicles for crime and other misconduct.

Again, thank you, Senator Lieberman for holding this hearing today.

EXCERPT FROM CORPORATIONS TODAY'S WEBSITE

Wyoming Aged Corporations		
Name of Company	Cost	Inc. Date
Elite Consulting Group Inc. with EIN and 4 years tax returns	$5895	5/2004
Blackjack Investments Inc. with EIN	Sale pending	9/2004
Brookside Management Inc.	Sale pending	12/2004
BestGlo Corp.**with EIN- S-Corp**	$4295	9/2005
Prime Systems **with EIN**	$4295	9/2005

Source: http://www.corporationstoday.com/aged-corporation (viewed 6/3/2009)

Prepared by U.S. Senate Permanent Subcommittee on Investigations, June 2009

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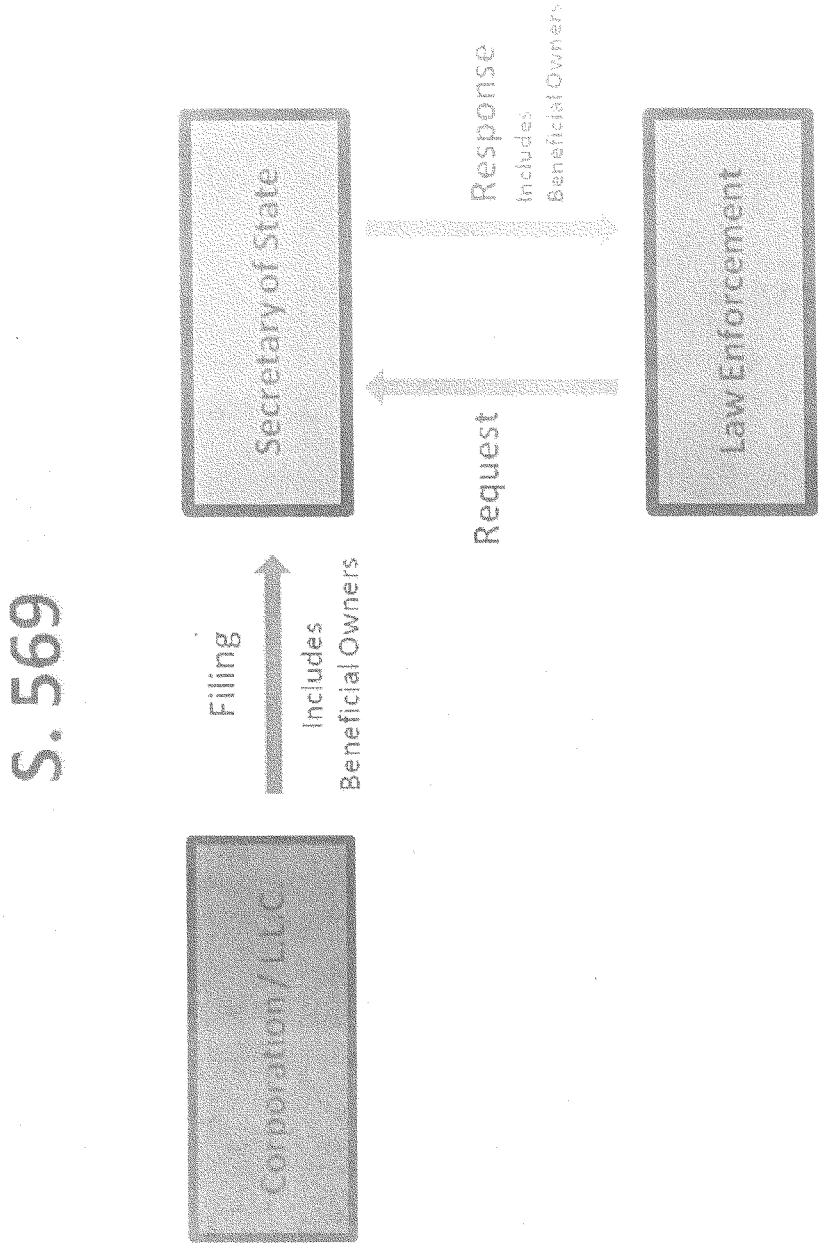
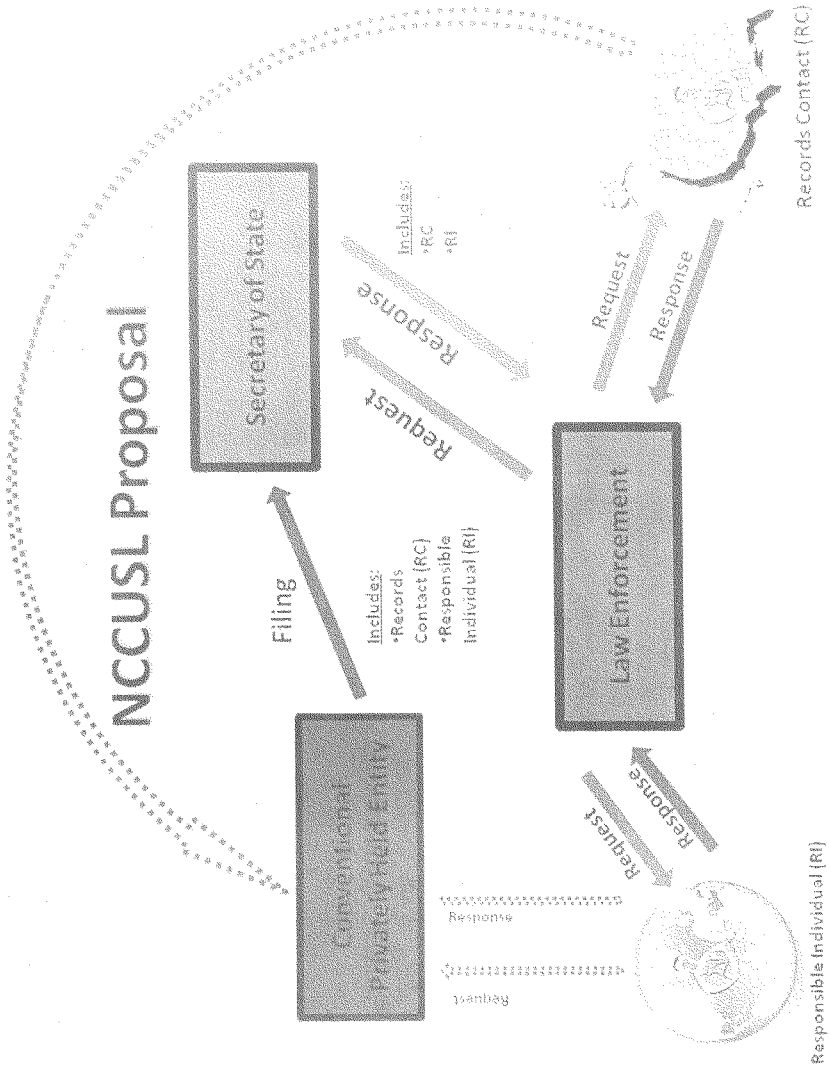

S. 569
Corporation / LLC
Filing
Includes
Beneficial Owners
Secretary of State
Request
Response
Includes
Beneficial Owners
Law Enforcement


NCCUSL Proposal
Filing
Includes:
•Records
Contact (RC)
•Responsible
Individual (RI)
Secretary of State
Request
Response
Includes:
•RC
•RI
Law Enforcement
Request
Response
Request
Response
Response
Request
Records Contact (RC)
Responsible Individual (RI)

Australian Government
Australian Taxation Office

COMMISSIONER OF TAXATION

Contact officer: Michael O'Neill
Telephone: + 61 2 9374 2538
Facsimile: + 61 2 9374 2763
Issue date: 18 June 2009

The Honorable Carl Levin
Chairman
Permanent Subcommittee on Investigations
Committee on Homeland Security and
Government Affairs
United State Senate
Washington, DC 20510

Dear Senator Levin,

I refer to your request, for Australian case studies showing the use of entities incorporated under the laws of some states in the United States of America. Following is a brief submission, Attachment 1 with case studies in summary form, and Attachment 2 providing these case studies in more detail. However, we note that the final tax position is yet to be settled in some cases.

We are very pleased to assist your efforts in enhancing the integrity of our respective taxation compliance systems.

Yours faithfully,

Michael D'Ascenzo

Michael D'Ascenzo
Commissioner of Taxation

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Submission from the Australian Taxation Office

The ATO believes that the use of secrecy havens (that may hide control or beneficial ownership of assets or income) continues to present a high compliance risk to Australia. The issues that require consideration include tax avoidance and evasion, investor fraud, manipulation of markets and sometimes more serious crimes like money laundering.

In our opinion, entities established in some states of the USA, for example some US incorporated companies, have some of these same attributes as entities established in secrecy havens.

The ATO works with partner agencies in Australia and internationally (including the US Internal Revenue Service) to attack abusive schemes linked to secrecy havens.

Our current compliance activity includes around 700 audits and 23 criminal investigations, raising tax liabilities exceeding $300 million and restraining criminal assets worth $75 million.

One important strategy for the Australian Tax Office is engagement with secrecy havens with a view to enhanced cooperation, transparency and reform.

This transparency includes commitments to tax treaties or Tax Information Exchange Agreements and the repeal of laws that obscure the underlying beneficial owners of bank accounts and/or entities.

In this context, we are pleased to provide to the US Congress some case studies showing the use of US corporations in schemes that may be linked to tax avoidance and evasion. We note, however, that the final position is yet to be settled in some cases.

These case studies are based on our compliance cases, with deletion of names/details to comply with Australian laws regarding privacy and secrecy of taxpayer information.

Consistent with our international collaboration, where our compliance activities suggest a relevant link, we will continue to share data and work cooperatively with the IRS.

Attachment 1 is a précis of our case studies.

Attachment 2 provides these case studies in more detail.

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Attachment 1

Case 1	US Corporation established as an executive share remuneration entity to cloud underlying ownership. Potential compliance risks relate to tax law, corporations law and regulation of Australian securities/equities.
Case 2	Interposition of a US Corporation in a chain of haven entities to hide the beneficial ownership of tens of millions of dollars.
Case 3	Use of US and Samoan entities to disguise ownership in a service contract for an Australian medical practice. Possible $6 million capital gain may be hidden.
Case 4	Use of US corporations in two schemes. The first involved an investment scheme promising large (uncommercial) profits. The second involved the sale of licences for franchises. These US corporations may facilitate defrauding investors and hiding profits of the promoter (tax avoidance or evasion).
Case 5	Scheme involving a US corporation and a Cook Islands superannuation/retirement fund. Scheme to hide a $1m profit on the sale of plant.
Case 6	Use of secrecy haven entities (including some US corporations) to inflate debt and interest tax deductions. One case involves interest tax deductions increasing significantly as a result of this scheme.
Case 7	Cross border financing arrangement involving a US Corporation to derive tax free dividends in Australia and to claim large interest deductions.
Case 8	Shifting ownership of Australian securities to a US Corporation entity resulting in access to foreign tax credits which shelter the income against Australian tax

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Attachment 2

Case 1

An Australian public company established a US corporation linked to its executive share remuneration scheme.

Because of the lack of transparency associated with this entity, it is difficult to determine compliance with Australian and US laws including taxation, corporations regulations, and the securities market.

Enquiries are ongoing, however potential compliance risks include:

- Hiding assets/income from tax agencies/creditors;
- Over claiming tax deductions;
- Opacity preventing accurate valuation; and
- Potentially blocking the application of accruals tax regimes (eg controlled foreign corporations) because of the difficulty in determining control and beneficial ownership.

Case 2

The taxpayer established a haven foundation of which they were nominated as a beneficiary. The taxpayer signed a mandate agreement in favour of a Swiss based bank which administered the haven foundation. That foundation had subsidiary entities incorporated in Bermuda and the British Virgin Islands, which in turn had subsidiary entities incorporated in the USA.

The interposition or layering of entities, including the US corporation, was intended to obscure the beneficial ownership of tens of millions of dollars.

Case 3

An Australian medical practice was restructured to enter into a new service contract.

The service provider was an Australian company, AUSCO, which was wholly owned by a US Corporation (USCO). STARCO, in turn, owned by a Samoan company described as a "bearer debenture company".

After some years, STARCO sold its interest in AUSCO for $6 million.

Enquiries are ongoing, however potential compliance risks include:

- The medical practice understating its income;
- Shifting profits/capital gains offshore (approximately $6 million);
- Stripping assets from companies to benefit individuals (the medical practitioners); and
- Tax avoidance / evasion.

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Case 4

The taxpayer incorporated two companies in the state USA. These two companies held bank accounts in Hong Kong, Singapore and Macau. The two US Corporations were used for two different uses.

First Scheme

The taxpayer commenced an investment scheme in 2001 which attracted investors by promising large returns on investments. Investors sent over $1 million to the foreign bank accounts controlled by the US Corporations. All of the investors in the scheme lost their money.

The taxpayer advised the investors that he had nothing to do with the US Corporations. He also claimed that he did not know who the controller of the companies was.

Second Scheme

The second US Corporation held "licences" from franchises. Franchises were sold to Australian investors. Upon the failure of these franchise businesses, the taxpayer denied his ownership/control of this American entity.

Mischief

The taxpayer directed the two US Corporations to send amounts to his Australian company in a round-robin scheme, claimed the amounts were loans and as such claimed large interest tax deductions.

The taxpayer had claimed that he was not the controller of the two American companies, insisting that he is merely an account signatory. The taxpayer also claimed that another US company was the corporate director of the first two US entities.

Result

After extensive questioning and numerous denials the taxpayer has recently admitted that he was the controller of the American companies.

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Case 5

1. Taxpayer is a director of Australian company, AUSCO.
2. AUSCO owned "widgets" for which they had paid $10,000.
3. A US Corporation, PCO and trust were established to purchase the widgets for $10,000.
4. The PCO on sold the widgets to another unrelated Australian company for $1 million.
5. The PCO profit of almost $1 million was paid through the trust to a superannuation / retirement fund located in the Cook Islands.
6. This Cook Islands fund loaned this $1 million to the taxpayer in Australia, who used these fund to repay his loans to AUSCO.

Compliance Risks

- Whether this scheme is a sham to hide a $1million profit.

Case 6

This particular case study has appeared in a number of variations using US entities or secrecy havens internationally. In a typical case, a foreign parent company sells shares it holds in its wholly owned Australian resident group or subsidiary to a newly incorporated Australian company. The shares are sold at market value. The new company pays for the shares by issuing shares in itself and borrowing from an off-shore related entity located in the USA. The new company's balance sheet shows the shares as an asset and its debt and equity equals the value of those shares. This restructure increased debt levels and interest tax deductions substantially.

Compliance Risks

Converting equity holdings in Australian subsidiaries to a mixture of debt and equity to maximise interest deductibility.

Case 7

The following summary provides an example of a situation in which it appears that USA tax advantages (utilisation of foreign tax credits) may be gained as a result of the use of a US corporation. The arrangement was apparently initiated by a USA banking entity which incorporates subsidiaries in the Cayman Islands and Delaware for the purposes of the facilitating the transaction outlined below.

1. An Australian entity borrows from a third party lender to invest in redeemable preference shares issued by a US subsidiary of the USA bank.

2. The US subsidiary on-lends those funds to a Cayman Islands registered subsidiary of the Australian entity.

3. The Cayman Islands company then lent the funds back to the Australian entity which uses these funds to repay the third party borrowing, thus completing the round-robin.

4. The investment by the Australian bank in the US subsidiary results in it deriving non-assessable income and claiming a deduction for interest on funds borrowed from its Cayman Islands subsidiary in respect of that income.

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Case 8

The arrangement can be summarised as follows:

1. Australian bank, as part of its liquidity management strategy, held a portfolio of securities on which the bank derived interest income and was fully taxed. It then established an Australian subsidiary, Aust Sub, to participate in the scheme.

2. The portfolio of securities transferred from the Australian Bank to capitalise Aust Sub was used to fund the subsidiary's investment into a US Partnership. Under the partnership agreement even though Aust Sub contributed only 60% of the partnership capital it was entitled to 98% of partnership income.

3. However, Aust Sub was entitled to 98% of the USA tax paid as foreign tax credits.

4. The US Partnership elected to be taxed as a corporation for USA tax purposes but for the purpose of Australian tax continued to be treated as a partnership.

5. Aust Sub returned 98% of the net income of the partnership as assessable income and then claimed foreign tax credits equal to 98% of the USA tax paid by US Partnership.

6. This arrangement allowed Aust Sub to continue to receive income equal to the amount of interest derived on the portfolio less an arrangement fee and to gain the benefit of foreign tax credits. As a result Australian Subsidiary effectively paid no tax in Australia on its interest income.

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CASE HISTORY: INVESTIGATION OF 800 U.S. SHELL COMPANIES UNABLE TO PROCEED DUE TO UNKNOWN CORPORATE BENEFICIAL OWNERS

Upon request, U.S. Immigration and Customs Enforcement (ICE), a leading law enforcement agency within the U.S. Department of Homeland Security, provided the U.S. Senate Permanent Subcommittee on Investigations with the following information about a money laundering investigation that was unable to proceed, because ICE was unable to obtain information on the true owners, or beneficial owners, of a number of U.S. shell companies suspected of involvement in crime.

In October 2004, ICE received information from foreign law enforcement that a company, incorporated and registered in the State of Utah, was linked to suspicious transactions totaling nearly $150 million. Further investigation by ICE revealed that the company was jointly owned by two offshore entities located in Panama. Investigative analysis revealed that the two offshore entities were part of a larger Panamanian group of holding companies, all located within the same Panama City office suite, which owned or controlled nearly 800 (as of 2005) U.S. corporate entities dispersed among nearly all of the 50 United States.

The transactions in which the Utah company was a participant, involved companies, controlled by the Panamanian network, that transferred large amounts of money to each other and into and out of high-risk jurisdictions, most often in Europe and former Soviet bloc countries. The purpose of these transactions was often listed as payment for the import or export of goods, but information from foreign law enforcement often indicated that the underlying import/export of tangible products was non-existent. In effect, the funds transfers appeared to be part of a massive financial shell game, in which U.S. entities were used as shell companies to disguise the movement of funds and conceal criminal activity behind seemingly legitimate transactions.

ICE investigators located and interviewed the registered agent of record for the Utah company. In addition to the company under investigation, ICE learned that this registered agent was also the agent of record for over 200 corporate entities registered in Utah and associated with the Panamanian holding companies. The registered agent identified the Panamanian holding companies as "clients of a client," who he identified as a registered agent in Delaware, who was employed by a prominent incorporation service provider there. The Utah registered agent stated he was in frequent contact with the Delaware registered agent who requested the company registrations and provided only the information required to be collected by Utah law, which is minimal. The Utah registered agent further explained that he believed many of the companies he registered for the Delaware agent were "shell companies," because they were created but not maintained.

Further investigation uncovered 8 past ICE (and U.S. Customs) cases involving the same Delaware incorporation service provider, the same Panamanian holding companies, and multiple U.S. companies:

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1) In 1998, Belorussian authorities requested the assistance of U.S. Customs to determine the corporate ownership of a Delaware company suspected in the smuggling of automobiles and stolen property in Byelorussia. The company's registered agent in Delaware admitted to U.S. Customs agents that the company was one of many incorporated on behalf of a Latvian client who would then sell the companies to other clients abroad.
2) In 1998, Russian authorities requested the assistance of U.S. Customs to determine the ownership of a company suspected of smuggling American cigarettes into Russia. U.S. Customs agents determined that the company was registered in Delaware and jointly owned by two of the Panamanian holding companies.
3) In 1998, Latvian authorities requested the assistance of U.S. Customs to determine the ownership of a Delaware company suspected of violations of Latvian customs laws. U.S. Customs agents interviewed the incorporator who stated that he incorporated such companies on behalf of a specific customer who would then sell the companies to overseas buyers.
4) In 2000, Polish authorities requested the assistance of U.S. Customs to determine the ownership of a company suspected of false invoicing of exports from Poland to the United States. U.S. Customs agents identified the company as registered in Delaware. U.S. Customs agents interviewed the incorporator who identified the company as one created for a foreign individual who requested the incorporation of approximately 40 companies a month through the incorporator's company. The incorporator stated that the companies were created to move money out of Russia, Latvia, and other former Soviet republics.
5) In 2001, Ukrainian authorities requested the assistance of U.S. Customs to determine the ownership of a company suspected of being a front for criminal activity in Ukraine. U.S. Customs agents identified the company as a Nevada registered entity, which had been registered in Nevada on behalf of the Delaware incorporation service provider. The Nevada company was jointly owned by two of the Panamanian holding companies.
6) In 2001, U.S. Customs agents received a request for investigative assistance pertaining to a suspicious shipment of oil from Russia to Poland involving a company incorporated by the Delaware incorporation service provider. A subsequent investigation determined that the company was jointly owned by two of the Panamanian holding companies.
7) In 2003, Ukrainian authorities requested the assistance of ICE to determine the ownership of a company registered in Oregon and suspected of criminal activity in Ukraine. An ICE investigation determined that the company had been registered in Oregon by a registered agent there at the request of the Delaware incorporation service, which had registered the company on behalf of a Latvian registered agent.
8) In 2003, Russian authorities requested the assistance of ICE to determine the ownership of a company suspected of involvement in Russian organized crime and millions of dollars of fraudulent financial activity. An ICE investigation determined that the company had been registered in Delaware by the Delaware incorporation service provider.

After consultation with the Department of Justice, ICE closed the investigation in September 2006. Although it appears that many of the U.S. companies have been used abroad in criminal activity, U.S. incorporators are not obligated to collect ownership information or know-your-customer information for the companies they form or the clients they deal with, nor conduct due diligence to determine the intended purpose and use of the corporations sold. ICE was unable to identify the U.S. companies' beneficial owners and unable to proceed with the investigation.

Prepared by the U.S. Senate Permanent Subcommittee on Investigations, June 2009

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Aged Companies

Here is a list of the companies that we currently have for sale. This list changes without notice. We have the largest inventory of aged shelf corporations in the United States. These are companies that we formed and put on the shelf, they have not been used by anyone. They come with Certificates Of Good Standing from the state, Certified Articles of Incorporation from the state, the corporate kit which includes 20 pre-printed stock certificates, corporate seal, and suggested meetings minutes. All state fees are paid through the renewal date of the company. If you need other services see our other services here.

If you are looking for a Publicly Traded company go here.

Click the state you are looking for: Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota, Tennessee, Texas, Utah, Virginia, Washington, Wisconsin, Wyoming

Prices subject to change without notice, so be sure and check with us to make sure the price and availability of the company is current.

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Aged Corporations		
Name of Company	Cost	Inc. Date
Alaska	Price	Date Formed
Advanced Management Services, Inc.	$1495	12/07
Commercial Services Corp.	$1395	2/08

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Aged Corporations

Key Developments, LLC	$1395	2/08
Defense Enterprises LLC	$1095	5/08
JG Services LLC	$1095	5/08
Mainstay Management Inc.	$1095	5/08
Sutton Management Services, Inc.	$1095	5/08
Ideal Business Services LLC	$995	6/08
Premier Business Services Inc.	$995	6/08

Arizona	Price	Date Formed
Eagle Eye Services LLC	$1095	3/08
Great West Marketing, Inc.	$1195	3/08
Intelligent Enterprises, LLC	$1095	3/08
Concept Creations Corp.	$1195	3/08
American Eagle Leasing LLC	$995	5/08
Canyon River Creations LLC	$995	5/08
Capital Edge Funding LLC	$995	5/08
Destiny Administration Services, LLC	$995	5/08
Snake Creek Enterprises LLC	$995	5/08
Top of the Line Developments, Inc.	$995	6/08
Canyon River Ventures Inc.	$995	7/08
Meridian Advisors Group Inc.	$995	7/08
Rustic Creations Inc	$895	12/08
Centurion Networking LLC	$895	12/08
Alliance Marketing Services LLC	$895	12/08
Amazing Marketing Services LLC	$895	12/08
Sage Consulting LLC	$895	12/08
Simple Innovations LLC	$895	12/08
Seabreeze Trading LLC	$795	1/09
Woodbury Creations Inc	$795	1/09

Arkansas	Price	Date Formed
Key Developments, LLC	$995	2/08
Premier Service Group Inc.	$995	2/08

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Aged Corporations

Intelligent Investments LLC	$995	2/08
Central Consulting Services, Inc.	$895	3/08
Concept Creations Corp.	$895	3/08
Eastern Developments LLC	$895	3/08
Flowing Waters, LLC	$895	5/08
Glasgow Marketing Inc.	$895	5/08
Accent Technologies Inc.	$795	6/08
Eastside Developments LLC	$795	7/08

California	Price	Date Formed
Advanced Marketing Associates Inc.	$2695	12/07
American Fidelity Partners LLC	$2695	12/07
Green Arbor LLC	$2695	12/07
Commercial Advisors LLC	$2395	4/08
Central Innovations LLC	$2395	4/08
Eagle Creations LLC	$1195	6/08
Prime Strategies LLC	$1195	6/08
Riverside Marketing LLC	$1195	6/08
Sage Funding Group LLC	$1195	6/08
Strategy Advancements LLC	$1195	6/08
Prestigious Strategies Inc.	$1195	6/08
Peak Design, Inc.	$1195	6/08
Freedom Development Inc.	$1195	6/08
Central Marketing Advisors Inc.	$995	07/08
Exclusive Marketing Inc.	$995	07/08
Fireside Developments Inc.	$995	07/08
Waterway Creations Inc.	$995	07/08
5 Star Business Concepts Inc.	$895	09/08
Freestyle Creations LLC	$895	10/08
Daybreak Solutions, Inc	$895	11/08
Elite Marketing Strategies Inc	$895	11/08
GoGreen Enterprises LLC	$895	12/08
Golden Sun Innovations LLC	$895	12/08
Direct Business Developments Inc	$795	1/09

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Aged Corporations

Colorado	Price	Date Formed
Ace Consulting Services, LLC	$1295	12/07
Ace Enterprise Investments LLC	$1295	12/07
American Acquisitions Limited	$1295	12/07
Bright Light Consulting LLC	$1295	12/07
Controlled Systems Inc.	$1295	12/07
Digital Management Services Corp.	$1295	12/07
Fidelity Associates LLC	$1295	12/07
Green Strategies Corp.	$1295	12/07
Accustom Industrial LLC	$1295	12/07
Leasing Technologies Corp.	$1295	12/07
Great West Marketing Inc.	$995	2/08
Central Consulting Corp.	$895	3/08
Concept Creations Corp.	$895	3/08
Eastern Developments LLC	$895	3/08
Lightning Services LLC	$895	3/08
Rock Solid Funding, Inc.	$895	4/08
Ace Imaging Services, LLC	$895	4/08
Arlington Funding Group, Inc.	$895	4/08
Hole-In-One Leasing, LLC	$895	4/08
Palimino Designs, LLC	$895	4/08
Solutions 4 Less, Inc.	$895	4/08
Tumbleweed Creations, Inc.	$895	4/08
Worldwide Developments, LLC	$895	4/08
Enterprise Management Group LLC	$895	6/08
Freedom Development Inc.	$895	6/08
Gone Green Inc.	$895	6/08
Grandview Management LLC	$895	6/08
Ideal Solutions Inc.	$895	6/08
Techstrom LLC	$895	6/08

Connecticut	Price	Date Formed

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Eastern Developments LLC	$895	4/08
Intelligent Enterprises LLC	$895	4/08
Concept Creations Corp.	$1495	4/08
Central Consulting Corp.	$1495	5/08
Superior Marketing, Inc.	$1495	5/08
Falling Cactus LLC	$895	6/08

Delaware	Price	Date Formed
Entertainment Enterprise Company LLC	$1895	8/07
Solutions for Sure Inc.	$1895	8/07
Management Services Center LLC	$1795	9/07
Coastal Acquisitions Corp.	$1795	9/07
Commercial Marketing Services Inc.	$1795	9/07
Decisive Marketing Concepts Corp.	$1795	9/07
Leasing Pro Corp.	$1795	9/07
Rock Solid Leasing Corp.	$1795	9/07
Sixshooter Financial Group Inc.	$1795	10/07
Tumbleweed Investments Corp.	$1795	10/07
Landsdawne Solutions Inc.	$1795	10/07
McLeod Partners Limited	$1795	10/07
Raindance Leasing Incorporated	$1795	10/07
Ace Investment Company Inc.	$1695	12/07
Central Services Solutions LLC	$1695	12/07
Digital Designs International Corp.	$1695	12/07
Ideal Building Solutions LLC	$1695	12/07
Investigative Systems Corp.	$1695	12/07
Unity Management Services LLC	$1695	12/07
Affiliate Air, LLC	$995	5/08
Hexagon Lake, LLC	$995	5/08
Hollywood Affiliates, LLC	$995	5/08
#1 Superior Homes, Inc.	$995	5/08
Broadband Specialty Company, Inc.	$995	5/08
Coin Air Enterprises Inc.	$995	5/08
Specialty Productions Corporation	$995	5/08

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Aged Corporations

Ace Marketing Inc.	$995	6/08
European Enterprises Inc.	$995	6/08
Hilltop Marketing Inc.	$995	6/08
Grand Energy Incorporated	$995	6/08
Wealth Marketing Incorporated	$995	9/08
Independent Marketing Solutions LLC	$995	9/08
Golden Technologies LLC	$995	9/08
Peak Funding Group LLC	$895	12/08
Capital City Developments LLC	$895	12/08
Advisory Trading Group Inc	$895	12/08
Divine Solutions Inc	$895	12/08
Florida	**Price**	**Date Formed**
Advanced Developments Intl LLC	$1895	8/07
Advantage Leasing & Development LLC	$1795	9/07
World Running Management Corp.	$1795	9/07
Palomino Consulting Group LLC	$1795	10/07
Palasades Management Group Inc.	$1795	10/07
Arlington Associated Partners Inc.	$1795	12/07
Berry Acres Industries LLC	$1795	12/07
Columbia Industrial Products Inc.	$1795	12/07
Commercial Property Partners LLC	$1795	12/07
Fidelity Capital Investments LLC	$1795	12/07
Investigative Solution Specialists Inc.	$1795	12/07
Breeze Consultants LLC	$1795	12/07
American Capital Investments Lmtd. Corp.	$1795	12/07
Key Developments, LLC	$1495	2/08
AAA Property Holdings, Inc.	$1395	3/08
Freedom Creations	$1195	5/08
Jubilee Advisors Inc.	$1195	5/08
Mainstay Marketing Inc.	$1195	5/08
Shape Up Innovations Inc.	$1195	5/08
Southland Management Services Inc.	$1195	5/08

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Aged Corporations

Fast Forward Networks LLC	$1195	5/08
Hilltop Creations LLC	$1195	5/08
Spring Creek Management Group, LLC	$1195	5/08
Sunset Innovations, LLC	$1195	5/08
Mutual Developments LLC	$1195	5/08
Unified Management Services	$1195	6/08
Weblink Technologies, LLC	$1195	6/08
Comtech Data LLC	$1195	6/08
Audio Data Services Inc.	$1195	6/08
Advanced Global Concepts LLC	$1195	6/08
5 Star Business Management Inc.	$1195	6/08
Trendy Solutions Inc	$1195	10/08
Vibe Business Concepts LLC	$1195	10/08
Center Stage Marketing LLC	$1195	11/08
Rustic Designs Inc	$1195	11/08
Daily Concepts LLC	$1095	12/08
Golden Sun Concepts LLC	$1095	12/08
Central Innovations Inc	$1095	12/08
Adobe Developments Inc	$1095	12/08
Central Networking Corp	$1095	12/08
Pro Image Innovations LLC	$1095	12/08
Georgia	**Price**	**Date Formed**
Bottom Line Investments Corp.	$1495	12/07
Capital Supply Company LLC	$1495	12/07
Cascade Custom Services Inc.	$1495	12/07
Common Ground Management Inc.	$1495	12/07
Common Ground Services LLC	$1495	12/07
Digital One Company LLC	$1495	12/07
Idea Marketing LLC	$1495	12/07
Investigative Technologies Inc.	$1495	12/07
Central Consulting Corp.	$1095	3/08
Intelligent Enterprises, LLC	$1095	3/08
Lightning Services, Inc.	$1095	3/08

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Aged Corporations

[redacted]

Eagle Eye Services LLC	$1095	3/08
Sequoyah Creations LLC	$995	5/08
Sugar Creek Solutions LLC	$995	5/08
Take Time Innovations LLC	$995	5/08
Big Red Technologies LLC	$995	5/08
Budget Marketing Services Inc.	$995	5/08
Fire & Ice Management Group LLC	$995	5/08
Oak Mountain Innovations Inc.	$995	5/08
Eagle Energy Group Inc.	$995	6/08
Capital Imaging LLC	$895	9/08
Choice Funding Inc	$895	9/08
Fundtech Distributing LLC	$895	9/08
Hawaii	**Price**	**Date Formed**
Business Ventures Inc.	$1295	12/07
Unique Solutions Inc.	$1295	12/07
Advanced Management Solutions Corp.	$1295	12/07
Sage Holding Company Inc.	$1295	12/07
Investigative Resources LLC	$1395	12/07
Preferred Solutions LLC	$1395	12/07
Sea Quest Ventures LLC	$1395	12/07
Wellington Fund	$1195	2/08
Key Developments LLC	$1195	2/08
Premier Service Group Inc.	$1195	2/08
Brook Ventures, Inc.	$895	5/08
Brown Research LLC	$895	5/08
Better World Technologies, Inc.	$895	6/08
Net Direct LLC	$895	6/08
Idaho	**Price**	**Date Formed**
Fidelity Leasing Systems Inc.	$1495	12/07
Concept Marketing Corp.	$1095	3/08
Great West Marketing, Inc.	$1095	3/08

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Aged Corporations

[redacted]

Concept Guardins Corp.	$995	4/08
Eagle Eye Development	$995	4/08
Intelligent Enterprises LLC	$995	4/08
Crowne World Inc.	$995	5/08
Executive Empire LLC	$995	5/08
Green Creations LLC	$995	6/08
Prime Business Solutions Inc.	$995	6/08

Illinois	Price	Date Formed
Bionic Services Inc.	$2295	12/07
Bright Future Systems Inc.	$2295	12/07
AAA Property Holdings Inc.	$2295	2/08
Key Developments LLC	$2395	2/08
Aquarius Designs LLC	$1995	5/08
Crown Management Services LLC	$1995	5/08
Daisy Creations LLC	$1995	5/08
Desoto Management LLC	$1995	5/08
Spring Bay Affiliates LLC	$1995	5/08
Key Creations Inc.	$1295	5/08
Mainstay Solutions Inc.	$1295	5/08
Trinity Creations Inc.	$1295	5/08
Waterway Marketing Inc.	$1295	6/08
Wealth Marketing Services LLC	$1995	6/08
Advantage Capital Ventures Inc.	$1095	7/08
Unified Management Services, Inc.	$1095	7/08

Indiana	Price	Date Formed
Central Consulting Corp.	$1095	3/08
Eastern Enterprises, LLC	$1095	3/08
Eagle Eye Services LLC	$1095	3/08
Lightning Services, Inc.	$1095	3/08
Capital Supply, LLC	$1095	5/08
Echo Administration Group, Inc.	$1095	5/08

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Aged Corporations

[redacted]

Freedom Enterprises, LLC	$1095	5/08
Summit Systems, Inc.	$1095	5/08
Master Development LLC	$995	6/08
Polar Star Development Inc.	$995	7/08

Iowa	Price	Date Formed
Concept Creations Corp	$995	4/08
Eagle Eye Services, LLC	$995	4/08
Lightning Services LLC	$995	4/08
Intelligent Enterprises LLC	$995	4/08
Dream Markets, Inc.	$995	5/08
Golden Movements LLC	$995	5/08
Green Solutions Inc	$695	1/09

Kansas	Price	Date Formed
Services Solutions Group Inc.	$1295	12/07
Central Consulting Corp.	$1095	3/08
Concept Creations Corp.	$1095	3/08
Eastern Developments LLC	$1095	3/08
Intelligent Enterprises, LLC	$1095	3/08
Familink Distributions, Inc.	$895	5/08

Kentucky	Price	Date Formed
Central Consulting Corp.	$995	3/08
Concepts Creations Corp.	$995	3/08
Intelligent Enterprises LLC	$995	3/08
Eagle Services, LLC	$995	3/08
Loud Enterprises, Inc.	$995	5/08
Red Bird Distributing, LLC	$995	5/08
Commerce Capital Enterprises, LLC	$995	5/08
Alabaster Ventures, Inc.	$995	5/08
Accurate Marketing Strategies LLC	$895	7/08
Commerce Capital Group Inc.	$895	7/08

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Professional Concepts LLC	$895	7/08
Louisiana	**Price**	**Date Formed**
Enterprises Services LLC	$1395	12/07
System Consultants, LLC	$1395	12/07
Techno One LLC	$1395	12/07
Technology Connections Corp.	$1395	12/07
Technology Ventures Inc.	$1395	12/07
The Marketing Advantage Corp.	$1395	12/07
Unlimited Systems LLC	$1395	12/07
All Sports Marketing Inc.	$895	5/08
Fireside Capital, LLC	$895	5/08
Brandini Marketing Inc/	$895	5/08
Conescere, Inc.	$895	5/08
Connective Network LLC	$895	6/08
Superior Development Services Inc.	$895	6/08
Maine	**Price**	**Date Formed**
Eagle Eye Services, LLC	$1195	5/08
Intelligent Enterprises, LLC	$1195	5/08
Ace Archer LLC	$1195	5/08
Commercial Trading LLC	$1195	6/08
5 Star Imaging, Inc.	$995	7/08
Cactus Cajin, Inc.	$995	7/08
Concept Creations Corp	$995	7/08
Lighting Services, Inc.	$995	7/08
Maryland	**Price**	**Date Formed**
Capital Energy Group Inc.	$1695	5/08
Freedom Capital Inc.	$1595	06/08
Massachusetts	**Price**	**Date Formed**

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Aged Corporations

Premier Service Group Inc.	$1995	2/08
Key Developments LLC	State pending	2/08
Heartland Creations LLC	$1895	6/08
Majestic Solutions LLC	$1895	6/08
Next Generations Advisors LLC	$1895	6/08
Quality 1 Advisors LLC	$1895	6/08
Michigan	**Price**	**Date Formed**
Amazon Holdings Corp.	$1495	8/07
Advantage Capital Investments LLC	$1495	8/07
5 Star Technical Services LLC	$1395	9/07
Integrated Marketing Techniques Inc.	$1395	9/07
Kingsbury Investment Group Inc.	$1395	10/07
McKinley Ventures Group LLC	$1395	10/07
Enterprise Systems Pros Inc.	$1295	12/07
The Consulting Company	$1295	12/07
Golden Horizon Administrations, Inc.	$995	5/08
Riverbend Marketing, Inc.	$995	5/08
Spring Mountain Solutions, Inc.	$995	5/08
Raindance Enterprises, Inc.	$995	5/08
Daisy Creek Services, LLC	$995	5/08
Sequoyah Enterprises, LLC	$995	5/08
Spring Creek Solutions, LLC	$995	5/08
Hilltop Technologies LLC	$995	5/08
Direct One Marketing Inc.	$895	6/08
Opulent Marketing LLC	$895	6/08
Red River Developments LLC	$895	6/08
Redline Funding LLC	$895	6/08
Jubilee Services Inc.	$895	6/08
Sterling Management Group Inc.	$895	6/08
Minnesota	**Price**	**Date Formed**
21st Century Management Corp	$1595	8/07

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Aged Corporations

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Advanced Energy Tech LLC	$1495	9/07
Bittersweet Financial Corp.	$1495	9/07
Lincoln Financial Solutions LLC	$1495	10/07
Waterford Management Inc.	$1595	10/07
American Industries Inc.	$1395	12/07
Masterpiece Industries LLC	$1395	12/07
Key Developments LLC	$1295	2/08
Commercial Services Inc.	$1295	3/08
Amazon Imaging Inc.	$1295	4/08
Atlantic Leasing Corp.	$1295	4/08
Decisive Designs LLC	$1295	4/08
Green Arbor Technologies, LLC	$1295	4/08
One Key Marketing Inc.	$1295	4/08
Aiva Enterprises Inc.	$1295	6/08
Green Home Association LLC	$1295	6/08
Ideal Management Inc.	$1295	6/08
Investigative Solutions LLC	$1295	6/08
Mississippi	**Price**	**Date Formed**
Investment Capital Services Inc.	$1295	12/07
Management Assets LLC	$1255	12/07
Principal Enterprises LLC	$1295	12/07
Capital Advantages Inc.	$1295	12/07
Technology Management Services Inc.	$1295	12/07
Peak Professionals Inc.	$995	5/08
Grand Solutions LLC	$995	5/08
Advanced Trading LLC	$995	6/08
Ace Enterprises Inc.	$995	6/08
Missouri	**Price**	**Date Formed**
Accelerated Marketing Group LLC	$1495	8/07
Little Valley Properties LLC	$1395	9/07
American Development Services Corp.	$1395	10/07

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Aged Corporations

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Glendale Ventures Inc.	$1395	10/07
Huntington Marketing Group LLC	$1395	10/07
First Class Systems LLC	$1395	12/07
Corporate Investments Inc.	$1395	12/07
Corporate Management Advisors Corp.	$1395	12/07
Creative Control Systems Inc.	$1395	12/07
Corporate Advisors LLC	$1295	4/08
Cascade Custom Developments Inc.	$1095	5/08
Five Star Advisors Inc.	$1095	5/08
Husky Ventures LLC	$995	6/08
Tri-Star Solutions LLC	$995	6/08
Gold Star Leasing Inc.	$995	6/08
Global Affiliates Group, LLC	$995	6/08
Mountain West Management Inc.	$995	6/08

Montana	Price	Date Formed
Prestigious Enterprises Inc. (With EIN)	$2195	12/07
Sundown Ventures Inc. (With EIN)	$2195	12/07
Taurus Enterprises Inc. (With EIN)	$2195	12/07
Crane Cycling Products, Inc. (With EIN)	$1895	5/08
Lucky Gene, LLC	$995	5/08
Red Eagle Enterprises, LLC	$995	5/08
Sutton Management Services, Inc. (With EIN)	$1895	5/08

Nebraska	Price	Date Formed
Service Associates LLC	$1195	12/07
Technical Solutions Inc.	$1195	12/07
Cactus Falls, LLC	$1095	5/08
Cactus Enterprises, Inc.	$1095	5/08
Absolute Technology Corporation	$995	6/08

New Hampshire	Price	Date Formed
Sterling Intelligent Technologies, Inc.	$1195	7/08

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Aged Corporations

The Tech-Com Technology Services LLC	$1195	8/08
Falcon Creations LLC	$895	12/08
Falcon Business Services Inc	$895	1/09
New Jersey	**Price**	**Date Formed**
A1 Service Solutions LLC (With EIN)	$2495	12/07
Advanced Resource Solutions Inc.	$2195	12/07
1st Choice Leasing, LLC (With EIN)	$1995	4/08
Eagle Eye Enterprises, LLC (With EIN)	$1995	4/08
Freedom Marketing Advisors, LLC (With EIN)	$1995	4/08
Jubilee Marketing Corporation (With EIN)	$1995	4/08
Key Creations Corporation (With EIN)	$1995	4/08
Spring Management Corp. (With EIN)	$1995	4/08
Concrete Marketing Corp. (With EIN)	$1995	6/08
Metro Technologies LLC (With EIN)	$1995	6/08
New Mexico	**Price**	**Date Formed**
Global Resources LLC	$1195	12/07
Lightning Services, LLC	$895	5/08
Alpha Industrial Services, LLC	$895	5/08
Creekside Marketing LLC	$895	5/08
Falcon Designs LLC	$895	5/08
Dhaven Movements, LLC	$895	5/08
Advanced Consulting LLC	$895	5/08
Eastern Developments LLC	$895	5/08
Intelligent Enterprises, LLC	$895	5/08
Tech Service Solutions LLC	$895	5/08
Anomaly Company, LLC	$895	5/08
Border Technology LLC	$895	5/08
Concept Creations Corp.	$995	5/08
Falcon Hill Corporation	$995	5/08
Falling Waters Inc.	$995	5/08
Glass Rose Inc.	$995	5/08

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Global Marketing Group Inc.	$995	5/08
Great West Marketing Inc.	$995	6/08
Tech Management Services Inc.	$995	6/08
Beneficial Business Solutions LLC	$895	6/08
North Star Developments LLC	$895	6/08
Technology Services Corporation	$995	7/08
TechPro Services LLC	$895	7/08
Tristar Marketing LLC	$895	7/08
Elemental Technologies LLC	$795	11/08
Newport Enterprises	$995	11/08
Priority Systems LLC	$795	11/08
Triad Leasing LLC	$795	11/08
Kaplan Advisors LLC	$695	12/08
Milestone Creations LLC	$695	12/08
Key Networking LLC	$695	12/08
Ameritech Enterprises LLC	$695	12/08
General Imaging Group LLC	$695	12/08
National Cornerstone Developments LLC	$695	12/08
Paramount Funding Group Inc	$695	12/08
Specialized Marketing Inc	$695	12/08
5 Star Developments Inc	$595	1/09

New York	Price	Date Formed
A+ Property Management LLC	$2395	9/07
Management Team Incorporated	$2395	9/07
Maritime Security Group LLC	$2295	12/07
Telecom Tech Solutions Inc.	$2295	12/07
Global Spectrum Inc.	$2295	12/07
Global Tech Systems Inc.	$2295	12/07
Prime Network Services, LLC	$1895	09/08
Daily Marketing Advisors Inc.	$1695	09/08
Fidelity Marketing Inc.	$1695	09/08
Living Green Inc.	$1695	09/08
ProData Systems Inc.	$1695	09/08

Aged Corporations

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United Advisors Inc.	$1695	09/08
Unlimited Innovations Inc.	$1695	09/08
Keepsake Enterprises LLC	$995	12/08
Omega Innovations LLC	$995	12/08
Accelerated Innovations Inc	$895	12/08
Common Ground Marketing Inc	$895	12/08
Corporate Marketing Solutions Inc	$895	12/08
Direct One Enterprises, Inc	$895	12/08
Edgewood Trading Inc	$895	12/08
Fourway Marketing Inc	$895	12/08
Valley Trading Group Inc	$895	12/08
Willow Bend Solutions Inc	$895	12/08
Worldwide Imaging Inc	$895	12/08
Central Networking Group Inc	$895	12/08
Golden Eagle Marketing LLC	$795	1/09
North Carolina	**Price**	**Date Formed**
Global Sourcing Insights, Inc	$1395	12/07
Global Spectrum LLC	$1395	12/07
N.C. Corporate Resources, Inc.	$1395	12/07
Apollo Marketing Services, Inc.	$1195	5/08
Hilltop Solutions Inc.	$1195	5/08
Blue Acre Development, LLC	$1195	5/08
Hillcrest Advisors Group LLC	$1195	5/08
Above-All Innovations Inc.	$1095	6/08
Gone Green Ventures, LLC	$1095	6/08
Triple A Management Inc.	$1095	6/08
Investigative Marketing LLC	$1095	6/08
Daily Marketing Advisors Inc	$995	9/08
Fidelity Marketing Inc	$995	9/08
Living Green Inc	$995	9/08
ProData Systems Inc	$995	9/08
United Advisors Inc	$995	9/08
Unlimited Innovations Inc.	$995	9/08

Aged Corporations

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North Dakota	Price	Date Formed
Elite Concepts, LLC	$1095	6/08
Simple Solutions, Inc.	$1095	6/08

Ohio	Price	Date Formed
Central Consulting Corp.	$1195	4/08
Concept Creations Corp.	$1195	4/08
Intelligent Distributing Corporation	$1095	5/08
King Creations, LLC	$1095	5/08
Silver Eagle Enterprises, LLC	$1095	5/08
Hertfordshire Developments, LLC	$1095	5/08
Golden Eagle Enterprises LLC	$1095	5/08
Intelligent Enterprises LLC	$1095	5/08
Kruse Imaging LLC	$995	9/08
Alpha Network Services Inc	$995	9/08
Wisteria Technologies LLC	$895	11/08

Oklahoma	Price	Date Formed
United Marketing Technologies Inc. with ein	$1695	12/07
Voice Tech Systems Inc. with ein	$1685	12/07
Key Developments LLC with ein	$1295	2/08
Performance Plan, LLC with ein	$1295	5/08

Oregon	Price	Date Formed
Consultants That Care LLC	$1495	8/07
First Choice Services LLC	$1395	9/07
The Ambrose Group Inc.	$1395	9/07
Worldwide Asset Management Inc.	$1395	9/07
Fairview Marketing LLC	$1295	10/07
The Glendale Group Inc.	$1295	10/07
Green Creations Inc.	$1295	12/07

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Aged Corporations

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A-Tek Computer Services LLC	$1295	12/07
Apex Holdings LLC	$1295	12/07
Bedford Property Management Inc.	$1295	12/07
Blue Knights Inc.	$1295	12/07
Net-Tech Inc.	$1295	12/07
Premier Coastal Properties LLC	$1295	12/07
Prime Property Management Inc.	$1295	12/07
Athena Professionals LLC	$1095	5/08
Business Dreams, LLC	$1095	5/08
Citrus Ventures, LLC	$1095	5/08
E-Soft Developers LLC	$1095	5/08
Eagle Plus Corporation	$1095	5/08
Fresh Futures, LLC	$1095	5/08
Iron Services Group, Inc.	$1095	5/08
Rapid Mountain Corporation	$1095	5/08
South East Trading Company Inc.	$1095	5/08
Grand Viking Distribution Inc.	$1095	5/08
Elite Business Solutions Inc.	$995	6/08
Gold Star Leasing LLC	$995	6/08
Ideal Dynamics LLC	$995	6/08
Master Distribution Corporation	$995	6/08
Apex Enterprises LLC	$795	09/08
Central Service Solutions LLC	$695	12/08
Valley Marketing Solutions LLC	$695	12/08
Pennsylvania	**Price**	**Date Formed**
Central Development Partners Inc.	$1495	12/07
Design Service Group Corp.	$1495	12/07
Desperado Enterprises LLC	$1395	12/07
Fabulous Enterprises LLC	$1395	12/07
Global Assets Group Inc.	$1495	12/07
Destination Discovery, Inc.	$1395	12/07
Waterway Systems, Inc.	$1095	5/08
Grand Atlantic Solutions, Inc.	$1095	5/08

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Aged Corporations

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Spin City Creations Inc.	$1095	5/08
Global Networking Inc.	$995	6/08
North Point Developments LLC	$995	6/08
South Carolina	**Price**	**Date Formed**
Global Capital Funding LLC	$1495	12/07
Unlimited Outsourcing Inc.	$1395	1/08
Northeastern Global Enterprises LLC	$1095	10/08
South Dakota	**Price**	**Date Formed**
Advanced Resources LLC	$1595	8/07
Advantech Corp.	$1595	8/07
Absolute Home Solutions LLC	$1495	9/07
American Property Partners Inc.	$1495	10/07
Burkitt Leasing LLC	$1495	10/07
Burrows Enterprises Inc.	$1495	10/07
Advisory Consultants LLC	$1395	12/07
Advocate Properties LLC	$1395	12/07
Capital City Investments Inc.	$1395	12/07
Computech LLC	$1395	12/07
Face Forward Technologies Inc.	$1395	12/07
Facilitech LLC	$1395	12/07
Facilities Management LLC	$1395	12/07
Design Specialties LLC	$1395	12/07
Destiny Center Inc.	$1395	12/07
Facilities Management LLC	$1395	12/07
Design Specialties LLC	$1395	12/07
Destiny Center Inc.	$1395	12/07
Global Funding Sources Corp.	$1395	12/07
Net-Tec LLC	$1395	12/07
Outsourcing Resources Inc.	$1395	12/07
TechAmerica Inc.	$1395	12/07
Worldwide Funding Corp.	$1395	12/07

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Aged Corporations

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Concept Creations Corp.	$1095	3/08
Eastern Enterprises LLC	$1095	3/08
Eastern Developments LLC	$1095	3/08
Lightning Services LLC	$1095	3/08
Ace Laboratories, Inc.	$995	5/08
Empire Energy Group, Inc.	$995	5/08
Red Eagle Enterprises, LLC	$995	5/08
Golden Energy Group LLC	$995	5/08
Accent Marketing Inc.	$895	6/08
Creative Concepts Inc.	$895	6/08
Intelligent Technologies LLC	$895	6/08
Preferred Services LLC	$895	6/08
Divine Creations Inc	$795	12/08
Digital Concepts Inc	$795	12/08
Advanced Marketing Concepts LLC	$795	12/08
Ideal Concepts LLC	$795	12/08

Tennessee	Price	Date Formed
2 B Marketing LLC	$2795	8/07
Access Management Corp.	$1895	8/07
Administrative Solutions Inc.	$1895	9/07
Capital Investment Properties LLC	$2695	9/07
Stagecoach Ventures Group LLC	$2695	10/07
Yalecrest Investments Inc.	$1995	10/07
Blazer Financial Services LLC	$2695	12/07
Colonial Care Services Inc.	$1495	12/07
General Management, Inc.	$1495	12/07
Sunset Community Development Inc.	$1495	12/07
A Plus Marketing Ventures, Inc.	$1295	5/08
Advanced Innovations LLC	$1595	5/08
Bottom Line Funding Group LLC	$1595	5/08
Can This Be Your Dream Creations, LLC	$1595	5/08
Digital Resources, LLC	$1595	5/08
Hillcrest Enterprises Inc.	$1095	5/08

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Aged Corporations

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Seagate Developments Inc.	$1095	5/08
Seagate Enterprises Inc.	$1095	5/08
Choice Enterprises Inc.	$1095	6/08
Unified Management Services LLC	$1395	6/08
Texas	**Price**	**Date Formed**
Windsor Creek, Inc **(with EIN)**	$9995	12/91
Pecantree Apartments, Inc **(with EIN)**	$8995	7/95
Walnut Villa Apartments, LLC **(with EIN)**	$7995	2/97
Walnut Villa Apartments 1, Inc **(with EIN)**	$6995	3/98
TechPro Computers Inc.	$1795	12/07
Vet-Tech Inc.	$1795	12/07
Ballie Leasing Incorporated	$1295	9/08
Summerfield Creations LLC	$1295	9/08
Atlantis Imaging Inc	$1195	10/08
Class Act Solutions Inc	$1195	10/08
Masterpiece Marketing LLC	$1195	10/08
Utah	**Price**	**Date Formed**
Contact America LLC	$1495	8/07
Continental Eagle Corp.	$1495	8/07
Advanced Energy Systems Corp.	$1295	9/07
Spaulding Financial Services Inc.	$1195	10/07
Community Associates LLC	$1195	12/07
Enterprise Productions LLC	$1195	12/07
Equitable Management LLC	$1195	12/07
Equity Resolutions, Inc.	$1195	12/07
Equity Risk Services LLC	$1195	12/07
The Funding Partners, Inc.	$1195	12/07
FundTech LLC	$1195	12/07
General Partnership, Inc.	$1195	12/07
Partnership Enterprises, Inc.	$1195	12/07
Prime Property Services, Inc.	$1195	12/07

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Aged Corporations

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Craft Corporation	$895	5/08
Creative Opportunities LLC	$895	5/08
Wise Professionals LLC	$895	5/08
Smart Technologies Inc.	$895	5/08
Digital Strategies Inc.	$895	6/08
5 Star Services LLC	$895	6/08
Clear Lake Enterprises LLC	$895	6/08
Pine Butte Services, Inc.	$895	6/08
Clover Networking Inc	$695	12/08
Elite Distribution Services LLC	$695	12/08
Valmont Leasing LLC	$695	12/08
Wellington Business Ventures Inc	$695	12/08
Telecom Dynamics LLC	$695	12/08

Virginia	Price	Date Formed
U Dream Management LLC	$1395	12/07
Capital City Investors LLC	$1395	12/07
Coach Administrations, Inc.	$1095	4/08
Greenlight Solutions, Inc.	$1095	4/08
Lighthouse Advisors Inc.	$1095	4/08
Kingsbury Systems LLC	$1095	4/08
Power of Now Marketing, LLC	$1095	4/08
Apollo Marketing Advisors LLC	$1095	4/08
Net Direct Marketing LLC	$995	6/08
Canyon Enterprises Inc.	$995	6/08

Washington	Price	Date Formed
Advocate Center LLC	$1495	12/07
Advisors Mutual, Inc.	$1495	12/07
Technical Products Group LLC	$1495	12/07
Techshare Marketing Inc.	$1495	12/07
Great West Marketing Inc.	$1395	2/08
A+ Affiliates, Inc. (With EIN)	$1695	5/08

Aged Corporations

Advanced Marketing Group Inc. (With EIN)	$1695	5/08
Blaze Holding Company, LLC (With EIN)	$1695	5/08
Echo Innovations Inc. (With EIN)	$1695	5/08
Fabulous Solutions, LLC (With EIN)	$1695	5/08
Heartland Marketing LLC (With EIN)	$1695	5/08
Central Key Innovations LLC	$1095	6/08
Direct Solutions Inc.	$1095	6/08

Wisconsin	Price	Date Formed
Advisory Consultants LLC	$1195	12/07
Marketing Advantage LLC	$1195	12/07
Commercial Funding Group, Inc.	$1095	4/08
Fidelity Direct Leasing, LLC	$1095	4/08
Five Star Management, Inc.	$1095	4/08
NetTech LLC	$995	6/08
Prime Time Management, Inc.	$995	6/08
Wyoming	**Click here for separate list**	

Wyoming Aged Corporations

Name of Company	Cost	Inc. Date
Elite Consulting Group Inc. with EIN and 4 years tax returns	$5895	5/2004
Blackjack Investments Inc. with EIN	Sale pending	9/2004
Brookside Management Inc.	Sale pending	12/2004
BestGlo Corp.**with EIN- S-Corp**	$4295	9/2005
Prime Systems **with EIN**	$4295	9/2005
Capital Mortgage Inc. **(with EIN)**	$3295	9/2006
Mid- America Credit Services Inc.	$2795	10/2006
Film Management Inc.	$2495	1/2007
No Strings Attached, Inc.	$2195	2/2007
Executive Estate Planning, Inc.	$2195	2/2007

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Aged Corporations

Preferred Investment Tools, Inc	$2195	2/2007
Master Asset Management, Inc.	$2195	2/2007
Designed Entity Concepts, Inc.	$2195	2/2007
Foreign Trade & Marketing, Inc.	$2195	2/2007
Global Village Advertising, Inc.	$2195	2/2007
Marketing Experts Inc.	$2095	3/2007
Corporate Travel Consultants, Inc.	$2095	3/2007
Financial Analysis Corp	$2095	3/2007
Estate Management, Inc.	$2095	3/2007
Data Capital Corp.	$2095	3/2007
Strategic Marketing Solutions, Inc.	$2095	3/2007
Financial Advantages, Inc.	$1995	4/2007
Finance & Investment Corp.	$1995	4/2007
United Accounting Systems Inc.	$1895	5/2007
Elite Security Services, Inc.	$1895	5/2007
Capital Network Systems, Inc.	$1895	5/2007
Advanced Network Services, Inc.	$1895	5/2007
Aken Financial, Inc.	$1895	5/2007
Enhanced Advertising Inc.	$1895	5/2007
The Under Takers, Inc	$1895	5/2007
United Global Network Inc.*	$1795	6/2007
Washington Mortgage Corp.	$1795	6/2007
Global Funding Enterprises, Inc.	Sale pending	6/2007
Life's Little Pleasures, Inc.	$1795	6/2007
Adminassist, Inc	$1795	6/2007
In A Breeze Technologies, Inc.	$1795	6/2007
Fresh Start Therapy, Inc.	$1795	6/2007
Communication Innovation Corporation	$1795	6/2007
Professional Business Management Corp.	$1795	6/2007
Grand Freedom Marketing, Inc	$1795	6/2007
PlanTech Productions, Inc	$1795	6/2007
Communications Task Group Incorporated	$1695	7/2007
Quick Fix Productions Inc.	$1695	7/2007
Corporate Accelerators Inc.	$1695	7/2007
Consumer Services, Inc.	$1595	8/2007
Applied Economics Inc.	$1595	8/2007
Artistic Designs Inc.	$1595	8/2007

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Aged Corporations

Applied Communications, Inc.	$1595	8/2007
Green Leasing, Inc.	$1595	8/2007
Economic Research, Inc.	$1595	8/2007
Share Resources Inc.	$1595	8/2007
Consolidated Capital & Leasing Corp.	$1495	9/2007
Clearview Properties, Inc.	$1495	9/2007
Dogwood Leasing Co., Inc.	$1495	9/2007
Buckingham Leasing Group, Inc.	$1395	10/2007
Sherwood Management Corp.	$1395	10/2007
Coventry Leasing, Inc.	$1395	10/2007
Krameria Management, Inc.	$1395	10/2007
Country Realty, Inc.	$1295	11/2007
Stanton Designs Inc.	$1295	11/2007
Accustom Artists, Inc.	$1295	11/2007
Alpha Power Services, Inc.	$1295	11/2007
Centurion Management Corp.	$1295	12/2007
A & B Investments, Inc.	$1295	12/2007
Technicare Systems Inc.	$1295	12/2007
Mutual Benefits Inc.	$1295	12/2007
Valley Investments Inc.	$1295	12/2007
International Bio Tech, Inc.	$1295	12/2007
Keepsake Capital Corporation	$1095	3/2008
JAZ Advertising, Inc.	$1095	3/2008
Regent Coating Inc.	$1095	3/2008
Redwood Services of Wyoming, Inc	$1095	3/2008
Garden Resources, Inc.	$1095	3/2008
1. Information Alliance Company	$995	4/2008
1. Northern Bay Systems Inc.	$995	4/2008
Center Capital Funding Group Inc.	$995	5/2008
Edge Capital Corp.	$995	5/2008
Adaptive Communications Inc.	$895	6/2008
Loyal Foods Inc. *	$895	7/2008
Escape Management, Inc.	$895	7/2008
Enhanced Technologies, Inc.	$895	7/2008
Deluxe Management Inc.	$895	8/2008
Extreme Opportunities Inc.	$895	8/2008
Dash Development Corp.	$895	9/2008

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Aged Corporations

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Buyers International Corp	$895	9/2008
Oregon Management Inc.	$895	9/2008
Impressive Services Inc.	$895	9/2008
Atlas Software Corp *	$795	10/2008
Enterprise Solution Corp*	$795	10/2008
Blazing Productions Inc.	$795	10/2008
Bizzare Investments Inc.	$795	10/2008
Burlington Accessories Inc.	$795	10/2008
Santa Fe Designs Inc.	$795	10/2008
U Dream Creations	$795	11/2008
First Choice Services Inc.	$795	11/2008
Suretech Marketing Inc.	$795	11/2008
Choice Services Inc.	$795	11/2008
Great West Management Services Inc.	$795	11/2008
Pro-Tech Systems Inc.	$795	11/2008
A Plus Marketing Inc.	$795	11/2008
Choice One Enterprises Inc.	$795	11/2008
Creative Funding Inc.	$795	12/2008
Treetop Developments Inc.	$795	12/2008
Access Business Group Inc.	$795	12/2008
Comtech Data Services Inc.	$795	12/2008
Hilltop Systems Inc.	$795	12/2008
Tumbleweed Marketing Inc.	$795	12/2008
Turion Technologies Inc.	$795	12/2008
Wintergreen Creations Inc.	$795	12/2008
Land Investor Inc	$695	1/2009
Effective Communications Inc.	$695	1/2009
Elegant Designers Inc.	$695	1/2009
Fundamental Resources Inc.	$695	1/2009
Ricchio Systems International	$695	2/2009
Infinite Funding, Inc.	$695	2/2009
Inside Resources, Inc.	$695	2/2009
Triumph Realty, Inc.	$695	2/2009
Upland Trading Corp	$695	2/2009
Inside Professionals, Inc.	$695	2/2009
Vivid Distribution Center	$595	3/2009
Aiva Corporation	$595	3/2009

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Aged Corporations

Americana Communications Inc.	$595	3/2009
Peak Arbor Designs Inc.	$595	3/2009
Simple Breeze Innovations Inc.	$595	3/2009
Rustic Developments Inc.	$595	3/2009
Superior Enterprises Inc.	$595	3/2009
Trans Service Corp	$595	3/2009
Unlimited Developments Inc.	$595	3/2009
Waterford Marketing Corp	Sale pending	3/2009
Euro Marketing Solutions Inc	$595	4/2009
Trinity Advisors Corp	$595	4/2009
Biotech Systems Inc	$595	4/2009
GP Technologies Inc	$595	4/2009
Universal Health Care Corp	$595	4/2009
Aqua Design Studio Inc	$595	4/2009
Virtual Home Designs Inc	$595	4/2009
Midwest Developments Corp	$595	4/2009
Keystone Financial Group Inc	$595	4/2009
Strategic Home Solutions Inc	$595	4/2009
American Marketing Advisors Corp	$595	4/2009
Wyoming Aged LLC's	**Price**	**Date Formed**
Wiman Trading Partners, LLC *	$5395	5/2004
United Distribution, LLC	$3295	12/2006
Travel Connections, LLC	$2495	1/2007
Political Researchers, LLC	$2495	1/2007
Data Direct Systems, LLC	$2395	2/2007
Advanced Communication Solutions, LLC	$2395	2/2007
Wyoming Financial Advisors, LLC	$2395	2/2007
Marketing Design Works, LLC	$2295	3/2007
WY-Telecommunications, LLC	$2295	3/2007
Internet Marketing Group, LLC	$2295	3/2007
Insite Research, LLC	$2295	3/2007
Institute of Estate Planning, LLC	$2295	3/2007
Hidden Lake Estates, LLC	$2295	3/2007
Real Marketing LLC	$2295	3/2007
Matrix Leasing, LLC	$2195	4/2007
National Mortgage Group, LLC	$2195	4/2007
Chartered Services, LLC	$2195	4/2007

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Aged Corporations

Integrated Technology Systems, LLC	$2195	4/2007
Graphic Designers, LLC	$2095	5/2007
Property Researchers, LLC	$2095	5/2007
Mountain View Holdings, LLC	$2095	5/2007
Creative Internet Designs, LLC	$2095	5/2007
Internet Solutions, LLC	$2095	5/2007
Worldwide Travel, LLC	$2095	5/2007
Property Development LLC	$2095	5/2007
Tectonics LLC	$2095	5/2007
Another Chance, LLC	$2095	5/2007
Data Creations, LLC	$2095	5/2007
Valley Brook Properties LLC	$2095	5/2007
Final Frontier Properties LLC	$2095	5/2007
Property Management Pro's LLC	$1995	6/2007
The Firm Alternative LLC	$1995	6/2007
Better Group Holdings LLC	$1995	6/2007
Solid Investments LLC	$1995	6/2007
Funding4U, LLC	$1995	6/2007
Discovery Adventures LLC	$1995	6/2007
Market Center of Wyoming LLC	$1995	6/2007
Myenterprise, LLC	$1995	6/2007
YNOTU Advertising LLC	$1995	6/2007
Harbor Realtor's LLC	$1995	6/2007
Capital Asset Recovery LLC	$1995	6/2007
Extra Effort Marketing LLC	$1895	7/2007
Final Touch Solutions LLC	$1895	7/2007
Front Gate Properties, LLC	$1895	7/2007
Corporate Building Center LLC	$1895	7/2007
Quiet Corner Enterprises LLC	$1895	7/2007
Capital Formation Company LLC	$1895	7/2007
Foundation Concepts, LLC	$1895	7/2007
Regal Investment Trading, LLC	$1895	7/2007
Special Care LLC	$1795	8/2007
Melrose Meltdown LLC	$1795	8/2007
Members Only Entertainment LLC	$1795	8/2007
Memorial Care Center LLC	$1795	8/2007
Memory Makers Studios LLC	$1795	8/2007

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Aged Corporations

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Intertab Marketing LLC	$1795	8/2007
Integrated Leasing LLC	$1795	8/2007
Interior Impressions LLC	$1795	8/2007
Firm Leasing LLC	$1795	8/2007
Brownsville Leasing LLC	$1795	8/2007
Atlantic Financial Group LLC	$1795	8/2007
Peace Investment LLC	$1795	8/2007
Accelerated Marketing Group, LLC	$1695	9/2007
B & B Marketing Services LLC	$1695	9/2007
Blue Collar Management, LLC	$1695	9/2007
Coordinated Financial LLC	$1695	9/2007
Douglas Leasing LLC	$1695	9/2007
All Good Services, LLC	$1695	9/2007
Mulberry Ventures Group LLC	$1595	10/2007
Arrowhead Leasing Group LLC	$1595	10/2007
Fairview Marketing LLC	$1595	10/2007
Snowy Range Ventures LLC	$1595	10/2007
Ridgeview Marketing Group LLC	$1595	10/2007
Filmore Ventures Group LLC	$1595	10/2007
Warren Enterprising LLC	$1595	10/2007
Lakewood Leasing Group LLC	$1595	10/2007
The Morrison Group, LLC	$1595	10/2007
Langly Leasing Group, LLC	$1595	10/2007
Claymont Management LLC	$1595	10/2007
Pointe Financial Group LLC	$1595	10/2007
Aahee Marketing LLC	$1595	10/2007
Pawnee Leasing LLC	$1595	10/2007
China Services LLC	$1595	10/2007
Watkins Leasing LLC	$1595	10/2007
India Marketing Group LLC	$1595	10/2007
Cascade Data Marketing LLC	$1495	11/2007
Capital Supply LLC	$1495	11/2007
Central Equip Services LLC	$1495	11/2007
EquipLeasing LLC	$1495	11/2007
Industrial Acceptance Co. LLC	$1495	11/2007
Universal Tech Investments, LLC	$1395	12/2007

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Aged Corporations

Enhanced Leasing LLC	$1395	12/2007
Western Movements LLC	$1395	12/2007
Peak Systems LLC	$1395	12/2007
Leasing Dynamics LLC	$1395	12/2007
A to Z Leasing LLC	$1395	12/2007
World Services Association LLC	$1395	12/2007
Better World Consulting LLC	$1395	12/2007
World Leisure LLC	$1395	12/2007
Red Oak Enterprises, LLC	$1395	12/2007
1st Investment Services, LLC	$1295	1/2008
The Profit Professionals LLC	$1195	2/2008
BondTech Distributing LLC	$1195	3/2008
Brown Research LLC	$1195	3/2008
Olive Research LLC	$1195	3/2008
New Generation Communications LLC	$1195	3/2008
Tengu Foods, LLC	$1195	3/2008
Summer Creek Developments, LLC	$1195	3/2008
1. Eastern Leasing LLC	$1095	4/2008
1. Eastern American Resources LLC	$1095	4/2008
1. Zigler Investments LLC	$1095	4/2008
1. Union Bay Management LLC	$1095	4/2008
Center Point Properties LLC	$995	5/2008
Research Technology Solutions LLC	$995	5/2008
Informational Concepts LLC	$995	5/2008
Beneficial Resource Management LLC	$995	5/2008
Direct Lending Associates LLC	$995	5/2008
Equable Communications, LLC	$995	5/2008
Foreign Exchange Partners LLC	$995	5/2008
Enhanced Funding, LLC	$895	7/2008
Burlington Developments, LLC	$895	7/2008
Rapid Deployment, LLC	$895	7/2008
Deluxe Properties LLC	$895	8/2008
Desired Enterprises, LLC	$895	8/2008
Daylight Technologies, LLC	$895	8/2008
Upstream Properties LLC	$895	8/2008
Diversity Communication LLC	$895	8/2008
Buyers Holdings LLC	$895	9/2008

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Aged Corporations

Oregon Properties LLC	$895	9/2008
Classic Design LLC	$895	9/2008
Impressive Strategies LLC	$895	9/2008
Metro Manufacturing LLC	$795	10/2008
Wholesale Lending LLC	$795	10/2008
Kingsbury Technologies LLC	$795	11/2008
Advanced Global Technologies LLC	$795	11/2008
Skyline Advisors Group LLC	$795	11/2008
Global Imaging LLC	$795	11/2008
Gigax Contracting LLC	$795	11/2008
Daily Financial Solutions LLC	$795	12/2008
Rock Solid Financial Group LLC	$795	12/2008
Fast Forward Financial Services LLC	$795	12/2008
Ultimate Design Group LLC	$795	12/2008
Creative Enterprises LLC	$795	12/2008
Accent Enterprises LLC	$795	12/2008
White Rock Marketing LLC	$795	12/2008
Falco Administration LLC	$795	12/2008
Guiding Point Properties, LLC	$695	2/2009
Hillcrest Communications, LLC	$695	2/2009
Infinite Aspects, LLC	$695	2/2009
Instant Suppliers, LLC	$695	2/2009
Inside Advisors, LLC	$695	2/2009
Vivid Productions, LLC	$695	2/2009
Windpower Transportation, LLC	$695	2/2009
Worthy Concepts, LLC	$695	2/2009
Amazon Industries LLC	$595	3/2009
Accent Creations LLC	$595	3/2009
Light On Marketing LLC	$595	3/2009
Dream Markets LLC	$595	3/2009
Decisive Technologies LLC	$595	3/2009
Villa Development LLC	$595	3/2009
Freestyle Enterprises LLC	$595	3/2009
Tuscano Developments LLC	$595	3/2009
Soul Solutions LLC	$595	3/2009
Right Innovations LLC	$595	3/2009
Golden Key Management LLC	Sale pending	3/2009

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Miracle Marketing LLC	$595	3/2009
Credit Strategies LLC	$595	3/2009
Go Green Enterprises LLC	$595	3/2009
Ideal Home Association LLC	$595	3/2009
Marketing Advisors LLC	$595	4/2009
Rocky Mountain Marketing Group LLC	$595	4/2009
Wyoming Advertisement Solutions LLC	$595	4/2009
Automotive Solutions LLC	$595	4/2009
Astro Leasing LLC	$595	4/2009
Erie Properties LLC	$595	4/2009
R.M. Leasing Group LLC	$595	4/2009
WebMarketing Group LLC	$595	4/2009
Copper Mills Development LLC	$595	4/2009
Summit Advertising LLC	$595	4/2009
Champion Enterprises LLC	$595	4/2009
Medical Care Technologies LLC	$595	4/2009
MileHigh Trading LLC	$595	4/2009

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*Kit in hand

Aged corporations are guaranteed to be clear of any debts or liabilities. The name of the company can be changed for a fee of $100 and the date of the incorporation will remain the same.

You may need an aged corporation for the following reasons:

- Corporate image is enhanced with age.
- Building corporate credit may be easier with age.
- Other companies may do business with an older company before a brand new one.

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Aged Corporations

- Establishing a history for your business.
- Bidding contracts at times require a certain age to your corporation.
- Obtaining bank loans may be easier when you can show you have history, the age is what matters most.
- Obtaining corporate credit cards and leases. For example, Dell Computers lease only to corporations 6 months old or more.

Top

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Excerpts from Corporations Today's Website

http://www.corporationstoday.com

"*Why Wyoming is Better*"

"Enjoy anonymity and privacy in Wyoming – The more information about you that appears in the public record the easier it is for you to become a target. Wyoming has no requirement for the names of shareholders to be filed with the state. It asks only for a simple 'annual report' which requires disclosure of only those assets located within the state of Wyoming and the name of one person, usually the one who submits the report."

"*Aged Companies*"

"Here is a list of the companies that we currently have for sale. This list changes without notice. We have the largest inventory of aged shelf corporations in the United States. These are companies that we formed and put on the shelf, they have not been used by anyone. They come with Certificates of Good Standing from the state, Certified Articles of Incorporation from the state, the corporate kit which includes 20 pre-printed stock certificates, corporate seal, and suggested meeting minutes. All state fees are paid through the renewal date of the company…

Aged corporations are guaranteed to be clear of any debts or liabilities. The name of the company can be changed for a fee of $100 and the date of the incorporation will remain the same.

You may need an aged corporation for the following reasons:

- Corporate image is enhanced with age.
- Building corporate credit may be easier with age.
- Other companies may do business with an older company before a brand new one.
- Establishing a history for your business.
- Bidding contracts at times require a certain age to your corporation.
- Obtaining bank loans may be easier when you can show you have history, the age is what matters most.
- Obtaining corporate credit cards and leases. For example, Dell Computers lease only to corporations 6 months old or more."

Prepared by U.S. Senate Permanent Subcommittee on Investigations, June 2009

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EXAMPLES OF LAW ENFORCEMENT REQUESTS FOR INFORMATION ON U.S. CORPORATIONS SUSPECTED OF WRONGDOING

June 18, 2009

Foreign law enforcement agencies make frequent requests for information about U.S. corporations suspected of involvement in criminal activity within their jurisdictions. To gain a deeper understanding of these requests and the type of wrongdoing which U.S. corporations are suspected of engaging in outside of the United States, the U.S. Senate Permanent Subcommittee on Investigations obtained sample requests from two sources: (1) requests made to the U.S. Department of Justice under a Mutual Legal Assistance Treaty (MLAT requests); and (2) requests made to two U.S. Immigration and Customs Enforcement attaché offices located abroad (ICE foreign attaché requests).

MLAT Requests[1]

1. Authorities in Latvia are seeking information about an Arkansas company as part of a criminal investigation into alleged tax evasion. (January 2007)
2. Authorities in the Ukraine are seeking information about United States corporations as part of a criminal investigation into alleged embezzlement. (January 2007)
3. Belgium has requested information about several United States companies that were allegedly used to defraud at least 50 investors out of millions of Euros in an investment scam. (March 2007)
4. Italy has requested information about several companies believed to be incorporated in the United States for use in a criminal investigation into fraud, tax evasion and money laundering. (March 2007)
5. Latvia has requested information about a New York company for use in a criminal investigation into alleged VAT fraud. (March 2007)
6. Russia has requested information about a Delaware corporation for use in a criminal investigation into alleged fraud. (March 2007)
7. Russia has requested information about a Delaware company for use in a criminal investigation into alleged VAT fraud. (March 2007)
8. Russia has requested evidence in Delaware for use in a criminal investigation into alleged smuggling involving Magelan Invest LLC. (March 2007)
9. Russia has requested information about a Delaware company for use in a criminal investigation into alleged theft. (March 2007)
10. Belarus is seeking information about two United States companies for use in criminal investigation into alleged embezzlement. (April 2007)

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[1] Source: http://www.kycnews.com/offshore_alert_back_issues.asp (viewed June 12 and 15, 2009). These MLAT Requests are listed in online editions of KYC OffshoreAlert, a monthly newsletter that examines offshore and money laundering issues. The requests appeared in the online editions from January 2007 through December 2008. Each request is a direct quotation taken from the edition cited.

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11. Russia has requested information about a New York company for use in a criminal investigation into alleged fraud. (April 2007)
12. The Ukraine has requested information about a Delaware firm FCTS Enterprises Lt. as part of a criminal investigation into alleged customs fraud. (April 2007)
13. The Ukraine has requested information about Delaware firm Actex Corporation for use in a criminal investigation into alleged smuggling. (April 2007)
14. Greece is seeking information concerning Delaware-registered Crystal Shipping Inc. for use in a criminal investigation into the alleged transportation of illegal immigrants into the country. (June 2007)
15. Latvia is seeking information concerning Delaware-registered E&W Trading Group LLC for use in a criminal investigation into alleged tax evasion, money laundering, and conducting business without a license. (June 2007)
16. Poland has requested information about many corporations with addresses in the United States as part of a criminal investigation into alleged fraud. (June 2007)
17. Latvia has requested evidence from a Delaware corporation as part of a criminal investigation into alleged tax evasion. (November 2007)
18. Poland has requested evidence from the representative of a Delaware corporation for use in a criminal investigation into alleged bank fraud and forgery involving a fake bank guarantee for 11.8 million Euro. (November 2007)
19. Russia has requested evidence from Delaware incorporator [redacted] as part of a criminal investigation into an alleged RUR 30 million fraud against the Republic of Buryatia, an autonomous Russian republic located in Serbia. (November 2007)
20. Ukraine has requested information about Delaware-registered Span Investments Holding LLC as part of a criminal investigation into the alleged smuggling of goods. (November 2007)
21. The Czech Republic has requested evidence from a Florida company as part of a criminal investigation into copyright infringement and theft of computer software. (January 2008)
22. Cyprus has requested evidence in the United States as part of a criminal investigation into an alleged multi-million theft and fraud by former officers of Delaware-registered AremisSoft Corporation. (February 2008)
23. Poland is seeking evidence from a Delaware-registered company as part of a criminal investigation into alleged fraud (February 2008)
24. Russia has requested information about a Delaware corporation as part of criminal investigation into alleged tax evasion. (February 2008)
25. Russia has requested evidence from a Delaware-registered corporation as part of a criminal investigation into alleged customs fraud. (February 2008)
26. Ukraine has requested evidence from a Delaware corporation as part of a criminal investigation into alleged customs fraud. (February 2008)
27. Latvia is seeking information about and from Delaware-registered Subterranean Lake Group LLC as part of a criminal investigation into alleged fraud. (March 2008)
28. The Slovak Republic has requested evidence about and from Delaware-registered Lingo Wood Inc. as part of a criminal investigation into alleged tax evasion. (March 2008)
29. Ukraine has requested information from and about Delaware-registered Brownsville LLC for a criminal investigation into alleged tax fraud and money laundering. (March 2008)

30. The Czech Republic has requested evidence from Delaware-registered Avenger Sales LLC as part of a criminal investigation into alleged bankruptcy fraud. (April 2008)
31. Estonia is seeking information about three companies in Delaware and one in Arkansas as a part of a criminal investigation into alleged import/export fraud. (April 2008)
32. Latvia is seeking evidence from Delaware-registered Drynam LLC as part of a criminal investigation into alleged fraud. (April 2008)
33. Switzerland has requested evidence from and about, Delaware-registered Dahll Scott Corporation as part of a criminal investigation in to a 68-year-old German citizen for alleged fraud and forgery. (April 2008)
34. Bulgaria has requested evidence from a Delaware company for a criminal investigation into smuggling and money laundering involving cigarettes. (June 2008)
35. Bulgaria has requested evidence from a Delaware company for a criminal investigation into the alleged illegal exportation of meat. (June 2008)
36. The Czech Republic is seeking information about two companies in Delaware and one in Arkansas as part of a criminal investigation into alleged embezzlement, breach of trust and insider trading. (June 2008)
37. The Czech Republic has requested information about US corporations as part of a criminal investigation into alleged embezzlement. (June 2008)
38. Latvia has requested information about Delaware-domiciled Westerman LLC as part of a criminal investigation into alleged tax evasion and money laundering. (June 2008)
39. Russia has requested evidence from Delaware-domiciled Ferbane Global LLC for a criminal investigation into alleged corruption. (June 2008)
40. Bulgaria is seeking evidence from Delaware-domiciled Kingston Enterprises LLC for a criminal investigation into alleged money laundering. (August 2008)
41. Ukraine is seeking evidence from Delaware-domiciled Balkandonsteel LLC for a criminal investigation into the "alleged failure to repatriate foreign currency proceeds". (August 2008)
42. Romania has requested evidence from three Delaware-domiciled companies and American Express Bank in New York as part of a criminal investigation into alleged bankruptcy fraud, money laundering, and embezzlement. (September 2008)
43. Ukraine has requested evidence from Delaware-domiciled Pharmaceutical Solution, Inc. for a criminal investigation into alleged customs fraud. (September 2008)
44. Ukraine is seeking evidence concerning Atlanet LLC in Delaware as part of a criminal investigation into alleged value added tax fraud, forgery, and money laundering. (October 2008)
45. Ukraine is seeking evidence from Toronto Projects, Inc. in Delaware for a criminal investigation into alleged value added tax fraud. (October 2008)
46. Ukraine is seeking evidence from Avenger Sales LLC in Delaware as part of a criminal investigation into alleged fraud. (October 2008)
47. Hungary has requested evidence from companies in Delaware and Florida as part of a criminal investigation by police in Budapest into a man accused of operating a car-import fraud. (December 2008)

ICE Foreign Attaché Requests[2]

The Subcommittee asked ICE to provide information about requests received from foreign law enforcement agencies seeking U.S. corporate ownership information. ICE indicated that such requests were frequent, singling out in particular two ICE attaché offices, located abroad, with principle responsibility for Eastern European law enforcement requests. ICE provided the following information for those two offices.

- **Frankfurt Attaché.** The ICE Attaché in Frankfurt, Germany receives numerous requests over the stated timeframe (2002-present) from the customs agencies in Georgia, Ukraine, Poland, Estonia, Latvia, Lithuania, Kazakhstan, Uzbekistan, Moldova, Denmark, Sweden, Finland and Norway (the Nordic countries were within the area of responsibility of the ICE Attaché Frankfurt from 2002-2006 and the Stans from 2002-2008) regarding False Country of Origin and the undervaluation of vehicles and other items exported from the U.S that result in a loss of customs duties and value added tax (VAT) revenue to the country of import. In an average month, approximately 10 requests are received by the ICE Attaché Frankfurt for original documents associated with this fraud. The ICE Attaché Frankfurt filters these requests and sends investigative leads to domestic ICE offices for their assistance in acquiring the original purchase and export documents approximately 40% of the time. Frequently, the documents and the associated investigations show that the exporter committing the fraud utilizes a U.S. shell company as the entity that purchased and/or exported the commodity. The ICE Attaché Frankfurt has been able to identify approximately 241 instances of this nature since 2004. The most common states of incorporation for these shell companies are Delaware and Nevada.

- **Vienna Attaché.** The ICE Attaché in Vienna, Austria has received numerous requests over the stated timeframe from the customs agencies in Bulgaria, Czech Republic, Hungary, Romania, Slovakia, and Slovenia regarding False Country of Origin and the undervaluation of vehicles and other items exported from the U.S that result in a loss of customs duties and value added tax (VAT) revenue to the country of import. In an average month, more than 100 requests are received by the ICE Attaché Vienna for original documents associated with this fraud. Frequently, the documents and the associated investigations show that the exporter committing the fraud utilizes a U.S. shell company as the entity that purchased and/or exported the commodity. The most common states of incorporation for these shell companies are Delaware and Florida. It is difficult to gauge the results of these investigations because the volume of these cases is so high that it would be resource intensive to track each disposition.

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[2] Source: ICE.

Statement of Senator Tom Carper
Before the Committee on Homeland Security and Governmental Affairs
On Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act
June 18, 2009

I want to welcome our witnesses today. Thank you for joining us today and for your input.

I want to thank Chairman Lieberman and Senator Levin and their staff for working closely with my staff, as you studied this topic and put this hearing together.

The last time we met on this issue, in November 2006, I emphasized the importance of this issue to my state. Business incorporations and related fees account for roughly 25 percent of Delaware's general fund revenues.

I continue to be proud that Delaware is the leading home of incorporations for businesses in this country. Delaware continues to be a leader in entity incorporation because the state has the expertise to ensure corporate success – from annually updating its laws to meet the changing needs of incorporated interests to a well-respected and renowned judiciary.

Delaware has enacted a number of laws to deter the formation of illicit businesses and ensure that law enforcement has better access to the information they need to prevent and solve crimes.

For example, Delaware was the first state in the nation to adopt legislation responding to the concerns expressed by law enforcement regarding illicit practices of registered agents. Delaware now regulates Commercial Registered Agents and has successfully removed a number of registered agents from doing business in our State.

Delaware requires every business entity to provide the name, address and phone number of a designated communications contact person that is available to law enforcement. And Delaware responded to international criticism that U.S. company law permits companies to issue bearer shares, stocks certificates whose record of ownership is not maintained by the issuing company, when we explicitly banned the practice in statute to be consistent with long-established Delaware case law.

There are a number of reasons for us to encourage more transparency and disclosure with respect to ownership of legal entities. But whenever we undertake legislation, we have to find the right balance. In this case, we need to provide law enforcement with the tools they need to prevent and prosecute crime.

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However, we must ensure that we do not put additional burdens on our states or our state budgets, many of which are operating in a deficit. 99.9% of corporate entities in the United States are good citizens. We should not burden the vast majority of good citizens with expansive and burdensome paperwork while trying to find the 0.1% of bad actors who are likely to try to evade such disclosures anyway. Whatever solutions we pursue, it is important that we are careful not to hinder legitimate business activity or invade the financial privacy rights of risk-taking entrepreneurs who have historically found the United States to be the freest economy in the world.

At our last hearing in November 2006, Delaware's Assistant Secretary of State, Rick Geisenberger, appeared before this Committee and discussed the issues related to the disclosure of "beneficial owners" of incorporated entities. Mr. Chairman, I would like to offer Mr. Geisenberger's testimony from that hearing into this hearing record if I may.

In his testimony, it was the Secretary of State's conclusion, and he was not alone, he was joined by the National Association of Secretaries of State, that requiring entities that incorporate in any state to disclose who the "beneficial owners" of a corporation are, at any certain point in time, would be difficult to implement. The act of defining "beneficial owners" is not easy and could be interpreted quite broadly – in some cases requiring the disclosure of hundreds, even thousands, of names.

After that hearing in 2006, I charged Mr. Geisenberger and the Delaware Secretary of State's office with the task of trying to find a compromise on this issue. The National Association of Secretaries of States, who are represented today by North Carolina Secretary of State Elaine Marshall, created a Company Formation Task Force to examine this issue in February 2007.

The Task Force asked the Uniform Law Commission, who are represented by Mr. Harry Haynsworth, to develop amendments to various uniform and model entity laws to help address these issues. The Uniform Law Commission drafting committee included representatives from the American Bar Association, and other stakeholders around the nation.

My understanding, and I'm sure the witnesses today can attest to this fact, is that this group has worked furiously for two years to find a compromise that would work – that would both assist law enforcement by providing the information that they need without putting an undue burden on the states or on legitimate American businesses.

I look forward to hearing from all of our witnesses today so that we can get an update on the lay of the land since our last hearing and determine whether a workable compromise has been achieved.

Thank you to our Chairman for holding this hearing and thank you to my friend from Michigan for his diligence on this issue to make sure our country is protected and for working to ensure that we find the right solution and the right balance here.

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U.S. Immigration and Customs Enforcement

STATEMENT

OF

JANICE AYALA

DEPUTY ASSISTANT DIRECTOR
OFFICE OF INVESTIGATIONS
U.S. IMMIGRATION AND CUSTOMS ENFORCEMENT
DEPARTMENT OF HOMELAND SECURITY

REGARDING A HEARING ON

"EXAMINING STATE BUSINESS INCORPORATION PRACTICES: A DISCUSSION OF THE INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT (S. 569)"

BEFORE THE

UNITED STATES SENATE
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

Thursday, June 18, 2009 @ 2:30 pm
342 Dirksen Senate Office Building

INTRODUCTION

Chairman Lieberman, Ranking Member Collins, and distinguished Members of the Committee:

On behalf of Secretary Napolitano and Assistant Secretary Morton, I would like to thank you for the opportunity to testify today on the efforts of U.S. Immigration and Customs Enforcement (ICE) to protect the United States from the growing threat of international money laundering. ICE has expansive investigative authority and the largest force of investigators in the Department of Homeland Security (DHS). We protect national security and uphold public safety by targeting transnational criminal networks and terrorist organizations that seek to exploit vulnerabilities at our borders.

ICE investigates individuals and organizations that exploit vulnerabilities in financial systems for the purpose of laundering illicit proceeds. ICE also addresses the financial component of every cross-border criminal investigation. ICE's financial investigative authorities and unique capabilities specifically given to and used by ICE enables it to identify, dismantle, and disrupt the financial criminal enterprises that threaten our nation's economy and security. The combination of successful financial investigations, Bank Secrecy Act (BSA) reporting requirements, and Anti Money Laundering (AML) compliance efforts by traditional and non traditional financial institutions has, historically, forced criminal organizations to seek other means to launder their illicit funds across our borders. One of the most effective methods to confront, dismantle, and disrupt these often violent, transnational criminal organizations is to target the criminal proceeds that fund their operations. However, in the attempts to accomplish this mission, law enforcement is often hindered by the lack of information available as to the true ownership or control of shell companies. Further, this impediment limits our abilities to work

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jointly with our international law enforcement partners and can inhibit our ability to take quick action where it may be required.

In addition, ICE participates in a working group chaired by the National Security Council focused on the United States Government response to large-scale corruption by foreign public officials, also referred to as "kleptocracy." ICE has played an integral role in the development of the strategy, as it is uniquely positioned as a U.S. cross-border investigative agency possessing international money laundering expertise, customs and immigration authorities, and extensive international investigative assets. In 2003, ICE established the Federal Foreign Corruption Task Force, which conducts investigations into the laundering of proceeds emanating from foreign public corruption, bribery, or embezzlement. The investigations are conducted jointly with representatives of foreign governments to prevent laundered money from entering the U.S. financial infrastructure, seize identified assets in the U.S., and repatriate these funds to the victimized governments.

ICE has long recognized the misuse of corporations and limited liability companies (LLCs) formed under State law as a serious threat to the ongoing effort to combat international criminal activities. The lack of corporate transparency has allowed criminal entities a gateway into the financial system and further veils their illicit activity. Investigations can be significantly hampered in cases where criminal targets utilize shell corporations. The difficulty for law enforcement to obtain true beneficial ownership information impedes investigators' ability to follow criminal proceeds. Furthermore, the 2005 U.S. Money Laundering Threat Assessment, the first government-wide analysis of money laundering in the United States, specified that "legal entities such as shell companies and trusts are used globally for legitimate business

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purposes, but because of their ability to hide ownership and mask financial details they have become popular tools for money launderers."

Obtaining information on true beneficial corporation owners and LLCs formed under State law, and providing the information to civil or criminal law enforcement upon receipt of a subpoena or summons, would assist DHS in its endeavor to protect the country. Currently, due to the disparity in the type and amount of corporate ownership information collected by individual States, law enforcement is often faced with the unavailability of needed information as to the true ownership of funds, accounts, or assets that are deemed to be linked to criminal activity. The collection by States of a standard minimum level of corporate ownership information, and the ability of law enforcement to access this information in a timely manner, would greatly assist law enforcement efforts.

At this time, I would like to share with you a few examples of investigations that demonstrate how "shell" corporations established in the United States have been utilized to commit crime against individuals throughout the world.

NEW YORK MONEY LAUNDERING INVESTIGATION – INVESTMENT FRAUD

Based on a tip, an investigation was initiated by our New York office against a criminal organization involved with defrauding investors out of millions of dollars and laundering the fraudulently obtained proceeds. The investigation revealed an enterprise of individuals offering fictitious instruments for investment programs described as "currency leasing trading programs," leading to more than $14 million in fraudulent transactions. These funds were laundered through a network of domestic and foreign bank accounts utilizing shell corporations, many of which had been established in the United States.

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The investigation revealed that one of the perpetrators operated an Internet web site out of Las Vegas, Nevada, which offered investors the opportunity to "lease" $1 million for a fee of $35,000. Once "leased," victims were told these funds would be placed into a high yield international trading program. The contracts provided to the investors indicated an expected return on their investment of as much as 25 percent every two weeks.

An additional co-conspirator in the scheme was responsible for establishing a complex web of bank and brokerage accounts, and shell companies. This individual established corporations in Delaware, Nevada, California, and Massachusetts in the United States along with companies in Denmark, Sweden, Luxembourg, and the Bahamas. Another co-conspirator opened cash management accounts at brokerages utilizing the shell corporations. Investors were told to send their $35,000 fee to the accounts established utilizing the shell corporation names. Once in this account, the funds were transferred to secondary accounts. From these accounts, the funds were then disbursed to various foreign and domestic accounts and liquidated through the use of checks, debit cards, and ATM cards. The investors never realized the profits they were promised. They merely received a litany of excuses for the delays and promises that the transactions would be completed. When they requested refunds, the investors were told that they were not entitled to a refund since they had received the service that they paid for, namely that the funds had been successfully leased.

In the end, six individuals pled or were found guilty of violating money laundering, wire fraud, and international transportation of stolen funds statutes. The defendant's use of domestic and foreign shell companies to layer the funds prevented full recovery of the fraudulently obtained funds.

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MIAMI MONEY LAUNDERING INVESTIGATION-BID RIGGING-BRIBERY

Another example of how these shell corporations are utilized for criminal activity is illustrated in a Miami office investigation. In this investigation, the violators utilized shell corporations to defraud the Government of Trinidad and Tobago out of more than $100,000,000. The foreign and domestic shell companies enabled them to engage in a bid-rigging scheme and then launder the fraudulently obtained proceeds. In this "bid-rigging" fraud scheme, the co-conspirators bribed members of a Trinidad and Tobago bid committee of the Piarco International Airport in order to win a competitive construction bid. The U.S. targets of the investigation operated a construction company and architectural firm in South Florida, which submitted a competitive bid for work in the construction of the airport. A Trinidadian Government Accessor believed the bid was too high and requested that the bid committee obtain a second bid. As a result, the targets of the investigation utilized a shell company to submit a second, much higher valued bid for the work. As a result of this much higher second bid, the contract was awarded to the targets of the investigation.

Once they had been paid by the Trinidadian Government, they laundered the proceeds of the fraud by layering them through a series of shell companies in the Bahamas, Lichtenstein, and the United States. Through handwritten notes kept by Bahamian bankers, ICE investigators identified the true beneficiaries of the funds. Six of eight indicted individuals were found guilty of violating money laundering, and wire fraud statutes. The two remaining indicted individuals are still pending extradition to face the charges. As part of the sentence, the court ordered approximately $22 million in restitution be paid, but the majority of that ordered restitution has not been realized.

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NATIONAL INITIATIVE - OPERATION PAYCHECK – DISGUISED PAYMENTS TO ALIEN WORKERS

In July 2006, ICE launched Operation Paycheck, a national initiative designed to combat criminal schemes involving the exploitation of the financial industry by businesses to pay the wages of illegal alien workers. Through ICE investigations, numerous financial schemes have been uncovered throughout the U.S., such as money laundering, structuring funds into and out of financial institutions, and the operation of unlicensed Money Service Business (MSB) to disguise the payment of illegal alien workers. To combat this threat, all ICE Offices of Investigations are leveraging their combined investigative expertise in financial crimes and worksite enforcement to identify, disrupt, and eliminate organizations seeking to exploit our financial industry to facilitate the employment of illegal aliens.

In most cases identified, many involving the construction industry in the southeastern U.S., the employer of illegal aliens establish shell companies that appear to operate as sub-contractors of the actual employer. The employers are then able to pay the shell company for their services, often in the form of one large check or numerous checks. The shell company (sub-contractor) then cashes the check or checks, frequently through a culpable MSB, and pays the illegal alien workforce in cash. In most instances, the person or persons posing as the sub-contractor charge a fee for this service, as does the culpable MSB.

This type of scheme may also involve a host of other state and federal violations. For example, by using the shell company and the payment of the illegal alien workers in cash, the employers avoid withholding state, federal, and social security taxes from employee's paychecks in violation of state and federal tax and labor laws.

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CONCLUSION

As noted in our testimony, the use of shell companies to engage in illicit activities, including money laundering and financial fraud, presents a number of investigative challenges for law enforcement. The lack of transparency and information on beneficial ownership of these entities has made their use an ideal mechanism for money laundering and the commission of other illegal activities, and has allowed criminals an entry into our financial system. Greater transparency of beneficial ownership of corporate entities and providing law enforcement reasonable access to this information would greatly assist our efforts to combat the use of shell companies for illegal activities.

I would like to thank the Committee Members for this opportunity to testify and for your continued support of ICE, CBP, DHS and our law enforcement mission. I will be happy to answer any questions that you may have at this time.

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Department of Justice

STATEMENT OF

JENNIFER SHASKY CALVERY
SENIOR COUNSEL TO THE DEPUTY ATTORNEY GENERAL
UNITED STATES DEPARTMENT OF JUSTICE

BEFORE THE

UNITED STATES SENATE
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

HEARING ENTITLED

"EXAMINING STATE BUSINESS INCORPORATION PRACTICES: A DISCUSSION OF THE INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT"

PRESENTED

JUNE 18, 2009

Good afternoon, Chairman Lieberman, Ranking Member Collins and distinguished Members of the Committee. I am honored to appear before the Homeland Security Committee to discuss the critical need for greater transparency in corporate formation in this country. Nearly three years ago the Department testified before the Permanent Subcommittee on Investigations of the Committee on Homeland Security and Governmental Affairs about the difficulties that U.S. shell companies often pose to law enforcement efforts—and the need for improved access to beneficial ownership information of these companies. In this context, we use the term "shell company" to refer to a legal entity, established under the laws of a State, that has no independent operations or assets of its own. Unfortunately, since the Committee last examined this issue, the problem has not improved. So I am pleased that the Department has another opportunity to speak with you about this important issue and that the conversation has now moved from framing the problem to developing possible legislative solutions.

The term shell company often evokes images of exotic offshore financial centers and money laundering havens. Unfortunately, some of the worst offenders are not "exotic" locales at all, but rather some of our own States. In 2006, we spoke of an unscientific internet search that we conducted using the words "shell corporation". This most basic search brought up dozens of websites touting the anonymity, speed, and ease of using their services to incorporate companies in various U.S. states. Unfortunately, the news is no better in 2009. A similar search continues to produce sites offering U.S. companies for sale, making advertising claims such as *"When you set up with one of these shell corporations, your name is not listed on public records as the "incorporator" and First Director, which can be very key when it comes to privacy."*; and *"Why wait months or years to establish business credit when you can own a turnkey Nevada shelf corporation with over 150k of bank credit"*. Far from attempting to disguise the anonymity that comes with shell companies or the fact that "aged" shell companies lend credibility and credit where it would otherwise not exist—on most sites these are the primary selling points. In an era of rampant mortgage and internet fraud, few things are more appealing to those seeking to evade the law than a company that comes with over $150,000 of available credit, a public veneer of credibility, and complete anonymity.

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We must find a solution that will meet core law enforcement needs by providing transparency to corporate ownership while not placing undue burdens in these turbulent economic times on the States or the vast majority of legitimate businesses who are rightly attracted to establishing a legal presence in one or more of our States.

Four critical issues must be addressed in any legislative solution: (1) the need to identify the beneficial owner of a legal entity at the point of formation; (2) the need for law enforcement to obtain accurate and timely information about the owners of existing U.S. legal entities; (3) the appropriate means of addressing the challenge of the transfer of corporate ownership—especially from corporate formation agents to corporate brokers; and (4) the penalties necessary to discourage the misuse of U.S. companies -- all without burdening the States and private business with undue costs and regulation. Several important legislative solutions have been offered by members of this Committee and by the States, I will not address those proposals directly other than to say that the Department strongly supports all efforts to address the lack of transparency in U.S. legal entities, believes that federal legislation must be at least part of the solution, and believes that the current proposals contain many good ideas upon which to base our discussions.

Background

Shell companies can be loosely defined as legal entities that have no significant operations, have no significant "brick and mortar assets" and exist primarily on paper—with any U.S. presence typically consisting of a postal box or a mail drop at a company service provider office. One company formation website, in an unsuccessful effort to draw a distinction between its "shelf" corporations and shell companies, describes a shell as "an incorporated company that does not have any significant assets or operational structure, but merely serves as a clearing house for dissolving corporations, tax evasion, or for the handling of illicit funds." This admission recognizes the reality of U.S. shell companies: Because of lax company formation laws criminals can form shell companies quickly and cheaply and obtain virtual anonymity. Even after the criminal activity is detected, so little information is currently collected during and after the formation process that the true ownership of the shell is just one more unanswered question in the overall financial investigation. This is the challenge that we face here today: how to arrive at a solution that will provide transparency to law enforcement and deprive the criminal of

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this valuable tool while not imposing undue burdens on the States and on small businesses that rely on legal entities to operate.

In our testimony three years ago, we discussed some of the difficulties domestic shell companies pose to criminal investigations. While corporations certainly have an important and legitimate commercial role to play in both the national and global economy, they may also be used for illicit purposes, including money laundering, bribery and corruption, fraud, tax evasion, immigration and visa fraud, and other forms of illegal activity. Increasingly, illicit money networks, or professional money launderers, if you will, use shell companies as a necessary tool of their trade in schemes to launder money for drug trafficking and other international criminal organizations, and to finance terrorism. Shell companies are specifically used for this purpose because they are very easily formed, can provide an essentially anonymous legal entity with which to open domestic and foreign bank accounts and, in the case of U.S. shells, carry an air of legitimacy. Criminals trade on this air of legitimacy and the good names of our States by sending illicit money through shell company bank accounts fraudulently disguised as legitimate economic trade. The criminal source, destination, and true ownership of the money is protected from law enforcement scrutiny by State laws which do not require the beneficial owners of companies to adequately identify themselves.

Shell companies, or facially legitimate companies, have been used in visa fraud schemes to facilitate the issuance of business visas (B-1, L and H visa categories) to those who wish to migrate to the U.S. illegally. They have also been used to facilitate the issuance of visas and entry into the U.S. of members of organized crime groups.

Companies are easily formed. To do so, a company principal or someone acting on the company's behalf submits formation documents to the appropriate State office. Documents may be submitted in person, by mail, or online, and "the process can take anywhere from 5 minutes to 60 days." *Company Formations: Minimal Ownership Information is Collected and Available* (GAO-06-376) (*GAO Report).* In addition, a "minimal amount of basic information generally is required to form a company." *(GAO Report*, p.7) Typically, the documents must give the company's name, an address where official notices can be sent to the company, share information for the company, and the

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names and signatures of the persons handling the incorporation process. Few states require ownership information when a company is formed, nor do they require any updates. (*GAO Report,* p.13) Even the initial required information regarding shareholders is not always accurate or up to date. *(GAO Report*, p.43) States generally do not verify the identities of incorporators or company officials. (*GAO Report,* p.21) In sum, someone either within or outside of the United States, without any verification of identification, can form a corporation within as little as five minutes. The corporation is then a legal entity that can engage in business and open a bank account.

Because shell companies effectively conceal the identities of the persons using the companies for illegal activity, the use of shell companies to facilitate criminal schemes continues to grow more sophisticated. Criminals want to use U.S. shell companies because those entities do not receive the same level of scrutiny as those established in foreign jurisdictions that share comparatively weak corporate regulation – jurisdictions that are often labeled "offshore havens." Additionally, the U.S. companies have an air of legitimacy in the foreign countries where criminals may want to obtain bank accounts. Criminals are increasingly opening bank accounts for their shell companies in offshore jurisdictions where customer identification requirements may be less rigorous than in the United States. These companies then gain access to the U.S. financial system through correspondent banking relationships with U.S. financial institutions.

The following scenario illustrates how this structure works. First, a corporate formation agent forms thousands of companies in a State that does not require the agent to collect or verify ownership information. The agent then markets these "shelf companies" around the world. A professional money launderer buys several and uses them to open bank accounts in a foreign country. The foreign bank has a correspondent account at a bank in New York. The criminals then make wire transfers using those accounts, which appear to be legitimate trade transactions from a U.S. company that has a bank account in New York. This kind of illicit money movement system allows international criminal organizations to move billions of dollars without detection. U.S. law enforcement agencies cannot determine who is perpetrating the scheme through the records maintained by the State of incorporation because the criminals used nominees on the paperwork and purchased the shell company via an intermediary. Law enforcement

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also cannot determine who is perpetrating the scheme through the U.S. bank account records because a correspondent account only identifies the foreign bank as its account holder. The records do not identify who controls accounts within the foreign bank, so ironically, U.S. law enforcement must try to get information about a U.S. company from the foreign country, which is difficult for many reasons, and often simply not possible at all.

The use of domestic shell companies in criminal schemes not only frustrates our domestic law enforcement efforts, but also frustrates the efforts of our foreign law enforcement counterparts. When the perpetrators use U.S. shell companies to open bank accounts in foreign countries to launder money or otherwise facilitate criminal activities in those countries, foreign law enforcement will go to the foreign bank to obtain information about the owners of the accounts. If the bank account is in the name of a U.S. company, foreign law enforcement has to request information on the beneficial owners of the company from the United States. The U.S. State in which the company was formed almost never has that information to provide because it is not required to be collected during corporate formation. The United States is unable to provide assistance to foreign law enforcement which not only frustrates foreign criminal enforcement efforts but also domestic enforcement efforts, but also damages our ongoing relationships with our foreign law enforcement counterparts. As you might imagine, foreign counterparts who have watched their investigations frustrated by weaknesses in U.S. law are not always quick to assist with U.S. investigations involving collection of evidence in their country.

In addition, the United States has been cited with non-compliance through the Financial Action Task Force (FATF) – a multilateral body whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing -- for our weak State incorporation laws which do not require the provision of beneficial ownership information. The FATF recognizes that shell companies are widely used to launder the proceeds from crime and that the identification of a company's beneficial owners is essential for preventing and punishing money laundering. *See FATF Report on Misuse of Corporate Vehicles*, p.5 (October 2006) (available at http://www.fatf-gafi.org/pages/0,2987,en_32250379_32235720_1_1_1_1_1,00.html).

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This problem of U.S. shell companies has indeed become so acute that other jurisdictions have recognized that criminals and tax evaders regularly use U.S. shell companies in their illicit activity when accurate beneficial ownership information is not required. For example, Brazil recently expanded its definition of tax havens, in Article 22 of Law 11,727/2008, to include countries and locations with laws that do not allow access to information concerning the corporate structure of legal entities, their ownership, or identification of the beneficial owner attributed to non-residents. Most, if not all, commentators suggest that this legislation was directed specifically at U.S. States such as Delaware and Nevada.

The lack of shell company ownership information, or access to it, presents an increasingly serious problem for domestic and foreign law enforcement in dismantling international criminal organizations and prosecuting money launderers. Moreover, the problem presented by formation agents who set up and sell multiple companies to foreign brokers requires not just verified information on beneficial ownership when the company is formed, but also regularly updated and accurate information maintained in the state of incorporation and readily accessible to law enforcement.

It is our job to solve this growing problem. The steps taken by other jurisdictions to address the problems presented by shell companies demonstrate that the problem is not insurmountable.

I) DOJ/Law Enforcement Priorities

The underlying criminal and national security problems to which U.S. shell companies contribute are unquestionably severe. Likewise, the scope of the problem, that is, the prevalence of criminals misusing U.S. shell companies, is certainly broad. That is why the Department is so heartened to see that, through the leadership of Members of this Committee, the discussion among all of the stakeholders has moved beyond the stage of defining the problem to developing a solution. We are convinced that such a solution is possible and can be crafted in a manner that is workable for law enforcement, State governments, and the private sector, that is, a solution that will benefit everyone but the would-be criminals and terrorists.

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As noted earlier, the Department has identified four critical issues that must be addressed for an effective and comprehensive solution to the problem of shell companies. I will address each of these issues in turn and discuss possible solutions from the Department's perspective.

A) Identifying the Individual/Beneficial Owner Behind the Entity

Criminals exploit and abuse current State incorporation standards to facilitate their criminal activities and conceal their identities by using shell companies that have no real existence and little to no transparency as to ownership—beneficial or otherwise.

The Department recognizes that no system will be foolproof and no system can ever provide perfect information. That being said, we believe the key to transparency of legal entities at the formation stage is threefold: (1) requiring the provision of correct beneficial ownership information at the time of formation for all legal entities; (2) consistently defining beneficial ownership across all 50 states to ensure that criminals cannot exploit definitional gaps between different state systems; and (3) requiring photo identification to provide law enforcement with at least a name and a face to further their investigation where the information provided to a state is either false or missing.

While the collection of beneficial owner information should be the focus of any comprehensive system, to be effective such information must be collected from more than just corporations. While company laws vary from state to state and thus no list is exhaustive, at a minimum, proposed legislation should include all statutory business entities in a particular state including: for profit corporations, nonprofit corporations, limited liability partnerships, limited partnerships, limited liability companies, associations, cooperatives and cooperative associations and statutory trust entities. Anything less than complete coverage of all legal entities will create loopholes and drive illicit traffic to that weak link. For example, if LLPs are not covered, but LLCs and corporations are, criminals will simply cease using LLCs and corporations and move to the less regulated LLPs. In law enforcement circles, this principle is known as "the least protected house" principle. Essentially, the house with the weakest locks is the one that gets burgled. In money laundering and other financial crimes, the weakest and least regulated industry, state or entity is often the one victimized.

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While the scope of covered entities must be as expansive as possible, the Department agrees with proposals that exempt certain well defined categories of legal entities. Broadly speaking, the Department believes that companies which are (1) regulated by a U.S. Federal or State body; and (2) required by the regulator to provide beneficial ownership information, should be exempt. Given the disparate norms used by foreign regulators and the fact that the relevant information is not maintained in the United States, we believe it is inappropriate to extend such an exemption to companies regulated by foreign regulatory bodies.

In addition to having a comprehensive list of covered entities, it is critical to have a consistent, working definition of beneficial ownership. While many claim that the task of defining beneficial ownership is impossible, to the contrary, there are a number of definitions worldwide for "beneficial owner" which may assist in drafting this important definition, including but not limited to the definitions contained in: 31 CFR 103.175; 17 CFR 240.13d-3; the United Kingdom Money Laundering Regulations, effective December 15, 2007;[1] and the European Union (Third Anti-Money Laundering Directive).[2] The definition adopted in S. 569 offers a reasonable approach, although we recommend that it should be slightly modified to clarify that the beneficial owner must be a "natural person" as opposed to another legal entity.

The Department strongly recommends that States be required to adopt a uniform definition of beneficial ownership and obtain the name, current address, and a copy of either a government-issued identification or passport, (including a legible photograph of either form of identification) for each beneficial owner. Due to the variety and quality of documentation world wide, we recommend that the States accept either government-issued identification issued in the United States or passports for U.S. persons, but only passports for foreign registrants.

Additionally, to the extent that a formation agent is used, we recommend that the agent be required to take reasonable steps to verify the information and sign a

[1] Used by the United Kingdom in conjunction with the Financial Action Task Force (FATF), a leading international organization combating money laundering and terrorist financing.
[2] Used by the European Union in conjunction with the FATF.

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certification that, to the best of his/her knowledge, the ownership information provided by the agent to the state is true and complete.

B) Obtain Information in an Accurate and Timely Manner

While the collection of accurate beneficial owner information is critical, its usefulness is significantly undermined if law enforcement cannot receive the information in an accurate and timely manner. Specifically, law enforcement must be able to obtain (through an appropriate process) all beneficial ownership information for a legal entity in a timely fashion. We recommend that the information be available upon service of (1) a civil, criminal or administrative subpoena, summons, or investigative demand from a federal or state law enforcement authority, federal or state prosecutor, federal or state agency or committee or subcommittee of the United States Congress; or (2) a written request made by the Federal Government on behalf of another country under an international treaty, agreement, convention or other mutual legal assistance request. We recommend that the information be provided no later than 5 working days after service of the request.

C) Issues Relating to Transfer of Ownership

Unfortunately, no matter how strong a system we create at the point of formation, this is only half the battle. Often, criminals will perpetrate their schemes using so-called "shelf" or "aged" companies that were created at some point in the past and are now a valuable commodity for resale because of their history of good standing, credit, and sometimes even their banking relationships. In such cases, the trail very often goes cold with either the initial company formation agent or the middleman who is brokering a re-sale, neither of whom know or often care who has purchased the shell company. Therefore, any meaningful legislative solution must also address the point of transfer.

As evidenced by the array of websites offering such services, the sale of "off the shelf" corporations and limited liability corporations (i.e., entities that are already formed and ready to be sold to a potential buyer) is big business in the United States. This is not to suggest that advertising companies on the internet in this manner is illegal or that either the seller or purchasers of companies advertised in this way necessarily intend to

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violate the law. However, one need only look at current websites offering such shelf companies to understand the allure to fraudsters, money launderers and other criminals.

For example, one website promotes such companies as follows:

SmallBiZ.com

Shelf Companies

A shelf company is a company that has been formed but never been used. Each company listed was originally filed by SmallBiZ.com, is in good standing, has no current business activity, no assets, no liabilities and no stock has been issued.

Why Buy a Shelf Corporation or LLC?

- **Instant History** - Establish months or years of history instantly.
- **Better Credit -** A company with history has an easier time obtaining financing, credit cards & leases.
- **Better Image** - A shelf company looks better with age.
- **Contract Bidding** - Some vendors require that your company have a minimum time of existence.
- **Save Time** - A shelf corporation is ready to begin business immediately. Any potential delays in startup are avoided.

Why Buy A SmallBiZ.com Shelf Company?

- **Price** - Our prices are the very lowest available anywhere!
- **Company Name** - Each of our shelf companies already have an excellent name. However, we can change the name of the company for only $100 more.
- **Buy Now** - Buy a shelf company now and we will send you your shelf company documents via Next Day Air (included).
- **Our Guarantee** - We guarantee that the company you purchase has never had any operational experience. We can guarantee this because we formed the company and maintained control since its formation.

What Comes With Each Shelf Company?

- **Original Articles** - Original file stamped docs from the formation state
- **Filing Receipt -** Original doc from state indicating filing completion
- **Appointment Form -** Original signed Appointment form to you
- **Tax Paid Acknowledgement -** Proof that taxes are paid up to date*
- **Forms CD -** Either Corp. Forms or Operating Agreement on CD included
- **Registered Agent -** Registered agent service for 12 months included
- **Other Items -** Each shelf company is slightly different (call for more info)

Available Shelf Companies

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Company Name	Type	State	Form. Date	Price	Details	How to Buy
Comprehensive Creations, Inc.	INC	CO	3/30/05	$2699	FOUR YEAR OLD CORP! Includes: SmallBiZ Secretary* compliance service!	BUY NOW
Forward Thinking Group, Inc.	INC	DE	07/30/07	$1249		SOLD
Begal Group, Inc.	INC	CO	12/29/07	$699	Includes: SmallBiZ Secretary* compliance service!	BUY NOW
Concept Dimensions, Inc.	INC	CO	12/29/07			SOLD
Platinum Choices, LLC	LLC	CO	12/29/07	$699		BUY NOW
Priceless Commodities, Inc.	INC	CO	12/29/07			SOLD
SomeDay Ventures, LLC	LLC	CO	12/29/07			SOLD
Nationwide Property Ventures, LLC	LLC	CO	12/29/07	$699		BUY NOW
	INC	FL	01/04/08	$699		SOLD
Capstone Properties, LLC	LLC	DE	08/01/08	$799		BUY NOW

Another website lists the following Nevada corporation for sale:

Shelf Corporation with Credit

AGED SHELF CORPORATION WITH CREDIT - TOLL FREE (888)286-9279

Shelf Corps with Credit For Sale

Aged shelf corporations with credit inventory:

Nevada Shelf Corporation with Credit

- D&B credit profile with 85 Paydex Score
- Multiple vendor tradelines
- 3 years old reputable, REAL business
- 100k credit line - equipment leasing™ - zero balance
- 30k bank issued credit lines - Visa, MC

Assur ***** Services Inc**

This company has been an operating business for over 3 years in the Clark County/Las Vegas, NV area. There is no outstanding debt and all tradelines have little or no balances

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owing. No late payments have ever been made on any accounts. As a matter of fact, payments are usually made at least a week or two in advance of the payment due date which is why the Paydex Score is so high - an 85 Paydex score is equivalent to a 750+ personal FICO score. Why wait months or years to establish business credit when you can own a turnkey Nevada shelf corporation with over 150k of bank credit and get a jumpstart on your business venture right now.

Own this Nevada shelf corporation with credit for $49,900

Criminals who are abusing State incorporation practices to conceal their identities seem to prefer such "off the shelf" corporations. By purchasing shelf companies, criminals can easily circumvent State incorporation requirements and rely on the fact that the current update requirements of most States will give criminals months if not a year head start on law enforcement authorities that are pursuing an investigation. To combat this practice, the Department strongly recommends legislation that: (1) requires all covered legal entities to provide updated beneficial ownership information to the State at the time of any transfer, sale, or change in beneficial ownership; (2) provides the sale or transfer of the ownership interest is not effective until such time as the proper documentation has been received by the Secretary of State; and (3) requires all legal entities to yearly certify that their beneficial ownership information is current, true and correct.

This increase in the sale of "shelf" or existing companies highlights an important loophole that the proposal endorsed by the National Conference of Commissioners on Uniform State Laws (NCCUSL) seeks to correct: that of a "look back" to existing companies. There are literally hundreds of thousands of U.S. companies that currently exist. Unless a mechanism is put into place to also regulate these entities and gather their beneficial ownership information, there exists a serious risk that they can and will be misused.

Take for example another U.S. company currently being offered for sale:

27 Years Old Nevada Corporation with Credit

- 22 Years old Experian credit file

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- EIN
- Bank Account
- No Judgements or Liens
- No UCC filings or Collections
- Clean credit history

***** Music ****

This company has been an operating business since early 1981 in the state of Nevada - Mineral County area. There is no outstanding debt and it has a clean credit history. Business classification is "Furniture and Home Furnishings Store" - SIC code 5700.

Shelf-Corp.com offers the lowest pricing on aged corporations guaranteed! Why pay $30,000, $40,000 or more somewhere else when you can buy this **aged corp with credit** here for thousands less!

27 years aged old, Nevada corporation is on sale now for only $15,000

Here, a company that has been in existence since 1981 can be purchased "with credit" for a mere $15,000. This ad illustrates the inherent problem of any legislation that is exclusively forward looking. Such legislation will again merely create a loophole, drive illegitimate traffic to that loophole, and create a new and lucrative market for "aged" companies that do not have to disclose any beneficial ownership information.

The Department recommends that current legislative efforts include a "look back" provision that will require existing companies to provide current beneficial ownership information. If the company fails to provide such information then the Secretary of State should be required to initiate dissolution proceedings against the company.

D) Penalties for the Misuse of Legal Entities/Penalties for False Information and/or Willful Blindness

In an effort to enforce this system, the Department believes it is critical for both States and the Federal Government to have a variety of tools at their disposal for the enforcement of shell company legislation. The Department envisions the legislation providing three distinct enforcement tools.

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First, in addition to any civil or criminal penalty that may be imposed by a State, the Department believes it is also critical to protect our national interest in enforcing federal law, by providing both civil and criminal penalties under federal law, similar to those contained in S. 569. The Department would strengthen the penalties in S. 569 by consistently applying the criminal intent of acting "knowingly." This modification will prevent individuals from escaping liability by acting "willfully blind" in their formation and use of our legal entities. Moreover, the Department also recommends adopting language similar to that contained in the Aggravated Identity Theft Statute, 18 U.S.C. 1028A §§ (2), (4), authorizing consecutive prison sentences for repeated and aggravated violations. Such a provision would target those criminally complicit service providers that are the worst offenders in this area and who repeatedly promote and use U.S. shell companies for criminal activity.

Second, those individuals who act negligently or recklessly in providing false information to the State or failing to update information with the State, should be subject to civil penalties.

Third, States should be required to immediately dissolve any legal entities that (1) fail to certify that their beneficial ownership on file with the State is current, true and correct; and (2) are shown to have otherwise failed to comply with the statute.

These three tools will allow the Government to bring effective, proportional and dissuasive sanctions against bad actors while not implicating otherwise innocent failures by small business to file required paperwork.

II) Other Issues

In addition to the broad framework that has been provided above, the Department believes there are a number of secondary suggestions that will positively impact any proposed legislation in this area.

First, in the course of discussing possible solutions, some parties have suggested making a specified individual located in the State of formation responsible for collecting beneficial ownership information only after a request is made by law enforcement for this information. The Department strongly opposes such an idea. Such a provision would be easy to evade as suspects could transfer ownership from one person to the next so that the

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trail is already cold by the time the specified individual reaches out to his last known contact. It would also openly signal the existence of a criminal investigation.

Next, the Department believes that any legislative solution must apply equally to both U.S. and foreign persons applying to form a legal entity or become a new owner of a preexisting legal entity. To only require foreign persons to provide beneficial ownership information or a copy of a passport would invite fraud as an increasing number of individuals could be expected to falsely claim to be a U.S. person or use straw actors. Such an approach may raise questions of consistency with our international undertakings and obligations, and would be contrary to the open investment policy of the United States.

Finally, the legislation should require that all States that have not already done so pass legislation prohibiting so called "bearer shares" to bring the United States fully into compliance with the Financial Action Task Force recommendations on this issue.

III)Conclu sion

I would like to conclude by expressing the gratitude of the Department of Justice for the continuing support that this Committee has demonstrated for anti-money laundering enforcement. The Department believes that we must continue to strengthen our anti-money laundering laws, not only to disrupt and dismantle drug trafficking and other international criminal organizations, but also to fight terrorism, white collar crime and all forms of criminal activity that generate or utilize illegal proceeds. The downside of globalization is that it affords perpetrators of crime new outlets and vehicles for these crimes, and thus poses new threats.

The Department is committed to safeguarding the privacy and civil liberty interests of Americans and is confident that those interests are not at risk when the federal government takes sensible steps to rein in the abuse of shell corporations. We in the Department of Justice look forward to working with Congress and with our colleagues in the Department of Treasury and the Department of Homeland Security, to address the issues identified in this hearing.

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HON. ELAINE MARSHALL,
NORTH CAROLINA SECRETARY OF STATE
CO-CHAIR, NATIONAL ASSOCIATION OF SECRETARIES OF STATE (NASS) COMPANY FORMATION TASK FORCE

TESTIMONY BEFORE THE SENATE HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS COMMITTEE

AMENDED TESTIMONY SUBMITTED
JUNE 18, 2009

National Association of Secretaries of State
444 North Capitol Street, NW – Suite 401
Washington, DC 20001
202-624-3525 Phone
202-624-3527 Fax
www.nass.org

NASS

Testimony of Hon. Elaine Marshall, North Carolina Secretary of State

Co-Chair, Company Formation Task Force, National Association of Secretaries of State

Before the Senate Homeland Security and Governmental Affairs Committee – June 18, 2009

"Examining State Business Incorporation Practices: A Discussion of S. 569: the Incorporation Transparency and Law Enforcement Assistance Act"

Chairman Lieberman, Ranking Member Collins, and Members of the Committee, on behalf of my colleagues at the National Association of Secretaries of State (NASS), I would like to extend our appreciation for your invitation to participate in this hearing. I am wearing two hats today; one as North Carolina Secretary of State, a job I have proudly held since 1997, and the other as the Co-Chair of the Company Formation Task Force formed by the National Association of Secretaries of State (NASS) in February 2007.

As Co-Chair of the NASS Company Formation Task Force, I oversaw the drafting and release of the body's report and recommendations, which were adopted by the full membership in July 2007 and reaffirmed in July 2008. I also helped to introduce a resolution to oppose the first iteration of the bill we are here today to discuss, S. 2956: "The Incorporation Transparency and Law Enforcement Assistance Act," a resolution which was unanimously supported by my peers and adopted by NASS in July 2008.

As such, I remain opposed to the enactment S.569 because of the additional record keeping requirements it will place on states and the uncertainty of the costs associated with implementing such broad changes. In making the case against this bill, I would like to discuss the mechanics of business formation and record keeping at the state level and highlight how the passage of S.569 will negatively alter those processes. I will also explain why the NASS approach is more prudent and less expensive. To the extent that much of the information sought by law enforcement already resides with financial institutions and in IRS files, we respectfully suggest that Congress redirect its attention to requiring those institutions to share it, instead of having state agencies collect it.

First, a bit of background on how NASS became involved in this issue. Along with many of my colleagues, I became aware that several federal agencies were examining the issue of ownership information collection by state governments at the beginning of 2006, just before the U.S. Government Accountability Office (GAO) released its April 2006 report on this topic.[1] As you may know, GAO concluded that the laws of incorporation in most states allow company owners varying degrees of anonymity and privacy, which led some in Washington to wonder if the process was being used by criminals hoping to elude detection by authorities. Just prior to the release of the GAO report, a separate report from the U.S. Treasury and other agencies raised related concerns about limited beneficial ownership information.[2] In November 2006, Senator Levin (D-MI) chaired a hearing in the Permanent Subcommittee on Investigations and heard testimony from the federal agencies responsible for these reports, as well as the state corporate division directors from Massachusetts, Delaware, and Nevada. At the conclusion of the hearing, Senator Levin announced

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that he was not satisfied with the efforts of the states to collect ownership information, warning that more aggressive state action was needed to improve what he saw as inadequate practices.

In early 2007, I sent a letter to Senator Levin on behalf of NASS asking that he hold off on introducing federal legislation until our association had an opportunity to convene a Task Force to review the issue and develop meaningful recommendations for federal and state consideration.[3] In February 2007, Nebraska Secretary of State John Gale and I agreed to serve as Co-Chairs of the NASS Company Formation Task Force, along with other members, including Secretaries from Georgia, Indiana, Minnesota, Nevada, New York, and Wyoming. Senior corporations division staff from Delaware, Massachusetts, and Maine also agreed to participate.

In July 2007, members approved the NASS Company Formation Task Force Report and Recommendations,[4] which include the following:

- A ban of bearer shares and interests in bearer form, a practice that was for all intents and purposes prohibited by states' case law, but not clearly outlined in state statute.[5]

- A requirement that entities file a periodic report that includes the name and address of a natural person in the U.S. who has responsibility for providing access to the list of owners of record for a business entity. That name would be a part of the public record and, therefore, available to law enforcement without a subpoena.[6]

These basic recommendations have served as the basis for drafting the Uniform Law Enforcement Access to Entity Information Act, which is scheduled for a final vote before the Uniform Law Commission in July 2009. You will hear more details about this body and its draft language from Harry Haynsworth, but it is important to note that we have worked with this group since they began their drafting in 2007.

In May 2008, Senator Levin expressed his dissatisfaction with the NASS approach and introduced the Incorporation Transparency and Law Enforcement Assistance Act (S.2956). He reintroduced this bill in March 2009 as S.569. NASS and a number of other prominent organizations are currently on record in opposition to this bill, including: the Uniform Law Commissioners, the American Bar Association (ABA), and the National Conference of State Legislatures (NCSL).

During the past several years, this coalition has been working together to find appropriate state legislative and administrative answers that would:

1. Avoid the federalization of the company formation process, which has always been a state function. Federal legislation will bring federal rulemaking and regulatory authority into an area that has traditionally been the jurisdiction of states;

2. Create a way for company ownership data to be held by private individuals designated by the entities, rather than the Secretary of State or other state agency;

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3. Require that law enforcement agencies use subpoenas to inspect the ownership records rather than mandating that the Secretaries of State or state governments secure and provide them;

4. Avoid an immense, unfunded mandate requiring states to fund the hardware, software and staffing to collect, update, preserve and make accessible such data. There would also be a substantial cost for public education efforts regarding the complete change to filing requirements;

5. Prevent the office of the Secretary of State from becoming a law enforcement agency if compelled to regularly cross-check the entity ownership data against the Office of Foreign Asset Control's Specially Designated Nationals (SDN) List and report any suspicious matches. States are concerned that if required to collect and maintain beneficial ownership information, they will ultimately be required to verify the information and cross-check it all with the SDN List. This issue is especially important because while verification and cross-checking are not required in S.569, Senators Levin and Grassley, as co-sponsors, have said that states should verify the ownership information and run the information against the SDN List.

Here are some additional reasons why the NASS approach is more desirable:

The NASS recommendations strike an appropriate balance by supporting the goals of law enforcement without unnecessarily restructuring state governments or negatively impacting the business community. In its 2006 report on ownership information laws for corporations, GAO concluded that, "if a requirement to collect company ownership is considered, it would be useful for policymakers to consider options that balance the conflicting concerns among states, agents and law enforcement agencies."[7]

With nearly two million corporations and limited liability companies (LLCs) currently being formed within the United States each year, the NASS approach does not place an enormous unfunded mandate on state governments. Redirecting state agencies away from their current, ministerial role to one of collecting and processing ownership information will be an extremely costly venture.

As part of cost comparison research that is currently being conducted by NASS, initial state responses indicate that the costs associated with implementing S.569 are generally higher than the costs associated with the state uniform law approach being drafted by the Uniform Law Commissioners; and in some cases, substantially higher. For even the most technologically advanced states, maintaining beneficial ownership in a database will require the development and design of a new system. In some cases, this move will involve multiple state agencies (i.e. Secretary of State and Department of Licensing.) It will also require the states to conduct extensive, comprehensive and costly public education campaigns to ensure compliance.

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Furthermore, there is concern regarding the competitive grant program in S.569 that is supposed to provide funding for states to carry out the mandates of the federal law. We believe this funding is already overcommitted with original requirements to support state and local homeland security efforts. Much of the funding is also required, by law, to go straight to local government for first responders. Therefore, it is unlikely that the Secretary of State's office would ever see any of this funding.

Finally, states have spent tens of millions of dollars in recent years improving their online transactions in order to make state government more responsive to the needs of citizens and business communities. Transactions that used to take substantial time are now conducted swiftly and efficiently with Internet-based, online technologies. We are concerned that S.569 will turn back the clock and undo such state progress and technological investments. States need to meet the needs of the American legal and business community to facilitate important and legitimate commercial transactions worth trillions of dollars.

Additionally, the NASS approach does not overburden small businesses, many of whom are struggling economically right now. In crafting its recommendations, one of the major goals of the NASS Company Formation Task Force was to avoid any increased financial or filing burdens on small businesses, particularly "mom and pop" or family-owned businesses. These entities are easily identified by bankers and chambers of commerce as legitimate, small business enterprises. NASS also recognizes the millions of entities that consist of owners who are licensed by the states to perform specialized services, such as doctors, lawyers, accountants, engineers and realtors. Since these professionals are already vetted under state law and must have their licenses renewed on a regular basis, we believe it is important to avoid adding to their document filing duties and related costs.

It is also important that any changes in law remain simple and straightforward so as not to result in unintentional non-compliance. Definitions used for "beneficial owner" in S.569 assume that whoever controls the funds of the entity also controls the management. This is not necessarily the case and confusion about definitions could lead to problems for small businesses. Definitional clarity/consensus is an issue that is specifically acknowledged by the Financial Action Task Force (FATF) in its 2005-2006 report entitled, "Annual Review of Non-Cooperative Countries and Territories."[8] The FATF report states,

> ....the exercise was a useful tool for FATF members to identify several areas where there were differences of interpretation within the FATF regarding certain FATF NCCT criteria ("horizontal issues"), for instance:...difficulties in establishing beneficial ownership with regards to legal entities, including bearer shares and trusts. The FATF decided that no reviewed jurisdiction would be listed based on these issues.[9]

Unlike S.569, the NASS Company Formation Task Force recommendations also support the protection of privacy for investors and family members and would not make their personal business matters a part of the public record. While S.569 does leave it up to each state as to how it would

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handle the public nature of the additional information that must be collected, that simply means the state would be forced to establish and maintain costly redaction and parallel systems – one public and one protected. We hope that representatives from the small business community, venture capitalists, and other business-related entities will be asked to discuss the impact that S.569 would have on them and that they will be involved in any deliberations on this legislation. It does not appear that any are here today to testify.

In summary, the NASS approach and the work of individual states reflects significant progress in addressing the Financial Action Task Force (FATF) Recommendations. To date, only one nation in the world – Italy – is in compliance with their recommendation on the collection of beneficial ownership information.[10] In its mutual evaluation of the United States in June 2006, FATF notes of its Recommendation 33 on beneficial ownership,

> While the investigative powers are generally sound and widely used, there are no measures in place to ensure that there is adequate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities. There are no measures taken by those jurisdictions which permit the issuance of bearer shares to ensure that bearer shares are not misused for money laundering.[11]

The official FATF recommendation for corrective measures on Recommendation 33 was to,

> Undertake a comprehensive review to determine ways in which adequate and accurate information on beneficial ownership information may be available on a timely basis to law enforcement authorities for companies which do not offer securities to the public or whose securities are not listed on a recognized U.S. stock exchange. It is important that this information be available across all states as uniformly as possible.[12]

That is exactly what the NASS Task Force and collaborating organizations have done by proposing an alternative approach to S.569.

In the meantime, the states that have been scrutinized in those early federal government reports have moved forward to strengthen their processes and to address real or perceived loopholes in the law. For example, Nevada, which was featured during the subcommittee hearing in 2006, passed legislation in July 2007 that requires any non-publicly traded corporation to maintain a list of its owners of record at a registered office or principle place of business in the state.[13] The entity must also file the name and contact information of the custodian of the list of owners with the Secretary of State's office. Any change to the list of owners must be updated within 10 days. Upon the request of any law enforcement agency in the course of a criminal investigation, the Secretary of State can require the corporation to provide a copy of the list of owners within three business days. Failure to do so could result in suspension or revocation of the entity's charter. For an LLC, the same requirements apply, however the list that is required is of managers and members.

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Wyoming and Delaware have also passed significant legislation since the release of the multi-agency, federal government reports in 2006. The NASS Web site (.nass.) offers summaries of business formation laws and filing requirements if you would like additional information.[14]

In my home state of North Carolina, S.569 would be a significant burden, and we are a state recognized for innovation with technology and maintain an in-house programming staff, who report to me. Other states will experience an even larger burden if they are not as well developed electronically or have to depend upon outside vendors or other state agencies to perform and manage their computer programming work. Our experience with technology has been achieving a high level of customer satisfaction as well as internal efficiencies for filing and cash management functions. We would be very reluctant to consider any rollback on technology with regard to managing the workload in North Carolina.

North Carolina currently has 548,000 entities within our databases, and all filings are examined before filing to prevent our databases from population by legally deficient entities. North Carolina does not permit online creation filings, but does accept Annual Reports online. We have robust online filing abilities in other subject matter areas, including electronic notarization with a well-developed law, national e-notary standards, and a few authorized e-notary vendors. More than 100 individual notarized lobbying reports were filed online for the first quarter of 2009.

To assess the costs to the states under S.569 is almost impossible. Without administrative rules, calculating the cost is an inaccurate undertaking. What the bill states versus what we think it means – or will mean – in order to be effective are quite different. For example, adding additional fields to forms is not very hard, establishing a new searchable database is not overly difficult if you have prior experience in the activity, and committing the business logic rules to text is the tedious "finishing up" activity that requires discipline. All are doable when looking to the future.

My colleagues and I have a serious concern regarding certain provisions of S.569 in that there will be a huge burden on both the entity as well as the filing agent at the time of creation. No corporation or LLC has any members or owners of any description at the moment the filing is made. It is only after that filing has been made that ownership interest or other stakeholders can be determined. Therefore, the filing process will be a two-fold filing function rather than a one-time event. Please note that almost every state has an expedited filing process to meet the legitimate needs of the business community, as requested by the business Bar of each state.

In 2008, 58,000 new entities were created in North Carolina. The unknown, but expected, requirement for this bill to be meaningful is the application to existing business entities. If proposed Sec.2009.(a)(1)(B) requires all existing entities to provide beneficial ownership information on an annual basis (not just those businesses created after the effective date), then entirely new processing and educational programs will have to be crafted. Everyone will need to provide citizenship or status information. Screening by physical addresses will be inadequate. Responsibility is placed on formation agents, but the bill is silent as to the responsibility for those entities created without a formation agent, estimated to be sixty percent of North Carolina's filings. An educational undertaking to all new entities, approximately 58,000 per year, is of one cost. If all 548,000 entities

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of record must be informed, the cost is much greater. Theoretically, we have annual contact with 450,000 entities; however, for the 94,000 North Carolina nonprofits that have no current annual report filing requirement, the challenge will be extremely difficult.

If existing entities (548,000) will be made to comply, several staff members will need to be added or redirected from existing workloads to assist filers to understand the changes and to begin the dissolution process for noncompliance. Without additional staff, either current processing becomes delayed for all or backlogs build up for certain other equally valuable functions. Additional personnel costs are hard to determine without addressing concerns expressed by my colleagues as to the application and interpretation of S.569. Attempting an evaluation based on most responsibility falling on the state, I estimate a minimum fifty percent staff increase in the customer service and back office functions of North Carolina's corporations division.

If there is *no* requirement for existing entities to comply, costs for North Carolina would be under $100,000 to create new forms, a new confidential database, and the associated business rules and search abilities. If S.569 is applied to the existing 548,000 active North Carolina business entities of record, costs seriously escalate. A single mailing (letter size, folded with three sides perforated, mailed at bulk rate) by a competitive bid will cost approximately slightly under $390,000. A re-mailing of a fifteen percent default group would be almost $58,000. Storage of paper filings and archiving become costs estimated at $150,000 per year, as retention schedules are met. As online filings become more common, storage and archiving costs become lower but equipment replacement expenses escalate.

The huge volume of materials S.569 will generate over just a few years needs to be considered. On its face, Annual Report numbers will not increase, but Annual Reports are public in most states. If they contain confidential beneficial ownership information in order to keep current, redaction will need to occur or separate filing systems will need to be maintained, possibly increasing the image load exponentially. North Carolina is currently "burning out" two of our sixteen servers a year as we find ourselves in a constant backup mode with the 20 million images we currently maintain (not all of these are business entity items).

I can predict two significant factors that will occur in North Carolina if nonprofits are made to file Annual Reports. First, general confusion will be the norm as nonprofits seldom have "owners" of any definition; second, resistance and pushback will be huge as church folks especially consider reporting to the state *highly* objectionable (North Carolina knows this from trying to implement nonprofit Annual Reports in the early 1990's); and the Secretary of State's Office will spend vast amounts of resources dissolving and reinstating nonprofits, as well as others, for years. I can't begin to describe the ongoing societal nightmare and administrative difficulties this will create.

Secretaries of State around the country are very concerned that the term "beneficial ownership" is not well-established in American jurisprudence and that it will fall upon us to interpret what that means. It is also of concern that the law would apply to formation agents but does not specify who would be responsible in the case that a formation agent is not used. Filing offices have no desire to be the default keeper and verifier of the identity of non-United States citizen beneficial owners. We are also concerned that verification of such information may ultimately fall on the filing

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entity, which would create a larger than imaginable problem for us. Also of concern is that states will be required to compare the list of entities in their databases with the Suspicious Designated National list, unless Secretaries of State or other state filing agencies are exempted from that provision of federal law.

We have a history of cooperation with all law enforcement in North Carolina, and as I now begin my thirteenth year as Secretary of State, we have never had a request from a law enforcement agency that we could not fulfill.

If you sense resistance from my colleagues, you are correct. We understand the concern with money laundering – we all want it discovered and stopped, and we all want to assist law enforcement. But we do feel these efforts are going to be of limited effectiveness compared to other possible avenues of recourse, such as through other government agencies or adding safeguards to the multiple money pathways existing today.

Because of the foregoing, the NASS Company Formation Task Force has been working with the drafting committee of the Uniform Law Commission (ULC)during the past year and a half to craft an alternative that will provide a pathway to find the information that the Senate seeks, without placing the burden on the state administrative filing office.

Given the lack of a clear belief in the efficacy of this plan, additional functions will be necessary. Verification will be needed by someone, cross checking with other lists will be needed, concern that updating will be inconsistent (annual to some, as needed with others), and difficulty with definitions are a few of these layers. Fearing those future costly requirements, NASS requested ULC to propose a uniform law with an expectation that it could provide meaningful assistance to law enforcement with a minimum burden on the large number of legitimate small businesses that populate our databases and provide the economic engines of our states.

S.569 (previously S.2956) has already had a serious beneficial effect and has achieved results. Highlighted states have closed perceived gaps in the law. We have put considerable intellectual effort into an alternative workable process that I believe is doable for states to enact. NASS has not taken an official position on the ULC Uniform Act proposal because ULC has not finished its processing, though it will finish by mid-July. Shortly thereafter, NASS will hold its annual summer meeting. I will honestly tell you I have concerns about the NASS meeting due to state budget travel restrictions, including North Carolina's, but I will be there.

Whether or not beneficial ownership information is public or confidential is of concern. Since beneficial ownership under S.569 is to be provided upon specific legal process, it is deduced the information shall be confidential. Some states have strong open records laws and constitutional provisions that will be problematic. I would intend to have an additional database developed in North Carolina and declared an exception to North Carolina's public records law to avoid all the inquiries and complaints regarding marketing mailings, family law litigants seeking corporate information, debt collectors, the just plain nosey, and more. If we are required to verify the information against the Specially Designated Nationals List that would be a huge challenge of unknown cost. Public education costs could be expensive.

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We all must remember that either of these proposals represents a cultural change – not just for the filing offices who view their function as simply ministerial, but a cultural change for everyone engaged in business of most types in the United States of America. Sadly, ground zero for the fallout to these cultural changes will be each state's filing office, and we are gravely concerned. Viewing the financial and human asset commitment contrasted with the efficacy of the proposal, it is hard to find significant added value and meaningfulness.

In closing, NASS members are wary of any federal law that burdens states and legitimate businesses yet provides lawbreakers with the ability to evade it. The obvious argument is that the extremely small number of entities that are registered to do business that may be engaged in money laundering, terrorist financing and tax evasions are probably not going to file accurate or truthful information to state government. Therefore for the overwhelming number of legitimate, law abiding businesses, trying to stay afloat in these difficult times, we think the NASS approach is a more reasonable, simple and unobtrusive solution which would allow small business owners to comply without having to hire a legal team to decipher filing requirements.

My colleagues and I are thankful for the opportunity to testify today and for the opportunity to submit additional written testimony for the record. I am including the NASS Company Formation Task Force Report and Recommendations, along with the association's July 2008 resolution to pursue our alternative approach to S.569.[15]

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[1] U.S. Government Accountability Office, *Company Formations: Minimal Ownership Information is Collected and Available*, GAO-06-376, April 2006, available at http://www.gao.gov/new.items/d06376.pdf.

[2] U.S. Department of Treasury, et. al., *U.S. Money Laundering Threat Assessment*, December 2005 (Released January 2006), available at http://www.ustreas.gov/offices/enforcement/pdf/mlta.pdf.

[3] National Association of Secretaries of State, "Letter to Chairman Levin (D-MI) Regarding Results of Task Force," September 13, 2007, available at http://nass.org/index.php?option=com_content&task=view&id=113&Itemid=312.

[4] National Association of Secretaries of State, NASS Company Formation Task Force Report & Recommendations, July 2007, available at http://nass.org/index.php?option=com_content&task=view&id=113&Itemid=312.

[5] Ibid, p. 6.

[6] Ibid, p. 5.

[7] U.S. Government Accountability Office, *Company Formations: Minimal Ownership Information is Collected and Available*, GAO-06-376, April 2006, p. 1 (sidebar).

[8] Financial Action Task Force, *Annual Review of Non-Cooperative Countries and Territories: 2005-2006*, June 2006, available at http://www.fatf-gafi.org/dataoecd/44/9/37101772.pdf.

[9] Ibid, p. 17.

[10] Information provided in Financial Action Task Force Letter to Congress, January 2007.

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[11] Financial Action Task Force, *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism - United States*, June 2006, p. 237, available at http://www.fatf-gafi.org/dataoecd/44/9/37101772.pdf.

[12] Ibid, p. 237.

[13] Nevada Model Registered Agents Act (NRS 77.310), Chapter 77. Sec. 010-270, July 1, 2008, available at http://www.leg.state.nv.us/Nrs/NRS-077.html.

[14] National Association of Secretaries of State, *Survey of State Business Entity Laws*, May 2009, available at http://nass.org/index.php?option=com_docman&task=doc_download&gid=653.

[15] National Association of Secretaries of State, "NASS Renews Company Formation Task Force for 2008/2009 with Expanded Mission Statement," July 2008, available at http://nass.org/index.php?option=com_docman&task=doc_download&gid=318.

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NASS Company Formation Task Force Report & Recommendations

Approved by the NASS Membership on 7/18/07

Co-Chairs:
Hon. Elaine Marshall (NC)
Hon. John Gale (NE)

BACKGROUND

At the beginning of 2006, the federal government produced two major reports on the company formation process that raised important questions for Secretaries of State.

At the request of U.S. Senators Carl Levin (D-MI) and Norm Coleman (R-MN), the leaders of the Senate Homeland Security Committee's Permanent Subcommittee on Investigations, the U.S. Government Accountability Office (GAO) released an April 2006 report on the collection of beneficial ownership information during the company formation process. Its conclusion that the laws of incorporation in most states allow company owners to remain anonymous led some to wonder if the process was being used by criminals hoping to elude detection by authorities.

Meanwhile, a separate multi-agency report entitled, "Money Laundering Threat Assessment" raised related concerns about limited beneficial ownership information. Federal agencies contributing to this report included the U.S. Treasury, Internal Revenue Service, U.S. Department of Justice, U.S. Department of Homeland Security, the Federal Reserve and the U.S. Postal Service.

Based upon the findings of these reports, Senators Levin and Coleman arranged for the Senate Permanent Subcommittee on Investigations to hold an oversight hearing in November 2006. The hearing sought to examine how the lack of company ownership information in state files impeded law enforcement efforts in combating criminal activities. Officials from Delaware, Massachusetts, and Nevada joined federal agency representatives in testifying about their state procedures and requirements for forming business entities.

At the time of the hearing, Senator Levin expressed interest in a Massachusetts law that requires companies to maintain their list of beneficial owners and to provide that list to the Secretary of State upon request. In his view, the lack of information gathering practices employed by states could prevent authorities from identifying tax cheats, money launderers, and possibly, terrorists. He also expressed concern over a Financial Action Task Force (FATF)[1] evaluation that gave the U.S. a failing grade in collecting beneficial ownership information. Senator Levin warned that if the states didn't come up with some solutions to address his concerns, he would introduce federal legislation to create greater transparency.

In January 2007, NASS Business Services Committee Chair Elaine Marshall of North Carolina took action. She sent a letter to Senator Levin's office requesting the opportunity to convene a NASS task force to study the company formation process and to develop meaningful recommendations for federal and state consideration. Senator Levin agreed to postpone the introduction of any legislation until NASS had the opportunity to issue its findings.

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[1] World leaders established the Financial Action Task Force on Money Laundering (FATF) at the G-7 Summit held in Paris in 1989.

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The following month at the NASS 2007 winter conference, Secretary Marshall (NC) and Secretary of State John Gale of Nebraska agreed to serve as co-chairs of the NASS Company Formation Task Force. Other Secretaries of State serving on the NASS Business Services Committee volunteered to serve on the task force and some offered to recruit their state director of corporations to assist with this endeavor.

As such, the NASS Company Formation Task Force consisted of the following members:

Secretaries of State	Secretary of State Office Staff
Hon. Elaine Marshall, North Carolina (Co-Chair)	Haley Haynes, North Carolina
Hon. John Gale, Nebraska (Co-Chair)	Judy Jobman, Nebraska Colleen Byelick, Nebraska
	Rick Geisenberger, Delaware Eileen Simpson, Delaware
Hon. Karen Handel, Georgia	Chauncey Newsome, Georgia
Hon. Todd Rokita, Indiana (NASS President-Elect)	Liz Keele, Indiana Marci Reddick, Indiana
	Laurie Flynn, Massachusetts
	Tim Poulin, Maine
Hon. Mark Ritchie, Minnesota	Bert Black, Minnesota
Hon. Ross Miller, Nevada	Scott Anderson , Nevada
Hon. Lorraine Cortez-Vazquez, New York	Paul LaPoint, New York Denise Lauer, New York
Hon. Max Maxfield, Wyoming	Tom Cowan, Wyoming Genie Sawyer, Wyoming Barb Boyer, Wyoming

MEETINGS

The NASS Company Formation Task Force met via conference call every two weeks from early March through July 2007. Member participation rates were very high and the calls allowed for lively debate and discussion. During the first few calls, the task force decided upon its mission, goals, and process. Members decided early on to limit task force participation to Secretaries of State and/or their designated staff. However, the following stakeholders received notification about the task force and its work:

- Other state agencies responsible for company formation
- International Association of Commercial Administrators (IACA)
- The American Bar Association (ABA) Corporate Laws Committee
- The ABA Partnership Laws Committee
- National Conference of Commissioners on Uniform State Laws (NCCUSL)

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- National Governor's Association
- Registered agent community
- Various federal agencies

The NASS Company Formation Task Force held a conference call with several of the stakeholders in early May and followed that with an in-person meeting later that month during the IACA Annual Conference. These discussions provided an excellent opportunity to explore shared goals and to craft reasonable, workable solutions in a short period of time.

Early conference call discussions focused on first identifying issues with potentially simple resolutions. Another key focus was clarifying Senator Levin's exact concerns and addressing those from a state perspective. Meetings between a task force member, NASS staff and Laura Stuber of Senator Levin's office produced two key directives that the task force recommendations needed to address:

1. Find a way to provide a list of shareholders, members, or beneficial owners kept in the state of organization that would be available to law enforcement without a subpoena.
2. During the company formation process, someone must be required to check the Office of Foreign Asset Control's (OFAC) Specially Designated Nationals (SDN) List to ensure that none of the owners, members, or shareholders is on the watch list.

At the IACA Annual Conference in May, the NASS Company Formation Task Force met in person to begin drafting recommendations. Because so many task force participants attended the conference, it was an ideal time for holding a drafting session. In addition to NASS Company Formation Task Force participants, representatives from the registered agents, the ABA, and NCCUSL observed this drafting session. The task force developed draft language for six recommendations at this meeting with more than thirty participants. In addition, the IACA Business Organization Section passed a resolution endorsing the efforts of the task force.

The task force soon notified both ABA and NCCUSL that their assistance would be requested in drafting amendments to the Model and Uniform Business Entity Laws if NASS members approved the task force's recommendations at the association's July 2007 summer conference. Both organizations needed to get a written notification in order to place the request in their drafting queue.

Additionally, the task force developed a survey on state company formation practices. More than thirty states responded, providing a solid framework for members to use during development of their recommendations.

The results of the survey and other useful resources became part of a web-based information page for task force members. It also includes new and pending company formation legislation from Delaware, Massachusetts, and Wyoming.

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RECOMMENDATIONS OF THE NASS COMPANY FORMATION TASK FORCE

On July 18, 2007, the NASS Membership Approved the approved the following recommendations developed by the NASS Task Force and amended by the NASS Business Services Committee:

1. NASS will draft a letter to OFAC regarding state promotion of the current obligation that individuals and business entities have to comply with the Trading with the Enemy Act (31 CFR, Subtitle B, Chapter V, as amended), and suggest a meeting to discuss usability issues, public education, etc. (attachment 1)

2. NASS and IACA will compile and periodically update a comprehensive overview of state business entity laws for federal and international law enforcement use. The report would cover how each U.S. business entity statute handles the collection of ownership information, filing requirements, and periodic reporting requirements. It will also explain how law enforcement can access ownership and other relevant information.

3. States are encouraged to engage in educational outreach to the relevant communities about checking the OFAC SDN List. Pending resolution of the issues contained in recommendations 1 and 4, states are encouraged to examine their statutes and other requirements for annual or biennial reporting by business entities and determine what amendments to statutes and additional language may need to be added to the statutes, applicable notices, or forms to advise entities of the OFAC SDN List, and to identify specific individuals who may be contacted by federal law enforcement authorities with regard to investigative concerns about owners of record for their business.

4. NASS will draft a letter requesting that ABA and NCCUSL develop language to amend Model or Uniform Business entity laws requiring entities to file a periodic report that includes a name and address of a natural person in the United States that has responsibility for providing access to the list of owners of record for a business entity. That name would be a part of the public record and therefore available to law enforcement without a subpoena. NASS also recommends that NCCUSL and ABA consider the historical precedent of confidentiality of company ownership when developing recommended language for Uniform and Model Business Entity Acts.

5. NASS recommends a two-pronged approach to "bearer shares and interests held in bearer form." First, NASS will include a request in letters to ABA and NCCUSL that they also address clarifying Model and Uniform Entity Laws that bearer shares and interests held in bearer form are not permitted. In the interest of time, states should also examine their statutes to clarify prohibitions on bearer shares and interests held in bearer form. Currently state laws do not allow bearer shares, but language can be vague.

NEXT STEPS

If the NASS membership approves and adopts the task force recommendations, a follow-up letter must be sent to both ABA and NCCUSL containing this language and asking them to begin their drafting processes. The ABA drafting timeline could be complete by April 2008, whereas the NCCUSL process will take until July 2008.

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NASS will also request a meeting with Senator Levin and Senator Coleman and other concerned members of the Senate Permanent Subcommittee on Investigations to present them with the recommendations and discuss next steps.

Finally, NASS will convene a meeting of business entity law drafters to define and clarify the differences, if any, between "beneficial owners" and "owners of record."

For more information on the NASS Company Formation Task Force, please contact:

Leslie Reynolds, Executive Director
National Association of Secretaries of State
444 North Capitol Street, NW-Suite 401
Washington, DC 20001
202-624-3525
reynolds@sso.org
://www.nass.

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Attachment 1

NASS
National Association
of Secretaries of State

June 8, 2007

Mr. John Smith
Associate Director, Program, Policy and Implementation
Office of Foreign Asset Control
United States Treasury
1500 Pennsylvania Avenue, N.W.
Washington, DC 20220

Dear Mr. Smith:

The National Association of Secretaries of State (NASS) has put together a Company Formation Task Force to address issues of ownership information and the company formation process. The NASS Business Services Committee decided to organize this Task Force to respond to and address concerns raised by Sen. Levin and other members of Congress on these issues.

The NASS Task Force has had regular conference calls on the broad issues and regulatory implications of providing ownership information to investigative authorities. We have also addressed the issues of the OFAC Specially Designated Nationals List (SDN). The Task Force has participants from 12 states and has conferred with other organizations including committee representatives from the American Bar Association (ABA) and the National Conference of Commissioners on Uniform State Laws (NCCUSL). Our Task Force met recently during the annual conference of the International Association of Commercial Administrators (IACA) to begin drafting some recommendations that the NASS membership will consider during our July 2007 Summer Conference.

One of the goals of the NASS Task Force is to find ways to assist OFAC in performing its duty to educate businesses and individuals about the importance of checking the OFAC SDN List.

The states are very willing to provide assistance in the area of public education. However, before we can encourage the public to utilize the SDN List, it is vitally important to clarify and simplify some of the processes first:

1. In earlier discussions with OFAC, we addressed our concerns about the usability and "searchability" of the OFAC SDN List. If states are going to begin referring businesses to the OFAC website and OFAC publications, it will be critical to address the fact that the current SDN List published on OFAC's website is not user-friendly for typical businesses and individuals that are required to check the list. We discussed bringing together a group of filings officers and company formation agents to advise OFAC on ways to make the list searchable and "real-time". We would like follow up on this suggestion. In its current form, the SDN List is not searchable, is not certified by OFAC as accurate and is not updated frequently enough to make any certification that the list has been checked meaningful. Once improvements are made to the list, we think states would be willing to include a link to the SDN list on their website.

2. We would like to help arrange OFAC training seminars for state filing offices. A review of the training seminars on your website indicates that the sessions are targeted to specific industries like banking,

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international trade and insurance. We would like to work with you to develop a training class that could be done for state officials so that they could assist in educating the business community about their obligations under federal law, including the SDN List and how to use it.

3. We would also like a "talking points" document that could help us to promote compliance with federal law and the specifics and details involved with the OFAC List. We want to ensure that simple, accurate information is provided in print and online that informs individuals and entities of their responsibilities under federal law. Contact information for OFAC so that questions may be answered and clear, simple instructions are essential to ensure compliance by the public. We would also like to work with you to create a list of vendors that might be able to help those states who would like to try and perform searches from their state system.

4. At the above mentioned IACA conference, a representative of the Small Business Administration (SBA) talked about a program they have established through the offices of the Secretaries of State. Representatives from SBA have developed materials and come to the state offices on a regular basis to answer questions for people interested in starting a business. In our discussions with SBA, it became clear that they were not familiar with the SDN List. We would encourage OFAC to reach out to the SBA to include them in any sort of public education campaign.

In short, we are committed to helping OFAC educate the public and the business community at large about the extremely important work you do and the reasons why people need to be vigilant about checking the SDN List. It should not be the duty of the office of the Secretary of State (or other relevant state agency) to check names of beneficial owners against the OFAC SDN List.

The Senate Permanent Subcommittee members have emphasized the importance of our working together and we take that responsibility very seriously. We would like to meet with you to discuss how to move forward on these very important issues. Please contact Leslie Reynolds (202)624-3525 at the National Association of Secretaries of State to coordinate this meeting.

We appreciate your commitment to this issue and we look forward to working with you.

Sincerely,

Elaine F. Marshall

John A. Gale

Hon. Elaine Marshall, NC Secretary of State
Co-Chair
NASS Company Formation Task Force

Hon. John Gale, NE Secretary of State
Co-Chair
NASS Company Formation Task Force

cc: NASS Company Formation Task Force
Hon. Deb Markowitz, Vermont Secretary of State, NASS President
Laura Stuber, Majority Counsel, Senate Permanent Subcommittee on Investigations

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NASS
National Association
of Secretaries of State

NASS Renews Company Formation Task Force for 2008/2009 and Expanded Mission Statement

The NASS Company Formation Task Force is renewed and reauthorized for a full year from this date and the 2008-2009 President of NASS is authorized to appoint such leadership and committee restructuring as he deems appropriate; and

The reauthorized NASS Company Formation Task Force will:

- develop a strategy to oppose S.2956 The Incorporation Transparency and Law Enforcement Assistance Act,
- seek U.S. Senate committee hearings on said bill before any committee markup might occur,
- alert the Secretaries of State when contacts need to be made with their U.S. Senators,
- cooperate with our NASS partners, including but not limited to ABA, NCCUSL, and NCSL to continue developing reasonable, practical, cost-effective and appropriate state-based responses to the issues raised by S. 2956 and,
- continue to meet and negotiate with federal agencies and U.S. Senate staff on the reasons why S.2956 is an extreme approach and why the NASS approach is the most sensible approach.

ADOPTED the day of July 2008 in Grand Rapids, MI

Hall of States, 444 N. Capitol Street, N.W., Suite 401, Washington, DC 20001
(202) 624-3525 Phone (202) 624.3527 Fax www.nass.org

WRITTEN TESTIMONY BY

THE HONORABLE ROBERT M. MORGENTHAU
DISTRICT ATTORNEY FOR NEW YORK COUNTY, STATE OF NEW YORK

Delivered By

ASSISTANT DISTRICT ATTORNEY ADAM S. KAUFMANN
CHIEF OF INVESTIGATION DIVISION CENTRAL
NEW YORK COUNTY DISTRICT ATTORNEY'S OFFICE

BEFORE THE UNITED STATES SENATE COMMITTEE ON
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

EXAMINING STATE BUSINESS INCORPORATION PRACTICES:
A DISCUSSION OF THE INCORPORATION TRANSPARENCY
AND LAW ENFORCEMENT ASSISTANCE ACT

WASHINGTON D.C.
JUNE 18, 2009

I would like to thank Chairman Lieberman, Senator Collins, and the Committee and Staff for the opportunity to present testimony at this hearing on state incorporation processes and the need for systemic reform. Senators Levin, Grassley and McCaskill have introduced an excellent piece of legislation that merits the support of the law enforcement community, and we thought it important to participate in today's debate and discussion.

Not only does the bill merit the support of the law enforcement community – it fully has its support. To quote a colleague who works on financial criminal investigations for a federal agency, "It's a no-brainer." This bill, from our perspective, is exactly what is needed to address the problems associated with shell companies created to hide criminal activity.

In so many areas of financial crime we see transparency as a simple solution to a host of problems. Systems promoting opacity and secrecy are the best friend of the money launderer, the child pornographer, the tax cheat, the fraudster, the corrupt politician, and indeed, the financier of networks of terror. The beauty of the bill we are discussing today is the simple solution it brings to a host of problems: Transparency. If there is one lesson we have learned in investigating financial crimes, it is that the best and easiest solution for many areas of criminal conduct is to encourage and require transparency in financial arrangements. Lack of transparency played a role in almost all of the major financial cases prosecuted by my office. Going back to the early 1990's and our investigation of the Bank of Credit and Commerce International (BCCI), our prosecutions of boiler rooms and pump-and-dump stock schemes since the 1990's, and our recently announced investigations into the movement of funds by Iranian banks and the Iranian

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military; the criminal actors in all of these cases benefited from systems lacking transparency.

My goal in presenting this testimony is to provide the law enforcement perspective on the issue of beneficial ownership registration; to wit, that anonymous shell companies present current and ongoing problems to the law enforcement community, and why Senate Bill 569 (S. 569) is the best solution. My remarks are organized as follows: First, I discuss the current lack of standards among the 50 states. Second, I analyze the alternative measures and discuss why, from the viewpoint of the law enforcement community, they fall well short of the mark. Third, I discuss the standing of the United States in the global financial and anti-money laundering community, and why our current standards lag behind those of many foreign nations, even some generally viewed as problematic by the United States. In this regard, I note the impression of hypocrisy this double standard leaves with the international law enforcement community. Finally, to illustrate the importance of transparency, and to demonstrate the use of the corporate structure for criminal purpose, I will discuss briefly a few cases prosecuted by my staff over the past decade where criminal organizations used corporate structures to engage in criminal conduct. Make no mistake – S. 569 is not a panacea. Criminals will still find ways to hide their identities and use corporate entities for their criminal purposes. But by providing more transparency, and by creating accountability and the possibility of criminal prosecution for incorporating agents, this bill will help us stop corporate criminals.

I was appalled to learn of the current state of the law for incorporation standards. According to a summary prepared by the General Accounting Office in 2006, only two states require any statement of beneficial ownership in their incorporation processes. I believe only seven have such a requirement for LLC's. The reasons behind this, while cynical, make sense. For many states, incorporation fees are a tremendous source of revenue. Any state that raised its standards unilaterally would put itself at a competitive disadvantage as opposed to other states with lower standards. It would be foolish to expect any state to act against its financial self-interest, especially in this economic climate.

I have reviewed some of the alternative proposals under debate today. The proposal from the National Association of Secretaries of State (NASS) would require "owner-of-record" information. This is of little value from a law enforcement perspective. The owner-of-record can be another shell company, another straw owner, an incorporation service – anything. Beneficial ownership – who really owns the corporation - is the important information, and S. 569 quite rightly focuses on this concept.

Moreover, the proposal from the National Conference of Commissioners on Uniform State Laws (NCCUSL) suffers from deficiencies similar to those of the NASS proposal. First, it will not be binding unless adopted by the States. Again, no state will be the first to enact such requirements, and the states that, from the law enforcement perspective, most need reform are least likely to enact. That gives little cause for optimism. The "race to the bottom" will be on, and the worst states will seek a competitive advantage

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over those that seek reform. Even with a federal mandate requiring adoption of the NCCUSL proposal, it would still impose an entirely new regime. S. 569 would be much simpler and more direct: simply collect a statement of beneficial ownership and keep it in the same type of file currently maintained by the states.

In addition, the complicated structure of "Record Contact" and "Responsible Individual" in the NCCUSL proposal will actually make matters worse from a law enforcement perspective, not better, for a number of reasons. First, either system will destroy the ability of law enforcement to gather corporate information without alerting the targets of the investigation. In any long term investigation, we must find ways to gather evidence while maintaining confidentiality. If our suspects learn of the investigation, they may flee, records may be destroyed, criminal techniques may be altered. Thus, we constantly seek ways to gather evidence without alerting the suspects. This is particularly true of the type of sophisticated criminal who takes the time to set up shell companies to hide his or her involvement. Under the Senate bill, information of beneficial ownership would be provided to the State, and law enforcement seeking such information would use a subpoena to obtain it from the State. It is simple, direct, and would take only days. And, most importantly, it would not alert the suspect.

Compare that to the NCCUSL proposal. A request would have to be made to the Record Contact (who could be anywhere in the United States and would have to be located). The Record Contact is someone designated by the corporation to act on its behalf. Contacting this person is akin to picking up the telephone, calling the suspect, and saying, "You're under investigation." I can already hear the shredders starting to whir. The concept of the Responsible Individual suffers from the same shortcoming. An inquiry to the Responsible Individual is akin to a direct notification to the company that it is under investigation. Moreover, from a law enforcement perspective, the Responsible Individual is something of a mystery. The Responsible Individual is defined as someone "who, directly or indirectly, participates in the control or management of an entity." There is no requirement that this person be in the United States. The interpretation of someone who "directly or indirectly controls a corporation" is vague enough to mean anything. Could a nominee, officer or director who is an employee of an incorporation service in Panama be someone "who indirectly controls" a shell company? Of course he could. This is a huge loophole that would defeat the purpose of this legislative reform.

Finally, I note that this bill would render impotent one tool commonly employed by law enforcement. Federal law and the laws of many states allow us to obtain non-disclosure orders for our subpoenas. For example, when we obtain phone records, bank accounts, credit card information or other investigative data, such an order prevents banks and other subpoenaed entities from notifying the account holders. The very structure created by the NCCUSL proposal nullifies such orders, as the system the proposal would create requires the Record Contact to notify the corporation upon receipt of the subpoena. For those seeking to abuse the system and hide their involvement, the twin concepts of the Record Contact and the Responsible Individual will be a bonanza, in that they will create a system that will frustrate law enforcement investigations by its very structure. We would be better off, from a law enforcement perspective, with no legislation at all.

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There is an aspect of this issue not readily apparent to those who do not investigate and prosecute crime for a living. Critics have charged that the law will not work because criminals will continue to use false names to hide their identities. This criticism misses the point. By requiring the inclusion of beneficial ownership information, all people seeking the benefits of corporate status from the states will be expected and required to provide accurate and truthful information. When a criminal uses a false name, or a straw man, or incorporates in the name of a family member – there are two significant results from the law enforcement perspective.

- First, it provides evidence of what the criminal law refers to as "consciousness of guilt." To put it another way – why would someone use false information? Would an innocent person do that? The answer is usually "no," and this type of evidence is tremendously important in establishing a suspect's criminal intent. Simply by requiring information regarding beneficial ownership, criminals would be forced to lie. And a lie goes a long way to establishing criminal intent.

- Second, and equally importantly, it will give law enforcement a criminal charge to bring against criminals who use false information to incorporate, and also against the agents who intentionally assist such criminals. If an incorporation agent sets up 100 shell companies for an identity theft ring that plans to steal and launder money, the incorporation agent may or may not be guilty as an accomplice to identity theft, larceny, and money laundering. But, the agent is certainly guilty of filing false incorporation documents with the state. The ability to punish the enablers and middle men will go far in cleaning up corruption. For example, according to information gathered by the Financial Crimes Enforcement Network, there is one U.S.-based incorporation service that, for the period from April 2005 to March 2006, was named in 86 separate Suspicious Activity Reports for its association with corporations involved in over $100 million in suspicious conduct. During the period from April 2006 to March 2007, this same service provider was named in an additional 218 Suspicious Activity Reports, five of which alone totaled over $100 million in suspicious transactions.

I think it is important to note that we do not support imposing a verification requirement on the States. Often legitimate businesses need to set up corporations quickly, and a verification requirement for all incorporation processes would hamper the normal practices of business and would impose a financial burden on the States. The states are not expected to verify the data or take any extra steps – they simply would have to make sure that the information identifying beneficial ownership is obtained from the party seeking incorporation. The solution seems to be as simple as an extra data field in an online form, and a simple and easily understood requirement for incorporation agents. There would be no extra costs for the states, and because the bill would set a uniform minimal standard for all states, there would be no concern that any state could have a competitive advantage. There could be no "race to the bottom."

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Equally important, we do not necessarily support making information of beneficial ownership publicly available. Under the Senate bill, it would be available only by means of a subpoena from law enforcement and, while not within my area of concern, presumably available pursuant to a civil subpoena issued by a court in civil litigation. Individuals can have legitimate interests in maintaining the privacy of their business affairs, but that interest must be balanced against the need of law enforcement agencies to investigate criminal conduct and the state's interest in protecting the incorporation process from abuse. This bill will strike a reasonable balance at no cost to businesses or the states.

Finally, there are moral reasons – and reasons of national pride -- to support this bill. My Office is well known for its work chasing offshore tax cheats, corrupt politicians, dirty banks, and other international cases. We regularly speak to law enforcement agents and prosecutors around the world. It is difficult to speak with moral authority in criticizing offshore bank secrecy jurisdictions when they can point an accusing finger back at us. The British Virgin Islands is a well-known (in law enforcement circles) bastion for dirty shell companies, but even the British Virgin Islands can level criticism at the lack of transparency in the incorporation processes in our states. That we were deemed "non-compliant" by the Financial Action Task Force is an embarrassment. That we have made no progress in the three years since then is absurd. Our statement of national transparency standards should be something more than: "U.S. financial transparency: Better than Lichtenstein and trying to catch up to Panama." Simply put, we lag behind many other countries in the world in this regard, and it makes our statements concerning transparency and tax evasion ring hollow and hypocritical.

Foreign law enforcement authorities even refer to certain states as "offshore U.S. jurisdictions." And when asked, I am hard-pressed to define why these well-known states are any different from Cayman or the British Virgin Islands. The Committee should also know the imprimatur of respectability that a certificate of incorporation from a U.S. state carries with it, and the access it gives a foreign citizen to open bank accounts and engage in all manner of business, both legitimate and otherwise. And, for many foreign persons wishing to hide their income in an "offshore jurisdiction," there is no need to turn to a Caribbean hide-away. In one case where we rendered assistance to foreign prosecutors, we were able to connect the head of a foreign central bank to an "offshore" Delaware corporation. He used the corporate entity to open a bank account in Florida. He used black market money systems (prosecuted in New York) to move funds to this secret account he held in Florida. By obtaining a corporate entity, this corrupt official could rest assured that his funds would be safe in the United States, and his name would not easily be linked to the corporation. I am hard-pressed to find a difference between his use of a Delaware corporation to open a Florida bank account and the use by a U.S. taxpayer of a Lichtenstein corporation to open a Swiss bank account. At the end of the day, both systems provide a security blanket of anonymity for those who seek it.

Having discussed the issues in the abstract, allow me to present a few cases where we have seen criminals employ shell companies. The historic record is replete with more examples, including the federal investigation and prosecutions of Hezbollah members for

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smuggling cigarettes and the ongoing federal prosecution of associates of the accused Iraqi terrorist Shawqi Omar. Both of these criminal organizations used domestic shell companies to launder criminal proceeds, ultimately to the benefit of terrorist organizations. Here then, are a few more examples of cases in which criminals created anonymous domestic shell companies to further their criminal schemes.

Money Laundering by Iran

The Manhattan District Attorney's Office recently announced a number of cases involving the movement of funds through banks in New York by entities controlled by the Iranian military. In at least two related matters, domestic shell companies in two different states were opened to hide secret Iranian interests. In one of these cases, individuals working on behalf of the government of Iran created a New York shell company to own assets in the United States, and to move funds to secret accounts held in offshore jurisdictions. Our investigation led us to a corporate parent in this offshore "bank secrecy" jurisdiction. Ironically, the foreign government wherein the corporate parent was created was able to give us more information about the ownership of the New York corporation than was the State of New York. A required declaration of beneficial ownership might not have stopped the Iranians, but even a false statement would have been an extra tool for law enforcement to shut down this misconduct and prosecute the perpetrators.

Tax Evasion: Consulting Fees to Shell Companies

A frequently observed fact pattern involves tax evasion through the use of payments of so-called "consulting fees" to shell companies. In these schemes, the owner of a business sets up domestic shell companies and causes the business to send payments to them. These payments are recorded in the books of the business as consulting fees or vendor fees. The shell company maintains a bank account or accounts (because multiple accounts make it more complicated to trace the funds), and the payments sent from the business to the shell company are deposited and then used to pay personal expenses of the business owner. As a tax scam, it is a double hit – the business gets a false deduction (for the bogus consulting fees) and the owner receives income he does not declare. This is the tax scam that led to convictions of the principal owners of the infamous Manhattan strip club called Scores. We have prosecuted this fact pattern dozens, if not hundreds, of times in the past decade.

Mortgage Fraud

My office has a number of ongoing investigations into mortgage fraud. In these cases, which involve upward of $100 million in larcenous conduct, we see the same use of domestic shell companies as described above for tax evasion. The criminals use wildly inflated appraisals and false paperwork to obtain mortgages on properties. They deposit checks from the closings into accounts set up in the names of the shell companies. They can then withdraw the ill-gotten funds as they see fit, or use them to pay personal expenses. The lender issuing the mortgage is out of luck.

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Creation of Multiple Entities for Tax Evasion and Larceny

Another common fact pattern occurs when an individual creates a shell company with a name similar to some other corporation. For example, in a case indicted early last year, eight people were charged in a fraud scheme involving stolen checks. The ring leader hired an accomplice who worked in the mail room of a major corporation. The mail room clerk stole numerous checks issued by the corporation to various vendors. The checks ranged in value from about $10,000 to $75,000. Once he had the checks, the ring leader would create domestic shell companies or obtain business certificates in a name close to the payee on the check. For example, a check made out to "Con Edison" would prompt the ring leader to obtain corporate papers in a name like "Consulated Edison." The ringleader would then hire straw men to open business bank accounts in their own names, "doing business as" the bogus corporation. The ringleader and accomplices would deposit the stolen checks and withdraw or transfer the funds. The indictment covered about $350,000 in fraud of this nature, but the ringleader was involved in an array of frauds. This is a common scheme employed by organized identity theft rings.

Sales Tax Evasion and Use of the Corporate Entity to Hide Control

Another current investigation from my office involves a business that provides security protection services for residential facilities (such as senior citizen centers and health care clinics), in the form of armed and unarmed guards. Under current New York law, the NYS Department of State is the agency licensing such a company, and it is also the agency that oversees and maintains records of incorporation of corporate entities.

The business has had at least three New York corporate identities in the past few years. It seems that the business regularly and repeatedly fails to file payroll taxes, its owners seem regularly to under-estimate their income tax liability, and the companies have other irregularities that, in our estimation, raise questions about whether it should be hiring and deploying armed guards. However, every time the tax department files a tax lien against this company, the business owners simply dissolve that corporate iteration and re-form under a different corporate name. No agency within the State of New York requires a statement of ownership for the corporate entity, although the ownership appears to be consistent and the repeated re-incorporation seems to be a simple dodge to avoid tax liability.

Bribery / Political Corruption

In a case prosecuted by the Department of Justice that resulted in a guilty plea last month, two Florida residents admitted using a Florida shell company to pay bribes to corrupt government officials in Haiti. The defendants, Juan Diaz and Antonio Perez, admitted that they created a shell company in Florida and used it to open a corporate bank account. They then laundered over one million dollars through the shell company account to pay off the Haitian officials to obtain telecommunications contracts. These payments were recorded on the books of the Florida telecomm companies where the defendants worked as "consulting services."

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We also receive regular requests from foreign law enforcement seeking to trace money moved through accounts held by U.S. corporate entities. A case indicted in Brazil involved criminal proceeds sent to an account at a U.S. bank. Again, a U.S. shell corporation was created and used to open the account. In this case, the defendants discussed using a British Virgin Island company as the nominee director of the corporation. Consider the following communication from the U.S. incorporating agent to the Brazilian defendant:

> *The recommendation is to open a US Limited Liability Company (LLC). This entity combine the advantages of a limited with the ones of a partnership, especially about the taxes (we will open "a pass-through entity)."*
>
> *The instruction is to not mention in the public files the owners' names.*
>
> *It is possible to point a Registered Agent to receive the official letters.*
>
> *The LLC might be managed directly by its owners, but it must be done preferentially by operating managers (equivalent to directors) and that will have duties and responsibilities similar to the corporation's directors.*
>
> *The Managers don't need to be American citizens or to live in United States and their data may, but not necessarily, be disclosure to the public records.*
>
> *The total cost for the opening procedures is US$ 6,000 including a Nominee Member. Per year the managing will cost US$ 1,600.*

This communication, and the examples set forth above, demonstrate how the systems of anonymity in this country's incorporation processes are being exploited by criminals. They also demonstrate why we need to be able to retrieve beneficial ownership information from the states directly, and not from the sham nominee of a domestic shell company.

Ultimately the Levin-Grassley-McCaskill bill strikes a reasonable balance between the call for transparency and accountability from the law enforcement community and the need to encourage responsible business growth and development. The investigations referenced in this testimony, as well as the practices outlined in the GAO Report and in Senator Levin's investigation, paint a clear picture as to why change is necessary. The cases mentioned in this testimony barely scratch the surface of the problem. S. 569 provides a minimalist and direct answer to a difficult problem. It places almost no burdens on the states or on business, while simultaneously addressing our security needs. I urge the Committee to adopt it and recommend its passage.

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Written Testimony of Harry J. Haynsworth
Chair, Drafting Committee on the Uniform Law
Enforcement Access to Entity Information Act
of the Uniform Law Commission

To the
United States Senate Committee on
Homeland Security and Governmental Affairs

On the Incorporation Transparency and
Law Enforcement Assistance Act (S.569)

June 18, 2009

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Thank you for the opportunity to submit written testimony on behalf of the of Uniform Law Commission (ULC, also known as the National Conference of Commissioners on Uniform State Laws). I am the Chair of the ULC's Drafting Committee on Uniform Law Enforcement Access to Entity Information Act (the "Uniform Act").

I have been a ULC commissioner since 1992. My appointment must be approved by the Governor, the Attorney General and the Chief Justice of the Minnesota Supreme Court. I receive no remuneration for my work as a commissioner other than reimbursement of travel and meeting expenses. I have been a practicing lawyer and law school professor for almost 45 years. I have been the dean of three law schools (University of South Carolina, Southern Illinois University School of Law and William Mitchell College of Law in St. Paul, Minnesota). For the past several years I have been Of Counsel to Briggs and Morgan in Minneapolis, Minnesota. Throughout my career as a practitioner and an academic, my primary focus has been in the area of business law. Since becoming a commissioner, I have been a member of several uniform act business law entity acts in addition to the Uniform Law Enforcement Access to Entity Information Act, including the Uniform Partnership Act (1994), the Uniform Limited Partnership Act (2001), the Uniform Limited Liability Company Act (1996, 2006), and the Uniform Unincorporated Nonprofit Associations Act (2008). I have been the chair of several of these drafting committees and have been actively involved in getting these acts adopted by the states.

The Uniform Act deals with the same subject matter as the Incorporation Transparency and Law Enforcement Assistance Act (S.569) but differs in many respects from S.569. The following is a brief outline of my testimony:

- Basic information about the ULC;
- Background information on the development of the Uniform Act;
- An overview of the Uniform Act and the major differences between the Uniform Act and S. 569; and
- A recommendation on how to get a statute that meets the objectives of S.569 enacted on a uniform basis in all the states in the shortest possible time.

Uniform Law Commission

The ULC is a state governmental entity operated as a non-profit unincorporated association, comprised of state commissions on uniform laws from each state, the District of Columbia, the Commonwealth of Puerto Rico, and the U.S. Virgin Islands. Each jurisdiction determines the method of appointment and the number of commissioners actually appointed. All commissioners must be lawyers, qualified to practice law. While some serve as state legislators, or employees of state government, most are private practitioners, judges, or law professors. Commissioners donate their time and expertise as a pro bono service and receive no salary or fee for their work with the ULC.

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Now in its 117th year, the ULC works to harmonize state laws in critical areas where consistency is desirable and practical and supports the federal system by addressing issues of national significance best resolved at the state level. The ULC has drafted more than 250 uniform acts in various fields of law setting patterns for uniformity across the nation, in such areas as business entity law, interstate child support and custody, investment allocation rules, and trust and estates law. The ULC's work prevents states from having to perform duplicative and costly research in addressing shared legislative issues. Uniform Acts are voluntarily adopted by state legislatures and localized to respond to each state's statutory framework and concerns.

Draft acts are then submitted for initial debate of the entire ULC at an annual meeting. Each act must be considered section by section, at no less than two annual meetings by all commissioners sitting as a Committee of the Whole. Following extensive debate and promulgation in a vote by states, commissioners in each state and territory submit ULC acts for legislative consideration.

The ULC is not an interest group; drafting meetings are open to the public and all drafts are available on the internet at the ULC's website: www.nccusl.org. Because ULC drafting projects are national in scope, we are able to attract a broad range of advisors and observers to participate in our projects, resulting in a drafting process that has the benefit of a greater range and depth of expertise than could be brought to bear upon any individual state's legislative effort.

Background of the Uniform Act

In July 2007, the National Association of Secretaries of State (NASS) requested that the ULC and the American Bar Association draft legislation that would amend state legal entity statutes to address concerns about law enforcement access to entity ownership information raised by two major federal governmental reports, the 2006 GAO Report on Company Formations and the multi-agency report entitled "Money Laundering Threat Assessment," which led to an oversight hearing in November 2006 before the Senate Permanent Subcommittee on Investigations. At that hearing the compliance report of the Financial Action Task Force (FATF), an international organization which is engaged in a worldwide effort to combat money laundering and to stop the financing of terrorist activities, was considered. The report stated that the United States, which is a member of FATF, was not in compliance with FATF Recommendation 33 regarding information on the beneficial ownership and control of legal entities and the prohibition of bearer shares.

The NASS Company Formation Task Force Recommendations Report pointed out that what type of ownership information is kept by entities and what information about entities is filed in the offices of Secretaries of State has always been a matter of state statutes, and the ULC has promulgated all the major unincorporated entity acts (Uniform Partnership Act, Uniform Limited Partnership Act, Uniform Limited Liability Company Act, Uniform Limited Cooperative Association Act, Uniform Unincorporated Nonprofit Associations Act, and Uniform Statutory Trust Entity Act) and the American Bar Association has promulgated the two major corporate entity acts (the Model Business Corporation Act and the Model Nonprofit Corporation Act).

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ULC and the ABA Business Law Section Committee on Corporate Laws (CCL) agreed to undertake the drafting projects requested by NASS. They each established drafting committees in 2007. The original charge of the committees was to draft a uniform set of amendments to all of the unincorporated and corporate entity acts. Last fall the ULC and the CCL decided that rather than requiring the states to make amendments to every one of their entity laws, it would be preferable to prepare a single statute that could be enacted by the states to address the issues raised by the various reports referred to above and the Incorporation Transparency and Law Enforcement Assistance Act, originally introduced in May 2008 as S.2956 and reintroduced in May 2009 as S.596.

The drafting process has been open, inclusive and intense. Beginning in the fall of 2007, the Uniform Act drafting committee has held four in-person meetings and four conference call meetings. Drafts of the Act were reviewed at each meeting. There were 12 commissioners on the drafting committee from across the country (Maine, Pennsylvania, Delaware, Kentucky, Arkansas, Alabama, Minnesota, Texas, Illinois and Oregon). In addition there were 22 advisors and observers from a very broad range of organizations that have expressed an interest in and would be impacted by this legislation, including three Secretaries of State, several entity filing officials from various states, representatives from the National Conference of State Legislatures, the American College of Trusts and Estates Counsel (ACTEC), the American College of Real Estate Lawyers (ACREL), the American Bankers Association, CT Corporation (a leading provider of registered agents and other services for corporations and other types of entities), and the American Bar Association and several of its sections and committees (Business Law Section Committee on Corporate Laws, Limited Liability Companies, Partnerships and Other Unincorporated Entities Committee; and the Real Property, Probate and Trust Section).

Three U.S. Treasury Department officials also have been observers. They forcefully presented Treasury's concerns about beneficial ownership issues and related matters raised by the Office of Terrorist Financing and Financial Crimes and other units within Treasury. No lawyers from the Department of Justice were advisors or observers, but members of the drafting committee met with various officials in the Department of Justice both before the drafting project was undertaken and during the course of our deliberations, and various drafts of the Uniform Act were sent to the Department of Justice. Drafts of the Uniform Act have also been reviewed by the stakeholder organizations, including bar association committees, NASS and IACA (International Association of Commercial Administrators), and the feedback from these draft reviews has been very helpful in the refinement of the Act.

The Uniform Act had a first reading at the ULC Annual Meeting last summer. It is scheduled for a second and final reading at the upcoming ULC Annual Meeting in July. Approval is anticipated. The Committee on Corporate Laws of the Section of Business Law of the American Bar Association formally approved the Annual Meeting Draft of the Uniform Act on June 13, 2009.

Guiding Principles

The following important principles have guided the drafting committee's work:

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- The state entity laws need to be amended to provide law enforcement officials with better access to adequate, accurate and timely ownership, and control information about legal entities.
- The necessity of having a statutory prohibition against the issuance of bearer shares by entities.
- Unmanageable workloads for the Secretaries of State must not be created.
- Unnecessary and unworkable compliance burdens must not be imposed on legitimate businesses.
- Legitimate privacy rights must be protected.
- Foreign investment in the United States must not be discouraged.
- A uniform act enacted by all states covering all entities that file organic documents in the office of the Secretary of State is necessary because: (1) what entity documents are filed in the offices of the Secretaries of State are and always have been incorporated into state entity statutes throughout the United States; and (2) a substantially similar set of standards adopted by all states is the only way to achieve the law enforcement access goal.

The Uniform Act

The following is a brief overview of the Uniform Act. A more detailed summary of the Act and a copy of the Annual Meeting Draft of the Act are attached to my written testimony.

The Uniform Act deals with two principal issues. The first is a provision that prohibits all filing entities from issuing certificates of bearer shares. In some countries, it is possible to issue bearer shares, but to the best of my knowledge, no United States entity has ever issued bearer shares. Nevertheless, since FATF Recommendation 33 requires a country to prohibit bearer shares, including a specific prohibition in the Act was considered to be prudent.

The second principal issue is the access by law enforcement officials to ownership and control information about filing entities. Most of the Act deals with the various aspects of this issue: (1) who is entitled to get ownership and control information and how do they get it; (2) what types of entities are covered by the Act and what kinds of information are these entities required to provide law enforcement officials; and (3) what information relating to ownership and control is required to be filed in the office of the Secretary of State.

Subject to certain exceptions, the Act applies to all filing entities having 50 or fewer interest holders. These entities are called a "conventional privately held entity" (CPE). In most states this would include limited liability partnerships, limited partnerships, limited liability companies, statutory entity trusts (business trusts), co-operatives and for profit and nonprofit corporations. Some states have other types of filing entities, *e.g.*, professional associations, which would also

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be covered by the Act if they have 50 or more interest holders. In terms of numbers of entities, the Uniform Act covers approximately 95% or more of all the approximately 18,000,000+ filing entities in the United States. Thus the Uniform Act has much broader coverage than S.569, which only covers corporations and limited liability companies. In addition, S.569 only covers corporations and limited liability companies formed after it has been enacted. In 2007, the latest year for which I could find reasonably complete statistics, there were approximately 2,000,000 corporations and limited liability companies formed in the United States. The Uniform Act, on the other hand, covers existing filing entities as well as newly formed filing entities. Existing entities have two years after a state enacts the Uniform Act to comply with its requirements. The principal reason for this broader coverage is that if some entities are covered and others are not, the individuals law enforcement most interested in pursuing will simply form (or acquire) a non-covered entity.

The entities exempted from the coverage of the Uniform Act are highly regulated companies like banks, and law enforcement officials already have the ability to obtain ownership and control information about them; filing entities that have a large enough number of owners that it is unlikely they would be controlled by individuals who are of interest to law enforcement officials, and entities that are tax exempt and file ownership and control information that is available to the public (*e.g.*, Form 990).

The Act requires that all CPEs file in the office of the Secretary of State an initial information statement (existing CPEs must file the initial information statement by the two-year deadline mentioned above) at the time the initial public organic document (*e.g.*, articles of incorporation) is filed. The entity information statement contains the name and business or residential address of the CPE's "record contact" (RC) and "responsible individual" (RI). The RC must be an individual whose principal residence is in the United States. The RI must also be an individual and must be someone who directly or indirectly participates in the control or management of the CPE. Any changes in the RC and RI must be promptly filed in the office of the Secretary of State. A CPE can be administratively dissolved if it fails to keep the information about the RC and RI current. A federal law enforcement authority, federal agency, or committee or subcommittee of the U.S. Congress (states have the option to expand the list to include state and local law enforcement authorities, state agencies and state legislatures) can obtain the name and contact information of the RI and RC from the Secretary of State and then proceed pursuant to a subpoena to contact the RI and RC.

Since the RI must be someone who is knowledgeable about the activities of the entity, the ability of law enforcement officials to directly contact the RI gives law enforcement officials a valuable investigative resource. The fact that the RI would be subject to perjury and other sanctions should be a sufficient deterrent for anyone who does not really know anything about the operations of the entity to sign a document filed in the Office of the Secretary of State stating he or she is the RI for the entity.

Upon receipt of an appropriate request for information from law enforcement officials, the RC is required to obtain from the CPE on a timely basis pursuant to the subpoena ownership and control information about the CPE. The records that the CPE must provide the RC, who in turn gives the information to the appropriate law enforcement officials, are:

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1. a list of the name and last known address of each interest holder and transferee and, if the interest holder or transferee is an entity, the name of the state or country where it was formed;

2. the name and address of each governor (*e.g.*, director), including a government issued photo identification document of a governor whose principal residence is outside the United States;

3. a government issued photo identification document for its RI if the RI's principal residence is outside the United States;

4. the name and contact information of the RI of a non-U.S. entity that is an interest holder or transferee of a CPE;

5. any records the CPE maintains regarding the process by which its governors are elected or otherwise designated;

6. the voting power of each interest holder or a description of the manner in which each interest holder's voting power in the entity is determined;

7. the names of the individuals responsible for preparing the information; and

8. a certificate that the information accurately reflects the current records of the CPE.

In addition to the number and types of entities covered, the Uniform Act differs from S.569 with respect to the required ownership and control information in several respects. A topical chart comparing the two acts is attached to my written testimony. The two most significant differences between the Uniform Act and S.569 concern: (1) what entity information is filed in the office of the Secretary of State; and (2) beneficial ownership information.

S.569 requires that entity beneficial ownership information be filed in the office of the Secretary of State at the time the entity is formed and that the information be updated annually in states which do not require annual reports, a CPE would be required to file any changes in beneficial ownership at the time the change occurs.

The Uniform Act only requires the names and contact information of the RC and RI to be filed in the office of the Secretary of State. There are three principal reasons why the drafting committee chose this path. The first is that the Secretaries of State do not currently keep any substantial ownership and control information and what information they do require to be filed is public record information. Setting up a filing system to accommodate and maintain detailed ownership and control information would be very expensive. The second reason is that maintaining this information as confidential documents would immensely complicate the filing process, and in some states could not be accomplished without amending the state's constitution. The third reason is that since updates are only required annually in states that require annual reports, the information on file would not reflect any changes in ownership and control occurring between the filing of the initial information statement and the filing of the first annual report or between

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annual reports. Moreover, requiring CPEs to file an updated list of changes on a real-time basis would be an administrative nightmare both for the CPEs and the Secretaries of State.

After careful study and consideration, the ULEAEIA Drafting Committee determined that requiring entities to collect and maintain beneficial ownership records that would comply with the definition in S.569 (and its predecessor S.2956) would be an enormous burden, a radical departure from existing entity record keeping requirements, and because of the complexities involved in determining beneficial ownership, would create a records system with massive amounts of noncompliance, most of which would be unintentional.

S.569 defines a beneficial owner as:

> an individual who has a level of control over, or entitlement to, the funds or assets of a corporation or limited liability company that, as a practical matter, enables the individual, directly or indirectly, to control, manage or direct the corporation or limited liability company.

This definition is far too general and vague to be a concrete guide for determining exactly what kind of information must be kept by entities. The key operative terms "control" and "directly and indirectly" would have to be defined. All the other statutes and regulations that use the term "control" as the critical factor have a threshold percentage of ownership interest that determines if control exists, *e.g.,* more than 50% of the stock of a corporation. What is meant by "direct and indirect" ownership would have to be spelled out in the statute. The difficulty and complexity is in determining "indirect" ownership. Other existing statutes and regulations generally contain two categories of indirect or constructive ownership. The first is family members and the second is constructive ownership based on ownership interests in trusts, estate, and various forms of business entities.

I have attached to my written testimony a Memorandum I prepared for the Uniform Act Drafting Committee which describes some of the major issues that would have to be dealt with in drafting a statute containing indirect or constructive ownership rules. The statutes would of necessity be very complex. Two examples, one from the UK and one from the Internal Revenue Code Tax Regulations are included as exhibits to the Memorandum.

In order to determine if there were any beneficial owners who were in control of an entity, the entity would have to know all the members of the family, as defined in the statute, of each of its individual record owners, and the names of all the shareholders, partners and members of any entity that is an equity owner of the entity. If one or more of the equity owners is an entity of some kind, the entity would also need to know the owners of that entity, and so on down the chain, as well as the names of the beneficiaries of any trust and estates that hold an ownership interest in the entity. An additional complexity would be the necessity of keeping track of any changes in the various ownership interests, for example, a change in the beneficiaries of a trust that owns stock in a corporation A or one of the shareholders of corporation B that owns stock in corporation A sells his corporation A stock to C. Unless the trustee of the trust or corporation B notifies corporation A of the change, corporation A would not have any way of knowing about these changes.

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The Uniform Act gives law enforcement officials access, through the RC, to current, accurate information on the record ownership, voting rights and managers of an entity which is the overall objective of S.569 without the complexities of the beneficial ownership concept. In some cases after receiving the required information from the RC, additional investigation into identification of family members of interest holders, beneficiaries of trust and estates that are interest holders and the owners of entities that are interest holders in the entity being investigated will have to be conducted, but the ownership, management and control information received from the RC will provide law enforcement officials with the necessary basic information to trace this ownership trail.

The Uniform Act accomplishes the purposes set forth in S.569 in a more comprehensive, more cost effective and less complex manner than that Act. Since the states will have to enact legislation to implement S.569, it makes sense to amend S.569 to provide that states must adopt the Uniform Act.

We believe that federal legislation incorporating the Uniform Act should have at least the following elements:

- It would require that states adopt legislation substantially similar to the Uniform Act by a date certain that is long enough in the future to permit all state legislatures a reasonable opportunity to consider and act upon the Uniform Act.

- Provide a reliable source of federal funding to assist states in funding the one-time costs of revising their procedures and systems to obtain and manage the information required by the Uniform Act; and

- In addition to the funding "carrot," the federal legislation would provide some form of penalty or other consequence if a state has not adopted legislation substantially similar to the Uniform Act by some future date certain.

The broad discussions that we have had around the country concerning S.569 and the Uniform Act have led us to conclude that, while there is broad support for the Uniform Act as a far preferable vehicle than S.569 for providing law enforcement additional effective tools to combat money-laundering and the financing of terrorism, there also is little likelihood that the Uniform Act would achieve anything near widespread adoption unless there were both a federal "carrot" and a federal "stick" to encourage action by the states.

The ULC has had valuable experience in drafting uniform state legislation that is incorporated in federal legislation that provides a mandate that states enact the uniform legislation by some date certain.

- At the request of the State Department and the Department of Human Services, during 2007-08 ULC drafted amendments to the Uniform Interstate Family Support Act (UIFSA) in order to implement provisions of the Hague Family Maintenance Convention, which the United States had recently signed. Those UIFSA revisions were adopted by the ULC in July 2008 and proposed federal legislation requires states to adopt UIFSA by

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a future date or risk loss of child support funding. Action on the proposed legislation and Senate Advice and Consent to the Treaty are pending.

- In 1999 the ULC drafted the Uniform Electronic Transactions Act (UETA), and in 2000 Congress enacted the Electronic Signatures in Global and National Commerce Act ("E-Sign"), which provided pre-emptive federal legislation covering essentially the same topics as UETA and provided that the federal legislation would control unless a state adopted state legislation substantially similar to UETA. To date 46 states have adopted UETA.

Conclusion

The ULC welcomes the opportunity to work with the Chair and other members of the Committee to craft workable legislation that will provide law enforcement officials with improved and timely access to accurate ownership and control information about legal entities.

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FOR DISCUSSION ONLY

UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT

NATIONAL CONFERENCE OF COMMISSIONERS

ON UNIFORM STATE LAWS

Annual Meeting Draft

With Prefatory Note and Comments

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By
NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

The ideas and conclusions set forth in this draft, including the proposed statutory language and prefatory note, legislative notes, and comments, have not been passed upon by the National Conference of Commissioners on Uniform State Laws. They do not necessarily reflect the views of the Conference and its Commissioners and the Drafting Committee and its Members and Reporter. Proposed statutory language may not be used to ascertain the intent or meaning of any promulgated final statutory proposal.

June 2, 2009

PHTRANS/ 798855.4

DRAFTING COMMITTEE ON UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT

The Committee appointed by and representing the National Conference of Commissioners on Uniform State Laws in preparing this Act consists of the following individuals:

HARRY J. HAYNSWORTH, IV, 2200 IDS Center, 80 S. 8th St., Minneapolis, MN 55402, *Chair*

BRUCE A. COGGESHALL, One Monument Sq., Portland, ME 04101

ANN E. CONAWAY, Widener University School of Law, 4601 Concord Pike, Wilmington, DE 19803

DAVID C. MCBRIDE, 1000 West St., P.O. Box 391, Wilmington, DE 19899

DAVID G. NIXON, 2340 Green Acres Rd., Suite 12, Fayetteville, AR 72703

STEVE WILBORN, 306 Tower Dr., Shelbyville, KY 40065

NORA WINKELMAN, Legal Counsel's Office, Room 620 Main Capitol, Harrisburg, PA 17120

WILLIAM H. CLARK, JR., One Logan Square, 18th and Cherry Streets, Philadelphia, PA 19103-6996, *Reporter*

EX OFFICIO

MARTHA LEE WALTERS, Oregon Supreme Court, 1163 State St., Salem, OR 97301-2563, *President*

WILLIAM H. HENNING, University of Alabama, Box 870382, Tuscaloosa, AL 35487-0382, *Division Chair*

AMERICAN BAR ASSOCIATION ADVISOR

ALLAN G. DONN, One Commercial Place, Suite 1800, Norfolk, VA 23510, *ABA Advisor*

ERIC FELDMAN, 1313 N. Market St., P.O. Box 951, Wilmington, DE 19899-0951, *ABA Section Advisor*

ROBERT R. KEATINGE, 555 17th St., Suite 3200, Denver, CO 80202-3979, *ABA Section Advisor*

EXECUTIVE DIRECTOR

JOHN A. SEBERT, 111 N. Wabash Ave., Suite 1010, Chicago, IL 60602, *Executive Director*

Copies of this Act may be obtained from:

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS
111 N. Wabash Ave., Suite 1010
Chicago, Illinois 60602
312/450-6600
www.nccusl.org

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UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT

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UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT

Prefatory Note

This act is part of an international effort to fight money laundering and stop the financing of terrorist activities. Among other things, the act implements Recommendation 33 of the Financial Action Task Force (FATF).

The website of FATF describes the history of FATF as follows:

> "In response to mounting concern over money laundering, the Financial Action Task Force on Money Laundering (FATF) was established by the G-7 Summit that was held in Paris in 1989. Recognizing the threat posed to the banking system and to financial institutions, the G-7 Heads of State or Government and President of the European Commission convened the Task Force from the G-7 member States, the European Commission and eight other countries.
>
> "The Task Force was given the responsibility of examining money laundering techniques and trends, reviewing the action which had already been taken at a national or international level, and setting out the measures that still needed to be taken to combat money laundering. In April 1990, less than one year after its creation, the FATF issued a report containing a set of Forty Recommendations, which provide a comprehensive plan of action needed to fight against money laundering."

Recommendation 33 of the Forty Recommendations provides that:

> "Countries should take measures to prevent the unlawful use of legal persons by money launderers. Countries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities. In particular, countries that have legal persons that are able to issue bearer shares should take appropriate measures to ensure that they are not misused for money laundering and be able to demonstrate the adequacy of those measures."

A Congressional hearing relating to the issues raised by FATF Recommendation 33 was held on November 14, 2006 by the Permanent Subcommittee on Investigations of the Committee on Homeland Security and Governmental Affairs of the United States Senate. The testimony at that hearing led to the introduction of legislation in both the 110th Congress (S. 681, S. 2956, and H.R. 2136) and the 111th Congress (S. 569).

On June 11, 2007, the National Association of Secretaries of State (NASS) requested that the Conference draft amendments to the various uniform unincorporated entity laws to address the issues raised by FATF Recommendation 33. NASS similarly requested that the Committee

on Corporate Laws (CCL) of the Section on Business Law of the American Bar Association prepare similar amendments to the Model Business Corporation Act. Underlying the NASS requests was a desire to address the issues in a way that would be less burdensome for the private sector and Secretaries of State than the proposals in the federal legislation but still meet the needs of law enforcement and satisfy FATF Recommendation 33.

Both the Conference and the CCL agreed to undertake the drafting efforts requested by NASS. Proposed amendments to the Uniform Limited Liability Company Act were given first reading at the 2008 annual meeting of the Conference, and the CCL prepared a first draft of amendments to the Model Business Corporation Act. The Conference and the CCL then decided that, rather than requiring the states to make amendments to each of their entity laws, it would be preferable to prepare a single statute that could be enacted by a state to address the issues raised by FATF Recommendation 33. The unified approach taken in this act was considered desirable particularly because each state has a unique pattern of entity laws and no state has adopted the Model Business Corporation Act and all of the current uniform unincorporated entity laws. This act provides a single statute that can be enacted to address the issues raised by FATF Recommendation 33.

UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT

SECTION 1. SHORT TITLE. This [act] may be cited as the Uniform Law Enforcement Access to Entity Information Act.

SECTION 2. DEFINITIONS. In this [act]:

(1) "Appropriate request" means:

(A) a civil, criminal, or administrative subpoena or summons from a [state, local, or] federal law enforcement authority, [state agency,] federal agency, or committee or subcommittee of the United States Congress [or a state legislature]; or

(B) a request in the form of a record made by a federal agency on behalf of another country under:

(i) an international treaty, agreement, or convention; or

(ii) 28 U.S.C. Section 1782.

(2) "Conventional privately held entity":

(A) means a domestic filing entity that has, or will have on the effective date of its initial public organic record, no more than 50 interest holders; and

(B) does not include a domestic filing entity:

(i) in which one or more domestic or foreign entities with more than 50 interest holders each holds, directly or indirectly, more than 25 percent of the outstanding interests;

(ii) that is licensed or otherwise authorized to conduct business, or has filed an application which has not been denied with the appropriate federal or state agency for a license or other authorization to conduct business, as a bank or other depository institution, trust

company, insurance company, public utility, or securities or commodities broker or dealer;

(iii) that is registered, or has filed an application for registration which has not been denied, as an investment company under the Investment Company Act of 1940;

(iv) that is registered, or has filed an application for registration which has not been denied, as an investment advisor under the Investment Advisors Act of 1940 or the law of any state;

(v) in which one or more domestic or foreign entities of the types described in subparagraph (ii), (iii), or (iv) holds, directly or indirectly, a majority of the outstanding interests;

(vi) that holds, directly or indirectly, a majority of the outstanding interests in a domestic or foreign entity of a type described in subparagraph (ii), (iii), or (iv);

(vii) that has filed with the Internal Revenue Service a current annual information return as an exempt organization or private foundation; or

(viii) that has filed with the Internal Revenue Service an application for recognition of exemption from federal income tax, if that exemption has not been denied and the due date (including any extension granted) for filing its first annual information return as an exempt organization or private foundation has not yet passed.

(3) "Domestic", with respect to an entity, means an entity whose internal affairs are governed by the law of this state.

(4) "Domestic filing entity" means:

(A) a domestic business corporation;

(B) a domestic nonprofit corporation;

(C) a domestic limited liability partnership that is not also a limited partnership;

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(D) a domestic limited partnership, including a limited liability limited partnership;

(E) a domestic limited liability company;

(F) a domestic limited cooperative association; [or]

(G) a domestic statutory trust entity[; or]

[(H) list other types of entities authorized by the law of the state].

(5) "Entity information statement" means the initial or amended statement described in Section 4(a) or (c).

(6) "Foreign", with respect to an entity, means an entity whose internal affairs are governed by the law of a jurisdiction other than this state.

(7) "Governance interest" means the right under the organic law or organic rules of an unincorporated entity, other than as a governor, agent, assignee, or proxy, to:

(A) receive or demand access to:

(i) information concerning the entity; or

(ii) the books and records of the entity;

(B) vote for the election of the governors of the entity; or

(C) vote on issues involving the internal affairs of the entity.

(8) "Governor" means:

(A) a director of a business corporation [or a shareholder of a close corporation that is managed by its shareholders instead of a board of directors];

(B) a director [or member of a designated body] of a nonprofit corporation;

(C) a general partner of a limited liability partnership that is not also a limited partnership;

(D) a general partner of a limited partnership;

(E) a manager of a limited liability company or other person that materially participates in the management of a limited liability company pursuant to its organic law and organic rules;

(F) a director of a limited cooperative association; [or]

(G) a trustee of a statutory trust entity[; or]

[(H) list governors of other types of entities authorized by the law of the state].

(9) "Interest" means:

(A) a governance interest;

(B) a transferable interest;

(C) a share of a business corporation; or

(D) a membership in a nonprofit corporation.

(10) "Interest holder" of an entity means:

(A) a shareholder of a business corporation;

(B) a member of a nonprofit corporation;

(C) a general partner of a limited liability partnership that is not also a limited partnership;

(D) a general partner of a limited partnership;

(E) a limited partner of a limited partnership;

(F) a member of a limited liability company;

(G) a member of a limited cooperative association; [or]

(H) a beneficiary of a statutory trust entity[; or]

[(I) list similar persons in other types of entities authorized by the law of the

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state].

(11) "Non-US entity" means an entity whose internal affairs are governed by the laws of a jurisdiction other than a state or the United States.

(12) "Organic law" means the statutes of an entity's jurisdiction of incorporation, organization, or other formation which govern the internal affairs of the entity.

(13) "Organic rules" means the public organic record and private organic rules of an entity.

(14) "Person" means an individual, corporation, estate, trust, partnership, limited liability company, business or similar trust, cooperative, association, joint venture, public corporation, government or governmental subdivision, agency, or instrumentality, or any other legal or commercial entity.

(15) "Private organic rules" means:

(A) the bylaws of a business corporation;

(B) the bylaws of a nonprofit corporation;

(C) the partnership agreement of a limited liability partnership that is not a limited partnership;

(D) the partnership agreement of a limited partnership;

(E) the operating agreement of a limited liability company;

(F) the bylaws of a limited cooperative association;

(G) the trust instrument of a statutory trust entity; [and]

(H) [list similar documents for other types of entities authorized by the law of the state; and

(I)] any other rules, whether or not in a record, that govern the internal affairs of

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a domestic filing entity, are binding on all of its interest holders, and are not part of its public organic record, if any.

(16) "Public organic record" means:

(A) the articles of incorporation of a business corporation;

(B) the articles of incorporation of a nonprofit corporation;

(C) the statement of qualification of a limited liability partnership that is not a limited partnership;

(D) the certificate of limited partnership of a limited partnership;

(E) the certificate of organization of a limited liability company;

(F) the articles of organization of a limited cooperative association; [and]

(G) the certificate of trust of a statutory trust entity[; and]

[(H) list similar documents for other types of entities authorized by the law of the state].

(17) "Record", used as a noun, means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

(18) "Records contact" means an individual whose principal residence is in the United States and who has access to and can produce within the United States on a timely basis upon appropriate request the information described in Section 7(a).

(19) "Responsible individual" means an individual who, directly or indirectly, participates in the control or management of an entity or, in the case of an entity being formed, will participate in the control or management of the entity.

(20) "Sign" means, with present intent to authenticate or adopt a record:

(A) to execute or adopt a tangible symbol; or

(B) to attach to or logically associate with the record an electronic sound, symbol, or process.

(21) "Transferable interest" means the right under the organic law of an unincorporated entity to receive distributions from the entity.

(22) "Transferee" means a person to which all or part of a transferable interest has been transferred without a governance interest, whether or not the transferee is an interest holder.

(23) "Unincorporated entity" means an entity that is not a corporation.

Legislative Notes:

(1) "Appropriate request": An enacting state must decide whether to include the optional provisions in this definition which have the effect of extending to local or state authorities the right of access to information provided in this act.

(2) "Conventional privately held entity": Subparagraph (B) should be revised to omit any of the types of entities listed that are formed under a law that applies only to that type of entity, for example a banking corporation act or insurance company act. Those entities should also not be included in the definition of "domestic filing entity" because this act does not need to include those entities for any purpose.

(4) "Domestic filing entity": The entities referred to in this definition are illustrative only. The list as enacted by a state should include all the types of non-governmental entities that may be created under the state's laws where a filing must be made with the Secretary of State to create or confirm the status or existence of the entity. An enacting state should revise this definition so that (i) the entities are referred to in the manner they are referred to in the state's other laws and (ii) it includes all of the types of entities that fit within the concept and are recognized by the laws of the state.

It is not necessary to list in this definition entities that are a subset of a type of entity listed if reference to the more generic type of entity includes entities in that subset. For example, if professional corporations are subject to the state's business corporation law so that referring to business corporations includes professional corporations, this definition does not need to list professional corporations; but if professional corporations are incorporated under a separate statute and a reference to business corporations would not include professional corporations, then professional corporations should be listed separately.

If a type of entity described in subparagraph (B)(ii) of the definition of "conventional privately held entity" is formed under a law that applies only to that type of entity, for example a banking corporation act or insurance company act, that type of entity may be omitted from this definition because "domestic filing entity" does not need to include that type of entity for any

purpose under this act.

(8) "Governor": An enacting state should revise this definition so that it refers to the appropriate persons with respect to each type of entity listed in the definition of "domestic filing entity."

If an enacting state authorizes a business corporation with a limited number of shareholders to dispense with a board of directors in favor of management by its shareholders, the optional phrase at the end of subparagraph (A) should be included with appropriate changes to conform to the terminology used in the enacting state.

The Model Nonprofit Corporation Act permits a nonprofit corporation to give some of the responsibilities and obligations of the board of directors to another group of persons known as a "designated body." If the law of an enacting state permits that type of governance structure, the optional phrase in subparagraph (B) should be included with appropriate changes to conform to the terminology used in the enacting state.

(10) "Interest holder": An enacting state should revise this definition so that it includes references to the appropriate persons with respect to each type of entity listed in the definition of "domestic filing entity."

(15) "Private organic rules": An enacting state should revise this definition so that it refers to the appropriate item with respect to each type of entity listed in the definition of "domestic filing entity."

(16) "Public organic record": An enacting state should revise this definition so that it refers to the appropriate document with respect to each type of entity listed in the definition of "domestic filing entity."

Comment

"Appropriate request." This definition is patterned after Section 2009(a)(1)(D) of the Homeland Security Act of 2002 (6 U.S.C. § 601 et seq.), as proposed to be added by S. 569 (111th Congress).

"Conventional privately held entity." The annual information returns referred to in subparagraphs (B)(vii) and (viii) of this definition are the form 990, 990-EZ, and 990-PF returns that are filed by private foundations or organizations exempt from federal income tax under sections 501(c), 527, or 4947(a)(1) of the Internal Revenue Code. Those returns, as well as applications for tax exempt status, are publicly available and require disclosure of, among other things, the officers, directors, trustees, and most highly compensated employees of an exempt organization and thus it is not necessary to require those organizations to comply with the disclosure provisions of this act.

If a nonprofit corporation does not have any members, it will fall within subparagraph (A) of this definition because it will have fewer than 50 interest holders, i.e., none.

"Governor." The second clause of subparagraph (E) of this definition, which refers to persons who are not managers of a limited liability company but participate materially in its management, is patterned after 6 Del. Code § 18-109(a). It is not intended that the power to elect or otherwise select or to participate in the election or selection of a person to be a manager of a limited liability company will, by itself, constitute participation in the management of the company.

"Interest holder." Whether a person is a member of a nonprofit corporation will be determined under a state's nonprofit corporation law. Many nonprofit corporations refer to their financial supporters as "members" even though those contributors do not have governance rights under the organic law and organic rules of the corporation.

"Responsible individual." A responsible individual may be an individual who is a governor of the entity, an agent of another person, or an agent or officer of the entity itself, or who meets the requirements of this definition because of ownership of an interest in the entity or other factors. To qualify as a responsible individual, what is required is that the individual participate in the control or management of the entity. A responsible individual may have sole responsibility for the management of the entity or may share that responsibility with others. The term has been created for use in this act and is not intended to change the law with respect to the governance of any form of entity.

SECTION 3. PUBLIC ORGANIC RECORDS.

(a) The public organic record of a domestic filing entity must include, in addition to any other information required by its organic law, a statement as to whether the entity is a conventional privately held entity. The delivery to the [Secretary of State] for filing of an initial or amended public organic record is an affirmation under the penalties of perjury by the entity and by any person signing the record that the statement required by this subsection is correct.

(b) When the initial public organic record of a conventional privately held entity is delivered to the [Secretary of State] for filing, it must be accompanied by an initial entity information statement.

(c) If the statement required by subsection (a) becomes incorrect, the entity shall deliver promptly to the [Secretary of State] for filing an amendment of its public organic record correcting the statement. [An amendment pursuant to this subsection need not be approved by

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the governors or interest holders.] [The [Secretary of State] may not charge a fee for filing an amendment pursuant to this subsection.]

(d) An amendment filed under subsection (c) indicating that an entity has become a conventional privately held entity must be accompanied by an entity information statement.

(e) Subsection (b) does not apply to an initial public organic record delivered to the [Secretary of State] before [the effective date of this act]. Subsections (a), (c), and (d) do not apply to a domestic filing entity that is in existence on [the effective date of this act] until the date provided in Section 16.

Legislative Notes:

Subsection (a): States should consider adding a reference to the requirements of subsection (a) in the section of the organic law of each domestic filing entity dealing with the entity's public organic record so that people consulting that law will be aware of the requirements of subsection (a). Such a reference in the section of the organic law of an entity dealing with the contents of its public organic record might read, for example, "the statement required by [Section 3(a) of the Uniform Law Enforcement Access to Entity Information Act]."

Subsection (c): The optional penultimate sentence of subsection (c) is intended to simplify the procedure for approving an amendment of the public organic record so that, for example, an amendment to the articles of incorporation of a business corporation to change the statement as to whether the corporation is a conventional privately held entity may be filed without action by the board of directors or shareholders. Enacting states may choose to place that type of provision in the individual organic laws for each type of entity listed in the definition of "domestic filing entity" in Section 2 or may decide to vary the rule of that sentence for some types of entities by requiring, for example, approval by the governors.

The last sentence of subsection (c) is optional because an enacting state may choose to require a fee for filing an amendment of the public organic record that is required under subsection (c). It will be preferable, however, for states not to require a fee as a way of encouraging amendments that keep the public records up to date regarding the status of an entity. If a state chooses to impose a fee, the fee will presumably be the same as for filing any other amendment to a public organic record. Thus the possibility of a fee being charged for a filing under subsection (c) has not been included in Section 13.

Comment

The public organic record of every domestic filing entity must include a statement satisfying subsection (a), either that the entity is a conventional privately held entity or that the

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entity is not a conventional privately held entity.

If a domestic filing entity ceases to be a conventional privately held entity, for example because it conducts a public offering of its equity securities, it will need to amend its public organic record to reflect the change in its status. Entity information statements previously delivered to the Secretary of State will remain in the records of the Secretary of State, but the entity will no longer have an obligation to update the information in the statements. The individuals previously identified as its records contact and responsible individual will cease to have that status.

Most organic laws provide that it is a criminal offense to sign a document delivered to the Secretary of State for filing that the signatory knows to be false in any material respect. The last sentence of subsection (a) confirms that result and also imposes liability on the entity for a false statement as to its status as a conventional privately held entity.

SECTION 4. ENTITY INFORMATION STATEMENT.

(a) An entity information statement must set forth:

(1) the name of the conventional privately held entity;

(2) the name and a business or residential address of the records contact of the entity; and

(3) the name and a business or residential address of a responsible individual of the entity.

(b) An initial entity information statement must be signed:

(1) on behalf of the conventional privately held entity;

(2) by the records contact named in the statement; and

(3) by the responsible individual named in the statement.

(c) If any of the information in a filed entity information statement becomes incorrect or incomplete, the conventional privately held entity shall deliver promptly to the [Secretary of State] for filing an amended entity information statement that is correct as of the date of its delivery to the [Secretary of State] and includes the information required by subsection (a).

(d) An amended entity information statement must be signed:

(1) on behalf of the conventional privately held entity;

(2) by any new records contact or new responsible individual named in the amended statement; and

(3) by any records contact or responsible individual whose address is being changed.

(e) A records contact or responsible individual may change his or her address or resign by delivering to the [Secretary of State] for filing a statement of change signed by the records contact or responsible individual that sets forth:

(1) the name of the conventional privately held entity; and

(2) either:

(A) the new address; or

(B) a statement that the records contact or responsible individual resigns.

(f) A records contact or responsible individual who delivers to the [Secretary of State] for filing a statement of change pursuant to subsection (e) shall furnish promptly to the conventional privately held entity notice in a record of the delivery to the [Secretary of State] of the statement of change and a copy of the statement.

(g) An initial entity information statement filed under subsection (a) takes effect upon filing or any later effective time of the initial or amended public organic record in connection with which the statement is delivered to the [Secretary of State] for filing. An amended entity information statement filed under subsection (c) or a statement of change filed under subsection (e) takes effect upon filing.

(h) The signing by a records contact or responsible individual of an entity information statement or a statement of change that reflects a change of address constitutes an affirmation

under the penalties of perjury that:

(1) the address of the signing person is correct; and

(2) either:

(A) the records contact understands the duties of a records contact under this [act] and has agreed to serve in that capacity; or

(B) the responsible individual meets the definition of a responsible individual in Section 2.

(i) Every signature of a records contact or responsible individual on an entity information statement or statement of change must be notarized.

(j) If the principal residence of the responsible individual identified in the current entity information statement is outside the United States, the responsible individual must provide to the records contact a copy of a passport, driver's license, or other government-issued photo identification document for the responsible individual.

[(k) The [Secretary of State] may not charge a fee for filing an amended entity information statement or statement of change.]

Legislative Notes:

Subsection (i): Subsection (i) does not specify the manner in which the required notarizations must be submitted. That is an issue to be determined by the enacting state and may require amendment of subsection (i) or other state law. Some states may choose to accept only paper filings, while other states may provide for electronic notarization or delivery of notarized documents by electronic means. If the Secretary of State only accepts electronic filings, an enacting state will need to provide for either electronic notarization or the delivery of notarized documents by electronic means.

Subsection (k): Subsection (k) is optional because an enacting state may choose to require a fee for filing an amended entity information statement or statement of change. It will be preferable, however, for states not to require a fee as a way of encouraging filings that keep the public records up to date. If a state chooses to impose a fee, the fee should be included in Section 13.

Comment

1. The same individual may serve as the records contact and responsible individual for a conventional privately held entity. When an entity needs to be formed on a rush basis, or when a records contact or responsible individual has not yet been identified for an entity, a person forming the entity, such as an incorporator, may serve as an accommodation in the capacities of records contact and responsible individual. Regardless of the reason why the person forming the entity is also shown as the records contact, so long as the person is named in that capacity, the person will have the duties and liabilities attendant to that position under this act.

2. Because subsection (c) requires an amended entity information statement to include all of the information required by subsection (a), a conventional privately held entity must always have a records contact and responsible individual identified in the records of the Secretary of State. *But see* the transitional provisions in Section 16.

3. Subsection (d) does not require that an amended entity information statement be signed by an individual named in an earlier statement as records contact or responsible individual if the information regarding that individual has not changed.

4. Subsection (g) provides that a statement of change under subsection (e), which could include a resignation by a records contact or responsible individual, takes effect upon filing. That is different from the practice in some states of delaying the effectiveness of a resignation of a registered agent. *See, e.g.*, Model Registered Agents Act § 11 (delaying a resignation for 31 days). The main function of a registered agent is simply to forward service of process to the represented entity, and delaying resignation from that position typically does not pose problems for either the registered agent or the represented entity. A records contact or responsible individual, in contrast, has an important place in the law enforcement process created by this act, making it more important for the records contact or responsible individual to be able to resign immediately in appropriate circumstances. Making a resignation effective immediately under subsection (g) also provides an earlier start to the period in which the entity must replace the records contact or responsible individual if the entity wishes to avoid administrative dissolution under Section 9.

5. The purpose of subsection (i) is to use the notarial process to provide some verification of the identity of a records contact or responsible individual since notarization requires the notary to know or verify the identity of the individual whose signature is being notarized.

Notarization may include taking an acknowledgment, administering an oath or affirmation, taking a verification upon oath or affirmation, or witnessing or attesting a signature. *See* Uniform Law on Notarial Acts (1982) § 1(1) ("notarial act"). The persons who may perform those acts are determined by state law and may be changed by a state to broaden or restrict the types of persons so authorized.

The manner in which a document with a notarized signature may be delivered to the Secretary of State will be determined by the Secretary of State and may include by fax or in

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portable document form (pdf). Modern law on notarial acts is also evolving to permit notarization of electronic records, and thus even in those states where all entity filings are made electronically it should be possible to comply with subsection (i).

Every state has statutory provisions dealing with notarial acts, although not every state has adopted the Uniform Law on Notarial Acts (1982). Those state statutes typically have separate provisions covering notarial acts performed within the state, under federal authority, and in foreign countries. Section 6 of the Uniform Law on Notarial Acts (1982) provides, for example, with respect to notarial acts performed in foreign countries:

> (a) A notarial act has the same effect under the law of this State as if performed by a notarial officer of this State if performed within the jurisdiction of and under authority of a foreign nation or its constituent units or a multi-national or international organization by any of the following persons:
>
> (1) a notary public or notary;
>
> (2) a judge, clerk, or deputy clerk of a court of record; or
>
> (3) any other person authorized by the law of that jurisdiction to perform notarial acts.
>
> (b) An "Apostille" in the form prescribed by the Hague Convention of October 5, 1961, conclusively establishes that the signature of the notarial officer is genuine and that the officer holds the indicated office.
>
> (c) A certificate by a foreign service or consular officer of the United States stationed in the nation under the jurisdiction of which the notarial act was performed, or a certificate by a foreign service or consular officer of that nation stationed in the United States, conclusively establishes any matter relating to the authenticity or validity of the notarial act set forth in the certificate.
>
> (d) An official stamp or seal of the person performing the notarial act is prima facie evidence that the signature is genuine and that the person holds the indicated title.
>
> (e) An official stamp or seal of an officer listed in subsection (a)(1) or (a)(2) is prima facie evidence that a person with the indicated title has authority to perform notarial acts.
>
> (f) If the title of office and indication of authority to perform notarial acts appears either in a digest of foreign law or in a list customarily used as a source for that information, the authority of an officer with that title to perform notarial acts is conclusively established.

Subsection (i) does not address the duty of the Secretary of State to verify that the notarization of a signature on an entity information statement is valid. The procedures for acceptance of notarized documents by the Secretary of State will be governed by other law of the state. That law often deals separately with notarizations performed within the state, outside of the state, under federal authority, or in foreign countries. *See, e.g.*, Uniform Law on Notarial Acts (1982) §§ 3-6.

1 **SECTION 5. DUTIES OF RECORDS CONTACT.**

2 (a) A records contact for a conventional privately held entity must:

3 (1) inquire at the time the records contact signs an initial or amended entity
4 information statement whether the current responsible individual is required to comply with
5 Section 4(j) and, if the responsible individual is required to comply but does not do so within five
6 business days after the [Secretary of State] files the initial or amended entity information
7 statement, to resign as records contact in the manner provided in Section 4(e);

8 (2) request promptly from the entity the information described in Section 7 when
9 the records contact receives an appropriate request for the information;

10 (3) produce on a timely basis to a party making an appropriate request:

11 (A) the photo identification document, if any, for the entity's responsible
12 individual required by Section 4(j);

13 (B) any information described in Section 7(a) which is provided by the
14 entity to the records contact; and

15 (C) any certification described in Section 7(b) which is provided by the
16 entity to the records contact;

17 (4) resign under Section 4(e) if the records contact acquires actual knowledge,
18 before receiving an appropriate request, that a request by the records contact to the entity for the
19 information described in Section 7(a) will not be honored by the entity on a timely basis; and

20 (5) if information in response to an appropriate request is not provided on a
21 timely basis by the entity upon request by the records contact, notify the party that made the
22 appropriate request of:

23 (A) the name and a business or residential address of the individual whom

the records contact believed would supply the information to the record contacts; or

(B) if there is no such individual, the source or location from which the records contact believed the information could be obtained.

(b) A records contact, as such, does not have a duty to verify the accuracy of information described in Section 4(j) or 7(a) or a certification under Section 7(b).

Comment

If there is a failure to respond to an appropriate request for information, the consequences of that failure and possible sanctions will depend on the nature of the request. For example, failure to respond to a subpoena will have the same consequences and sanctions as any other failure to respond to a subpoena under the applicable federal or state law. Whether the consequences of a failure to respond to an appropriate request for information should be imposed on the records contact or on the conventional privately held entity will depend on whether the records contact has performed the duties required by this section.

If an entity believes that it has defenses to a failure to respond to an appropriate request or should be excused from responding, it may raise those defenses or excuses in a proceeding to enforce the appropriate request or the entity may commence a proceeding to contest the appropriate request.

The requirement in subsection (a)(3) that information be produced on a "timely basis" is intended to satisfy Recommendation 33 of the 40 Recommendations of the Financial Action Task Force. In the case of a subpoena, what will be a timely response will be controlled by the response date in the subpoena and whether an appropriate challenge to the subpoena is made. A response date in a request made under a treaty, however, does not have the force of law and will not necessarily be binding.

A records contact may wish as a matter of good business practice to verify periodically that the records contact continues to have the required access to information, although an obligation to verify that the records contact continues to have access to information is not part of the required duties of a records contact.

If a records contact acquires actual knowledge that information will not be provided by an entity as required by this act, the records contact has a duty to resign under subsection (a)(4) even though there is no pending appropriate request.

A records contact is defined in Section 2(18) as an individual who has access to the information required by Section 7, and when a records contact signs an entity information statement under Section 4 that signature constitutes an affirmation that the individual understands the duties of a records contact.

Subsection (b) applies only to a records contact in the individual's capacity as a records contact. If the individual also maintains the records required to be produced under Section 7(a) in another capacity, for example as a corporate secretary, the individual will have the obligations associated with serving in that capacity. This act does not address those obligations.

SECTION 6. INTEREST HOLDERS FROM OUTSIDE UNITED STATES.

(a) Except as provided in subsection (e), when a non-US entity first becomes a transferee or interest holder in a conventional privately held entity after [the effective date of this act], whether by transfer, issuance of an interest, or admission as an interest holder, the transferee or interest holder shall provide the entity with a certification signed under the penalties of perjury stating the name and a business or residential address of a responsible individual for the transferee or interest holder.

(b) Except as provided in subsection (e), if any of the information in a certification provided under subsection (a) becomes incorrect, the interest holder or transferee shall provide promptly to the conventional privately held entity a corrected certification.

(c) A certification provided under subsection (a) or (b) that is incorrect or incomplete, or the failure of a conventional privately held entity to obtain a required certification, does not affect the existence of the conventional privately held entity, the validity of any acts of the entity, the interest of any interest holder or transferee, or the status of a person as an interest holder or transferee.

(d) A non-US entity that is required to provide a certification under this section may not maintain a proceeding in any court in this state with respect to the interest giving rise to the obligation to provide the certification unless the non-US entity complies with this section.

(e) Subsections (a) and (b) apply only to an interest holder or transferee that would be a conventional privately held entity if the interest holder or transferee were a domestic filing entity.

Comment

This section is patterned in part after Section 2009(a)(2) of the Homeland Security Act of 2002 (6 U.S.C. § 601 et seq.), as proposed to be added by S. 569 (111th Congress).

This section is not intended to require the conventional privately held entity to track transfers of interest. It is the obligation of a transferee to provide the certifications required by this section.

Subsection (c) is patterned in part after Model Business Corporation Act, 4th Ed. § 2.03 and Uniform Limited Liability Company Act § 2.01(d). Section 2.03(b) of the Model Act, for example, provides that "The secretary of state's filing of the articles of incorporation is conclusive proof that the incorporators satisfied all conditions precedent to incorporation except in a proceeding by the state to cancel or revoke the incorporation or involuntarily dissolve the corporation." States should consider whether to amend those types of provisions in their entity laws to make them consistent with subsection (c).

Subsection (d) is patterned after the provision found in many state entity laws that prohibits a foreign entity from maintaining a lawsuit in a state if the entity is transacting business in the state but has not registered to do business as a foreign entity. See, e.g., Model Business Corporation Act (4th Ed.) § 15.02(a) and Uniform Limited Liability Company Act (2006) § 808(a).

SECTION 7. RECORDS OF CONVENTIONAL PRIVATELY HELD ENTITIES.

(a) A conventional privately held entity must have a records contact at all times while it is a conventional privately held entity. When the records contact notifies the entity that an appropriate request has been received, the entity shall provide on a timely basis to the records contact information in a record that:

(1) includes the name and last known address of each current transferee of which the entity has actual knowledge, each current interest holder in the entity, and any other person to which the entity has been instructed to send distributions;

(2) indicates for each current transferee of which the entity has actual knowledge or current interest holder that is a foreign or domestic entity, the jurisdiction whose laws govern its internal affairs;

(3) includes the name and a residential or business address for each governor of

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the entity;

(4) includes a copy of a passport, driver's license, or other government-issued photo identification document for:

(A) each governor of the entity who is an individual and whose principal residence at the time the individual became a governor was outside the United States; and

(B) its responsible individual if the principal residence of the responsible individual is outside the United States;

(5) includes any records maintained by the entity regarding the process by which the governors of the entity are elected or otherwise designated;

(6) indicates the voting power in the entity held by each of its interest holders or describes the manner in which each interest holder's voting power in the entity is determined;

(7) identifies the individuals responsible for preparing the information provided to the records contact under this subsection; and

(8) includes the certifications required by section 6(a) and (b).

(b) When information is provided pursuant to subsection (a), it must include a certification by the conventional privately held entity, signed under the penalties of perjury, that the information accurately reflects the current records of the entity.

Comment

A non-U.S. resident is not required to supply a photo identification document as a condition to becoming a governor under paragraph (a)(4)(A). That paragraph simply requires that when an appropriate request is made the conventional privately held entity must be able to supply the required document. The entity may obtain the document at that time, but many entities will choose to obtain the document earlier because they otherwise run the risk of being unable to obtain the document on a timely basis once an appropriate request has been made. In contrast, if the principal residence of a responsible individual is outside the United States, the entity has a continuing obligation to obtain a photo identification document under subparagraph (a)(4)(B). The responsible individual also has an obligation to provide a photo identification document to the records contact under Section 4(j).

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The obligation to provide information under paragraph (a)(6) about voting power in the conventional privately held entity may be satisfied by supplying a copy of the operative documents that determine that voting power. Those documents will often be simply the public organic record or private organic rules of the entity, such as the articles of incorporation of a corporation or the operating agreement of a limited liability company; but may include other documents such as shareholder agreements, voting agreements, investor rights agreements, etc.

SECTION 8. JUDICIAL DISSOLUTION.

(a) The [name or describe court or courts] may dissolve a conventional privately held entity in a proceeding by [the Attorney General] if it is established that the entity materially failed to comply with Sections 7 or 12.

(b) It is not necessary to make interest holders or transferees parties to a proceeding to dissolve a conventional privately held entity under this section unless relief is sought against them individually.

(c) Until a full hearing is held, the court may issue injunctions, appoint a receiver or custodian with the powers and duties the court directs, and order other action required to preserve the assets and carry on the business of the conventional privately held entity.

(d) The court may appoint a receiver to wind up and liquidate the business and affairs of the conventional privately held entity. The court shall hold a hearing, after notifying all parties to the proceeding and any interested persons designated by the court, before appointing a receiver. The court appointing a receiver has exclusive jurisdiction over the entity and all of its property wherever located.

(e) The court may appoint as a receiver an individual, a domestic entity, or a foreign entity authorized to transact business in this state. The court may require the receiver to post bond, with or without sureties, in an amount the court directs.

(f) The court shall prescribe the powers and duties of the receiver in its appointing order,

which may be amended. The powers of the receiver may include the power to:

(1) dispose of all or any part of the assets of the conventional privately held entity wherever located, at a public or private sale, if authorized by the court; and

(2) sue and defend in the receiver's own name as receiver of the entity in all courts of this state.

(g) The court from time to time during the receivership may order compensation paid and expense disbursements or reimbursements made to the receiver and counsel for the receiver from the assets of the conventional privately held entity or from proceeds from the sale of the assets.

(h) If after a hearing the court determines that a ground under this section exists for judicial dissolution of a conventional privately held entity, the court shall order dissolution of the entity and specify the effective date of the dissolution. The clerk of the court shall deliver a certified copy of the decree to the [Secretary of State] for filing.

(i) After ordering dissolution, the court shall direct the winding-up of the business and affairs of the conventional privately held entity in accordance with the organic law of the entity.

Legislative Note: *If an enacting state has existing judicial dissolution procedures for some or all of the entities included in the definition of "domestic filing entity" in Section 2, this section may be revised so that it only applies to those entities for which the state does not already have judicial dissolution procedures. For those entities excluded from the scope of this section, subsection (a) will need to be added to the judicial dissolution provisions in the organic laws of those entities as an additional basis for judicial dissolution.*

Comment

If a conventional privately held entity believes that it has defenses to a proceeding to dissolve it under this section, those issues may be raised and tried in the dissolution proceeding.

An action under this section will usually involve just the conventional privately held entity. However, subsection (b) permits the interest holders or transferees to be made parties to the dissolution proceeding because it may be appropriate to seek relief against them, for example in a proceeding brought to dissolve an entity that has violated the prohibition in Section 12 on

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issuing bearer interests.

Judicial dissolution under this section is in addition to judicial dissolution on other grounds that may be provided in the organic law of an entity or an enacting state's other law.

SECTION 9. ADMINISTRATIVE DISSOLUTION.

(a) The [Secretary of State] shall administratively dissolve:

(1) a conventional privately held entity if the records of the [Secretary of State] do not show a current records contact or responsible individual for the entity for [60] consecutive days; and

(2) a domestic filing entity if its public organic record does not contain the statement required by Section 3(a).

(b) If the [Secretary of State] determines that a ground exists for dissolving an entity under subsection (a), the [Secretary of State] shall file a record of the determination and serve the entity with a copy of the filed record.

(c) If not later than [60] days after service of the copy pursuant to subsection (b) the entity does not correct each ground for dissolution or demonstrate to the reasonable satisfaction of the [Secretary of State] that each ground determined by the [Secretary of State] does not exist,, the [Secretary of State] shall administratively dissolve the entity by preparing, signing, and filing a declaration of dissolution stating the grounds for dissolution. The [Secretary of State] shall serve the entity with a copy of the filed declaration.

(d) An entity that has been dissolved under this section continues in existence but, subject to subsection (i), may carry on only activities necessary to wind up its activities under its organic law.

(e) The dissolution of an entity under this section does not terminate the authority of its agent for service of process or the responsibilities of a records contact shown in the records of

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the [Secretary of State] at the time of dissolution.

(f) An entity that has been dissolved under this section may apply to the [Secretary of State] for reinstatement by delivering to the [Secretary of State] for filing an application signed by the entity that states:

(1) the name of the entity and the effective date of its dissolution;

(2) either:

(A) the name and a business or residential address of the entity's records contact and the name and a business or residential address of the entity's responsible individual; or

(B) that the entity is not a conventional privately held entity; and

(3) if the entity's name is no longer available, a new name that satisfies the requirements of the entity's organic law.

(g) If the statement required by Section 3(a) in the public organic record of an entity that has been dissolved under this section is not consistent with the entity's application for reinstatement under subsection (f), the application must be accompanied by an amendment of the public organic record which states whether the entity is a conventional privately held entity.

(h) If the [Secretary of State] determines that an application under subsection (f) contains the required information and is accompanied by any required amendment of the entity's public organic record, the [Secretary of State] shall prepare a declaration of reinstatement that states those determinations, sign and file the original of the declaration of reinstatement, and serve the entity with a copy.

(i) When a reinstatement under subsection (h) becomes effective, it relates back to and takes effect as of the effective date of the administrative dissolution and the entity may resume

its activities as if the dissolution had not occurred.

(j) This section does not apply to a domestic filing entity in existence on [the effective date of this act] until the date provided in Section 16(b).

Legislative Note: *If an enacting state has existing administrative dissolution procedures, or procedures for voiding or cancelling an entity that is not in compliance with tax obligations or requirements of its organic law (all of the foregoing, "pre-existing procedures") for some or all of the entities included in the definition of "domestic filing entity" in Section 2, this section may be revised so that it only applies to those entities for which the state does not already have pre-existing procedures. For those entities excluded from the scope of this section, subsection (a) will need to be added to the pre-existing procedures in the organic laws of those entities as an additional basis for dissolution, voiding, or cancellation.*

This section may be conformed to the pre-existing procedures in the state. For example, if the existing practice in a state is for the Secretary of State to mail notice of an administrative dissolution, voiding, or cancellation to the entity, that practice may be substituted for the requirement in subsection (c) that the Secretary of State serve the filed declaration of dissolution on the entity.

Some state administrative dissolution statutes may include a time limit on reinstatement, unlike this section which does not impose a time limit on reinstatement. States should decide whether they wish to impose such a limit under this section.

Comment

This section applies to all domestic filing entities and not just conventional privately held entities. After the transition period provided in Section 16, failure of a domestic filing entity that is not a conventional privately held entity to include in its public organic record the statement required by Section 3(b) will be grounds for administrative dissolution of the entity.

A consequence of administrative dissolution in many states is to permit the use of the name of the dissolved entity by another entity. Thus subsection (f)(3) requires an entity seeking reinstatement to adopt a new name if its prior name has become unavailable because it has been appropriated by another entity during the period the entity seeking reinstatement was dissolved. *See, e.g.*, Model Business Corporation Act (4th Ed.) § 14.22(a)(3) and Uniform Limited Liability Company Act (2006) § 706(a)(3).

Administrative dissolution under this section is in addition to administrative dissolution on other grounds that may be provided in the organic law of an entity or an enacting state's other law.

SECTION 10. LIMITATION OF LIABILITIES.

(a) A records contact of a conventional privately held entity is not liable to the entity or

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its interest holders or transferees for producing upon an appropriate request the information described in Section 7(a) or the certification described in Section 7(b).

(b) Unless a contract between a conventional privately held entity and a records contact provides otherwise, a records contact is not liable for any inaccuracy in or omission from the information described in Section 7(a) or the certification described in Section 7(b), but this subsection does not limit the liability of a records contact for recklessness, intentional misconduct, or criminal conduct.

(c) A records contact or responsible individual is not liable under law other than this [act] solely because of being identified as a records contact or responsible individual in the records of the [Secretary of State].

(d) Compliance or noncompliance by a domestic filing entity with this [act] is not a ground for imposing liability on its interest holders, beneficial owners, transferees, or governors for the debts, obligations, or other liabilities of the entity.

Comment

Identifying an individual as a responsible individual does not by itself confer on the individual any power, or impose any duties, with respect to the control or management of the conventional privately held entity. The individual must have, however, whatever powers or duties are the basis for the determination that the individual participates in the control or management of the entity in a manner that satisfies the definition of "responsible individual" in Section 2(19). Similarly, identifying an individual as a responsible individual does not by itself make the individual liable for any of the debts, obligations, or liabilities of the entity.

Subsection (d) makes clear that the failure of a domestic filing entity to comply with the requirements of this act is not a basis for piercing the veil of the entity. That subsection also makes clear that complying with this act is not a basis for imposing liability on the interest holders or governors of an entity on the basis of an alter ego theory.

SECTION 11. ADDRESSES. Whenever this [act] requires the provision of an address, the following information must be provided:

(1) a street address or rural route box number; and

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(2) a mailing address, if different from the address under paragraph (1).

SECTION 12. PROHIBITION OF BEARER INTERESTS. A domestic filing entity may not issue a certificate in bearer form evidencing either a whole or fractional interest.

Legislative Note: *Enacting states may choose to omit this section and instead prohibit the issuance of bearer certificates in the individual organic laws for each type of entity listed in the definition of "domestic filing entity" in Section 2.*

Comment

In states that require legislation to be limited to a single subject, a question may arise as to whether this section deals with the same subject as the rest of the act. As discussed in the Prefatory Note, an important purpose of this act is to comply with FATF Recommendation 33, which requires both disclosure of ownership and control of entities and also the prohibition of bearer shares. When a purpose of the act is seen as complying with FATF Recommendation 33, the inclusion of this section should be within that single purpose. If a state nonetheless believes that including this section in the act may make the act unconstitutional, this section (or the alternative approach described in the Legislative Note) should be enacted by separate legislation.

SECTION 13. FEES.

Alternative A

(a) The [Secretary of State] shall collect the following fees when a document is delivered for filing under this [act]:

(1) initial entity information statement $___

(2) [amended entity information statement $___

(3) statement of change $___

(4)] application for reinstatement following administrative dissolution $___

Alternative B

(a) The [Secretary of State] shall adopt rules, in accordance with [the state's administrative procedure act] setting the fees for processing filings under this [act]. [The fees must be set at amounts such that the total amount of fees collected during a year is not less than

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the annual costs incurred by the [Secretary of State] in administering this [act].]

End of Alternatives

[(b) The fees collected under subsection (a) shall be deposited into a restricted account within the [general fund]. Funds in the restricted account shall be used only to administer this [act].]

Legislative Notes:

Alternative A: With respect to optional paragraphs (a)(2) and (3), see the Legislative Note to Section 4(k).

Subsection (b): Subsection (b) is optional. If subsection (b) is omitted by a state and Alternative B for subsection (a) is used, the last sentence of subsection (a) should also be omitted. If subsection (b) is adopted by a state, it should be revised to conform to the state's practice in establishing special purpose funds.

SECTION 14. PROCESSING OF DOCUMENTS. The [Secretary of State] may not file a document if the document or any aspect of its delivery to the [Secretary of State] does not comply with this [act].

[SECTION 15. CONFIDENTIALITY.

(a) The initial entity information statement of a conventional privately held entity and any amended statement or statement of change must be kept confidential by the [Secretary of State] and may be disclosed only:

(1) to an authorized agent of a [state, local, or] federal law enforcement agency, [state agency,] federal agency, or committee or subcommittee of the United States Congress [or a state legislature] upon the request of the agent in a signed record;

(2) in response to a request made in a record by a federal agency on behalf of another country under:

(A) an international treaty, agreement, or convention; or

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(B) 28 U.S.C. Section 1782; or

(3) to a person that is shown in the records of the [Secretary of State] as a current records contact, responsible individual, governor, or officer of the entity upon the request of the person in a signed record.

(b) A request pursuant to subsection (a)(1) or (2) must be kept confidential by the [Secretary of State] and may be disclosed only pursuant to a request under subsection (a)(1) or (2).]

Legislative Note: *With respect to subsection (a)(1), see the Legislative Note to Section 2(1).*

Comment

This section is optional because it implicates policy concerns beyond the scope of this act. Enactment or omission of this section will not affect the purpose of this act to provide law enforcement with important sources of information about conventional privately held entities. Some states may decide that it is appropriate to keep entity information statements confidential as permitted by this section. Other states may conclude that it is appropriate to make the contents of entity information statements publicly available.

This section does not require that the request of a law enforcement agency for access to an entity information statement must be an "appropriate request" as defined in Section 2. Any request in a record from an authorized law enforcement agent should be honored by the Secretary of State.

SECTION 16. TRANSITIONAL PROVISION.

(a) On or before the date provided in subsection (b), a domestic filing entity in existence on [the effective date of this act] shall deliver to the [Secretary of State] for filing:

(1) an amendment of its public organic record that contains the statement required by Section 3(a); and

(2) if it is a conventional privately held entity, an initial entity information statement.

(b) A domestic filing entity shall comply with subsection (a) by the earlier of:

(1) two years after the effective date of this act; or

(2) the date the entity first delivers any other document to the [Secretary of State] for filing under its organic law.

(c) The [Secretary of State], not earlier than one year after the effective date of this act, shall mail to every domestic filing entity that has not complied with subsection (a) a notice advising the entity of the requirement to comply with subsection (a). Failure by the [Secretary of State] to provide the notice to any entity, or failure by any person to receive the notice, shall not relieve an entity of the obligation to comply with subsection (a).

[(d) The amendment required by subsection (a)(1) need not be approved by the governors or interest holders of a domestic filing entity.]

Legislative Note: *Optional subsection (d) is intended to simplify the procedure for approving an amendment of the public organic record so that, for example, an amendment to the articles of incorporation of a business corporation to adopt the statement as to whether the corporation is a conventional privately held entity may be filed without action by the board of directors or shareholders. As with the similar optional provision in Section 3(c), an enacting state may choose to place that provision in the individual organic laws for each type of entity listed in the definition of "domestic filing entity" in Section 2 or may decide to vary the rule of subsection (d) for some types of entities by requiring, for example, approval by the governors.*

Comment

The intention of this act is that all entities will be in compliance within two years after the effective date of the act. Subsection (d) requires the Secretary of State to send out a reminder notice one year after the effective date to facilitate compliance. That notice or lack thereof does not modify or affect the requirement that all entities must comply with subsection (a) within two years after the effective date of the act. Failure of a domestic filing entity to comply with subsection (a) is grounds for administrative dissolution of the entity under Section 9.

SECTION 17. UNIFORMITY OF APPLICATION AND CONSTRUCTION. In applying and construing this uniform act, consideration must be given to the need to promote uniformity of the law with respect to its subject matter among states that enact it.

SECTION 18. RELATION TO ELECTRONIC SIGNATURES IN GLOBAL AND

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NATIONAL COMMERCE ACT. This [act] modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., but does not modify, limit, or supersede Section 101(c) of that act, 15 U.S.C. Section 7001(c), or authorize electronic delivery of any of the notices described in Section 103(b) of that act, 15 U.S.C. Section 7003(b).

SECTION 19. REPEALS. The following acts and parts of acts are repealed:

(1)

Legislative Note: *If a state chooses to include optional Section 15, it must consider the relationship between that section and its open records or similar right to know law. The state could amend or repeal its open records or similar law to the extent it would require that an entity information statement or statement of change not be kept confidential as provided in Section 15, or Section 15 could provide that initial and amended entity information statements and statements of change are not subject to the state's open records or similar law.*

SECTION 20. EFFECTIVE DATE. This [act] takes effect on . . . .

SUMMARY OF THE UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT

All domestic filing entities are prohibited from issuing certificates of bearer shares and are required to include in their initial public organic document (IPOD) filed in the office of the Secretary of State (SOS) a statement declaring whether or not the entity is a "conventional privately-held entity entity" (CPE).

A CPE is an entity that has no more than 50 interest holders. In addition to that ownership test, there are several exceptions. The most significant are: (i) highly regulated business entities such as depository institutions, insurance companies, public utilities, securities and commodity brokers or dealers, and registered investment companies and investment advisors; (ii) a majority owned subsidiary of one of those highly regulated entities; (iii) entities in which an entity with more than 50 interest holders holds more than 25% of the outstanding interests; and (iv) tax exempt entities and private foundations that have filed an annual information return as an exempt organization with the Internal Revenue Service.

A CPE must file an initial information statement (EIS) in the SOS at the same time the CPE files its IPOD. The EIS must contain the name and business or residential address of the CPE's "record contact" (RC) and "responsible individual" (RI). Changes in the RC and RI must promptly be filed in the SOS. The RI and RC must sign the EIS or a statement of change and these signatures must be notarized. An enacting state can elect to have the EIS treated as a confidential document to be disclosed only to authorized agents of law enforcement agencies and other specified agencies and committees.

An entity in existence when the Act becomes effective has 2 years from the effective date to amend its IPOD to state whether or not it is a CPE and if it is, to file in the SOS the required information concerning its RI and RC.

The RC must seek to obtain specified information about the ownership and control of a CPE upon receiving a subpoena or summons from a federal law enforcement authority, federal agency or committee or subcommittee of the United States Congress or a request by a federal agency on behalf of another country ("appropriate request") (AR). States have the option of expanding the list of persons who can make ARs to include state and local law enforcement authorities, state agencies and state legislatures.

The CPE must provide the RC on a timely basis: the name and last known address of each interest holder and transferee; the name and address for each governor; any records regarding the process by which governors are elected or otherwise designated; the voting power of each interest holder; and the names of the individuals responsible for preparing this information. The CPE must include a certification, signed under penalties of perjury, that the information accurately reflects its current records.

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Non-US entities that become interest holders or transferees of a CPE must provide the CPE with a certification, signed under penalties of perjury, stating the name and address of a RI. If a RI's principal residence is outside the US, the RI must provide a photo I.D. to the CPE. If the principal residence of a governor is outside the US, the governor must provide a photo I.D. to the CPE.

A RI is defined as an individual who, directly or indirectly, participates in the control or management of a CPE. A RI can be anyone associated with the CPE that meets the definition. He or she may, but need not, be a governor or have agency authority to bind the CPE to third parties. The purpose of having a RI is to have an individual who has detailed knowledge about a CPE that federal law enforcement officials and others who are entitled to make ARs can talk to about the entity and its operations.

A RC is liable for recklessness, intentional misconduct, or criminal conduct. A RI could be held liable for perjury if it turns out that he or she does not meet the qualifications of a RI and also may be held liable for refusal to comply with a AR subpoena or summons.

The enacting state's attorney general can bring a proceeding to dissolve a CPE for materially failing to provide the AR information requested by the RC or for issuing bearer certificates. The SOS must administratively dissolve an entity for failure to designate in its IPOD whether or not it is a CPE or if the SOS records do not show a current RC or RI for 60 consecutive days. Reinstatement is possible if the deficiencies are corrected.

Filing fees for the various documents required to be filed by the Act are authorized. The fees are required to be deposited in a restricted account that can only be used for administration of the Act.

The SOS can refuse to file any document required by the Act that does not comply with the Act. The SOS does not have any responsibility to verify any information submitted in any document filed pursuant to the Act.

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COMPARISON OF UNIFORM LAW ENFORCEMENT ACCESS TO ENTITY INFORMATION ACT AND THE LEVIN-GRASSLEY-MCCASKILL INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT (S.569)

Uniform Act	**S.569**
Coverage: Conventional privately held entities (CPE) defined as an entity with no more than 50 interest holders (e.g., shareholders) that must file an initial public organic record to be formed as a legal entity.	**Coverage**: Initially only corporations and limited liability companies (LLCs); possibility of additional legislation to cover partnerships, trusts and other legal entities on the basis of a report by Comptroller General 1 year after enactment.
Entities otherwise qualifying as a CPE in which an entity with more than 50 interest holders holds more than 25% of the outstanding interests, entities that are generally classified as "regulated" industries such as banks and other depository institutions, trust companies, insurance companies, public utilities, and securities and commodities brokers or dealers, investment companies, investment advisors and tax exempt entities that have filed a return as an exempt organization or private foundation with the Internal Revenue Service are exempt.	Corporations and LLCs that have issued securities registered under Section 12 or that are required to file reports under Section 15 of the 1934 Securities Exchange Act, and entities formed by state or the United States are exempt. Other exemption must be jointly approved by the Attorney General and the Administration of the Department of Homeland Security.
Entities in existence at the time the Act is effective have 2 years to comply.	Only Corporations and LLCs formed after the effective date of the Act are subject to the Act.
Compliance. A filing entity must include in its initial public organic record a statement as to whether or not it is a CPE. A CPE must also file in the office of the Secretary of State an "entity information statement" (EIS) at the time the initial public organic document is filed. The EIS contains the name and address of a "responsible individual" (RI), defined as an individual who directly or indirectly participates in the control or management of the entity, and the name and address of a records contact (RC), defined as an individual whose	**Compliance.** Corporations and LLCs must file with the State (no office, e.g. Secretary of State is designated) during the "formation process" (an undefined term) a list of the names and current addresses of all "beneficial owners" and must update the list annually if the state requires an annual filing. If no annual report is required, then the CPE must file updates at the time there are any changes in the list. "Beneficial owner" is defined as "an individual who has a level of control over, or entitlement to, the funds or assets of a corporation or

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principal residence is in the United States who has access to and can produce on a timely basis ownership and control information about the entity.

The records that the CPE must provide the RC upon an appropriate request are:

(1) a list of the name and last known address of each interest holder and transferee and if the interest holder or transferee is an entity, the name of the state or country where it was formed;

(2) name and address of each governor (e.g., director);

(3) any records the CPE maintains regarding the process by which its governors are elected or otherwise designated;

(4) the voting power of each interest holder or a description of the manner in which each interest holder's voting power in the entity is determined;

(5) the names of the individuals responsible for preparing the information; and

(6) a certificate that the information accurately reflects the current records of the CPE.

Appropriate Request: The RC contacts the CPE for the above information upon service of a civil, criminal or administrative subpoena or summons from a federal law enforcement authority, federal agency or committee or subcommittee of the US Congress (states can expand the list to include state and local law enforcement authorities, state agencies and state legislatures); and a written request made by a federal agency

limited liability company that, as a practical matter, enables the individual directly or indirectly, to control, manage, or direct the corporation or limited liability company." An individual who controls an entity that is a record owner of a corporation or LLC is a beneficial owner of the corporation or LLC if that entity is an a position to exercise control of the corporation or LLC.

Appropriate Request: The state must provide the beneficial ownership information pursuant to a civil or criminal subpoena or summons from a state or federal agency or congressional committee or subcommittee; and a written request made by a federal agency on behalf of another country under an international treaty, agreement or convention, or 28 U.S.C. § 1782.

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on behalf of another country under an international treaty, agreement, or convention or 28 U.S.C. § 1782.

Special Requirements for Non-US Entities/Citizen/Residents. A CPE must have in its records and deliver to the RC: (1) a certification from a non-US entity that is an interest holder or transferee stating the name and address of a RI for the Non-US entity; (2) a copy of a passport, driver's license, or other photo ID for any RI whose principal residence is outside the US; and (3) a copy of a passport, driver's license or other government-issued photo ID for each governor whose principal residence is outside the US at the time the individual becomes a governor.

Penalties and Sanctions

(1) the State's civil and criminal penalties for violation of a subpoena or summons.

(2) the entity and the person signing any document filed in the office of the Secretary of State that contains false information is subject to the state remedies for perjury.

(3) the RI and RC certify, under penalties of perjury that they meet the statutory qualifications for their positions; and the signature of both the RI and the RC in the EIS and any change in the RI or RC must be notarized.

(4) the person signing the certification that the records provided to the RC accurately reflect the current records of

Special Requirements for Non-US Entities/Citizen/Residents. Beneficial owners who are not US citizens or lawful permanent residents of the US must provide to the formation agent (defined as a "person, who, for compensation acts on behalf of another person to assist in the formation of a corporation or limited liability company") a copy of a page of the government-issued passport on which a photograph of the beneficial owner appears. The formation agent must certify that he or she has verified the name, address and identity of each of these beneficial owners and has obtained the required photo ID in the document containing the beneficial ownership information filed with the state. The formation agent must also provide proof of the verification and the photograph as part of the response to the subpoena or summons.

Penalties and Sanctions

In addition to any civil or criminal penalty that may be imposed by a state, any person who "knowingly" provides fake beneficial ownership information to a state or "intentionally" fails to provide beneficial ownership information (1) shall be liable to the United States for a civil penalty or not more than $10,000; and (2) may be fined under title 18, US Code, imprisoned for not more than 3 years, or both.

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the entity is subject to penalties or perjury.

(5) the certificates filed by a non-US entity designating a RI must be signed under penalties of perjury; and the non-US entity cannot maintain any proceeding in the state with respect to its interest in the CPE until it files the certificate.

(6) an enacting state's attorney general can bring an action to dissolve a CPE for material failure to comply with an appropriate request for information or for issuing bearer certificates. The court can issue appropriate injunctions and appoint a receiver for the entity.

(7) The secretary of state must administratively dissolve an entity for (a) failure to comply with the requirement that the entity state whether or not it is a CPE in its initial public organic document filing; or (b) the secretary of state's records do not show a current RC or RI for a period of 60 consecutive days.

(8) The RC is liable for "recklessness, intentional misconduct; or criminal conduct" for failure to perform his or her responsibilities.

Confidentiality. An enacting state has the option of designating the EIS which names the RI and RC and any document indicating changes in the RI and RC confidential and available only to (1) law enforcement agencies and others who have the right to make an appropriate request, (2) the current RI or RC or (3) a governor or officer of the entity.

Confidentiality. S.569 does not address the issue of confidentiality.

Bearer Interests. No filing entity can issue bearer equity interests in the entity.

Bearer Interests. S.569 does not address bearer interests. The equivalent bill introduced in congress in 2008 did prohibit bearer

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interests.

Funding. Filing fees for the various documents that must be filed pursuant to the Act are authorized and are required to be held in a restricted account for use only in the administration of the act.

Funding. The administration of the Department of Homeland Security may allocate DHS funds "to enable a State to obtain and manage" beneficial ownership information for corporations and LLCs, including funding to "assess, plan, develop, test, or implement relevant policies, procedures, or systems modifications."

Compliance Date. Each enacting state determines the effective date of the Act. All CPEs formed after the effective date must comply with the Act at the time of formation. Each one formed before the effective date must be in compliance no later than from 2 years after the effective date.

Compliance Date. Every state that receives DHS funding must "use an incorporation system" that meets the requirements of S.569 by no later than the beginning of fiscal year 2012.

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Memorandum

TO: DRAFTING COMMITTEE ON RECORD OWNERS OF BUSINESSES ACT

FROM: Harry J. Haynsworth, Chair

DATE: March 4, 2008

RE: **Overview of Issues Involved in Determining Beneficial Ownership and Control of Interests in Business Entities**

Collection and maintenance of accurate business entity beneficial ownership and control information is a key component of the anti-money laundering business entity proposals that have been made by FATF, the U.S. Senate Homeland Security Committee Permanent Subcommittee on Investigations, the Department of Justice and various units within the Treasury Department dealing with money laundering issues. The purpose of this memorandum is to provide a brief overview of the issues and problems that will arise if business entities are required to collect and maintain complete beneficial ownership information in addition to record owner information, which is and always has been the recordkeeping standard in U.S. business entity laws.

Several samples of beneficial ownership statutes are attached as exhibits. All of them share certain common characteristics. First, all of them have as their objective determining who actually controls the entity. Second, they all contain an indirect as well as a direct ownership requirement.

1. Control

Control is generally defined as having a specified percentage of voting power sufficient to elect or remove the managers of a business entity. The percentage figure used in current statutes varies considerably. European Union Directive 2005/60/EC (Exhibit 1) uses 25% as does the United Kingdom definition (Exhibit 2). The most recent Department of Justice proposal (Exhibit 3) specifies 15%. I have seen some control definitions relating to publicly-traded corporations that use a 10% figure (*see* Exhibit 4). The general statutory rule for election of directors in a corporation is a majority (50%+) of the shares entitled to vote for directors. The general statutory rule in U.S. uniform unincorporated entity statutes is unanimity (100%), but this percentage can be changed by agreement of the partners (partnership) or members (limited

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liability company).[1] Many state unincorporated entity statutes, however, use a majority member or percentage of capital vote as the default rule for the election of managers.

Two additional differences between corporate and unincorporated entity statutes complicate the control analysis. The first is that in U.S. unincorporated entities managerial and financial rights are severable. Therefore, it is possible to have 100% of the voting and managerial rights in one or more individuals and 100% of the financial rights in another person. This type of arrangement is fairly common in limited partnerships where there is typically a single general partner who manages the partnership and may have a right to some of the profits and limited partners who have few, if any, voting rights but are entitled to most of the profits and distributions.[2] Also, it is possible in an unincorporated entity for an owner to transfer all of the owner's rights to profits distributions to a third party (called a transferee), but to retain all of the voting and managerial rights.

A second difference is that in many U.S. unincorporated entities both voting rights and distribution rights are based on the relative percentage of each partner's or member's capital account (roughly capital contributions and undistributed profits), which can change on a daily basis, whereas in a corporation voting rights and distribution and equity rights are based on the relative percentage of stock ownership rights and change only where there is a transfer of the underlying stock. Thus in a partnership a partner might have 51% of the total capital accounts on day 1 and because of a disproportionate distribution made at the end of day 1 have only 49% of the capital on day 2 without any transfer of the underlying equity interest having taken place. If a 50% control test was the benchmark, the partner would be in control on day 1 but not on day 2.

The beneficial ownership proposals made by FATF, et al. all exclude publicly held companies[3] and seem to be aimed at determining "control" in companies that are classified as closely held, a term that is generally understood to mean a business entity having a small number of equity owners.[4] This being the case, it would seem that the "control" standard should be

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[1] The default unanimity rule in many unincorporated entity statutes raises an interesting "control" issue. Since each owner has in effect a veto power on all decisions, does that mean that all the owners have a controlling interest or that none of them have a controlling interest?

[2] It is possible to achieve basically the same result in a corporation by use of non-voting stock.

[3] As a general rule, a publicly held company is one whose ownership interests are widely held. A common standard would be a business entity whose ownership interests are listed on a stock exchange and/or are required to file reports with the SEC under the 1934 Securities and Exchange Act (300 or more shareholders). Publicly held companies constitute less than 1% of all U.S. business entities.

[4] There is no agreed-upon standard for the maximum number of owners in a closely held business. The maximum number of shareholders a corporation can have to qualify for taxation under Subchapter S of the Internal Revenue Code is 75 (when Subchapter S was first enacted approximately 50 years ago, the maximum was 10). The Subchapter S maximum would be on the high side of "closely held" definitions used in other statutes and in cases.

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"more than 50%"[5] since that is the standard for election of directors/managers in U.S. corporation statutes and many U.S. unincorporated entity statutes. A 25% or less control standard makes more sense with respect to publicly held companies because the holders of large blocks of stock constituting much less than 50% in a publicly held corporation can in many cases be sufficient to control the outcome of director elections, etc.

2. Indirect Ownership

A second characteristic shared by all existing beneficial ownership statutes is that an individual is deemed to own not only the equity interest in a business entity that the individual owns directly but also equity interests that the individual owns indirectly. These indirect interests are added to the direct interests to determine the total interest the individual owns. The existing statutes generally contain two categories of indirect or constructive ownership. The first is family members and the second is constructive ownership based on ownership interests in trusts, estates, and various forms of business entities.

Under family member constructive ownership rules, stock (or any other ownership interest) is attributed to and from other family members. First, you have to determine which family members are included. How far up and down the family tree is appropriate, *i.e.*, are grandparents and grandchildren included? What about stepchildren and adopted children and spouses and the spouse's parents, etc.? Are individuals who live in the same home as the record owner but are not related by blood to the record owner considered as family for purposes of the constructive ownership rules?[6]

Several issues involving attribution to and from trusts, estates and various business entities must also be resolved. With respect to trusts, should there be a distinction between revocable and irrevocable trusts? What if an individual is the trustee of the trust but is not a beneficiary of the trust? How should contingent as opposed to vested interests be treated? What percentage of beneficial interest is necessary to trigger the attribution of the interest to an individual in order to determine control? Beneficial ownership interests in estates raise these same questions. With respect to attribution to and from various forms of business entities, you would have to specify in the statute what percentage ownership in the entity is necessary to trigger the attribution. Other issues that have to be determined are how are options and warrants and convertible securities treated? Is non-voting stock included in the calculation? In unincorporated entities, is the attribution based solely on voting rights, as is the case with a corporation, or should it be based on the partner's share of the capital account or both? Should S

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[5] Any statute or regulation defining control would have to state how options to acquire stock or other equity interests should be treated in determining the interest held by an individual. Whether only vested options should be counted would also have to be specified.

[6] A category not included in many of the existing beneficial ownership statutes is a relationship based not on family but on employment or a contractual relationship. For example, what if Osama Bin Laden's chauffeur is the record owner of stock in a corporation. Should that stock nevertheless be attributed to Osama Bin Laden because of the "control" he would have over the chauffeur?

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corporations, which are corporations for state law purposes but are treated somewhat like partnerships for federal tax purposes, be treated the same as C corporations or as partnerships?

Once the constructive ownership rules have been established, then you have to apply them to a specific set of facts. The examples in Treas. Reg. 1-318-2 through -4, (*see* Exhibit 6), applying the constructive ownership rules in Section 318 of the Internal Revenue Code illustrate the complexities of making this determination.[7] For the most part, the determination of beneficial ownership must be made by accountants and lawyers for the entity and the owners of the entity for a particular purpose (*e.g.*, taxes, SEC reporting requirements) at a particular point in time. The calculation is not made on a day-to-day basis because so many events can occur (*e.g.*, death, bankruptcy, voluntary transfers) that can affect the beneficial ownership calculation.

Requiring a business entity to collect and maintain on an ongoing basis all the information necessary to make the beneficial ownership determination would be an enormous burden and a radical departure from existing recordkeeping requirements. Moreover, because of the complexities involved, there would undoubtedly be massive amounts of noncompliance, most of which would be unintentional. An entity would have to know all of an individual's family, as defined in the statute and the names of all the shareholders, partners and members of any entity that is an equity owner in the entity responsible for keeping the information. It would also need to know the name of the owners of any entity that was an owner of that second entity, and so on, as well as the beneficiaries of estates and trusts that have an ownership interest in any of the entities in the chain. It is quite common in the U.S. to have three or more tiers of entity ownership, which complicates the analysis. An even more difficult task would be the necessity to obtain knowledge of any changes in the various ownership interests in the chain, many of which it would have no notice of unless the transferor notifies the entity of the change because the transfer does not cause a change in the record owners of the entity. A change in beneficiaries of an estate or trust is an example. Another example would be a transfer by an owner of an entity that is an equity holder of the entity that is required to keep the beneficial ownership information current where the transfer does not result in a change in the name of that entity.[8]

Having individuals maintain beneficial owner records and file any changes in any company they own with the Secretary of State, which is Part B of the Department of Justice Proposal (Exhibit 3) does not solve any of the complex problems involved with having these records kept by business entities. The statute would still have to define what control and indirect ownership rules apply and inadvertent noncompliance would undoubtedly be even greater than if companies were required to keep the information. Moreover, requiring this information to be filed in the Secretary of State raises another level of additional complexity. The issues that

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[7] The examples show that in many cases more than one individual could be deemed to own a "controlling" interest because of the constructive ownership rules. *See* Treas. Reg. §1.318-2(b) where four family members each own directly 25% of the stock but constructively three of the four own 100% of the stock and the fourth owns 75% of the stock.

[8] Control can also be achieved by private contractual arrangements such as voting agreements, which the business entity might not know about because this type of arrangement does not involve a change of record ownership in the entity.

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would have to be determined include the following: Would the individual have to file this information in the state of his or her residence or in the state where the business entity was formed (or in which it has become domesticated). Would these beneficial owner records be public or non-public? Who would have access to this information? Are the secretaries of state capable of keeping dual sets of easily retrievable records on companies, one set dealing with public information and a second dealing with non-public information? Who would have to bear the cost of this new recordkeeping requirement?[9]

Amending the record owner provisions in existing U.S. entity laws to enable law enforcement officials to trace ownership in an entity back to the individuals who ultimately control the entity (using whatever definition of control is deemed appropriate under applicable criminal statutes) will provide a workable system that will accomplish the legitimate needs of law enforcement officials to obtain beneficial ownership information without the imposition or the enormous costs and complexities of amending business entity laws to require companies to maintain accurate, current beneficial ownership records.

HJH/nr
Attach.

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[9] If only individuals rather than entities are required to keep and/or file beneficial ownership records, this would require statutory law other than amendments to the state business entity statutes, which only deal with compliance issues applicable to an entity, the relationship between the owners and managers and the entity and the rights and liabilities of the entity to third parties.

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EXHIBIT 1

(6) 'beneficial owner' means the natural person(s) who ultimately owns or controls the customer and/or the natural person on whose behalf a transaction or activity is being conducted. The beneficial owner shall at least include:

(a) in the case of corporate entities:

(i) the natural person(s) who ultimately owns or controls a legal entity through direct or indirect ownership or control over a sufficient percentage of the shares or voting rights in that legal entity, including through bearer share holdings, other than a company listed on a regulated market that is subject to disclosure requirements consistent with Community legislation or subject to equivalent international standards; a percentage of 25 % plus one share shall be deemed sufficient to meet this criterion;

(ii) the natural person(s) who otherwise exercises control over the management of a legal entity;

(b) in the case of legal entities, such as foundations, and legal arrangements, such as trusts, which administer and distribute funds:

(i) where the future beneficiaries have already been determined, the natural person(s) who is the beneficiary of 25 % or more of the property of a legal arrangement or entity;

(ii) where the individuals that benefit from the legal arrangement or entity have yet to be determined, the class of persons in whose main interest the legal arrangement or entity is set up or operates;

(iii) the natural person(s) who exercises control over 25 % or more of the property of a legal arrangement or entity;

(7) 'trust and company service providers' means any natural or legal person which by way of business provides any of the following services to third parties:

(a) forming companies or other legal persons;

(b) acting as or arranging for another person to act as a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons;

(c) providing a registered office, business address, correspondence or administrative address and other related services for a company, a partnership or any other legal person or arrangement;

(d) acting as or arranging for another person to act as a trustee of an express trust or a similar legal arrangement;

(e) acting as or arranging for another person to act as a nominee shareholder for another person other than a company listed on a regulated market that is subject to disclosure requirements in conformity with Community legislation or subject to equivalent international standards;

(8) 'politically exposed persons' means natural persons who are or have been entrusted with prominent public functions and immediate family members, or persons known to be close associates, of such persons;

(9) 'business relationship' means a business, professional or commercial relationship which is connected with the professional activities of the institutions and persons covered by this Directive and which is expected, at the time when the contact is established, to have an element of duration;

(10) 'shell bank' means a credit institution, or an institution engaged in equivalent activities, incorporated in a jurisdiction in which it has no physical presence, involving meaningful mind and management, and which is unaffiliated with a regulated financial group.

Article 4

1. Member States shall ensure that the provisions of this Directive are extended in whole or in part to professions and to categories of undertakings, other than the institutions and persons referred to in Article 2(1), which engage in activities which are particularly likely to be used for money laundering or terrorist financing purposes.

2. Where a Member State decides to extend the provisions of this Directive to professions and to categories of undertakings other than those referred to in Article 2(1), it shall inform the Commission thereof.

Article 5

The Member States may adopt or retain in force stricter provisions in the field covered by this Directive to prevent money laundering and terrorist financing.

EXHIBIT 2

12/4/2007

Meaning of beneficial owner

(1) In the case of a body corporate, "beneficial owner" means any individual who—
(a) as respects any body other than a company whose securities are listed on a regulated market, ultimately owns or controls (whether through direct or indirect ownership or control, including through bearer share holdings) more than 25% of the shares or voting rights in the body; or
(b) as respects any body corporate, otherwise exercises control over the management of the body.

(2) In the case of a partnership (other than a limited liability partnership), "beneficial owner" means any individual who—
(a) ultimately is entitled to or controls (whether the entitlement or control is direct or indirect) more than a 25% share of the capital or profits of the partnership or more than 25% of the voting rights in the partnership; or
(b) otherwise exercises control over the management of the partnership.

(3) In the case of a trust, "beneficial owner" means—
(a) any individual who is entitled to a specified interest in at least 25% of the capital of the trust property;
(b) as respects any trust other than one which is set up or operates entirely for the benefit of individuals falling within sub-paragraph (a), the class of persons in whose main interest the trust is set up or operates;
(c) any individual who has control over the trust.

(4) In paragraph (3)—
"specified interest" means a vested interest which is—
(a) in possession or in remainder or reversion (or, in Scotland, in fee); and
(b) defeasible or indefeasible;
"control" means a power (whether exercisable alone, jointly with another person or with the consent of another person) under the trust instrument or by law to—
(a) dispose of, advance, lend, invest, pay or apply trust property;
(b) vary the trust;
(c) add or remove a person as a beneficiary or to or from a class of beneficiaries;
(d) appoint or remove trustees;
(e) direct, withhold consent to or veto the exercise of a power such as is mentioned in subparagraph (a), (b), (c) or (d).

(5) For the purposes of paragraph (3)—
(a) where an individual is the beneficial owner of a body corporate which is entitled to a specified interest in the capital of the trust property or which has control over the trust, the individual is to be regarded as entitled to the interest or having control over the trust; and
(b) an individual does not have control solely as a result of—
(i) his consent being required in accordance with section 32(1)(c) of the Trustee Act 1925 (power of advancement);
(ii) any discretion delegated to him under section 34 of the Pensions Act 1995 (power of investment and delegation);
(iii) the power to give a direction conferred on him by section 19(2) of the Trusts of Land and Appointment of Trustees Act 1996 (appointment and retirement of trustee at instance of beneficiaries); or
(iv) the power exercisable collectively at common law to vary or extinguish a trust where the beneficiaries under the trust are of full age and capacity and (taken together) absolutely entitled to the property subject to the trust (or, in Scotland, have a full and unqualified right to the fee).

(6) In the case of a legal entity or legal arrangement which does not fall within paragraph (1), (2) or (3), "beneficial owner" means—

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EXHIBIT 3

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The following is a draft summary of the basic requirements that the Department of Justice deems necessary to include in any legislation establishing minimum requirements for the collection of beneficial owner information by the States. The objective of any legislative change is to establish the collection and maintenance of accurate records which identify the true beneficial owner(s) of a business. The proposed legislation must include the following:

A. Establish a definition of "beneficial owner". There are a number of definitions worldwide for "beneficial owner", which may assist in drafting this important definition, including but not limited to the definitions contained in: 31 CFR 103.175; 17 CFR 240.13d-3; the United Kingdom Money Laundering Regulations, effective December 15, 2007;[1] and the European Union (Third Anti-Money Laundering Directive).[2] For purposes of this concept paper, the following definition of beneficial owner has been elected:

> "beneficial owner" means (a) a natural individual who has a level of control over, or entitlement to, the funds or assets of the corporation or limited liability company or partnership that, as a practical matter, enables such individual, directly or indirectly, to control, manage or direct such entity; or (b) a natural individual who owns more than 15% of the corporation or limited liability company or partnership. If a natural individual exercises such control or ownership over such corporation or limited liability company or partnership through another legal entity, such as a corporation, limited liability company or a partnership, the beneficial owners shall also identify each such legal entity being used by such individual to exercise control over the corporation or limited liability company or partnership and the majority beneficial owner of such entity.

B. Require the beneficial owner of a business:

1. to provide a State with adequate information regarding the identity and location of the beneficial owners, prior to the initial incorporation of the entity. The objective of this requirement is that the beneficial owners provide, and that the States collect the names, current addresses and photos of the natural individuals (rather than legal entities) who will be the true owners of the business that the States are being asked to form. For United States Citizens, the beneficial owner must provide either a copy of his or her driver's license or passport. All other beneficial owners must provide a copy of his or her passport.

[1] Used by the United Kingdom in conjunction with the Financial Action Task Force (FATF), a leading international organization combating money laundering and terrorist financing.
[2] Used by the European Union in conjunction with the FATF.

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2. to verify through signature, subject to criminal penalty, that the information provided to the States has been reviewed, and is true and accurate. This provision is to ensure that there are sufficient criminal penalties to allow either State or Federal authorities to prosecute individuals who provide false information to the State regarding beneficial owners.

3. to be subject to criminal and civil liability until the new beneficial owners' documents are provided to the incorporating State, when an existing business is sold or transferred to a new beneficial owner. This provision is to ensure that businesses maintain and update accurate records with the incorporating State. It is anticipated that there will be criminal penalties for the knowing failure to document the attempted transfer of beneficial ownership. Additionally, it is anticipated that—when the identity documents for a new beneficial owner has not been filed with the proper State authorities—any attempted transfer of ownership will be void, and civil liability for damages caused by the corporation after the date of the putative transfer will attach to the existing beneficial owners. This civil liability will include a rebuttable presumption that the corporate veil is pierced as to the beneficial owners.

C. Require the States to maintain the information regarding the beneficial owner. This provision is to ensure that law enforcement has access to the beneficial owner documents (including payment information for State taxes and fees) for a reasonable period of time (e.g. five to seven years) after the business has ceased to exist.

D. Allow State and Federal law enforcement access to the beneficial owners' information within a reasonable amount of time, after a written request has been made by a law enforcement agency. This provision is to ensure that State and Federal law enforcement have timely access to the beneficial owners' information so the agents may expeditiously use and benefit from the information when investigating criminal activity. State and Federal law enforcement must also have the ability to share beneficial owner records with their foreign law enforcement counterparts when requested within the context of their official duties. To address concerns of those States that do not wish to make the beneficial owners' information available to the general public, this provision will be limited so that only law enforcement will have access to the information in conjunction with a criminal investigation or request from a foreign counterpart.

E. Establish an exception to the above requirements for publicly traded companies, such as those traded on the New York Stock Exchange (e.g. Ford Motor Company); and for larger legitimate privately owned companies (e.g. Mars Incorporated). This provision is intended to avoid burdening both the States and the larger legitimate public and private corporations with the requirement to produce and maintain a large number of documents. These larger corporations have no history of facilitating criminal activity through the use of shell companies; and are already required, as are the corporations' subsidiary companies, to provide Federal and State regulators with significant amounts of information regarding the corporation's ownership and management.

EXHIBIT 4

Notes on Terms Used in Comments

In the Official Comments to subchapter F sections, the director who has a conflicting interest is for convenience referred to as "the director" or "*D*," and the corporation of which he or she is a director is referred to as "the corporation" or "*X* Co." A subsidiary of the corporation is referred to as "*S* Co." Another corporation dealing with *X* Co. is referred to as "*Y* Co."

§ 8.60 Subchapter Definitions

In this subchapter:

(1) "Director's conflicting interest transaction" means a transaction effected or proposed to be effected by the corporation (or by an entity controlled by the corporation)

(i) to which, at the relevant time, the director is a party; or

(ii) respecting which, at the relevant time, the director had knowledge and a material financial interest known to the director; or

(iii) respecting which, at the relevant time, the director knew that a related person was a party or had a material financial interest.

(2) "Control" (including the term "controlled by") means (i) having the power, directly or indirectly, to elect or remove a majority of the members of the board of directors or other governing body of an entity, whether through the ownership of voting shares or interests, by contract, or otherwise, or (ii) being subject to a majority of the risk of loss from the entity's activities or entitled to receive a majority of the entity's residual returns.

(3) "Relevant time" means (i) the time at which directors' action respecting the transaction is taken in compliance with section 8.62, or (ii) if the transaction is not brought before the board of directors of the corporation (or its committee) for action under section 8.62, at the time the corporation (or an entity controlled by the corporation) becomes legally obligated to consummate the transaction.

(4) "Material financial interest" means a financial interest in a transaction that would reasonably be expected to impair the objectivity of the director's judgment when participating in action on the authorization of the transaction.

(5) "Related person" means:

(i) the director's spouse;

(ii) a child, stepchild, grandchild, parent, step parent, grandparent, sibling, step sibling, half sibling, aunt, uncle, niece or nephew (or spouse of any thereof) of the director or of the director's spouse;

(iii) an individual living in the same home as the director;

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(iv) an entity (other than the corporation or an entity controlled by the corporation) controlled by the director or any person specified above in this subdivision (5);

(v) a domestic or foreign (A) business or nonprofit corporation (other than the corporation or an entity controlled by the corporation) of which the director is a director, (B) unincorporated entity of which the director is a general partner or a member of the governing body, or (C) individual, trust or estate for whom or of which the director is a trustee, guardian, personal representative or like fiduciary; or

(vi) a person that is, or an entity that is controlled by, an employer of the director.

(6) "Fair to the corporation" means, for purposes of section 8.61(b)(3), that the transaction as a whole was beneficial to the corporation, taking into appropriate account whether it was (i) fair in terms of the director's dealings with the corporation, and (ii) comparable to what might have been obtainable in an arm's length transaction, given the consideration paid or received by the corporation.

(7) "Required disclosure" means disclosure of (i) the existence and nature of the director's conflicting interest, and (ii) all facts known to the director respecting the subject matter of the transaction that a director free of such conflicting interest would reasonably believe to be material in deciding whether to proceed with the transaction.

Official Comment

The definitions set forth in section 8.60 apply only to subchapter F's provisions and, except to the extent relevant to subchapter G, have no application elsewhere in the Model Act. (For the meaning and use of certain terms used below, such as "*D*," "*X* Co." and "*Y* Co.", see the Note at the end of the Introductory Comment of subchapter F.)

1. Director's Conflicting Interest Transaction

The definition of "director's conflicting interest transaction" in subdivision (1) is the core concept underlying subchapter F, demarcating the transactional area that lies within—and without—the scope of the subchapter's provisions. The definition operates preclusively in that, as used in section 8.61, it denies the power of a court to invalidate transactions or otherwise to remedy conduct that falls outside the statutory definition of "director's conflicting interest transaction" solely on the ground that the director has a conflict of interest in the transaction. (Nevertheless, as stated in the Introductory Comment, the transaction might be open to attack under rules of law concerning director misbehavior other than rules based solely on the existence of a conflict of interest transaction, as to which subchapter F is preclusive).

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EXHIBIT 5

Chapter 80B
CORPORATE TAKEOVERS

Section
80B.01. Definitions.
80B.02. Repealed.
80B.03. Registration of takeover offers.
80B.04. Filing of solicitation materials.
80B.05. Fraudulent and deceptive practices.
80B.06. Limitations on offerors.
80B.07. Administration, rules and orders.
80B.08. Fees and expenses.
80B.09. Injunctions.
80B.10. Penalties.
80B.11. Civil liabilities.
80B.12. Application of corporate takeover law.
80B.13. Application of securities law.

For complete statutory history see Minnesota Statutes Annotated.

80B.01. Definitions

Subdivision 1. Scope. When used in sections 80B.01 to 80B.13, unless the context otherwise requires, the following words shall have the meanings herein ascribed to them.

Subd. 2. Affiliate. "Affiliate" of a person means any person controlling, controlled by, or under common control with such person.

Subd. 3. Associate. "Associate" of a person means any person acting jointly or in concert with such person for the purpose of acquiring, holding or disposing of, or exercising any voting rights attached to the equity securities of an issuer.

Subd. 4. Commissioner. "Commissioner" means the commissioner of commerce.

Subd. 5. Equity security. "Equity security" means any stock or similar security; or any security convertible, with or without consideration, into such a security; or carrying any warrant or right to subscribe to or purchase such a security; or any such warrant or right; or any other security which the commissioner shall deem to be of similar nature and consider necessary or appropriate, by such rules as the commissioner may prescribe in the public interest and for the protection of investors, to treat as an equity security.

Subd. 6. Offeror. "Offeror" means a person who makes or in any way participates in making a takeover offer. Offeror does not include any bank or broker-dealer loaning funds to an offeror in the ordinary course of its business, or any bank, broker-dealer, attorney, accountant, consultant, employee, or other person furnishing information or advice to or performing ministerial

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duties for an offeror, and not otherwise participating in the takeover offer. When two or more persons act as a partnership, limited partnership, syndicate, or other group pursuant to any agreement, arrangement, relationship, understanding, or otherwise (whether or not in writing) for the purpose of acquiring, owning, or voting securities of a target company, all members of the partnership, syndicate, or other group constitute "a person."

Subd. 7. Offeree. "Offeree" means the beneficial owner, residing in Minnesota, of equity securities which an offeror offers to acquire in connection with a takeover offer.

Subd. 8. Takeover offer. "Takeover offer" means the offer to acquire any equity securities of a target company from a resident of this state pursuant to a tender offer or request or invitation for tenders, if after the acquisition of all securities acquired pursuant to the offer either (1) the offeror would be directly or indirectly a beneficial owner of more than ten percent of any class of the outstanding equity securities of the target company and was directly or indirectly the beneficial owner of less than ten percent of any class of the outstanding equity securities of the target company prior to the commencement of the offer; or (2) the beneficial ownership by the offeror of any class of the outstanding equity securities of the target company would be increased by more than ten percent of that class and the offeror was directly or indirectly the beneficial owner of ten percent or more of any class of the outstanding equity securities of the target company prior to the commencement of the offer. Takeover offer does not include:

(a) an offer in connection with the acquisition of a security which, together with all other acquisitions by the offeror of securities of the same class of equity securities of the issuer, would not result in the offeror having acquired more than two percent of this class during the preceding 12-month period;

(b) an offer by the issuer to acquire its own equity securities unless the offer is made during the pendency of a takeover offer by a person who is not an associate or affiliate of the issuer;

(c) an offer in which the target company is an insurance company subject to regulation by the commissioner, a financial institution regulated by the commissioner, or a public service utility subject to regulation by the public utilities commission.

Subd. 9. Target company. "Target company" means an issuer of publicly traded equity securities (a) which (1) has its principal place of business or its principal executive office located in this state, or (2) owns or controls assets located within this state which have a fair market value of at least $1,000,000, and (b) which (1) has more than ten percent of its beneficial or record equity securityholders resident in this state, (2) has more than ten percent of its equity securities owned beneficially or of record by residents in this state, or (3) has more than 1,000 beneficial or record equity securityholders resident in this state. For the purposes of this chapter, an equity security is publicly traded if a trading market exists for the security at the time the offeror makes a takeover offer for the security. A trading market exists if the security is traded on a

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national securities exchange, whether or not registered pursuant to the Securities Exchange Act of 1934,[1] or the over-the-counter market.

Subd. 10. Beneficial owner. "Beneficial owner" includes, but is not limited to, any person who directly or indirectly through any contract, arrangement, understanding, relationship, or otherwise has or shares the power to vote or direct the voting of a security and/or the power to dispose of, or direct the disposition of, the security. "Beneficial ownership" includes, but is not limited to, the right, exercisable within 60 days, to acquire securities through the exercise of options, warrants, or rights or the conversion of convertible securities, or otherwise. The securities subject to these options, warrants, rights, or conversion privileges held by a person shall be deemed to be outstanding for the purpose of computing the percentage of outstanding securities of the class owned by this person, but shall not be deemed to be outstanding for the purpose of computing the percentage of the class owned by any other person. A person shall be deemed the beneficial owner of securities beneficially owned by any relative or spouse or relative of the spouse residing in the home of this person, any trust or estate in which this person owns ten percent or more of the total beneficial interest or serves as trustee or executor, any corporation or entity in which this person owns ten percent or more of the equity, and any affiliate or associate of this person.

Laws 1973, c. 331, § 1. Amended by Laws 1974, c. 406, §§ 94, 95; Laws 1980, c. 516, § 2; Laws 1984, c. 488, § 2; Laws 1985, 1st Sp., c. 5, §§ 1 to 3; Laws 1986, c. 444; Laws 1987, 1st Sp., c. 1, §§ 1, 2, eff. June 1, 1987.

[1] 15 U.S.C.A. §§ 77b to 77e, 77j, 77k, 77m, 77o, 77s, 78a to 78o, 78o–3, 78p to 78hh.

Historical and Statutory Notes

Laws 1984, c. 488, § 1, provides:

"Subdivision 1. Findings. The legislature finds that take-overs, particularly hostile take-overs:

"(1) exaggerate the tendency of many businesses to focus on short-term performance to the detriment of such long-term societal interests as increased research and development, improved productivity, and the modernization of physical plant and employee capabilities;

"(2) are often inconsistent with the economic interests of shareholders;

"(3) in many instances threaten the jobs and careers of Minnesota citizens and undermine the ethical foundations of companies, as when jobs are eliminated and career commitments to employees are breached or ignored;

"(4) often result in plant closings or consolidations that damage communities dependent on the jobs and taxes provided by these plants;

"(5) not infrequently wipe out long-standing customer/supplier relationships and the stability and continuity which these relationships provide throughout society;

"(6) frequently tie up billions of dollars of scarce capital that could be more effectively applied;

"(7) all too often stifle, and ultimately destroy, the entrepreneurial, innovative spirit of creative individuals in independent firms; and

"(8) are usually conducted in an atmosphere and pursuant to laws that do not provide a reasonable opportunity for affected parties to make informed decisions.

"Subd. 2. Purposes. The purposes of Laws 1984, chapter 488, sections 1 to 18 [amending §§ 80B.01, 80B.03, 80B.05, 80B.06 to 80B.08, 80B.10, 80B.12, 302A.011, 302A.449, 302A.671 and repealing § 80B.02] are to:

"(1) assure that the impacts of take-overs on all affected constituencies are identified and disclosed prior to the consummation of these transactions;

"(2) provide to shareholders both necessary information and the opportunity to thus cast fully informed votes on any take-over transactions;

"(3) encourage reasoned decision-making by assuring equal financial treatment of all share-

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The preceding sentence shall not apply for purposes of determining whether stock in the S corporation is constructively owned by any person.

(b) CROSS REFERENCES.—

For provisions to which the rules contained in subsection (a) apply, see—

(1) section 302 (relating to redemption of stock);

(2) section 304 (relating to redemption by related corporations);

(3) section 306(b)(1)(A) (relating to disposition of section 306stock);

(4) section 338(h)(3) (defining purchase);

(5) section 382(l)(3) (relating to special limitations on net operating loss carryovers);

(6) section 856(d) (relating to definition of rents from real property in the case of real estate investment trusts);

(7) section 958(b) (relating to constructive ownership rules with respect to controlled foreign corporations); and

(8) section 6038(e)(2) (relating to information with respect to certain foreign corporations).

.01 Amended by P.L. 109-135 (clerical amendment), P.L. 105-34 (technical amendment), P.L. 99-514 (conforming amendment), P.L. 98-369, P.L. 97-248 (technical amendment), P.L. 88-554, P.L. 87-834 and P.L. 86-779. For details see the Code Volumes.

.019 Committee Report on P.L. 99-514 (Tax Reform Act of 1986) is at ¶ 17,101.0125.

Committee Report on P.L. 98-369 (Deficit Reduction Act of 1984)

.02 Under present law, in applying attribution of ownership rules under section 318, a partnership is deemed to own proportionately stock owned by the partnership, and the partnership is deemed to own all the stock owned by the partners. In the case of a corporation, attribution to and from shareholders occur[s] only with respect to shareholders owning 50 percent or more in value of the corporation's stock.

The bill provides that the attribution of stock to or from an S corporation and its shareholders would apply in the same manner as if the S corporation (and its shareholders) were a partnership (with partners). Thus, attribution will occur to and from shareholders owning less than 50 percent of the corporation's stock.—**House Committee Report.**

.03 Committee Report on P.L. 88-554 (1964) is at 1964-2 CB 705, 707.

.035 Committee Report on P.L. 87-834 (Revenue Act of 1962) is at 1962-3 CB 405.

.04 Committee Report on P.L. 86-779 (1960) was reproduced at 624 CCH ¶ 4099A.20.

.10 Committee Reports on 1954 Code Sec. 318 as originally enacted were reproduced at 562 CCH ¶ 2388.10.

• *Regulations*

[¶ 15,901] § 1.318-1. **Constructive ownership of stock; introduction.**—(a) For the purposes of certain provisions of chapter 1 of the Code, section 318(a) provides that stock owned by a taxpayer includes stock constructively owned by such taxpayer under the rules set forth in such section. An individual is considered to own the stock owned, directly or indirectly, by or for his spouse (other than a spouse who is legally separated from the individual under a decree of divorce or separate maintenance), and by or for his children, grandchildren, and parents. Under section 318(a)(2) and (3), constructive ownership rules are established for partnerships and partners, estates and beneficiaries, trusts and beneficiaries, and corporations and stockholders. If any person has an option to acquire stock, such stock is considered as owned by such person. The term "option" includes an option to acquire such an option and each of a series of such options.

(b) In applying section 318(a) to determine the stock ownership of any person for any one purpose.—(1) A corporation shall not be considered to own its own stock by reason of section 318(a)(3)(C);

(2) In any case in which an amount of stock owned by any person may be included in the computation more than one time, such stock shall be included only once, in the manner in which it will impute to the person concerned the largest total stock ownership; and

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(3) In determining the 50-percent requirement of section 318(a)(2)(C) and (3)(C) all of the stock owned actually and constructively by the person concerned shall be aggregated. [Reg. § 1.318-1.]

.01 **Historical Comment:** Proposed 12/11/54. Adopted 12/2/55 by T.D. 6152. Amended 4/25/62 by T.D. 6598, 11/30/62 by T.D. 6621, and 8/22/68 by T.D. 6969.

• ***Regulations***

Caution: Reg. §1.318-2 does not reflect recent law changes. For details, see ¶15,902.01.

[¶15,902] § 1.318-2. **Application of general rules.**—(a) The application of paragraph (b) of § 1.318-1 may be illustrated by the following examples:

Example (1). H, an individual owns all of the stock of Corporation A. Corporation A is not considered to own the stock owned by H in Corporation A.

Example (2). H, an individual, his wife, W, and his son, S, each own one-third of the stock of the Green Corporation. For purposes of determining the amount of stock owned by H, W, or S for the purpose of section 318(a)(2)(C) and (3)(C), the amount of stock held by the other members of the family shall be added pursuant to paragraph (b)(3) of § 1.318-1 in applying the 50-percent requirement of such section. H, W, or S, as the case may be, is for this purpose deemed to own 100 percent of the stock of the Green Corporation.

(b) The application of section 318(a)(1), relating to members of a family, may be illustrated by the following example:

Example. An individual, H, his wife, W, his son, S, and his grandson (S's son), G, own the 100 outstanding shares of stock of a corporation, each owning 25 shares. H, W, and S are each considered as owning 100 shares. G is considered as owning only 50 shares, that is, his own and his father's.

(c) The application of section 318(a)(2) and (3), relating to partnerships, trusts and corporations, may be illustrated by the following examples:

Example (1). A, an individual, has a 50 percent interest in a partnership. The partnership owns 50 of the 100 outstanding shares of stock of a corporation, the remaining 50 shares being owned by A. The partnership is considered as owning 100 shares. A is considered as owning 75 shares.

Example (2). A testamentary trust owns 25 of the outstanding 100 shares of stock of a corporation. A, an individual, who holds a vested remainder in the trust having a value, computed actuarially equal to 4 percent of the value of the trust property, owns the remaining 75 shares. Since the interest of A in the trust is a vested interest rather than a contingent interest (whether or not remote), the trust is considered as owning 100 shares. A is considered as owning 76 shares.

Example (3). The facts are the same as in (2), above, except that A's interest in the trust is a contingent remainder. A is considered as owning 76 shares. However, since A's interest in the trust is a remote contingent interest, the trust is not considered as owning any of the shares owned by A.

Example (4). A and B, unrelated individuals, own 70 percent and 30 percent, respectively, in value of the stock of Corporation M. Corporation M owns 50 of the 100 outstanding shares of stock of Corporation O, the remaining 50 shares being owned by A. Corporation M is considered as owning 100 shares of Corporation O, and A is considered as owning 85 shares.

Example (5). A and B, unrelated individuals, own 70 percent and 30 percent, respectively, of the stock of corporation M. A, B, and corporation M all own stock of corporation O. Since B owns less than 50 percent in value of the stock of corporation M, neither B nor corporation M constructively owns the stock of corporation O owned by the other. However, for purposes of certain sections of the Code, such as sections 304 and 856(d), the 50-percent limitation of section 318(a)(2)(C) and (3)(C) is disregarded or is

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Caution: Reg. §1.318-2 does not reflect recent law changes: For details, see ¶15,902.01.

reduced to less than 30 percent. For such purposes, B constructively owns his proportionate share of the stock of corporation O owned directly by corporation M, and corporation M constructively owns the stock of corporation O owned by B. [Reg. §1.318-2.]

.01 **Historical Comment:** Proposed 12/11/54. Adopted 12/2/55 by T.D. 6152. Amended 8/22/68 by T.D. 6969. [Reg. §1.318-2 does not reflect P.L. 98-369 (1984). See ¶15,900.02 and ¶15,906.035.]

Regulations

[¶15,903] §1.318-3. **Estates, trusts, and options.**—(a) For the purpose of applying section 318(a), relating to estates, property of a decedent shall be considered as owned by his estate if such property is subject to administration by the executor or administrator for the purpose of paying claims against the estate and expenses of administration notwithstanding that, under local law, legal title to such property vests in the decedent's heirs, legatees or devisees immediately upon death. The term "beneficiary" includes any person entitled to receive property of a decedent pursuant to a will or pursuant to laws of descent and distribution. A person shall no longer be considered a beneficiary of an estate when all the property to which he is entitled has been received by him, when he no longer has a claim against the estate arising out of having been a beneficiary, and when there is only a remote possibility that it will be necessary for the estate to seek the return of property or to seek payment from him by contribution or otherwise to satisfy claims against the estate or expenses of administration. When, pursuant to the preceding sentence, a person ceases to be a beneficiary, stock owned by him shall not thereafter be considered owned by the estate, and stock owned by the estate shall not thereafter be considered owned by him. The application of section 318(a) relating to estates may be illustrated by the following examples:

Example (1). (a) A decedent's estate owns 50 of the 100 outstanding shares of stock of corporation X. The remaining shares are owned by three unrelated individuals, A, B, and C, who together own the entire interest in the estate. A owns 12 shares of stock of corporation X directly and is entitled to 50 percent of the estate. B owns 18 shares directly and has a life estate in the remaining 50 percent of the estate. C owns 20 shares directly and also owns the remainder interest after B's life estate.

(b) If section 318(a)(5)(C) applies (see paragraph (c)(3) of §1.318-4), the stock of corporation X is considered to be owned as follows: the estate is considered as owning 80 shares, 50 shares directly, 12 shares constructively through A, and 18 shares constructively through B; A is considered as owning 37 shares, 12 shares directly, and 25 shares constructively (50 percent of the 50 shares owned directly by the estate); B is considered as owning 43 shares, 18 shares directly and 25 shares constructively (50 percent of the 50 shares owned directly by the estate); C is considered as owning 20 shares directly and no shares constructively. C is not considered a beneficiary of the estate under section 318(a) since he has no direct present interest in the property held by the estate nor in the income produced by such property.

(c) If section 318(a)(5)(C) does not apply, A is considered as owning nine additional shares (50 percent of the 18 shares owned constuctively by the estate through B), and B is considered as owning six additional shares (50 percent of the 12 shares owned constructively by the estate through A).

Example (2). Under the will of A, Blackacre is left to B for life, remainder to C, an unrelated individual. The residue of the estate consisting of stock of a corporation is left to D. B and D are beneficiaries of the estate under section 318(a). C is not considered a beneficiary since he has no direct present interest in Blackacre nor in the income produced by such property. The stock owned by the estate is considered as owned proportionately by B and D.

(b) For the purpose of section 318(a)(2)(B) stock owned by a trust will be considered as being owned by its beneficiaries only to the extent of the interest of such

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beneficiaries in the trust. Accordingly, the interest of income beneficiaries, remainder beneficiaries, and other beneficiaries will be computed on an actuarial basis. Thus, if a trust owns 100 percent of the stock of Corporation A, and if, on an actuarial basis, W's life interest in the trust is 15 percent, Y's life interest is 25 percent, and Z's remainder interest is 60 percent, under this provision W will be considered to be the owner of 15 percent of the stock of Corporation A, Y will be considered to be the owner of 25 percent of such stock, and Z will be considered to be the owner of 60 percent of such stock. The factors and methods prescribed in §20.2031-7 of this chapter (Estate Tax Regulations) for use in ascertaining the value of an interest in property for estate tax purposes shall be used in determining a beneficiary's actuarial interest in a trust for purposes of this section. See §20.2031-7 of this chapter (Estate Tax Regulations) for examples illustrating the use of these factors and methods. [Reg. §20.2031-7 of this chapter is reproduced at ¶15,904.—CCH.]

(c) The application of section 318(a) relating to options may be illustrated by the following example:

Example. A and B, unrelated individuals, own all of the 100 outstanding shares of stock of a corporation, each owning 50 shares. A has an option to acquire 25 of B's shares and has an option to acquire a further option to acquire the remaining 25 of B's shares. A is considered as owning the entire 100 shares of stock of the corporation. [Reg. §1.318-3.]

.01 **Historical Comment:** Proposed 12/11/54. Adopted 12/2/55 by T.D. 6152. Amended 5/5/60 by T.D. 6462 and 8/22/68 by T.D. 6969.

• *Estate Tax Regulations*

Note: Reg. §20.2031-7, below, and Reg. §20.2031-7A, below, are estate tax Regulations, reproduced here in connection with the references in income tax Reg. §1.318-3(b), above.

[¶15,904] §20.2031-7. **Valuation of annuities, interests for life or term of years, and remainder or reversionary interests.**—(a) *In general.*—Except as otherwise provided in paragraph (b) of this section and §20.7520-3(b) (pertaining to certain limitations on the use of prescribed tables), the fair market value of annuities, life estates, terms of years, remainders, and reversionary interests for estates of decedents is the present value of such interests, determined under paragraph (d) of this section. The regulations in this and in related sections provide tables with standard actuarial factors and examples that illustrate how to use the tables to compute the present value of ordinary annuity, life, and remainder interests in property. These sections also refer to standard and special actuarial factors that may be necessary to compute the present value of similar interests in more unusual fact situations.

(b) *Commercial annuities and insurance contracts.*—The value of annuities issued by companies regularly engaged in their sale, and of insurance policies on the lives of persons other than the decedent, is determined under §20.2031-8. See §20.2042-1 with respect to insurance policies on the decedent's life.

(c) *Actuarial valuations.*—The present value of annuities, life estates, terms of years, remainders, and reversions for estates of decedents for which the valuation date of the gross estate is after April 30, 1999, is determined under paragraph (d) of this section. The present value of annuities, life estates, terms of years, remainders, and reversions for estates of decedents for which the valuation date of the gross estate is before May 1, 1999, is determined under the following sections:

Valuation Dates		
After	*Before*	*Applicable Regulations*
	01-01-52	20.2031-7A(a)
12-31-51	01-01-71	20.2031-7A(b)

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P.O. Box 326 Lewisberry, PA 17339
www.fleoa.org
(717) 938-2300

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June 7th, 2009

The Honorable Joseph I. Lieberman
Chairman, Senate Homeland Security and Governmental Affairs Committee
Washington, D.C. 20510

The Honorable Susan M. Collins
Ranking Member, Senate Homeland Security and Governmental Affairs Committee
Washington, D.C. 20510

Dear Chair Lieberman and Ranking Member Collins:

On behalf of the 26,000 members of the Federal Law Enforcement Officers Association (FLEOA), I am memorializing our support for Senate Bill 569. The proposed legislation is very important to our ICE, FBI and IRS members as they are the lead agencies that investigate money laundering and terrorist financing cases.

While criminals cower behind the anonymity of their corporate filings, they continue to exploit this system as a means to commit terrorist financing and money laundering. Using a registered agent or attorney as the "front-person" for their company, terrorists/criminals are able to circumvent law enforcement and accomplish the following:

1. Use shell company bank accounts to launder millions of dollars;
2. Use shell companies to attempt to acquire a significant ownership interest in a financial institution;
3. Purchase real property through their shell companies to be used as stash houses to stockpile drugs or weapons/explosives;
4. Operate money remitter businesses to move their illegal proceeds to off-shore accounts;
5. Engage in cyber-terrorism attacks by disseminating contaminated emails from ostensibly legitimate companies.

Law enforcement's ability to investigate and enforce the provisions of the Bank Secrecy Act has been impeded by terrorists/criminals who hide behind the corporate veil. This costs law enforcement agencies a substantial amount of time and money, i.e., long-term surveillance and subpoena service on numerous third parties, and allows the terrorist and/or criminal to remain "ten-steps" ahead. FLEOA maintains that the identity of the real beneficial owners should be made available to law enforcement officers who make legally authorized requests pursuant to official investigations.

While our membership respects the spirit of free enterprise in our country, we do not want to see the United States adopt the financial safe-haven image of Switzerland. If our country's laws require individuals to register vehicle or firearm ownership, the same should apply to corporate filers. The consequences for allowing terrorists and/or criminals to exploit our corporate filing system are severe. In the spirit of homeland security and protecting our great nation, we cannot permit this to continue.

We hope your committee will embrace the importance of S. 569, and work together to move it forward for consideration before the full senate. Please don't hesitate to call should you require additional input or testimony from our membership.

Respectfully submitted,

J. Adler

J. Adler
National President

National Association of Assistant United States Attorneys
12427 Hedges Run Dr. • Ste 104 • Lake Ridge, VA 22192-1715
Tel: (800) 455-5661 • Fax: (800) 528-3492
Web: www.naausa.org

October 2, 2008

The Honorable Carl Levin
Chairman
Permanent Subcommittee on Investigations
Committee on Homeland Security
and Governmental Affairs
Washington, DC 20510

The Honorable Norm Coleman
Ranking Member
Permanent Subcommittee on Investigations
Committee on Homeland Security
and Governmental Affairs
Washington, DC 20510

Re: S. 2956, The Incorporation Transparency and Law Enforcement Assistance Act

Dear Chairman Levin and Ranking Member Coleman:

I write to extend the strong support of the National Association of Assistant United States Attorneys for S. 2956, The Incorporation Transparency and Law Enforcement Assistance Act, and to thank you for your leadership in introducing this necessary legislation.

Your measure will require States to obtain the names of the beneficial owners of each corporation or limited liability company formed under their laws, ensure that this information is annually updated, and make such information available to law enforcement authorities when legally authorized. Mindful of the ease with which criminals establish "front organizations' to assist in money laundering, terrorist financing, tax evasion and other misconduct, it is shocking and unacceptable that many State laws permit the creation of corporations without asking for the identity of the corporation's beneficial owners. Your legislation will guard against that from happening, and no longer permit criminals to exploit the lack of transparency in the registration of corporations.

Your bill will create a critical information gathering tool by giving law enforcement authorities access to the true identity of the owners behind certain corporations suspected of criminal acts, without unduly intruding upon individual privacy.

On behalf of the Assistant United States Attorneys represented by our association, I applaud your continued dedication to the pursuit of justice through the introduction of this important legislation. If I can be of any additional help on this matter, please do not hesitate to contact me or our Washington counsel Bruce Moyer.

Sincerely,

Richard L. Delonis

Richard Delonis
National President

President: Richard L. Delonis, ED of Michigan
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UNITED STATES MARSHALS SERVICE ASSOCIATION

2654 W. Horizon Ridge Pkwy, B-5, — PMB 110
Henderson, NV 89052

August 27, 2008

The Honorable Carl Levin
Chairman
The Honorable Norm Coleman
Ranking Member
Permanent Subcommittee on Investigations
Senate Committee on Homeland Security and Government Affairs
340 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Levin and Ranking Member Coleman:

On behalf of the membership of the United States Marshals Service Association, I am writing to offer support for S 2956, The Incorporation Transparency and Law Enforcement Assistance Act.

The necessity to identify contacts for the formation of corporations and LLC's is a must to eliminate criminal gain. Law Enforcement must have every tool available to combat terrorism, money laundering and other misconduct that prevails with non-disclosure. This single requirement will greatly enhance the efforts of law enforcement.

Making these requirements mandatory will not violate the privacy of legitimate businesses but will prevent criminal activity in forming "shell companies" to advance illegal enterprises.

The United States Marshals Service Association stands strong behind this legislation and appreciates all your efforts.

Sincerely,

Marvin Lutes
President

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JAMES O. PASCO, JR.
EXECUTIVE DIRECTOR

25 August 2008

08 SEP -5 AM 9:14

The Honorable Carl Levin
Chairman
Permanent Subcommittee on Investigations
Committee on Homeland Security and Governmental Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman,

I am writing on behalf of the members of the Fraternal Order of Police to advise you of our support for your bill, S. 2956, the "Incorporation Transparency and Law Enforcement Assistance Act." This bill is a critical step in cracking corporate secrecy that sometimes exists to act as a cover for illegal enterprises.

The bill would help law enforcement combat the misuse of U.S. corporations by requiring States to obtain beneficial ownership information for corporations and limited liability companies (LLCs) formed under State law. The bill would do this by providing law enforcement access to this information upon receipt of a subpoena or summons.

For years corporations have been used as front organizations for criminals in the conduct of illegal activity such as money laundering, fraud and tax evasion. Your legislation would act as a critical information gathering tool for law enforcement in combating these crimes by giving law enforcement access to the true identity of the owners behind certain corporations suspected of criminal acts.

On behalf of the more than 325,000 members of the FOP, I thank you for your continuing leadership on homeland security and law enforcement issues. If I can be of any additional help on this matter, please do not hesitate to contact me or Executive Jim Pasco in my Washington office.

Sincerely,

Chuck Canterbury
National President

—BUILDING ON A PROUD TRADITION—

NATIONAL NARCOTIC OFFICERS' ASSOCIATIONS COALITION

P.O. Box 2456 West Covina, California 91793-2456 • (626) 960-3328 • Fax (626) 960-3328

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Wisconsin Narcotic Officers' Assn

August 4, 2008

The Honorable Carl Levin
Chairman
The Honorable Norm Coleman
Ranking Member
Permanent Subcommittee on Investigations
Senate Committee on Homeland Security and Government Affairs
340 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Levin and Ranking Member Coleman:

On behalf of the National Narcotic Officers' Associations' Coalition (NNOAC) and the more than 70,000 law enforcement officers we represent, I'm pleased to offer my full support for S. 2956, The Incorporation Transparency and Law Enforcement Assistance Act.

This bill would require states to log basic contact information - a name and a mailing address - for persons who apply to form a corporation or an LLC. Currently, when individuals form corporations and LLC's, they do not need to provide any significant information about the identity of the beneficial owner. As a result, criminals are able to conceal their identities and commit crimes - such as drug trafficking and money laundering - through these corporations and LLC's without punishment.

Mandating a name and a mailing address in order to form a new corporation or LLC is the most basic of requirements. Requiring this information does not violate the privacy concerns of legitimate businesses and is sound policy for preventing criminal organizations and drug trafficking enterprises from forming "shell companies" to legitimize illegal activity. While this bill provides funding flexibility by allowing states to use homeland security grant funding to offset costs associated with this rule change, the NNOAC believes that the funding for this effort should come from somewhere other than public safety - whose budgets remain woefully underfunded.

The NNOAC applauds S. 2956 and appreciates your continued dedication to helping state and local law enforcement tackle the tough challenges we face every day.

Sincerely,

Ronald E. Brooks
President

Association of Former ATF Agents

To: Selected Members of Congress 9/12/08
From: Dick Goodson
Re: S.2956

Senators Levin, Coleman, and Obama introduced Senate File 2956 on May 1. The purpose of the legislation is to require states to obtain additional information on corporations formed under their laws and to provide access to the information to law enforcement agencies upon receipt of a subpoena or summons.

Senator Levin stated "Criminals are hiding behind U.S. corporations while committing all sorts of crimes – from terrorism to money laundering, fraud, and tax evasion." Senator Coleman was quoted as saying "Criminal activities that exploit the lack of transparency in U.S. corporate regulations are more costly than ever."

The purpose of the bill is to shed light on these illegal activities and provide additional tools to law enforcement, while still protecting individual privacy. AFATFA applauds such an approach as outlined in the bill and is especially pleased that a bi-partisan approach is being taken on such an important issue. We urge your support of S.2956.

Sincerely,

Dick Goodson
Executive Director
Association of Former ATF Agents

525 SW 5th Street, Suite A • Des Moines, IA 50309
Phone: 515-282-8192 • Fax: 515-282-9117
Email: afatfa@assoc-mgmt.com • Web: www.afatfa.org

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SOCIETY OF FORMER SPECIAL AGENTS OF THE FEDERAL BUREAU OF INVESTIGATION, INC.

March 13, 2009

The Honorable Carl Levin, Chairman
Permanent Subcommittee on Investigations
Senate Committee on Homeland Security &
Government Affairs
340 Dirksen Senate Office Building
Washington, D. C. 20510

Re: The Incorporation Transparency and Law Enforcement Assistance Act

Dear Chairman Levin:

Enactment of captioned Bill will regulate shell companies by mandating states follow consistent and equally applied regulations, so these companies must identify by name and address the corporate principles. In this way, criminals and potential terrorists cannot use the current loopholes to avoid detection thus facilitating their unlawful activities.

According to FinCEN (Financial Crimes Enforcement Network), the term "shell company" refers to non-publicly traded corporations, limited liability companies and trusts that typically have no physical presence (other than a mailing address) and generate little to no independent economic value. In April 2006, the Government Accounting Office (GAO) published a report on company formations, which cited the proliferation of shell company formations and the critical lack of ownership information and transparency. In November 2006, FinCEN issued guidance about the potential money laundering risks related to shell companies, as follows:

- Every state has statutes governing the organization and operation of business entities, to include shell companies. The requirements differ from state to state causing the lack of uniformity
- According to the GAO report, states form nearly 2 million new corporations and LLCs in 2004, absent any knowledge about the principals or ownership of those corporations. Ownership anonymity and lack of transparency has been the source of exploitation by criminals, money launders and terrorists financiers
- States generate considerable revenue from the formation of new companies especially through the use of the Internet
- A number of states do not believe or have an understanding of the problem, which results in a lack of consensus among members of Congress

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The FBI has been involved in several matters illustrating the seriousness of this situation. In circa 1998, Agents in North Carolina initiated "Operation Smokescreen," in which Hezbollah was smuggling cigarettes for the purpose of financing their terrorist activities. A shell company was used to facilitate the transfer of illicitly obtained cash from the scheme. In another case, Shawqui Omar, who was a lieutenant to Abu Musab al-Zarqawi, was arrested in Iraq in 2004. Subsequently, five of Omar's relatives were indicted and arrested in 2006, for perpetrating a series of bank frauds and money laundering schemes. Proceeds from the frauds were laundered from the United States to Jordan. It has been alleged the funds were withdrawn in cash and then couriered to Omar in Iraq.

These cases are troubling and suggest significant systematic vulnerability to the financial system in the United States. By virtue of offering ownership anonymity and lacking transparency, shell companies afford criminals, money launders and terrorists financiers a mechanism to exploit the financial system and operate with impunity.

Superficially, the solution to the problem would appear to be relatively simple. Identify and implement mechanisms requiring identification of the beneficial owners of shell companies. Ownership identification would enable financial institutions to perform adequate "know your customer due diligent inquiries." This process would seriously minimize the risk caused by shell companies. However, the lack of consistency and consensus among states makes solving this problem quite challenging. Money launders pose a threat to the economy, while terrorists pose a threat to national security.

While the currently proposed act is a start, it is woefully inadequate to address the crux of the problem. There must be uniform regulations equally applied in all states requiring transparency and specific ownership information, as well as enforcement provisions in the act. While this matter continues to be debated in Congress, criminals and terrorists continue to benefit from huge sums of cash resulting from gaping holes in federal regulations.

While the Society endorses the currently proposed Bill, it would prefer Congress strengthen the proposed law, despite the apparent lack of support from the states. If Congress decides to hold additional hearings on this matter, the Society can afford the Committee with former special agents, who could provide probative testimony.

Please contact the Society's National Office at the numbers below if the Society can be of any assistance in this matter.

Very truly yours,

Johnie L. Joyce
President

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United States Senate

COMMITTEE ON
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
WASHINGTON, DC 20510-6250

November 13, 2007

VIA U.S. MAIL AND EMAIL (Reynolds@sso.org)

The Honorable Elaine Marshall
North Carolina Secretary of State
NASS Company Formation Task Force Co-Chair

The Honorable John Gale
Nebraska Secretary of State
NASS Company Formation Task Force Co-Chair
Hall of States
444 N. Capitol Street, N.W., Suite 401
Washington, DC 20001

Dear Secretaries Marshall and Gale:

Thank you for your September letter regarding the Task Force's plans to address concerns related to the state formation of U.S. companies whose owners are unidentified.

As you know, the U.S. Senate Permanent Subcommittee on Investigations, as well as a number of federal law enforcement agencies, have a long-standing concern about the failure of the states to collect, update, and maintain beneficial ownership information for the legal entities they form, such as corporations and limited liability companies. Under current practice, states are forming nearly 2 million companies each year without knowing who is behind them.

In November 2000, at the request of the Subcommittee, the Government Accountability Office (GAO) conducted an investigation and released a report entitled, *Suspicious Banking Activities: Possible Money Laundering by U.S. Corporations Formed for Russian Entities.* This report revealed, among other information, that a Russian immigrant living in the United States was able to set up more than 2,000 Delaware shell corporations and, without disclosing the identity of the beneficial owners, open bank accounts for those corporations, which then collectively moved about $1.4 billion through the accounts. In April 2006, again at the Subcommittee's request, GAO released a report entitled, *Company Formations: Minimal Ownership Information Is Collected and Available*, which reviewed the formation laws in all 50 states. GAO reported that most states do not collect any information on the beneficial owners of the legal entities they establish. Both GAO reports also discuss the problems for law enforcement caused by this lack of beneficial ownership information.

On November 14, 2006, the Subcommittee held a hearing on these matters. At the hearing, representatives of the U.S. Department of Justice, the Internal Revenue Service, and the Department of Treasury's Financial Crimes Enforcement Network (FinCEN) all testified that the failure of the states to collect adequate information on the beneficial owners of the legal entities they form had impeded federal efforts to investigate and prosecute criminal acts such as money laundering, securities fraud and tax evasion. For example:

> The Department of Justice testified: "We had allegations of corrupt foreign officials using these [U.S.] shell accounts to launder money, but were unable – due to lack of identifying information in the corporate records – to fully investigate this area."
>
> The IRS testified: "Within our own borders, the laws of some states regarding the formation of legal entities have significant transparency gaps which may even rival the secrecy afforded in the most attractive tax havens."
>
> FinCEN identified 768 incidents of suspicious international wire transfer activity involving U.S. shell companies.

In addition, the Financial Action Task Force (FATF), the leading international organization combating money laundering and terrorist financing, submitted a written statement to the Subcommittee in which it described its recent review of U.S. anti-money laundering and anti-terrorist financing programs and found that the United States was not in compliance with a key FATF standard requiring jurisdictions to obtain beneficial ownership information for the legal entities they form. The United States apparently has until June 2008 to come into compliance with that standard or risk being removed from this important international organization.

Representatives of three states, Delaware, Nevada, and Massachusetts, also testified at the Subcommittee hearing and responded to questions about shell companies abusing their state status to commit crimes involving money laundering, tax evasion, and other misconduct. Each of the states described a different approach to collecting ownership information. The testimony and evidence at the hearing reinforces concern about the ability of individual states to tackle the ownership issue, given that each is competing against the other states for formation fees, is under pressure to form new entities quickly and cheaply, and if one state were to strengthen its disclosure requirements, applicants could simply turn to other states for their formation needs. As I indicated at the hearing, if the states were unwilling to act quickly to strengthen their formation procedures, federal action might be necessary to set minimum standards for the collection of beneficial ownership information, to ensure adequate assistance to law enforcement investigations of U.S. shell companies, and help the United States meet its obligation to come into compliance with FATF guidelines by June 2008.

At the request of the states, I delayed introducing federal legislation to provide the states with an opportunity to craft a solution. Throughout the states' deliberations leading up to the NASS Report, Subcommittee staff participated in conferences and meetings, suggested key principles, and provided comments on draft Task Force proposals. Unfortunately, the final Task Force Recommendations contained in your letter do not reflect my concerns, lack a number of key elements, and propose an unsatisfactory timetable for state action.

In my view, the Recommendations should satisfy the following five key principles:

1. **Identification of the natural individuals who will beneficially own the entity being formed.** The most important objective in this matter is a requirement that the states collect the names of the individuals who will be the true owners of the legal entities that the states are being asked to form. The NASS proposal as currently drafted, however, calls only for the compilation of a "list of owners of record." This approach is wholly inadequate, since it is common practice for those who want to hide the real owners to name as the "owner of record" an attorney, corporate nominee, trust, or third party with no true ownership interest in or ability to control the entity being formed. The proposal also fails to require the list to name natural individuals, rather than legal entities. In contrast to this proposal, I believe that, to ensure adequate assistance to law enforcement investigations of U.S. shell companies suspected of wrongdoing and to ensure U.S. compliance with the FATF disclosure standard, the states must obtain identification of the natural individuals who will beneficially own the entities being formed.

2. **Annual information updates.** The NASS proposal also fails to recommend that ownership information be updated on a regular basis, instead advising states only to "examine their statutes and other requirements for annual or biennial reporting." Without a requirement for updated information, unscrupulous operators can list a set of beneficial owners on a company's initial formation documents and immediately transfer the company to new owners not named in the state records. Most states already require companies to file annual updates of their corporate records and pay annual fees. To assist law enforcement and meet the FATF standard, the states should also require the entities they form to update a list of their beneficial owners on at least an annual basis.

3. **Reliable access to ownership information.** In addition to collecting updated beneficial ownership information for the entities they form, the states must be able to provide this information to law enforcement in a reasonable amount of time after a request. The NASS proposal, however, does not contain that type of clear requirement. Instead it recommends that the states simply maintain the "name and address of a natural person in the United States" responsible for providing access to an entity's owners of record. This approach is, again, wholly inadequate. First, the proposal does not specify that the person have any relationship to the entity at issue.

Second, it does not require the person to reside in the state that formed the entity or to agree to be subject to that state's regulation. There is no requirement that the person maintain the names of the beneficial owner. Finally, the proposal does not specify that the information be furnished to law enforcement within a reasonable period of time upon request. In contrast to this flawed approach, a better recommendation would be for the state itself to retain the ownership information or, at a minimum, to require the information to be maintained by a state resident who is subject to state regulation, whose identity and address are updated annually, and who agrees to promptly supply the information to law enforcement upon request.

4. **Adequate record retention.** Beneficial ownership information should not only be collected and made accessible to law enforcement, it should be maintained for a reasonable period of time. The NASS proposal is silent on how long ownership records must be maintained. I believe that beneficial ownership records should be maintained not only during the period in which the entity is registered, but also for a minimum period after that registration expires. Since it is common for problems to surface after an entity's registration has lapsed, unless there is a requirement for adequate record retention, it will often be impossible for law enforcement to secure needed ownership information for an entity no longer in operation.

5. **Timely implementation of reforms.** Finally, there is the proposed timetable for state implementation. The NASS proposal suggests that the National Conference of Commissioners on Uniform State Laws complete a model statute by July 2008. States would then be responsible for enacting implementing legislation. This proposed timetable makes it impossible for the United States to meet the FATF deadline of June 2008.

I am disappointed that the states, despite the passage of nearly one year, have been unable to devise a better proposal to meet the needs of law enforcement and the U.S. obligation to comply with the FATF standard regarding beneficial ownership information. Given the many deficiencies in the NASS proposal, I am planning to introduce federal legislation setting minimum standards for beneficial ownership disclosure, create a level playing field among the states, and put an end to the practice of states creating millions of legal entities each year without knowing who is behind them.

Sincerely,

Carl Levin

Carl Levin
Chairman
Permanent Subcommittee on Investigations

cc: The Honorable Norm Coleman
Ranking Minority Member
Permanent Subcommittee on Investigations

Congress of the United States
Washington, DC 20510

February 27, 2007

The Honorable Janet Napolitano
NGA Chair
National Governors Association
444 N. Capitol St., Suite 267,
Washington, D.C. 20001-1512

Dear Governor Napolitano:

As the Governors assemble for their winter meeting in Washington, we write to urge the Governors to work with law enforcement and Congress to address a serious problem that impacts every state, facilitates crime, undermines our national security, and requires state action to address. The central problem is that the 50 states are currently forming nearly 2 million companies in the United States each year with little to no information about who is behind those companies. While the vast majority of those companies operate legitimately, a small percentage do not, functioning instead as conduits for organized crime, money laundering, terrorist financing, securities fraud, tax evasion, and other misconduct.

Four recent reports describe the many security risks created by the lack of transparency in the company formation processes of many states. These reports paint a vivid picture of the ease with which rogue U.S. companies may exploit lax ownership disclosure requirements to anonymously engage in domestic and international criminal activity. Moreover, these reports identify numerous difficulties faced by U.S. law enforcement in identifying the beneficial owners of these companies and preventing and prosecuting this criminal activity. The four reports are:

- *U.S. Money Laundering Threat Assessment,* a joint report issued in December 2005 by the Departments of Justice, Treasury, Homeland Security, and others, which includes a chapter on the law enforcement problems caused by anonymously-owned U.S. shell companies and trusts;

- *Company Formations: Minimal Ownership Information Is Collected and Available*, an April 2006 report issued by the Government Accountability Office that reviewed the laws of all 50 states, determined that most states have no information on the true owners of the companies being set up within their borders and described a variety of related law enforcement concerns;

- *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: United States of America*, a

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June 2006 report issued by the Financial Action Task Force (FATF), which found that the United States was not in compliance with a FATF standard requiring states to obtain beneficial ownership information for the companies they form and set a two-year deadline for the United States to meet its commitment to comply with FATF standards; and

- *The Role of Domestic Shell Companies in Financial Crime and Money Laundering: Limited Liability Companies,* a November 2006 report issued by the Department of Treasury's Financial Crimes Enforcement Network that described the problems encountered by law enforcement when dealing with limited liability companies with unknown owners.

In addition, two recent articles from USA Today and Forbes, copies attached, describe the current loopholes in some state laws and illustrate some of the serious problems confronting law enforcement as a result of the states' minimal company ownership information requirements.

It is important for the states to recognize and act on this important issue as soon as possible, in light of the United States' obligation to act within FATF's two-year framework. To that end, we have introduced legislation that would require company formation agents to know their clients before forming companies on their behalf and protect the U.S. financial system against money launderers and terrorist financing, by directing Treasury to include company formation agents in anti-money laundering regulations. We hope that you will support this legislation and encourage states to make this issue a priority. We would also appreciate your views on whether a federal standard in this area would help create a level playing field and ensure that no state obtained a competitive advantage by failing to obtain needed ownership information.

Thank you for your help in this matter. Should you or your staff have additional concerns or questions, please have your staff contact Laura Stuber in Senator Levin's office at 202/224-9579; Ian Solomon in Senator Obama's office at 202/224-2854; or Al Fitzpayne in Congressman Emanuel's office at 202/226-7644.

Sincerely,

Rahm Emanuel

Barack Obama

Carl Levin

Attachments

USA Today article
http://www.usatoday.com/money/companies/regulation/2007-02-23-tax-havens-usat_x.htm

Corporate owners hide assets, identities

Updated 2/23/2007 8:43 AM ET
By Kevin McCoy, USA TODAY

Roughly four miles from the famed Las Vegas casino strip, ABC Equity's corporate office is registered in a modest business suite located off West Sahara Avenue.

Great Fortune 600 is registered in the same suite. So are DK Financial, Hill 99, Stock Savant, ZZYZX Holdings — and more than 1,000 other corporations.

They share something in common besides their business address. Each lists the same man as its sole corporate officer in Nevada incorporation records. He is William Reed, a businessman with a suspended law license and the target of a Federal Trade Commission lawsuit that alleges he and a convicted felon teamed in a business that promoted forming Nevada corporations to shield assets "from 'capricious federal judges and any government agency.' "

BACKGROUND: Got $95 and 5 minutes? That's about all it takes

A USA TODAY computer-aided review shows that the two men and their business, Asset Protection Group, are part of a thriving mini-industry that has capitalized on real or perceived gaps in domestic incorporation laws and virtually non-existent government oversight to promote some U.S. states as secrecy rivals of offshore havens.

A multi-agency U.S. Money Laundering Threat Assessment issued in 2005 cited Nevada, Wyoming and Delaware as the states with laws most conducive to anonymous corporate ownership. USA TODAY's review, which examined databases of all Nevada and Wyoming incorporations but was unable to obtain comprehensive data for Delaware, found:

•A Florida man who served a federal prison term for an international currency trading scam used his secret ownership of a Nevada corporation to launch a similar fraud after he was released. More than 120 victims lost $8 million.

•Interpol or other international investigators probing suspected crimes overseas have contacted the Wyoming Secretary of State's office about corporations registered by a businessman whose Internet-based venture advertised using Wyoming firms to shield assets.

•The sole publicly listed officer for nearly 100 firms incorporated in Wyoming is a woman whose listed address is a postal box in the Republic of Seychelles, an Indian Ocean nation that has been the focus of corporate secrecy concerns.

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USA TODAY's findings buttressed the money laundering report's warning that a "race to the bottom" among states vying to set minimal corporate information requirements has enabled companies to hide the identities of their owners, thereby making it harder for law enforcement agencies to track suspected tax evasion, money laundering and other crimes.

Law enforcement agency concerns

"The purpose of corporations originally was to provide limited liability, not anonymity," said Sen. Carl Levin, D-Mich., chairman of the Senate Permanent Subcommittee on Investigations, which held a recent hearing on the issue. "Now they're providing both limited liability and anonymity, and the law enforcement folks … are very upset. They want to know who it is that's behind these corporations."

Concern about camouflaged corporate ownership prompted the IRS to list the tactic this week in its 2007 "Dirty Dozen" tax scams. The IRS said anonymous entities are facilitating "underreporting of income, non-filing of tax returns … money laundering, financial crimes and possibly terrorist financing."

Most states don't require companies to provide ownership information when they incorporate. And they exercise virtually no oversight on the corporations' internal operations. In part, that's because most corporations operate legally, generate new jobs and fuel economic expansion, plus registration fees.

Nevada and Wyoming officials said their laws encourage legitimate businesses with reasonable registration requirements. "The law isn't unscrupulous. It's the individuals that use it in an improper manner," said Tom Cowan, head of the securities division in the Wyoming Secretary of State's office.

But law enforcement officials say relaxed state requirements let the mini-industry facilitate formation of shell companies that have no employees, exist chiefly on paper, yet conduct financial transactions.

Nominees shield real owners

Most states require companies to list the names of their officers in incorporation filings. However, a 2006 Government Accountability Office report showed most states do not bar the use of nominee officers, who may be straw men who camouflage the identities and activities of the real owners.

Secrecy marketers in the mini-industry provide nominee officers for Nevada and Wyoming corporations for an annual fee. They also tout the use of so-called bearer shares, an ownership system in which controlling shares may be physically transferred from one person to another in secret.

Referring to corporations whose owners are shielded by nominee officers, bearer shares and other tactics, the money laundering report said "Delaware, Nevada and Wyoming are

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often cited as the most accommodating jurisdictions in the United States for the organization of these legal entities."

The Nevada Secretary of State's website even proclaims: "No IRS Information Sharing Agreement."

Secretary of State officials in Nevada and Wyoming said in interviews that while they cooperate with law enforcement agencies, current laws in most cases don't let them challenge or investigate incorporations. "We're a filing office, and we don't make the law," said Nevada Deputy Secretary of State Scott Anderson, head of the Commercial Recordings Division.

Nonetheless, the officials said their state legislatures are expected to respond to law enforcement concerns by enacting changes as early as this year to close real or perceived loopholes.

That's welcome news for John Colledge, head of the Reno office of Immigration and Customs Enforcement. He complained that corporate anonymity, a "large stumbling block," thwarted him in 2004 when he checked a bank's tip about a Swiss man who had formed two Nevada corporations.

The man had flown from Zurich to Reno and opened corporate accounts that received thousands of euros and quickly redirected the funds overseas, Colledge said. Although he suspected that the funds were being laundered, Colledge said he could not get enough information to determine for sure.

"To fly from Zurich to Reno for a long weekend is a very unusual sort of thing. I think most of us (in law enforcement) who have some experience in this international area historically would look at somebody flying from Reno to Switzerland to do something in reverse," said Colledge.

The operations of Asset Protection Group demonstrate the level of anonymous activity available under some states' incorporation laws. The firm attracted clients in part with a promotional video in which actor Robert Wagner warned that without asset protection, "You could lose everything you've worked so hard for, in a flash."

Wagner publicist Alan Nierob called the video "a one-shot deal," and said his client didn't endorse Asset Protection Group.

USA TODAY's analysis found that more than 1,000 Nevada corporations list William Reed, a 56-year-old executive identified in the Federal Trade Commission lawsuit as Asset Protection Group's operator, as the sole officer. Each corporation listed the firm's office address as its own.

A Colorado Supreme Court disciplinary panel suspended Reed's law license in 1997 for "dishonest" conduct in transferring purported ownership interests to employees of his

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former law firm, a court record shows. Reed did not seek reinstatement. Separately, under questioning in an October deposition for the Federal Trade Commission case, Reed said he was under IRS investigation.

Misleading claims alleged

Government lawyers in the case allege that Reed teamed with Richard Neiswonger, 55, who headed Asset Protection Group's marketing affiliate. Court records show Neiswonger was sentenced to 18 months in federal prison in 1998 after pleading guilty to money laundering and wire fraud charges. The case involved misleading marketing claims in a previous business.

The Federal Trade Commission lawsuit alleges Reed, Neiswonger and Asset Protection Group used misleading income projections to defraud scores of consultants who paid $9,800 each in hope of marketing the firm's privacy tactics.

Defense attorneys said Reed, Neiswonger and Asset Protection Group did nothing wrong. They have asked U.S. District Judge Stephen Limbaugh to dismiss the lawsuit. Limbaugh named a receiver to administer Asset Protection Group pending the outcome of the case.

The receiver, Robb Evans & Associates, alleged in court filings that Asset Protection Group may have facilitated money laundering by a suspected crime ring thousands of miles away. Police in Fairfax County, Va., notified Asset Protection Group in May that suspects in a string of identity thefts had used the company "to set up multiple corporations and open bank accounts," the receiver reported in a court filing.

"I have reviewed bank statements for two of the corporations, and over $500,000 in apparently stolen funds (from the suspected Virginia identity thefts) was deposited in these accounts," M. Val Miller, an attorney working with the court receiver, wrote.

Fairfax police said no arrests had been made in the case. Miller said detectives told the receiver's office the suspects were believed to have fled the country.

Anderson, the Nevada deputy secretary of state, said the agency did not know about the federal allegations against Reed, Neiswonger and Asset Protection group.

Felon may have secretly run corporation

The Secretary of State's office became aware of another Nevada corporation, Par Three Financial, in 2005 after the Securities and Exchange Commission filed a federal court complaint that accused the firm and its secret owner of using a pyramid scheme to scam investors. In such a scheme, money from newly recruited investors is used to pay those who invested earlier.

Nevada records show Par Three was based in Las Vegas and at various times listed a Carson City businessman or a Nevada attorney as its sole publicly listed officer. But, the

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SEC lawsuit alleged, the company was secretly controlled by Melvin Ruth, a Florida felon who served nearly three years in federal prison after he pleaded guilty to conspiracy to commit mail and wire fraud in a scam involving stolen investments.

In November 2003, shortly after he was released from prison, Ruth allegedly used Par Three to mount a similar scam. The firm offered potential investors a monthly return of at least 2% on loans to check-cashing stores, company and court records show. Par Three raised at least $8 million from more than 120 investors who were unaware of Ruth's role, the SEC alleged.

In December 2005, the SEC got a court judgment that permanently restrained Ruth and anyone working with him from violating securities laws. The judgment ordered Ruth to pay a civil penalty and give up ill-gotten gains, with interest. Ruth died last year of cancer complications amid efforts to recover Par Three assets that could repay investors, said his lawyer, Carl Schoeppl.

USA TODAY's review of incorporations found that Wyoming, like Nevada, has multiple examples where a single person is the sole officer for a string of companies.

Guillermo Jalil, for instance, runs AssetProfile.com, which sells Wyoming corporations and provides nominee officers. State records list him as an officer of more than 100 corporations, from A+ Shadow Systems to Yokohama Technologies.

Investigators from Interpol, the international law enforcement agency, have contacted the Wyoming Secretary of State's office about several of the corporations registered by Jalil, said Cowan, the securities division chief. None of the inquiries directly involved Jalil, who operates legally and sells corporations that typically may be used outside the USA, Cowan said.

In a recent interview, Jalil said he had not been contacted by Interpol and knew nothing about the inquiries to the Secretary of State. He said he conducts background checks on anyone seeking nominee officers for a corporation.

Ownership transparency obstacles

Jalil contended that the IRS and law enforcement investigators can check on any company by examining bank records. Claiming that corporation secrecy laws can block investigators "doesn't sound like reality to me," Jalil said.

But the internal workings of some corporations prove particularly resistant to transparency. Wyoming incorporation records show that at least 90 companies created since 2002 list Stella Port-Louis as the sole listed officer. Many of the firms, such as Export Deutschland AG and Motorcomsa S.A., have foreign corporate names.

The only address for Port-Louis listed in the records is a postal box in the Republic of Seychelles. A USA TODAY interview request mailed in January to Port-Louis' postal

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box could not be delivered. Port-Louis did not respond to a message relayed via Registered Agency Services, the Cheyenne company that is the local agent for the corporations that list her as an officer.

JoLyn Jordan, an official of Registered Agency Services, a firm that files incorporations, said she believed Port-Louis was a nominee for owners outside the USA. "I don't know who she is, or if she's for real," said Jordan. Asked how to determine if they were shell firms created for crime, Jordan said, "You don't know."

Jack Blum, an international tax expert and former special counsel to the Senate Foreign Relations Committee, said money laundering investigations have historically focused on the Seychelles. While saying he had no information about the Port-Louis firms, he said the filings seemed designed to frustrate.

"Whoever's trying to research it will go batty," said Blum.

Contributing: Barbara Hansen

Forbes magazine article
http://www.forbes.com/home/free_forbes/2007/0212/096.html

Shell Games
Elizabeth MacDonald 02.12.07

With no federal oversight, the states are helping to shelter crooks, money launderers and, possibly, terrorists.

Shawqi Omar has been cooling his heels in a U.S. military brig in Iraq since he was arrested in Baghdad in October 2004. The 44-year-old Kuwaiti native with American and Jordanian citizenship was charged, along with the late terrorist and leader of al Qaeda in Iraq, Abu Musab al- Zarqawi, with plotting an aborted chemical attack on the Jordanian intelligence agency. The FBI has also taken an interest: Five of Omar's relatives have been charged with using U.S. shell companies in Utah and California to commit bank fraud and money laundering and possibly to fund terrorist activities in the Middle East. One defendant has copped a plea to accusations of fraud and money laundering and awaits sentencing; three others have pleaded not guilty, and one was dismissed for medical reasons. "The fact that U.S. shell corporations can be used to commit criminal activity is increasingly a major weakness in our system," says Gregory Bretzing, supervisor of the FBI's joint terrorism task force in Salt Lake City.

Once ideal vehicles for tax evasion, shell companies--that is, corporations with no operations, no employees and no physical assets--have lately become shelters for far more nefarious criminal activities, says Stuart Nash, an associate deputy attorney general at the Justice Department. Crooks benefit in several ways. A U.S. company address lends credibility in global trade and painless access to American bank accounts. And thanks to loose laws of incorporation in many states, it's easy for offenders to remain anonymous--and to elude the authorities. Unlike publicly held companies, private entities are not obliged to reveal ownership. And without such information the police come to a dead end, unless they can tease the information they need out of bank records.

How widespread is the problem? No one really knows for sure because the states "have no idea who is behind the companies they have incorporated," says Senator Carl Levin (D--Mich.), who is trying to force the states to insist on greater transparency. "The United States should never be the situs of choice for international crime, but that is exactly what the lax regulatory regimes in some of our states are inviting." The Financial Crimes Enforcement Network, the U.S. Treasury bureau investigating money laundering, says roughly $14 billion worth of suspicious transactions involving private U.S. shells and overseas bank accounts came in from banks from 2004 to 2005, the latest Treasury data available. That's up from $4 billion for the long stretch between April 1996 and January 2004. Now, estimates the FBI, anonymously held U.S. shell companies have laundered $36 billion to date just from the former Soviet Union.

State governments provide plenty of cover for bad guys. Every year they incorporate 1.9 million or so private companies, but no state verifies or records the identities of owners,

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much less screens ownership information against criminal watch lists, according to a study by the Government Accountability Office. "You have to supply more information to get a driver's license than you do to form one of these nonpublicly traded corporations," says Senator Levin.

In many cases the documents of incorporation require only a company name, an address where official notices can be sent and the names and signatures of folks handling the paperwork--not of the owner or controlling shareholder. You can submit the forms in person, by mail or, increasingly, via the Web in a process that takes from 5 minutes to 60 days, depending on the state. The median fee is $95. A network of registration agents here and abroad help set up a vast number of shells each year. Once the minimal work is complete, the corporation, a perfectly legal entity, can conduct business and, in many cases, open a bank account.

Why doesn't Delaware crack down on anonymous incorporation? It would be a futile gesture; the crooks would just take their business to Nevada. Also note that chartering out-of-state corporations is a big industry in an itty-bitty state, which brought in $4.6 million a year in franchise fees in 2005 and kept many a lawyer occupied in Wilmington. Richard Geisenberger, Delaware's assistant secretary of state, says investigating the owners of new corporations would be untenable. "Costs are tremendous, and benefits are likely to be illusory," he says. "Crooks will give you false information absent a verification system." Then there's a "principle" at stake. "Consensus is that having disclosure of all of the shareholders would violate privacy and be a major burden to the state's resource allocation," says Laurie Flynn, chief legal counsel for the secretary of state of Massachusetts. "We have to stop terrorism, but we need to keep commerce [flourishing]."

Given the paucity of information, nailing criminals means relying on bank records. That's what happened in the Omar case. Shawqi Omar's relatives used two shell companies incorporated in Salt Lake City and San Diego, as well as two other front companies, to defraud local banks of at least $327,000 taken in the form of loans. The FBI says that, in at least one instance, a stateside family member wired $150,000 to an account in Amman, Jordan. The bureau is investigating whether that money was used to fund terror in Iraq.

Sometimes it's a foreign investigator who gets stonewalled. Authorities from overseas, mostly from Russia and Ukraine, sent in 143 demands for private-company data to the Justice Department in 2005. They almost always came away empty-handed. Uncle Sam couldn't investigate, much less prosecute, a Nevada corporation it declines to name that received 3,700-plus suspicious wire transfers totaling $81 million from such locations as the Bahamas, British Virgin Islands, Latvia and Russia. The situation has made a mockery of American demands that other nations do more to stop financial crimes. The U.S. has been pressuring the Financial Action Task Force on Money Laundering, a 33-nation organization Washington helped set up in 1989.

The shell problem was spectacularly demonstrated in the **Bank of New York** (nyse: BK - news - people) case. Peter Berlin, a Russian immigrant, with the help of his wife, Lucy

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Edwards, a Russian national as well, and a bank vice president, opened up accounts in 1996 at the bank for two private shells, Benex International and BECS International. According to allegations in a criminal case, they laundered $7 billion over the next three and a half years. The money came from Russian businessmen seeking to duck customs duties and hide profits from tax authorities. Convicted of money laundering, Berlin and Edwards were given five-year suspended sentences and six months' house arrest; they were ordered to pay fines of $20,000 apiece and pay the IRS $685,000.

Bank records helped finger Garri Grigorian, a 44-year-old native Russian. He struggled with a job at a fast-food joint in Sandy, Utah, then opened a deli--and, according to the feds, from October 1998 through January 2001 he laundered $133 million on behalf of customers of Intellect Bank in Moscow. He did it by setting up two U.S. shells and opening bank accounts to give the appearance of legitimate wire transfers to and from Intellect Bank. For his troubles he got $800,000 and interests in an apartment building and a golf course. Grigorian was caught because he made the mistake of using his own name to set up a bank account. He was sentenced in August 2005 to 51 months and ordered to pay $17 million in restitution to Russia for unpaid taxes and customs duties on money transferred out of that country.

Sometimes these schemes imperil strategic interests. Uncle Sam has charged Evgeniy O. Adamov, Russia's former atomic energy minister, and Mark Kaushansky, a onetime Westinghouse engineer, of using a couple of U.S. shells to divert $15 million that was supposed to upgrade nuclear safety at power plants in Russia and eastern Europe. In September Kaushansky pleaded guilty in federal court to conspiracy and tax evasion. Adamov is being tried in Russia.

Incorporation agents are not shy about promoting the privacy offered by U.S. laws. Atrium Incorporators of London promotes Delaware on its Web site as "an offshore tax haven for non-U.S. residents." Advantages: "Owners' names are not disclosed to the state," and "the company is not required to report any assets." Another Web site, corp95.com, promises that for as little as $69, plus filing fees, it can set up a corporation in Nevada, which "may provide for anonymous ownership and bearer shares." The site also offers "shelf" corporations, already incorporated businesses that have sat dormant but have some operating history.

"The upside is, you can develop a credit history easier with a shelf company," says Wayne Andre, 59, who runs Nevada First Holdings in Las Vegas, which offers shelf companies--and much more--to convince creditors that a shell is really in business. Andre also rents out his own employees to serve as directors or officers to a prospective company in order to help the real owners "retain a higher level of anonymity," a company advertisement says. Such execs for hire can use their own names to obtain an employer identification number from the IRS on behalf of the new company's owners. And if you need a business address or telephone services, Nevada First can help there, too; it has already assigned 1,800 addresses for "suites" within its Vegas offices.

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As for hanky-panky among his clients, "We don't have a single company we know of that's done criminal activity," says Andre. Yet he himself took a wrong turn. In 1998 he pleaded guilty to embezzling $2 million from his clients and was later sentenced to four years in prison. Using the name Wayne McMiniment at the time, he offered incorporating services and set up bank accounts but retained signature authority over them, diverting funds, supposedly headed for offshore accounts, for his own "lavish lifestyle," says a court document.

Other shell promoters have ended up in the slammer. Paul D. Harris of Elizabeth, Colo. was sentenced in January 2006 to five and a half years in prison on tax fraud charges. Through his company, Tower Executive Resources of Denver, Harris set up shells used to conceal $9 million in taxable income for clients, who sheltered funds in secret bank accounts in the Turks and Caicos Islands and other offshore hideaways.

What's to be done? "The systemic vulnerability we face in the United States from shell companies can only be addressed by Congress through legislation to specifically regulate shell companies," says Dennis M. Lormel, senior vice president of Corporate Risk International in Reston, Va., the former chief of the financial crimes section in the FBI. If the states don't fix the problem themselves, Senator Levin says he will have to introduce legislation seeking a uniform standard. His solution: require states to force owners of companies they incorporate to disclose the owners' names on state incorporation forms. But there seems to be little urgency among his peers.

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Richard J. Geisenberger

Invited Testimony

United States Senate
Committee on Homeland Security and Governmental Affairs
Permanent Subcommittee on Investigations

The Honorable Norm Coleman, Chairman
The Honorable Carl Levin, Ranking Minority Member

November 14, 2006

Mr. Chairman and Members of the Subcommittee:

Thank you for this opportunity to address the Subcommittee and to provide testimony on behalf of the State of Delaware in response to the Subcommittee's letter of November 1, 2006 and to share our observations and comments on the Government Accountability Office (GAO) report entitled *Company Formations: Minimal Ownership Information Is Collected and Available* (the "GAO report") as well as Chapter 8 of the December 2005 *U.S. Money Laundering Threat Assessment* (the "MLTA report"), and Section 5.1 of the *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: United States of America* (the "FATF report") (together the "Reports").

My name is Rick Geisenberger, and I am Delaware's Assistant Secretary of State as well as the Director of the Delaware Division of Corporations. I have served in this position for the past six years. I wish to thank the numerous corporate and alternative entity law attorneys in Delaware who have assisted the State in preparing this testimony.

Our testimony specifically responds to the eight matters raised in the Subcommittee's letter as follows:

(1) The approximate number of non-publicly traded corporations and limited liability corporations (hereinafter "corporations") formed in Delaware each year; the procedures typically used to form corporations in Delaware, including the role of on-line procedures and registered agents; the typical amount of time required by Delaware authorities to form a corporation; and the typical fees charged.

Under the federal system in the United States, each state and the District of Columbia has the authority to charter corporations and other business entities. As noted in the GAO report, along with Florida, California, and New York, Delaware is one of the largest filing offices in the United States. Just over half of all publicly traded companies in the United States are incorporated in Delaware including 61% of Fortune 500 companies. Last year, 119 initial public offerings (IPO's) or 73% of all IPO's on U.S. exchanges were incorporated in Delaware.

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Delaware officials including our Governor and Congressional Delegation have traveled the world telling the Delaware story to corporate attorneys, venture capitalists, large institutional investors and others that advise businesses on where to incorporate. The Delaware story is a compelling one -- -- modern and flexible laws that are updated annually to enable businesses to structure their internal affairs in ways that meet changing business conditions, a highly regarded judiciary that has written much of the modern case law on fiduciary duties, a well-developed corporate and legal services industry in our State that is expert in the application of Delaware corporate law and active in its development, unparalleled service and responsiveness from the Delaware Division of Corporations which handles complex documents efficiently and effectively, and an elected leadership in Delaware with an enduring commitment to ensuring the continued success of our corporate laws.

Due to these strengths, in 2005, more than 133,000 new, non-publicly traded corporations, limited liability companies, limited partnerships, general partnerships and statutory trusts made Delaware their legal domicile. As of November 4, 2006 there were 753,684 active domestic business entities and 9,397 active foreign entities (that is, having their legal domicile in a jurisdiction other than Delaware) on the State's corporate record. The legal entities incorporated in Delaware and other States represent every segment of the nation's economy including the for-profit, religious, governmental and charitable sectors.

At one end of the spectrum are large, well-capitalized public and privately held companies. Delaware is the legal home of thousands of publicly traded companies such as General Motors, Google and the New York Stock Exchange. Delaware is also home to many large privately held firms. Some of these firms, such as Cargill and Cox Enterprises, have millions of authorized shares held by thousands of beneficial owners. Some of the largest closely held corporations in America such as Mars Incorporated are Delaware business entities. A significant percentage of the legal entities formed in Delaware are subsidiaries or affiliates of such large firms, and are created for the purpose of arranging the financings, asset-backed securitizations, mergers and acquisitions, roll-ups, investment vehicles and strategic alliances in which those large businesses engage.

At the other end of the spectrum are small Mom & Pop businesses, private investment and real estate vehicles as well as religious, charitable and civic organizations. Due to the wide diversity of types of businesses formed in Delaware and the importance of speed and efficiency to large multi-national corporations, the Delaware Division of Corporations has developed a variety of innovative services to meet the business needs of such companies. For example, while some documents filed via paper might take a week or more to be approved by the State, the typical document is processed within 24 hours of receipt. It is not uncommon for large corporations to pay for expedited service options enabling documents to be processed in under an hour. The typical formation fee paid to the State is $90 plus a $30 fee for a certified copy of the formation document. Expedited service fees range from $40 to $1,000 depending on the level of expedited service requested.

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(2) The extent of beneficial ownership information typically obtained by Delaware authorities during the incorporation process, including initial incorporation and period reporting requirements; why corporations but not limited liability corporations are required to file annual reports in Delaware; and Delaware policy on establishing corporations that issue bearer shares.

As noted in the Reports, neither Delaware nor other states' filing offices obtain beneficial ownership information, either at the time of formation or through periodic reports. It should be noted that the purpose of a public filing by a company has never been to ascertain beneficial owners. Rather the purpose of the public filing is to create a public record of the existence of a legal entity, the state or country of its legal domicile, and its address for service of process.

Like many corporation laws in other states, the Delaware General Corporation Law ("DGCL") does require that corporations file with the Delaware Secretary of State an annual report that includes the names and addresses of all of the corporation's directors, one officer and the number and description of authorized shares of stock. For several reasons outlined below, these reporting requirements do not readily fit the legal structure of Delaware limited liability companies.

First, from its inception, the Delaware Limited Liability Company Act ("DLLCA") has been a contract-oriented statute, modeled largely on Delaware's successful partnership laws. It was not modeled on the DGCL and as a result, the DGCL's annual report requirement was not replicated in the DLLCA.

Second, while Delaware corporations have a predictable form of governance, there are limitless options available for managing a Delaware limited liability company. Except in the rarest of situations, Delaware corporations are managed by a board of directors, and the DGCL contains numerous provisions regarding the manner in which such boards function and govern the corporation. By contrast, the DLLCA does not require any particular form for the management of a Delaware limited liability company, but rather leaves that to determination of the parties ("members" in limited liability company parlance). The DLLCA does provide a default rule for management by the members in the event the contract among the members does not otherwise provide.

Third, the DGCL contemplates an annual election of directors and it often follows that there is a change in officers at the same time. The annual report provides a useful means of making such annual changes in the composition of the board of directors and senior management a matter of public record. Unlike the DGCL, there is no analogous mandate for periodic elections under the DLLCA. Indeed, in many instances, management does not change in a predictable timeframe and sometimes not at all during the life of a Delaware limited liability company. Because a limited liability company is a creature of contract, the parties are generally already aware of the identity of the party or parties managing the limited liability company. To the extent parties desire to provide for a

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notice requirement similar to the information rights afforded by the annual report of a Delaware corporation, they may do so by way of the agreement among them.

Fourth, in contrast to the DGCL, the DLLCA reflects an almost completely contract-oriented approach to intra-entity relationships. Whereas the DGCL provides stockholders with access to information (e.g., the name and addresses of directors) by way of a statutory mandate, the DLLCA allows parties to the contract governing a Delaware limited liability company to provide similar information rights by way of that agreement, if desired. Thus, the absence of an annual report analogous to the requirement under the DGCL illustrates this principle that Delaware limited liability companies are creatures of contract.

With respect to bearer shares, the DGCL Section 158 was amended in 2002 to clarify what had previously been generally understood: "A corporation shall not have power to issue a certificate in bearer form." For limited liability companies, bearer shares, or bearer limited liability company interests, are neither specifically permitted nor specifically prohibited under the DLLCA. Based on the experiences of a number of leading Delaware lawyers who practice in the field, bearer limited liability company interests are not used. While theoretically it might be possible for the contract governing a limited liability company to be drafted to permit bearer shares, the DLLCA is not structured to facilitate this. On the contrary, the default rules of the DLLCA contemplate that all members of a limited liability company generally be known by the limited liability company, just like all partners of a partnership are generally known by the partnership.

(3) The role and legal responsibilities of third party agents paid to assist in the formation of Delaware corporations, including whether they are required to obtain and verify beneficial ownership information; and Delaware procedures for overseeing the actions of such company formation agents;

Businesses typically form legal entities with the assistance of a third party such as an attorney, an accountant or a company formation agent. Some companies submit formation documents without the assistance of a third party. Some company formation businesses in Delaware have requested and been granted "online access" to the Delaware Corporation Information System (DCIS) by the Division of Corporations. This access permits such businesses to view certain public information in the State's database and enables "imaging" agents to scan and automatically transmit images of corporate documents to State officials. This system dramatically improves the State's efficiency and timeliness in the processing of complex corporate filings.

In exchange for such access, each of the State's 54 authorized online agents sign a contract with the State agreeing to comply with a variety of policies set by the Division. The contract is broadly drafted to permit the State to deny, revoke, or suspend online access to an agent or its officers, directors, partners, owners or key employees that 1) do not satisfy the minimum statutory qualifications to serve as a registered agent in Delaware; 2) have a criminal background or are known to associate with persons of

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nefarious backgrounds or disreputable characters; 3) demonstrate financial irresponsibility in dealings with the Secretary of State; 4) demonstrate a pattern of submitting documents which contain inaccuracies or false statements; 5) fail to be responsive in addressing questions and concerns of the Secretary of State; 6) fail to comply with the laws and regulations of federal, state or local governments; or 7) have information coming before the Secretary of State related to the agent's competency, financial capability, honesty, integrity, reputation, habits or associations. The State does deny online access to company formation agents that fail to meet these standards.

Many company formation businesses in the State also offer registered agent services to their customers. Every company in the State is required to have a registered agent in the State to accept service of process. The registered agent may be the company itself, an individual resident of the State, or another legal entity. Registered agents are required under Delaware law to maintain a business office in the State which is generally open, or if an individual, they are required to be generally present at a designated location in the State at sufficiently frequent times to accept service of process and forward State correspondence to the entities they represent. There are more than 32,000 registered agents in the State of Delaware. The vast majority of registered agents in Delaware (more than 96%) represent three or fewer business entities.

We, of course, share the concern of federal law enforcement officials that business entities ought not to be formed for illicit purposes. In June 2006, the State adopted legislation designed to ensure that law enforcement will have better access to information that identifies a person who is acting as a representative of a Delaware business entity. Under this new legislation that takes effect on January 1, 2007, every Delaware business entity will be required to provide to their registered agent and to update from time to time the name, business address and business telephone number of a natural person who is an officer, director, employee or designated agent of the business entity who is authorized to receive communications from the registered agent. Every registered agent will be required to retain such information in paper or electronic form for every entity they represent.

Delaware has also become the first state in the nation to adopt legislation responding to concerns expressed by law enforcement regarding illicit practices of registered agents. Delaware has approached this issue from two angles. First, Delaware is making a conscious effort to ensure that the State gathers more information on companies engaged in the registered agent business. Effective January 1, 2007, 237 registered agents in Delaware -- those representing directly or through affiliates 50 or more business entities -- will be required to meet additional qualifications as "Commercial Registered Agents". Commercial Registered Agents in Delaware will be required to maintain a Delaware business license, have generally present in their office an officer, director or managing agent, and provide to the State such information identifying and enabling communication with the Commercial Registered Agent as the Secretary of State shall require. For the first time, the Secretary of State will be explicitly authorized to refuse to file documents on behalf of any registered agent that fails to meet the qualifications for being a registered agent. In addition, the new legislation creates a mechanism allowing the

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Delaware Court of Chancery to enjoin any person or entity from serving as a registered agent for failure to meet the qualifications to be a registered agent; for conviction of a felony or crimes involving dishonesty, fraud or moral turpitude; or, for being engaged in conduct in connection with acting as a registered agent that is intended or likely to deceive or defraud the public. We believe that these new provisions of Delaware law will have the desired deterrent effect while continuing to enable legitimate business entities to conduct their affairs quickly, at minimum cost and without deterring economic activity and business investment by impinging on privacy.

(4) The extent to which Delaware permits the use of nominee shareholders, directors, and officers for corporations formed in the United States, and the justifications for the use of such nominees in the United States.

Directors: DGCL Section 141(b) establishes that directors must be natural persons ("The board of directors of a corporation shall consist of 1 or more members, each of whom shall be a natural person").

By default rule under the DLLCA, the members of a Delaware limited liability company share authority to manage the affairs of the entity. By contractual arrangement, however, the DLLCA permits the use of other management structures, including ones where the parties with managerial control are acting in a representative capacity on behalf of the members or other interested parties. The flexibility in the DLLCA in this regard responds to the personal, tax and business needs of contracting parties and is consistent with the overall contractual nature of limited liability companies. A party acting in such a representative capacity (i.e., a "nominee") need not be a natural person and may be another entity. For example, an individual (e.g., a parent) acting as trustee on behalf of beneficiaries (e.g., her children) may in her trustee capacity legally become a member of a Delaware limited liability company and as such manage the Delaware limited liability company; an investor in a Delaware limited liability company may be entitled to nominate a firm (e.g., a financial services firm) to manage some aspect of the Delaware limited liability company's business (e.g., formulating and executing its investment strategy) and that "nominee" manager legally may do so. Contracting parties demand flexibility to achieve legitimate tax, business and other goals, and the foregoing are just several examples of the limitless options available in structuring the management of a limited liability company.

Officers: The DGCL no longer explicitly establishes that officers must be natural persons. Until 1998, however, the statute governing the selection of corporate officers (Section 142(b)) implicitly recognized that officers must be natural persons, providing that "[e]ach officer shall hold *his* office until *his* successor is elected and qualified or until *his* earlier resignation or removal." (emphasis added). In 1998, in the interest of removing gender distinctions throughout the DGCL, the words "his" were eliminated in favor of the term "such officer's." This amendment was not intended, however, to expand Section 142 to permit non-natural persons to serve as corporate officers. To our knowledge, moreover, it remains universal practice that officers of Delaware corporations are natural persons.

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The DLLCA does not require that a Delaware limited liability company have any officers. By contractual arrangement, however, a Delaware limited liability company may have one or more "officers." Under the DLLCA, a person who is an officer of a Delaware limited liability company need not be a natural person and may be an entity. As discussed with respect to directors, the management of a Delaware limited liability company may be structured in a manner that such an officer is acting in a representative capacity. As noted above, the DLLCA's flexibility in these respects furthers legitimate interests.

Stockholders: Like the Model Business Corporation Act,[1] the DGCL and the DLLCA permit persons to hold formal or nominal title to shares or other equity interests in the name of other persons as beneficial owners. Taking advantage of that flexibility, the large majority of equity securities traded on the national securities exchanges and national securities markets are held in "street name," by depository nominees for the benefit of banks and brokers who, in turn, hold such securities for the benefit of clients as beneficial owners. The identities of the beneficial owners are largely unknown to the corporations or other entities that issue such securities. The Depository Trust Company, a principal securities clearinghouse, reports that it "retain[s] custody of almost 2.5 million securities issues worth about $28.3 trillion, including securities issued in the United States and more than 100 other countries."[2] It is therefore no understatement to say that without business entity laws permitting such nominee ownership, the equity capital markets in the United States would collapse as unmanageable.

In addition, flexibility as to the manner of ownership of stock and limited liability company interests fosters investment and capital formation (by securing for investors the limited liability that accompanies the use of a separate legal entity as the investment vehicle) and promotes efficiency (by enabling investment at the entity level). For example, an institutional investor (e.g., an insurance company or a pension plan) or a private investment firm may purchase interests in an investment fund created in the form of a Delaware limited liability company; two corporations may invest in a separate joint venture corporation or Delaware limited liability company in order to pursue a strategic alliance, and that investment vehicle in turn may make investments in other business entities for purposes of carrying out the strategic alliance; an individual (e.g., a parent) acting as trustee on behalf of beneficiaries (e.g., his children) legally may hold in his trustee capacity an economic interest in a Delaware limited liability company created to own real estate or other investment property.

(5) The approximate number of requests made over the last five years by law enforcement for beneficial ownership information related to Delaware shell corporations, and the extent to which the state was able to provide that information.

All documents filed with the Delaware Secretary of State are public information. The Secretary of State responds to hundreds of thousands of requests annually for copies of

[1] See Model Business Corporation Act §7.23 ("Shares Held by Nominees")
[2] http://www.dtcc.com/AboutUs/affiliates.htm?shell=false.

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such documents and certificates of good standing. Delaware does not track the number of requests made for beneficial ownership information. We field daily requests for beneficial ownership information from citizens and/or members of the media that may, for example, be interested in researching the ownership of a particular privately-held investment or real estate venture. However, since federal, state and local law enforcement officials are already well aware that states do not track such information, we seldom receives such requests from law enforcement. We do, however, field frequent requests from law enforcement for annual reports, registered agent information and copies of company filings. Sometimes these requests come in the form of a subpoena although it is the position of the Division that requests for public information do not require a subpoena. The Division occasionally receives subpoenas requesting non-public information such as ad-hoc reports prepared by the State or information on depository accounts maintained at the State on behalf of customers of the Division. The State of Delaware fully cooperates with law enforcement and tax authorities in all such matters.

(6) Any information the state may have on the extent to which the lack of beneficial corporate ownership information in state records can impede or has impeded domestic and international law enforcement investigations.

The State has no specific knowledge of the extent to which the lack of beneficial ownership information by federal, state and local government records impedes or has impeded domestic and international law enforcement investigations.

(7) Delaware's views of: (a) the GAO report; (b) Chapter 8 of the December 2005 report, U.S. Money Laundering Threat Assessment, issued jointly by the Departments of Justice, Treasury, Homeland Security and others; and (c) section 5.1 of the 2006 Financial Action Task Force report, Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: United States of America, each of which addresses the issue that the United States does not obtain beneficial ownership information for shell corporations formed within U.S. borders.

The stated concern of the Reports is money-laundering, that is, the use of corporations and other business entities, the owners of which are anonymous, to facilitate illegal transactions. The ostensible solution offered by these Reports appears to be having each of the 51 jurisdictions in the United States impose a mandatory rule that would require companies to identify who their beneficial owners are, and then make that information available to the State and, perhaps, to the public.

In summary, it is the view of Delaware that (i) a beneficial ownership reporting system that included public companies would be a logistical and costly nightmare for corporations; (ii) even a self-reporting system that exempted public companies and their "affiliates" would have immense verification costs and definitional administrative problems;[3] and (iii) as applied to non-public companies, such a system would impose

[3] First, it will be difficult for the State to determine who would qualify as an "affiliate" under such an exemption. Second, since it is a self-reporting system, there is little doubt

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costs on legitimate private businesses that seem vast in relation to benefits that are at best uncertain.

Part A of this portion of our testimony sets the stage for our comments on the GAO, MLTA and FATF reports by providing a brief summary of the concepts of record and beneficial ownership under Delaware law, as well as the current record-keeping requirements imposed on corporations governed by the DGCL. Part B of this portion of our testimony provides specific responses to the Delaware corporation law issues raised in the Reports.

A. Delaware State Law Concepts of Record and Beneficial Ownership

A "stockholder" under the Delaware General Corporation Law (the "DGCL") has historically been considered to be the "holder of record," and not the "beneficial owner" of a company's shares. The same is true in those states that have adopted the Model Business Corporation Act (the "Model Act").[4] In part, the law-- both in Delaware and elsewhere-- has developed this way for practical reasons. For example, Delaware corporations rely on a list of record holders in order to determine which of their stockholders are entitled to notice of a stockholder meeting. In contrast, corporations are not required to send notice of stockholder meetings to beneficial owners. This is because such a requirement would impose an unfair responsibility on the corporation to uncover all persons who hold a beneficial interest in its stock. Indeed, sorting through the various layers behind beneficial ownership would result in a logistical nightmare for the corporation (private companies included). It would also compromise the efficiency and certainty that reliance on a list of record holders provides to corporations.

Under the DGCL, record holders are considered the "stockholders" of a company. Delaware corporate law has traditionally limited the rights of stockholders to stockholders of record,[5] and has long recognized the "rule that a corporation may rely on its stock ledger in determining which stockholders are eligible to vote or exercise the important rights of a stockholder."[6] In fact, a corporation satisfies its obligations to its stockholders by communicating with record holders and is not required under Delaware

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that potential money-launderers will report that they are eligible affiliates of a public company and, the State, for all intents and purposes, could not easily determine their status.

[4] Model Business Corporation Act §7.23, Official Comment ("Traditionally, a corporation recognizes only the registered owner as the owner of shares.").

[5] For decades the Delaware Supreme court has consistently defined the term "stockholder" as a holder of record. *See In re Giant Portland Cement Co.*, 26 Del. Ch. 32 (Del. Ch. 1941); *Salt Dome Oil Corp. v. Schenck*, Del. Supr., 28 Del. Ch. 433, 41 A.2d 583, 589 (1945); *Carl M. Loeb, Rhoades & Co. v. Hilton Hotels Corp.*, Del. Supr., 43 Del. Ch. 206, 222 A.2d 789 (1966); *ENSTAR Corp. v. Senouf*, Del. Supr., 535 A.2d 1351, 1354 (1987); *Shaw v. Agri-Mark, Inc.*, 663 A.2d 464, 469 (Del. 1995); *Haft v. Dart Group Corp.*, 1997 Del. Ch. LEXIS 46 (Del. Ch. 1997).

[6] *See Shaw*, 663 A.2d at 469.

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law to identify and disclose all of its beneficial owners. For example, Delaware law does not require corporations to send notice of stockholder meetings to beneficial owners or accept demand for appraisals from beneficial owners.[7]

This is so because corporations must have a practical means by which they can ascertain the names of the individuals with whom they need to communicate in regard to corporate transactions, or other significant corporate events.[8] Using the list of record holders provides "order and certainty," by allowing corporations to deal freely with the registered holders without having to investigate the beneficial ownership of its stock.[9] According to the Supreme Court of Delaware:

> The corporation ought not to be involved in possible misunderstandings or clashes of opinion between the non-registered and registered holder of shares. It may rightfully look to the corporate books as the sole evidence of membership.[10]

A contrary rule, such as the rule contemplated by the Reports, would amount to an unreasonable burden on corporations. It would also compromise the certainty and expediency that relying on a list of record holders provides to corporations. Corporations would be faced with the near impossible task of uncovering, on a continuous basis, all persons who hold an interest in their stock, whether through a business entity, trust, or some other form of ownership.

Indeed, to comply with such a rule, public corporations would have to sift through various levels of the holders of stock, including the brokerage houses, banks, depositories and other nominees, to discover the identity of their beneficial owners (who had chosen to have those entities register their respective shares). Such a task would be incredibly time-consuming and costly. This is especially true for large private companies that have a number of shareholders who spread out their ownership and hold shares in multiple trusts, or some other business entity.

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[7] *See Gilliland v. Motorola, Inc.*, 859 A.2d 80, 85 (Del. Ch. 2004) (holding that the corporation satisfies its notice obligation under section 262 by sending notice to the brokers or fiduciaries, and is not required to send notice to the beneficial owners.); *see also Edgerly v. Hechinger*, 1998 Del. Ch. LEXIS 177 (Del. Ch. 1998) (holding that only a holder of record can demand an appraisal); *Bandell v. TC/GP, Inc.*, 1996 Del. LEXIS 23, Del. Supr., No. 247, 1995, Berger, J. (Jan. 26, 1996) (ORDER) (holding that an appraisal action must be filed by the record owner).

[8] *See In re Northeastern Water Co.*, 28 Del. Ch. 139, 150-151 (Del. Ch. 1944) (holding that "failure to have shares registered so as to indicate an interest in others than the registered holder may reasonably be deemed a manifestation of intent that the corporation should deal freely with the registered holder as the true owner without investigating his authority.").

[9] *Salt Dome Oil Corp.*, at 441 A.2d at 589.

[10] *Id.*

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Apart from concern about the impact on corporations, there are nearly countless situations in which disclosure of beneficial ownership information of privately held firms would run counter to legitimate personal or business interests of equity owners:

(1) An investment fund, sponsored by an investment management firm, may take the form of a Delaware limited liability company. A listing of the investors in that Delaware limited liability company might effectively constitute the client list of the sponsor, which clients have been identified and cultivated by the sponsor at considerable effort and expense. Disclosure of the investors' identities in that case would permit a competing investment management firm to obtain and potentially trade unfairly on the sponsor's proprietary client list. Indeed, because investment management firms commonly invest in each other's investment vehicles, there are compelling competitive reasons not to reveal to the limited liability company investment vehicle the information as to the beneficial ownership of its various investors.

(2) A joint venture between two large companies, created for the purpose of developing a new manufacturing process, may take the form of a Delaware corporation. The mere existence of this joint venture relationship may be a sensitive business matter. Disclosure of the alliance could unfairly advantage rival firms by providing insight into their competitors' business initiatives and strategies.

(3) A Delaware limited liability company may be used as a personal estate planning vehicle. Many non-public Delaware limited liability companies hold significant "family" investments or other family assets or serve as a private mutual fund permitting family members to participate in a controlled investment structure. Disclosure of the beneficial ownership of the Delaware limited liability company in that circumstance could intrude on a family's realistic expectation that such sensitive matters will remain private. Moreover, disclosure of the beneficial owners could expose the family members to harassment by persons seeking to invade the family assets or expose a family member to actual physical danger.

B. Responses To Delaware Corporation Law Issues Raised In The Reports.

1. The GAO Report - The GAO Report is generally balanced and factually accurate in describing the types of information collected by States, such as Delaware, in connection with the formation of corporations. However, because the GAO Report was completed in April, 2006, it does not take into account the changes Delaware made this summer to its statutes as described in Section 3 of this testimony.

The GAO Report is important in that it highlights some of the practical problems and administrative challenges that requiring collection of beneficial ownership information in connection with the formation and maintenance of corporations would create. For example, many states, including Delaware, do not have the physical capacity, either in

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staffing or technology, to assemble and maintain this information themselves. Indeed, in Delaware, such a requirement would require legislative action to mandate the provision of such information to the State or to registered agents.

Even if such a system were imposed, verifying information about beneficial owners at formation would be difficult, if not impossible, given the reasons for and timing of the formation of corporations. For example, a law firm may be instructed to form an investment vehicle for a client before the ownership of the entity is even determined. In addition, beneficial ownership information may (and frequently does) change following formation, and it would not be practical to require Delaware or registered agents to enforce reporting requirements regarding such changes. Moreover, many persons forming new corporations are themselves entities, such as public corporations and investment professionals, who are taking advantage of the benefits of the corporate form for legitimate business reasons, such as limiting liability exposure or facilitating more affordable borrowing rates through the use of so-called "bankruptcy remote" entities.

Finally, we share the concern expressed in the GAO Report that the experience of other jurisdictions could be repeated in Delaware and other states if this type of inquiry is mandated. It is hard not to envision a drop in the number of entities formed in the United States and a corresponding flight of capital if the beneficial ownership reporting requirements contemplated by the GAO Report are imposed.

2. MLTA Report - Chapter 8 of the MLTA Report ("Shell Companies and Trusts") is flawed in several important respects.

First, the specific reference in Chapter 8 to a "handful of U.S. states," and its identification and study of Delaware, Nevada and Wyoming, create the incorrect impression that Delaware offers what the report describes as "cloaking features" that are distinct and more protective of privacy than what most if not all other states also offer. This is not the case. The Model Act – the template for the majority of corporate statutes outside of Delaware – allows for nominee ownership (see §13.03, "Assertion of Rights by Nominees and Beneficial Owners"); the Model Act vests in the board of directors the discretion to dispense with share certificates (§6.26); unlike the Delaware General Corporation Law as recently amended, the Model Act makes no provision for closing down commercial registered agents for fraud or the like (see Model Act §§5.01-5.04); like Delaware law, the Model Act contains no limitation on share ownership by a national of any jurisdiction, regardless of place of residence, and permits the corporation to operate worldwide (see, e.g., §3.02(10) (corporate power to "conduct its business … within or without this state"); and like Delaware law, the Model Act requires no annual reporting of assets (§16.21). It is misleading to single out Delaware as if it were unusually hospitable to business participants seeking privacy for illegitimate purposes.

Second, Chapter 8 is flawed by an incomplete and cursory assessment of the importance of legitimate uses of so-called "cloaking features." For example, it asserts that "allowance of nominee shareholders undermines the usefulness of the shareholder register … because the shareholder may not be the ultimate beneficial owner." The

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suggestion is that this feature of Delaware corporate law is a "cloaking feature" conducive to money laundering, but there is no recognition that the ability to hold shares in nominee name is central to the operation of U.S. securities markets, among many other important legitimate business purposes. Likewise, as an example of a claimed "race to the bottom" that creates "a real money laundering threat," Chapter 8 notes that "a Delaware-registered company may be owned by a national of any jurisdiction, regardless of his or her place of residence," and that "the company can be operated and managed worldwide …." What is missing is an acknowledgement that the ability to attract ownership from all over the world, and the ability to operate in any area of the world, is a necessary underpinning of all capital investment in U.S.-chartered entities, and is a necessary underpinning of the ability of such entities to conduct business overseas as well as domestically, to the great benefit of U.S. investors, taxing authorities and citizens generally.

To be fair, Chapter 8 does acknowledge that shell companies and trusts "are used globally for legitimate business purposes." On the other hand, while it acknowledges that shell companies legitimately "serve as a holding company for intellectual property rights," Chapter 8 omits a wide variety of other uses of shell companies in real estate and other legitimate investment transactions. Similarly, while Chapter 8 acknowledges that trusts "are useful when assets are given to minors or individuals who are incapacitated," it fails to acknowledge the important role of trusts as estate planning devices for families of even relatively modest means.

Third, the "Side by Side Comparison of Wyoming and Nevada and Delaware" at the end of Chapter 8 is factually and legally erroneous in quite a few respects. As previously noted, Delaware law, just like the Model Act, does allow nominee shareholders and permit corporations to dispense with share certificates. The "Side by Side Comparison" fails to note either of these points. Likewise, it fails to note that, like the Model Business Corporation Act (§§8.50-8.59), Delaware law provides for indemnification of directors and officers of corporations. What this has to do with money laundering threats is not disclosed in Chapter 8, but the matter is another in which the "Side by Side Comparison" is erroneous in an obvious way.

Finally, it should be noted that much of the content of Chapter 8 was not the independent work product of the team that compiled the Threat Assessment. For example, much of the text merely rehashes the content of a GAO report that dated from October 2000. The "Side by Side Comparison" was copied verbatim from the website of a company formation business in Wyoming with no attempt at independent verification. Had Delaware officials been consulted regarding this chart and Chapter 8 in general, we could have corrected any erroneous information. While we may not agree with the GAO and FATF reports in their entirely, both the GAO and FATF, to their credit, took the time and effort to visit Delaware and seek input and comment from knowledgeable officials. No such effort was made by the authors of the Threat Assessment. This failure of communication and consultation by the authors of the Threat Assessment might account for its many flaws. In sum, it is our view that Chapter 8 is too cursory, unbalanced and inaccurate to be taken as a reliable basis for regulatory judgment in the area it addresses.

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3. FATF Report - The general premise of Section 5.1 of the FATF Report is correct -- Delaware does not require corporations to track beneficial ownership nor does it require Delaware corporations to report such information to the registered agent or the Secretary of State so that such information is a matter of public record. However, the FATF Report is incomplete in a number of respects, and fails to take into account the costs and logistical problems associated with a policy of beneficial ownership disclosure, as well as the limited benefits to be gained by such a reporting requirement.

First, the FATF Report makes a somewhat illusory statement when it claims that "there is no obligation to file the name of any shareholder or beneficial owner when establishing either a corporation or an LLC" in Delaware. The report fails to mention that corporations do not ordinarily have beneficial or record shareholders at the moment of incorporation. Specifically, pursuant to Delaware General Corporation Law, the following sequence of events occurs in forming a corporation:

(1) The certificate of incorporation is filed with the Secretary of State. (Section 101).
(2) The certificate of incorporation contains, among other things, the name and address of the incorporators or the initial directors. (Section 102)
(3) An organizational meeting is held where the corporation adopts bylaws and elects directors and officers. (Section 108)
(4) The directors issue stock in the corporation, and the recipients of the shares become stockholders of the company after payment for the stock.

Accordingly, at the formation stage when the certificate is filed, the company has not yet issued stock in the corporation. Therefore, it would be inapt to require corporations to disclose beneficial ownership at the moment of incorporation.

Moreover, even if detailed disclosure of stock ownership (once shares are issued) were required, it would not provide information about the individuals responsible for the daily controls of the corporation. Under Section 141 of Delaware law, the business and affairs of a corporation are managed under the direction of the board of directors. The stockholders of a corporation are generally not authorized to direct the business of the corporation. For example, in the case of a shell corporation with a single shareholder, the stockholder generally is not permitted to open bank accounts, sign contracts, or take any action to bind the company without specific authorization by the board of directors. Therefore, disclosing the identities of beneficial stock holders of such shell companies would not necessarily address the concerns of the FATF.

Second, the collection of beneficial ownership information contemplated by the FATF Report goes well beyond the current requirements imposed on Delaware corporations. As noted in the FATF Report, the DGCL requires a corporation to maintain information about the record ownership of its shares, but does not require corporations to maintain lists of its beneficial owners. As explained more fully in Part A of this section, *supra*, under Delaware law, the stockholders of record are recognized as the "official

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stockholders" of a company. This is because the rights associated with being a stockholder of a company are, for the most part, granted to the stockholders of record. It is the stockholders of record that are required to provide the corporation with information concerning the transfer of stock ownership. In fact, if a stockholder transfers record ownership of its shares to another person or entity, and fails to inform the corporation of this transaction, the corporation may refuse to permit the transferee to vote the shares or otherwise exercise the rights associated with record ownership.

The proposal contemplated by the FATF Report, which would require corporations to disclose changes in beneficial ownership and report such changes to the Secretary of State on a continuous basis, would be unduly burdensome and costly, requiring corporations and the State to employ a significant amount of resources. Moreover, even if the resources were available, such a reporting system would depend on the cooperation of the beneficial stockholders. As a self-reporting system, the beneficial stockholders would have to be willing to disclose the information to the company and the State. Furthermore, even if the beneficial owner disclosed his or her identity, the company and the State would have to expend additional resources verifying whether the information submitted by beneficial owners was current and accurate.

Finally, the FATF report fails to consider that many beneficial owners choose to remain anonymous for legitimate reasons. For example, many start-up companies get financing from so-called "angel investors" who do not want to disclose their identity, because they may have other investments in competing businesses, they value the privacy of their investment strategy, or they recognize that there is a potential for misuse of this information. In addition, many private companies choose to be private because they do not want ownership information publicly disclosed. Take, for example, a private company with many employees and competitors. Assume that the company has been owned of record and beneficially by its founder from its formation. As its founder ages, the founder might, for planning purposes, want to transfer shares of the corporation to various family members or faithful employees. The founder would not want that information available to competitors (potential purchasers of the shares) or to its other employees.

In sum, the FATF Report unfairly characterizes the Delaware system as one that encourages "secrecy" in the formation and ownership of companies. The report fails to take into account that there are numerous lawful and practical reasons why anonymity is valued in the realm of investments and business dealings. Furthermore, the report's suggestion that Delaware's (and other state's) policies are driven by a "powerful lobby" of "company formation agents" who want to maintain the status quo is untrue. The laws enacted under the DGCL and the policies of the Secretary of State are the result of the combined efforts and input of local practitioners, practitioners across the United States, and Delaware's legislature, and reflect the balanced interests of companies, investors, law enforcement, practitioners, and various government agencies.

(8) Recent steps taken by Delaware to address this issue, any recommendations for additional reforms, and any comments on ways to solve this problem.

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Delaware has taken a number of recent steps addressing these issues, specifically enactment of a statute in June 2006 that establishes minimum qualifications for Commercial Registered Agents, creates procedures for enjoining a "rogue" registered agent or its principals from doing business in the State, and requires all Delaware business entities to provide a communications contact to its registered agent. We recommend that other states adopt similar measures to ensure reasonable oversight of registered agents and to assure that basic customer contact information is being gathered and retained and is available to law enforcement officials through normal investigatory and judicial procedures.

We also recommend that the federal government study whether existing federal laws should be augmented to address the concerns identified in the Reports. It is our belief that the mere act of forming a business entity is never an act of money laundering. Rather, money laundering occurs when illicit funds are moved through the United States and international financial systems. The United States has in force a number of homeland security, tax and banking laws that require financial institutions to obtain information from their customers that could be augmented through stronger enforcement, new regulations or amendments.

To this end, the most comprehensive federal law is the USA PATRIOT ACT. Section 326 of the USA PATRIOT ACT requires the Secretary of the Treasury, jointly with other agencies, to prescribe regulations that require financial institutions to implement reasonable procedures to (i) verify the identity of any person seeking to open an account, (ii) maintain records used to verify such person's identity, including name, address and other identifying information, and (iii) determine whether any such person appears on any list of known or suspected terrorists or terrorist organizations provided to financial institutions by any government agency. Section 326 of the USA PATRIOT ACT applies to all "financial institutions," which is very broadly defined to include a large range of types of financial institutions, including, without limitation, banks, trust companies, thrifts, credit unions, investment companies, brokers and dealers in securities, futures commission merchants, insurance companies, travel agents, pawnbrokers, dealers in precious metals, other money service businesses, and casinos. Under the regulations implementing Section 326 of the USA PATRIOT ACT, financial institutions are required, at a minimum, to obtain the following information for a customer prior to opening an account: (i) name, (ii) date of birth, if an individual, (iii) an address, and (iv) an identification number. Based on a risk assessment, a financial institution may also obtain information with respect to the beneficial owners of an entity opening an account, or information with respect to any person with authority over an account.

As to the requirement relating to the tax identification number, for U.S. persons, this will be such person's tax identification number. If the customer is an individual, the individual's social security number will be used as the individual's tax identification number. If the customer is not an individual, but is an entity (such as a corporation, limited liability company, partnership or statutory trust), pursuant to IRC § 6109(c), the entity must file a Form SS-4 with the Internal Revenue Service in order to obtain a tax

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identification number. The applicant is required to sign the form SS-4 under penalties of perjury. The tax identification number will be issued by the Internal Revenue Service if the information requested on the Form SS-4 is supplied. The information required to be supplied by the entity on the Form SS-4, includes among other things the name of the principal officer, general partner, owner, grantor or trustor of the entity and the taxpayer identification number of such principal officer, general partner, owner, grantor or trustor of the entity.

Although the information provided on Form SS-4 is confidential, pursuant to IRC Section 6103(d), (e), (f), (h) and (i), upon request the information can be disclosed to persons having a material interest, federal, state and local law enforcement agencies and committees of Congress. If necessary, Congress could choose to expand the information requested on Form SS-4 to include beneficial ownership information. However, in the same way that beneficial ownership disclosure at the State level would create a massive State bureaucracy, such a system of beneficial disclosure through federal tax forms would likely create a massive and costly federal bureaucracy. While Delaware does not advocate this approach, it certainly is an option for federal policymakers to consider and one that would avoid a patchwork quilt of 51 different requirements in the states and District of Columbia.

The Bank Secrecy Act also requires financial institutions to comply with recordkeeping and reporting requirements involving certain financial transactions, including certain funds transfer and currency transactions, as well as transactions that are suspicious in nature, and provides law enforcement agencies with the means to trace the flow of illegal funds through the financial system. In order to comply with these recordkeeping and reporting requirements, financial institutions must obtain and retain certain customer identifying information

Revisions to the above-mentioned federal banking or tax laws (or any similar federal laws) may offer the best means for addressing the concerns about illegal activities identified in the Reports.

If there were to be a mandate to collect beneficial ownership information at the state level, we are concerned about the increased cost of collecting and assembling such data. Forms would need to be modified, computer systems reprogrammed, fees adjusted to handle increased labor costs associated with reviewing documents for compliance, increased costs for storage and retention of documents and increased demand for information retrieval and reporting. If such information were required to be maintained by lawyers, accountants, company formation businesses and/or registered agents, the costs would simply be passed on to private industry which would recover the costs in the form of possibly substantially higher representation fees. Also, policy makers would have to consider whether such a mandate would need to be accompanied by a prohibition on self-representation – since it would be impossible to verify whether such beneficial ownership records were being maintained by self-represented entities.

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We are also deeply concerned about privacy and disclosure issues. If such a mandate were to place personal identifying information of tens or perhaps hundreds of millions of equity holders on the public record, it would create a huge risk of identity theft. Similar security issues would be raised if such information were not on the public record, but required to be maintained in the files or databases held by lawyers, accountants and company formation agents. Traditionally the owners of private businesses engage in entrepreneurial and investment activity with the expectation of complete privacy. Even SEC regulations permit shareholders to accumulate positions in large publicly traded organizations without disclosure up to a certain percentage. If the ownership of every investment in the United States is entered into massive databases, it certainly presents countless public policy concerns and issues with respect to privacy, security, and insider trading to name a few.

But perhaps the single greatest concern for the State of Delaware is the likelihood that the role of Delaware and, indeed the United States, would shift from that of providing an attractive investment environment for domestic and international capital to one of having regulatory or investigative oversight of equity holders of legal entities. In light of the various challenges and tremendous costs – both financial and economic – that would be associated with attempting to track beneficial ownership of more than 15 million legal entities registered in the nation's 51 jurisdictions, it is unlikely that the State of Delaware would support legislation requiring full beneficial ownership disclosure.

Instead, we believe that any additional reforms at the federal or State level are best focused on enhancing the ability of federal and state officials to "follow the money" through the financial services system, providing law enforcement with the resources to investigate alleged illicit activities and seeking to deter such activity in the first place. This is why we believe Delaware's recent amendments establishing more demanding requirements for Commercial Registered Agents are a step in the right direction and deserve the consideration of other jurisdictions.

The State of Delaware is keenly aware that we are but one of many stakeholders in this issue. In fact, the persons most affected by any reforms are businesses both here and abroad. We believe that any discussion of beneficial ownership disclosure requires input and comment from the persons who will be most affected by such regulations – namely large, medium and small businesses and investors. Perhaps hundreds of millions of individuals in the United States are beneficial holders of public and privately held for-profit and charitable organizations and would be affected by beneficial ownership disclosure. It is critically important to ensure that their voices are heard regarding the costs and benefits of such a system.

On behalf of the State of Delaware, I thank you for this opportunity to share our comments and I look forward to responding to any questions you may have.

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State of North Carolina
Department of the Secretary of State

ELAINE F. MARSHALL
SECRETARY OF STATE

July 2, 2009

The Honorable Carl Levin
United States Senate
Washington, DC 20510

Dear Senator Levin:

On behalf of my colleagues at the National Association of Secretaries of State (NASS), I would once again like to thank you for the opportunity to offer the perspective of state officials on the possible impact of S.569, the Incorporation Transparency and Law Enforcement Assistance Act.

Pursuant to my testimony of June 18, 2009, before the Committee on Homeland Security and Governmental Affairs, I am submitting this letter to you with additional information on the projected costs for North Carolina to implement S.569. Since the true cost of implementation of this law cannot be accurately forecast until administrative rulemaking is complete, the numbers provided in my testimony and in this letter are truly an estimate.

The following totals are based on the following assumptions: (1) that the database created in the Secretary of State's office would have a high level of security and segregation from other data due to the confidential and sensitive nature of the information reported; (2) that an additional nine (9) FTEs would be required to perform additional duties required by the bill; and (3) that the cost for software reprogramming estimated here is much less that other Secretaries of State would encounter since most Secretaries do not have in-house programming capabilities as we do. Given the foregoing, we estimate that there will be a one-time start up cost of $340,000 and an annual recurring amount of $456,500 necessary to carry out the requirements of this legislation.

Since the day of my testimony, I realized that the recurring cost estimate quoted above does not take into account the significant postal budget required to communicate with hundreds of thousands of entities in North Carolina on a yearly basis. Therefore, assuming that at least one (1) first-class mailing would be necessary to contact each entity per year, with additional correspondence for at least fifty percent (50%) of entities, an additional $575,000 should also be included in the annual recurring requirements for implementation of this legislation, with a new revised total of $1,031,500 recurring costs.

Once again, thank you for the opportunity to participate in the discussions of this issue; NASS appreciates the attention of you and the Committee to our concerns and looks forward to working together in a spirit of cooperation. If you need any further information, please contact me at (919) 807-2005.

Sincerely,

Elaine F. Marshall

Elaine F. Marshall

PO Box 29622
Raleigh NC 27626-0622

website: www.sosnc.com

Telephone (919) 807-2005
Facsimile (919) 807-2010

State Survey on Cost Estimates for Implementing S.569 as of June 30, 2009

After conducting a review of S.569, the Incorporation Transparency and Law Enforcement Assistance Act, NASS asked the states to estimate the financial impact of S.569.

- S.569 would currently impact the information you collect for non-publicly traded corporations and limited liability companies. However, S.569 also requires the federal government to conduct a study within a year of implementation to determine if partnerships, trusts and other legal entities should be included.

  _____ How many corporations and LLCs would be impacted in your state?

  _____ If the categories expand, how many entities could be impacted?

- S. 569 says that by the October 2012, states that receive Homeland Security grants (we have been told that all states do) would have to implement a system that can collect and store **all** beneficial ownership name and address info for each LLC and non-publicly traded corporation at the time of formation. To catch those that existed prior to October 2012, all LLC's and non-publicly traded corporations would also have to file an annual report listing updated beneficial owner name and address. If your state doesn't require annual reports for these entities, then the entity must file updated beneficial owner info every time there is a change. The state is required to maintain this info for the life of the entity and five years beyond the entity's termination. Any LLC or non-publicly traded company that has any beneficial owners that are not US citizens or lawful permanent residents of the US must have these individuals provide their name, address and passport for verification with a formation agent. This agent must provide a written certification to the state at the time of formation or when updating – whichever is relevant. Whether or not you keep the beneficial ownership information confidential would be an issue for state law. If confidential, then must provide access to law enforcement upon subpoena.

  Things to consider when calculating costs:
  - Do you have an online filing system for your entity formation process? What would be the costs for re-programming to collect beneficial ownership info? Can you accept attachments to accommodate certification by formation agents of any non-US citizen info re beneficial owners?
  - Do you have a paper filing process for entity formation? What would be the costs of redesigning forms and instructions? What would be the costs to expand the paper system to accommodate all beneficial ownership information? Do you have a digitizing process to convert paper to electronic files? What would be the costs to expand this system to account for all the new information being filed?

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(202) 624-3525 (202) 624.3527 Fax
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- Do you have an online filing system for annual reporting? If you don't require annual reports for these entities, what type of system will you develop to accept updated beneficial ownership info? If you do have annual reporting online, what would be the costs for reprogramming.? Can your online filing system accommodate attachments for certification by formation agents of any non-US citizen info re beneficial owners?
- Do you have a paper filing system for annual reporting? What would be the costs of expanding the paper system to accommodate all beneficial ownership information?
- Does your state law allow for confidential filings? Does your state currently redact certain information from filings? Would your system need to be redesigned to accommodate confidential filings? Would you need to maintain dual systems?
- Would you need to increase staffing to accommodate the changes required by S.569
- What would your public education costs be to inform public about what a beneficial owner is, what companies have to change their filings, when the filings need to be changed, what information needs to be included and penalties for non-compliance? Public education campaign development costs, printing costs, mailing costs?

Total **Estimate** for Implementing S.569 the Incorporation Transparency and Law Enforcement Assistance Act

	Corporations/LLC's Affected	Entities Affected if Conditions Expand	Implementation Cost Estimate	Ongoing Cost Estimate
California	1,304,550	1,413,281	$17,500,000	$4,500,000
Connecticut			$540,000	$270,000
Florida	1,228,854	1,263,683	$1,667,848	$932,648
Indiana	350,000	350,000	$150,350	
Kansas	120,000	150,000	$600,000	$300,000
Kentucky	110,000	114,500	$150,00	$50,000
Montana	123,453	125,304	$402,000	
Nebraska	74,136	79,733	$185,260	
Nevada			$5,000,000-$6,000,000	$500,000-$600,000
North Dakota	28,900	33,177	$350,000	$75,000
Pennsylvania	929,409	982,602	$868,123	
South Dakota	39,653	56,612	$750,000	
Texas	896,578	1,041,527		
Utah	214,407	330,973	$230,000	
Washington	300,000	450,000	$14,925,124	$452,124
Wyoming	53,777	60,577	$1,030,984	$183,600

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(202) 624-3525 (202) 624.3527 Fax
www.nass.org

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Defending Liberty
Pursuing Justice

Thomas M. Susman
Director
Governmental Affairs Office

AMERICAN BAR ASSOCIATION
740 Fifteenth Street, NW
Washington, DC 20005-1022
(202) 662-1760
FAX: (202) 662-1762
SusmanT@staff.abanet.org

June 30, 2009

The Honorable Joseph Lieberman
Chairman
Committee on Homeland Security and Governmental Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing on behalf of the American Bar Association regarding the June 18, 2009 hearing on S. 569, the "Incorporation Transparency and Law Enforcement Assistance Act," and respectfully request that you include this letter in the record of the hearing.

The ABA supports all reasonable and necessary domestic and international efforts to combat money laundering, tax evasion, and terrorist financing. However, the ABA opposes enactment of S. 569. Enclosed please find ABA Resolutions 300 (August 2008) and 104 (February 2003), which further outline the ABA's opposition to S. 569 specifically, as well as to any legislation that purports to impose government-mandated suspicious activity reporting (SAR) obligations on the legal profession.

With respect to S. 569, the ABA is specifically concerned with two aspects: the federal mandates regulating state incorporation practices and the creation of a new group of "financial institutions" known as "formation agents" that could include lawyers. The ABA has, ever since the passage of Resolution 104 in 2003, consistently objected to government-mandated reporting obligations for the legal profession, where the reporting would be triggered by suspicion. The Association also reiterated its concerns regarding SAR requirements in Resolution 300, passed in August 2008.

The ABA is concerned that S. 569 would create new federal mandates and regulation of state incorporation practices. The legislation requires states to maintain beneficial ownership information; such information must be obtained, kept current, and made available to law enforcement authorities by the states upon request or subpoena. The ABA recognizes the need for improvement in company formation processes and increased visibility of persons forming nonpublic entities in the United States, but believes that federal legislation regulating this aspect of state incorporation practice is premature and is not the most effective means for addressing the threat of money laundering and terrorist activities in the U.S.

The Permanent Subcommittee on Investigations, through a series of hearings and investigations into tax abuse havens, and the Financial Action Task Force's (FATF) mutual evaluation of the United States have both expressed strong concerns that the U.S. company

formation process is at risk for exploitation by money launderers, tax evaders and terrorist financiers. As the ABA understands the problem identified by S. 569 and by FATF's mutual evaluation, law enforcement often is unable to locate the beneficial owners of privately held entities. Consequently, money laundering, tax evasion, and terrorist financing investigations are difficult to resolve, and the U.S. financial sector is at a heightened risk for abuse. However, S. 569 would impose undue burdens on state authorities and legitimate businesses at a time when the U.S. financial system and the domestic economy are under severe stress.

Despite objections to S. 569, the ABA is supportive of efforts to combat money laundering that do not infringe upon state sovereignty. Alternatives such as the Uniform Law Enforcement Access to Entity Information Act (Uniform Act) are being developed; this legislation holds the potential of providing law enforcement with the necessary information identifying the record owners and key officers of non-publicly traded entities formed under state law. While the ABA has not formally endorsed the Uniform Act, we believe that effective state laws and proposals like the Uniform Act could obviate the need for federal regulation of business entities while still meeting the requirements of FATF's Recommendation 33 (requiring countries to take measures to prevent the unlawful use of legal persons by money launderers).

In addition to our concerns about federal encroachment on states, the ABA also objects to Section 4 of S. 569. Section 4 would establish a new class of "financial institutions" under U.S. anti-money laundering law, covering "any person involved in forming a corporation, limited liability company, partnership, trust, or other legal entity" (formation agents). These formation agents would then be required to adopt certain enhanced anti-money laundering compliance mechanisms, much like U.S. banks have done, in order to detect possible money laundering activities in the formation of entities. While not explicit on its face, the definition of formation agents would appear to include lawyers involved in establishing entities. This legislation would therefore, for the first time, impose new, enhanced, anti-money laundering compliance requirements on the legal profession and would treat lawyers as if they were banks. This treatment is not warranted, nor does it make sense in light of the obvious distinctions between large financial institutions, the resources at their disposal, and their handling of money transactions, as compared to solo practitioners and law firms.

Moreover, designation of formation agents as financial institutions could potentially impose SAR requirements on the legal profession. The Treasury Department, pursuant to S. 569, could have the authority to impose such requirements on lawyers. Government-mandated SAR requirements could erode the attorney-client privilege and create conflicts between lawyers and their clients. A SAR requirement could also alter the client-lawyer relationship, as lawyers would no longer be acting independently of the state and in the best interests of their clients. These requirements could conflict with ethical obligations of lawyers under state confidentiality laws and could create inherent conflicts between lawyers and their clients; that is, lawyers could be acting as informants under pain of criminal prosecution (for failure to file a SAR), and would therefore be required to place their own interests ahead of their clients. Lawyers also would be prohibited from informing their clients of any such reports, creating an even more untenable conflict situation. Therefore, the ABA opposes imposing federally mandated SAR obligations on the legal profession. We have voiced these

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objections to the Department of Justice, the Department of the Treasury, and FATF. The concerns underlying the ABA position are shared by legal professionals around the world. Indeed, these types of concerns were at the heart of litigation in Canada successfully challenging the imposition of reporting requirements on Canadian lawyers.

At the same time, the ABA has been working diligently to enhance the ability of legal professionals to identify and avoid illicit money laundering activities. In coordination with the U.S. Treasury Department, FATF, and legal professionals throughout the world, the ABA is educating members of the legal profession on anti-money laundering and counter-terrorist financing compliance. FATF has been actively collaborating with specially designated non-financial businesses and professions, including lawyers, to develop a risk-based system to further minimize the risk that lawyers and other professionals would be used unwittingly by unscrupulous clients to launder illegally obtained money. The ABA and members of other U.S. legal professional associations, along with our counterparts in the United Kingdom and elsewhere, participated extensively in this effort, attending numerous meetings with FATF officials and assisting in the preparation of the draft guidance on client due diligence to avoid money laundering and terrorist financing risks. The FATF adopted and issued this guidance in October 2008. Through the efforts of members of the ABA Task Force on Gatekeeper Regulation and the Profession, as well as others in the ABA, the American College of Trust and Estate Counsel, the American College of Real Estate Lawyers, the American College of Mortgage Attorneys, and other professional organizations in the U.S., additional voluntary good practices guidance on client due diligence is being prepared in consultation with members of the U.S. Department of the Treasury. Members of the ABA active in this area continue to disseminate education material to the profession at large. (See, e.g., Kevin Shepherd, "Guardians at the Gate: The Gatekeeper Initiative and the Risk Based Approach for Transactional Lawyers," 43 Real Property, Trust and Estate Law Journal, no. 2 (Winter 2009).) The ABA will continue to be active in this area and is working to enhance anti-money laundering compliance awareness within the legal profession.

The American Bar Association appreciates the Committee's efforts to combat money laundering and terrorist financing activity. While opposed to premature federal legislation, the ABA will continue to support state efforts countering these illegal activities in ways that minimize the impact on our economy and state regulators. We look forward to working with you on developing a comprehensive solution that addresses the mutual objectives of all concerned.

Sincerely,

Thomas M. Susman

Enclosures

cc: Members of Homeland Security and Governmental Affairs Committee

104

AMERICAN BAR ASSOCIATION

ADOPTED BY THE HOUSE OF DELEGATES
February 10-11, 2003

RESOLVED, That the American Bar Association supports the enactment of reasonable and balanced initiatives designed to detect and prevent domestic and international money laundering and terrorist financing.

FURTHER RESOLVED, That any efforts to establish and implement international and United States policies to combat domestic and international money laundering and terrorist financing should be consistent with the following principles:

(1) lawyers play a critical and independent role in the administration of justice and in ensuring lawful compliance by persons and entities involved in commercial and financial activities;

(2) the judiciary and the organized bar are responsible for establishing ethical rules governing the activities of lawyers and for ensuring that the profession adheres to the highest standards of professional and lawful conduct; and

(3) there is a critical need for confidentiality in client communications with lawyers to ensure the independence of the bar, protect the lawyer-client relationship, and support the proper functioning of the legal system;

FURTHER RESOLVED, That the American Bar Association:

(1) opposes any law or regulation that, while taking action to combat money laundering or terrorist financing, would compel lawyers to disclose confidential information to government officials or otherwise compromise the lawyer-client relationship or the independence of the bar; and

(2) will continue to review the Model Rules of Professional Responsibility and evaluate whether the rules permitting, in appropriate circumstances, disclosure of confidential information should be modified to permit disclosure of information demonstrating the clear intent of a client to commit criminal acts such as money laundering; and

(3) urges bar associations and law schools to undertake education efforts to ensure that lawyers are informed regarding the scope of money laundering laws and the anti-money laundering requirements that apply to lawyers to safeguard the profession from being used to facilitate money laundering or terrorist financing activity.

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AMERICAN BAR ASSOCIATION

ADOPTED BY THE HOUSE OF DELEGATES

AUGUST 11-12, 2008

RECOMMENDATION

RESOLVED, That the American Bar Association supports all reasonable and necessary efforts of the United States government and the international community to combat money laundering and terrorist financing activity in the international financial system;

FURTHER RESOLVED, That the American Bar Association urges that the regulation of those involved in the formation of business entities within the states and territories of the United States should remain a matter of state and territorial law and state sovereign prerogative, with a minimum of federal governmental regulation;

FURTHER RESOLVED, That the American Bar Association urges Congress to refrain from enacting legislation that would regulate lawyers in the formation of business entities and to defer to the states as they consider amendments to the Model Business Corporation Act, Uniform Partnership Act, Uniform Limited Partnership Act, Uniform Limited Liability Company Act, and Uniform Limited Cooperative Association Act (collectively, the "Entity Paradigm Laws") proposed by the American Bar Association, the National Conference of Commissioners on Uniform State Laws, and others;

FURTHER RESOLVED, That the American Bar Association urges that the manner in which lawyers conduct client due diligence for purposes of rendering legal services and the manner in which record or beneficial ownership of business entities is documented, verified, and made available to law enforcement authorities, not conflict with the ethical requirements and regulations imposed by state authorities on the legal profession, be risk-based, and take into account:

(1) the actual risk of money laundering and terrorist financing in the formation of business entities; and

(2) the burdens that such requirements or regulations might impose on state and territorial authorities, those involved in the formation of such entities, and the bona fide investment community; and

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FURTHER RESOLVED, That the American Bar Association urges state and local bar associations, and other appropriate constituencies within the legal profession, with the assistance of the ABA Task Force on Gatekeeper Regulation & the Profession, to develop appropriate guidance on adopting voluntary risk-based approaches to client due diligence that will inform legal professionals of the risks of money laundering and terrorist financing, and assist them in taking appropriate steps for compliance with anti-money laundering and anti-terrorist financing legal requirements.

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REPORT

I. Executive Summary

The American Bar Association's Task Force on Gatekeeper Regulation and the Profession ("Task Force") was formed over five years ago to address certain issues arising from increased interest among U.S. government and foreign regulatory officials in combating money laundering and terrorist financing and enlisting the assistance of certain professionals, including lawyers, in this effort ("Gatekeeper Initiative"). Two recent developments affecting the Gatekeeper Initiative require that the American Bar Association adopt policy to address concerns with these developments.

Federal legislation was proposed in May 2008 to require those who form unincorporated business entities, trusts, partnerships, and other organizational structures to document, verify, and make available to law enforcement authorities the record and beneficial ownership of these business entities. This legislation would impose significant and difficult burdens on company formation agents (including lawyers in some circumstances), state authorities, and others to comply with this legislation. States, and not the federal government, should retain the authority to regulate those who form these business entities. Amendments to certain uniform and model laws relating to the formation of these business entities are currently under review to address concerns raised by law enforcement officials and policy makers. These amendments would render the proposed federal legislation unnecessary, and they represent a more efficient way to address regulatory concerns without unduly burdening state authorities, those involved in the formation of business entities, and bona fide businesses themselves.

The second development relates to recent efforts by the Financial Action Task Force ("FATF") to adopt a risk-based approach to client due diligence in the delivery of legal services. FATF is collaborating with certain designated non-financial businesses and professions, including lawyers, to develop voluntary risk-based guidance for legal professionals. FATF expects to adopt this guidance at its October 2008 plenary meeting. Assuming this guidance is adopted, U.S. lawyers should work to develop voluntary risk-based guidance for client due diligence. The proposed recommendation will allow the American Bar Association to develop this voluntary guidance for one or more of its constituent sections and to engage with the federal government and other interested parties in this process. Absent this voluntary guidance, it is possible that federal regulators and lawmakers may impose a rules-based approach on the legal profession, thereby triggering significant issues with regard to the attorney-client privilege, the duty of client confidentiality, the attorney-client relationship, and the delivery of legal services more generally.

II. Background on the Gatekeeper Initiative

The Gatekeeper Initiative originates from the Moscow Communiqué issued at the 1999 meeting of the G-8 Finance Ministers. It calls upon countries to consider various means to address

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money laundering through the efforts of professional gatekeepers of the international financial system, including lawyers, accountants, company formation agents, and others.

In recent years, the fight against money laundering has gained importance in the priorities of many countries. Moved by the FATF, the leading global organization in the fight against money laundering, governments from countries that comprise the principal financial centers have worked collaboratively to identify money laundering typologies, develop recommendations on best practices to combat money laundering, criminalize money laundering around the world, and encourage cooperation among national law enforcement and regulation agencies. Following the Moscow Communiqué, FATF created a working group that has identified several professions as "gatekeepers" with respect to money laundering. On May 31, 2002, FATF published a consultation paper entitled "Review of the FATF 40 Recommendations" in which the FATF identified several areas where possible changes could be made to the FATF anti-money laundering framework. The broad topics covered concern customer due diligence and suspicious transaction reporting ("STR"), beneficial ownership and control of corporate vehicles, and the application of anti-money laundering obligations to non-financial businesses and professions, including the legal profession.

In the United States, the Money Laundering and Financial Crime Strategy Act of 1998 obligates the U.S. Departments of Justice and Treasury to issue an annual "National Money Laundering Strategy Report," outlining a plan of action to enhance U.S. anti-money laundering efforts. The report for 2000 tasked the Justice Department with reviewing the professional responsibilities of lawyers and making recommendations "ranging from enhanced professional education, standards, or rules, or legislation, as may be needed." A similar theme was set forth in the report for 2001. An inter-agency working group was established, including the Department of Justice, the Department of Treasury, the Securities and Exchange Commission, and Treasury's Financial Crimes and Enforcement Network ("FinCEN"). This inter-agency group is charged with developing a U.S. position on the Gatekeeper Initiative.

III. Gatekeeper Task Force

A. Background

The Task Force was created in February 2002 by ABA President Robert E. Hirshon to address the Gatekeeper Initiative. The mission of the Task Force is to respond to initiatives by the U.S. Department of Justice, U.S. Department of the Treasury, the Congress, the Financial Action Task Force ("FATF"), and others that will impact on the attorney-client relationship in the context of anti-money laundering enforcement. The Task Force reviews and evaluates ABA policies and rules regarding the ability of attorneys to disclose client activity and information, and works to develop positions on the Gatekeeper issue. The Task Force also develops educational programs for legal professionals and law students, and organizes resource materials to allow lawyers to comply with their anti-money laundering responsibilities. At the time the Task Force was established, the principal focus of the Task Force with regard to U.S. anti-money laundering policy was whether the U.S. government would impose a mandatory STR requirement on lawyers – i.e., filing with U.S. government regulators or law enforcement personnel reports on suspicious activity by clients, and being prohibited from informing clients that such a report had been filed (the so-called "no tipping off" rule). This would have made lawyers subject to

reporting obligations that are similar to what banks and other financial institutions have with regard to reporting suspicious financing transactions to FinCEN.

B. Efforts

In response to concerns with the imposition of the STR requirement on the U.S. legal profession, in February 2002, the ABA Criminal Justice Section proposed a recommendation before the ABA House of Delegates that stated "That the American Bar Association urges the United States government to seek to protect and uphold the attorney/client relationship, including the attorney/client privilege, in dealing with international money laundering."

In addition, in February 2003, the Task Force, together with the Section of Real Property, Probate and Trust Law (now the Section of Real Property, Trust and Estate Law), the Criminal Justice Section, the Section of Litigation, and the Section of International Law, submitted a Recommendation and Report to the House of Delegates with regard to the Gatekeeper Initiative. The Recommendation supported the enactment of reasonable and balanced initiatives to detect and prevent money laundering and terrorist financing. At the same time, the Recommendation opposed any law or regulation that would compel lawyers to disclose confidential information to government officials or otherwise compromise the attorney-client relationship of independence of the bar. The Recommendation also noted that the Model Rules of Professional Responsibility would continue to be reviewed as they relate to the obligations of lawyers to maintain client confidences, and urged bar associations and law schools to undertake educational efforts with regard to money laundering risks and concerns.

The Report accompanying this recommendation explained the appropriate role of lawyers in U.S. government efforts to combat money laundering; analyzed the legal and ethical problems arising from any mandatory reporting obligation to the U.S. government to reveal client information that involves a "suspicion" of possible money laundering or other criminal activity; and discussed existing legal and ethical requirements that minimize the risk that lawyers will be involved in money laundering activities.

Since that time the Task Force has been involved in encouraging lawyer educational programs with regard to anti-money laundering risks and compliance more generally; with continuing a dialogue with the U.S. government and the FATF concerning the imposition of STR and other anti-money laundering requirements on the legal profession; and liaising with other U.S. and non-U.S. bar associations and legal professional organizations concerning government policy and the work of the FATF regarding the role of the legal profession in preventing money laundering and terrorist financing.

IV. Lack of Beneficial Ownership Information for Law Enforcement – Background

One issue that has recently arisen with regard to the legal profession concerns the possible abuse of trusts and other forms of business organization by persons involved in illegal activity. Specifically, there has been an increasing concern with undisclosed owners or beneficiaries of such corporate entities who might be establishing such entities in order to pursue illegal objectives, such as tax evasion or money laundering. While the focus on identifying "beneficial

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ownership" information for all companies formed within the United States is rooted in the FATF's efforts over the last nine years, a more recent focus has arisen as a result of legislation proposed by Senator Levin in his capacity as Chairman of the Permanent Subcommittee on Investigations for the Homeland Security Committee and FATF Recommendation 33.

A. The Financial Action Task Force

The FATF is an inter-governmental body whose self-described purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing. The FATF describes itself as "a policy-making body which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas."[1] To this end, the FATF monitors members' progress in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally. In performing these activities, the FATF collaborates with other international bodies involved in combating money laundering and terrorist financing.

Prior to September 11, 2001, the FATF was primarily focused on anti-money laundering and issued the Forty Recommendations (the "Recommendations")[2] to provide a set of counter-measures against money laundering. The Recommendations cover a wide range of topics, such as an effective criminal justice system and law enforcement procedures to combat money laundering, the type of structure and mechanisms for effective regulation of a country's financial system, and international co-operation. These Recommendations have been endorsed or adopted by many international bodies and are designed to allow countries a certain flexibility in implementing these principles according to their particular circumstances and constitutional frameworks. Though not a binding international convention, many countries (including the United States) have made a political commitment to combat money laundering by implementing the Recommendations.[3]

1. Recommendation 33

FATF Recommendation 33 provides the impetus for much of the current activity to amend entity formation and beneficial ownership laws. Recommendation 33 addresses the exploitation of

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[1] *See* Financial Action Task Force on Money Laundering, *The Forty Recommendations* (Oct. 22, 2004), *available at* http://www.oecd.org/dataoecd/7/40/34849567.PDF.

[2] Initially developed in 1990, the Recommendations were revised for the first time in 1996 to take into account changes in money laundering trends and to anticipate potential future threats. More recently, the FATF has completed a thorough review and update of the Forty Recommendations (2003). The FATF has also elaborated various Interpretative Notes that are designed to clarify the application of specific Recommendations and to provide additional guidance. *See* Forty Recommendations *available at*: http://www.fatf-gafi.org/document/28/0,3343,en_32250379_32236930_33658140_1_1_1_1,00.html.

[3] After September 11, FATF revised its focus to also include counter-terrorist financing provisions. These take the form of the additional Nine Special Recommendations. *See* Nine Special Recommendations on Terrorist Financing *available at* http://www.fatf-gafi.org/document/9/0,3343,en_32250379_32236920_34032073_1_1_1_1,00.html.

legal persons by money launderers and identifies as the solution to such abuse a need for complete and accessible information about beneficial ownership.[4] The Recommendation reads:

> Countries should take measures to prevent the unlawful use of legal persons by money launderers. Countries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities. In particular, countries that have legal persons that are able to issue bearer shares should take appropriate measures to ensure that they are not misused for money laundering and be able to demonstrate the adequacy of those measures. Countries could consider measures to facilitate access to beneficial ownership and control information to financial institutions undertaking the requirements set out in Recommendation 5.[5]

FATF defines "beneficial owner" as "the natural person(s) who ultimately owns or controls a customer and/or the person on whose behalf a transaction is being conducted," as well as "those persons who exercise ultimate effective control over a legal person or arrangement."[6]

2. FATF Report: Methodology for Assessing Compliance with the Forty Recommendations and the FATF 9 Special Recommendations

To aid countries in their attempts to comply with the Recommendations, FATF issued a report outlining how it assesses compliance with each Recommendation.[7] Regarding Recommendation 33, FATF identified three "examples of mechanisms" that countries could use to ensure they had adequate transparency concerning beneficial ownership and control of legal persons.[8] The report advised that "these mechanisms are, to a large degree, complementary and countries may find it highly desirable and beneficial to use a combination of them."[9] The identified mechanisms are:

1. A system of central registration (or up front disclosure system) where a national registry records the required ownership and control details for all companies and other legal persons registered in that country. The relevant information could be either publicly available or only available to competent authorities. Changes in ownership and control information would need to be kept up to date.

2. Requiring company service providers to obtain, verify and retain records of the beneficial ownership and control of legal persons.

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[4] *See id.* at 9.

[5] FATF, *Recommendations*, at 9.

[6] FATF, *Key Topics, 40 Recommendations Glossary, available at* http://www.oecd.org/glossary/0,3414,en_32250379_32236889_35433764_1_1_1_1,00.html#34276864.

[7] *See* FATF, *Methodology for Assessing Compliance with the FATF 40 Recommendations and the FATF 9 Special Recommendations* (February 2008), *available at* http://www.oecd.org/dataoecd/16/54/40339628.pdf.

[8] *Id.*

[9] *Id.*

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3. Relying on the investigative and other powers of law enforcement, regulatory, supervisory, or other competent authorities in a jurisdiction to obtain or have access to the information.[10]

Furthermore, FATF explained that "whatever mechanism is used it is essential that: (a) competent authorities are able to obtain or have access in a timely fashion to the beneficial ownership and control information, (b) the information is adequate, accurate and timely, and (c) competent authorities are able to share such information with other competent authorities domestically or internationally."[11] Therefore, it would seem that a country could use any one of the three example mechanisms, or a combination thereof – so long as these three results are attained.

3. FATF Mutual Evaluation Report: United Kingdom

FATF teams perform mutual evaluations of each country's compliance with the Recommendations, and produce reports providing additional guidance on FATF's expectations for each respective country.

FATF evaluated the United Kingdom ("UK") in 2007 and rated its programs regarding beneficial ownership and transparency in corporate formation as "partially compliant."[12] FATF's explanation of the UK's program noted the UK's requirement that all limited companies and limited liability partnerships must provide to a national registry a full list of their shareholders or partners, contact information, and information about the company's registered office.[13] Furthermore, the report stated that the UK had, in 2002, considered a system requiring up-front disclosure of beneficial ownership and determined that a cost-benefit analysis counseled against its implementation.[14] FATF stated that "the UK system for access to beneficial ownership and control information of legal persons basically relies upon investigatory powers available to law enforcement."[15]

The evaluation team did have a number of concerns, including "concerns regarding the possibility to use nominee shareholders who would appear on public record at the company registry instead of the real beneficial owner", as well as similar concerns that legal persons acting as company directors or shareholders would mean that investigators would need to pursue a chain of entities before reaching the ultimate beneficial owner.[16] There were also concerns regarding the accuracy of information and the use of share warrants to a "bearer".[17] FATF recommended that the UK bring company formation agents into an anti-money laundering

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[10] *Id.*

[11] *Id.*

[12] *See* FATF, *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: The United Kingdom of Great Britain and Northern Ireland* at 292 (June 29 2007), *available at* http://www.oecd.org/dataoecd/55/29/39064399.pdf.

[13] *Id.* at 231.

[14] *Id.* at 234.

[15] *Id.* at 236.

[16] *Id.* at 231.

[17] *Id.* at 236.

compliance regime.[18] However, FATF recognized that improvements were soon to be made to the UK system, and recognized as among these improvements a new UK legal requirement that at least one director be a natural person and the reporting of a usual residential address and a service address for directors.[19]

4. FATF Mutual Evaluation Report: United States

In 2006, FATF conducted an evaluation of the United States' compliance with the FATF Recommendations, and found the U.S. "non-compliant" with Recommendation 33,[20] giving the United States until July 2008 to make progress toward compliance.[21] In its "Summary of Factors Underlying Ratings," the Mutual Evaluation Report of the U.S. identified two factors contributing to the "non-compliant" rating:

- While the investigative powers are generally sound and widely used, there are no measures in place to ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities.

- There are no measures taken by those jurisdictions which permit the issue of bearer shares to ensure that bearer shares are not misused for money laundering.[22]

Additionally, the FATF criticized the United States for its lack of available information for private companies registered within its borders.[23] In its recommendations, the FATF stated that "the proposal [from FinCEN] to bring company formation agents within the [Bank Secrecy Act] framework, and to require them to implement [anti-money laundering programs] and [Customer Identification Procedures] should be taken forward in the very near future."[24]

5. FATF Guidance for Non-Financial Businesses

FATF also issued guidance on its recommendation to apply anti-money laundering regulations to non-financial businesses and professions ("DNFBPs"), such as lawyers. On May 30, 2002, FATF issued a "Consultation Paper" outlining various options for strengthening national anti-money laundering measures and sought comments on those options.[25] As noted in the introduction, the

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[18] *Id.*

[19] *Id.* This acknowledgment is a significant point as to why the amendments to the Entity Paradigm Laws discussed below adequately address the FATF Recommendation 33 while obviating the need for federal legislation.

[20] *See* Financial Action Task Force, *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism* (June 23, 2006), *available at* http://www.oecd.org/dataoecd/44/9/37101772.pdf.

[21] *Introducing the Incorporation Transparency and Law Enforcement Assistance Act*, 110th Cong. (May 1, 2008) (statement of Sen. Carl Levin, S. Comm. on Homeland Sec. and Gov't Affairs).

[22] *Id.*

[23] The Financial Action Task Force, Mutual Evaluation Report: United States (June 23, 2006). Published at http://www.fatf-gafi.org/dataoecd/44/9/37101772.pdf.

[24] Mutual Evaluation Report at 308.

[25] *See* Financial Action Task Force on Money Laundering, *Review of the FATF Forty Recommendations: Consultation Paper*, May 30, 2002.

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Consultation Paper proposed that certain anti-money laundering measures be extended to lawyers including (1) increased regulation and supervision of the profession, (2) increased due diligence requirements on clients, (3) new internal compliance training and record-keeping requirements for lawyers and law firms, and (4) new STR requirements mandating that lawyers report to a government enforcement agency or a self-regulatory organization ("SRO") information that triggers a "suspicion" of money laundering relating to a client activity. Furthermore, the Consultation Paper indicated that lawyers would be prohibited from informing their clients when an STR has been filed with the government. The Consultation Paper proposed that the STR requirement be enforced through criminal, administrative or other sanctions.[26]

While the Consultation Paper recommended the imposition of such regulations, it also established the framework for a certain amount of flexibility by providing a number of "options" for countries to choose from when developing their individual anti-money laundering system. The Consultation Paper also acknowledged the special role played by the legal profession and recognized that lawyers would be under no obligation to report in instances where attorney-client privilege would be implicated. As noted above, the ABA passed a resolution in February 2003 opposing any mandatory STR obligation that would compromise the confidentiality of client information or adversely affect the attorney-client relationship in the U.S. justice system.

B. The Senate Committee on Homeland Security and Governmental Affairs

The United States Senate Committee on Homeland Security and Governmental Affairs, Permanent Subcommittee on Investigations ("PSI") held a series of hearings beginning in 2001 that investigated the role of domestically and internationally formed private companies and the role those entities play in U.S. tax evasion, money laundering, and terrorist financing. In each of these hearings, the presumption was that lack of information about underlying beneficial ownership impeded law enforcement investigations. Specifically,

- In 2001, the PSI examined "the historic and ongoing lack of cooperation by some offshore tax havens with international tax enforcement efforts and their resistance to divulging information needed to detect, stop and prosecute U.S. tax evasion."

- In December 2002, the PSI conducted an "in-depth examination of an abusive tax shelter used by Enron."

- In November 2003, the PSI held hearings looking into "how accounting firms, banks, investment advisors, and lawyers have become engines pushing the design, sale and implementation of abusive tax shelters to corporations and individuals across the country."

- In August 2006, the PSI held hearings covering "case histories on the use of offshore trusts and corporations to circumvent U.S. tax, securities and anti-money laundering laws."

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[26] Id., at p. 103.

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- In November 2006, the PSI held a hearing to examine "the issue of states routinely incorporating hundreds of thousands of new, non-publicly traded companies in the United States each year without obtaining the identity of the corporate owners, thereby impeding law enforcement investigations into persons misusing U.S. shell corporations for money laundering, tax evasion, terrorist financing, or other crimes." The hearing featured the April 2006 GAO report prepared at the Subcommittee's request, "Company Formations: Minimal Ownership Information Is Collected and Available." Published at http://hsgac.senate.gov/index.cfm?Fuseaction=Hearings.Home.

- In July 2008, the PSI held a hearing on Tax Haven Banks and U.S. Compliance to examine "how financial institutions located in offshore tax havens . . . may be engaged in banking practices that could facilitate, and in some instances have resulted in, tax evasion and other misconduct by U.S. clients. The hearing will also examine how U.S. domestic and international tax enforcement efforts could be strengthened."

As a result of these findings, on February 17, 2007, Senators Levin, Coleman and Obama proposed S. 681 (Stop Tax Haven Abuse Act) that *inter alia*, proposed to subject persons involved in the formation of companies to anti-money laundering program requirements of the Bank Secrecy Act.[27] Section 203 of S. 681 would have amended the definition of "financial institution" to include a new category, namely "corporate formation agents", in the Bank Secrecy Act to include "persons involved in forming new corporations, limited liability companies, partnerships, trusts, or other legal entities." This new category was broad enough to include, among others, lawyers and any other person even tangentially involved in the process (including secretaries of state).

In response, various industry groups involved in entity formation including the ABA's Business Law Section, the ABA Committee on Corporate Laws, the National Conference of Commissioners on Uniform State Law ("NCCUSL"), the National Association of Secretaries of State, the National Conference of State Legislatures, the International Association of Commercial Administrators, and Association of Registered Agents began to work together with representatives from the Department of Justice's Asset Forfeiture and Money Laundering Section in the Criminal Division, the Department of the Treasury's Office of Terrorist Financing, the Office of Foreign Assets Control ("OFAC") and FinCEN to discuss entity formation laws, to understand the type of information sought by law enforcement in their respective investigations, and to offer to work together to resolve law enforcement's information gathering issues through a means other than federal legislation. These industry groups worked with Treasury to draft amended entity laws that would require privately held entities to maintain ownership information and make it readily accessible to law enforcement.

Although most of the parties involved believed that progress was being made to address the issues identified by the FATF, the GAO Reports, and the PSI, and thus new legislation would not

[27] See section 203 of S. 681, To Restrict the Use of Offshore Tax Havens and Abusive Tax Shelters to Inappropriately Avoid Federal Taxation, and for Other Purposes. Published at http://www.levin.senate.gov/newsroom/supporting/2007/PSI.OffshoreTaxBill.021707.pdf.

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be pursued, on May 1 2008, Senator Levin together with Senators Obama and Coleman, introduced S. 2956, largely an updated version of S. 681.

C. Current Efforts on the Hill: S. 2956

S. 2956 would require privately held entities to provide more extensive beneficial ownership information to state governments and law enforcement authorities. S. 2956 would require each applicant seeking to form a corporation or limited liability company ("LLC") to provide the state of formation with a list of its beneficial owners (including their names and current addresses). This list would have to be updated either annually or each time a change is made, and the states would be required to maintain this information for five years after the entity is terminated. This beneficial ownership information would be provided to law enforcement or a congressional committee upon service of a subpoena to the state. For foreign beneficial owners of an entity, additional information would have to be provided. This additional information would include a written certification by a formation agent that the agent has verified the name, address, and identity of each beneficial owner and a certification that the formation agent has obtained a copy of the beneficial owner's passport. The formation agent would be required to retain this information for a specified period of time and produce it upon request. Penalties to be imposed under the bill for the provision of false beneficial ownership information would include civil penalties of up to $10,000, imprisonment for up to three years, or both.

Section 4 of S. 2956 (much like section 203 of S. 681) would create a new category of "financial institution" under the Bank Secrecy Act – i.e., corporate formation agents defined to include "any person involved in forming a corporation, limited liability company, partnership, trust, or other legal entity." The legislation would require the Department of the Treasury to require corporate formation agents, defined broadly enough to include lawyers, to establish anti-money laundering programs to ensure that they are not forming corporations or LLCs for money launderers. To satisfy these programs, lawyers and their law firms involved in the formation of these types of business entities would be required to establish internal policies, procedures, and controls, designate a compliance officer, conduct ongoing employee training programs, and permit independent audit functions to test programs. Moreover, at some point in the future, STR and due diligence requirements could potentially be imposed under such a program.

For purposes of the legislation, "beneficial owner" is defined as "an individual who has a level of control over, or entitlement to, the funds or assets of a corporation or limited liability company that, as a practical matter, enables the individual, directly or indirectly, to control, manage, or direct the corporation or limited liability company." A "formation agent" is defined as "a person, who, for compensation, acts on behalf of another person to assist in the formation of a corporation or limited liability company under the laws of a state." The Bank Secrecy Act would be amended to impose anti-money laundering obligations on "any person involved in forming a corporation, limited liability company, partnership, trust, or other legal entity."

V. Drawbacks to Proposed Federal Legislation

A. Anti-Money Laundering Program Requirements for Entity Formation Agents (including lawyers)

To the extent that S. 681 and S. 2956 require those involved in the entity formation process to be incorporated under the Bank Secrecy Act Regulations, lawyers (and others) will be required to maintain anti-money laundering programs, which could in the future include the filing of STRs.[1] This latter requirement does not acknowledge the sanctity of the attorney-client privilege nor does it pose a reasonable solution to PSI's identified problem, whereby U.S. privately held entities can be abused by money launderers, tax abusers and terrorist financers. While all parties involved recognize the threat that money laundering, terrorist financing and tax evasion pose to the U.S. national security, it does not appear that S. 681 or S. 2956 resolves the problem effectively. In practice, S. 681 and S. 2956 impose an undue burden on U.S. businesses and persons involved in entity formation (including lawyers). Moreover, the combination of Entity Paradigm Laws (as identified in Section VI of this Report) and risk based guidance for legal professionals effectively addresses the problem of beneficial ownership without the undue burdens of S. 2956 and S. 681.

B. S. 681 May Draw the United States into WTO Case for discriminatory practices

S. 681 arguably violates the principle in Article II of the General Agreement on Trade in Services (GATS) that prohibits countries from discriminating among foreign trading partners on the basis of nationality and requires that rules and regulations be based on objective, nondiscriminatory criteria.[2] Enactment of S. 681 could result in additional litigation against the United States before the WTO.

The cumulative adverse impact of burdensome tax enforcement on foreign investment, more U.S. losses in the WTO as a result of U.S. discriminatory regulation, and a downturn in foreign investments – with little likelihood of actually addressing money laundering and terrorist financing abuse of the U.S. financial sector – are strong arguments in favor of opposing federal legislation as drafted and supporting the alternatives – including Risk-Based Guidance for Legal Professionals discussed in Section VI.

VI. Alternative to Federal Legislation

The ABA and NCCUSL, working together with private industry, with the secretaries of state and with Treasury's Office of Terrorist Financing, have been developing an alternative solution to the beneficial ownership issue identified by both the FATF and those sponsoring S. 681 and S. 2956. The ABA Committee on Corporate Laws has been preparing amendments to the Model Business Corporation Act and NCCUSL has been preparing amendments to the Uniform Partnership Act, Uniform Limited Partnership Act, Uniform Limited Liability Company Act, and Uniform Limited Cooperative Association Act (collectively, the "Entity Paradigm Laws").

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[1] The Treasury Department could take the position that it has the discretion to impose STR requirements on legal professionals without further legislative action or guidance.

[2] WTO Economic Research and Analysis Division, Special Studies 6, Market Access: Unfinished Business Post-Uruguay Round Inventory and Issues 99.

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The most recent version of the ABA amendments to the Model Business Corporation Act would require public disclosure of the directors and officers of a corporation throughout its existence. The provision that allowed "persons" to act as incorporators would be amended to require incorporators to be "individuals". The amendments further impose duties on the incorporator – an incorporator would now have the duties and liabilities of (1) a director until either a director has been named in an annual report, and (2) a records contact until a records contact has been named. The ABA amendments impose an additional requirement on closely-held companies, to identify themselves as such and to provide the secretary of state with the name and a business or residential street address of its records contact. Annual reports to the secretary of state must now be promptly amended whenever information becomes incorrect or incomplete.

The general record-keeping requirements of a corporation would be updated under the ABA amendments. These amendments would make the following enhancements to record-keeping procedures so as to address the concerns of U.S. law enforcement and regulatory officials. First, a closely-held company would be required to maintain a current record showing the name and last known address of each shareholder. The record must indicate for each shareholder that is a person incorporated or formed by a public filing, whether within or outside the United States, the jurisdiction under whose laws the person is incorporated or formed. The individuals responsible for preparing and maintaining the record would also need to be named. To ensure that this information is accessible to law enforcement when necessary, a closely-held company would need, at all times, to have an individual whose principal residence is in the United States who has access to the record and can produce it within the United States promptly upon request by an authorized agent of a governmental body. This individual must also be able to produce a copy of a passport, driver's license or other government-issued, photo identification document for each director at the time who is an individual and whose principal residence is outside the United States.

The proposed amendments also impose requirements on those becoming shareholders. A person incorporated or formed under the laws of a foreign jurisdiction would need to provide the company with a current certification stating the name and business or residential street address in the United States of an individual whose principal residence is in the United States and who has access to the company's records, to be produced promptly upon request by an authorized agent of a governmental body. These records must include the name and last known address of each record owner of the shareholder, indicate for each record owner of the shareholder that is not an individual the jurisdiction under whose laws the record owner is incorporated or formed.

It is anticipated that NCCUSL will prepare amendments to the other Entity Paradigm Laws similar to the ABA amendments described above. Business trusts will also be covered by the amendments.

The proposed ABA amendments received general – albeit informal – approval from various officials at the Department of the Treasury. It also appears that these proposals would satisfy the FATF's three mechanisms for compliance with Recommendation 33. The FATF's Mutual Evaluation Report for the UK indicated that the UK's intent to implement a similar reporting requirement for a director and natural person would be a move toward complying with

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Recommendation 33. As a result, it appears that the ABA and NCCUSL efforts can meet Recommendation 33 requirements without the need for congressional intervention.

VII. Solution: Risk Based Guidance to Legal Professionals through Best Practices Guidance rather than a Rules-Based Solution

The proposed ABA resolution would also make clear the Task Force's ability to participate in future discussions with the U.S. Government, the FATF or other governmental bodies relating to client due diligence initiatives for the legal profession, including suggestions for a set of voluntary best practices guidelines on client due diligence for the legal profession. A risk-based guidance on client due diligence for legal professionals, combined with the Entity Paradigm Laws and other policies proposed by industry groups, will obviate the need for new federal legislation such as S. 681 and S. 2956.

FATF has been active in developing risk-based guidance for financial institutions and DNFBPs, including legal professionals. In June 2007, the FATF adopted Guidance on the Risk-Based Approach to Combating Money Laundering and Terrorist Financing: High Level Principles and Procedures, which includes guidance for public authorities and guidance for financial institutions ("Financial Institution Guidance"). This effort was the culmination of extensive consultation between private and public sector members of an Electronic Advisory Group ("EAG") established by the FATF.

In addition to financial institutions, the FATF Recommendations also cover a number of DNFBPs. At its June 2007 meeting, the FATF's Working Group on Evaluation and Implementation ("WGEI") endorsed a proposal to convene a meeting of the representatives from the DNFBPs to assess the possibility of developing guidance on the risk-based approach for their sectors, using the same structure and style as the Financial Institution Guidance.

Three months later, in September 2007, FATF convened a meeting in London attended by members of organizations that represent lawyers, notaries, trust and company service providers ("TCSPs"), accountants, casinos, real estate agents and dealers in precious metals and dealers in precious stones. Task Force representatives attended this meeting. This private sector group expressed an interest in contributing to FATF guidance on implementing a risk-based approach for their sectors. The guidance for the DNFBPs would follow the principles of the risk-based approach already established by FATF, and would highlight risk factors specific to the DNFBPs, as well as suggest mitigation strategies that fit with the particular activities and businesses of the DNFBPs. The FATF established another EAG to facilitate the work. The U.S. government was supportive of the FATF effort and outreach to the private sector.

The private sector group met again in December 2007 in Bern, Switzerland and was joined by a number of specialist public sector members, including representatives from the Task Force and the American College of Trust and Estate Counsel. Separate working groups comprising public and private sectors members were established, and private sector chairs were appointed. The EAG met in Paris in April 2008 and in London in June 2008 to advance discussions on developing guidance for legal professionals. During the course of the discussions with the FATF, Task Force members made clear to the participants the ABA resolution from 2003 opposing the imposition of any STR requirement on the U.S. legal profession, and indicated that

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the STR provisions of the FATF Forty Recommendations should not be part of the risk-based client due diligence guidance for the legal profession. Members of the FATF Secretariat appear to have acceded to this position at this time, noting that the requirement on lawyers to file STRs regarding client activities is a matter of specific legal requirements in different jurisdictions, and therefore was not a matter for a risk-based approach to client due diligence. The Task Force will continue to espouse the policy of the ABA opposing mandatory reporting requirements with regard to "suspicious" client activities.

The draft guidance is scheduled to be presented to the WGEI in Ottawa, Canada in September 2008. After further international consultation with both public and private sectors, the FATF anticipates to adopt this guidance at its October 2008 plenary in Rio de Janeiro. Guidance for each of the other DNFBP sectors is being published separately.

A key component contained in the current draft of the guidance for legal professionals is recognition of the need for the legal profession (and not a third party or governmental entity) to develop guidance for its members that is specifically tailored to address any risks that might arise. To that end, and assuming the draft guidance is adopted at FATF's October 2008 plenary, the Task Force understands through discussions with representatives of the Treasury Department that it would be helpful for the ABA to exhibit leadership in the development of non-governmentally imposed risk-based guidance for U.S. lawyers. Because Task Force representatives have been directly and intimately involved in the development of FATF guidance paper for legal professionals since its inception, the Task Force is uniquely qualified to assist in the development of voluntary risk-based guidance. The Task Force's efforts in this area, coupled with on-going dialogue with Treasury Department representatives in the development of such guidance, would obviate the need for Congress to enact legislation designed to impose a rules-based system on U.S. lawyers.

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GENERAL INFORMATION FORM

To Be Appended to Reports with Recommendations
(Please refer to instructions for completing this form.)

Submitting Entity: Task Force on Gatekeeper Regulation and the Profession
Section of Real Property, Trust and Estate Law

Submitted By: Edward J. Krauland

1. Summary of Recommendation(s).

The Recommendation addresses certain proposed legislation and international policy initiatives intended to impose obligations on company formation agents, including lawyers, to undertake extensive due diligence and determine "beneficial owners" when assisting in the formation of non-publicly traded business entities and trusts. It urges that federal legislation is not needed; that the appropriate way to address these issues is through existing state laws and regulatory bodies; that any requirement to determine beneficial ownership and conduct client due diligence be reasonable, risk-based, cost-effective, and not interfere with lawyer ethical obligations; and that the legal profession undertake voluntary initiatives to provide guidance to members as to the risk of money laundering and terrorist financing and complying with existing laws.

2. Approval by Submitting Entity.

The ABA Task Force on Gatekeeper Regulation and the Profession prepared this Recommendation and Report and approved it on July 25th, as has the Council of the ABA Section of Real Property, Trust and Estate Law. Other Sections considering the Recommendation and Report are the Sections of Business Law, Criminal Justice, International Law, and Taxation. Action by the Councils of these Sections is expected by or on August 8, 2008.

3. Has this or a similar recommendation been submitted to the ABA House of Delegates or Board of Governors previously?

No. However, the ABA Gatekeeper Task Force did submit a Recommendation at the Midyear Meeting of the ABA in February 2003. That Recommendation opposed the imposition of mandatory "suspicious transaction reporting" requirements on lawyers, in connection with initiatives by the U.S. government and the Financial Action Task Force to impose new anti-money laundering compliance requirements on the legal profession. The Recommendation was approved (Resolution 104).

4. What existing Association policies are relevant to this recommendation and how would they be affected by its adoption?

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No other Association policies, other than that identified in response to question 3, are known to be relevant to this Recommendation. This Recommendation would be consistent with the policy described in response to question 3.

5. What urgency exists which requires action at this meeting of the House?

Legislation (S.2956) has been introduced in the Senate (and hearings have been held), which seeks to impose onerous and unworkable requirements on company formation agents, including lawyers. We understand that a mark-up of this legislation is expected later this year. Therefore, it is urgent that the ABA take a position on the legislation as soon as possible. Even if the legislation does not move this year, we have been informed it will be re-introduced early next year. The ABA Office of Government Affairs has requested the Task Force to move forward with a Recommendation at this annual meeting in order to be in a position to advocate on behalf of the legal profession with regard to S.2956 and any related bills. Furthermore, the Financial Action Task Force is expected to release a paper in October 2008, providing its views on how the legal profession should conduct client due diligence in order to comply with anti-money laundering and anti-terrorist financing legal requirements. The ABA Task Force wants to be in a position to work with the U.S. government to address the views set forth in the FATF paper, and to prevent any effort to impose new regulatory requirements in this area on the legal profession.

6. Status of Legislation. (If applicable.)

S.2956 has been introduced in the U.S. Senate. It has been referred to the Senate Committee on Homeland Security and Governmental Affairs.

7. Cost to the Association. (Both direct and indirect costs.)

None expected at this time. There may be certain travel requirements that will arise in the future, but $5,000 has already been budgeted to cover any such costs.

8. Disclosure of Interest. (If applicable.)

None.

9. Referrals. (List entities to which the recommendation has been referred, the date of referral and the response of each entity if known.)

See response to question 2. Also, the Recommendation has been referred to the Task Force on Attorney-Client Privilege and the Section of Litigation. Efforts are also underway to refer the Recommendation to the Standing Committee on Ethics and

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Professional Responsibility, Standing Committee on Governmental Affairs, General Practice, Solo and Small Firm Division, Law Practice Management Section, Tort Trial & Insurance Practice, and Young Lawyers Division.

10. Contact Person. (Prior to the meeting. Please include name, address, telephone number and email address.)

Edward Krauland,
Steptoe & Johnson LLP,
1330 Connecticut Avenue, NW,
Washington, D.C. 20036;
202-429-8083;
ekrauland@steptoe.com

11. Contact Person. (Who will present the report to the House. Please include email address and cell phone number.)

Neal R. Sonnett,
Neal R. Sonnett PA,
Suite 2600,
2 S Biscayne Blvd,
Miami, FL 33131;
nrs@sonnett.com;
305-358-2000;
(cell) 305-333-5444;

Stephen A. Saltzburg,
George Washington University School of Law,
2000 H Street, NW,
Washington, D.C., 20052;
ssaltz@law.gwu.edu;
202-994-7089;
(cell) 202-489-7464.

Edward Krauland, Chair
ABA Task Force on Gatekeeper Regulation and the Profession
August 2008

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EXECUTIVE SUMMARY

1. Summary of the Recommendation:

The Recommendation addresses certain proposed legislation and international policy initiatives intended to impose obligations on company formation agents, including lawyers, to undertake extensive due diligence on clients, and to determine "beneficial owners" when assisting in the formation of non-publicly traded business entities and trusts. This is being driven by concerns over money laundering, tax evasion, terrorist financing, and abuse of corporate vehicles for improper purposes. The Recommendation urges that federal legislation is not needed to address the concerns of U.S. regulators; that the appropriate way to address these issues is through existing state laws and regulatory bodies; that any requirement to determine beneficial ownership and conduct client due diligence be reasonable, risk-based, cost-effective, and not interfere with lawyer ethical obligations; and that the legal profession undertake voluntary initiatives to provide client due diligence guidance to members, so as to help address the risk of money laundering and terrorist financing and assist members in complying with existing laws.

2. Summary of the Issue that the Resolution Addresses:

See answer to item 1. The Recommendation addresses the appropriate way for the U.S. government to approach the oversight of company formation agents, including lawyers, in areas such as identifying "beneficial owners" when forming business entities and trusts, conducting client due diligence when initiating client relationships, and avoiding money laundering and terrorist financing risks in the performance of legal services.

3. Please Explain How the Proposed Policy Position will Address the Issue

The Recommendation will provide the ABA Office of Government Affairs with necessary ABA policy to more effectively oppose S. 2956 and work with Congress to pass legislation less burdensome on lawyers, and which secures the attorney-client privilege. The Recommendation urges that new federal legislation is not needed, nor is it the most effective way to address U.S. and international concerns with regard to the impact of non-transparent beneficial ownership in business entities on money laundering and terrorist financing activities. Rather, existing state laws and state regulatory regimes, as appropriately modified through ongoing work of the ABA and other organizations (such as the ABA Committee on Corporate Laws, the ABA Section of Business Law, the National Conference of Commissioners on Uniform State Laws, the National Conference of State Legislatures, the National Association of Secretaries of State), are the appropriate way to increase transparency and information available to regulators. Moreover, client due diligence should be the subject of voluntary guidance developed by the profession, to help educate and assist lawyers to identify and address money laundering and terrorist financing risks when delivering legal services.

4. Summary of Minority Views

There are no known minority views.

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June 11, 2009

The Hon. Joseph I. Lieberman
Chairman
Senate Committee on Homeland Security and Governmental Affairs
SD-340 Dirksen Senate Office Building
Washington, D.C. 20510

The Hon. Susan M. Collins
Ranking Minority Member
Senate Committee on Homeland Security and Governmental Affairs
SD-344 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senators Lieberman and Collins:

Thank you for allowing the Association of Registered Agents ("ARA") and the National Public Records and Research Association ("NPRRA") to submit this letter summarizing our activities over the past three years regarding the use, by some individuals, of business entities formed in the United States for the purposes of money laundering or terrorist financing.

The Association of Registered Agents is made up of companies that offer registered agent and formation services across the United States. Collectively we represent approximately 10% of all business entities registered to do business in the 50 states and the District of Columbia. The NPRRA is an association of local and regional businesses engaged in public record filing, research and information retrieval. As trade associations, we have been successful in working with states to solve problems related to our industry.

No issue is more important to us than ensuring that we, as an industry, are not facilitating the illicit use of US business entities. We attended and listened with great interest to the hearing held by the Senate Permanent Subcommittee on Investigations in November of 2006 on the possible abuses by individuals who form US companies for nefarious purposes. After the hearing we took immediate action.

We initiated meetings with Treasury's Office of Foreign Assets Control and the Financial Crimes Enforcement Network. We wanted to understand the current US law as it applies to our industry – and to ensure that we are in compliance with those laws. As a result of our meetings, each member of our Associations has undertaken a risk assessment to examine each facet of our businesses and to develop safeguards to ensure that our companies are not complicit with those individuals who would abuse our law. We have also worked with together to develop best practices for national, regional and local service providers.

Moreover, we have been working with the National Association of Secretaries of State ("NASS") to further explore the complexities of obtaining and maintaining business entity ownership information. To that end, we participated on a panel at the Association meeting in February of 2007 which led to the creation of the NASS Task Force on Company Formations. That task force then asked the National Conference of Commissioners on Uniform State Laws ("NCCUSL") to address those issues and to develop a uniform approach to resolve those issues through State business entity law. We have met with the National Conference of State Legislators ("NCSL") to provide background information for their Executive Committee Task Force on

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Corporate Formations. NCSL has also recommended that we allow NCCUSL to address the availability of ownership information in the United States.

Finally, our Associations have studied the reports of, and worked directly with, the Financial Actions Task Force's ("FATF") Working Group of Evaluations and Implementations to further understand the international implications of these issues. We have participated with, and made recommendations to the FATF on their Risk-Based guidance for Trust Companies and Company Service Providers, a set of best practices for our industry worldwide. We have discussed compliance matters with registry officials from many other countries to further understand how they have approached this problem. Using the information gained from this international forum, we have worked with many interested parties to develop the best way to provide ownership information to appropriate authorities while protecting the rights of individuals who form US businesses.

Over the past three years, we, as an industry, have come to understand and appreciate the full extent of law enforcement's difficulties in collecting and identifying ownership information and the potential impact on our national security. We also recognize that there are a number of ways to resolve this problem. For example, the Organization for Economic Cooperation and Development in a paper on the subject issued in 2002 has identified at least three different ways that ownership information might be provided. NASS, NCCUSL, NCSL, the American Bar Association, the Departments of Treasury and Justice and our industry have worked together to find a way which would balance law enforcement's need to know who owns and controls a particular entity with business owners' rights to privacy and due process. We believe that NCCUSL's current efforts, with continuing input from all concerned parties will result in the best solution for the United States.

On behalf of the Association of Registered Agents and the National Public Records and Research Association, We remain

Sincerely,

Charlene P. Dawkins
Secretary/Treasurer
Association of Registered Agents
150 Fayetteville St., Box 1011
Raleigh, NC 27601
919-833-1115

Daniel Denham
President
NPRRA
1535 Grant St. Ste. 140
Denver, CO 80203-1843
303-863-1800

NATIONAL
FRATERNAL ORDER OF POLICE®

309 MASSACHUSETTS AVE., N. E.
WASHINGTON, DC 20002
PHONE 202-547-8189 • FAX 202-547-8190

CHUCK CANTERBURY
NATIONAL PRESIDENT

JAMES O. PASCO, JR.
EXECUTIVE DIRECTOR

19 June 2009

The Honorable Joseph Lieberman
Chairman
Committee on Homeland Security
and Governmental Affairs
United States Senate
Washington, DC 20510

The Honorable Susan Collins
Ranking Member
Committee on Homeland Security
and Governmental Affairs
United States Senate
Washington, DC 20510

Dear Mr. Chairman and Senator Collins,

I am writing on behalf of the members of the Fraternal Order of Police to advise you of our support for a bill that was the subject of a hearing this week– S. 569, the "Incorporation Transparency and Law Enforcement Assistance Act." This legislation was introduced by Senator Carl Levin (D-MI) and is a critical step in cracking corporate secrecy that sometimes exists to conceal illegal enterprises.

The "Incorporation Transparency and Law Enforcement Assistance Act" would help law enforcement combat the misuse of U.S. corporations by requiring States to obtain beneficial ownership information for corporations and limited liability companies formed under State law. The bill would accomplish this by providing law enforcement access to this information upon receipt of a subpoena or summons.

For years corporations have been used as front organizations for criminals in the conduct of illegal activity such as money laundering, fraud, and tax evasion. This legislation would act as a critical information gathering tool for law enforcement in combating these crimes by giving law enforcement access to the true identity of the owners behind certain corporations suspected of criminal acts. The sharing of this information will work to speed up the ability of law enforcement to investigate any possible connection between these corporations and terrorist funding.

On behalf of the more than 327,000 members of the FOP, I thank you for your continuing leadership on homeland security and law enforcement issues. If I can be of any additional assistance on this matter please do not hesitate to contact me or Executive Jim Pasco in my Washington office.

Sincerely,

Chuck Canterbury
National President

—BUILDING ON A PROUD TRADITION—

TESTIMONY OF THE KANSAS SECRETARY OF STATE ON S. 569
SENATE HOMELAND SECURITY and GOVERNMENTAL AFFAIRS COMMITTEE
"Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act."
JUNE 18, 2009

Senators:

The Kansas secretary of state appreciates the opportunity to submit written testimony on S. 569, the Incorporation Transparency and Law Enforcement Assistance Act. We believe the passage and implementation of S. 569 will have a negative impact on the office of the Kansas secretary of state. Our staff collected data to predict the impact of S. 569 on our state and we have estimated that over 120,000 corporations and LLC's would be impacted during the first year. If the categories were to expand such that partnerships, trusts and other legal entities were included, the number of entities that would be impacted would climb to 150,000. Several factors were considered in our study:

- The cost for reprogramming our online entity formation filing system to accommodate the requirements of the beneficial ownership information.
- The cost of redesigning forms for entity formation filed on a paper form.
- The cost for reprogramming our filing system to accommodate attachments for certification by formation agents of any non-US citizen. Also, the cost of expanding the paper system to accommodate all beneficial ownership information.
- The need to increase staff to accommodate the changes required by S.569
- The Kansas legislature has cut budgets and swept fee funds from all state agencies, including the secretary of state. The cost to implement S. 569 in Kansas is estimated to be $600,000.

Senate bill 569 is problematic because it would limit or eliminate a customers' ability to make electronic filings, it will reduce access to a filing system that works well for thousands of filers, and it would place an undue burden on the filing agency. The philosophy of the filing agency has always been to serve the customer and accept business filings. This proposal will not accomplish the goal of protecting the United States from U.S. corporations being misused to commit terrorism. It will however, impose responsibilities that are above and beyond the filing agencies abilities, force the filing agencies to raise fees to offset cost of implementation while it penalizes our customers, and impose bureaucracy into a system that was never intended to be run by bureaucrats.

The fiscal impact of S. 569 is even more problematic. Currently, our office is coping with reduced revenues and budget cuts while we maintain a level of service that our customers have come to expect. In the fiscal climate that we are working in, there simply are no resources to implement the large scale changes that S. 569 would require.

I appreciate the opportunity to submit this written testimony in opposition to S. 569.

Respectfully submitted,

RON THORNBURGH
KANSAS SECRETARY OF STATE

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MATTHEW DUNLAP
SECRETARY OF STATE

STATE OF MAINE

OFFICE
OF THE
SECRETARY OF STATE

Testimony of Hon. Matthew Dunlap, Maine Secretary of State

For the Senate Homeland Security and Governmental Affairs Committee Informational Hearing of June 18, 2009 on *"Examining State Business Incorporation Practices: A Discussion of S. 569: the Incorporation Transparency and Law Enforcement Assistance Act"*

Dear Chairman Lieberman, Ranking Member Collins, and Members of the Committee, I am the Secretary of State for the State of Maine, and I have been involved with the Company Formation Task Force formed by the National Association of Secretaries of State (NASS) since February 2007.

I participated both directly and through my senior staff with the drafting and release of the body's report and recommendations, which were adopted by the full membership in July 2007 and reaffirmed in July 2008. I also opposed the first iteration of the bill, S. 2956: "The Incorporation Transparency and Law Enforcement Assistance Act." I supported a resolution in opposition to S. 2956; the resolution was unanimously approved by my peers and adopted by NASS in July 2008.

Today, I remain opposed to the enactment S.569 because of the additional record keeping requirements it will place on states and the uncertainty of the costs associated with implementing such broad changes.

I support the testimony of my esteemed colleague, Hon. Elaine Marshall, North Carolina Secretary of State, who appeared before you at the hearing. She made compelling arguments against S.569 and I want to reiterate some of those points with you as well and describe the impact here in Maine.

I underscore Secretary Marshall's point that the information sought under S.569 already resides with financial institutions, credit unions and with the IRS. If the information is already available from other sources, why is there a need to have the Secretary of State collect, store and deal with privacy issues surrounding this information?

As Secretary Marshall indicated in her testimony, NASS asked Senator Levin to hold off on introducing federal legislation until our association had an opportunity to convene a Task Force to review the issue and develop meaningful recommendations for federal and state consideration. In July 2007, members approved the NASS Company Formation Task Force Report and Recommendations, which includes the following:

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- A ban of bearer shares and interests in bearer form, a practice that was for all intents and purposes prohibited by states' case law, but not clearly outlined in state statute.
- A requirement that entities file a periodic report that includes the name and address of a natural person in the U.S. who has responsibility for providing access to the list of owners of record for a business entity. That name would be a part of the public record and, therefore, available to law enforcement without a subpoena.

These basic recommendations have served as the basis for drafting the Uniform Law Enforcement Access to Entity Information Act, crafted by the Uniform Law Commission with significant input from the legal, law enforcement and filing office communities. You heard details about this draft language from Harry Haynsworth, but Senator Levin dismissed it out of hand since it did not provide shape to his definitional term of beneficial ownership. As Secretary Marshall and Mr. Haynsworth indicated, there is no clear definition in business entity law in the United States for this term; yet Senator Levin continues to push a definition that was crafted for financial transactions disclosure not disclosure under the business entities law.

In May 2008, Senator Levin expressed his dissatisfaction with the NASS approach and introduced the Incorporation Transparency and Law Enforcement Assistance Act (S.2956). He reintroduced this bill in March 2009 as S.569. NASS and a number of other prominent organizations are on record in opposition to this bill, including the Uniform Law Commissioners, the American Bar Association (ABA), and the National Conference of State Legislatures (NCSL).

As Secretary Marshall indicated in her testimony and it is important to emphasize again, during the years since this issue has been brought to the public forefront, the coalition of NASS, ABA, ULC, NCSL has been working together to find appropriate state legislative and administrative answers that would accomplish the following:

- Avoid the federalization of the company formation process, which has always been a state function. Federal legislation will bring federal rulemaking and regulatory authority into an area that has traditionally been the jurisdiction of states;
- Create a way for company ownership data to be held by private individuals designated by the entities, rather than the Secretary of State or other state agency;
- Require that law enforcement agencies use subpoenas to inspect the ownership records rather than mandating that the Secretaries of State or state governments collect, secure and provide them;
- Avoid an immense, unfunded mandate requiring states to fund the hardware, software and staffing to collect, update, preserve and make accessible this ownership data. There would also be a substantial cost for public education efforts regarding the complete change to filing requirements;
- Prevent the office of the Secretary of State from becoming a law enforcement agency if compelled to regularly cross-check the entity ownership data against the Office of Foreign Asset Control's Specially Designated Nationals (SDN) List and report any suspicious matches.

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Overall, the NASS recommendations strike an appropriate balance by supporting the goals of law enforcement without unnecessarily restructuring state governments into Federal branch agencies or negatively impacting the business community.

For even the most technologically advanced states, maintaining ownership information in a database will require the development and design of a new system. It will also require the states to conduct extensive, comprehensive and costly public education campaigns to ensure compliance.

Additionally, the NASS approach does not overburden small businesses, many of which are struggling economically right now. In crafting its recommendations, one of the major goals of the NASS Company Formation Task Force was to avoid any increased financial or filing burdens on small businesses, particularly "mom and pop" or family-owned businesses. It is also important that any changes in law remain simple and straightforward so as not to result in unintentional non-compliance.

Unlike S.569, the NASS Company Formation Task Force recommendations also support the protection of privacy for investors and family members and would not make their personal business matters a part of the public record. While S.569 does leave it up to each state as to how it would handle the public nature of the additional information that must be collected, the creation of a pubic and confidential filings information system is likely to be a nightmare for state filing offices to handle, since this type of confidential filing is not typical of a business entity filing office at the state level. Significant training of internal staff on the functioning and liability of access to this sensitive information will create a totally different level of responsibility for staff; many of my staffers will be reluctant, with good reason, to have any access to this information.

The issues Secretary Marshall and I raise regarding S.569 are not solely issues for my colleagues and me, but they are also issues for the small business community, venture capitalists, and other business-related entities. I strongly urge the Committee to seek out input from this segment of the business community to hear the impact that it will have on the backbone of our economy – small businesses.

In Maine, S.569 would be a significant burden, and we are a state recognized for innovation with online technology. Unlike Secretary Marshall, I have a 2 person technology staff to make changes to our existing system. S.569 will likely require a significant change in our system hardware and software configurations. Maine currently has 70,000 active corporations and limited liability companies within our databases, and all filings are examined before filing. While Maine is not a legal review state, our staff does review filings for completeness of the required statutory information. Maine does not permit online filing of formation documents, but does accept Annual Reports online.

As Secretary Marshall testified, to assess the real costs to the states under S.569 is almost impossible. A great disconnect exists between what the bill states and what we think it will mean in order to be effective. The unknown, but expected, requirement for this bill to be meaningful is the application to existing business entities. If proposed Sec.2009.(a)(1)(B) requires all existing entities to provide beneficial ownership information on an annual basis (not just those businesses created after the effective date), then entirely new processing and educational programs will have to be crafted. Everyone will need to provide citizenship or status information. Screening by

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physical addresses will be inadequate. Responsibility is placed on formation agents, but the bill is silent as to the responsibility for those entities created without a formation agent. An educational undertaking to all new entities, approximately 4,000 – 5,000 per year in Maine, is one of significant cost. If all 70,000 entities of record must be informed, the cost grows greatly.

The huge volume of materials S.569 will generate over just a few years needs to be considered. On its face, Annual Report numbers will not increase, but Annual Reports are public records in Maine. If they contain confidential ownership information in order to keep current, redaction will need to occur or separate filing systems will need to be maintained, possibly increasing the image load exponentially. Maine is currently using hardware that is near or at the end of its lifespan. I am concerned that to put more pressure on existing hardware with the volume of new or expanded filings will cause catastrophic issues. In Maine, we have had to reduce our budgets so substantially over the last 4 years that we are struggling to meet our ongoing expenses. Going to the Maine Legislature to ask for money above and beyond normal operating expenses to fund federally mandated programs will be an exercise of profound exasperation. Given the narrowing band of available public resources, Maine simply does not have available the estimated $1.1 million necessary to make upgrades to meet the requirements of S.569.

I concur with Secretary Marshall's assertion regarding the impact of S.569 on nonprofit corporations - general confusion will be the norm as nonprofits seldom have "owners" of any definition. Who are the "beneficial owners" of incorporated VFW organizations, American Legion organizations, Granges, churches, Lions Clubs International, Elk Lodges et cetera.? In Maine, these types of fraternal and social organization make up a large percentage of our nonprofit corporations. I would invite, but do not expect, any Federal assistance in answering the almost 13,000 telephone calls that my office will get on this issue from nonprofit corporations alone.

Secretaries of State around the country are very concerned that the term "beneficial ownership" is not well-established in American jurisprudence and that it will fall upon us to interpret what that means. It is also of concern that the law would apply to formation agents but does not specify who would be responsible in the case that a formation agent is not used. Filing offices have no desire to be the default keeper and verifier of the identity of non-United States citizen beneficial owners. The definition of formation agent itself is of concern since formation does not occur until my office accepts and files it; am I, the Secretary of State, then by definition a formation agent?

I share Secretary Marshall's concern regarding the possible verification of ownership information falling to our offices; which then leads to states comparing ownership names against OFAC's SDN list. The verification and comparison to this list would be a nightmare of biblical proportions. Starting on July 1st, I will have 5 less staffers in my office due to budget reductions. Any verification and checking would require me to double my staff; not reduce it.

Because I am also the state's chief Motor Vehicle official, I am also responsible for issuing state driver licenses and identity credentials. Using a combination of AAMVA naming protocols and existing names on the SDN list, finding matches on the SDN list through even a normal business proceeding—which would occur if an agent presents a driver's license as identity—would be problematic. Assuming their name was more than 15 characters long and hyphens were removed, if it were entered against the SDN list, it would *not generate a match,* even if the individual were listed on the OFAC SDN list. Naming protocols for the list demand an exact match. Bear in mind

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that this assumes that no fraud has occurred in procuring any original document. The terrorists of September 11th, 2001 were able to obtain state credentials using Federally-issued travel documents, which were obtained in several cases through fraud. I would invite an amendment to this bill that would obligate the Federal government to uphold its end of the bargain on national security.

If you sense resistance and frustration from Secretary Marshall and me, you are correct. Clearly, I am not an advocate of Maine companies being used for money laundering or other illicit purposes. But we all feel these efforts are going to be of limited effectiveness compared to other possible avenues of recourse described in my testimony. Do you really think that the bad guys will think twice about providing fraudulent information at the time of formation? Ironically, this bill will not stop criminals, but will deter legitimate businesses from forming. Rather than creating entities that would be held to new filing requirements by S.569, entrepreneurs will create entities like sole proprietorships which don't file with our office. But by creating these types of entities, the businesses sacrifice the liability shield and tax benefits afforded to corporations and limited liability companies. What is the impact of reduced entity filings? Undoubtedly it would result in a major loss of revenue for states. In Maine, we generate revenue in access of $10 million annually for the Maine General Fund.

S. 569 represents a cultural change – not just for the filing offices who view their function as simply ministerial, but a cultural change for everyone engaged in business of most types in the United States. As Secretary Marshall points out, ground zero for the fallout from these cultural changes will be each state's filing office, and we are gravely concerned. Viewing the financial and human asset commitment contrasted with the efficacy of the proposal, it is hard to find significant added value and meaningfulness.

In closing, I too, as Secretary Marshall indicated, am very wary of any federal law that burdens states and legitimate businesses yet provides lawbreakers with the ability to evade it. The obvious argument is that the extremely small number of entities that are registered to do business that may be engaged in money laundering, terrorist financing and tax evasions are probably not going to file accurate or truthful information to state government. The bill can only serve to severely impact the vast majority of legitimate, law abiding businesses trying to stay afloat in turbulent economic times.

Thank you for allowing me to provide my thoughts on this very difficult matter.

Sincerely,

Matthew Dunlap
Secretary of State
State of Maine

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National Association of Assistant United States Attorneys
12427 Hedges Run Dr. • Ste 104 •Lake Ridge, VA 22192-1715
Tel: (800) 455-5661 • Fax: (800) 528-3492
Web: www.naausa.org

June 18, 2009

The Honorable Joseph Lieberman
Chairman
U.S. Senate
Committee on Homeland Security
and Governmental Affairs
Washington, DC 20510

The Honorable Susan Collins
Ranking Member
U.S. Senate
Committee on Homeland Security
and Governmental Affairs
Washington, DC 20510

Re: S. 569, The Incorporation Transparency
and Law Enforcement Assistance Act

Dear Chairman Lieberman and Ranking Member Collins:

I write to express the strong support of the National Association of Assistant United States Attorneys for S.569, the Incorporation Transparency and Law Enforcement Assistance Act, and urge swift action to approve this measure.

This legislation, introduced by Senators Levin, Grassley and McCaskill, will require States to obtain the names of the beneficial owners of each corporation or limited liability company formed under their laws, ensure that this information is annually updated, and make such information available to law enforcement authorities when legally authorized. Mindful of the ease with which criminals establish "front organizations" to assist in money laundering, terrorist financing, tax evasion and other misconduct, it is shocking and unacceptable that many state laws permit the creation of corporations without asking for the identity of the corporation's beneficial owners. S. 596 will guard against that, and no longer permit criminals to exploit the lack of transparency in the registration of corporations. It also will create a critical information gathering tool by giving law enforcement authorities access to the true identity of the owners behind certain corporations suspected of criminal acts, without unduly intruding upon individual privacy.

On behalf of the Assistant United States Attorneys represented by our association, we thank you for holding the hearing on this bill on June 18 and urge swift approval by your Committee. Thank you for your leadership and for consideration of our comments.

Sincerely,

Steven H. Cook USATNE
National President

President: Steven H. Cook, ED of Tennessee
Vice President for Policy: Robert E. Mydans, District of Colorado
Vice President for Operations and Membership: John E. Nordin II, CD of California
Treasurer: Robert Gay Guthrie, ED of Oklahoma
Secretary: Rita R. Valdrini, ND of West Virginia

Wyoming Secretary of State

Max Maxfield
Secretary of State

Patricia O'Brien Arp
Deputy Secretary of State

June 16, 2009

Honorable Joseph Lieberman, Chairman
Senate Committee on Homeland Security and Governmental Affairs
340 Dirksen Senate Office Building
Washington, DC 20510

RE: S.569 Incorporation Transparency and Law Enforcement Assistance Act

Dear Chairman Lieberman and Members of the Committee:

Thank you for the opportunity to present information to the Committee on behalf of the State of Wyoming.

The Problem: First let me say that Wyoming has candidly acknowledged that the structure of our business laws was problematic in that, in an attempt to be business friendly, our laws were also found to be fraud friendly. During my first week in office in January of 2007, I was contacted by the national media about Wyoming's business laws. I had already made a commitment to take action. Wyoming has not denied, nor made light of, the problem facing us.

Actions Taken: Immediately, my office began working with the State Legislature. A law specifically barring bearer shares was passed in 2007 and two very large pieces of legislation; The Wyoming Registered Offices and Agents Act, and the companion bill allowing enforcement authority were passed in 2008, effective January 2009.

The above two laws now require the following of registered agents (formation agents):

- Each company must have a registered agent (human being) in our State at a physical location – no drop boxes;
- The registered agent must keep information about key players of each company represented;
- The registered agent must also have information about a contact person for each company.

The new laws:

- Provide for increased enforcement authority;
- Provide a felony provision for filing false documents.

Opposition to Wyoming's Actions: As a serious aside, I must make note of the fact that it was very difficult to get this State legislation passed. The Wyoming Joint Corporations Committee worked closely with my office for months working on final versions of the bills. We had the full support of the Governor, as evidenced by the fact that for perhaps the first time in Wyoming history a Governor testified before the Legislature about a specific bill. The Governor, a former U.S. Attorney, was all too familiar with our problem. Nonetheless, it was one of the hardest fought battles to get these laws passed. Influences external to Wyoming lobbied, hired lobbyists and flew into Wyoming to testify and fight against these bills. It is of note that the most opposition came from large formation companies who did not want to be responsible for "knowing who their clients were" and who did not want to be responsible for keeping information about their clients. They were all too happy to pass that responsibility to government; and place it upon the State to try to keep track of the players involved in these businesses which they were forming and representing.

State Capitol Building
200 West 24th Street

E-mail: secofstate@state.wy.us
Website: http://soswy.state.wy.us

Cheyenne, WY 82002
Phone: (307) 777-7378

Wyoming's Success: Wyoming's laws were passed in 2008, effective January 2009. Already a few registered agents who represented hundreds of companies each have folded up shop. In just the first few months the bill has been in effect, Wyoming has dissolved thousands of companies represented by these few agents. In addition, we are working with the White Collar Crime Task Force (FBI, Postal Service, U.S. Attorney's Office, Secret Service and Wyoming Secretary of State's Office) to bring cases forward to the U.S. Attorney for prosecution. The Wyoming Secretary of State's Office has been an active member of the White Collar Crime Task Force for almost 15 years and it is a satisfaction to now have the laws necessary to obtain information and assist law enforcement in the prosecution of individuals who have used Wyoming's laws for evil.

Concerns About S.569: While we understand the premise of S.569; and while we applaud Senator Levin for his desire to better protect our country, we have serious concerns that the passage of S.569 will set Wyoming back in our efforts to fight fraud. We have the following serious concerns.

1. Our greatest concern is that if the federal law passes, there will be serious attempts to rescind Wyoming's laws. The argument will be that as long as a company meets the federal law that should be enough.
2. If Wyoming's laws were to be rescinded, we would lose the key component of requiring a human being in our State TO BE RESPONSIBLE FOR REPRESENTING THE COMPANIES THEY SERVE. We would be back to registered agents just being there for service of process, taking an otherwise hands off approach to the responsibility which they should shoulder.
3. If Wyoming's laws were to be rescinded, we would also lose the requirement that the registered agent have a contact person for each company they represent. We FIRMLY BELIEVE that a person leading you to another person is infinitely better than having paper on file. Fraudulent people file fraudulent paper; but a person face to face being held responsible generally knows of another person who can be contacted.
4. Whatever information is determined to be kept, it should be kept by the registered agent, not by government. This is a responsibility issue. States should not be taking the responsibility to know the players for each company; states are not forming these companies or using them for potential ill. Formation agents and the registered agents who are forming and making money off these companies (or the individuals themselves if the owner acts as his own registered agent) should be responsible for retaining and providing all required information. Without personal responsibility for the paper, the paper has very little value, except to make it APPEAR AS IF government is trying to locate the bad actors.

Exemption: Should S.569 proceed through the Committee because it is determined to have value in states which do not have laws, such as Wyoming's new laws, then we would respectfully ask the Committee to consider an exemption. The exemption would be for any state which meets the spirit of S.569 - and that could even be defined as requiring that beneficial owners' information and special documents for international owners be required to be kept under state laws.

Sincerely,

Max Maxfield
Wyoming Secretary of State

Question#:	1
Topic:	information
Hearing:	Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act
Primary:	The Honorable Carl Levin
Committee:	HOMELAND SECURITY (SENATE)

Post-Hearing Questions and Answers for the Record
Submitted to Janice Ayala

Question: From a law enforcement perspective, what is the value of obtaining beneficial ownership information from a state entity, such as the Secretary of State's office, as opposed to some other individual including a "records contact" as required by the NCCUSL proposal?

Response:

There are possible advantages in having beneficial ownership information collected by a government entity and housed with that entity instead of only with a private individual or incorporation service. Because the person providing this information to the incorporation service is the client of that business and pays for the business's services, it could be argued that there would be a conflict of interest for the incorporation service to obtain and maintain objective, accurate, and updated information. In these instances, one might suspect that the business collecting the information would be less likely than an objective third-party government entity to question its paying client, especially when the business's client wishes to veil his identity. However, this would not be a valid assumption in this context, for two reasons. First of all, the NCCUSL Uniform Act calls for the name and street address of a Records Contact and a Responsible Individual (who must be familiar with the affairs of the company, participate in its control or management, and who may not be a nominee) to be filed the Secretary of State, and for the Records Contact (who may be an incorporation service) to collect and maintain a copy of the Responsible Individual's government issued photo identity document and to have access to additional beneficial ownership information. Secondly, a Secretary of State does not question the content of any information filed, but simply accepts it for filing.

Additionally, one might argue that an advantage in requiring that ownership information must be provided to a governmental entity is that there is liability for the failure to do so. However, neither is this a valid criticism of the NCCUSL Uniform Act for the following reasons. In the case of law enforcement queries, if the copy of the government-issued photo identity document has not been collected by the Records Contact, the Records Contact must resign, which triggers the dissolution of the legal entity. If the information regarding the Responsible Individual becomes stale, inaccurate, or incomplete, and the Responsible Individual fails to notify either the Records Contact or the Secretary of State, there would be little if any recourse against the Records Contact, nor would there be any recourse against the Secretary of State for the failure of the Responsible Individual to update the required information.. When targets of criminal investigations provide false

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Question#:	1
Topic:	information
Hearing:	Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act
Primary:	The Honorable Carl Levin
Committee:	HOMELAND SECURITY (SENATE)

information to a government entity, there is recourse against the person providing false information. Since the information must be provided to the government under the NCCUSL Uniform Act, an individual can be prosecuted for providing false statements or entries. Further, when assembling the facts for prosecution of the organization, the mere act of providing false information to a government entity can be utilized as an indicator of the criminal intent of the target.

Finally, and most importantly, there would be no mechanism, under the NCCUSL proposal, to prevent the incorporation service from disclosing requests for information to their clients. Grand jury non-disclosure provisions and other court orders would not apply, under current law, to these incorporation services. Law enforcement could request that the inquiry not be disclosed, but could not compel non-disclosure. As such, and with the beneficial owner of the shell company being a client of the incorporation service, it could result in subjects of an ongoing investigation being notified of law enforcement queries. This could jeopardize the ongoing investigation and could lead to the funds, targeted by the investigation, being moved and further hidden from law enforcement. Without the ability to access beneficial ownership information in a manner that ensures both accuracy and confidentiality, collecting the information would not be useful to law enforcement. This problem is ameliorated under the NCCUSL Uniform Act by the fact that the name and street address of the Records Contact and Responsible Individual must be filed with the Secretary of State, and law enforcement could obtain that information without contacting anyone else.

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Post-Hearing Questions for the Record
Submitted to Adam S. Kaufman
From Senator Carl Levin

"Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act"
June 18, 2009

1. From a law enforcement perspective, what is the value of obtaining beneficial ownership information from a state entity, such as the Secretary of State's office, as opposed to some other individual including a "records contact" as required by the NCCUSL proposal?

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DISTRICT ATTORNEY
OF THE
COUNTY OF NEW YORK
ONE HOGAN PLACE
New York, N. Y. 10013
(212) 335-9000

ROBERT M. MORGENTHAU
DISTRICT ATTORNEY

August 7, 2009

The Honorable Joseph Lieberman
Chairman
United States Senate Committee on Homeland Security and Governmental Affairs
Washington, D.C. 20510-6250

Dear Senator Lieberman:

I write this letter to address the question posed by Senator Carl Levin following the hearing before the Committee on June 18, 2009, specifically asking for a comparison of the value of obtaining beneficial ownership from a state entity as opposed to another individual, including the "records contact" as required by the NCCUSL proposal. I was honored to appear before the committee in June, and it is my pleasure to address this question now, for it strikes at the heart of the concerns voiced by law enforcement authorities with regard to the NCCUSL proposal.

In my testimony, I stated that law enforcement would be better served if Congress were to enact no law than it would be if the NCCUSL proposal were enacted, and I stand by that statement now. From a law enforcement perspective, the NCCUSL proposal simply does not make sense. Any proposal intended to enhance the ability of law enforcement to investigate shell companies utilized by criminal organizations must address two primary concerns. It must allow law enforcement to obtain information without alerting the criminal organization, and to do so as quickly as possible. The NCCUSL proposal fails on both counts.

First, regarding secrecy, any criminal investigation must be able to proceed without alerting the suspects to the existence of the investigation. The reasons are simple. Once alerted, the suspects will destroy evidence, alter their behavior, and/or flee the jurisdiction. Often our investigations proceed at a deliberate and measured pace, simply because any overt action by law enforcement would alert the suspects. A criminal case is built on numerous pieces of evidence, each piece gathered in secrecy during the investigation. We cannot take action that will alert the suspects until we are prepared to execute search warrants, seize assets, and make arrests. This is particularly true for long term investigations of sophisticated criminal organizations that often utilize shell companies. We may only have one chance at taking down the organization, so we have to move at a painstaking pace until we have built a solid case.

The NCCUSL bill would require us to notify an individual designated by the company (the "records contact") to obtain ownership information about the company. This is tantamount to calling the suspects to tell them they are under investigation. The effect is

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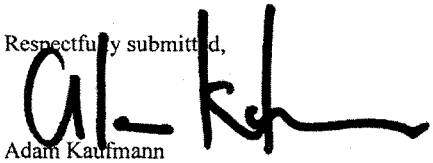
the same: we would have to notify the agent of a suspected criminal organization in order to request information. As a general rule, we do not serve subpoenas on criminal organizations and we do not give them warnings that they are under investigation. Yet this would be the precise impact of the NCCUSL proposal, which demonstrates a complete lack of understanding about the criminal investigative process.

Moreover, when law enforcement tries to adduce the beneficial ownership of a corporate entity, we seek the quickest method possible. As noted above, there is enough delay inherently built into our investigations – the NCCUSL proposal would simply add more. Senator Levin introduced a chart depicting the tangled web of multiple steps required by the NCCUSL proposal: first a subpoena to the "records contact" to ascertain the identity of the company's designated "responsible individual" (who could be an offshore nominee not susceptible to subpoena), followed by an attempt to serve the "responsible individual" with a subpoena. The complexity and unworkable nature of the proposal are manifest; particularly when compared the simple and logical act of serving a subpoena on a secretary of state. One process presents a bureaucratic quagmire that will serve only to notify the suspects of the investigations; the other is a direct and confidential request to a state official. From a law enforcement perspective, the choice is obvious.

Finally, the burden imposed by S 569 on state governments is simply the retention of the name of the beneficial owner and his/her Photo Identification, while NCCUSL requires the retention of the name of the records contact. These burdens are similar in nature, coverage and extent. The proponents of the NCCUSL bill portray the requirements of S 569 as draconian governmental intrusions. From a records-keeping perspective, I fail to perceive a significant difference between the proposals. However, their effects on law enforcement could not be more divergent. NCCUSL completely fails to advance any interest of law enforcement, and will benefit criminal organizations by legislating a system guaranteed to give them advance notice of criminal investigations. I urge the Committee to report favorably on S 569.

I thank you again for the opportunity to address the Committee and these important issues.

Respectfully submitted,



Adam Kaufmann
Assistant District Attorney
Chief, Investigation Division Central
New York County District Attorney's Office

cc: Senator Carl Levin

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Questions for the Record Jennifer Shasky Calvery
"Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act"
June 18, 2009

QUESTIONS FROM SENATOR LEVIN

1. **In 2006, Stuart Nash from the Department of Justice submitted testimony to the Permanent Subcommittee on Investigations where he noted that the lack of beneficial ownership is "a hugely significant problem and we are having investigations, and important investigations, that are hitting brick walls because there is no one out there that has the information regarding beneficial ownership that we need to pursue those investigations."**

   Please describe the scope of the problem faced by law enforcement due to a lack of company beneficial ownership information. In addition, please provide examples of investigations that have been thwarted due to the lack of company beneficial ownership information.

RESPONSE:

In criminal investigations, law enforcement often faces a problem uncovering the criminals responsible for instigating crimes when they use shell companies, primarily to open foreign bank accounts. This is due, in part, to the lack of beneficial ownership information gathered on shell companies. Although the Department does not collect statistics on the scope of this problem, the following information reported by investigators and prosecutors indicates that the problem is widespread:

- When questioned about whether a lack of information about a U.S. shell company had hindered their investigations, nearly all of a 75 person audience of federal investigators and prosecutors from throughout the country responded that it had. The audience — including investigators from nine federal law enforcement agencies and prosecutors from a variety of districts and offices — was attending a financial investigation seminar designed to teach them how to investigate the financial aspects of international criminal organizations. The instructor, who was lecturing on U.S. shell companies, asked the members of the audience to raise their hand if they had ever reached a dead end in one of their investigations because of a U.S. shell company. Nearly every person in the room raised his or her hand. Departmental instructors report that such a response is common in money laundering courses delivered both domestically and abroad.

- Likewise, participants in Suspicious Activity Report (SAR) Review Teams report that many investigations involving U.S. shell companies are never even pursued. SAR Review Teams exist in most judicial districts around the country and are comprised of prosecutors, federal investigators, and often state and local law enforcement. Their mission is to review SARs and uncover links that can lead to criminal prosecutions,

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forfeitures, and seizures. The teams report that often they do not pursue leads contained in the SARs under review because the reported suspicious financial activity was done through an account held in the name of a U.S. shell company. Realizing that beneficial ownership information for the U.S. shell company is not available in the United States and the underlying account under review was established in a foreign country, the teams never pursue an investigation. The total amount of money associated with suspicious financial transactions involving U.S. shell companies that is reported in SARs on an annual basis is quite high, often in the billions of dollars.

- Finally, as detailed in the earlier testimony of both Stuart Nash and Jennifer Shasky Calvery, the lack of beneficial ownership information for U.S. entities also provides challenges for the United States when responding to requests for assistance from our foreign partners. Stuart Nash, in particular, testified about the scope of the problem and rise in requests for information related to shell companies during 2004 and 2005. The Department's Office of International Affairs (OIA) reports that, since that time, OIA has spent considerable effort educating our foreign counterparts about our inability to obtain and provide beneficial ownership information. As a result, OIA reports that is has seen the number of requests drop. Not unexpectedly, foreign investigators and prosecutors continue to approach DOJ speakers at foreign events to complain about investigations that were terminated due to their inability to obtain beneficial ownership information about U.S. companies. This problem not only damages our reputation but is also counterproductive to our efforts to join with foreign counterparts in a global offensive against organized crime and terrorism.

The following case example illustrates how a lack of beneficial ownership information thwarts an investigation and why such an experience might lead law enforcement to avoid pursuing such investigations:

Numerous victims in the United States complained to law enforcement investigators about losing money when attempting to purchase automobiles over the Internet via an online auction website. The fraud scheme was facilitated by the use of U.S. shell companies which were used to move the victims' proceeds out of the United States and into Latvia, subsequently disbursing those proceeds among the unidentified criminal participants.

In essence, the victims were induced to purchase an automobile using a well-known online website. The criminal participants would identify a legitimate vehicle for sale on the site and then, acting as potential buyer of the vehicle, they would obtain necessary information such as the vehicle title and photographs. The criminal participants would then pose as the purported seller of that vehicle. Interested buyers would email the criminal participants (purported seller) to inquire about the availability of the car and the criminal participants would reply to the buyer via email, and not through the auction website. In the course of transferring payment for the cars, victims were directed to use entities that had the same name as licensed and bonded escrow companies located in the United States. The criminal participants would create false web

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sites for these entities and direct the victims to log on to the false sites with an assigned ID and password in order to receive payment instructions.

Victims were then directed by the false escrow companies to wire funds to a financial institution located in New York, "Bank A," for further credit to the named U.S. shell company. Based upon the wiring instructions that they received, the victims believed that they were sending money to a U.S. bank account held by the escrow company in New York. In reality, the wire instructions showed that the funds were ultimately sent to an account maintained under the name of the U.S. shell company at a bank located in Riga, Latvia via a correspondent account in the name of the Latvian Bank which was located at Bank A in New York. Obviously, the correspondent account records for the Latvian Bank, held at Bank A, had no details on the owners of the U.S. shell company.

Corporate documents for the U.S. shell company obtained from the Secretary of State of the respective state provided names of two individuals acting on behalf of corporate entities in Tortola, British Virgin Islands, both with addresses in Tortola. The U.S. shell company was associated with two U.S. addresses, both of which were addresses of a U.S. registered agent and used simply as mail drops.

It required three formal treaty requests, over the span of nearly two years, to obtain documentation from Latvia that specifically identified the individual who was the signatory on the bank account held in Latvia in the name of the U.S. shell company. A copy of this individual's foreign passport (which was Ukrainian) had been maintained by the Latvian bank. However, a review of the bank records for the account in the name of the U.S. shell company revealed that funds from the U.S. victims received into that account had been transferred out of that account into another account in the name of another U.S. shell company, necessitating a repeat of the entire process, including additional treaty requests to identify additional bank account signatories. Those signatories all held foreign passports, none of which were Latvian.

Ultimately, this case was never charged because investigators were unable to establish whether the signatories on the bank accounts had knowledge of the underlying fraud that generated the funds or whether they were the beneficiaries of those funds as opposed to merely financial service providers responsible for moving the funds. In essence, the investigators could not establish the beneficial owner of the U.S. shell company and its assets (the fraud proceeds).

This case illustrates how a lack of corporate transparency in the United States can frustrate an investigation at several different junctures. First, the success or failure of a U.S. investigation requiring the identification of a beneficial owner of a U.S. shell company depends upon the existence and effectiveness of a U.S. treaty relationship with a foreign country. An investigation is often frustrated when no treaty relationship or an ineffectual treaty relationship exists with another involved country and the case reaches a dead end. However, the investigation can also be frustrated even when, as in the case described above, a viable treaty relationship exists. The investigation is frustrated

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because the significant investigative delays associated with treaty requests result in criminal participants staying several steps ahead of law enforcement, the trail turning cold, or the case being terminated for statute of limitations or other delay-related reasons.

2. **From a law enforcement perspective, what is the value of obtaining beneficial ownership information from a state entity, such as the Secretary of State's office, as opposed to some other individual including a "records contact" as required by the NCCUSL proposal?**[1]

RESPONSE:

It is critical for law enforcement to obtain beneficial ownership information from the government, or a government affiliated entity, rather than from an individual affiliated with the company, such as a "records contact."[2] A company affiliated contact places a nominee between law enforcement and the criminal suspect, and it forces law enforcement to alert the suspect entity to its criminal investigation. In practice, this system would effectively force law enforcement to refrain from requesting any ownership information rather than tip off the suspects.

Alternatively, requiring a company to provide beneficial ownership information directly to a government entity, at the time of formation or change of ownership, removes these impediments to law enforcement. Law enforcement can obtain beneficial ownership information about a suspect company without any contact with an agent or nominee of the suspect company. Also, there is no nominee standing between the required beneficial ownership information and law enforcement. As a result, if the beneficial owner provides fraudulent information, there is no nominee in the middle obscuring criminal liability.

From a law enforcement perspective, if the owners of a shell corporation provide the minimal information required by the proposed bill at incorporation to a government entity, it helps the criminal investigation. It is either legitimate and provides some additional, valuable leads, or it is inaccurate and may prove invaluable in establishing the fraudulent intent and criminal culpability of those involved in intentionally providing false information.

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[1] Treasury would like to clarify that the NCCUSL Uniform Act requires that each legal entity must file with the Secretary of State a statement containing the name and address of a "Responsible Individual," who must be generally familiar with the affairs of the entity and who participates, directly or indirectly, in the control or management of the entity. Law enforcement must go to a "Records Contact" in order to obtain additional beneficial ownership information, including a credible and legible photocopy of a government-issued identity document of the Responsible Individual.

[2] Treasury believes that, although there are advantages to obtaining ownership information from a governmental entity, this may not be necessary for an effective solution to this problem, and there may be advantages to other means of obtaining access to this information.

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"Business Formation and Financial Crime:
Finding a Legislative Solution"
Homeland Security and Governmental Affairs Committee
Chairman Joseph Lieberman
November 5, 2009

Good morning and welcome to our hearing today. This is our Committee's second hearing on the Incorporation Transparency and Law Enforcement Assistance Act, S. 569, which was introduced by Senators Levin and McCaskill, who are members of this Committee, and by Senator Grassley, Ranking Member of the Finance Committee. This legislation - the result of work by Senator Levin's Permanent Subcommittee on Investigations over the years, - seeks to increase the transparency of business formation practices in order to reduce what is estimated as billions of dollars in fraud perpetrated by shell corporations.

Each year, nearly two million new corporations and limited liability companies are established in the 50 states and the District of Columbia. That's comes to more than 5,000 new businesses per day. This is really the American way - entrepreneurship at its best: generating revenue and creating jobs.

But, each year, some of those new businesses are incorporated for improper or illegal purposes—to try to use registered corporations to defraud innocent people, to cheat tax authorities, to hide the true transactions, or to launder ill-gotten funds.

Right now, a majority of states require some basic information from those seeking to establish a corporation. Most require the name and address of the company, the name of a registered agent, who represents the company, and a list of officers and or directors. This information is typically considered a public record.

But most states allow the individuals with actual ownership interest – including the investors who control the corporation or partnership – to remain anonymous to state authorities and, therefore, to the public. And this is a problem for law enforcement

Senator Levin's bill offers one solution: setting a national minimum standard for state incorporation practices that requires states to collect, maintain, and update so-called "beneficial ownership" information.

But there are critics of this method who argue that a well-intended desire for more sunshine must be weighed against other factors, including the privacy rights of those making personal investment decisions, and the potential costs of administration and enforcement that would fall on companies and state governments.

Our goal today is to hear today from experts in this problem so we can make a judgment about how to deal with what everyone considers a problem.

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We have a series of witnesses today who will help us sort out the benefits and consequences of S.569. On the first panel, we will hear for the first time from the Treasury Department, which administers anti-money laundering laws and leads U.S. efforts to stop the flow of terrorist financing. Treasury has worked tirelessly on corporate transparency issues, engaging with stakeholders to consider all the possible approaches to improving practices in this area. We will also hear from the Department of Justice, which has first-hand experience in the challenges of law-enforcement s they try to combat the use of corporations for nefarious purposes.

Our second panel of witnesses represents the business and legal communities, which have distinct concerns about the smooth flow of commerce for legitimate corporate purposes. We will also hear from a representative of the Federal Law Enforcement Officers Association and an expert on tax havens, both of whom support the general approach taken by the bill.

So, this is an interesting and important matter on which we hope to shed some light this morning.

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STATEMENT OF SENATOR CARL LEVIN (D-MICH)
ON
BUSINESS FORMATION AND FINANCIAL CRIME:
FINDING A LEGISLATIVE SOLUTION

November 5, 2009

This is the Committee's second hearing on how current incorporation practices, which allow the formation of U.S. corporations with hidden owners, are fueling the misuse of U.S. corporations to the detriment of our nation. Here's an example of the problem.

Viktor Bout, a Russian, is one of the most notorious arms traffickers in the world, and is featured in a book called Merchant of Death. Last year, the United States indicted him for conspiracy to kill United States nationals, the acquisition and use anti-aircraft missiles, and providing material support to terrorists. To carry out his activities, he is known to use a network of shell companies around the world, including companies formed in countries like Liberia, Moldova, and the United States.

Chart One lists the names of ten Texas and Florida companies alleged to have been used by Viktor Bout over the years. It also includes two Delaware companies that were alleged in a 2002 Interpol notice, based on information from Belgium, to have been used by Viktor Bout to transfer $325 million to carry out his activities.

The chart does not include another Delaware company, Garland Global Corporation, which Romania believes may also relate to Viktor Bout, but whose beneficial owners are unknown. In July 2009, Romania filed a formal request with the United States for the names of the company's owners and other information. But it is unlikely that the United States can supply the names since, as this Committee has heard before, our 50 states are forming nearly 2 million companies each year and, in virtually all cases, doing so without obtaining the names of the people who will control or benefit from those companies.

The end result is that a U.S. company may be associated with an alleged arms trafficker and supporter of terrorism, but we are stymied in finding out, in part because our States allow corporations with hidden owners.

Here's another aspect of the problem. Last month, my staff went on the Internet and typed in "shell company" as a search term. The first entry that came up was for "Aged Shell Companies" and provided a link to the website of a company called Go Risk Free which offers corporations for sale in all 50 states. As Chart Two shows, Go Risk Free promises: "if you need a company that is … in a certain state or age, CONTACT US, and [we] will help you find it!"

On the date we checked, Go Risk Free had over 200 companies available for sale. The prices start at $3,500. The first was a Nevada company incorporated on October 22, 1928, over 80 years ago. Think about that. A secret buyer of this company could pretend to have had a U.S. business in operation for decades. He could use that shell company to convince a bank to open an account or issue a credit card, and go on from there. These sales seemingly have no purpose

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other than to create a misleading impression. The potential for criminals to buy these types of U.S. companies without ever divulging their names or interests is a disaster waiting to happen and a threat to our security and well being.

At the Committee's hearing in June, we were told about a New York corporation that was secretly owned by members of the Iranian military. Our government learned of that ownership interest, not from New York state records, but because another country had the beneficial ownership information that we didn't.

We also heard about a network of 800 U.S. companies across the country that had attracted law enforcement attention because they were transferring suspect funds to each other and in and out of high-risk jurisdictions. When the Department of Homeland Security's Immigration and Customs Enforcement or ICE, tried to find out the companies' owners, all it could learn was that they were associated with a shadowy group of shell companies in Panama. ICE eventually dropped its investigation, in part because not one of the 800 company formation documents had any information on the true owners.

These are only a few examples of U.S. companies being used to engage in a wide range of wrongdoing, from money laundering to tax evasion to drug trafficking, and worse. This abuse is possible in part because our states routinely create corporations with hidden owners.

Right now, we require people to provide more information to obtain a drivers license or a bank account, than to acquire a U.S. corporation. Most of our States allow hidden owners to buy companies online within 24 hours of a request. In two States, for an extra $1,000, hidden owners can form a U.S. company within a single hour.

Despite the significant evidence of misuse of U.S. corporations by hidden owners, and despite years of law enforcement complaints, many of our States are reluctant to admit there is a problem. Too many of our States are eager to explain how quick and easy it is to set up corporations within their borders, without acknowledging that those same quick and easy procedures enable wrongdoers to acquire and abuse U.S. corporations both here and abroad.

In 2006, the leading international anti-money laundering body in the world, the Financial Action Task Force on Money Laundering – known as FATF – issued a report criticizing the United States for failing to comply with the FATF standard requiring countries to obtain the true owners – the beneficial owners -- of the corporations formed in their countries. FATF set a goal of two years, until July 2008, for the United States to strengthen its compliance with the FATF standard. We are now more than a year past due with no progress to speak of.

That's why my colleagues and I have introduced S. 569, the Levin-Grassley-McCaskill bill that is the subject of today's hearing. Our bill would require states to add a question to their existing incorporation forms asking for the names and addresses of the beneficial owners of the proposed company. That means an applicant would have to disclose the real individuals who would own or control the company, without using nominee directors, shell companies, or other phony fronts. Penalties would apply to persons who submit false information, and foreign owners would have to supply a passport photograph to a corporate formation agent within the

State. Those corporate formation agents would be required to know their customers and refrain from doing business with suspect clients.

Beneficial ownership information would be made available to law enforcement presenting a subpoena or summons. That information would be available to the public only if State law so provided. The minimal cost of adding a question to State incorporation forms could be paid for with funds already provided to States on an annual basis by the Department of Homeland Security.

Our bill provides a common sense, modest, indeed minimalist approach to solving the law enforcement and homeland security problem created by U.S. corporations with hidden owners. One question, added to existing State incorporation forms, would enable law enforcement to gain access to vital information needed to protect the United States from money laundering, tax evasion, and even terrorist threats.

A host of law enforcement groups have endorsed the bill including the Federal Law Enforcement Officers Association which we will hear from today. It has also been endorsed by groups combating financial crime, corruption and tax evasion, including the Tax Justice Network USA, Global Financial Integrity, Citizens for Tax Justice, Public Citizen, and more. An identical version of the bill was cosponsored by President Obama last year when he was a Senator.

Introducing this legislation wasn't our first choice, as I said at the last hearing. At the request of the States, we waited a year to provide the States with an opportunity to craft their own solution. But the States were unable to devise an effective proposal, in part because they are competing against each other to attract the incorporation fees associated with forming U.S. companies. It's a classic case of competition causing a race to the bottom -- creating pressure on States to allow quick and easy incorporations, and making it difficult for any one State to do the right thing and request the names of beneficial owners.

Only federal legislation can level the playing field among the States, set minimum standards for obtaining beneficial ownership information, stop the creation of U.S. companies with hidden owners, and bring the United States into compliance with its international commitments.

One last point. Many of you know that, for years, I have been fighting offshore secrecy laws that enable wrongdoers to secretly control offshore corporations. We've made some progress on that front, and more is hopefully coming. But one of the impediments we run into in combating offshore secrecy is the claim by some offshore jurisdictions that the United States itself promotes corporate secrecy. A report released by Tax Justice Network earlier this week asserting that Delaware provides more corporate secrecy than Switzerland demonstrates that we need to get our own house in order and comply with FATF's international standards on beneficial ownership.

Corporations are intended to shield owners from personal liability for corporate acts, not hide ownership. But today, the corporate form is being corrupted into serving those who use the corporate veil to hide their identities while committing crimes or dodging taxes and robbing our treasury and taxpayers of billions of dollars each year. It is past time to stop this misuse of the corporate form. But if we want to end inappropriate corporate secrecy offshore, we need to stop it here at home, and start helping instead of impeding law enforcement efforts to combat terrorism, money laundering, tax evasion, and other wrongdoing.

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1	Company Name Private	Nevada	10/22/1928	80 years 10 months 7 days		Available
2	Company Name Private	Georgia	8/1/1955	54 years 0 months 28 days		Available
3	Company Name Private	Nevada	1/4/1956	53 years 7 months 25 days		Available
4	Company Name Private	Nevada	4/26/1957	52 years 4 months 3 days		Sold
5	Company Name Private	Florida	8/14/1959	50 years 0 months 15 days		Available

Excerpt from http://goriskfree.com/existing-company/existing-companies-list (as of October 19, 2009).
Prepared by Senate Permanent Subcommittee on Investigations, October 2009.

U.S. Corporations Associated with Viktor Bout

Viktor Bout, indicted in the U.S. for conspiracy to kill United States nationals, conspiracy to acquire and use anti-aircraft missiles, and conspiracy to provide material support or resources to a terrorist organization.

Airbas Transportation (Texas)

Central African Development Fund (Texas)

Continue Professional Education (Texas)

Daytona Pools (Texas)

DHH Enterprises (Texas)

IB of America Holdings (Texas)

Orient Star Corporation (Texas)

San Air General Trading (Texas)

Trans Aviation Global Group (Texas)

Vial Corp. (Delaware)

Yuralex Corp. (Delaware)

Air-Cess (Florida)

Source: Department of Treasury, Office of Foreign Assets Control; 2002 Interpol Request, Based on Belgium; International Consortium of Investigative Journalists

Prepared by Senate Permanent Subcommittee on Investigations, November 2009

Statement of Senator Tom Carper
Before the Committee on Homeland Security and Governmental Affairs
"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

I want to welcome our witnesses today. Thank you for joining us today and for your testimony.

I want to thank Chairman Lieberman and Senator Levin and their staff for working closely with my staff, as you studied this topic and put this hearing together. I'm grateful that we have a chance to hear from other perspectives, many of which we did not hear from at our last hearing, about this important issue.

Every member of this Committee is committed to finding new ways to combat money laundering. As we heard at our last hearing this summer, law enforcement is facing some challenges in identifying money launderers and others who perpetrate financial crimes.

However, we also need to ensure that we don't punish the thousands of legitimate businesses and business owners in this process.

At our last hearing, we heard from law enforcement, the Secretaries of State and the Uniform Law Commission. I'm pleased that we'll hear from Treasury and the corporate community today, especially with respect to the impact this bill will have on small business.

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We are relying on our small businesses to help pull us out of this economic downturn. With the uncertainty these businesses already face with respect to the real issues we in the Senate are working on - taxes, health care, climate change and financial regulatory reform – we certainly do not need to put more financial pressure or regulatory burdens on this important sector of our economy.

As currently drafted, the bill exempts publicly-traded corporations and the businesses they form. Meanwhile, the bill applies to more than ten million small businesses in the United States placing them at a competitive disadvantage to their larger brethren. Is this really the best possible way to combat money laundering? And since the bill notably exempts partnerships and several other business forms, including sole proprietorships, won't criminals just find another entity under which to conduct their criminal enterprises?

I know some of us are confused as to why we are discussing this issue in this Committee and not the Banking Committee which has jurisdiction over anti-money laundering policy. The reason is that the bill permits states to redirect their federal Homeland Security dollars to comply with its provisions. We need to ensure that we have very good reasons to deprive police, firefighters and other first responders of very limited federal funds before we move forward.

Recent press articles and reports have unfairly singled out the United States and notably my state for its corporate laws. A report by the Tax Justice Network, that is represented on our second panel today (and notably funded by the Ford Foundation in Michigan), asserts that the United States and the sub-jurisdiction of Delaware are the most secretive jurisdictions in the world. The report actually rates the transparency of the United States above other jurisdictions. But because the report applies a weighting factor that is based on the size of the United States' economy, the formula results in the U.S. receiving the highest secrecy index in the world. Without such a weighting, the U.S. would be tied with 16 other jurisdictions for 15th place.

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Let me very clear that the report provides no evidence to support its assertions. In fact Delaware's state company formation laws are essentially identical to laws on the books in Michigan, Connecticut, Missouri and many other states. Of the 12 criteria used by the report's authors to establish the secrecy rankings, six are matters purely of federal law or compliance and one of the criteria was based on whether the jurisdiction answered a survey, which Delaware's Secretary of State asserts it never received. Even more troubling, no other state in the United States was included in the survey. It appears, even to the most casual observer, that this report may have been contrived to achieve a particular result.

In fact, Delaware is doing a number of things to deter criminal enterprise and has enacted laws that provide law enforcement with better access to the information they need to prevent and solve crimes.

For example, Delaware was the first state in the nation to adopt legislation responding to the concerns expressed by law enforcement regarding illicit practices of registered agents. Delaware now regulates Commercial Registered Agents and has successfully removed a number of registered agents from doing business in our State.

Delaware requires every business entity to provide the name, address and phone number of a designated communications contact person that is available to law enforcement. And Delaware responded to international criticism that U.S. company law permits companies to issue bearer shares, stocks certificates whose record of ownership is not maintained by the issuing company, when we explicitly banned the practice in statute to be consistent with long-established Delaware case law.

We have heard from a number of diverse interests with respect to this bill. The National Association of Secretaries of State, the United States Chamber of Commerce, the National Association of Manufacturers, the National Conference of State Legislators, the American Bar Association and others all have raised legitimate concerns with S. 569.

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And as we will hear from the Treasury Department in testimony today, even the international community has been unable to comply with FATF recommendations on beneficial ownership and therefore unable to find a suitable way to date to address these complex issues.

We heard from the Uniform Law Commission at the last hearing and they have worked on an approach that is designed to balance all the interests – providing greater transparency, respecting state primacy and mitigating the negative impacts on the economy and small business.
There are a number of reasons for us to encourage more transparency and disclosure with respect to ownership of legal entities. However, I fear that S. 569 would impose undue burdens on state authorities and legitimate businesses—especially our struggling small business -- at a time when the U.S. financial system and the domestic economy are under severe stress.

I believe there is a balance that we can achieve by working together. We should start with respecting the job that our governors and Secretaries of State are doing in their individual States and through the Uniform Law Commission. I also appreciate the work that has been done since our last hearing at the Departments of Justice and Treasury. Together, I am confident that we can achieve an approach that works for all stakeholders.

Thank you to our Chairman for holding this hearing and thank you Senator Levin for working so hard on this issue as we try to ensure that we get this right. Let's work together on an approach that works for all stakeholders. There is a lot at stake.

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Senator John Ensign
Hearing on
"Business Formation and Financial Crime: Finding a Legislative Solution."
Homeland Security and Governmental Affairs Committee
Opening Statement
November 5, 2009

Thank you, Mr. Chairman. I am pleased to join you here today to discuss S. 569, the Incorporation Transparency and Law Enforcement Assistance Act.

This is a very important piece of legislation because it affects a number of different issues, not the least of which is its impact on the small business community, which serves as the backbone of our economy. Corporate law has long been within a state's domain.

By forcing states to amend their individual laws on corporate formation, Congress is effectively imposing a federal standard on business creation, ignoring the particularities of each state's business culture. With such a new federal standard, there is no incentive to choose one state over another when deciding where to form a business. This will hurt many business-friendly states such as Nevada.

Businesses choose Nevada as their state of incorporation because of our state regulatory climate, tax situation and flexibility for companies to run their businesses as they like. This week, I received comments from the Nevada Secretary of State for this hearing that I would like to submit for the record.

If enacted, S.569 would require my state to add additional staff, undertake an extensive rewrite of the e-Secretary of State processing system and deploy a new system, maintain a separate nonpublic database, and deal with other operational infrastructure needs. According to their office, the estimated cost for initial implementation could reach as high as $10 million, with ongoing costs of approximately $1 million annually.

These are costs that Nevada simply cannot afford.

As a former small business owner, I know firsthand how difficult it is to start and grow a business. It is certainly more difficult in today's economic environment. Every dollar spent on the burdensome requirements under this bill is one less that can be reinvested in the business.

Too often in Washington, we see unintended consequences of bills that, while they have a valuable purpose, turn out to be overreaching in their application. I fear that is the case with this bill. It will result in significant regulatory and compliance costs that may have a chilling effect on the creation of new business and new jobs at a time when our economy can least afford it.

The term "beneficial ownership" as defined in the bill is simply too broad. Rather than qualifying it by some clear cut standard, the language in the bill is borrowed from the Treasury Department's use of the term to determine the proper taxpayer on a bank account. Because of the number of different entities involved, this is not a workable comparison for corporations and LLCs. It leaves open the possibility to interpret the definition differently.

Rather than risk the harsh penalties associated with noncompliance, entrepreneurs will be encouraged to register their businesses only after consulting with certain professionals, such as attorneys or accountants. The expense associated with the new registration process will simply be too great for many smaller start-up businesses to bear, resulting in less business activity and less job creation.

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Mr. Chairman, we are not the first economic power to consider the regulatory system proposed under this bill. In fact, efforts to enact a similar regulatory scheme have failed in other jurisdictions, most notably in the U.K. I understand that one of the witnesses in the Committee's last hearing on the topic mentioned this. The U.K. considered a system requiring up-front disclosure of beneficial ownership, as defined in a manner consistent with the definition in S.569. The U.K. authorities rejected this approach, concluding that 'there were significant disadvantages and no clear benefits, particularly when taking into account the costs of introducing such measures.'

As a basis for their conclusion, these authorities noted that 'those engaged in criminal activities would not provide true information about the beneficial owners' and that 'disclosure would result in misleading information being included on the register.' According to these authorities, requiring further details of beneficial ownership 'would be harmful to investigations through the resulting misleading information provided by both criminal and innocent shareholders.'

Mr. Chairman, it is my hope that we can continue to work together on this very important issue to ensure that the needs of law enforcement are adequately met, while not overburdening our states or business communities. Thank you.

51788.290

Prepared Statement of Senator Roland W. Burris
"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

Thank you Chairman Lieberman and Ranking Member Collins.

The focus of today's hearing is especially interesting to me. As a legislator, the need to crack down on financial crime is evident, as I know our witnesses will express.

However, as a former Comptroller and Attorney General for the State of Illinois, I have concerns about how we can most effectively close the window of opportunity for criminals with nefarious intentions and also protect the integrity of legitimate American business.

Law-abiding corporations should not have to suffer the consequences of criminals' activities, and I am interested to hear our witnesses' recommendations on how we can deter criminals from incorporating shell companies and lessen the frequency of these cases without placing unnecessary burdens and costs on corporations.

Senator Levin's bill is a critical step forward for the law enforcement community, and I hope today we can address the concerns being raised by small businesses and government agencies.

Regardless of how this legislation evolves, it sends a much-needed message to the criminals and terrorists that the days of quick and easy U.S. business incorporation are coming to an end.

I hope to leave here today with a better sense of how Congress can move forward in a way that places minimal burdens and provides maximum benefits for everyone involved. We must find a way to strike a balance between protecting our nation's entrepreneurial freedom while eliminating the opportunities for criminals to exploit that freedom.

Thank you Mr. Chairman.

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STATEMENT OF SEN. PAUL G. KIRK, JR.
Committee on Homeland Security and Government Affairs
Business Formation and Financial Crime: Finding a Legislative Solution
Thursday, November 5, 2009

Chairman Lieberman, I commend you for holding this hearing today. Preventing the criminal misuse of corporate formation laws is an urgent, but complex task, and I welcome the Committee's reaching out to hear from our expert witnesses today.

Massachusetts has among the strongest rules of any state for requiring information to be provided to regulators during the corporate formation process. According to GAO, the Massachusetts requirements for articles of incorporation include the disclosure of names and addresses for corporate officers and directors, which is beyond the requirements of nearly all other states. Nevertheless, even our state—like nearly all states—doesn't require the collection of beneficial owner information.

This information is a significant loophole that is being exploited by criminals for money-laundering and other scams. We're told that unless shell companies are required to disclose beneficial owner information during the incorporation process, the ability of law enforcement to crack down on such illegal activities will continue to be frustrated.

Senator Levin and his Investigations Subcommittee staff have done remarkable work on this issue. His legislation with Senators McCaskill and Grassley to require the disclosure of beneficial ownership information to state regulators deserves the serious consideration of our Committee.

Our expert witnesses today will provide a range of views on this important issue. Congressional action may have a far reaching impact on law enforcement, entrepreneurs, and state regulators, so it is essential that we have as much information as possible to assess the choices before us.

I'm particularly interested in hearing from our witnesses about ideas to enable law enforcement to obtain useful information for investigations, but without creating unnecessary burdens for states or entrepreneurs.

Again, I commend the Chairman for calling this hearing.

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Testimony of Assistant Secretary for Terrorist Financing David S. Cohen

United States Department of the Treasury

Senate Committee on Homeland Security and Governmental Affairs

"Business Formation and Financial Crime: Finding a Legislative Solution"

November 5, 2009

I. Introduction

Chairman Lieberman, Ranking Member Collins, distinguished members of the Committee, thank you for inviting me to testify today. I am pleased to have the opportunity to present the Department of the Treasury's views on the global challenge of enhancing access to beneficial ownership information in order to combat the abuse of legal entities by those engaging in financial crime.

I would like to begin by thanking Senator Levin for his leadership on this important and pressing topic, and for raising awareness in the U.S. and globally of an issue that is of paramount importance in our efforts to combat financial crime. I would also like to extend my appreciation to colleagues across the government and private sector, here at home and internationally, who have worked with the Department of the Treasury and invested a tremendous amount of time and energy in attempting to address the challenges of making beneficial ownership information more readily available.

My colleagues across the Department of the Treasury, including from the Office of Terrorism and Financial Intelligence, Domestic Finance, International Affairs and Tax Policy, have all contributed to Treasury's thinking on how best to require the disclosure of beneficial ownership information in a way that effectively combats the criminal misuse of legal entities while, at the

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same time, ensuring that we do not unduly complicate the company formation process, which plays such an important role in our nation's economic prosperity. I look forward today to outlining Treasury's approach to this critically important and difficult challenge, explaining the basis for our current thinking, and offering the Administration's views on S. 569, the "Incorporation Transparency and Law Enforcement Assistance Act".

At the outset, it is important to recognize a number of key considerations that have informed our thinking:

First, the ability of criminal and other illicit actors to form corporations in the United States without disclosing their true identity presents a serious vulnerability. It creates a pathway for criminal actors to gain access to the international financial system, and creates significant obstacles in our ability to investigate financial crime. As I will explain, there is ample evidence that criminal organizations and others who threaten our national security exploit this vulnerability.

Second, information on the true beneficial ownership of a legal entity – at the time a business is formed, as ownership changes during its lifespan, and when it seeks to open accounts at financial institutions – is critical to stopping the exploitation of legal entities by criminal actors.

Third, the challenge of enhancing access to the beneficial ownership information of legal entities is complex and requires a global solution. While we work within the Administration and with Congress to address this issue domestically, Treasury is also working with our foreign counterparts to improve global understanding and capability to address this challenge worldwide.

Fourth, in seeking to make beneficial ownership information available in ways that effectively address the misuse of legal entities, we are keenly aware of the need to preserve an efficient and straightforward entity formation process in the United States, and not to create

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unnecessary impediments to accessing the financial system for the vast majority of new and existing businesses that pose no threat whatsoever.

Finally, because we are starting from a situation in which beneficial ownership information is not required at the time of company formation, we believe that even incremental progress in this area is likely to yield substantial positive results.

These considerations inform and shape our views on S. 569. This bill addresses a key issue – namely, helping ensure that information on the beneficial ownership of legal entities created in the United States is readily available to law enforcement for investigative purposes. As I will explain in detail, the Administration believes that S. 569 is an important step in the right direction on this issue, and provides a useful platform on which to construct an effective legislative solution, provided that it is amended and modified in the manner that I describe below. We are fully committed to working with the Congress and our interagency partners to craft legislative text to amend the Bill in order to address our concerns.

My testimony will focus on the following three areas:

(i) The ways in which lax company formation laws are abused by criminals to perpetrate crime while hiding behind the corporate form;

(ii) Treasury's comprehensive approach to enhance access to information on the beneficial ownership of legal entities; and

(iii) Our views on S. 569, in particular the amendments and modifications that we think are necessary to craft legislation that will effectively and efficiently enhance the availability of beneficial ownership information of legal entities created in the United States.

II. Challenges Posed by the Misuse of Legal Entities

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In order to develop an effective way forward in combating the criminal abuse of legal entities through enhanced access to beneficial ownership information, it is essential at the outset to recognize and balance the substantial threat presented by the abuse of legal entities to facilitate financial crime, and the countervailing importance of maintaining efficient processes in creating legal entities and in promoting access to financial services.

The substantial threat presented by abuse of legal entities to facilitate financial crime

Criminal organizations abuse legal entities to obscure the beneficial ownership and control of businesses they operate. This allows criminal actors to gain access to the international financial system – because the true risk associated with providing accounts to these entities is masked – and thus facilitates financial crime. Years of research and law enforcement investigations have conclusively demonstrated the link between the abuse of legal entities, on the one hand, and, on the other hand, WMD proliferation, terrorist financing, sanctions evasion, tax evasion, corruption and money laundering for virtually all forms of serious criminal activity.[1]

As these reports and investigations indicate, this abuse is particularly prevalent with respect to legal entities created in the United States. We know how easy it is for illicit actors around the world to create a legal entity in the United States. And we know that these actors then use the presumed legitimacy of a US-based entity to gain access to the international financial system and disguise the source of their funds or the purpose of their financial transactions. We also know that some disreputable company formation agents in the United States have facilitated

[1] See, e.g., 2007 National Money Laundering Strategy at 63-65; "Potential Money Laundering Risk Related to Shell Companies," FinCEN, FIN-2006-G014, November 9, 2006; S.539, 111th Cong. 1st Session, Section 2 Findings; Senate Committee on Homeland Security and Governmental Affairs: 'Examining State Business Incorporation Practices: A Discussion of the Incorporation Transparency and Law Enforcement Assistance Act.' June 18th, 2009:http://hsgac.senate.gov/public/index.cfm?FuseAction=Hearings.Hearing&Hearing_ID=ef10e125-2c1d-4344-baf1-07f6061611c1; House Committee on Financial Services: 'Capital Loss, Corruption, and the Role of Western Financial Institutions.' May 19th, 2009. http://www.house.gov/apps/list/hearing/financialsvcs_dem/hrfc051309.shtml

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this activity by promoting the ease of setting up a legal entity – in some cases it can be done in a matter of minutes – together with techniques that legally enable individuals behind the legal entity to maintain anonymity even when the legal entity becomes the subject of a criminal investigation.

These practices have been highlighted in a number of public reports, such as the 2006 GAO Report on Company Formation, the 2006 Financial Crimes Enforcement Network (FinCEN) Guidance on Potential Money Laundering Risk Related to Shell Companies, and the 2007 National Money Laundering Strategy. The two prior hearings on beneficial ownership held by this Committee and the Permanent Subcommittee on Investigations also provided detailed testimony from the Department of the Treasury, the Department of Justice, the Department of Homeland Security, the New York District Attorney and others on the extent of this problem.

These reports, and the testimony previously presented to this Committee and its subcommittee, are replete with examples of how criminals and other illicit actors abuse the lax company formation processes in the United States to facilitate their endeavors. These reports and prior testimony from the Treasury Department and other agencies describe in great detail how our existing company formation laws undermine efforts to promote transparency across the international financial system and impede investigations of significant cases of money laundering, terrorist financing, and other financial crime.

It is important to note, however, that the United States is not alone in grappling with this question. Jurisdictions all over the world continue to struggle to find ways of making meaningful beneficial ownership information about legal entities available to relevant authorities. The Financial Action Task Force (FATF), the international policy and standard-setting body for combating financial crime, has issued an international standard stating that "[c]ountries should ensure that there is adequate, accurate, and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities." Out of over 125 jurisdictions assessed against this standard

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by the FATF, FATF-Style Regional Bodies, the International Monetary Fund or the World Bank, the overwhelming majority have failed to substantially comply. In the case of legal entities created in the United States, the FATF has stated that "there are no measures in place to ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities." Bringing our company formation laws in line with FATF's standards is an important objective, especially when, as here, it reinforces a clearly articulated law enforcement priority.

The importance of maintaining efficient processes in creating legal entities and in promoting access to financial services

In working to enhance access to beneficial ownership information, Treasury is also mindful of the very significant interests in preserving efficient processes in creating legal entities and in promoting access to financial services, both of which are essential to a well-functioning economy and the efficient operation of the domestic and international financial system. Foreign and domestic persons with legitimate economic interests rely upon the ability to create legal entities quickly and easily for a variety of entirely beneficial and lawful reasons. In addition, ensuring the ability of legal entities to open bank accounts and otherwise access financial services facilitates entrepreneurship, economic growth and development. In considering ways to enhance the availability of beneficial ownership information of legal entities, we must be careful not to infringe on these entirely legitimate, and fundamentally important, interests.

III. Treasury's Comprehensive Approach to Enhance Access to Beneficial Ownership Information of Legal Entities

The Department of the Treasury has been focused for several years on the question of how best to enhance access to beneficial ownership information to combat the abuse of legal

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entities, and we are currently pursuing a three-pronged approach to advance these interests. Our approach generally balances the need to enhance access to beneficial ownership information of legal entities with the need to maintain efficient processes in creating legal entities and in promoting access to financial services. Our comprehensive approach includes the following elements:

- ***Enhance the availability of beneficial ownership information of legal entities created in the United States:*** Promote legislation that requires (a) the submission of beneficial ownership information at the time of company formation; (b) the obligation to keep that information updated throughout the entity's existence; and (c) the availability of that information upon proper request by law enforcement. To ensure compliance, the legislation must impose significant penalties for failure to abide by these requirements. We are focusing our current efforts on working with our interagency partners and the Congress to amend S. 569 so that it more effectively and efficiently accomplishes these goals.
- ***Clarify and strengthen customer due diligence requirements for U.S. financial institutions with respect to the beneficial ownership of legal entity accountholders:*** Treasury is currently working with the federal financial regulatory agencies to consider guidance for U.S. financial institutions that will clarify when and how financial institutions should identify and verify beneficial ownership as a component of conducting customer due diligence of accountholders that are legal entities. We are also working with the regulatory and law enforcement communities, and consulting with the private sector, to determine whether and, if so, how such due diligence requirements should be strengthened through rulemaking or otherwise.
- ***Clarify and facilitate global implementation of international standards regarding beneficial ownership:*** In 2003 the FATF reviewed and updated its 40 Recommendations for jurisdictions to implement appropriate countermeasures against money laundering. Three of those Recommendations – Recommendations 5, 33 and 34 – specifically address obtaining beneficial ownership information. These Recommendations, however, have created implementation challenges for the overwhelming majority of

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jurisdictions around the world. As we move forward in addressing the issue of beneficial ownership in the United States, we are also working with our counterparts in the FATF to ensure that its standards evolve in a way in which compliance is both achievable and effective. Even if we make progress domestically, failure to achieve consistency internationally will merely shift the locus of the problem to another jurisdiction and fail to address the problems that flow from lack of beneficial ownership transparency.

IV. Amending S. 569 to Enhance the Availability of Beneficial Ownership Information of Legal Entities Created in the United States

The Treasury Department clearly recognizes the need for federal legislation to enhance the availability of beneficial ownership information of legal entities created in the United States. The gravity and complexity of the ongoing abuse of legal entities by a broad spectrum of criminals and others who threaten our national security demand nothing less. And we view S. 569 as a productive step in the direction of requiring the availability of meaningful beneficial ownership information about legal entities created in the United States. We believe that with modifications, S. 569 could serve as the appropriate legislative vehicle to address this issue.

I also want to be clear that Treasury recognizes that there is no perfect solution to this complex problem. Whatever action we take will not prevent all criminals from misusing legal entities to perpetrate financial crime. And whatever action we take will entail some cost and burden in the company formation process. Our goal is meaningful progress, capitalizing on what we have learned over the past few years in studying this problem, and laying the groundwork for future action if it proves necessary.

While Treasury fully supports the objective of enhancing law enforcement access to beneficial ownership information of legal entities created in the United States, in order for us to support S. 569, we believe it must be amended to address the following key issues:

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- ***Clarify and limit the beneficial ownership definition and corresponding information disclosure requirements:*** Under S. 569 as currently drafted, the ambiguity and breadth of the definition of beneficial ownership, coupled with burdensome disclosure requirements, makes compliance uncertain, time-consuming and costly. The definition and application of beneficial ownership information requirements should be sufficiently straightforward and simple in application to work for the full range of covered legal entities – from small, start-up businesses to large, complex legal entities – and regardless of whether the applicant is a foreign or U.S. person.

- ***Eliminate expansion of anti-money laundering obligations to company formation agents in favor of broader civil and criminal federal liability for noncompliance:*** As currently drafted, S. 569 would effectively require Treasury to subject attorneys who provide company formation services for their clients to anti-money laundering regulation, thereby raising substantial legal, policy and practical challenges. Subjecting company formation agents in general to such regulation would also present tremendous administrative challenges for Treasury, largely due to the lack of an existing functional regulator for this industry. We believe S. 569 should not attempt to regulate company formation agents under the Bank Secrecy Act, but instead should establish clear and significant federal criminal and civil liability for persons who fail to provide accurate beneficial ownership information as required by law.

- ***Establish documentation requirements:*** As currently drafted, S. 569 does not establish any documentation requirements for beneficial owners who are U.S. persons, although it does require foreign persons to provide a copy of a passport page on which the beneficial owner's photograph appears. In our view, S. 569 should require robust documentation for all beneficial owners, foreign and domestic, to be held within the State and made available upon proper demand by law enforcement. Generally, that documentation would be a credible and legible copy of government-issued photographic identification, such as driver's license or a passport.

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- ***Require further study of illicit finance vulnerabilities associated with the transfer of legal entities and potential solutions for updating beneficial ownership information:*** S. 569 allows for company formation applicants to update their beneficial ownership information in an annual filing with the State. This time gap introduces a significant vulnerability for abuse upon the transfer of a legal entity and requires further study.

- ***Preserve State Homeland Security Grant funds:*** As currently drafted, S. 569 authorizes States to use State Homeland Security Grant funds to carry out the obligations imposed by the Bill. These funds, however, are already relied upon by States to finance first responders in preparing for and responding to emergency situations. In our view, S. 569 should not authorize States to draw from the State Homeland Security Grant program to defray the costs of implementation.

Based on recent discussions with our interagency partners and the Congress, we firmly believe that S. 569 can be amended to address these key issues. We are fully committed to working with our interagency partners and the Congress to make this happen, and we have already begun to draft proposed legislative text to address the five concerns I have described above.

V. Conclusion

Looking ahead, Treasury intends to make progress on each of the elements of our comprehensive beneficial ownership strategy to address the abuse of legal entities in facilitating all forms of financial crime:

- Treasury will work in earnest with the Congress and our interagency partners to have S. 569 amended along the lines described above in order to enhance the availability of beneficial ownership information of entities created in the United States in an effective and workable manner.

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- In consultation with the federal financial regulators, Treasury will be considering guidance to the financial community, and will consider engaging in rulemaking, to clarify and enhance customer due diligence obligations for financial institutions regarding the identification and verification of beneficial ownership information of legal entity accountholders under a risk-based approach.
- Treasury will continue to work with the Financial Action Task Force to clarify and facilitate implementation of international standards addressing beneficial ownership, building from our domestic experience.

Although we know that there is still much to do, we have seen tremendous progress over the last several years. We have developed and are moving forward with a comprehensive approach to address the challenges of beneficial ownership. With respect to the particular challenge of enhancing the availability of beneficial ownership information of legal entities created in the United States, we have moved from discussions about the problem to discussions about solutions. This is no simple accomplishment, especially considering that the issue involves the highly sensitive issue of modifying the process by which corporate entities are created.

On behalf of the Department of the Treasury, I would like to thank the Committee for inviting me to testify today, and I look forward to answering your questions.

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Department of Justice

STATEMENT OF

JENNIFER SHASKY
SENIOR COUNSEL TO THE DEPUTY ATTORNEY GENERAL

BEFORE THE

COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

ENTITLED

"BUSINESS FORMATION AND FINANCIAL CRIME: FINDING A LEGISLATIVE SOLUTION"

PRESENTED

NOVEMBER 5, 2009

JENNIFER SHASKY
SENIOR COUNSEL TO THE DEPUTY ATTORNEY GENERAL
Before the U.S. Senate Committee on the Homeland Security and Governmental Affairs
November 5, 2009

Good afternoon, Chairman Lieberman, Ranking Member Collins and distinguished Members of the Committee. I am honored to appear before the Homeland Security Committee to discuss S. 569 which addresses the need for greater transparency in corporate formation in the United States.

Several months ago the Department testified before this Committee about the difficulties both foreign and domestic law enforcement agents face when investigating U.S. shell companies. The testimony identified the need for improved access to beneficial ownership information of U.S. companies and the four areas of concern: (1) the need to identify the beneficial owner of a legal entity at the point of formation; (2) the need for law enforcement to obtain accurate and timely information about the owners of existing U.S. legal entities; (3) the appropriate means of addressing the challenge of the transfer of corporate ownership—especially from corporate formation agents to corporate brokers; and (4) the penalties necessary to discourage the misuse of U.S. companies.

As I will explain in detail, the Administration believes that S. 569 is an important step in the right direction on this issue, and provides a useful platform on which to construct an effective legislative solution, provided that it is amended and modified consistent with several recommendations that I describe below. We are fully committed to working with Congress and our interagency partners to craft legislative text to amend the legislation in order to address our concerns.

The Lack of Transparency in Corporate Formation Inhibits Law Enforcement Efforts

While the topic of corporate transparency does not readily evoke images of the criminal and extremist underworld, it must not be overlooked that some of the worst actors seek to exploit the lack of transparency associated with U.S. companies to harm our national and economic security. For example, Viktor Bout, designated by the U.S. Department of Treasury, Office of Foreign Assets Control as an arms merchant and war profiteer, used U.S. shell companies to further his illegal arms trafficking activities. The Sinaloa Cartel, one of the major Mexican drug trafficking organizations, is believed by U.S. law enforcement to use U.S. shell companies to launder its drug proceeds. Semion Mogilevich, recently named to the Federal Bureau of Investigation's Ten Most Wanted Fugitives List, and his criminal organization are charged with using U.S. shell companies to hide their involvement in investment activities and to launder money.

Each of these examples involves the relatively rare instance in which law enforcement identified the perpetrator misusing the U.S. shell companies. Far too often, we are unable to do so. Take for example the instance in which a foreign partner notified U.S. law enforcement after uncovering a plot to send military cargo, mislabeled as farm equipment, to Iran. Why contact

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U.S. law enforcement? Because the seller listed in the shipping documentation was a U.S. shell company. Unfortunately, through this case and others, our foreign partners have learned that, in most instances, U.S. law enforcement cannot identify the individuals who own and misuse U.S. legal entities.

The following case example further details how a lack of corporate transparency prevented investigators from identifying the perpetrators of a large cyber fraud and provides some insight into why such an experience discourages law enforcement from even pursuing such investigations.

In this case, numerous U.S. individuals complained to law enforcement about losing money when attempting to purchase automobiles over the Internet via an online auction website. A subsequent investigation revealed that the criminal participants would identify a legitimate vehicle for sale on the Internet site and then pose as the purported sellers of that vehicle. To appear legitimate, the criminal participants would direct interested buyers to transfer payment for the cars to entities that had the same name as licensed and bonded escrow companies located in the United States.

Victims were then directed by the false escrow companies to wire funds to "Bank A," a financial institution located in New York, for further credit to a named U.S. shell company. Based upon the wiring instructions, the victims believed that they were sending money to a U.S. bank account held by the escrow company in New York. In reality, the victims were being tricked into sending their funds to an account maintained under the name of the U.S. shell company at a bank located in Eastern Europe – "Bank B." Investigators discovered that Bank A in New York merely held a correspondent account in the name of Bank B such that any money the victims sent to Bank A went into the account of Bank B. As is common practice, the correspondent account records for Bank B, held at Bank A, did not contain details on the beneficial owners for each of Bank B's account holders in Eastern Europe, and thus no information on the beneficial owners of the U.S. shell company.

Corporate documents for the U.S. shell company obtained from the Secretary of State of the relevant state provided names of two individuals acting on behalf of corporate entities in Tortola, British Virgin Islands, both with addresses in Tortola. The U.S. shell company was associated with two U.S. addresses, both of which were addresses of a U.S. corporate formation agent and used simply as mail drops. The U.S. corporate formation agent did not know and is not required to know, by law, who controls the U.S. shell company.

It required three formal treaty requests, over the span of nearly two years, to obtain documentation from the Eastern European country in the example above that specifically identified the individual who was the signatory on the bank account held in Bank B in the name of the U.S. shell company. A copy of this individual's foreign passport (which was from yet another country) had been maintained by Bank B. However, a review of the bank records for the account in the name of the U.S. shell company revealed that funds from the U.S. victims received into that account had been transferred out of that account into another account in the name of another U.S. shell company, thereby necessitating a repeat of the entire process,

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including additional treaty requests to identify additional bank account signatories. Those signatories all held foreign passports, none of which were from the Eastern European country.

Ultimately, this case was never charged because investigators were unable to establish whether the signatories on the bank accounts had knowledge of the underlying fraud that generated the funds or whether they were the beneficiaries of those funds as opposed to merely financial service providers responsible for moving the funds. In essence, the investigators could not establish the beneficial owner of the U.S. shell company and its assets (the fraud proceeds).

This case illustrates how a lack of corporate transparency in the United States can frustrate an investigation at several different junctures. First, the success or failure of a U.S. investigation requiring the identification of a beneficial owner of a U.S. shell company depends upon the existence and effectiveness of a U.S. treaty relationship with a foreign country. An investigation is often hindered when no treaty relationship or an ineffectual treaty relationship exists with another involved country and the case reaches a dead end. However, the investigation can also be frustrated even when, as in this case, a viable treaty relationship exists due to the significant investigative delays associated with treaty requests that result in criminal participants staying several steps ahead of law enforcement, the trail turning cold, or the case being terminated for statute of limitations or other delay-related reasons.

Extent of Problem

In criminal investigations, law enforcement often faces a problem uncovering the criminals responsible for using shell companies to further their criminal schemes. This is due, in large part, to the lack of beneficial ownership information gathered on shell companies. Although the Department does not collect statistics on the scope of this problem, the following information reported by investigators and prosecutors indicates that the problem is widespread:

When questioned about whether a lack of information about a U.S. shell company had hindered their investigations, nearly all of a 75-person audience consisting of federal investigators and prosecutors from throughout the country responded that it had. The audience — including investigators from nine federal law enforcement agencies and prosecutors from a variety of districts and offices — was attending a financial investigation seminar designed to teach them how to investigate the financial aspects of international criminal organizations. The instructor, who was lecturing on U.S. shell companies, asked the members of the audience to raise their hand if they had ever reached a dead end in one of their investigations because of a U.S. shell company. Nearly every person in the room raised his or her hand. Departmental instructors report that such a response is common in money laundering courses delivered both domestically and abroad.

Likewise, participants in Suspicious Activity Report (SAR) Review Teams report that many investigations involving U.S. shell companies are never even pursued. SAR Review Teams exist in most judicial districts around the country and are comprised of prosecutors, federal investigators, and often state and local law enforcement. Their mission is to review SARs and uncover links that can lead to criminal prosecutions, forfeitures, and seizures. The teams report that often they do not pursue leads contained in the SARs under review because the

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reported suspicious financial activity was done through an account held in the name of a U.S. shell company. Realizing that beneficial ownership information for the U.S. shell company is not available in the United States and the underlying account under review was established in a foreign country, the teams never pursue an investigation. The total amount of money associated with suspicious financial transactions involving U.S. shell companies that is reported in SARs on an annual basis is quite high, often in the billions of dollars.

Finally, as detailed in the Department's earlier testimony, the lack of beneficial ownership information for U.S. entities also provides challenges for the United States when responding to requests for assistance from our foreign partners. In particular, we testified about the scope of the problem and the rise in requests for information related to shell companies during 2004 and 2005. The Department's Office of International Affairs (OIA) reports that, since that time, OIA has spent considerable effort educating our foreign counterparts about our inability to obtain and provide beneficial ownership information. As a result, OIA reports that it has seen the number of requests drop. Not unexpectedly, foreign investigators and prosecutors continue to approach DOJ speakers at foreign events to complain about investigations that were terminated due to their inability to obtain beneficial ownership information about U.S. companies. This problem not only damages our reputation but is also counterproductive to our efforts to join with foreign counterparts in a global offensive against organized crime and terrorism.

Discussion of S. 569

The Administration believes that S. 569 is an important step in the right direction on this issue, and provides a useful platform on which to construct an effective legislative solution. We have a number of recommendations that should strengthen S 569 and are fully committed to working with the Congress and our interagency partners to craft legislative text to amend the Legislation in order to address our concerns. The Administration recognizes, however, that no legislation can provide a perfect solution to this problem. Whatever legislation we enact will have some costs to legitimate businesses and will have some weaknesses that criminals can exploit. Despite this fact, the Administration is committed to taking what it has learned from studying this problem and working with Congress to craft a legislative solution that has maximum effectiveness with minimum burden on legitimate businesses.

As noted in the Department's previous testimony, the first and most critical issue facing law enforcement is the ability to identify the living, breathing beneficial owner of a legal entity. As currently drafted, S. 569 takes a significant step forward on this point by including a definition of beneficial ownership that would apply across all 50 States and ensure that criminals cannot exploit definitional gaps between differing State systems. However, the Administration would like to work with this Committee to amend and further refine that definition to address concerns in the business community that the ambiguity and breadth of the definition will make compliance uncertain, time-consuming, and costly. We believe the interests of law enforcement can be met, while also ensuring that the definition is sufficiently straightforward and limited in application to work for the full range of covered legal entities.

Once a more limited application is achieved, the Administration recommends that S. 569 also be strengthened to require a credible and legible photocopy of government-issued

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identification for each beneficial owner to be held within the State. The provision and retention of such information is critical to any meaningful effort to promote transparency by assuring that law enforcement will have a "name and a face" for all beneficial owners. Currently, S. 569 requires beneficial owners to provide their names and addresses to the State -- a requirement that should remain in place. However, the Legislation only requires foreign beneficial owners to take the additional step of providing a legible photo identification. The Administration recommends that this requirement be extended to all beneficial owners. Recognizing the challenges, both fiscal and technological, that come with this effort, we believe it would be sufficient for the photo identification to be maintained in the State, and not necessarily with the State, subject to the enhanced civil and criminal penalties addressed later in this testimony.

The second critical issue identified by the Department is the need for law enforcement to be able to obtain beneficial ownership information in an accurate and timely manner. S. 569 fully addresses this concern.

Third, the Department noted that many problem companies encountered by law enforcement are so-called "shelf", or aged, companies. Law enforcement has seen time and again that criminals can easily throw investigators off the trail by purchasing shelf companies and then never officially transferring the ownership. In such cases the investigation often leads to a formation agent who has long ago sold the company with no records of the purchaser and no obligation to note the ownership change. To address this vulnerability and prevent criminals from simply wholesale shifting their operations to "shelf" companies to avoid the reach of S. 569, we believe the Legislation should address the transfer of beneficial ownership. While S. 569 partially addresses this problem, the Administration recommends further study of the vulnerabilities associated with the transfer of legal entities and potential solutions for updating beneficial ownership information so that we can close any remaining vulnerability gaps.

The Department's fourth and final concern is that any bill should contain a persuasive enforcement regime. Federal criminal penalties, in particular, are an essential ingredient for law enforcement to target professional money launderers and their clients in the criminal and extremist underworld. To this end, the Administration recommends eliminating the expansion of anti-money laundering obligations to company formation agents – a significant administrative and regulatory burden -- in favor of broader civil and criminal federal liability for noncompliance. Specifically, the federal penalties in S. 569 could be amended to include federal criminal and civil liability for persons obligated to hold beneficial ownership information, if they fail to meet their statutory obligations, including an obligation to maintain the confidentiality of subpoenas and other legal process.

Finally, the Department notes that S. 569 authorizes states to use State Homeland Security Grant funds to carry out the obligations imposed by the legislation. These funds are already relied upon by States to finance first responders in preparing for and responding to emergency situations. The Administration believes that S. 569 should not authorize states to draw from the State Homeland Security Grant program to defray the costs of implementation.

I would like to conclude by expressing the gratitude of the Department of Justice for the continuing support that this Committee has demonstrated for anti-money laundering enforcement. In particular, the Department would like to thank Senator Levin and the Committee for its hard work on S. 569. The Department believes that we must continue to

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strengthen our anti-money laundering laws, not only to disrupt and dismantle drug trafficking and other international criminal organizations, but also to fight terrorism, white collar crime and all forms of criminal activity that generate or utilize illegal proceeds.

The Department is committed to safeguarding the privacy and civil liberty interests of Americans and is confident that those interests are not at risk when the federal government takes sensible steps to rein in the abuse of shell corporations. We in the Department of Justice look forward to working with Congress and with our colleagues in the Department of Treasury and the Department of Homeland Security, to address the issues identified in this hearing.

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Testimony before the Senate Committee on Homeland Security and Governmental Affairs
Thursday, November 5, 2009

Statement of David H. Kellogg
President and CEO of Solers Inc.

INTRODUCTION

Thank you Chairman Lieberman, Ranking Member Collins and members of the Committee on Homeland Security and Governmental Affairs, for the opportunity to testify today on the impact to business if S.569, the *Incorporation Transparency and Law Enforcement Assistance Act*, were to pass and be enacted. Solers believes strong corporate governance and capital formation are vital part of any vibrant economy. We also agree with the priority of combating terrorism and money laundering. However, I must express my serious concerns with S.569 because it does not appear to combat money laundering and places additional burdens on American businesses during the worst economic downturn in 75 years. While I agree with the stated goal of your legislation, I have significant concerns with your implementation.

Founded in 1999, the Solers employee owners are proud to be a part of the effort to make our Nation safer through our primary lines of business -- Net-Centric Systems and Mission Support Services. We have a strong working relationship with the Department of Defense and Intelligence Community and our mission at Solers is to find practical and innovative solutions to meet the challenges they face in fulfilling their vital missions.

To achieve this critical mission for our Nations defense, Solers relies on our principal asset -- our talented staff, which is comprised primarily of engineers and scientists. We currently have 200 employees and hope to grow our workforce in the coming years. By providing a flexible and supportive work environment coupled with well-structured incentives, Solers has consistently attracted and retained high quality staff. Solers' successful staff performance and retention has led directly to numerous long-term client relationships built upon delivering on our commitments.

An important component to attracting and retaining our high performing team is that our employees have an opportunity to own a piece of Solers. After being employed by Solers for about one year, employees are eligible to become shareholders. Therefore, Solers is privately held by its employees, former employees and directors and is a Virginia "C" corporation

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with about 140 stockholders. We anticipate that we will grow to approximately 180 stockholders by early next year. The majority of Solers staff think of themselves as owners at Solers and we have found that our employee owners greatly value this benefit. With our employees owning stock in the company, they satisfy the definition of "beneficial owners" under S. 569.

CONCERNS

Upon review of S. 569, I was struck by several issues that I believe would both impede the effectiveness of the legislation, such that it would not be an effective deterrent to illegal activity and at the same time penalize legitimate, law abiding businesses and their workers.

NO CLEAR DEFINITION OF BENEFICIAL OWNER

First, I would like to speak to the difficulty of determining beneficial ownership under S. 569. The bill lacks a clear-cut definition of beneficial owner that can be understood and applied by lawyers, let alone by the common business person like me. The definition derives from Treasury regulations related to the identification of beneficial owners of accounts. Furthermore, the definition is overly broad in its breadth and scope to the extent that it may be impossible for a business to comply with a standard that can be subjectively interpreted.

For example, as the bill is now written, any shareholder, family member of a shareholder, an individual who has the power of attorney for financial purposes of a shareholder, an accountant employed or retained by the business, lien holder, bondholder of the company, credit card company or financial institution extending credit to the business and any other individual who may have a legal interest in or entitlement to the company and its assets will be required to be reported as a beneficial owner. Any change in the relationship between any of these entities and the business will require new documents to be compiled and filed with the appropriate legal authorities.

For instance the change in the familial status of a shareholder could change the status of beneficial owner under the bill. With such an overbroad definition, the company would be required to track and file information that is beyond its control. The vagueness and lack of precision in a standard that requires an assessment of when as "practical matter" a person exercises control is particularly troubling in a law that carries criminal penalties.

The ambiguous nature of S. 569's beneficial owner definition is unworkable even when considering more practical and mundane business

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arrangements, such as when entities are owned by other entities. S. 569 require corporations and limited liability companies to trace ownership to an individual. This means, for instance, that if a record owner of a corporation is another entity, such as a corporation, limited liability company, partnership or trust, then the corporation would need to know the identity of all of the shareholders, members, partners and beneficiaries of the record owner entity. And if that record owner entity is owned by another entity, and if that entity is owned by another entity, and so on, the corporation would be required to trace ownership and control all the way up the chain until it reaches individuals. This would very difficult and nearly impossible to do.

Also, S. 569 requires keeping track of and reporting any changes in beneficial ownership ongoing complexity and potential liability to businesses. Take the example where one of our employee stockholders decided to own her Solers shares in a trust or family limited partnership, which are often used estate planning tools. For a number of reasons over time, the beneficiaries of the trust or the limited partners may change – hardly an unusual occurrence. Unless the employee had the presence of mind to inform the company, they would have no way of knowing about these changes and could potentially violate the law.

This hidden trap in S. 569 applies equally to other common occurrences in business. For instance, the sale of shares by a shareholder of Corporation X that owns shares of Corporation Y would probably never be known to Corporation Y without being notified of the sale by Corporation X. In all of these examples, the stockholder on corporation Y's records never changed.

Unquestionably, preventing money laundering, tax evasion and other illegal activities are laudable goals, but S. 569's indiscernible requirement to disclose beneficial owners based on the uncommon and vague definition used in this bill fails to advance these goals. Criminals will simply ignore S. 569's requirements and legitimate companies will be unable to understand or comply with them. Criminals who desire the benefits of limited liability associated with forming corporations or LLCs will simply lie in their disclosures. They can also select different forms of business entities other than the two regulated by this bill to conduct their illicit activities.

This bill will place burdens upon law abiding companies, cause a chilling effect upon potential avenues of investment for small businesses, creating an economic disadvantage for anyone who were to choose a corporation model. It should be remembered that companies such as Microsoft, Wal-Mart and Ford

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have all started as small corporations and grown into large ones. Faced with the expensive, time consuming and virtually impossible task of determining beneficial owners, my prediction is that if S. 569 is passed, some law abiding entrepreneurs creating or running corporations subject to this law will forego the corporate model and employee ownership, and the benefits it gives workers, rather than risk the potential of up to three years imprisonment.

OWNER PRIVACY

Second, I would like to speak to the privacy rights and safety of investors, business owners and in Solers case, our employees. S. 569 would require states to amend their incorporation law practices to comply with new federally mandated standards. This would include providing and documenting the detailed personal information, including home address, of all the beneficial owners of a non-public corporation or limited liability company and further place the burden on business to have it updated in the event of any change.

According to the National Association of Secretaries of State, at least 38 states would require compliance with their own internal "Right to Know Laws" and other regulations. Once the states collect this data it is immediately made public, at which point many trade journals actually issue reports with this information. Needless to say, this private information is now in the public domain.

I fear that the "beneficial owner" list of Solers employee owners will be used by recruiters and competitors to solicit my staff. Like any professional services firm, my staff is my most valuable asset and providing a list, complete with home addresses, to professional recruiters and competitors puts Solers at a distinct disadvantage relative to the numerous public companies that are my competitors. In short, without a privacy protection treating Solers beneficial ownership information as sensitive financial data, S. 569 will put Solers at a disadvantage to my public company competitors. We urge you to consider a privacy provision for the beneficial ownership information to prevent its use by competitors, recruiters and other parties or activist groups who would use it for their own purposes.

CORPORATE COMPETITIVENESS

When operating in the competitive environment, businesses make decisions and purchases and seek to conceal them from their competitors. It is a perfectly legitimate business practice to protect trade secrets. This is true for my company or any business to ensure that the business entity can receive the first movers' advantage, as we seek to develop markets.

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These companies are not interested in breaking the law; they are interested in being a competitive, effective force in their industry. By passing S. 569, small companies will be placed at a competitive disadvantage in relation to large public companies, partnerships, sole proprietorships and even foreign competitors. Further, all U.S. companies would operate at a competitive disadvantage to the international community, because international competitors could use this signaling information to block or bid up legitimate investment.

Venture capital firms invest in new product lines and small companies and form a vital cog in the formation of capital for small businesses. However, this financial backing, sometimes known as angel financing, is undisclosed so as to prevent market signaling. Nevertheless, these financing vehicles would now have to be publically disclosed, potentially cutting off start up financing for small businesses that account for 80% of the job growth in the United States.

Competitors could also use this information to intimidate investors out of investing in a particular company. If this private information is publically disclosed, what is to stop competition from filing lawsuits against particular beneficial owners? This could also be done through the work of activists groups devoted to intimidating legitimate capital formation.

Furthermore, it is unclear how S.569, by targeting only nonpublic and limited liability corporations, would stem money laundering or terrorist financing. Bad actors will not hesitate to exploit that large loophole and simply form business entities not covered by S. 569, leaving only legitimate businesses with an unreasonable burden and possible criminal penalties for non compliance. In that regard, we are punishing the whole class, because of one student's bad behavior.

HOMELAND SECURITY

S. 569 could also create other unintended consequences including new and onerous recordkeeping requirements on states. While estimates vary by state, the National Association of Secretaries of State estimates that the cost of implementing S. 569 in California could be as high as $17.5 million dollars.

As the legislation is currently written, the funding for the program would be siphoned from homeland security grant funding to the states. As a private citizen, I would like to express hesitation on this point, because I do not believe that funding for this program should be taken from fire fighters and first responders and other important homeland security functions of the states. If

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the mandate is important, then Congress should fund it fully and further provide incentives for business compliance rather than punishments. Legitimate businesses are not looking to skirt legal requirements, but it will be these same legitimate businesses that are penalized for non-compliance while illegal actors find other ways around the law.

FOREIGN INCORPORATION PRACTICE AND FATF

I think it is also important to consider S. 569's requirements in relation to what other countries require. At least one European Union country, the United Kingdom, considered a beneficial ownership disclosure system similar to that being mandated by S. 569 with an almost identical definition of beneficial owner.[1] According to FATF's evaluation, the United Kingdom engaged consultants in 2002 to produce a report on the proposed system and then subjected it to public consultation.[2] The conclusion of this process with respect to this strikingly similar proposed beneficial ownership disclosure system was "that there were significant disadvantages and no clear benefits, particularly when taking into account the costs of introducing such measures. Reasons included:

1. disclosure of beneficial ownership would add no information of benefit...Those engaged in criminal activities would not provide true information about the beneficial owners;

2. disclosure would result in misleading information being included on the register. Because beneficial ownership is, as a matter of law, impossible to define precisely, any information requirement designed to require by law disclosure would have to be complex and detailed. Many ordinary, innocent shareholders would be unable to understand it or comply with it;[3]

3. according to FATF, the United Kingdom authorities concluded that their current entity formation regime, which does not require beneficial ownership disclosure, provided investigators with as much as any disclosure regime could, and that attempting to add a beneficial

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[1] See Financial Action Task Force, *Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism The United Kingdom of Great Britain and Northern Ireland*, Section 1132 at page 234 (June 29, 2007), available at http://www.fatf-gafi.org/dataoecd/55/29/39064399.pdf.
[2] *Id.*
[3] *Id.*

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ownership disclosure requirement "would be harmful to investigations through the resulting misleading information provided by both criminal and innocent shareholders."[4]

FEDERALIZATION OF STATE INCORPORATION LAWS

Lastly, corporate law, within the United States, has been the domain of the states for over 150 years. This system has allowed for differing corporate and management structures that have created the foundation of the free enterprise system. S.569 would effectively place federal mandates on corporate law and create a one size fits all approach. This federalization could hamper capital formation and discourage entrepreneurialism in the current economic downturn and beyond.

CLOSING

I appreciate the opportunity to speak to you regarding this important issue. Again, while we share the goals of protecting this country, we do have disagreement with the methods being employed. I seek to make sure that this legislation actually accomplishes its goal, without hurting legitimate businesses in the process. Thank you and I look forward to your questions.

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[4] *Id.* Section 1133 at page 234

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AMERICAN BAR ASSOCIATION
GOVERNMENTAL AFFAIRS OFFICE • 740 FIFTEENTH STREET, NW • WASHINGTON, DC 20005-1022 • (202) 662-1760

STATEMENT OF KEVIN L. SHEPHERD

Member, Task Force on Gatekeeper Regulation and the Profession

On behalf of the
AMERICAN BAR ASSOCIATION

Before the

Senate Committee on Homeland Security

and Governmental Affairs

CONCERNING S. 569, "INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT"

November 5, 2009

Mr. Chairman and Members of the Committee:

My name is Kevin L. Shepherd, and I am a member of the American Bar Association's ("ABA") Task Force on Gatekeeper Regulation and the Profession and a former chair of the ABA Section of Real Property, Trust and Estate Law. I am the co-chair of the Real Estate Practice Group at Venable LLP and President of the American College of Real Estate Lawyers. I appreciate the opportunity to present the ABA's views on S. 569, the "Incorporation Transparency and Law Enforcement Assistance Act." I am appearing on behalf of the ABA, and my testimony here today is limited to that legislation.

The ABA supports all reasonable and necessary domestic and international efforts to combat money laundering, tax evasion, and terrorist financing activity. Indeed, the ABA has collaboratively worked with the Financial Action Task Force ("FATF") and the U.S. Department of Treasury in developing risk-based guidance for legal professionals and is presently working to implement this guidance by developing good practices guidance for U.S. lawyers. These efforts underscore the ABA's unwavering commitment to work with the national and international communities in combating money laundering, tax evasion, and terrorist financing activity. The ABA, however, opposes the proposed regulatory approach set forth in S. 569 and any other legislation that would unnecessarily regulate state incorporation practices and impose government-mandated suspicious activity reporting ("SAR") on the legal profession. The ABA's opposition is grounded in three fundamental aspects of the proposed legislation.

First, S. 569 would essentially federalize state incorporation practices, meaning that states would be required to obtain, keep current, and make available to law

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enforcement authorities "beneficial ownership" information on corporations and limited liability companies. In our view, the imposition of a federal regulatory regime focused on beneficial ownership information is not workable, would be extremely costly, would impose onerous burdens on state authorities and legitimate businesses, would run counter to formation practices of major countries (including Canada, Mexico, Japan, and China), and will not achieve the laudable goal of assisting federal law enforcement authorities with pursuing and prosecuting criminal activity. For instance, obligating state agencies to collect beneficial ownership information would involve significant and expensive hardware and software changes, including the creation of a parallel record keeping system consisting of public and non-public information. These impediments, coupled with an unwieldy definition of beneficial ownership and the bill's focus on only a limited number of entities, would sow confusion into the formation process that would not enhance law enforcement's goals.

Second, S. 569 would create a new class of "financial institutions," known as formation agents, that would be subject to enhanced anti-money laundering ("AML") requirements. Because lawyers assist clients in forming corporations and limited liability companies, the designation of formation agents as financial institutions subject to additional AML requirements threatens to sweep in U.S. lawyers and treat them as the functional equivalents of banks.

Third, S. 569 could potentially impose SAR requirements on the legal profession, meaning that lawyers would have to report to governmental authorities a suspicion that their clients are engaging in money laundering or terrorist financing activity. These requirements are in direct conflict with ethical obligations of confidentiality, the attorney-

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client privilege, and fundamental aspects of the attorney-client relationship. They could also undermine the rule of law by dissuading clients from seeking legal counsel from lawyers on proposed conduct.

The ABA believes that a more effective and workable solution would involve collective and collaborative action of state government representatives, working with U.S. Department of Treasury and U.S. Department of Justice, as described below. While the ABA has not taken a position on any such proposal since we favor a state-based approach, we suggest that Congress give this solution an opportunity to be implemented and assessed for its effectiveness before imposing unprecedented federal regulation of state incorporation practices. The ABA believes that the effort to designate formation agents as "financial institutions" is premature and does not take adequate account of the implications for the legal profession. In light of other initiatives that the legal profession is undertaking on a voluntary basis, such as the development of the good practices guidance noted above, the ABA believes the imposition of AML requirements on the legal profession is unnecessary.

Beneficial Ownership Information

The Permanent Subcommittee on Investigations ("PSI"), through a series of hearings and investigations into tax abuse havens, and FATF's Mutual Evaluation of the United States ("Mutual Evaluation"), separately have expressed strong concerns that the U.S. company formation process is at risk for exploitation by money launderers, tax evaders, and terrorist financiers. Without trying to examine the strength and depth of that concern, the ABA (and others) recognize that improvements are needed in the company

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formation process with a view to having more visibility on those involved in forming non-public entities in the 50 states and the District of Columbia.

The ABA, however, believes that federal legislation is premature and is neither necessary nor the most effective means for addressing the concerns prompting S. 569. The National Conference of Commissioners on Uniform State Laws ("NCCUSL") adopted in July 2009 the "Uniform Law Enforcement Access to Entity Information Act." This suggested legislation was developed through the collective efforts of NCCUSL, members of the ABA, and others and is intended both to balance the interests of the various stakeholders and to address effectively the risks identified by the PSI and FATF without imposing undue burdens on state authorities and legitimate businesses. Congress should give these and other efforts a fair chance to work, especially at this time when the U.S. financial system and the domestic economy are under severe stress and the economic recovery remains fragile.

The PSI has expressed concerns that the U.S. is not in compliance with FATF Recommendation 33, which has prompted, in part, the introduction of S. 569. FATF Recommendation 33 states in pertinent part that countries should "ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities." According to law enforcement authorities, the U.S.'s non-compliance with Recommendation 33 hampers their ability in many instances to locate the "beneficial owners" of privately held corporations and limited liability companies. As a result, these authorities contend that money laundering, tax evasion, and terrorist financing

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investigations can be difficult to resolve and the U.S. financial sector is at heightened risk for abuse.

The ABA believes that effective state laws can obviate the need for federal regulation of business entities while meeting the requirements of FATF Recommendation 33. It also appears to me that the approach taken by the Uniform Commissioners is consistent with the mechanisms for compliance identified in the FATF Report: Methodology for Assessing Compliance with the FATF 40 Recommendations and the FATF 9 Special Recommendations (February 2008). *See* FATF, *Methodology for Assessing Compliance with the FATF 40 Recommendations and the FATF 9 Special Recommendations* (February 2008), *available at* http://www.oecd.org/dataoecd/16/54/40339628.pdf.

It is noteworthy that the United Kingdom studied the merit of a system that would require the up-front disclosure of beneficial ownership. According to the 2007 Mutual Evaluation Report prepared by FATF for the United Kingdom, the UK authorities concluded that there were significant disadvantages and no clear benefits to adopting such a system, particularly when taking into account the costs of introducing such measures. These authorities concluded that the disclosure of beneficial ownership information would add no information of benefit to the register of members and that those engaged in criminal activities would not provide true information about the beneficial owners. Another reason was that disclosure would result in misleading information being included in the register. According to the UK Mutual Evaluation report, "beneficial ownership is, as a matter of law, impossible to define precisely [and]

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any information requirement designed to require by law disclosure would have to be complex and detailed. Many ordinary, innocent shareholders would be unable to understand or comply with it." *See* FATF, *Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, The United Kingdom of Great Britain and Northern Ireland* (June 29, 2007), at ¶1132 (p. 234), *available at* http://www.fatf-gafi.org/dataoecd/55/29/39064399.pdf.

The ABA, during its August 2008 annual meeting, adopted Resolution 300 supporting the efforts of the states to assume responsibility for a more effective incorporation regime that is supportive of U.S. law enforcement needs, and noted that absent effective state law action, the case for federal legislation would be more compelling. NCCUSL, with participation from the ABA Business Law Section's Committee on Corporate Laws, the National Association of Secretaries of State, the National Conference of State Legislatures, the International Association of Commercial Administrators, the Association of Registered Agents, and the National Public Records Research Association have developed a model state law. The model law would require, among other things, an incorporator to identify an individual within the U.S. who could provide law enforcement with the necessary information identifying the record owners and key officers of non-publicly traded entities formed under state law. The model law would enhance record-keeping requirements for covered businesses by requiring those businesses to maintain current and accurate records on record owners and managers, and on the individuals responsible for maintaining those records, and by assuring that this information is accessible by law enforcement officials. It would include penalties for

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failing to abide by the requirements for identifying a responsible records contact, as well as failure to comply with a request for information.

For these reasons, S. 569 is ill-designed to achieve law enforcement's goals and runs the very real risk of imposing unreasonable burdens on state authorities and legitimate businesses. The ABA will continue its efforts to work closely with the various stakeholders in developing an effective, workable, and balanced state-based solution meeting the requirements of FATF Recommendation 33.

Lawyers as Financial Institutions

Section 4 of S. 569 would establish a new class of "financial institutions" under U.S. AML laws that would cover "any person who, for compensation, acts on behalf of another person to assist in the formation of a corporation or limited liability company" (i.e., formation agents). These formation agents would then be required to adopt certain AML compliance mechanisms, much like U.S. banks have done, to detect possible money laundering and terrorist financing activities in the formation of corporations and limited liability companies. These requirements would include the following four elements: the development of internal policies, procedures, and controls; the designation of a compliance officer; an ongoing employee training program; and an independent audit function to test programs.

Although not explicit on its face, the definition of "formation agents" in S. 569 would appear to include lawyers (and many others) involved in the formation of corporations and limited liability companies. This legislation would thus impose federal regulation on the legal profession for AML purposes, and treat lawyers as if they were banks. The ABA believes such treatment is inappropriate, nor does it make sense given

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the obvious distinctions between large financial institutions, the resources they have at their disposal, and the function they play in handling money transactions, as compared to sole practitioners and small and medium firms – which make up the vast majority of the U.S. legal profession.

Suspicious Activity Reporting

Designating new formation agents in this manner runs the substantial risk of imposing SAR obligations on lawyers. Pursuant to S. 569, the Treasury Department would have the ability to impose SAR obligations on lawyers. The ABA has strongly objected to making lawyers subject to the SAR obligation. Starting in 2003 with the passage of ABA Resolution 104 and reiterated in 2008 with the passage of ABA Resolution 300, the ABA has consistently expressed its concerns with, and objections to, imposing government-mandated reporting obligations on lawyers vis-à-vis their clients based on "suspicion"; imposing an obligation on lawyers to not inform clients of any such report if provided to the government (the so-called "no tipping off" rule); and imposing criminal penalties on lawyers if a SAR is not filed.

The ABA has registered these objections with representatives of the Department of Justice, the Department of Treasury, and the FATF, and the concerns underlying the ABA position are shared by legal professionals in many jurisdictions around the world, and led to litigation in Canada successfully challenging the imposition of such requirements on Canadian lawyers. Tellingly, FATF's recently adopted risk based guidance for legal professionals specifically does not impose the SAR (referred to within FATF as "suspicious transaction reporting") obligation on lawyers.

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The attached Resolutions and accompanying reports detail these objections, but they center on the most fundamental core principles of the legal profession. Government-mandated SAR requirements would, among other untoward consequences, erode the attorney-client privilege that is a bedrock of the U.S. judicial system and effective counseling of clients on legal compliance. The SAR requirement would conflict with ethical obligations of lawyers under various state law rules to maintain client confidentiality. It would also create inherent conflicts between lawyers and their clients as lawyers would be acting as informants vis-à-vis their clients, be precluded from informing the client of the filing of a SAR, and elevate the lawyer's own interests over the client to avoid criminal liability for failure to report. A SAR requirement would also alter the attorney-client relationship, as lawyers would no longer be acting independent of the state and in the best interests of their clients.

There are also practical concerns with any SAR requirement, including the fact that no basis exists to believe that imposing this type of requirement will materially add to the quality of information the federal government already receives from tens of thousands of such reports received annually from financial institutions. As regulators in the United Kingdom have discovered, the legal profession routinely files SARs defensively in an abundance of caution so as not to run afoul of the reporting requirements. This type of defensive filing activity does nothing to enhance the fight against money laundering and terrorist financing.

ABA's Engagement with the FATF

The ABA has been working collaboratively with legal professionals throughout the world, FATF, and the Treasury Department to develop risk-based guidance on client

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due diligence ("CDD") for legal professionals, so as to enhance the ability of legal professionals to identify and avoid illicit money laundering and terrorist financing activities. FATF has been actively collaborating with specially designated non-financial businesses and professions, including lawyers, to produce voluntary, risk-based guidance for the legal profession to ensure that adequate CDD is performed at the outset and during the course of a client representation, so as to further minimize the risk that lawyers would be used by unscrupulous clients to launder illegally-obtained money. The ABA and members of other U.S. specialty bar associations, along with counterparts in the United Kingdom and elsewhere, participated extensively in this effort, attended numerous meetings with FATF officials, and assisted in the preparation of the guidance. The proposal for legal professionals was released by the FATF on October 28, 2008. This was a major achievement for the FATF and resulted directly from the active and extensive participation of the U.S. legal profession in this effort.

Education of U.S. lawyers regarding anti-money laundering and counter-terrorist financing compliance is an important cornerstone of an effective AML compliance program. The ABA, as well as members of specialty bar associations, continues to be active in this educational area. Through the efforts of members of the ABA Gatekeeper Task Force, as well as others in the ABA, the American College of Real Estate Lawyers, the American College of Mortgage Attorneys, and the American College of Trust & Estate Counsel, and other professional organizations in the United States, additional voluntary CDD guidance is being prepared in collaboration with members of the Treasury Department. On a personal note, I have written extensively on this topic in an effort to educate the U.S. legal profession on this topic.

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Combating money laundering, tax evasion, and terrorist financing activity while minimizing the impact on our economy and state regulators are critical objectives. The ABA, together with other private and government sector groups, has expended a considerable amount of resources – and has made great headway – in developing an effective solution to the identified problem. We continue to support collaborative state efforts and oppose premature federal legislation. We look forward to working with you on developing a comprehensive solution that addresses the mutual objectives of all concerned.

Thank you for the opportunity to appear before you today to present the views of the ABA on S. 569.

I would be happy to answer any questions you may have.

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FEDERAL LAW ENFORCEMENT OFFICERS ASSOCIATION
P.O. Box 326, Lewisberry, PA 17339
www.fleoa.org

STATEMENT

OF

JOHN R. RAMSEY

NATIONAL VICE PRESIDENT

FEDERAL LAW ENFORCEMENT OFFICERS ASSOCIATION

REGARDING A HEARING ON

"BUSINESS FORMATION AND FINANCIAL CRIME: FINDING A LEGISLATIVE SOLUTION"

IN REFERENCE TO THE INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT (S. 569)

BEFORE THE

UNITED STATES SENATE

COMMITTEE ON HOMELAND SECURITY AND

GOVERNMENTAL AFFAIRS

Thursday, November 5, 2009 @ 10:00 am

INTRODUCTION

Chairman Lieberman, and distinguished Members of the Committee:

I would like to thank you for the opportunity to testify today. I appear before you today in my official capacity as the National Vice President of the Federal Law Enforcement Officers Association (FLEOA). On behalf of the 26,000 members of the FLEOA, I am memorializing our support for Senate Bill 569. The proposed legislation is very important to our FBI, ICE and IRS members as they are the lead agencies that investigate money laundering and terrorist financing cases, as well as other Federal law enforcement agencies. Incorporation transparency is an invaluable tool to (i) combat national and international crime and terrorism, (ii) hinder the financing thereof, and (iii) frustrate the ability of perpetrators to hide and benefit from the proceeds of their crimes.

While criminals cower behind the anonymity of their corporate filings, they continue to exploit this system as a means to commit terrorist financing and money laundering. Using a registered agent or attorney as the "front-person" for their company, terrorists/criminals are able to circumvent law enforcement and accomplish the following:

1. Use shell company bank accounts to launder millions of dollars;
2. Use shell companies to attempt to acquire a significant ownership interest in a financial institution;
3. Purchase real property through their shell companies to be used as stash houses to stockpile drugs or weapons/explosives;
4. Operate money remitter businesses to move their illegal proceeds to off-shore accounts;
5. Engage in cyber-terrorism attacks by disseminating contaminated emails from ostensibly legitimate companies.

By attacking and addressing the above-mentioned five points would allow for greater protection of our vulnerabilities with regards to our homeland security front. Alleged "inconveniences" for the business owners and perceived costs of implementation should not be placed on a higher pedestal and have a greater value than the protection of our Homeland.

We are aware of some of the concerns that have been voiced by industry and at the state level with respect to this Bill. To address some of these misconceptions, specifically, this Bill does not require any state to enact any law with respect to corporations; it merely requires the states to add one more question to their existing incorporation forms and to make the information provided available to law enforcement upon presentation of a legally authorized subpoena or summons. This information is beneficial to law enforcement and homeland security to prevent the misuse of U.S. corporations by criminals and other wrongdoers within or outside of the United States. With regards to costs, beneficial ownership information can be collected via existing electronic incorporation methods and stored in existing electronic databases. Alternatively, such information can be obtained by adding the relevant question and space for a response on existing paper incorporation forms. The lack of truthful disclosure is not necessarily an obstacle, but merely identifies a direction in which to proceed in order to identify the criminal enterprise, and ultimately, showing criminal intent.

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Law enforcement's ability to investigate and enforce the provisions of the Bank Secrecy Act has been impeded by terrorists/criminals who hide behind the corporate veil. This costs law enforcement agencies a substantial amount of time and money, i.e., long-term surveillance and subpoena service on numerous third parties, and allows the terrorist and/or criminal to remain "ten-steps" ahead. FLEOA maintains that the identity of the real beneficial owners should be made available to law enforcement officers who make legally authorized requests pursuant to official investigations.

At this time, I would like to share with you just a few examples of past investigations that demonstrate how "shell" corporations have been utilized to commit crimes against individuals in the United States and impacted our homeland security.

Owner of La Bamba Check Cashing and Corporation Sentenced in Connection with $132,000,000 in False Currency Transaction Reports

On June 23, 2009, in Miami, Fla., Juan Rene Caro and the company he owned and operated, Maytemar Corporation, dba "La Bamba Check Cashing," were sentenced on one count of conspiracy and 15 substantive counts of failing to file currency transaction reports (CTRs). Caro was sentenced to 216 months in prison and ordered to pay a $250,000 fine. The Court also ordered the forfeiture of more than $11 million in cash and properties. The Maytemar Corporation was also sentenced to probation, the only possible sentence for a corporation. According to the evidence presented at trial, the defendants executed a scheme to assist individuals and entities in South Florida to cash checks in anonymity, in exchange for a commission based on the face value of the check. Defendants Oscar Alberto Valle and Meylin Maria Morales, working with Caro, identified and recruited customers, mostly local construction companies and subcontractors, who were interested in cashing checks at La Bamba through shell companies that the defendants owned or controlled. In this way, the construction companies participating in the scheme would cash checks payable to the shell companies, and get cash back from La Bamba. Thereafter, the defendants would file CTRs with the Treasury Department falsely stating that the shell company and/or nominee owner had conducted the transaction, concealing the true parties involved in the transaction and the source of the funds. For this service, La Bamba, Caro, and others earned substantial fees. Throughout the course of the conspiracy, the defendants in this case filed CTRs with the Treasury Department reflecting transactions in the name of shell companies; these transactions totaled more than $132,000,000.

Louisiana Women Sentenced to 20 Years; Two Corporations Sentenced

On April 15, 2009, in New Orleans, La., Gwendolyn Joseph Moyo was sentenced to 240 months in prison, to be followed by three years of supervised release, and ordered to pay $2,463,807 in restitution. In addition, AA Communication, Inc. and Capital Management Asset Group (CMAG) were each sentenced to one year probation. Moyo was convicted in October 2008 on federal charges of conspiracy to commit mail fraud and wire fraud; mail fraud and aiding and abetting; wire fraud and aiding and abetting; engaging in the business of insurance after having been convicted of a crime involving dishonesty and a breach of trust; conspiracy to commit

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money laundering; and money laundering and aiding and abetting. AA Communication was convicted of conspiracy to commit mail and wire fraud, mail fraud, wire fraud, conspiracy to commit money laundering, and money laundering. CMAG was also convicted of conspiracy to commit mail and wire fraud, mail fraud, wire fraud, and conspiracy to commit money laundering. The jury further ordered Moyo, AA Communications, and CMAG to forfeit $1,495,521 as to the mail and wire fraud charges and ordered Moyo and AA Communications to forfeit $1,548,246 as to the money laundering charges. According to court documents, Moyo was twice convicted in 1989 and 1991 in the District of Arizona for conspiracy to defraud the United States; making false statements; mail fraud; wire fraud; and fraudulent use of a Social Security number; all felony crimes involving dishonesty and breach of trust. Despite being prohibited from participating in the insurance business because of her prior convictions, Moyo, through her companies, AA Communications and CMAG, marketed construction bonds to contractors and other entities which had difficulty placing coverage in the standard market. Moyo's clients paid her for worthless performance, payment, or bid bonds and then completed the jobs without realizing they had not been covered. Moyo's co-defendant, James Zoucha, acted as the President of AA Communications, serving essentially as a "straw man" or nominee for Moyo, generally facilitating the business while keeping Moyo's name off the legal documentation.

Labor Broker Gets Nearly 16-Year Prison Sentence

In March 2004, the owner of American Immigration Agency was sentence to nearly 16 years in prison after being found guilty in June 2003 of immigration and bank fraud. A joint investigation found that he filed dozens of applications for labor certifications that contained false information. In those applications, he declared that he owned numerous businesses that were in fact shell corporations created solely for obtaining green cards under false pretenses.

CONCLUSION

While our membership respects the spirit of free enterprise in our country, we do not want to see the United States adopt the financial safe-haven image of other countries around the world. If our country's laws require individuals to register vehicle or firearm ownership, the same should apply to corporate filers. The consequences for allowing terrorists and/or criminals to exploit our corporate filing system are severe. In the spirit of homeland security and protecting our great nation, we cannot permit this to continue. The content of this Bill does not disvalue the American dream, but addresses the American deception. We should not permit corporate secrecy to be used as a shield to hide corporate misconduct. We hope your committee will embrace the importance of Senate Bill 569, and work together to move it forward for consideration before the full Senate.

I would like to thank the Committee Members, again, for this opportunity to testify and for your continued support of law enforcement and its mission. I will be happy to answer any questions that you may have at this time.

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Testimony of Jack A. Blum, Esq.
before
The United States Senate Committee on Homeland Security and Governmental Affairs
on
S.569, the Incorporation Transparency and Law Enforcement Assistance Act
November 5, 2009

My name is Jack Blum. I am a Washington attorney specializing in money laundering compliance and issues of offshore tax evasion. I am appearing on behalf the Tax Justice Network-USA and Global Financial Integrity. Both organizations endorse the bill sponsored by Senator Levin, S. 569, the Incorporation Transparency and Law Enforcement Assistance Act.

The single most important tool in the toolkit of people trying to hide money from law enforcement and tax collection is the anonymous shell corporation. These shell corporations have no physical place of business, use nominee officers and directors, and as a rule do no business in the place of incorporation. Their sole purpose is hiding where money is, who controls it, and where it is moving, from law enforcement and tax collectors. These shell companies should not be allowed remain anonymous.

States that offer corporations to individuals without insisting on information on beneficial ownership are undermining the efforts of law enforcement to prevent crime, recover stolen assets and collect tax. They are also putting the United States out of compliance with international standards for customer identification. From our perspective gathering basic information about ownership for government use is essential to protect national security and to limit financial crime and tax evasion.

Anti-money laundering compliance is dependent on 'know your customer.' Without that knowledge financial institutions cannot evaluate the legitimacy of a transaction. Knowing that one shell corporation is owned by another shell corporation is not helpful. Having the details of the "owner's" directors who are usually professional directors who work for a corporate service company in another jurisdiction is useless. Financial institutions need to know who is behind a company to judge whether the transactions they monitor are suspicious. They need to know whether the beneficial owner is on the OFAC list, the other sanctions lists is a politically exposed person.

The proposed legislation would end the all too frequent use of loopholes in State incorporation laws to hide money.

In supporting this legislation and asking for an end to corporate anonymity let me explain my concerns and alternatively what is not at issue.

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I am not talking about making beneficial ownership information part of a public record. I am talking about having it available to law enforcement and tax authorities upon appropriate request. Personal privacy is not at issue.

I am not talking about all corporations. I am focused on corporations that have a small number of owners -- under ten -- and especially those that have a single owner. In those small corporations all I am concerned about is the identity of owners with more than a ten percent interest. Public corporations are not the problem.

Opponents of this bill have complained about the burdens it will impose on small business. As someone who has advised clients setting up a small business, I can say from broad practical experience that gathering ownership information at the time of incorporation and reporting ownership changes on an annual return is the least of a small business's problems. The numerous other agencies demanding information for licenses and permits, and the regular filings regarding employees, employee benefits and unemployment insurance dwarf corporation ownership issues.

Incorporation agents should bear the same responsibility as financial institutions under the anti-money laundering laws. We now require jewelers, auto dealers, money transmitters and other businesses that can be used to launder money to have an anti-money laundering program and to report suspicious activity. The required program is risk based. Each firm must do a risk assessment and develop a program in line with that assessment. It makes sense to impose a similar regime on incorporation agents.

The burden of setting up an AML compliance program would fall most heavily on corporate formation agents who offer their services to all comers through the internet. They have no other business relationship with the corporate principals. They deal with strangers on the web. Thus, if a request for a corporation came to a web based agent from a country such as Moldova, the risk would be high. The level of due diligence required of the agent would be high. The AML program would have to be robust. The agent would have the responsibility of establishing the identity of the customer and should have some knowledge about the legitimacy of the corporate purpose. The agent would have the responsibility or running the customer's name against the various sanctions lists and checking his political exposure.

In contrast a local lawyer who does few incorporations, and does them for regular business clients would not be seriously burdened. That lawyer runs little or no risk of helping a criminal.

Opponents of the legislation have argued that keeping corporate data updated will impose an unfunded mandate on the states. I disagree. The incorporation business is a profit center for the states and a profit center for the incorporation agents. If the states and the incorporation agents want to maintain existing profit levels, a very small fee increase would more than cover the cost of adding a few lines of information to the corporate data base. In many cases there is existing data on directors and officers but the states in question allow nominee names. The nominee names could be replaced with real ones at no cost.

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A further argument is made that people will still be able to conceal the identity of the beneficial owner by lying on the forms. Of course they are correct. Lying on the forms is a possibility. But the lies will entail risks. If it is later determined that someone lied on the form to conceal ownership, the fact of the lie will become evidence of criminal intent in a financial fraud or tax evasion scheme. The lie itself could become a prosecutable offense.

I have been asked to explain how the availability of shell corporations has undermined law enforcement and tax collection.

The most dangerous of the groups using United States incorporation services are foreigners who want anonymous shells to facilitate financial crime, money laundering and tax evasion. They like the prestige of an American incorporation. Fraudsters use the fact a that a company is incorporated here to impress their victims.

The United States has been inundated with requests from foreign law enforcement authorities seeking information about corporate ownership and activities in connection with cases of fraud and money laundering. Many of the requests wind up on the miscellaneous docket of the Delaware District Court where they languish because US law enforcement cannot identify the people behind the corporation or obtain records relating to its activities. US legal attachés in our embassies around the world are routinely asked for help in investigations involving US companies. I have attached a partial list of such requests to my testimony and ask that it be made part of the record.

Several years ago I spoke at an anti-money laundering forum in Panama City. I berated the Panamanians for their anonymous shell corporations. Eduardo Morgan, a partner in the Law Firm of Morgan & Morgan, and former Panamanian ambassador to the United States, told the audience that he knew that the best corporation to use for hiding assets was a Delaware corporation. He argued that people around the world assumed that a Delaware corporation carried legitimacy and that its activities were policed by the state and federal government.

He then went on to say that the corporation would not have to file a Federal or state tax return if it did no business in Delaware. Even if a return were required there would be no way for IRS to enforce the requirement. "Pass through" entities need not file returns and need not have taxpayer identification numbers. IRS cannot match incorporation lists at the state level with returns filed. I had assumed that all corporations were required to filed Federal income tax returns. I was wrong.

If I were a terrorist seeking to make funds available for use in the United States I would use a foreign shell corporation set up a corporation in any one of a number of states that offer anonymity. I would then open an account with a U.S. brokerage firm. I would file an IRS form W-8 with the broker indicating that the beneficial owner of the account was the foreign corporation, and then in response to further information requests from the broker produce the passport photos and other documentation regarding the identity of the nominee officers and directors of the offshore shell.

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The final step would be to obtain a debit card attached to the brokerage account. The holder of the card could then use funds wired in from almost anywhere in the world. If the right bank and the right jurisdictions are selected there will be no information on the wire explaining who sent the money.

Tax evaders use these corporations as well. I have seen cases in which a US person used a US shell set up by a foreign shell to conceal the movement of money from the US to a hedge fund operated from the US but incorporated abroad. In the first instance the money went from the taxpayer's US account to the account of US shell and from there to the hedge fund. The US shell had no taxpayer ID number and there was no ownership information available for it.

Similar problems arise when states attempt to track down corporations doing business in their jurisdiction to collect taxes due. California, for example, has had a difficult time collecting tax from corporations doing business in California but incorporated in Nevada and not registered in California. Without information identifying a real person and beneficial ownership the hunt for the tax cheat is almost hopeless.

Although Nevada now requires some information on its incorporation reports it still permits nominee officers and directors and its incorporation agents still advertise anonymity on the web.

Wyoming, another state which was in the anonymous incorporation business has just improved its laws by eliminating bearer share corporations and by requiring the corporation to have a registered agent who is presumed to know how to contact the beneficial owner of the corporation.

The problem with the Wyoming solution and with the proposal advanced by the State Secretaries of State is the issue of "tipping off." If law enforcement has to contact the corporation's registered agent in order to then find the beneficial owner of the corporation, the target will have time to move the money out of reach. Money moves with the speed of light -- law enforcement requests do not. A key objective in fraud and tax evasion cases is seizing the proceeds of crime. Giving the criminal time to move the money makes no sense.

The way Wyoming got into the shell company business is instructive. Jerome Schneider, a purveyor of tax evasion schemes lobbied hard and talked the legislature into passing the secrecy laws. Schneider was later convicted for his many efforts to help US persons evade tax by moving assets offshore.

My experience with following the money trail is that time is of the essence and that each piece of information leads to requests for further information. If gathering ownership information takes weeks because of delays in locating the responsible party and then turning it over to a government agency that will then forward it to law enforcement ,important, time sensitive, investigations may be derailed. I can imagine a terrorism investigation which turns on learning the source of funding for a terror suspect being delayed long enough for the terrorist to have the chance to carry out his mission.

Some members of the bar are concerned that imposing AML responsibility of lawyers who act as incorporation agents will violate lawyer client privilege. I believe that there is a bright line between giving a client legal advice, which is protected by privilege, and performing transactional work that requires interaction with government agencies. If a lawyer explains to a client that he must gather certain information and turn it over to the government as a condition of incorporation the client

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should have no expectation of confidentiality.

If a lawyer handles an incorporation in a situation where that lawyer knows the corporation will be used as part of a money laundering scheme then the lawyer ceases being a lawyer and becomes a co-conspirator. Under those circumstances neither the lawyer nor the client deserves protection.

This committee should be aware that the United States now lags behind much of the rest of the world in obtaining beneficial ownership information. I was recently on the Island of Jersey where I met with trust company officials who showed me the questionnaire they require of anyone wanting to set up a Jersey structure. The principals must show proof of identity and indicate the source of their wealth. To nail down the identity of the person providing the funds, a copy of the passport or other government identification is required and its authenticity must be certified. For proof of address the principals are asked to produce utility bill and other evidence that the residence address they list is truly theirs. Information on the grantors who set up foundations is kept by the local agent. Every agent is required to provide the government with the basic information. I have attached a sample of a Jersey formation agent's questionnaire to my testimony.

We should be able to meet the standard they have set.

Finally, I would argue that anonymous shell corporations are not in any way related to the legitimate historical purpose of the corporation -- encouraging people to take entrepreneurial risks without risking everything they have.

Historically, corporations were considered to be a privilege granted by the state. Sates controlled the limits of corporate operations and limited their activities by insisting on narrow language in their charters. Early corporations could not operate outside the boundaries of the state of incorporation. Early corporations had a limited life span. Today corporations also serve the purpose of allowing the business entity to outlive the participants and to survive the departure of one or more of the officers directors and employees.

Corporations were also required to have a stated paid in capital so that creditors would be able to understand the risks they were taking in doing business with the corporation. The modern corporation is an essential part of the economy and the ability to form and operate a corporation across state lines has enabled out economy to develop. Because of its importance the corporation has been given substantial rights under US law including constitutional status for certain purposes.

Secrecy has no place in this picture. There is no business purpose served by allowing people who are not actually running a business to hide their activities behind a corporate form. The corporations we are talking about here are secrecy shells and nothing more. To the extent that they have other legitimate purposes nothing in the proposed legislation will cause them problems.

It is obvious to me that we need to attach the name of a real person who is responsible for the corporation to the act of forming the company and to insist that the identity of the real person is updated on the annual corporate filing.

I urge the committee to report out S.569 so that it can be enacted into law. It is a national embarrassment for us to tell the rest of the world what it must do to control money laundering and financial crime at the same time we continue to provide money launderers and criminals with anonymous shell companies -- companies that we have told others facilitate crime.

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AIB Jersey

Application Form

AIBJerseytrust Limited

Company Administration / Company Formation

AIB Jersey is the registered business name of AIB Bank (CI) Limited and AIBJerseytrust Limited which are both regulated by the Jersey Financial Services Commission. AIBJerseytrust Limited is a wholly owned subsidiary of AIB Bank (CI) Limited, which is a wholly owned subsidiary of Allied Irish Banks, p.l.c. The registered office of the above Jersey companies is AIB House, 25 Esplanade, St Helier, Jersey, JE1 2AB

February 2008

AIB Jersey

This application form will be used by AIBJerseytrust Limited ("AIBJT") to consider new business applications. The form should be completed in conjunction with professional advice. If there is insufficient space, please attach an additional sheet(s) to the form and cross reference, accordingly.

Please note AIBJT will normally provide a Board of Directors resident in Jersey.

I / We request AIBJT to act on my / our behalf in the establishment of a Company and / or provision of administration services details of which are:

Please indicate status of required company:

Creation of New Company	☐	Transfer In	☐
Please confirm direct ownership of Company:		AIBJT administered	☐
		Non AIBJT administered	☐

Beneficial owner
Provider of the funds
See note 1

Legal name

Former name(s)
Aliases

Principal
residential
address

Postcode

Mailing address
(if different)

Postcode

Telephone

Fax

Email

Occupation

Source(s) of wealth

Date of birth

Place of birth

Gender

Marital status

Nationality

ID number

Country of residence
for tax purposes
(include arrival date)

AIB Jersey

Verification of identify
See note 2

In respect of the beneficial owner and any person providing funds to the Company please supply the following:

- copy of a passport or national identity card, certified by a professional person (e.g. lawyer, accountant, banker) (see note 2 for the format of the certification);
- one original utility bill (except mobile phones) with the home address;
- a reference from a professional (lawyer / accountant) confirming source of wealth; and
- a bank reference.

Referee's name

Referee's firm

Referee's address

Postcode

Company details

Suggested name for the proposed Company

Name

Alternative 1

Alternative 2

If none of the above names are available, should AIBJT choose an alternative? Yes ☐ No ☐

Proposed activities
See note 3

Provide details of the proposed activities of the Company:

Source of funds / assets to be introduced

Provide details of the source of funds to be used for the incorporation and subsequent funding of the Company:

Tax advice

In order for us to understand fully the rationale for incorporating the Company, and so that it can be correctly incorporated and managed, we require a copy of all relevant tax advice.

AIB Jersey

Rationale for using Jersey to administer the Company
See note 3

Country of incorporation

In which jurisdiction is the proposed Company to be incorporated?

Jersey ☐ British Virgin Islands ☐ Other (please specify below) ☐

AIBJT will arrange for the provision of a registered office in the required jurisdiction.

Please explain the benefit of the country of incorporation:

Tax status in country of incorporation
See note 3

Please indicate the preferred tax status:

Exempt Company ☐ Resident for Income Tax ☐ Other (please specify below) ☐

Tax residence

Will the proposed Company be tax resident anywhere other than the country of incorporation? Yes ☐ No ☐

If YES, please provide details:

Company requirements
See note 3

Please indicate which type is required:

Limited Company ☐ Unlimited Company ☐

Cell Company ☐ SPV ☐

Other (please provide details)

Par value shares ☐ No par value shares ☐

Nominal value (currency) of shares:

Authorised share capital:

Are there any additional / special requirements to be included?

Yes ☐ No ☐

If YES, please provide details:

AIB Jersey

Share capital
See note 4

Our standard service involves the incorporation of a limited liability Private Company with one class of ordinary voting shares, usually with capital representing the minimum governmental duties upon formation.
Standard incorporation:

Jersey - £10,000 share capital divided into 10,000 ordinary shares of £1.00 each;
BVI - US$ 50,000 share capital divided into 50,000 ordinary shares of US$1.00 each

Incorporate Company with standard share capital – Jersey / BVI only. Yes ☐ No ☐
(If NO, please detail below required share capital)

Amount of Share capital | Par value of each share

Type(s) of share(s) | Voting rights

Currency of issued shares if other than GBP US $ ☐ € ☐ Other ☐

Where other selected, please specify:

Is share capital to be issued at a premium? *(If YES please provide details)* Yes ☐ No ☐

Details of issued share capital:

AIBJT standard for a Jersey / BVI company – minimum of two registered shares of £1.00 / US$1.00 each. Please confirm agreement *(If NO, please provide details)* Yes ☐ No ☐

AIB Jersey

Shareholders
See note 5

Nominee shareholders:

Our standard service includes the provision of AIBJT nominee shareholders. Please confirm your agreement or advise of any alternative shareholders? *(If NO please provide details requested)* Yes ☐ No ☐

Legal name:

Former name(s)
Aliases

Principle
residential
address:

Postcode

Date of birth | Place of birth

Gender | Marital status

Nationality | ID number

Occupation | No of shares:

Initial share issue:

AIBJT standard practice is to issue initial shares to the nominee shareholder. If the beneficial shareholder(s) are being issued with initial shares, please indicate how many shares are to be issued to each beneficial owner:

Public Offering:

Is it intended that shares or securities will be offered to the public at any time?

No ☐ Yes ☐

Additional Owners:

Is it intended that any additional beneficial owners will be introduced within six months of incorporation? No ☐ Yes ☐

If YES, please provide equivalent information as detailed for the beneficial owner on page 2:

AIB Jersey

Administrative details

Financial statements

Jersey company law requires annual financial statements to be prepared. AIBJT will prepare these and the cost will be charged to the Company. (Auditors will not normally be appointed unless requested by the applicant or a specific legal requirement exists in the jurisdiction where the company is registered).
Financial statements will be provided to the beneficial owner.

Base reporting currency

Financial statements will be prepared in the same currency as the principal asset. If an alternative currency is preferred, please specify here.

Accounting year end

Please give preference appropriate for tax or other reporting requirements.

Declarations

Declarations of good standing

Please declare as follows:

1. None of the beneficial owner(s) have ever been declared bankrupt in any part of the world, or have ever been a Director or Officer, or otherwise concerned in the management of a Company which has been subject to an insolvent liquidation or been the subject of a judicial enquiry:

Confirmed ☐ Not confirmed ☐

2. None of the beneficial owner(s) have ever been engaged in or benefited from criminal conduct in any part of the world and assets which are subject to the proposed arrangements do not wholly or in part directly or indirectly represent the proceeds of criminal conduct:

Confirmed ☐ Not confirmed ☐

AIB Jersey

General declarations and understanding

I / We confirm that:

- The beneficial owner(s) is not acting as a nominee or representative of any third party;
- There are no judgements or pending litigation outstanding against the beneficial owner. Nor does the beneficial owner have any judgements or pending litigation against another party;
- Any funds intended to be transferred to AIBJT are completely legitimate and have not been obtained through illegal activities;
- I / We acknowledge AIBJT's advice to take independent professional legal and taxation advice and I / we have taken steps which I / we deem appropriate in my / our circumstances and in accordance with my / our absolute responsibility in this regard;
- I / We have taken all advice necessary in regard to completion of this application and absolve AIBJT from any responsibility arising from actions taken based on the foregoing application statements;
- I / We have read the standard AIBJT terms and conditions of service and agree to be bound by them;
- I / We have read the standard scale of fees and confirm my / our agreement to the establishment costs / transfer costs and annual fees as set out therein or as may be agreed by way of separate quotation. I / We accept that the standard fee scale may be varied from time to time but the agreed fee scale will remain in force until otherwise agreed;
- I / We accept that any statutory fees / duties payable in the jurisdiction concerned will be charged separately together with any third party charges;
- The information provided by me / us to AIBJT may be used for the provision of banking, asset management, accounting and administration services. It may be necessary to disclose such information to third parties both in Jersey and abroad in order to obtain access to these and other services;
- I / We acknowledge that acceptance of business is subject to approval of the New Business Committee of AIBJT and satisfactory receipt of the appropriate references and proof of identity and such other due diligence procedures as are deemed necessary in the circumstances; and
- All the information given herein is true to the best of my / our knowledge and belief.

AIB Jersey

Data protection notice

AIBJT shall use the information that you give together with any other information that AIBJT obtains for the purposes for administering your entities.

In administering your entities AIBJT may share information concerning you with other members of the AIB Group. To establish your identity and to open accounts / facilities with other Financial Institutions the Company may share information with or obtain information from other banks, investment managers, agents, credit reference agencies and persons authorised by you to provide references or certifying copy documentation. In addition AIBJT may disclose information about you to auditors, legal advisors and regulatory bodies.

AIBJT may from time to time like to advise you by post, telephone or electronically of additional, improved or new products or services from AIBJT or companies within the AIB Group which AIBJT considers may be of interest to you.

If you wish us to advise you of such products and services, please tick this box. ☐

Subject to the above and unless disclosure is required under compulsion of law AIBJT shall not disclose any information about you or your entities without your prior consent.

You have a right to see a copy of the records relating to you that AIBJT holds and you have the right to have any errors corrected. If you wish to see a copy of our records relating to you, you should apply in writing to: The Data Protection Officer, AIBJerseytrust Limited, AIB House, 25 Esplanade, St Helier, Jersey, JE1 2AB You should be aware that the Company may levy a fee up to a statutory maximum (currently £10.00) for access to your records.

Signature(s)

Signed

Date

Name in full

Capacity if not acting for self

Submitted by Sen. Levin

NYDailyNews.com
DAILY NEWS

A no-brainer bill to fight crime: Require corporations to disclose who runs them

By Robert Morgenthau
Sunday, June 28th 2009, 5:51 PM

The U.S. Senate Committee for Homeland Security and Governmental Affairs is considering a bill that would require the states, when they allow someone to create a corporate entity, to obtain information about the true ownership of the corporation.

The pending bill, the Incorporation Transparency and Law Enforcement Assistance Act, has bi-partisan support and is sponsored by Sens. Carl Levin (D-Mich.), Chuck Grassley (R-Iowa) and Claire McCaskill (D-MI). This bill is being reviewed by committee Chairman Joe Lieberman, who is a straight-shooting and no-nonsense senator with a track record of supporting law enforcement and national security.

The bill is as simple and straight-forward as it sounds. It would require a simple line on the registration form - "State the beneficial owner of the corporation" - and would require the person creating the corporation to provide some form of identification.

Believe it or not, only two states (Alabama and Alaska) currently require this basic piece of information before granting a corporate license.

Why do we need this bill? The answer is simple: It is a tool that will help us stop and deter criminals. Every kind of criminal organization uses shell companies, both foreign and domestic, to open bank accounts, launder money and hide the activities of its owners. Tax cheats, money launderers, securities fraudsters and even the financiers of terror need shell companies for their nefarious activities. For instance, we recently found $1 billion that had been transmitted by a foreign bank to an account in a small town U.S. bank opened in the name of a company of unknown ownership.

Requiring a simple statement of ownership will make it harder for criminals to form shell companies and will give law enforcement an important tool in proving crimes at trial.

It will also bring the United States up to international standards. It is difficult for us to lecture to the Cayman Islands, Switzerland and other "secrecy jurisdictions" when we have 48 states providing their own versions of secrecy corporations right here at home.

Virtually every law enforcement group that has considered this bill supports it.

http://www.nydailynews.com/opinions/2009/06/29/2009-06-29_a_nobrainer_bill_to_fight_crime.html

Submitted by Sen. Levin

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

The Honorable Christopher Dodd
Chairman
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, DC 20510

Dear Senator Dodd:

Thank you for your letter of September 22, 2009, inquiring about the Department of the Treasury's efforts to enhance our government's access to information regarding beneficial ownership of legal entities. Addressing the misuse of legal entities is key to our efforts to combat various forms of financial crime – including money laundering, terrorist financing, tax evasion, and sanctions evasion – as well as to protect the integrity of our financial system. As you indicate in your letter, enhancing access to beneficial ownership information is a global challenge. In our effort to develop a comprehensive approach to address this challenge, Treasury is collaborating with interagency partners in the law enforcement and regulatory communities, the Congress, state-based authorities, the private sector and our international counterparts. Our goal is to enhance the availability of beneficial ownership information of legal entities, while maintaining an open investment policy and refraining from actions that disadvantaging our nation's economic prosperity.

Our comprehensive approach for achieving this goal includes ongoing efforts to advance the following three fundamental objectives:

- **Make "beneficial ownership" information about legal entities created in the United States available to law enforcement** – Treasury is developing a proposal for federal legislation that: (i) encourages States to reform their entity creation laws to require the submission and availability of beneficial ownership information at the time of creation of the entity and throughout its existence; and (ii) introduces penalties to discourage the misuse of legal entities created in the United States. The legislative proposal will address these concerns and build upon the Uniform Law Enforcement Access to Entity Information Act approved by the National Conference of Commissioners for Uniform State Laws (NCCUSL). We will continue to work with the Congress, the law enforcement community, State-based authorities and the private sector in developing our legislative proposal, which we anticipate completing by year-end.

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- **Clarify and strengthen customer due diligence requirements for U.S. financial institutions with respect to the beneficial ownership of legal entity accountholders** – We are developing guidance for financial institutions to clarify when and how to identify and verify beneficial ownership as a necessary component of conducting customer due diligence of legal entity accountholders. We are currently working with the regulatory community to determine the form and content of that guidance. We will also continue to work with the regulatory and law enforcement communities and with industry in determining whether and, if so, how such due diligence requirements may need to be strengthened.

- **Clarify and facilitate global implementation of international standards regarding beneficial ownership** – As you note in your letter, in 2003 the Financial Action Task Force (FATF) reviewed and updated its 40 recommendations for jurisdictions to implement appropriate countermeasures against money laundering. Two of those recommendations – Recommendation 5 and Recommendation 33 – specifically address beneficial ownership and have created implementation challenges for the overwhelming majority of jurisdictions around the world. As we move forward in addressing these beneficial ownership challenges in the United States, we are also working with our counterparts in the FATF to ensure that these standards evolve in a way that is achievable in a practical sense, as well as effective, and that our efforts are consistent with the evolving views and ongoing efforts of the international community.

As always, we are grateful for your leadership on these issues and the continued support of the Congress as we move forward.

Sincerely,

Timothy F. Geithner

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Submitted by Sen. Ensign

OFFICE OF THE SECRETARY OF STATE

ROSS MILLER
Secretary of State

November 4, 2009

The Honorable John Ensign
United States Senator
119 Russell Senate Building
Washington, D.C. 20510

Dear Senator Ensign:

Enclosed, please find my comments regarding S. 569, the *Incorporation Transparency and Law Enforcement Assistance Act,* and include them as part of the record of the hearing on Business Formation and Financial Crime to be held Thursday, Nov. 5, by the U.S. Senate Committee on Homeland Security and Government Affairs.

I hope you share my concerns and those of my colleagues in other states that the legislation, as written, will place an unnecessary burden on Nevada, those states and millions of businesses across the country. This legislation is questionable policy in the best of times, but is particularly ill-advised considering the current business climate. While I agree that financial crimes must be aggressively investigated, I believe this bill takes the wrong approach and that the efforts the states and other organizations have made towards addressing the committee's concerns will be seriously considered in the ultimate resolution of this issue.

Thank you for the opportunity to share my concerns in the form of this written testimony.

Respectfully,

ROSS MILLER
Secretary of State

Encl.

ONE HUNDRED ONE NORTH CARSON STREET, SUITE THREE
CARSON CITY, NEVADA 89701-4786
(775) 684-5708 • FAX (775) 684-5717

Submitted by Sen. Ensign

Senate Homeland Security and Governmental Affairs Committee
Hearing on
"Business Formation and Financial Crime: Finding a Legislative Solution"
Thursday, November 5, 2009
Written Testimony Submitted by:
Nevada Secretary of State Ross Miller

Chairman Lieberman, Ranking Member Ensign, and Members of the Committee, thank you for this opportunity to state my reasons for opposing S. 569, the *Incorporation Transparency and Law Enforcement Assistance Act.*

I am opposed to the passage of S.569, as proposed, and instead advocate an approach similar to those currently under consideration by the National Association of Secretaries of State (NASS), the International Association of Commercial Administrators (IACA) and the Uniform Laws Commission (ULC) and others.

Most of the Secretaries of State in this country accept and process business formation documents and maintain those documents as part of the public record. Our offices are widely recognized as experts in this area, but mainly in the ministerial "filing" function, not one of strict regulation and enforcement. It is absolutely in the best interests of the states to make sure that legitimate businesses are properly licensed and registered. While providing certain required information to the public, business formation filings generate revenue for our states. It is also clearly in our best interests to make sure that illegitimate businesses find no safe haven in our borders that would put our citizens at risk and reduce the public's trust in their government.

My office does not have the authority to regulate or enforce business entity laws, nor is it equipped to do so. This is true with most other U.S. filing offices. I am one of only ten Secretaries of State who also serve as their state's securities regulator. These few states have staff trained to investigate a very different kind of crime, securities fraud. But the vast majority of secretaries of state have no experience whatsoever in the financial crime business. Traditionally, this has not been their area of responsibility.

In November 2006, the Nevada Secretary of State's office participated in the U.S. Senate Permanent Subcommittee on Investigations of the Homeland Security and Government affairs hearing regarding state business formation practices. Since that time, the State of Nevada and my office have taken action in response to the concerns raised in that hearing, including legislation and other efforts including:

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- A strict prohibition on the issuance of bearer shares by Nevada corporations
- A requirement that a list of owners of record be kept at a registered office or principal place of business within the state and that the name and contact of the custodian of the list be provided to the Secretary of State
- A requirement that the list be provided upon demand of the Secretary of State
- A requirement that answers to any interrogatory submitted in the course of a criminal investigation be provided within 3 days of the request
- The authority for the Secretary of State to suspend or revoke the charter of any business that does not comply
- The limitation on the creation of any new corporation sole, with a full prohibition in 2011
- Additional authority regarding fraudulent filings and those doing business in Nevada without proper registration
- Participation on the National Association of Secretaries of States busness filing task force, Uniform Laws Commission working groups
- Worked with the Nevada Registered Agents Association in the development and support of a best practices policy for Nevada Registered Agents.

Other states, including Wyoming and Delaware, where like Nevada, extraordinary numbers of businesses are incorporated, have also taken action regarding these concerns.

These actions and those of NASS, IACA, the ULC and others address, or are addressing the issues identified by this committee and others and have recommended solutions that are measured, reasonable, cost-effective, and workable within the traditional responsibilities of the filing office.

My office has implemented various new processes for the filing and maintaining of the public record. This legislation would require a complete rework of my office's processes, including the rewriting of computer applications, significant additions to staff, infrastructure and other resources, while creating delays and barriers to commerce. This is even more apparent now as budgets and other resources have been cut. We should be facilitating the creation of legitimate businesses in this country and the trillions of dollars in associated transactions, not making it more difficult.

The costs of transforming the role of Secretaries of State and other filing officers from administrators of a business registry to law enforcers will be enormous. The burden on and barriers placed on business will be even greater. This legislation provides for a funding mechanism that my office may request, but would need to justify such requests over those of first responders and others critical services vying for those same funds. It would be imprudent and irresponsible to divert those kinds of resources when the results are new and burdensome requirements for the states and their customers on an issue that the states and others are working together to resolve, and deny the public the other services my office has a duty to provide.

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I am also concerned that those conducting terrorism-related money laundering activities or other financial crimes will actually file a list of beneficial owners with my office, thus placing the real burden on the legitimate businesses that comply with our laws. As Nevada's securities regulator, I can attest that the vast majority of those running investment scams are not licensed with my office and their product is not registered; a fundamental principle of our investor education program. We advise people who question an investment offer to call our office; to check before they invest.

My office also cooperates with a number of other law enforcement agencies that for a variety of reasons investigate businesses incorporated in Nevada, but in my 3 years in office, not one investigation has centered on a suspicion of terrorism-related money laundering.

In summary, the measures requiring state business registries to collect information on beneficial owners as proposed by S.569, will prove detrimental to the states and businesses alike and is not necessary if the states and those working towards a solution are allowed to continue working towards a reasonable solutions The measures outlined in S.569 will not have the intended results, will penalize the millions of legitimate businesses operating in this country, will cost states in terms of real dollars and public good will, and will erase many of the gains states have made in providing efficient customer service to the business community.

Please allow the states, working with our many public and private partners, to continue to address the issues identified by this committee and others. Thank you.

51788.358

CONGRESSIONAL FIRE SERVICES INSTITUTE

900 2nd Street, N.E.
Suite 303
Washington, D.C. 20002
Phone: 202-371-1277
Fax: 202-682-FIRE
Email: update@cfsi.org

William M. Webb
Executive Director

William Jenaway
President

Board of Directors
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November 5, 2009

The Honorable Joseph Lieberman
Chairman, Senate Homeland Security and Governmental Affairs Committee
Washington, DC 20510

The Honorable Susan Collins
Ranking Member, Senate Homeland Security and Governmental Affairs Committee
Washington, DC 20510

Dear Chairman Lieberman and Ranking Member Collins:

While the Incorporation Transparency and Law Enforcement Assistance Act (S 569) shows strong potential to fight money laundering and the financing of terrorist activities, please give serious thought to possible unintended consequences if the measure is funded with federal resources currently used for homeland security programs that benefit first responders.

It is our understanding that the legislation could draw funding from the State Homeland Security Grant Program (SHSGP) and other programs that benefit first responders. Before further action is taken on this measure, please consider any impact this would have on our nation's first responders.

Thank you for your continued support of our nation's firefighters and emergency services personnel.

Sincerely,

Bill Webb
Executive Director

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FEDERAL LAW ENFORCEMENT OFFICERS ASSOCIATION
P.O. Box 326 Lewisberry, PA 17339
www.fleoa.org
(717) 938-2300

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NATIONAL AERONAUTICS & SPACE ADMIN. - OIG
NUCLEAR REGULATORY COMMISSION - OIG
POSTAL SERVICE-OIG & Inspection
RAILROAD RETIREMENT BOARD - OIG
SECURITIES & EXCHANGE COMMISSION - OIG
SMALL BUSINESS ADMINISTRATION - OIG
SOCIAL SECURITY ADMINISTRATION - OIG
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National Chapters Director
RASHEED TAHIR
National Awards Director
SHANON MAST-MCPHERSON
Legislative Consultants
McAllister and Quinn
Andy Quinn
Legislative Counsel

June 7th, 2009

The Honorable Joseph I. Lieberman
Chairman, Senate Homeland Security and Governmental Affairs Committee
Washington, D.C. 20510

The Honorable Susan M. Collins
Ranking Member, Senate Homeland Security and Governmental Affairs Committee
Washington, D.C. 20510

Dear Chair Lieberman and Ranking Member Collins:

On behalf of the 26,000 members of the Federal Law Enforcement Officers Association (FLEOA), I am memorializing our support for Senate Bill 569. The proposed legislation is very important to our ICE, FBI and IRS members as they are the lead agencies that investigate money laundering and terrorist financing cases.

While criminals cower behind the anonymity of their corporate filings, they continue to exploit this system as a means to commit terrorist financing and money laundering. Using a registered agent or attorney as the "front-person" for their company, terrorists/criminals are able to circumvent law enforcement and accomplish the following:

1. Use shell company bank accounts to launder millions of dollars;
2. Use shell companies to attempt to acquire a significant ownership interest in a financial institution;
3. Purchase real property through their shell companies to be used as stash houses to stockpile drugs or weapons/explosives;
4. Operate money remitter businesses to move their illegal proceeds to off-shore accounts;
5. Engage in cyber-terrorism attacks by disseminating contaminated emails from ostensibly legitimate companies.

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Law enforcement's ability to investigate and enforce the provisions of the Bank Secrecy Act has been impeded by terrorists/criminals who hide behind the corporate veil. This costs law enforcement agencies a substantial amount of time and money, i.e., long-term surveillance and subpoena service on numerous third parties, and allows the terrorist and/or criminal to remain "ten-steps" ahead. FLEOA maintains that the identity of the real beneficial owners should be made available to law enforcement officers who make legally authorized requests pursuant to official investigations.

While our membership respects the spirit of free enterprise in our country, we do not want to see the United States adopt the financial safe-haven image of Switzerland. If our country's laws require individuals to register vehicle or firearm ownership, the same should apply to corporate filers. The consequences for allowing terrorists and/or criminals to exploit our corporate filing system are severe. In the spirit of homeland security and protecting our great nation, we cannot permit this to continue.

We hope your committee will embrace the importance of S. 569, and work together to move it forward for consideration before the full senate. Please don't hesitate to call should you require additional input or testimony from our membership.

Respectfully submitted,

J. Adler

J. Adler
National President

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GLOBAL FINANCIAL INTEGRITY

WRITTEN STATEMENT FOR THE RECORD

OF

RAYMOND BAKER, DIRECTOR

AND

HEATHER LOWE, LEGAL COUNSEL

GLOBAL FINANCIAL INTEGRITY

THE

UNITED STATES SENATE

COMMITTEE ON HOMELAND SECURITY AND

GOVERNMENTAL AFFAIRS

Thursday, November 5, 2009

In Consideration of Senate Bill S. 569

"THE INCORPORATION TRANSPARENCY AND LAW ENFORCEMENT ASSISTANCE ACT"

Introduction:

Chairman Lieberman, Ranking member Collins, and distinguished Members of the Committee:

Thank you for providing a forum in which Global Financial Integrity (GFI) can discuss a critical issue in global law enforcement: The Incorporation Transparency and Law Enforcement Act, S. 569.

GFI promotes national and multilateral policies, safeguards and agreements aimed at curtailing the cross-border flow of illegal money in order to decrease the flight of capital out of developing countries. Our organization has identified five policy areas in the global financial system that have the greatest impact on the ability of corrupt individuals and other criminals to siphon money out of developing countries, launder it, and either hide it in accounts abroad or spend the proceeds. One of the five policy areas that we focus on is incorporation transparency.

The free flow of illicit money, terrorist financing and tax evading funds worldwide is significantly enabled by the lack of transparency in the international financial system. One of the areas where transparency would make a substantial difference in the ability of crime fighters to identify both the origins and ultimate beneficiaries of such illegal acts is in beneficial ownership of corporate entities and trusts. Corporate entities and trusts have been shown to be the vehicle of choice for the transportation of funds derived from illicit acts from one location to another and from one individual to another. At the prior hearing on Senate Bill S. 569 in June, testimony from Immigration and Customs Enforcement, the Department of Justice and the District Attorney for New York should have left little doubt that the availability of beneficial ownership information would significantly assist them in their work on a daily basis. Indeed I understand that this second hearing on S. 569 is not intended to focus on the need for incorporation transparency because that need has already been established. Instead, we understand that the Committee would like to better understand if S. 569 adequately meets the need for greater information and whether there are alternative ways of meeting the same goal.

We believe that S. 569 provides the necessary framework for addressing the many problems created by a lack of incorporation transparency. Any statement that we make herein regarding suggested improvements should not be construed as a criticism of S. 569 or as an effort to sidetrack the process of passing this important piece of legislation.

The S. 569 Approach

We note that the Organization of Economic Cooperation and Development (OECD) has identified three approaches to the issue of access to beneficial information. The first is up-front collection, which is the model on which S. 569 is based. It is characterized by collecting beneficial ownership information at the corporate formation stage by the authority charged with incorporation. The second approach is for the information to be collected and held by formation agents. The third is to create enough powers for law enforcement to be able to discover the information. The problem with the third approach is that unless the beneficial ownership information is adequately captured somewhere, powers of investigation are meaningless. The United States currently follows this third approach, but relies on financial institutions with a strong commercial reason for collecting as little information as possible to be the information resource that law enforcement would tap. This has proven ineffective. The first and second approaches both have merit, but the first approach— up-front collection— has several advantages. First,

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from an administrative standpoint it affects one government office in each state. On the other hand, placing the onus on formation agents to be the repository for data that law enforcement will need to tap into creates an arguably greater burden on an entire industry in the United States. It also opens the implementation of this law to greater interpretation and therefore less certainty for American corporations. Keeping the requirements transparent and the information private at the secretary of state level is the simplest approach without adversely impacting any one industry. We believe that altering this approach would be an error.

Entities Covered by S. 569

FATF Recommendation 33 states that "countries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities." The term "legal persons" would include partnerships and trusts. As you know, S. 569 requires beneficial ownership information to be gathered at the corporate formation stage for non-public corporations and LLCs. It does not create the same requirements for partnerships or trusts, but does compel a study into the necessity and feasibility of doing so. We do not recognize a need for different regulations with respect to partnerships and trusts and believe that mandating uniform changes would actually make compliance easier for incorporators (removing any doubt as to whether the information is necessary) and for the states (allowing them to implement one uniform change to their corporate information systems). We therefore recommend that beneficial ownership information with respect to partnerships and trusts also be collected at the state level and that this provision be enacted at the same time as the provisions with respect to corporations and LLCs.

Application of AML Laws to Formation Agents: Implications for Legal Representation

Formation agents are a front line defense in the battle against the use of corporations to launder or hide funds from illicit activities because they have the first opportunity to determine the purpose for which a legal entity is being formed and the ability to collect identifying information regarding the beneficial owners. Under S. 569, formation agents would collect the beneficial ownership information to be included on incorporation forms. There does not appear to be a concern with subjecting formation agents generally to anti-money laundering (AML) requirements, but concerns have been raised with respect to lawyers who act as formation agents in their regular course of business. One of the criticisms is that it is not clear whether AML reporting requirements would apply to all the activities of a lawyer just because he or she acts, in some circumstances, as a formation agent.

Perhaps the European model can provide guidance here. The European Union's Money Laundering Directives require lawyers to comply with AML reporting requirements while carrying out their transactional work, including corporate and trust creation, operation and management of corporations, providing tax advice, buying and selling real property and businesses, and managing client money, securities or other assets and related accounts. A distinction is made between a lawyer acting in the aforementioned capacity and a lawyer approached by a client for legal advice or who becomes a client for the purpose of legal defense. As a result, the ability of a lawyer to provide a zealous defense and ensure the right to a fair trial is not compromised. We recommend that a similarly limiting proviso be added to the amendments contemplated by Section 4 of the Bill.

Another possible approach to this issue would be to permit lawyers to choose to either report suspicious activity or withdraw their representation of or services to the client in question. This would not be a new concept.

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While every state has its own laws and rules regarding legal representation, they all have some provision stipulating when a lawyer may, and when he must, withdraw his representation. Law breaking and suspicion of law breaking are usually valid bases for withdrawal. Therefore, if a lawyer suspects that he is forming a company for illegal purposes, withdrawal is justified. Finally, all lawyers are required to establish the terms of their representation with their client, usually including an avis that they will not be able to represent the client if the lawyer discovers a conflict of interest. This is usually done in writing. It would be appropriate for a client to be informed of a lawyers AML responsibilities at that stage as well, stating that the lawyer will be complying with his duties under AML laws and that as a result of those duties it may be necessary for him to withdraw his representation.

The Definition of Beneficial Owner

S. 569 adopts a United States Treasury definition of Beneficial Owner. Given that this definition is already in use in U.S. law, it is a sensible approach. It is, however, still a subject of great debate even within the Treasury. It may be helpful to take a step back, however, and think of what we are trying to accomplish. We are trying to create a definition of beneficial ownership that is appropriate for this piece of legislation. We do not have to define the term in such a way that it changes existing use in other laws, nor do we have to find a definition that will work for all future laws that might be drawn.

The concern with the definition of beneficial ownership in S. 569 seems to be that with respect to companies with a large number of shareholders, and those that change regularly, reporting all beneficial owners and updating that information whenever a change occurred would be burdensome. If one felt sympathetic to this argument, and it should be noted that many do not, there are ways to limit the reporting requirement that would still provide significant amounts of the information that S. 569 seeks to gather. For example a beneficial owner could be defined as someone who, directly or indirectly, owns 5% of the interest in the company or received 5% or more of the profits of the company. The top 10 recipients of the largest amount of profit and/or percentage ownership of the company could be used as a definition. We are not trying to place unreasonable demands on a company through this definition; we are trying to identify significant and, if possible, multiple leads for law enforcement should they need to understand who is really benefitting from the activities of a given company.

We would also point out that the European Union's Third Money Laundering Directive not only contains this sort of threshold definition of beneficial owner but also excludes certain types of companies from needing to provide beneficial ownership information for various reasons. It might be worthwhile for the Committee to review these exclusions.

Answering the Critics

One of the main criticisms of S. 569 has been that this legislation is too financially and technologically burdensome on the states. As a threshold matter, we would like to point out that the Bill provides a source of federal funds that may be used to pay for the implementation and maintenance of a system to collect and retain beneficial ownership information. In addition to this initial observation, however, we would like to make the following points:

1. The "technologically burdensome" argument is based on the need to keep the beneficial ownership information private (not accessible by the public). The states already have the mechanisms in place to

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prevent the disclosure of information to the public. Taking a few minutes to access corporate information on any state's corporations division website, it will be noted that some initial information regarding the corporation is available simply by typing in relevant corporation details, but a fee must be paid in order to access other types of information, such as a company's certificate of incorporation, tax status, etc. The argument that the states are unable to restrict access to a particular type of information and will need to incur substantial costs in order to comply is simply false. States restrict access to information every day.

2. The Secretary of State for North Carolina has testified before you that it would cost her state in the hundreds of thousands of dollars to draft new corporation forms and laws to reflect the new requirements, undertake a public mailing campaign to spread the word of the changes, and add to and maintain the state's paper filing system (noting that, of course, this would decrease over time with the use of electronic filings). We encourage the Committee to ask for greater detail with respect to these estimates because we do not see how the addition of either (a) one line on an incorporation form, or (b) one page with one question regarding beneficial ownership (a separate page being provided to ensure that the information could be kept confidential), and the addition of one question on the online filing system could cost hundreds of thousands of dollars. We are also similarly dubious that the addition of one extra piece of paper per entity will cause an insupportable burden on their paper filing abilities, as was claimed by the Secretary of State for North Carolina. Some corporations already have corporate files held with the Secretary of State's office that include formation, merger, split, restatement, change of address and other filings that can easily run an average of between 10 and 50 pages. An additional page will hardly overburden the system.

3. The Secretary of State for North Carolina does not make the North Carolina Corporations Division budget available for public review, but we note that Delaware's 2007 Annual Report states that the revenue raised by the Division of Corporations alone was $700.8 million while its operating expenses were a mere $12 million. We will let these numbers speak for themselves.

Conclusion

We appreciate the time and effort that the Members of Congress are dedicating to S. 569; it is indeed a subject worthy of your attention. Given all of the advances that have been made in recent years to fight cross-border crime, terrorism and our own home-grown criminal element, it behooves us to provide law enforcement with the tools that are badly needed to keep not only America safe but also have a positive impact on global security. Incorporation transparency is a key part of this process. As citizens we have the expectation that our elected representatives will choose to support measures such as this for the benefit of all persons. We encourage you to meet this expectation.

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INTERNATIONAL ASSOCIATION OF FIRE FIGHTERS

HAROLD A. SCHAITBERGER VINCENT J. BOLLON

October 27, 2009

The Honorable Joseph Lieberman
Chairman
Homeland Security and
Governmental Affairs Committee
United States Senate
Washington, DC 20510

The Honorable Susan Collins
Ranking Minority Member
Homeland Security and
Governmental Affairs Committee
United States Senate
Washington, DC 20510

Dear Chairman Lieberman and Ranking Member Collins:

The IAFF wishes to express our concern on a very specific aspect of the Levin-Grassley-McCaskill Incorporation Transparency and Law Enforcement Assistance Act S. 569. While our organization certainly applauds the sponsors' desire to fight money laundering and the financing of terrorist activities, we are concerned that there might be unintended consequences that could impact America's first responders and the security of local communities.

The manner in which the proposal is currently structured and which is before your Committee envisions states being able to use existing homeland security resources (grant programs) to finance compliance with this act.

We feel that this will lead to money being siphoned from vital first responder programs, such as the State Homeland Security Grant Program (SHSGP) and to the programs that provide dollars to America's first responders.

We strongly suggest that this potential problem be corrected before the Committee acts upon this legislation.

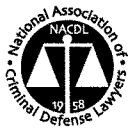
Sincerely,

A

Harold A. Schaitberger
General President

HAS:jzm

1750 NEW YORK AVENUE, N.W., WASHINGTON, D.C. 20006-5395 • (202) 737-8484 • FAX (202) 737-8418 • WWW.IAFF.ORG



NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS

October 30, 2009

The Honorable Joseph Lieberman
Chairman
Committee on Homeland Security
and Governmental Affairs
United States Senate
Washington, DC 20510

The Honorable Susan Collins
Ranking Member
Committee on Homeland Security
and Governmental Affairs
United States Senate
Washington, DC 20510

Re: Hearing on S. 569, the Incorporation Transparency and Law Enforcement Assistance Act

Dear Chairman Lieberman and Ranking Member Collins:

The National Association of Criminal Defense Lawyers (NACDL) opposes S. 569, the Incorporation Transparency and Law Enforcement Assistance Act, and urges you to vote against it. Specifically, this bill imposes a criminal penalty of up to three years imprisonment for conduct that is, in essence, a paperwork violation. Innocent, law-abiding citizens can be convicted under this offense even where there is no evidence of wrongful intent.

This bill seeks to force states to amend their incorporation laws to require those forming new corporations and LLCs to provide a list of the "beneficial owners" of the business to the state of formation. In addition to the initial filing, businesses must also update their filing annually, in those states requiring annual filings, or anytime there is a change in the beneficial ownership information in those states that do not require annual filings. This bill also seeks to amend the United States Code to include individuals who form new corporations and LLCs within the definition of "financial institutions," thereby subjecting these individuals to a variety of recordkeeping and reporting regulations under existing federal laws.

NACDL is especially concerned with Section 3(b), which would establish criminal penalties for failure to comply with the bill's numerous requirements. Specifically, providing incorrect beneficial ownership information, attempting to provide incorrect beneficial ownership information, or intentionally failing to provide updated ownership information would each be

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punishable by civil fines up to $10,000, criminal fines, and imprisonment of up to three years.[1] Such penalties would be in addition to any civil or criminal penalty that may be imposed by a state.

NACDL opposes the inclusion of a criminal provision in this bill for a number of reasons. First, this bill criminalizes the failure to provide beneficial ownership information or providing incorrect beneficial ownership information, but the bill's definition of who constitutes a "beneficial owner" is so vague, overbroad and unknowable that any number of individuals could be prosecuted for simply failing to understand what the law actually requires.[2] Fundamental notions of fairness, as well as basic constitutional principles, require that individuals understand what is required of them under the law before they can be imprisoned for noncompliance.

Second, NACDL opposes Section 3(b) of this bill because the criminal offenses it would create lack meaningful culpable state-of-mind (or *mens rea*) requirements, which would inevitably lead to unjust prosecutions, convictions, and punishments. With rare exception, the government should not be allowed to wield its power against an individual without having to prove that he or she acted with a wrongful intent. Absent a meaningful *mens rea* requirement, an individual's other legal and constitutional rights cannot protect him or her from unjust punishment for making honest mistakes or engaging in conduct that he or she had every reason to believe was legal. This is particularly true in the case of certain paperwork violations like those set forth in this bill.

This bill only requires general intent, i.e. "knowing" conduct,[3] which federal courts usually interpret to mean conduct done consciously. An individual need not have known that he or she was violating the law or acting in a wrongful manner in order to be convicted. In the case of some crimes, general intent is sufficient because the conduct is in itself wrongful. However, when applied to conduct that is not inherently wrongful, such as certain paperwork violations, the "knowingly" *mens rea* requirement allows for punishment without any shred of wrongful

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[1] Oddly, although all of S. 569's burdensome requirements would be implemented through state law, any fines levied against noncompliant individuals would be paid to the federal government—an issue that underscores the bill's problematic dismissal of the principles of federalism.

[2] Other organizations have noted the vagueness of the bill's definition of "beneficial owner." *See* Hans A. von Spakovsky and Andrew M. Grossman, *Another Sarbanes-Oxley: Threatening Small Businesses with the "Beneficial" Ownership Bill*, Legal Memorandum, No. 48, October 6, 2009, p. 5 available at http://www.heritage.org/Research/legalIssues/lm0048.cfm (detailing numerous questions about what the phrase "beneficial ownership" could mean).

[3] The *mens rea* term "intentionally," which is used in two of the offenses created in this section, also fails to provide adequate protection for would-be defendants as that term has also been held by courts to not require a specific intent to violate the law. *E.g., Alvarez v. Joan of Arc, Inc.*, 658 F.2d 1217, 1224 (7th Cir. 1981).

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intent, culpability, or sometimes even negligence. Despite every intention to follow the law, even the most cautious citizen could be found guilty under such laws. Further, these types of criminal provisions do not effectively deter criminal activity because they do not require the defendant to have any notice of the law or the wrongful nature of his or her conduct.

Third, NACDL objects to the inclusion of a criminal provision in S. 569 because there is no justification for why a "paperwork" violation, particularly a first-time violation, requires a criminal penalty. Criminal prosecution and punishment constitute the greatest power that a government routinely uses against its own citizens. As Harvard Professor Herbert Wechsler famously put it, criminal law "governs the strongest force that we permit official agencies to bring to bear on individuals."[4] This bill could result in a criminal conviction and, in some cases a term of imprisonment, for a person's failure to provide the proper paperwork. This is, quite simply, a punishment that does not fit the crime. A civil penalty would be more appropriate to address and effectively deter such conduct. In addition, whereas the criminal process is executed at the taxpayer's expense and often causes innocent employees to lose their jobs, civil enforcement can minimize those costs and produce financial benefits without guaranteeing business failure and job losses.

In addition to our opposition to the inclusion of a criminal provision with weak *mens rea* protection in S. 569, NACDL is also troubled by provisions of S. 569 that would impose government-mandated reporting obligations on members of the legal profession. Moreover, we strongly oppose any obligation that would erode the attorney-client privilege or that would create a conflict between a lawyer's legal obligations and a lawyer's ethical obligations to his or her client. On these issues, we adopt the ABA's comments as set forth in their June 30, 2009 letter.

The injury inflicted by a single misguided act of overcriminalization is not limited to an individual defendant and his or her family, but rather it undermines our entire criminal justice system and public confidence therein. For all these reasons, NACDL opposes S. 569 and urges you to do the same.

Respectfully,

Cynthia Hujar Orr

President, National Association of Criminal Defense Lawyers

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[4] Herbert Wechsler, *The Challenge of a Model Penal Code*, 65 Harv. L. Rev. 1097, 1098 (1952).

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National Association of Manufacturers

Marc-Anthony Signorino

Director
Technology Policy

August 11, 2009

The Honorable Joseph Lieberman
Chairman
Homeland Security and
Governmental Affairs Committee
United States Senate
Washington, DC 20510

The Honorable Susan Collins
Ranking Member
Homeland Security and
Governmental Affairs Committee
United States Senate
Washington, DC 20510

RE: S. 569, the "Incorporation Transparency and Law Enforcement Act"

Dear Chairman Lieberman and Ranking Member Collins:

The National Association of Manufacturers (NAM)—the nation's largest industrial trade association—shares Congress' interest in assisting law enforcement agencies in identifying and prosecuting criminals who help fund crime and terrorism. At the same time, we are extremely concerned that the Incorporation Transparency and Law Enforcement Act (S. 569), which requires states to collect more information about owners of private corporations, would significantly expose the proprietary business strategies and information of privately-held businesses in the United States.

S. 569 would require states to rewrite their business formation and associated record-keeping and reporting laws, as a condition of receiving federal homeland security grant funding. Specifically, the bill would require states to collect from privately-held corporations detailed personal information about any individuals who have control of or are entitled to company funds or assets. The proposed legislation does not contain any assurances or protections against the disclosure of the confidential or proprietary information that would be required in the business formation documents.

We are concerned that the lack of confidentiality safeguards in S. 569 would discourage the formation of new corporate entities for partnering or acquisition opportunities. For example, an existing business may form a new corporation to purchase an undervalued asset, to avoid alerting their competition to the opportunity. In order for the new acquisition to succeed, the confidentiality of the beneficial owners is critical; exposure of this ownership information could expose secret business strategy and hinder legitimate commerce.

Maintaining confidentiality of potential business acquisitions is also important in maintaining America's global competitiveness. While many of our trading partners have adopted new rules to fight money laundering that funds terrorism, S. 569 has much broader definitions and is far more intrusive than what other countries have done.

1331 Pennsylvania Avenue, NW • Washington, DC 20004-1790 • (202) 637-3072 • Fax (202) 637-3182 • msignorino@nam.org • www.nam.org

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NAM also is concerned that S. 569 threatens the personal privacy of the beneficial owners of private businesses and their families. In the vast majority of states, corporate filing information is publicly accessible. As noted above, the bill contains no assurance or protections against the disclosure of confidential information. Consequently, the names and home addresses of private business owners and their families would be available to the general public, including corporate activists.

In sum, as outlined above, NAM members believe that the disclosure provisions in S.569, as currently written, are overbroad and could have a negative impact on legitimate business activity and personal privacy. Thank you in advance for considering our concerns.

Sincerely,

Marc-Anthony Signorino

November 3, 2009

The Honorable Joseph Lieberman
Chairman
Senate Committee on Homeland Security and Governmental Affairs
340 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Lieberman:

As Co-Chairs of the Company Formation Task Force of the National Association of Secretaries of State (NASS), we are writing once again to express our opposition to S. 569, the Incorporation Transparency and Law Enforcement Assistance Act. With the Homeland Security and Governmental Affairs Committee (HSGAC) preparing to hold another hearing on this bill on November 5, it is important that you are aware of the negative impacts of this legislation. Above all, S. 569 would impose an unfunded federal mandate on states, create additional, unnecessary bureaucracy for states and businesses alike, and result in a myriad of unintended consequences that we fear would ultimately harm the business community throughout the U.S.

In its current form, the bill requires states to collect and maintain beneficial ownership information from corporations and limited liability companies formed under their laws, and to provide this information to law enforcement upon receipt of a subpoena. This legislation transforms what is largely the ministerial role of state agencies to one of oversight through the collection and processing of ownership information. Not only will this be a costly venture requiring states to fund the hardware, software, and staff to collect, store, and make accessible such data, there will also be a considerable cost to educating the public. We do not support such an expenditure of state resources, particularly during these difficult economic times.

In addition to the hardship S. 569 would impose on states, we are deeply concerned about the effects of this proposed legislation on the tens of millions of legitimate, law-abiding Americans who conduct their business through corporations. The disclosure requirements and secret access afforded to federal law enforcement may ultimately prove to be an affirmative disincentive to the creation of new businesses.

There are better, state-based solutions that already exist. For the past two and a half years, NASS has been working with a number of other prominent organizations, including the Uniform Law Commissioners, the American Bar Association, the National Conference of State Legislatures and the International Association of Commercial Administrators, to develop options that support the goals of law enforcement without unnecessarily restructuring state governments into federal agencies and negatively impacting the business community. We believe state laws and proposals like the Uniform Law Enforcement Access to Entity Information Act are the more practical and effective means by which to adopt the Financial Action Task Force's (FATF) recommendations for combating international money laundering. In addition to being state-based, these alternative approaches are simple to administer and do not seek to alter the role of the Secretary of State's office as a registration agent without enforcement powers.

As fellow public officials, we applaud the Committee's efforts to ensure that our government is being proactive in combating money laundering and other financial crimes. Although we are strongly opposed to S. 569, we will continue to work with federal agencies and law enforcement to fight illegal activity related to the company formation process.

Sincerely,

Elaine F. Marshall

Hon. Elaine Marshall
North Carolina Secretary of State
NASS Company Formation Task Force Co-Chair

Ron Thornburgh

Hon. Ron Thornburgh
Kansas Secretary of State
NASS Company Formation Task Force Co-Chair

cc: Senate Homeland Security and Governmental Affairs Committee Members

Hall of States, 444 N. Capitol Street, N.W., Suite 401, Washington, DC 20001
(202) 624-3525 Phone (202) 624.3527 Fax www.nass.org

STATE OF NEBRASKA

JOHN A. GALE
SECRETARY OF STATE

P.O. Box 94608
State Capitol, Suite 2300
Lincoln, NE 68509-4608
Phone 402-471-2554
Fax 402-471-3237
www.sos.state.ne.us

November 4, 2009

The Honorable Joseph I. Lieberman, Chairman
Committee on Homeland Security and Governmental Affairs
United States Senate
340 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Lieberman:

I am writing to express opposition to S. 569, the Incorporation Transparency and Law Enforcement Assistance Act, which is scheduled for a hearing in your committee on Thursday, November 5.

The purpose of the bill is to prevent people from exploiting U.S. corporations for criminal purposes, such as terrorism and money laundering. However, I believe the bill is extremely overbroad and would prove detrimental to the U.S. economy and to state agencies, such as the Office of the Nebraska Secretary of State, that are involved in the incorporation process.

Beginning with fiscal year 2012, S. 569 provides that each state that receives funding from the U.S. Department of Homeland Security must use an incorporation system that meets stringent requirements. Each application to form a corporation or limited liability company (LLC) must provide a list of each beneficial owner and must periodically update the list of beneficial owners. The state must provide beneficial ownership information on each corporation or LLC in response to a civil or criminal subpoena or written request from a federal agency on behalf of a foreign country.

I fear the bill raises serious privacy concerns. Passage of the bill could discourage people from forming or investing in companies to the detriment of our economy. In addition, the bill would create a paperwork burden on companies to provide the necessary information.

Passage of the bill would place a staggering burden on the Nebraska Secretary of State's Office. The bill would change the basic function of the office from a ministerial role to one of collecting and processing ownership information, and scrutinizing that information to a law enforcement standard that is beyond their qualification to judge.

I am naturally sympathetic to the law enforcement problems that S. 569 is attempting to deal with. However, I believe that banks through use of their Suspicious Activity Lists and the Internal Revenue Service are far more effective means of securing the desired information than the business entity registration process. Furthermore, I believe that state laws and proposals

similar to the Uniform Law Enforcement Access to Entity Information Act proposed by the Uniform Law Commissioners can enhance law enforcement needs in this area.

I respectfully ask that the Committee on Homeland Security and Governmental Affairs refrain from further action on S.569, and continue to monitor the progress being made by the National Association of Secretaries of State, the National Conference of State Legislatures, and the Uniform Law Commissioners toward an appropriate state-based response to the issues raised by S. 569.

Sincerely,

John A. Gale
Nebraska Secretary of State

CHAMBER OF COMMERCE
OF THE
UNITED STATES OF AMERICA

R. BRUCE JOSTEN
EXECUTIVE VICE PRESIDENT
GOVERNMENT AFFAIRS

1615 H STREET, N.W.
WASHINGTON, D.C. 20062-2000
202/463-5310

October 1, 2009

The Honorable Joseph Lieberman
Chairman
Committee on Homeland Security and
Government Affairs
United States Senate
Washington, DC 20510

The Honorable Susan Collins
Ranking Member
Committee on Homeland Security and
Government Affairs
United States Senate
Washington, DC 20510

Dear Chairman Lieberman and Ranking Member Collins:

The U.S. Chamber of Commerce, the world's largest business federation representing more than three million businesses and organizations of every size, sector,a nd region, believes that strong corporate governance and capital formation are an important part of the foundation for a vibrant and growing economy. The Chamber also believes that strong homeland security policies are necessary for the safety and well being of the United States.

The Chamber has serious concerns about S.569, the "Incorporation Transparency and Law Enforcement Act," because the bill would federalize existing state corporate law, add another unnecessary layer of government that would weaken U.S. homeland security, stifle investment,and impose significant restrictions on private businesses. This legislation is another example of government attempting to go too far in regulating the American free enterprise system.

Furthermore, the Chamber is concerned that the bill is being considered out of regular order. Traditionally, anti-money laundering measures have been under the jurisdiction of the Banking Committee, yet the bill to date has been under consideration in the Homeland Security and Government Affairs committee. Because of the bill's broad impacts upon the United States economy, the Chamber urges that the consideration of S.569 goes through regular order.

S.569 would require states to amend their corporate laws compelling detailed personal information of all beneficial owners of a non-public corporation or limited liability company to be publicly disclosed. This information would have to be updated annually. "Right to Know Laws" currently exist in almost all states,which require this private information to be made public. State eligibility for homeland security funding would be contingent upon these state corporate law amendments.

Corporate law, within the United States, has been the domain of the states for more than 150 years. This system has allowed for differing corporate and management structures that have created the foundation of the free enterprise system. S.569 would effectively federalize corporate law and create a one size fits all approach. This federalization could hamper capital formation

and discourage entrepreneurialism during the worst economic crisis in the past 75 years, by placing a chilling effect on legitimate business activity.

Corporate formation and changes go on continuously. Bedrocks of the American economy, such as Microsoft and Wal-Mart,started off as small businesses and grew into large ones creating untold wealth and thousands of jobs. Providing competition with information on who is behind a legitimate business transaction would put the United States at a competitive disadvantage in the international community. Further, requiring the home addresses of owners and then making that information public is completely unreasonable. This sort of requirement would merely inspire legitimate businesses to incorporate outside of the United States.

By publicly disclosing beneficial ownership information at the moment of incorporation, entrepreneurs may be less likely to form businesses within the United States because of the potential dissemination of private information and legitimate business functions.

S.569 could also create other unintended consequences including new and onerous recordkeeping requirements on states. While estimates vary by state, the national Association of Secretaries of State estimates that the cost of implementing S. 569 in California could be as high as $17.5 million dollars. As the legislation is currently written,the funding for the program would be siphoned from homeland security grant funding to the states. The Chamber believes that funding for this program should not be taken from police, fire fighters, EMT personnel,and other first responders performing the critically important homeland security functions of the states.

Because S.569 only applies to nonpublic corporations and limited liability corporations, many other forms of businesses are exempted from such disclosure regimes. It is unclear how S.569, by targeting only nonpublic and limited liability corporations, would stem money laundering or terrorist financing. Bad actors will not hesitate to exploit loopholes regarding other forms of business entities.

Lastly, the stated goal of the legislation is to respond to the recommendations from the Financial Action Task Force (FATF) in 2006. The Chamber believes that the proposed mandates go beyond the requirements of FATF and encourage Congress to work with the private sector and states to develop an alternative. There are other proposals in the public domain that could better accomplish the goal of money laundering prevention without the harmful effects on all parties involved.

Small and emerging businesses, which are often formed as nonpublic and limited liability corporations,a re the engine for economic growth and job creation in the United States. Accordingly, the Chamber urges you to oppose S.569 because it would create a chilling effect upon legitimate business activity and harm economic growth and job creation.

Sincerely,

R. Bruce Josten

Cc: The Members of the United States Senate

51788.377

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

The Honorable Christopher Dodd
Chairman
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, DC 20510

Dear Senator Dodd:

Thank you for your letter of September 22, 2009, inquiring about the Department of the Treasury's efforts to enhance our government's access to information regarding beneficial ownership of legal entities. Addressing the misuse of legal entities is key to our efforts to combat various forms of financial crime – including money laundering, terrorist financing, tax evasion, and sanctions evasion – as well as to protect the integrity of our financial system. As you indicate in your letter, enhancing access to beneficial ownership information is a global challenge. In our effort to develop a comprehensive approach to address this challenge, Treasury is collaborating with interagency partners in the law enforcement and regulatory communities, the Congress, state-based authorities, the private sector and our international counterparts. Our goal is to enhance the availability of beneficial ownership information of legal entities, while maintaining an open investment policy and refraining from actions that disadvantaging our nation's economic prosperity.

Our comprehensive approach for achieving this goal includes ongoing efforts to advance the following three fundamental objectives:

- **Make "beneficial ownership" information about legal entities created in the United States available to law enforcement** – Treasury is developing a proposal for federal legislation that: (i) encourages States to reform their entity creation laws to require the submission and availability of beneficial ownership information at the time of creation of the entity and throughout its existence; and (ii) introduces penalties to discourage the misuse of legal entities created in the United States. The legislative proposal will address these concerns and build upon the Uniform Law Enforcement Access to Entity Information Act approved by the National Conference of Commissioners for Uniform State Laws (NCCUSL). We will continue to work with the Congress, the law enforcement community, State-based authorities and the private sector in developing our legislative proposal, which we anticipate completing by year-end.

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- **Clarify and strengthen customer due diligence requirements for U.S. financial institutions with respect to the beneficial ownership of legal entity accountholders** – We are developing guidance for financial institutions to clarify when and how to identify and verify beneficial ownership as a necessary component of conducting customer due diligence of legal entity accountholders. We are currently working with the regulatory community to determine the form and content of that guidance. We will also continue to work with the regulatory and law enforcement communities and with industry in determining whether and, if so, how such due diligence requirements may need to be strengthened.

- **Clarify and facilitate global implementation of international standards regarding beneficial ownership** – As you note in your letter, in 2003 the Financial Action Task Force (FATF) reviewed and updated its 40 recommendations for jurisdictions to implement appropriate countermeasures against money laundering. Two of those recommendations – Recommendation 5 and Recommendation 33 – specifically address beneficial ownership and have created implementation challenges for the overwhelming majority of jurisdictions around the world. As we move forward in addressing these beneficial ownership challenges in the United States, we are also working with our counterparts in the FATF to ensure that these standards evolve in a way that is achievable in a practical sense, as well as effective, and that our efforts are consistent with the evolving views and ongoing efforts of the international community.

As always, we are grateful for your leadership on these issues and the continued support of the Congress as we move forward.

Sincerely,

Timothy F. Geithner

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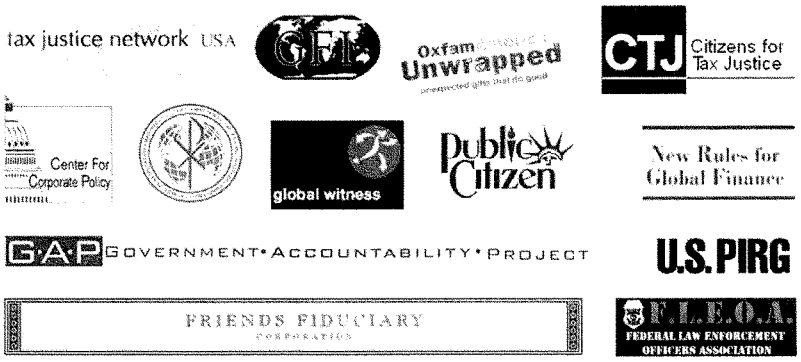

November 4,200 9

The Honorable Senator Joseph I. Lieberman, Chairman
The Honorable Senator Susan M. Collins, Ranking Member
Senate Committee on Homeland Security and Governmental Affairs
340 Dirksen Senate Office Building
Washington, DC, 20510

Re: Update to letter dated June 18, 2009 submitted in support of the S. 569, The Incorporation Transparency and Law Enforcement Act

Dear Mr. Chairman and Ranking Member:

In advance of the Hearing before the Homeland Security and Governmental Affairs Committee on November 5, 2009 concerning Senate Bill 569, the Incorporation Transparency and Law Enforcement Assistance Act (S. 569), we are writing to express our support for the adoption of S. 569 as drafted. Incorporation transparency is an invaluable tool to (i) combat national and international crime and terrorism, (ii) hinder the financing thereof, and (iii) frustrate the ability of perpetrators to hide and benefit from the proceeds of their crimes.

You may recall that several of the undersigned organizations submitted a letter to you in support of S. 569, dated June 18, 2009 (attached hereto for reference). The signatories hereto confirm or re-affirm the sentiments expressed in that letter. **In the time that has elapsed since the June 18th letter was delivered to you, however, we have become aware of some of the concerns that have been voiced by industry and at the state level with respect to this Bill. We would like to supplement the June 18th letter by identifying and responding to some of those concerns as follows:**

1. Concern: S. 569 is trying to federalize state incorporation laws.

   Response: S. 569 does not require any state to enact any law with respect to corporations; it merely requires the states to add one more question to their existing incorporation forms and to make the information provided available to law enforcement upon presentation of a subpoena or summons. Federalization would be a fair charge if the bill required federal control of the corporate formation process or the incorporation determination, but no such requirements are part of the bill. Instead, the bill requires one additional piece of information to be collected regarding the beneficial owners of the corporations being formed to prevent the misuse of U.S. corporations by criminals and other wrongdoers within or outside of the United States.

2. Concern: S. 569 will be contrary to "Right to Know" laws on the books in many states.

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Response: Some states have chosen to put into place laws allowing public access to incorporation information, reflecting a decision by each such state legislature to support a policy of general public access. Those laws are also subject to state interpretation, and may permit certain personal information to be kept nonpublic, if a state chooses that course of action. S. 569 does not preempt state law. To the contrary, S. 569 expressly permits states to keep corporate beneficial ownership information non-public and limit access to such information to appropriate law enforcement authorities.

3. Concern: S. 569 will make public information that is important to safeguard corporate strategy.

   Response: Again, S. 569 takes no position on the issue of public access and expressly permits states to keep corporate beneficial ownership information non-public and limit access to such information to appropriate law enforcement authorities. To the extent that some states choose to make such information public, corporations should have no cause for concern if any strategies revealed do not break federal or state laws. We should not permit corporate secrecy to be used as a shield to hide corporate misconduct.

4. Concern: Implementation of S. 569 at the state level will be a costly burden on states.

   Response: Beneficial ownership information can be collected via existing electronic incorporation methods and stored in existing electronic databases. Alternatively, such information can be obtained by adding the relevant question and space for a response on existing paper incorporation forms. Still another approach would be for a state to add one additional piece of paper to the exiting form requesting beneficial ownership information which would not be included in the publicly available information. It is important to note that while incorporation information may be a matter of public record in many states, states do charge a variety of fees for collecting such information and for supplying such information to the public upon request, and these fees are always subject to change. Only a portion of this information is reproduced by the states free of charge. States use these fees to either underwrite or offset the cost of their incorporation activities and in some cases as a source of additional revenue. For example, according to the 2007 Annual Report from the Division of Corporations, the Division's operating expenses for 2007 totaled $12 million, while the Division's revenue exceeded $700 million. Furthermore, the Bill provides for any initial start-up costs and the cost of any ongoing management to be sourced from the states' allocated Homeland Security monies.

We appreciate your considered attention to the Incorporation Transparency and Law Enforcement Assistance Act. We encourage you to focus on providing law enforcement with the tools needed to effectively fight crime and the criminals that rely, as a matter of course, on the lack of incorporation transparency to shield both the nature and extent of their crimes as well as their personal involvement in those crimes.

Sincerely,

Charlie Cray, Director, Center for Corporate Policy
Robert S. McIntyre, Director, Citizens for Tax Justice
Constance Brookes, Executive Director, Friends Fiduciary Corporation
Raymond Baker, Director, Global Financial Integrity
Corinna Gilfillan, Global Witness
Bea Edwards, International Program Director, Government Accountability Project
Marie Dennis, Director, MaryKnoll Office for Global Concerns
Jo Marie Griesgraber, Executive Director, New Rules for Global Finance
Gawain Kripke, Director, Policy and Research, Oxfam America
Todd Tucker, Research Director, Public Citizen's Global Trade Watch
Sarah Lewis, Executive Director,Tax Justice Network USA
Nicole Tichon, Federal Tax and Budget Reform Advocate, U.S. Public Interest Research Groups (U.S. PIRG)
Jon Adler, National President, Federal Law Enforcement Officers Association

CC: The Honorable Timothy F. Geithner, Secretary, Department of the Treasury
The Honorable Peter R. Orszag, Director, Office of Management & Budget
The Honorable Max Baucus, Chairman, Senate Committee on Finance
The Honorable Charles B. Rangel, Chairman, House of Representatives Committee on Ways and Means Committee

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June 18, 2009

The Honorable Senator Joseph I. Lieberman, Chairman
The Honorable Senator Susan M. Collins, Ranking Member
Senate Committee on Homeland Security and Governmental Affairs
340 Dirksen Senate Office Building
Washington DC, 20510

Dear Mr. Chairman and Ranking Member:

We the undersigned write to express our support for Senate Bill 569, the Incorporation Transparency and Law Enforcement Assistance Act.

It is clear that implementing the provisions of this legislation will help law enforcement stop the misuse of U.S. corporations for tax fraud, money laundering, terrorist financing and other illicit financial transactions. Equally crucial will be to bring the United States in line with international standards of transparency.

Practitioners in offshore jurisdictions accuse the United States of demonstrating hypocrisy by calling for compliance with international standards to combat money laundering, terrorist financing, and tax evasion while failing to meet those standards itself. Cayman, Bahamas, BVI and other tax havens cite Delaware, Nevada, Wyoming, and other states for failing to comply with international standards requiring the collection of beneficial ownership information for the companies formed under their laws.

The Financial Action Task Force on Money Laundering (FATF) issued a report in 2006 criticizing the United States for its failure to comply with a FATF standard requiring countries to obtain beneficial ownership information for the corporations formed under their laws. The United States, to this day, remains non-compliant.

The FATF is an inter-governmental body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing. It is the leading international anti-money laundering body in the world. FATF Members and Associate Members include a number of nations commonly regarded as secrecy jurisdictions or tax havens.

In order for the United States to obtain international cooperation from other jurisdictions for combating tax evasion, money laundering and terrorist financing, it is essential for it to be seen as compliant with international standards of transparency. Enacting the Incorporation Transparency and Law Enforcement Assistance Act would ensure that the United States meets its commitment to comply with FATF anti-money laundering standards, and would restore a critical measure of credibility in its international stature.

Sincerely,

Charlie Cray, Director, Center for Corporate Policy
Robert S. McIntyre, Director, Citizens for Tax Justice
Constance Brookes, Executive Director, Friends Fiduciary Corporation
Raymond Baker, Director, Global Financial Integrity
Corinna Gilfillan, Global Witness
Bea Edwards, International Program Director, Government Accountability Project
Marie Dennis, Director, MaryKnoll Office for Global Concerns
Jo Marie Griesgraber, Executive Director, New Rules for Global Finance
Gawain Kripke, Director, Policy and Research, Oxfam America
Todd Tucker, Research Director, Public Citizen's Global Trade Watch
Sarah Lewis, Executive Director,Tax Justice Network USA

CC: The Honorable Timothy F. Geithner, Secretary, Department of the Treasury
The Honorable Peter R. Orszag, Director, Office of Management & Budget
The Honorable Max Baucus, Chairman, Senate Committee on Finance
The Honorable Charles B. Rangel, Chairman, House of Representatives Committee on Ways and Means Committee

51788.383

Post-Hearing Questions for the Record
Submitted to the Honorable David S. Cohen
From Senator Carl Levin

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. **Since the hearing, media reports have continued to identify U.S. corporations with hidden owners engaged in wrongdoing. For example, one New York corporation, Assa Corp., which was the record owner of a New York skyscraper and collected millions of dollars in rent, is alleged to have been secretly owned by the Alavi Foundation which allegedly funneled those millions of dollars to Iran. In Florida, a U.S. lawyer is alleged to have conducted a Ponzi scheme in which he allegedly siphoned off as much as $1 billion in investor money, used the money in part to purchase real estate, and formed dozens of U.S. corporations to hide his ownership of those real estate parcels.**

   (a) Are these the types of cases whose investigation by law enforcement would be assisted if States had beneficial ownership information for U.S. corporations in their files?

   Yes, Treasury strongly believes that law enforcement would be assisted if beneficial ownership for U.S. legal entities were available to law enforcement upon appropriate request.

   (b) Are these the types of cases where, if a person lied on a state incorporation form about the beneficial owner of a relevant U.S. corporation, that false information might nevertheless be useful to prosecutors attempting to establish criminal intent?

   Yes, we understand that false beneficial ownership information would nonetheless be useful to law enforcement in investigations involving legal entities. Proposed Administration Amendments to S. 569 would attach criminal and civil penalties for knowingly providing false information.

   (c) Would the collection of beneficial ownership information for U.S. corporations enable U.S. law enforcement to provide useful assistance to our foreign partners investigating wrongdoing by U.S. corporations acting outside of the United States?

   Yes, there is no question that the collection of meaningful beneficial ownership information would provide useful assistance to our foreign partners investigating U.S. legal entities.

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2. **The Department of Justice and Department of the Treasury's prepared testimonies states that the Administration believes that "S. 569 should not authorize states to draw from the State Homeland Security Grant program to defray the costs of implementation." Each of you also testified at the hearing that the Department of Justice and the Department of Treasury favor requiring States to request beneficial ownership information for the corporations formed under their laws, and oppose imposing this legal obligation on the States as an unfunded mandate. Please identify funding sources that the Department of Justice and Department of Treasury support being made available to the States to carry out S. 569.**

   Treasury is not in a position to identify a specific source of funds to support the implementation of this legislation.

3. **The Department of Justice's prepared testimony states: "the Administration recommends eliminating the expansion of anti-money laundering obligations to company formation agents -- a significant administrative and regulatory burden -- in favor of broader civil and criminal federal liability for noncompliance."**
   The Department of Treasury's prepared testimony states: "S.569 should not attempt to regulate company formation agents under the Bank Secrecy Act, but instead should establish clear and significant federal criminal and civil liability for persons who fail to provide accurate beneficial ownership information as required by law."

   (a) Do Recommendations 5 and 12(d) of the Financial Action Task Force on Money Laundering (FATF) call on FATF members to require their formation agents to exercise due diligence and know their customers prior to forming corporations for them?

   Yes, FATF Recommendation 12(e) requires that customer due diligence and record-keeping requirements set out in Recommendation 5 apply to Trust and Company Service Providers (TCSP). The extension of FATF customer due diligence and record keeping requirements and other AML obligations to gatekeepers do not effectively address the money laundering and terrorist financing risk associated with the misuse of legal entities unless the use of a gatekeeper to incorporate is required. Few if any jurisdictions globally require this. Further, the extension of these obligations to gatekeeper would raise significant legislative and political challenges to the U.S. as well as many other jurisdictions.

   (b) Would the United States be in compliance with those FATF recommendations if it did not require formation agents operating within the United States to exercise due diligence and know their customers prior to forming U.S. corporations for them?

   Compliance with Recommendation 12 requires anti-money laundering regulation of casinos, real estate agents, dealers in precious metals and stones, lawyers, accountants and TCSPs. The U.S. has extended BSA regulations to casinos and dealers in precious metals and stones but not to the other categories listed above. Even if the BSA were

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extended to TCSPs by requiring that they conduct due diligence and know their customers prior to forming U.S. corporations, the U.S. would not be compliant with Recommendation 12 because the U.S. does not extend AML obligations to real estate agents, lawyers or accountants.

(c) The European Union's 2005 Third Money Laundering Directive directed its 27 member nations, as of 2007, to require their formation agents to exercise due diligence and know their customers before forming corporations for them. Has this requirement disrupted corporate formation or the investment of capital within the European Union?

Treasury does not have access to statistics regarding the impact of the 3rd EU Money Laundering Directive on corporate formation or investment in the European Union. However, it is not clear that there has been any significant impact on company formation and investment of capital within the EU as a result of this requirement because, among other reasons, the EU 3rd AML Directive does not require the use of a TCSP to form a corporation.

(d) If the 27 European Union nations impose an anti-money laundering obligation on their formation agents requiring them to know their customers, but the United States does not, is it likely that more wrongdoers will attempt to use U.S. formation agents?

It is possible that the extension of AML obligations to TCSPs in the European Union may result in more illicit actors attempting to form U.S. legal entities with or without a formation agent. It is also possible that the extension may have no impact because illicit actors are not required to use a TCSP to form a legal entity in any of the European Union member states. It is clear that while requiring a regulated intermediary to create legal entities is one way to address this problem, there are few jurisdictions that require the use of an intermediary, and there are other ways in which meaningful beneficial ownership information can be collected and maintained.

51788.386

Post-Hearing Questions for the Record
Submitted to the Honorable David S. Cohen
From Senator Thomas R. Carper

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. **Is Finding #10 in S. 569 which states that "all countries in the European Union are required to identify beneficial owners of the corporations they form" an accurate statement?**

   No, finding #10 in S. 569 is not an accurate statement. The EU 3rd Money Laundering Directive (MLD) has been enacted in most EU jurisdictions. The Directive requires collection and verification of beneficial owners by Trust and Company Service Providers (TCSPs) and other gatekeepers, but not by chartering authorities. In most jurisdictions, individuals can choose to by-pass a TCSP and file directly with the chartering authority. Individuals are generally not required to give the name(s) of the beneficial owner(s) if they file directly with a chartering authority.

2. **Please provide a list of all FATF member countries that have been deemed by the FATF to be in full compliance with FATF Recommendation #33.**

   Italy is the only FATF member to be rated fully compliant with Recommendation 33, and Italy was one of the first countries to be assessed in the 3rd round. As a result of this poor compliance track record, the FATF has prioritized improving compliance with Recommendation 33 because of the growing awareness of the importance of these issues in combating all forms of financial crime and the G20s call for greater transparency in the financial system.

3. **As currently drafted, S. 569 calls for beneficial ownership information to be provided upon receipt of a civil or criminal subpoena or summons from a relatively broad group of state and federal government agencies and legislative bodies. Would the Administration agree that it would represent great progress in the fight against international terrorism, tax fraud and money laundering while allaying many privacy concerns if access to certain owner information were limited solely to federal law enforcement agencies?**

   The Administration does not agree that limiting access to federal law enforcement is the best approach. This would likely increase the burden on federal law enforcement, because State law enforcement agencies likely would request information through their federal counterparts. State law enforcement agencies have significant investigative jurisdiction and interest in combating financial crime, including through the use of beneficial ownership information with respect to suspect legal entities.

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4. **For the record, do you agree that the "records contact" and "responsible individual" as defined in NCCUSL's Uniform Law Enforcement Access to Entity Information Act (the "Uniform Law") are required to be natural persons? Do you agree that the Uniform Law prohibits the "responsible individual" from being a nominee?**

   Under NCCUSL's Uniform Law, both the "records contact" and the "responsible individual" are required to be an individual, i.e., a natural person.

   We believe that it would be very unlikely that a nominee (in the sense of someone designated for the purpose of masking the identity of another) would be able to satisfy NCCUSL's definition of records contact or responsible individual, and understand that it was the intention of the Uniform Law drafting committee that the definition would preclude a nominee from satisfying the definition. Regardless of how the definition of records contact and responsible definition are interpreted, they do not purport to be definitions of beneficial owner. Therefore, if we are committed to requiring the disclosure of beneficial ownership in the company formation process, the NCCUSL approach will not achieve this.

5. **Some witnesses have raised concerns about the problem of "tipping off" in the current NCCUSL proposal. If the "records contact" and "responsible individual" were subject to civil or criminal penalties in a "tipping off" scenario would this help to address some of these concerns?**

   Yes, adding civil or criminal penalties in a "tipping off" scenario in the current NCCUSL proposal would help address some of these concerns.

6. **During our recent hearing, several members of the Committee urged the Administration to seek out the input and advice of a broad group of businesses, entrepreneurs, investors and shareholders as it seeks to refine its position on S. 569 and better define "beneficial ownership". Please provide a sample listing of the groups and/or types of individuals that the Administration will consult during this process.**

   Please see the attached list of stakeholders Treasury has consulted since the November hearing.

51788.388

Consulted Entity
NCCUSL / American Bar Association
Koch Companies Public Sector, LLC (See US Chamber of Commerce)
National Association of Manufacturers (See: US Chamber of Commerce)
National Venture Capitalists Association
National Federation of Independent Businesses

Consulted Entity
Secretary of State: Delaware
Secretary of State: Connecticut
Secretary of State: Maine
Secretary of State: Nevada
National Association of Secretaries of States
Secretary of State: Wyoming
Secretary of State: Nebraska
Secretary of State: Florida
US Chamber of Commerce
US Chamber of Commerce (Follow-up Call)
Small Business Association Office of Advocacy
CT Corp.
Wiley Rein LLP (See: CT)

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Post-Hearing Questions for the Record
Submitted to the Honorable David S. Cohen
From Senator Susan M. Collins

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. **Some proponents of S. 569 argue that its enactment would ensure that the United States is in compliance with international agreements on anti-money laundering. Specifically, proponents point to Recommendation 33 of the Financial Action Task Force, which states that "[c]ountries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities." Yet, it is my understanding that the majority of European Union nations do not require the disclosure of beneficial ownership to incorporate. Indeed, after much consideration, the United Kingdom (UK) expressly declined to mandate beneficial ownership disclosure because its officials determined that the disadvantages outweighed the benefits of doing so. In the final analysis, UK officials concluded that criminals would not provide accurate information and that beneficial ownership is simply too difficult to define precisely. Would the concerns of UK officials not be applicable in the United States?**

   The issues raised by the U.K. authorities are serious ones that the U.S. must also address in order to have an effective and workable solution. These are concerns the Administration took into consideration in drafting amendments to S. 569. I testified last November that there is no perfect solution to this problem and that no legislation will completely prevent illicit actors from abusing legal entities. Nonetheless, the Administration believes that the steps we are proposing to take will have a demonstrable impact.

   Since the UK report referred to above was issued, the UK has enacted new legislation complying with the EU 3rd Money Laundering Directive that defines beneficial ownership and requires all financial institutions and company formation agents (among others) to collect beneficial ownership information for their customers.

   Since I testified last November, Treasury, in close collaboration with DOJ, drafted amendments to S. 569 to address five key issues, including the definition of beneficial ownership. The Administration attempted to address the concerns regarding the definition of beneficial ownership through a precise definition that is applicable to small and large legal entities. The Administration's proposal also includes federal penalties for criminals that provide false information.

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Post-Hearing Questions for the Record
Submitted to the Honorable David S. Cohen
From Senator John Ensign

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. **You have testified about the importance of law enforcement having access to beneficial ownership information as a critical tool in the fight against financial crime. Yet you have expressed some concern with the bill that is the subject of this hearing.**

   (a) Is it the Administration's view then that this Committee should wait until Treasury and Justice formally propose their revisions to this legislation before moving on this legislation?

   Yes.

2. **National Security Letters require businesses to produce specified records to federal officials in national security investigations. In 2006, for example, the FBI's issued more than 50,000 national security letters.**

   (a) Have National Security Letters been a useful tool in fighting terrorist financing?

   We defer to law enforcement on the utility of NSLs in combating terrorist financing.

   (b) S. 569's stated purpose is to assist law enforcement in detecting, preventing, and punishing terrorism, money laundering, and other misconduct involving United States corporations. Have National Security Letters been used to get some of the same information that S.569 attempts to obtain?

   Regardless of the legal process or investigative authority employed, the lack of accurate beneficial ownership information remains a significant impediment to law enforcement investigations.

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Post-Hearing Questions for the Record
Submitted to Jennifer Shasky
From Senator Carl Levin

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. Since the hearing, media reports have continued to identify U.S. corporations with hidden owners engaged in wrongdoing. For example, one New York corporation, Assa Corp., which was the record owner of a New York skyscraper and collected millions of dollars in rent, is alleged to have been secretly owned by the Alavi Foundation which allegedly funneled those millions of dollars to Iran. In Florida, a U.S. lawyer is alleged to have conducted a Ponzi scheme in which he allegedly siphoned off as much as $1 billion in investor money, used the money in part to purchase real estate, and formed dozens of U.S. corporations to hide his ownership of those real estate parcels.

   (a) Are these the types of cases whose investigation by law enforcement would be assisted if States had beneficial ownership information for U.S. corporations in their files?

   (b) Are these the types of cases where, if a person lied on a state incorporation form about the beneficial owner of a relevant U.S. corporation, that false information might nevertheless be useful to prosecutors attempting to establish criminal intent?

   (c) Would the collection of beneficial ownership information for U.S. corporations enable U.S. law enforcement to provide useful assistance to our foreign partners investigating wrongdoing by U.S. corporations acting outside of the United States?

2. The Department of Justice and Department of the Treasury's prepared testimonies states that the Administration believes that "S. 569 should not authorize states to draw from the State Homeland Security Grant program to defray the costs of implementation." Each of you also testified at the hearing that the Department of Justice and the Department of Treasury favor requiring States to request beneficial ownership information for the corporations formed under their laws, and oppose imposing this legal obligation on the States as an unfunded mandate.

   Please identify funding sources that the Department of Justice and Department of Treasury support being made available to the States to carry out S. 569.

3. The Department of Justice's prepared testimony states: "the Administration recommends eliminating the expansion of anti-money laundering obligations to

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company formation agents -- a significant administrative and regulatory burden -- in favor of broader civil and criminal federal liability for noncompliance."

The Department of Treasury's prepared testimony states: "S.569 should not attempt to regulate company formation agents under the Bank Secrecy Act, but instead should establish clear and significant federal criminal and civil liability for persons who fail to provide accurate beneficial ownership information as required by law."

(a) Do Recommendations 5 and 12(d) of the Financial Action Task Force on Money Laundering (FATF) call on FATF members to require their formation agents to exercise due diligence and know their customers prior to forming corporations for them?

(b) Would the United States be in compliance with those FATF recommendations if it did not require formation agents operating within the United States to exercise due diligence and know their customers prior to forming U.S. corporations for them?

(c) The European Union's 2005 Third Money Laundering Directive directed its 27 member nations, as of 2007, to require their formation agents to exercise due diligence and know their customers before forming corporations for them. Has this requirement disrupted corporate formation or the investment of capital within the European Union?

(d) If the 27 European Union nations impose an anti-money laundering obligation on their formation agents requiring them to know their customers, but the United States does not, is it likely that more wrongdoers will attempt to use U.S. formation agents?

Responses to these Questions for the Record were not received at time of printing.

Post-Hearing Questions for the Record
Submitted to Jennifer Shasky
From Senator Thomas R. Carper

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. You testified that beneficial ownership information should be held within the State of incorporation and not mandated to be held by the State. I agree. But I am wondering how this would apply to the majority of small businesses and non-profit legal entities that are self-represented – meaning their physical address within the State is their registered office and they do not currently have a relationship with a third party such as a lawyer, accountant or registered agent? Would it be acceptable for this information to be held by a representative, member, or employee of the entity itself? If not and it were required to be held by a third party – presumably for a fee – wouldn't this essentially function as an unfunded mandate on every small, incorporated business in the country?

Responses to these Questions for the Record were not received at time of printing.

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Post-Hearing Questions for the Record
Submitted to Jennifer Shasky
From Senator Susan M. Collins

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. In your written testimony, you state that the Obama Administration believes that S. 569 is an important step in the right direction and provides an important platform to address the need for greater transparency in corporate formation. You also state, however, that the Administration would like S. 569 to be modified in several respects. In particular, you point to the ambiguity in, and breadth of, the definition of "beneficial ownership" and express interest in working with this Committee to "amend and further refine that definition." The lack of precision in this definition is especially problematic for the business community. What are the Administration's suggestions for refining the definition of "beneficial ownership?"

Responses to these Questions for the Record were not received at time of printing.

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Post-Hearing Questions for the Record
Submitted to David H. Kellogg
From Senator Susan M. Collins

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. S. 569 would require the States to collect and maintain beneficial ownership information on non-public corporations and limited liability companies (LLCs). Yet, almost two million corporate entities are formed each year in the United States, and many of them are publicly traded, non-profit, or limited liability partnerships not covered by this legislation. Extending coverage to such entities, however, would further exacerbate the concerns raised by the business community and the States about S. 569. Given this loophole, will this bill adequately prevent money laundering, tax evasion, and terrorist financing? Are there alternative approaches that would provide law enforcement with access to the data that they need without the serious cost to businesses and State governments?

For this legislation to have the desired effect, it would need to apply to all forms of United States business entities. Many businesses formed within the United States are public companies, non-profits and limited liability partnerships while S.569 only applies to nonpublic corporations and limited liability corporations. It is therefore unclear how S.569, with such a limited and narrow scope, would help stem money laundering or terrorist financing. Bad actors will not hesitate to exploit these gaps, leaving only legitimate businesses with the burdens of compliance.

There are also significant problems with the public nature of the required disclosures, considering the *Right to Know Laws* that currently exist around the country. By publicly disclosing beneficial ownership information at the moment of incorporation, entrepreneurs would be less likely to form businesses within the United States because of the potential dissemination of private information and its impact on legitimate business functions. Additionally, angel financing, a critical form of liquidity for start-up firms will be adversely impacted by the passage of this legislation.

The bill lacks a clear-cut definition of beneficial owner that can be understood and applied by lawyers, let alone by the common business person like me. The definition is overly broad in its breadth and scope to the extent that it may be impossible for a business to comply with a standard that can be subjectively interpreted. Simplifying the definition would strengthen the legislation, because it would be easier for the business community to comply, and consequently easier to enforce.

The U.S. Department of Treasury also stated something similar during their comments at the November 5 hearing.

"Under S. 569 as currently drafted, the ambiguity and breadth of the definition of beneficial ownership, coupled with burdensome disclosure requirements, makes compliance uncertain, time-consuming and costly. The definition and application of beneficial ownership information requirements should be sufficiently straightforward and simple in application to work for the full range of covered legal entities – from small, start-up businesses to large, complex legal entities..."

In addition to the definitional concerns, we should note the Treasury Department's objection to the funding source for S. 569. This is an issue that has prompted strong expressions of concern from public safety organizations, such as the International Association of

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Firefighters. This highlights that there are concerns about the current bill from divergent quarters ranging from the business community, the Treasury Department, union officials and first responders.

To address your second question, there are plenty of ways to approach this problem in a more effective way. Legitimate businesses have no issue complying with reasonable and effective measure that crack down on illegal activity. During the hearing there was a lot of discussion about providing law enforcement with a "string to pull on". With that said, I would like to propose the following.

A system can be developed that would give law enforcement what it needs while avoiding the adverse impact Senator Bennett discussed on the competitiveness of U.S. business. This system might have the following features:

- Adopt a workable definition of who is behind a company in the sense of controlling ownership, rather than "beneficial ownership" by ensuring that law enforcement has access to the identity of: 1) the person with the single largest voting interest in an entity; and 2) someone involved in the day –to-day operations of the company. It may be a single person or two separate people.

- The party or parties identified above would provide a government-issued, photo ID with a document agent—not the state. The document agent could be the company itself if it has a physical presence in the United States or for companies without United States operations, they could use a registered agent. The state would merely access the name or names of the people described above through the document agent holding the identification documents.

- Access to these documents held by the document agent would be restricted to law enforcement operating in the course of a criminal investigation. The document agents would be subject to penalties if they did not have the required documents on the key personnel, and they would also be subject to penalties for tipping the key people off about any requests made by law enforcement. The document agents would of course also be responsible for ensuring that they kept current copies of the documents.

You may recall that much of the testimony concerned the use of shell companies as the preferred vehicle for criminals to conduct illegal activities and conceal their identities. With this in mind, there should also be some common sense exceptions for entities about which substantial information is already readily available and where there are plenty of existing "strings to pull." Some sensible exceptions should include:

1. Regulated Entities: Banks, Investment and Trust Companies or any entity operating on a registered exchange.
2. Government Contractors
3. Companies with greater than 50 shareholders
4. Operating Company Exemption - for companies with real operations (and their affiliates and subsidiaries) if the operating company has
    a) a physical location in the United States.
    b) 20 Employees or more
    c) at least $10 million in annual revenue.

Such a system would have the added benefit of greatly reducing the costs imposed on states to develop a reasonable system of.

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2. Small businesses are the engine of the nation's economy. They are certainly central to the economy of Maine. In your written testimony, you describe a number of the burdens that S. 569 would impose on entrepreneurs and small business owners and the likely negative effect on corporate formation at a difficult time for the economy. These burdens include, among other things, increased regulation, excessive paperwork, significant compliance costs, and the loss of proprietary information and privacy. Nevertheless, I am equally concerned that terrorists and criminals have been using business entities to evade taxes, launder money, and finance terrorism. What steps do you think businesses can, and should, take to increase transparency?

We are equally concerned that terrorists and criminals have been using business entities to evade taxes, launder money and finance terrorism. These criminal actors hurt legitimate business, and more importantly ignore the laws of our great country. While we recognize there is a problem and seek to find a solution, we merely disagree with the approach proposed in S.569. Considering this, I would like to review S.569 in terms of international business competition, because as you stated above, it is critical to our economy that we get this right.

When operating in the competitive environment, businesses seek to control the disclosure of sensitive information. For instance, it is a perfectly legitimate business practice to protect trade secrets. This is true for my company or any business to ensure that the company can benefit from the first movers' advantage, as we seek to develop markets.

These companies are not interested in breaking the law; they are interested in being a competitive, effective force in their industry. By passing S. 569, small and other private companies will be placed at a competitive disadvantage in relation to their public company counterparts, partnerships, sole proprietorships and even foreign competitors. Further, all U.S. companies would operate at a competitive disadvantage to the international community, because international competitors could use this signaling information to block or bid up legitimate investment.

Venture capital firms invest in new product lines and small companies and form a vital cog in the formation of capital for small businesses. However, this financial backing, sometimes known as angel financing, is undisclosed, so as to prevent market signaling. Nevertheless, these financing vehicles would now have to be publically disclosed, potentially cutting off start up financing for small businesses that account for 80% of the job growth in the United States.

Competitors could also use this information to intimidate investors out of investing in a particular company. If this private information is publically disclosed, what is to stop competition from filing lawsuits against particular beneficial owners? This could also be done through the work of activists groups devoted to intimidating legitimate capital formation.

It should also be noted that job creation is driven by small businesses particularly in the early stages of a recovery. The Small Business Administration estimated that 1.6 million of the 1.7 million jobs created in 2002-03, after our last recession, were done by firms with 20 employees or less. By adversely impacting small businesses, S.569 has the potential to be a jobs killer.

Considering all the problems with the current legislation, I would recommend that the appropriate government agencies reach out to the business community and craft a reasonable path forward to solve this important problem. My suggestions from the first question would be an excellent starting point.

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Post-Hearing Questions for the Record
Submitted to Kevin L. Shepherd
From Senator Carl Levin

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. During your testimony at the hearing, you referenced the FATF anti-money laundering review of the United Kingdom. You stated: "In 2007, the mutual evaluation report prepared by FATF on the United Kingdom admitted that the definition of beneficial ownership is incapable from a law interpretation standpoint of precise definition as a matter of law."

   Wasn't it the United Kingdom, rather than FATF, that made that criticism of the definition of beneficial ownership?

   In discussing the Third Mutual Evaluation Report for the United Kingdom of Great Britain and Northern Ireland dated June 29, 2007 prepared by FATF, I inadvertently indicated that FATF has expressed a sentiment that beneficial ownership is not capable of precise definition. As my written statement indicated, however, this sentiment was expressed by United Kingdom authorities, not by the FATF. This sentiment was set forth in the Third Mutual Evaluation Report at Paragraph 1132 on page 234 in the context of summarizing a report prepared by consultants engaged [presumably by United Kingdom authorities] in 2002. Accordingly, my testimony hereby revised to conform it to my written testimony.

2. In the FATF mutual evaluation you cited, FATF found the United Kingdom to be only partially compliant with its recommendations due to the failure of U.K. laws to require beneficial ownership information, explaining as follows:

   - "While the investigative powers are generally sound, there are not adequate measures in place to ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities.
   - Information on the companies' registrar pertains only to legal ownership/control (as opposed to beneficial ownership) and is not verified and is not necessarily reliable."

   (a) Do you agree that FATF recommends that its member countries obtain beneficial ownership information for the corporations formed under their laws?

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Recommendation 33 states, in part, that "[c]ountries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities." "Legal persons" includes corporations under the Forty Recommendations. Recommendation 33 suggests to me that countries need to ensure that beneficial ownership information be obtained or accessed by competent authorities. Note that I have not reviewed other FATF publications on this precise issue, such as interpretative notes or other forms of guidance that FATF may have published or issued on this precise issue.

(b) Do you agree that FATF criticized the United Kingdom for failing to obtain beneficial ownership information for the corporations formed under U.K. law?

The Third Mutual Evaluation Report on the United Kingdom noted above gave the U.K. a "partially compliant" rating for FATF Recommendation 33. The text you quote in the first bullet point under item 2 above explains the basis for the partially compliant rating. A partially compliant rating means that a country has taken some substantive action and complies with some of the essential criteria of the FATF Recommendation in question. I agree that the FATF gave the United Kingdom a partially compliant rating for FATF Recommendation 33, but I leave to others to make a subjective value judgment whether the issuance of a partially complaint rating constitutes criticism of a country's compliance, partial compliance, or non-compliance with a particular FATF Recommendation.

3. During the hearing, you objected to the provision in S.569 which would impose anti-money laundering obligations on formation agents, in particular because the provision would apply to lawyers who form corporations and limited liability companies within the United States.

Do Recommendations 5 and 12(d) of the Financial Action Task Force on Money Laundering (FATF) call on FATF member countries to require their formation agents to exercise due diligence and know their customers prior to forming corporations for them?

The customer due diligence requirements contained in Recommendation 5 apply to lawyers under Recommendation 12(d) when the lawyers "prepare for or carry out transactions" for their client concerning, among other things, the "creation . . . of legal persons[.]" Note that the Forty Recommendations do not define "prepare for or carry out," thus leaving to the reader what is meant by that terminology in the context of creating a legal person. The text of the Forty Recommendations does not use the term "formation

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agents" as noted in your question, but the Glossary to the Forty Recommendations refers to "formation agents" (see definition for "designated non-financial businesses and professions," clause (f)). I assume without deciding for purposes of this response that lawyers may be "formation agents." To the extent that lawyers form legal entities and are thus viewed as formation agents, lawyers cannot legally or ethically counsel a client to engage, or assist a client, in conduct that lawyer knows is criminal (see, e.g., ABA Model Rules of Professional Conduct Rule 1.2(d)). Legal and ethical constraints, coupled with the ABA's development and implementation of good practices guidance for the legal profession, serve as strong and effective deterrents to lawyers, if and when acting as formation agents, from engaging in criminal or unethical practices.

4. The European Union's 2005 Third Money Laundering Directive directed its 27 member nations, as of 2007, to require their formation agents to exercise due diligence and know their customers before forming corporations for them. A lawsuit which sought to prevent that directive from being applied to members of the legal profession was unsuccessful, losing a European Union court decision handed down on June 26, 2007.

(a) Are lawyers who operate within the European Union member countries and who perform the mechanical function of forming a corporation within the European Union now required to exercise due diligence and know their customers?

I have not reviewed the June 26, 2007 court decision referenced above and thus cannot form a view on that decision or this question. I am not an authority on the European Union, its legal system, the lawsuit noted above, the process for forming legal entities in the European Union, or the scope, quality, or merit of opinions issued in the European Union.

(b) If the 27 European Union nations require their formation agents to exercise due diligence and know their customers, but the United States does not, is it likely that more wrongdoers will attempt to use U.S. formation agents?

I am not in a position to gauge or assess the motivations of criminals or the prospect of criminal activity in the United States in response to external forces or events. I am a transactional real estate lawyer in the United States and primarily represent domestic institutional pension funds and real estate investment trusts. I am not an expert or authority on whether the imposition of a particular regulatory regime in one or more countries may have an unintended, unexpected, or adverse consequence in the United States.

With that said, I would offer two observations. First, as I previously stated, to the extent lawyers form legal entities and are thus viewed as formation agents, lawyers cannot legally or ethically counsel a client to engage, or assist a client, in conduct that lawyer knows is criminal (see, e.g., ABA Model Rules of Professional Conduct Rule 1.2(d)).

Second, FATF, in consultation with representatives from the legal profession, adopted risk based guidance (known as the RBA [Risk Based Approach] for Legal Professionals) for the legal profession at the FATF plenary meeting in Rio de Janeiro in October 2008. The ABA Task Force on Gatekeeper Regulation and the Profession has been working to educate the legal profession in the United States on money laundering and terrorist financing risks and to implement FATF's RBA for Legal Professionals by developing voluntary good practices guidance for combating money laundering and terrorist financing. In contrast to a rules-based approach, a risk-based approach provides collaborative and responsive solutions to addressing client due diligence consistent with the attorney-client privilege, the duty of client confidentiality, and the attorney-client relationship. These legal and ethical constraints, coupled with the development and implementation of good practices guidance for the legal profession, serve as strong and effective deterrents to lawyers, if and when acting as formation agents, from engaging in criminal or unethical practices.

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Post-Hearing Questions for the Record
Submitted to Kevin L. Shepherd
From Senator Susan M. Collins

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. S. 569 would require the States to collect and maintain beneficial ownership information on non-public corporations and limited liability companies (LLCs). Yet, almost two million corporate entities are formed each year in the United States, and many of them are publicly traded, non-profit, or limited liability partnerships not covered by this legislation. Extending coverage to such entities, however, would further exacerbate the concerns raised by the business community and the States about S. 569. Given this loophole, will this bill adequately prevent money laundering, tax evasion, and terrorist financing? Are there alternative approaches that would provide law enforcement with access to the data that they need without the serious cost to businesses and State governments?

It remains the view of the American Bar Association that S. 569, as currently drafted, would essentially federalize state incorporation practices, meaning that states would be required to obtain, keep current, and make available to law enforcement authorities "beneficial ownership" information on corporations and limited liability companies. The imposition of a federal regulatory regime focused on beneficial ownership information is not workable, would be extremely costly, would impose onerous burdens on state authorities and legitimate businesses, would run counter to formation practices of major countries (including Canada, Mexico, Japan, and China), and will not achieve the laudable goal of assisting federal law enforcement authorities with pursuing and prosecuting criminal activity. These impediments, coupled with an unwieldy definition of beneficial ownership and the bill's focus on only a limited number of entities, would sow confusion into the formation process that would not enhance law enforcement's goals.

In an effort to address the legitimate concerns of the law enforcement community, the National Conference of Commissioners on Uniform State Law ("NCCUSL") worked tirelessly with various stakeholders to develop the "Uniform Law Enforcement Access to Entity Information Act," which was adopted by NCCUSL in July 2009. The model law would require, among other things, an incorporator to identify an individual within the U.S. who could provide law enforcement with the necessary information identifying the record owners and key officers of non-publicly traded entities formed under state law. The model law would enhance record-keeping requirements for covered businesses by requiring those businesses to maintain current and accurate records on record owners and managers, and on the individuals responsible for maintaining those records, and by assuring that this

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information is accessible by law enforcement officials. It would include penalties for failing to abide by the requirements for identifying a responsible records contact, as well as failure to comply with a request for information.

In sum, this model law sought to balance the competing concerns of law enforcement authorities, the state secretaries of state, and other stakeholders without the need for an onerous and burdensome federal regulatory regime for entity formation.

2. Corporate law, especially the law of corporate formation, is a State responsibility. In fact, each State has developed its own unique laws and business culture over centuries. Do you believe that it is appropriate for the Federal government to preempt the States in this context?

The ABA remains of the view that formation practices should remain a matter of state and territorial law and state sovereign prerogative, with a minimum of federal governmental regulation.

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Post-Hearing Questions for the Record
Submitted to John R. Ramsey
From Senator Carl Levin

"Business Formation and Financial Crime: Finding a Legislative Solution"
November 5, 2009

1. Your prepared testimony states: "[O]n behalf of the 26,000 members of FLEOA, I am memorializing our support for Senate Bill S. 569." One of the provisions in S. 569 would allow Department of Homeland Security (DHS) grant funds to be used by the States to pay for adding a question to their incorporation forms to request the beneficial owners of a corporation formed under State law.

   The U.S. Department of the Treasury and Department of Justice expressed concern during the hearing that using DHS funds for this purpose would take money away from law enforcement. What is the perspective of the Federal Law Enforcement Officers Association regarding using DHS grant funds to help States address the problem of U.S. corporations with hidden owners?

2. The U.S. Department of the Treasury and Department of Justice also expressed concern about applying anti-money laundering (AML) obligations to formation agents. Many countries, including the 27 member nations of the European Union, already apply AML obligations to their formation agents, requiring them to know their customers.

   (a) If the 27 European Union nations impose an anti-money laundering obligation on their formation agents requiring them to know their customers, but the United States does not, is it likely that more wrongdoers will attempt to use U.S. formation agents?

   (b) How important is this provision to law enforcement?

Responses to these Questions for the Record were not received at time of printing.

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