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Financial Accountability & Corporate Transparency

U.S. Commission on Security and Cooperation in Europe  
Helsinki Commission

Hearing on  
Combating Kleptocracy with Incorporation Transparency

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Testimony of  
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Chairman Wicker, Co-Chairman Smith, Ranking Members Cardin and Hastings, and Commissioners of the Helsinki Commission, thank you for holding this important hearing.

On behalf of the Financial Accountability and Corporate Transparency (FACT) Coalition and our member organizations, I appreciate the opportunity to talk about a foundational reform in the global anti-corruption movement and the nexus between secrecy jurisdictions, corruption, human rights, and national security.

The FACT Coalition is a non-partisan alliance of more than 100 state, national, and international organizations working to combat the harmful impacts of corrupt financial practices.<sup>i</sup>

The Coalition first formed in 2011, but I came aboard just last year on April 11. I remember the date because it was roughly one week after the release of the Panama Papers. It was an interesting start.

The Panama Papers shed light on the corruption facilitated by anonymous companies. The details of how these entities were established and some of the particular individuals involved made headlines around the world. But, to me, it was the sheer magnitude of the disclosures that proved the most shocking and enlightening. Eleven million documents, 214,000 companies, 140 politicians from 50 countries — all from just one law firm in one country.<sup>ii</sup>

The fallout was widespread. The revelations led to the resignation of Iceland's prime minister, and the exploits of Russian President Vladimir Putin's associates were well documented in the media.

The Panama Papers exposed the direct connection between corrupt and criminal practices and the secrecy that affords kleptocrats and others a vehicle to hide the money, fund illicit activity, and move it around the globe with impunity. This hearing is an important opportunity to further explore that link.

### **What Is an Anonymous Company?**

When people create companies, they aren't required to disclose who really profits from their existence or controls their activities — the actual "beneficial owners" of the business. Instead, individuals who benefit can conceal their identity by using front people, or "nominees," to represent the company. For instance, the real owner's attorney can file paperwork under his or her own name even though the attorney has no control or economic stake in the company. Finding nominees is not terribly difficult — there are corporations whose entire business is to file paperwork and stand in for company owners.

### **The Dangers of Anonymous Companies**

Anonymous companies are the vehicle of choice for kleptocrats and others who need to launder money. These individuals are then able to use the funds to stay in power and engage in

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a host of harmful actions — including undermining emerging democratic movements, upsetting global commerce, engaging in human rights abuses, and threatening our national security.

### Undermining Democratic Movements

Former soviet military officer and notorious arms dealer, Viktor Bout, created twelve anonymous U.S. companies in Delaware, Florida, and Texas. Before he was finally brought to justice, he reportedly supplied weapons to the Taliban, Liberia's Charles Taylor, Libya's Muammar Gaddafi, and the FARC, among others.<sup>iii</sup>

### Upsetting Global Commerce

Kleptocrats are often engaged in transnational crime, taking money from their own countries and hiding it in others. Researchers at Global Financial Integrity, a Coalition member, in a March 2017 report, estimated the direct financial cost of transnational crime.

“...globally the business of transnational crime is valued at an average of \$1.6 trillion to \$2.2 trillion annually. The study evaluates the overall size of criminal markets in 11 categories: the trafficking of drugs, arms, humans, human organs, and cultural property; counterfeiting, illegal wildlife crime, illegal fishing, illegal logging, illegal mining, and crude oil theft.”<sup>iv</sup>

Recent Studies have estimated the scale of money laundering to be in the range of 3 to 5 % of global GDP.<sup>v</sup>

Traffickers in counterfeit and other illicit goods and services hide behind secret corporate entities and make it more costly and difficult for legitimate businesses to engage in global commerce.

This cost is why several multinational corporations have written in support of bills in Congress to address the issue and provide world leadership. In a recent letter signed by the Chief Executive Officers of Allianz, The Dow Chemical Group, Kering Group, Salesforce, Unilever, and Virgin Group, they wrote:

“When the true owners of companies put their own name on corporate formation papers, it increases integrity in the system and provides a higher level of confidence when managing risk, developing supply chains and allocating capital. If ownership information is on record, we can have greater reputational and legal certainty in our dealings with third parties, protecting our ability to enforce contracts and safeguard our investments.”<sup>vi</sup>

These CEOs are not alone. In fact, according to Ernst & Young's Fiscal Year 2016 Global Fraud Survey, 91 percent of senior executives believe it is important to know the ultimate owner of the entities with which you do business.<sup>vii</sup>

### Disrupting U.S. Markets

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Increasingly there are stories of secret owners bidding up prices on properties and then using them as “banks” rather than homes. Not only is our real estate market a magnet for kleptocrats but the secrecy potentially fuels a loss of affordable housing in growing numbers of communities due to skyrocketing real estate prices and vastly inflated markets.

- In Manhattan, eight blocks between Lenox Hill and Central Park are nearly 40 percent unoccupied, and on the Upper East Side, more than a quarter of the properties are owned-but-vacant. Middle-income families are being priced out by those looking to hide assets.<sup>viii</sup>
- In San Francisco, the South Beach neighborhood is one-fifth unoccupied, and, in the competitive California housing market, the rent crisis is affecting middle-income families.<sup>ix</sup>
- A 2016 story in *The Miami Herald* about the impact of offshore money on the local housing market found that, “...the boom also sent home prices soaring beyond the reach of many working- and middle-class families. Locals trying to buy homes with mortgages can’t compete with foreign buyers flush with cash and willing to pay the list price or more.”<sup>x</sup>

### Abusing Human Rights

Anonymous companies regularly serve as fronts for those engaged in crimes that involve human rights abuses. According to Global Witness, also a Coalition member, “A Moldovan gang used anonymous companies from Kansas, Missouri and Ohio to trick victims from overseas in a \$6 million human trafficking scheme.”<sup>xi</sup>

Stories like that convinced Polaris, one of the leading U.S.-based organizations fighting human trafficking, to join the call to crack down on anonymous companies. Recognizing the role of anonymous companies in trafficking and the difficulty of combatting trafficking schemes if law enforcement cannot “follow the money” to specific individuals profiting from the wrongdoing, Polaris wrote the following:

“In 2016, [we] analyzed public information to identify human trafficking occurring in businesses fronting as massage parlors in Tampa, Honolulu, Houston, San Francisco, Albany, Columbus, Oklahoma City, and Fairfax County, VA. The inability to identify beneficial ownership was a recurring challenge in every location .... In order to ensure accountability for human trafficking, Congress must pass legislation that requires corporations and LLCs to disclose their beneficial owners, thereby guaranteeing that law enforcement has access to this information. Until police and prosecutors can identify the individuals operating illicit massage businesses, criminals engaged in human trafficking will continue acting with impunity across the United States.”<sup>xii</sup>

Companies with hidden owners currently play a powerful role in fueling international crimes — posing huge costs for law enforcement and civil society.

### Threatening our National Security

The threats go beyond the commercial and criminal spheres; they also threaten our national security. The stories of anonymous companies obtaining contracts with the Department of

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Defense are numerous and disturbing. I submit for the record a Global Witness report called *Hidden Menace*, which identifies, in unsettling detail, the role of secrecy in endangering our troops and undermining U.S. security. One example details how an Afghan company that was contracted to supply our troops was secretly owned by the Taliban, which used the profits to fund weapons to attack our soldiers. A second troubling report, authored by the U.S. Government Accountability Office, details how corporations with hidden owners are leasing office space to sensitive U.S. military and law enforcement agencies, a situation rife with risks that shouldn't be allowed to continue.<sup>xiii</sup>

As Congress considers new economic sanctions to counter North Korean threats, the Commissioners should take note of a U.S. Department of Justice case closed earlier this year which confirmed that Iran evaded economic sanctions in part by reaping millions of dollars annually from a New York-based anonymous company with investments in Manhattan real estate.<sup>xiv</sup>

### **Current Lack of Incorporation Transparency**

To the extent that these examples illustrate the depth of the problem, it is important to acknowledge that we've often been able to pierce the veil of corporate secrecy through luck or leaks. That must not continue to be a substitute for critical information on criminal enterprises.

In a report written by former U.S. Treasury Special Agent John Casarra for the FACT Coalition, he noted that in efforts to reclaim laundered money, we are currently "a decimal point away from total failure."<sup>xv</sup> His analysis is based on estimates that globally we catch only about 0.1 percent of laundered money. While kleptocrats and other criminal enterprises have updated their tools for the 21<sup>st</sup> century by utilizing anonymous companies, we have not updated our laws to catch them.

In its 2016 mutual evaluation, the Financial Action Task Force (FATF) found that the U.S. anti-money laundering framework has "significant regulatory gaps" and that the "lack of timely access to accurate and current beneficial ownership information (BO) remains one of the fundamental gaps in the U.S. context."<sup>xvi</sup>

A 2014 report, by academics from the University of Texas-Austin, Brigham Young University, and Griffiths University, found that the United States is the easiest place in the world to establish an anonymous company.<sup>xvii</sup>

### **Progress on Incorporation Transparency**

There is some meaningful progress being made to end the abuse of anonymous companies. As you have heard, there is progress in the European Union.

In the Ukraine, a nation whose democracy has been compromised by kleptocracy, a generation of corrupt leadership has utilized anonymous companies to hide money and undermine

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economic and social progress. A new generation of public officials has identified incorporation transparency as a critical first step for lifting the veil of secrecy. The country has begun collecting beneficial ownership information and posting it online. The old guard is pushing back, but there is some hope today in a country that has been something of a poster child for corruption fueled by secrecy for decades.

The global trend is toward transparency.

Here in the United States, multiple bills have been introduced in this Congress to clamp down on corporate secrecy. I want to thank members of this Commission who have sponsored that legislation, including Senators Whitehouse and Rubio and Representatives Smith and Moore. The True Incorporation Transparency for Law Enforcement Act, or TITLE Act, S. 1454, and the Corporate Transparency Act of 2017, S. 1717 and H.R. 3068, would each directly address the problem we are discussing today.

The bills use different mechanisms to collect information, but each includes the critical provisions needed to identify corporate owners and provide access to that information to all law enforcement and financial institutions engaged in anti-money laundering activities. All of the bills define a beneficial owner as “a natural person who, directly or indirectly exercises substantial control over a corporation or limited liability company or has a substantial interest in or receives substantial economic benefits from the assets of a corporation or limited liability company.”

That definition, with its focus on natural persons, is important to prevent the shell games in which one company owns another which, in turn, owns another and so on — all to obfuscate the name of the individuals who exercise ultimate control. The bills would also prevent naming managers or nominee directors in lieu of the true owners. Mossack Fonseca, the now infamous Panamanian law firm, employed a woman who was named as the director for approximately 20,000 companies.<sup>xviii</sup> And on YouTube, a video shows a journalist establishing a company in Delaware for her cat, Suki.<sup>xix</sup> While Delaware has become notorious as a U.S. secrecy jurisdiction, it should be noted that not one of our states currently collects beneficial ownership information.

The value in collecting this information is one of the reasons that those asked to assist in U.S. anti-money laundering efforts are calling for legislation. The Clearing House, which represents the largest banks in the country, has sent a letter urging enactment of the legislation, stating:

“Our member institutions take their obligations under the Bank Secrecy Act, USA PATRIOT Act and other applicable Federal and state laws and regulations very seriously and are committed to combating money laundering and terrorist financing and other criminal activities. Your legislation would assist them in these efforts, as it would serve as a source of beneficial ownership information when conducting due diligence on their customers.”<sup>xx</sup>

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In addition, the Independent Community Bankers Association, National Association of Federally-Insured Credit Unions, and Credit Union National Association have all indicated support for the legislation to require the collection of beneficial ownership information.

In a separate but related effort to combat anonymous corporations active in U.S. real estate markets, the U.S. Department of Treasury's Financial Crime Enforcement Network (FinCEN) recently extended and expanded an initiative known as Geographic Targeting Orders (GTOs). The GTOs require the collection of beneficial ownership information for certain cash-financed, high-end real estate transactions. The GTOs now apply to the following metropolitan areas including: Bexar County, Texas; Miami-Dade, Broward, and Palm Beach Counties in Florida; Brooklyn, Queens, Staten Island, Manhattan, and the Bronx in New York City; the counties of San Diego, Los Angeles, San Francisco, San Mateo, and Santa Clara in California; and the latest addition, the city and county of Honolulu, Hawaii.<sup>xxi</sup>

In renewing the GTOs in August, FinCEN noted that, in 30 percent of the real estate transactions covered by the rule, the purchaser was someone who had a suspicious activity report filed on them. Prior to the GTOs, we would have had no idea who was behind the purchases.

The early results of the GTOs suggest that the collection of beneficial ownership information is a necessary reform that opens the door to additional changes to crackdown on kleptocrats and others engaged in illicit financing.

We are seeing progress globally, in congress, in the administration, in the private sector, and continued support from a wide range of anti-corruption, human rights, and other organizations.

## **Conclusion**

Kleptocrats and other criminals use anonymous shell companies to hide the money they steal and maintain the power they hold. The total amounts of money are impossible to know but what we can estimate runs into the trillions. The harm caused is widespread — impacting national security, human rights, and economic and political stability.

There are many reforms we need to make, such as better coordination and information sharing among law enforcement agencies, among others. Congress recently took a critically important step when they adopted the Global Magnitsky Act to more effectively target individuals engaged in human rights abuses and grand corruption. But we must lift the veil of secrecy. We must end the use and abuse of anonymous companies. If we are unable to identify the true owners of the front companies used to launder money, it will undermine our ability to identify those responsible for the underlying crimes and our ability to enforce any additional laws we adopt or strengthen.

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<sup>i</sup> The FACT Coalition website: <https://thefactcoalition.org/>

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- iii *Global Witness*, “The Great Rip-Off”, September 25, 2014, <https://www.globalwitness.org/documents/11789/the%20great%20rip%20off.pdf>.
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- v Cassara, John A. Countering International Money Laundering. FACT Coalition, 2017, Countering International Money Laundering, [thefactcoalition.org/wp-content/uploads/2017/08/Countering-International-Money-Laundering-Report-August-2017-FINAL.pdf](http://thefactcoalition.org/wp-content/uploads/2017/08/Countering-International-Money-Laundering-Report-August-2017-FINAL.pdf).
- vi Letter dated July 11, 2017, <http://bteam.org/announcements/u-s-government-action-crucial-to-fighting-corruption/>
- vii Ernst & Young, “EY – Global Fraud Survey 2016,” April 18, 2016, <https://go.ey.com/2vGBTLN>.
- viii Joseph Lawler. “Money Laundering is Shaping US Cities,” Washington Examiner, March 27, 2017, <http://washex.am/2mVy5BJ>.
- ix Ibid
- x Nicholas Nehamas. “How secret offshore money helps fuel Miami’s luxury real-estate boom.” The Miami Herald. April 3, 2016. <http://www.miamiherald.com/news/business/real-estate-news/article69248462.html>.
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- xii Fact sheet, Polaris, 2017 <https://thefactcoalition.org/wp-content/uploads/2017/08/Polaris-Anonymous-Companies-Fact-Sheet-10-17-2016-FINAL.pdf>
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- xvii Findley, Michael et al. “Global Shell Games: Experiments in Transnational Relations, Crime, and Terrorism.” *Cambridge University Press* (March 24, 2014), Page 74. <http://bit.ly/2uTLptQ>.
- xviii “Dirty Little Secrets.” Dirty Little Secrets, Fusion, [fusion.net/story/292198/dirty-little-secrets-panama-papers-documentary/](http://fusion.net/story/292198/dirty-little-secrets-panama-papers-documentary/).
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- xx Letter dated August 3, 2017, <https://thefactcoalition.org/wp-content/uploads/2017/08/TCH-BAFT-IIB-IIF-2017-Support-Letter-HR3089.pdf>
- xxi “FinCEN Targets Shell Companies Purchasing Luxury Properties in Seven Major Metropolitan Areas.” 22 Aug. 2017, [www.fincen.gov/news/news-releases/fincen-targets-shell-companies-purchasing-luxury-properties-seven-major](http://www.fincen.gov/news/news-releases/fincen-targets-shell-companies-purchasing-luxury-properties-seven-major).

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