

STATEMENT BY SENATOR CARL LEVIN (D-MICH)

BEFORE

PERMANENT SUBCOMMITTEE ON INVESTIGATIONS

ON

FAILURE TO IDENTIFY COMPANY OWNERS IMPEDES LAW ENFORCEMENT

November 14, 2006

In 2004, the United States was home to 12 million companies, including about 9 million corporations and 3.8 million limited liability corporations or LLCs. In that year alone, our 50 states incorporated more than 1.9 million new corporations and LLCs. The vast majority of those companies operate legitimately. But a small percentage do not, functioning instead as conduits for organized crime, money laundering, securities fraud, tax evasion, and other misconduct.

In most cases, our states have no idea who is behind the companies they have incorporated. A person who wants to set up a U.S. company typically provides less information than is required to open a bank account or get a driver's license. In most cases, they don't have to provide the name, address, or proof of identification of a single owner of the new company. That's because our states have been competing with each other to set up new companies faster than ever, at less cost, and with greater anonymity for the company owners.

Most U.S. states offer electronic services that incorporate a new company, and many will set up a new company in less than 24 hours. The median fee is less than \$100. In Delaware and Nevada, for an extra \$1,000, an applicant can set up a company in less than an hour. Colorado, which incorporates about 5,000 new companies each month, told the Subcommittee that it now sets up 99% of its companies by computer, without any human intervention or review of the information provided. Incorporating all these new companies generates annual revenues totaling hundreds of millions of dollars for the states.

The problem with incorporating nearly two million new U.S. companies each year – without knowing anything about who is behind them – is that it becomes an open invitation for criminal abuse. Take a look at a few websites from firms in the business of incorporating companies around the world. [Show chart.] This website from an international incorporation company promotes setting up companies in Delaware by saying: "DELAWARE - An Offshore Tax Haven for Non US Residents." One of the cited advantages is that "Owners' names are not disclosed to the state." Another website from a United Kingdom firm called "formacompany-offshore.com" lists a number of advantages to incorporating in Nevada. [Show chart.] The cited advantages include: "No I.R.S. Information Sharing Agreement" and "Stockholders are not on Public Record allowing complete anonymity." These are just two of dozens of websites that portray our states as welcoming those who want to operate U.S. companies with anonymity.

That type of anonymity is exactly what we've been criticizing offshore tax havens for offering to their clients. In fact, our last Subcommittee hearing lambasted offshore jurisdictions for setting up offshore corporations with secret U.S. owners engaged in transactions designed to evade U.S. taxes, leaving honest taxpayers to pick up the slack.

Some U.S. company formation firms advertise the same type of anonymity and take the same type of actions that this Subcommittee has been criticizing in the offshore community for years. Take a look, for example, at a Nevada firm called Nevada First Holdings. Nevada First advertises on the Internet, offering for sale "aged" or "shelf" companies that were set up in Nevada years earlier, pointing out that an older company can lend credibility to an operation. It sells these companies to anyone who can pay the price, without obtaining any information on the true owners of the companies, since it has no legal obligation to do so.

Nevada First offers a host of services to further shield the identity of a company's owners. For example, Nevada First employees can serve as a company's nominee directors or officers to enable the true owners to "retain a higher level of anonymity." A Nevada First employee, acting as a company officer or director, can provide his own name and social security number to open a company bank account or obtain an Employer Identification Number from the IRS, so the true owners don't have to. Nevada First will also allow a company to use Nevada First's own business address, and provide the company with mail forwarding and telephone services – all the bells and whistles needed to make a phony operation look like it is actually operating in Nevada. Nevada First told the Subcommittee that it has already assigned 1,850 addresses for "suites" within its offices to the companies it has formed, at least 850 of which are still in operation. None of those companies, of course, actually operates out of those offices. The potential for abuse in this situation is obvious, and is compounded by the fact that Nevada First is far from unique in offering these services – none of which, by the way, is illegal on its face. Key to this entire charade is the lack of any U.S. requirement to get the names of the true owners of the U.S. companies being formed.

Law enforcement officials testifying today are expected to describe how U.S. companies are being used for money laundering, drug sales, securities fraud, and other misconduct, and how, in too many cases, when law enforcement agents try to find out the company owners, they run smack into a blank wall. In most cases, the states that set up the companies asked no questions about the true owners and therefore have no ownership information for law enforcement to investigate. Here are a few examples of the problems that have resulted:

- Immigration and Customs Enforcement officials reported that a Nevada-based corporation received more than 3,700 suspicious wire transfers totaling \$81 million over 2 years, but the case was not pursued, because the agency was unable to identify the corporation's owners.
- The FBI told GAO that anonymously-held U.S. shell companies are being used to launder as much as \$36 billion from the former Soviet Union. The FBI also

reported that they have 103 open cases investigating stock market manipulation, most of which involve anonymously-held U.S. shell companies.

- The U.S. Treasury's Financial Crimes Enforcement Network (FinCEN) reported that, between April 1996 and January 2004, financial institutions filed 397 suspicious activity reports involving a total of almost \$4 billion deposited in or wired through U.S. financial institutions by anonymously-held U.S. shell companies.
- A Department of Justice report revealed that Russian officials used anonymously-held shell companies in Pennsylvania and Delaware to unlawfully divert \$15 million in international aid intended to upgrade the safety of former Soviet nuclear power plants.

For decades, the leading international body fighting money laundering, called the Financial Action Task Force on Money Laundering or FATF, has warned countries not to set up companies without first finding who is really behind them. In a set of 40 recommendations that have become international benchmarks for strong and effective anti-money laundering laws, FATF has urged countries to identify the beneficial owners of the companies they establish. Recommendation 33 states: "Countries should ensure that there is adequate, accurate and timely information on beneficial ownership and control of legal persons" – that includes companies – "that can be obtained or accessed in a timely fashion by competent authorities."

The United States is a leading member of FATF and has worked with that organization to convince countries around the world to comply with FATF's 40 recommendations. Today, even a number of offshore secrecy jurisdictions such as the Cayman Islands, Bahamas, Jersey, and Isle of Man comply with the recommendation to identify the owners of the companies they establish. But the United States doesn't comply, and we just got formally cited for that failure in a 2006 FATF review of U.S. anti-money laundering laws. We now have two years to comply, or we risk expulsion from FATF which, by the way, the United States was instrumental in forming.

We shouldn't need the threat of expulsion from FATF to force us to address this problem. We should correct it for our own sake, to eliminate a gaping vulnerability to criminal misconduct. Criminals are using U.S. companies inside our borders to commit crimes. They are also using U.S. companies to commit crimes outside of our borders, which not only gives us a bad name but also means U.S. companies are being used to facilitate crimes related to drug trafficking, financial fraud, corruption, and other wrongdoing that harm our national interest.

Four reports issued in the past year describe the law enforcement problems posed by U.S. companies with unknown owners. The first is the *U.S. Money Laundering Threat Assessment*, a joint report issued in December 2005 by the Departments of Justice, Treasury, Homeland Security, and others, to identify the most significant money laundering problems we face. It devotes an entire chapter to law enforcement problems caused by anonymously-held U.S. shell

companies and trusts. Next was the April 2006 report prepared by the Government Accountability Office (GAO) at the request of the Subcommittee, entitled *Company Formations: Minimal Ownership Information Is Collected and Available*, which 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. A third report, issued in June 2006 by FATF, entitled the *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: United States of America*, criticizes the United States for failing to obtain beneficial ownership information for U.S. companies and flatly states that the U.S. is not in compliance with this FATF standard. Most recent is a report released last week by the Department of Treasury's Financial Crimes Enforcement Network which focuses squarely on the problem of LLCs with unknown owners.

Together, these four reports paint a picture of rogue U.S. companies breaking laws inside and outside of U.S. borders, operating with inadequate government records that make it hard for law enforcement to find the companies' true owners, conduct investigations, and cooperate with international requests. It is difficult to judge the scope of this law enforcement threat, since we don't know how many companies are involved in wrongdoing. But if just one-tenth of one percent of the 12 million existing U.S. companies are engaged in misconduct, that means about 12,000 suspect companies are loose in this country and the world with no record of their beneficial ownership. That's an unacceptable risk to our national security and our treasury.

Our lax standards have also created problems for our country in the international arena. The United States has been a leading advocate for transparency and openness. We have criticized offshore tax havens for their secrecy and lack of transparency, and pressed them to change their ways. But look what's going on in our own backyard. The irony is that we don't suffer from lack of transparency - there is just no information to disclose. And when other countries ask us for company owners and we have to stand red-faced and empty-handed, it undermines our credibility and our ability to go after offshore tax havens that help rob honest U.S. taxpayers. It also places us in the position of being in non-compliance with the guidelines of the very international organization promoting our message of openness and transparency.

There are many possible solutions to this problem if we have the will to act. FinCEN is considering issuing new regulations requiring company formation agents to establish risk-based anti-money laundering programs which would require careful evaluations of requests for new companies made by high-risk persons. Another approach would be for Congress to set minimum standards, so that no state would be placed at a competitive disadvantage when asking for the name of a company's true owners. This nationwide approach would also ensure U.S. compliance with international anti-money laundering standards. Still another approach would be to expand on the work of a few states which already identify some ownership information, and ask the National Conference Committee on Uniform State Laws to strengthen existing model state incorporation laws by including requirements for beneficial ownership information, monetary penalties for false information, and annual information updates.

These and other solutions become possible only if we are first willing to admit there is a problem. I thank our Chairman, Sen. Coleman, for his and his staff's strong support of this effort and for their ongoing work to help find solutions to the law enforcement problems created by anonymously-held U.S. companies.



DELAWARE AN OFFSHORE TAX HAVEN FOR NON US RESIDENTS



LLC - LIMITED LIABILITY COMPANIES OFFSHORE INCORPORATION

Non Resident General Business Company

ADVANTAGES

Any national, regardless of place of residence, may own a Delaware LLC company.

It may have one or more members.

Owners' names are not disclosed to the state. The company is not required to report any assets.

The company can be operated and managed worldwide.

TAXATION

No V.A.T. or sales tax in Delaware.

No income tax for companies operating outside of Delaware.

No income tax for non-resident members.

FEATURES

“formacompany-offshore.com”

Excerpt from website of a U.K. based
corporate formation company

Nevada Company Formations

The Advantages of Nevada

- No Personal Income Tax
- No Corporate Income Tax
- No Corporation Franchise Tax
- No Corporation Succession Tax
- No Taxes on Corporate Shares
- No State Annual Franchise Tax
- No I.R.S. Information Sharing Agreement
- Nominal Annual Fees
- Minimal Reporting and Disclosure Requirements
- Stockholders are not on Public Record allowing complete anonymity
- Registered Office – Registered Agent service

<http://formacompany-offshore.com/nevada.html>

Emphasis Added