

## *Positive Developments on Beneficial Ownership*

It is widely accepted that illicit actors continue to create legal entities, masking beneficial ownership information in order to facilitate access to the financial system and conduct financial crimes. A number of developments have recently occurred that may help the United States make progress on requiring the identification of beneficial ownership of businesses and accountholders. First, a dedicated group of members of Congress, both in the House and Senate, have been working for many years to improve incorporation transparency in the United States. The recent introduction of bipartisan bills in both Houses of Congress may be an indication that the issue is getting more serious consideration. Second, as part of the Department of the Treasury's efforts to enhance financial transparency in order to strengthen efforts to combat financial crime, including money laundering, terrorist financing, and tax evasion, the Financial Crimes Enforcement Network (FinCEN), a Treasury bureau, has been developing a regulation that would apply an explicit customer due diligence obligation on financial institutions. This would include the identification of beneficial owners of accountholders. Third, the Financial Action Task Force (FATF), the leading anti-money laundering/counter terrorist financing (AML/CFT) international standards setting body, revised its recommendations in 2012 and has incorporated an assessment of effectiveness of recommendation implementation into its next round of country evaluations. These standards include beneficial ownership recommendations. According to press reports, FATF is scheduled to begin its evaluation of U.S. compliance with its standards in 2015. Each development is discussed briefly below.

### LEGISLATIVE DEVELOPMENTS

Senator Carl Levin (D-MI), the longtime chairman of the Permanent Subcommittee on Investigation (PSI) of the Senate Committee on Homeland Security and Governmental Affairs, has spearheaded the effort to improve incorporation transparency. In 2008, Senator Levin, then Senator Norm Coleman (R-MN,) and then Sen. Barack Obama (D-IL), introduced S. 2956, the Incorporation Transparency and Law Enforcement Assistance Act, to help law enforcement stop the misuse of U.S. corporations. The bill was reintroduced in March 2009 as S. 569 by Senators Levin, Charles Grassley (R-IA) and Claire McCaskill (D-MO). Most recently, bills with the same name have been introduced in both the House and Senate. Then Senator Levin introduced S. 1465 in August 2013 and Rep. Carolyn Maloney (D-NY) introduced HR 3331 in the House in October 2013. Both of these members of Congress introduced similar

bills in 2010. The Senate bill has bi-partisan support--it is co-sponsored by a Senators Grassley, Diane Feinstein (D-CA) and Tom Harkin (D-IA). Supporters became more optimistic that progress may be made on moving the bills through Congress when Rep. Peter King (R-NY) signed on to the House bill in February 2013.

In their August press release the Senate sponsors said that the purpose of the bill is to combat acts of terrorism, money laundering, tax evasion, and other wrongdoing facilitated by U.S. corporations with hidden owners. The United States forms almost two million corporations and limited liability companies (LLCs) each year, more than the rest of the world combined, and does so without asking for the identity of the owners. The bill would require the states to add a single question to their existing incorporation forms requesting the names of the natural persons -- the beneficial owners -- behind the corporations being formed. States would not be required to verify the information, but penalties would apply to persons who submit false information. Law enforcement would be given access to the information upon presentation of a subpoena or summons.

A summary of the bill states that the beneficial ownership provisions would:

- end the practice of the 50 states forming corporations for unidentified persons, and instead require the states, directly or through licensed formation agents, to obtain the identities of the persons behind the corporations formed under their laws and ensure the information is updated as well as provide the information to law enforcement upon receipt of a subpoena or summons;
- require formation agents who sell "shelf corporations" -- corporations formed for later sale to third parties -- to identify the beneficial owners who buy them;
- require corporations or LLCs bidding on federal contracts to provide beneficial ownership information to the federal government;
- require the provision of beneficial owners' names, addresses, and a U.S. driver's license or passport number, or information from a non-U.S. passport, and
- provide States with a two year transition period to begin requiring existing corporations and limited liability companies (LLCs) to provide beneficial ownership information.

In addition, paid formation agents would be required to establish anti-money laundering programs to guard against creating U.S. corporations for wrongdoers; however, attorneys using paid formation agents would be exempt from this requirement. The bill would provide \$40 million over three years to States from existing Departments of Justice and Treasury asset forfeiture funds to pay for the cost of complying with the act. The bill specifies that funds may not be withheld from any State for failure to comply with the act but it requires a Government Accountability Office (GAO) study in five years identifying any States not in compliance so a future Congress can determine if additional steps are needed. It also requires GAO to complete a study of existing beneficial ownership information requirements for partnerships, charities, and trusts. This would not be the first time that GAO assisted Congress by conducting

studies—in 2006, GAO provided PSI with a report entitled, “Company Formations: Minimal Ownership Information Is Collected and Available.” This GAO report reviewed the legal requirements in all 50 states to set up corporations and LLCs, found that most states failed to request beneficial ownership information, and reported that the absence of this ownership information impeded law enforcement investigations of suspect corporations. Earlier, in 2000, GAO prepared a report for PSI that examined an individual who set up over 2,000 Delaware shell companies, opened bank accounts for those companies, and then moved \$1.4 billion dollars through those bank accounts, all without revealing who was behind these transactions.

## **TREASURY RULEMAKING**

FinCEN is charged with writing the U.S AML/CFT regulations for financial institutions. In March 2012, FinCEN issued an Advance Notice of Proposed Rulemaking (ANPRM) to solicit public comment on a wide range of questions pertaining to the possible application of an explicit customer due diligence (CDD) obligation on financial institutions, including a requirement for financial institutions to identify beneficial ownership of their accountholders.

In addition to a 90-day comment period, Treasury held five public hearings to invite additional comment on specific issues raised during the comment period. These hearings were held in Washington, DC and around the country and were attended by representatives from various financial services industries and non-governmental organizations, as well as members of the regulatory, law enforcement and legislative communities. Many attendees stated that the collection of beneficial ownership information was hampered by the fact that this information is not required in public listings and there are no state registries of beneficial owners of accounts formed in the various states. Further, attendees stated that the verification of beneficial ownership information would be made more efficient if federal legislation was enacted that required beneficial ownership information be provided through the company formation process.

The next step is for FinCEN to issue a Notice of Proposed Rulemaking (NPRM), which will provide the public the opportunity to comment on various aspects of its proposed CDD rule. This step will eventually lead to the issuance of a final rule. Once a final rule is issued and becomes effective, financial institutions will be required to comply with its requirements. According to information posted on OMB’s [reginfo.gov](http://reginfo.gov) web site, OMB received FinCEN’s proposed rule, Financial Crimes Enforcement Network: Customer Due Diligence Requirements for Financial Institutions, on April 11, 2014.

## **FATF STANDARDS AND COUNTRY EVALUATIONS**

The 2012 FATF standards include two recommendations pertaining directly to the transparency of beneficial owners. The first pertains to “legal persons” and 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 second states that countries should take measures to prevent the

misuse of “legal arrangements” for money laundering or terrorist financing. In particular, countries should ensure that there is adequate, accurate and timely information on express trusts, including information on the settlor, trustee and beneficiaries, that can be obtained or accessed in a timely fashion by competent authorities. For both recommendations, countries should consider measures to facilitate access to beneficial ownership and control information by financial institutions and Designated Non-Financial Businesses and Professions (such as casinos, real estate agents, and legal professionals) undertaking the CDD requirements contained in other recommendations.

In June 2006, FATF issued a report, Mutual Evaluation of the United States, on how well the United States was complying with its recommendations. One of the criticisms was that the United States failed to adequately comply with the FATF standard requiring the collection of beneficial ownership information. The report urged the United States to correct this deficiency by July 2008. Specifically, the report said that customer identification requirements apply to most types of financial institutions; however, these could be strengthened, particularly in relation to the identification of beneficial owners. The United States will be undergoing a new mutual evaluation scheduled to begin in 2015 which will assess two components—technical compliance and effectiveness—for the first time. If no progress has been made in improving compliance with the beneficial ownership recommendations, this will be reflected in the final report.

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One of the issues raised in the comments on FinCEN's ANPRM was the fact that beneficial ownership information is not currently required in company incorporation documents. Without this information it is burdensome for financial institutions to collect and verify beneficial ownership information. The specter of the FATF evaluation may spur passage of legislation on the Hill requiring that the states collect beneficial ownership information as part of their company formation process. The implementation of such legislation would make it easier for financial institutions to identify beneficial owners and comply with whatever CDD requirements FinCEN eventually issues.

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