



Department of Justice

STATEMENT OF

**M. KENDALL DAY
ACTING DEPUTY ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION
U.S. DEPARTMENT OF JUSTICE**

BEFORE THE

**COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE**

FOR A HEARING ENTITLED

**“BENEFICIAL OWNERSHIP: FIGHTING ILLICIT INTERNATIONAL FINANCIAL
NETWORKS THROUGH TRANSPARENCY”**

PRESENTED

FEBRUARY 6, 2018

Statement of M. Kendall Day
Acting Deputy Assistant Attorney General
Criminal Division
U.S. Department of Justice

Before the Senate Judiciary Committee
February 6, 2018

Chairman Grassley, Ranking Member Feinstein, and Members of the Committee. Thank you for the opportunity to discuss the ways in which the misuse of corporate structures undermines our nation's anti-money laundering (AML) laws.

As economies and financial systems become increasingly global, so too do the criminal organizations and other bad actors who attempt to exploit them. Transnational criminal organizations, kleptocrats, cybercriminal groups, terrorists, drug cartels, and alien smugglers alike must find ways to disguise the origins of the proceeds of their crimes so that they can use the profits without jeopardizing their source. These criminal actors and their illicit proceeds—which best estimates peg at more than \$2 trillion annually—are a global problem. But this is a global problem with acute and specific effects here in the United States, where we enjoy some of the deepest, most liquid, and most stable markets in the world. Those features of the U.S. financial system attract legitimate trade and investment, foster economic development, and promote confidence in our markets and in our government. Those same advantages, however, also attract criminals and their illicit funds as they seek to launder their proceeds to enjoy the fruits of their crimes, promote still more criminal activity, or both.

One of the most effective ways to deter criminals and to stem the harms that flow from their actions—including harm to American citizens and our financial system—is to follow the criminals' money, expose their activity, and prevent their networks from benefiting from the enormous power of our economy and financial system. Identifying and disrupting illicit financial networks not only assists in the prosecution of criminal activity of all kinds, but also allows law enforcement to halt and dismantle criminal organizations and other bad actors before they harm our citizens or our financial system. More broadly, money laundering undermines the rule of law and our democracy because it supports and rewards corruption and organized crime, allowing it to grow and fester. Our efforts to combat money laundering thus directly affect the safety and security of the American public, and the stability of our nation.

The Department of Justice (Department), in coordination with our colleagues from other agencies as well as our international law enforcement partners, has had numerous recent successes in thwarting criminals who sought to move, hide, or otherwise shelter their criminal proceeds using the U.S. financial system. Despite our successes, criminals continue to exploit gaps and vulnerabilities in existing laws and regulations to find new methods to conduct their illicit transactions and abuse and weaken our financial system and economy, causing real harm to our country and its citizens. Thus, it is imperative that domestic and international law enforcement, policy makers, regulators, and industry continue to work together to implement and enforce strong AML laws to detect, target, and disrupt illicit financial networks that threaten our country.

I. Background

Crime is big business. The U.N. Office on Drugs and Crime estimates that annual illicit proceeds total more than \$2 trillion globally. Here in the United States, proceeds of crimes, excluding tax evasion, were estimated to total approximately \$300 billion in 2010, or about two percent of the overall U.S. economy at the time. Of that \$300 billion, drug trafficking sales in the United States were estimated to be \$64 billion annually. Fraud, human smuggling, organized crime, and public corruption also generate significant illicit proceeds.

For any illegal enterprise to succeed, criminals must be able to hide, move, and access the proceeds of their crimes. And they must find ways to do so without jeopardizing their ongoing criminal activities. Without usable profits, the criminal activity cannot continue. This is why criminals resort to money laundering.

Money laundering involves masking the source of criminally derived proceeds so that the proceeds appear legitimate, or masking the source of monies used to promote illegal conduct. Money laundering generally involves three steps: placing illicit proceeds into the financial system; layering, or the separation of the criminal proceeds from their origin; and integration, or the use of apparently legitimate transactions to disguise the illicit proceeds. Once criminal funds have entered the financial system, the layering and integration phases make it very difficult to track and trace the money.

II. Obscured Beneficial Ownership Facilitates Money Laundering

Criminals employ a host of methods to launder the proceeds of their crimes. Those methods range from well-established techniques for integrating dirty money into the financial system to more modern innovations that make use of emerging technologies to exploit vulnerabilities.

Increasingly, sophisticated criminals seek access to the U.S. financial system through the misuse of corporate structures. Corporations, limited liability companies, partnerships, and other entity structures play a vital role in global commerce—but they are also ripe for abuse. Under our existing regime, for example, corporate structures are formed pursuant to state-level registration requirements, and while states require varying levels of information on the officers, directors, and managers, none requires information regarding the identity of individuals who ultimately own or control legal entities—also known as beneficial ownership—upon formation of these entities. Not only does the state-level regime lack beneficial ownership information, but also no federal-level system exists to consolidate or supplement the information that is collected under those various state regimes. Moreover, except in very narrow circumstances, currently applicable federal laws do not require identification of beneficial owners at account opening with financial institutions. And although banks are required to obtain certain types of customer account information during the account-opening process, those requirements do not address the conduct of bad actors who make misrepresentations to banks to achieve their illicit purposes.

Criminals exploit these gaps for their illicit purposes, often seeking to mask the nature, purpose, or ownership of their accounts and the sources of their income through the use of front

companies, shell companies, or nominee accounts. Front companies typically combine illicit proceeds with lawful proceeds from legitimate business operations, obscuring the source, ownership, and control of the illegal funds. Shell companies typically have no physical operations or assets, and may be used only to hold property rights or financial assets. Nominee-held “funnel accounts” may be used to make deposits in multiple geographic locations and corresponding withdrawals in other locations, facilitating the movement and laundering of illicit funds through the financial system. All of these methods obscure the true owners and sources of funds. And without truthful information about who owns and controls an account, banks may not be able to accurately analyze account activity and identify legitimate (or illegitimate) transactions.

The pervasive use of front companies, shell companies, nominees, or other means to conceal the true beneficial owners of assets is one of the greatest loopholes in this country’s AML regime. Indeed, the Financial Action Task Force (FATF), the inter-governmental body responsible for developing and promoting policies to protect the global financial system against money laundering and other threats, highlighted this issue as one of the most critical gaps in the United States’ compliance with FATF standards in its most recent evaluation. FATF noted that the lack of beneficial ownership information can significantly slow investigations because determining the true ownership of bank accounts and other assets often requires that law enforcement undertake a time-consuming and resource-intensive process. For example, investigators may need grand jury subpoenas, witness interviews, or foreign legal assistance to unveil the true ownership structure of shell or front companies associated with serious criminal conduct. While it will soon change, the lack of a current legal requirement to collect beneficial ownership information also undermines financial institutions’ ability to determine which of their clients pose compliance risks, which in turn harms banks’ ability to guard against money laundering.

A case involving Teodoro Nguema Obiang Mangue, the Vice President of Equatorial Guinea, highlights the challenge of successfully prosecuting money laundering schemes when parties have concealed the true ownership of bank accounts and assets. In that case, Nguema Obiang reported an official government salary of less than \$100,000 a year during his 16 years in public office. Nguema Obiang, however, used his position and influence to amass more than \$300 million in assets through fraud and corruption, money which he used to buy luxury real estate and vehicles, among other things. Nguema Obiang then orchestrated a scheme to fraudulently open and use bank accounts at financial institutions in California to funnel millions of dollars into the United States. Because U.S. banks were unwilling to deal with Nguema Obiang out of concerns that his funds derived from corruption, Nguema Obiang used nominees to create companies that opened accounts in their names, thus masking his relationship to the accounts and the source of the funds brought into the United States. The Department ultimately reached a settlement of its civil forfeiture actions against assets owned by Nguema Obiang. However, the Department needs effective legal tools to directly target these types of fraudulent schemes and protect the integrity of the U.S. financial system from similar schemes.

The Treasury Department’s recent Customer Due Diligence Final Rule (CDD rule) is a critical step toward a system that makes it difficult for sophisticated criminals to circumvent the law through use of opaque corporate structures. Beginning in May 2018, the CDD rule will require that financial institutions collect and verify the identities of the beneficial owners who own, control, and profit from companies when those companies open accounts. The collection of

beneficial ownership information will generate better law enforcement leads and speed up investigations by improving financial institutions' ability to monitor and report suspicious activity, and will also enable the United States to better respond to foreign authorities' requests for assistance in the global fight against organized crime and terrorism.

Important as it is, however, the CDD rule is only one step toward greater transparency. More effective legal frameworks are needed to ensure that criminals cannot hide behind nominees, shell corporations, and other legal structures to frustrate law enforcement. Legislative attention to this critical issue will reduce the United States' vulnerability to criminals seeking access to our financial system, facilitate law enforcement investigations, and bring the United States into compliance with international AML and counter-terrorist financing standards. The Department therefore looks forward to continued discussions with its interagency partners, Congress, and industry regarding stronger laws that target individuals who seek to mask the ownership of companies, accounts and sources of funds, and proposals to require the collection and maintenance of beneficial ownership information.

III. Conclusion

I thank the Committee for holding this hearing today and bringing attention to the threat that the lack of beneficial ownership information poses to the efficacy of our AML regime, and thus our national security and our financial system. The Department looks forward to working with Congress in the global fight against money laundering.