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Testimony before the Senate Banking Committee

"Outside Perspectives on the Collection of Beneficial Ownership Information"

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Chairman Crapo, Ranking Member Brown, and members of the Committee, my name is Greg Baer and I am president and CEO of the Bank Policy Institute. BPI is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks. Our members include universal banks, regional banks and major foreign banks doing business in the United States. Collectively, they employ nearly 2 million Americans, make 72% of all loans and nearly half of the nation's small business loans, and serve as an engine for financial innovation and economic growth. BPI strongly supports legislation to end the use of anonymous shell companies and welcomes this hearing in the hope that it will prompt swift Congressional action.

*Introduction*

Anonymous shell companies are a key method used by criminals to hide assets for a range of dangerous and illicit activities, including human trafficking, terrorist financing, money laundering and kleptocracy. All too often criminal investigations hit a dead end when law enforcement encounters a company with hidden ownership and lacks the time and resources to peel back the many layers of secrecy currently permitted by U.S. law.[1] And the more sophisticated and sinister the criminal, the more layers there generally are.

This problem is not difficult to solve. It has been solved by most countries around the world. While as a general matter our country does more than any other to identify and block the proceeds of crime, we are among the worst when it comes to allowing criminals to use the corporate form to cloak ownership; as a result, the United States has become a safe haven for those who wish to hide the proceeds or instruments of illegal activity. We have therefore been repeatedly criticized by the Financial Action Task Force, an inter-governmental AML standard-setting body, for this deficiency in our system.

Legislation to allow law enforcement to look behind the corporate veil, including the draft recently circulated by a bipartisan group of Senators on this Committee, would thus reduce crime and terrorist activity, and enhance the status of the United States as a country that fights against, not harbors, the worst people in the world.

The nation's banks already provide significant assistance to law enforcement by determining the ownership of most companies that open a bank account and then using that information to monitor the account for suspicious activity. The requirement for banks to determine corporate ownership was put in place by the Treasury Department as a workaround to close this gap in the U.S. AML/CFT regime. For banks, and, importantly, for the clients who

[1] *See* Statement of Steven M. D'Antuono before the Committee on Baking, Housing, and Urban Affairs, United States Senate, (May 21, 2019); *available at* www.banking.senate.gov/imo/media/doc/D'Antuono%20Testimony%205-21-19.pdf.

must provide this information, legislation now has the potential to centralize that process and make it more efficient. Most importantly, this legislation can provide law enforcement a first look at true shell companies that never open a bank account because they conduct no business — employ no people, earn no money, pay no taxes — but rather just hold assets.

Two relevant concerns have been expressed about such legislation, however: potential burdens on small business and privacy. To evaluate those concerns, we should consider a few key facts.

First, the draft Senate legislation requires an individual who owns more than 25% of a covered company or exercises substantial control to, at the most, disclose five pieces of information: (1) name, (2) address, (3) date of birth, (4) nationality, and (5) unique identifying number (e.g. driver's license or passport number). That is all. The House bill includes similar requirements. It is less information than one must provide to book a flight on any airline. And since the great majority of American businesses have only one owner, it would be generally provided by and about one person.

Second, under current U.S. law, this information is generally already provided any time a company opens a bank account, except in most cases a social security number is provided in lieu of a driver's license or passport number. And it must be provided for each account, and to every bank used by the company, separately. Of course, any legitimate U.S. business, large or small, probably has a bank account, because any business that earns money or pays expenses or employs people must have a bank account. Thus, for small businesses, legislation would not increase reporting obligations.

Third, with respect to privacy, establishment of a directory for corporate ownership would mean that a law enforcement official could obtain an address, date of birth, and driver's license or passport number. However, this is information already known to various arms of government, including the DMV and the IRS. It is important to note that, unlike beneficial ownership directories established in other countries, the bills currently being considered in Congress would keep ownership information private from the general public and would only be accessible to law enforcement and financial institutions performing due diligence requirements. Again, it is difficult to understand how this would be a concern of legitimate businesses. It would, however, be a concern to a drug trafficker or kleptocrat using a shell company to hold a multi-million dollar condominium in West Palm Beach.

Most small business owners in fact agree that ending anonymous shell companies should be a priority and are willing to share additional information to help prevent the abuse of our financial system. According to a poll conducted by Morning Consult on behalf of BPI, small business owners across the aisle support measures to end anonymous shell companies. Of those who had an opinion, seventy five percent of small business owners surveyed support requiring business owners to provide their personal information when forming their company to help close this loophole in the U.S. AML/CFT regime. Further, two-thirds of small business owners agree

that providing their personal information when registering their company would not be burdensome.[2]

With the potential benefits and cost of legislation now in mind, let me turn to the details of such legislation.

*Current Law*

FinCEN finalized in 2016 its customer due diligence rule, which requires banks of all sizes to identify and verify the beneficial owners of their corporate customers each time they open a new account or when a triggering event occurs.[3] In particular, institutions are generally required to collect and certify information on two ownership prongs for most business customers: (i) an equity prong that requires the identification and verification of individuals who directly or indirectly own 25 percent or more; and (ii) a control prong that requires the identification and verification of an individual with "significant responsibility to control" the legal entity.[4]

The FinCEN rule has three gaps that legislation could fill. First, while institutions are generally able to rely on the beneficial ownership information provided by the business customer, they have no reliable, complete external source against which to verify the information. Second, information provided under FinCEN's CDD rule is not reported to law enforcement. Third, many criminals avoid the banking system and launder money by forming LLCs and using them to hold real estate, art, jewelry or other valuables—all without having to open a bank account. For them, no one collects this information.

*Key Principles for Legislation*

Weighing these costs and benefits, BPI supports legislation built on the following principles.

First, in order to fulfill their obligations under the Bank Secrecy Act and FinCEN's customer due diligence rule, financial institutions should be able to rely on the information in the directory to fulfill their CDD requirements. Banks are committed to helping law enforcement catch criminals and have spent almost 50 years developing methods and tools to identify suspicious activity. Indeed, the purpose of the BSA is to provide law enforcement with highly useful leads on illicit activity.

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2 *See* The Bank Policy Institute, "Small Business Owners Say Yes to Ending Anonymous Shell Companies," (June 2019*); available at* https://bpi.com/wp-content/uploads/2019/06/Ending-Anonymous-Shell-Companies-Survey-Infographic.pdf.

3 *See* 81 Fed. Reg. at 29, 398.

4 While the focus of this hearing is on ending anonymous shell companies, BPI remains concerned about the CDD rule's requirement that covered financial institutions must reconfirm the beneficial owners of an existing customer each time that same customer opens an additional account. There is no reason to believe that the opening of a new account, in and of itself, is an indication that the beneficial ownership of the customer has changed.

Second, any filing requirements for this directory should mirror FinCEN's customer due diligence rule in terms of who must provide the information and what information must be provided.

Third, covered entities should only be required to provide minimal, but key, information during the incorporation process, which is a cornerstone of both the House and Senate bills. With both drafts, we believe that small businesses would be required to provide identifying information once, at the time they become bank customers, instead of each time they open an account, which currently happens under the CDD rule.

Fourth, reporting requirements should be clear and easy to comply with. Businesses routinely file documents with state or federal government, who could assist in educating covered businesses about their beneficial ownership reporting obligations.

Fifth, legal risk for businesses should be minimal. Both the House and Senate bills achieve this goal because the legal standard that must be met for the imposition of penalties is very high: knowingly providing, or attempting to provide, false or fraudulent beneficial ownership information or willfully failing to provide complete or updated beneficial ownership information to FinCEN. Furthermore, policymakers continue to explore various avenues, examples of which are included in both the House and Senate bills, to ensure that violations that are not knowing or willful can be easily remedied.

Sixth, the privacy of the information submitted should be protected. Under the current bills, the directory as currently envisioned would only be accessible by law enforcement and financial institutions; it would not be a public directory like those employed in other countries such as the United Kingdom. Furthermore, both the House and Senate bills impose criminal penalties for the misuse or unauthorized disclosure of beneficial ownership information. Of course, banks generally already maintain this information under existing law.

In sum, under these principles, the only type of company that would see additional burden are those that have no U.S. bank account – in other words, a shell company that spends no money in the United States, produces no goods, and employs no Americans.

*The Need for AML Reform*

As I've raised previously with this committee, banks are spending an inordinate amount of resources complying with U.S. AML/CFT obligations but are not able to effectively protect our country.[5] Instead, today's regime is geared towards compliance expectations that bear little

[5] *See* Testimony of Greg Baer before the Before the Senate Committee on Banking, Housing, and Urban Affairs "Combating Money Laundering and Other Forms of Illicit Finance: Opportunities to Reform and Strengthen BSA Enforcement," (January 9, 2018); *available at* www.banking.senate.gov/imo/media/doc/Baer%20testimony%201-9-18.pdf.

relationship to the actual goal of preventing or detecting financial crime, and fail to consider collateral consequences for national security, global development and financial inclusion.

BPI recently conducted an empirical study to better understand the effectiveness of the current BSA/AML and sanctions regime.[6] The goal of the BSA regime is to provide information that is of a "high degree of usefulness"[7] to law enforcement, yet BPI's study found that almost 50% of AML personnel are not involved in tasks directly focused on reporting to law enforcement.[8] Instead, they are performing other tasks such as issuing policies and procedures; conducting quality assurance over data and processes; and auditing of such programs and systems, among other things. Furthermore, in 2017, survey participants reviewed approximately 16 million alerts and filed over 640,000 suspicious activity reports (SARs). Institutions that record data regarding law enforcement inquiries reported that a median of 4% of SARs resulted in follow-up inquiries from law enforcement. There is no data on how many prompted an arrest or conviction, or whether SAR data proved important when sought, as the industry does not have such data.[9]

We are pleased by the bicameral, bipartisan efforts to address this imbalance as well as recent efforts by regulators to encourage banks to adopt innovative AML compliance methods.[10] As you are aware, Congress vested exclusive authority to implement the BSA in Treasury, and the Secretary has delegated that authority to FinCEN.[11] Therefore, the Treasury Department should take a more prominent role in coordinating AML/CFT policy across the government to set priorities for the regime.[12] The existing system, where priorities are not clearly established and examinations are compliance focused, with zero tolerance across all types of activity, does not produce an effective U.S. AML/CFT regime.

Furthermore, as the data shows, bank resources could be more effectively deployed, so we also recommend that Treasury conduct a broad review of current BSA requirements and

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6 *Getting to Effectiveness – Report on U.S. Financial Institution Resources Devoted to BSA/AML & Sanctions Compliance*, (October 29, 2018); *available at* bpi.com/recent-activity/getting-to-effectiveness-report-on-u- s-financial-institution-resources-devoted-to-bsa-aml-sanctions-compliance/.

7 *See* 31 U.S.C. § 5311.

8 For example, developing suspicious activity models, screening transactions, investigating potentially suspicious activity and filing SARs.

9 As discussed in BPI's study, because there is no established metric for measuring whether banks' BSA reports are "useful" to law enforcement a proxy was used, which was derived from tracking instances where law enforcement reached out to institutions, including through subpoenas, national security letters or requests for SAR backup documentation.

10 *See* "Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing," (December 3, 2018); *available at* www.fincen.gov/sites/default/files/2018-12/Joint%20Statement%20on%20Innovation%20Statement%20%28Final%2011-30-18%29_508.pdf.

11 *See* Treasury Order 108-01 (July 1, 2014).

12 The production of the National Security Strategy and the National Intelligence Priorities Framework both use interagency processes to establish priorities.

guidance and prioritize the reporting of highly useful information to law enforcement.[13] Critically evaluating, updating and streamlining requirements would not only improve the utility of SARs, but would also make more resources available to other higher value AML/CFT efforts, such as more proactively identifying and developing techniques to combat emerging trends in illicit activity. Finally, Treasury must take a more prominent role in coordinating AML/CFT policy and examinations, which is presently dispersed amongst multiple federal and state regulatory agencies. The draft Senate legislation offers a thorough, thoughtful response to this state of affairs.

BPI urges Congress to quickly adopt AML reform legislation that puts an end to anonymous shell companies and stands ready to engage with members of Congress to assist in making the U.S. AML/CFT regime more effective.

I look forward to your questions.

[13] *See* The Clearing House letter to FinCEN on its "Request for Comments Regarding Suspicious Activity Report and Currency Transaction Report Requirements," (April 10, 2018), *available at* bpi.com/wp-content/uploads/2018/04/20180410_tch_comment_letter_to_fincen_on_sar_and_ctr_requirements.pdf.