Part 1. The Misuse of Corporate Vehicles

"Even so, I am quite clear that [these distinct legal entities] were just the puppets of Dr. Wallersteiner. He controlled their every movement. Each danced to his bidding. He pulled the strings . . . they were his agents to do as he commanded. He was the principal behind them. I am of the opinion that the court should pull aside the corporate veil and treat these concerns as being his creatures."

—Lord Denning[1]

1.1 Introduction

Suppose you want to give someone some money, and because it is for an illegal purpose, you do not want anyone else to know about it. What would you do? You could hand it over in cash—but that might be difficult if it were a large sum of money or if the recipient lived a long way away. Alternatively, you could transfer funds from your bank account to the recipient's—but then your respective banks would know about it. And they might tell the police, or at least they might offer information if the police came knocking. So your ideal solution would involve a bank account that you control, but that no one can link to you—or at least only with the greatest difficulty.

That, in a nutshell, is the starting point for this study: people who are trying to find ways of sending or receiving funds or assets while concealing their involvement. The funds in question derive from bribery, embezzlement of public funds, or other forms of corruption. In the past, people hid their involvement with funds through anonymous bank accounts or accounts in fictitious names. This option, however, is becoming increasingly less available. So now the preferred method is to use a legal entity or arrangement, known (in the terminology of the Organisation for Economic Co-operation and Development [OECD]) as a "corporate vehicle." This term is mainly used to refer to companies (or corporations), foundations and trusts, and national variations of these. As emerged from our research, corrupt officials do not normally establish a corporate vehicle on their own, but rather have others do it for them. Moreover, in many cases, not just one corporate vehicle is involved but a whole web of vehicles that are linked together across several different jurisdictions.

Attempts by individuals to conceal their involvement in corruption and create a "disconnect" between themselves and their illegal assets are triggered by the efforts of law enforcement agencies to detect them. As law enforcement becomes more skillful and better

1. Lord Denning in *Wallersteiner v. Moir* [1974] 1 WLR 99, 1013.

trained in the detection of corruption, so too will corrupt parties find more refined and ingenious ways of concealing their ill-gotten gains. Action, in other words, begets a never-ending chain of reactions. It is important to bear this point in mind, for any proposed "solution" to uncovering the concealment, whether through government regulation or otherwise, inevitably will address only the problem as it exists *at that point in time*. New forms of deception will be developed in response. The quest for a silver bullet is illusory.

In addition to examining the ways in which corrupt officials misuse corporate vehicles to conceal their interests, this report takes a closer look at the chain reaction that spurs both the corrupt officials and those seeking to track them down to continuous improvement of their methods. What is law enforcement doing to detect this type of behavior? How can it discover what natural person or persons are hiding behind a network of entities or arrangements? Or, if it already has its eye on an individual, how can it link that person to a company holding the suspicious assets? And how can it provide convincing evidence of that link? What sources of information could be useful to it in its investigations? What are banks doing to help law enforcement? And what about those who assist in setting up the corporate vehicles in question—that is, the specialized professional service providers? And what about the corporate registries that hold potentially relevant information on legal entities? What help could they offer? This report addresses these and similar questions, with the aim of improving our understanding of (a) what information is currently available to investigators and (b) how that information could be improved and made more accessible.

This report is not the first to be written on this topic and undoubtedly will not be the last. In fact, the concern over the misuse of corporate vehicles dates from long before much of the recent discussion on international corruption, tax havens, and offshore centers. In a 1937 letter to then U.S. President Franklin Delano Roosevelt, his secretary of the treasury, Henry Morgenthau Jr., wrote the following about a tax haven jurisdiction like Newfoundland:

> [T]heir corporation laws make it more difficult to ascertain who the actual stockholders are. Moreover, the stockholders have resorted to all manner of devices to prevent the acquisition of information regarding their companies. The companies are frequently organized through foreign lawyers, with dummy incorporators and dummy directors, so that the names of the real parties in interest do not appear.

As a matter of international policy concern, the misuse of corporate vehicles has been on the agenda for well over a decade. Since the United Nations Office on Drugs and Crime (UNODC; at that time the UNODCCP) issued its 1998 report titled *Financial Havens, Banking Secrecy and Money Laundering*, a steady stream of reports on the issue has been forthcoming, notably *Protecting the EU Financial System from the Exploitation of Financial Centres and Offshore Facilities by Organised Crime* (the Euroshore report, 2000), a report commissioned by the European Commission; *Behind the Corporate Veil: Using Corporate Entities for Illicit Purposes* (2001), commissioned by the OECD; *Towards a Level Playing Field: Regulating Corporate Vehicles in Cross-Border Transactions* (2002), commissioned by the International Trade and Investment Organization and the Society of Trust and Estate Practitioners; *The Misuse of Corporate Vehicles* (2006), by the Financial Action Task Force (FATF); and *Money Laundering Using Trust*

and Company Service Providers on Money Laundering (2010), a report by the Caribbean Financial Action Task Force.

These reports, and the policy recommendations based on them, have placed the issue firmly on the international agenda and have contributed to the formulation of international standards on transparency of legal entities and arrangements. The FATF 40 Recommendations on Money Laundering (2003), which represent the international standard on this issue, note the importance of ensuring transparency of legal entities and arrangements and of identifying the beneficial owner in various places. According to Recommendations 5 and 12 on customer due diligence (CDD), financial institutions and other economic service providers[2] should be required to establish the identity of the beneficial owner of a legal person or arrangement. Recommendations 33 and 34 oblige countries to ensure that there is adequate, accurate, and timely information on the beneficial ownership and control of legal persons (33) and legal arrangements (34) and to ensure that this information can be obtained or accessed in a timely fashion by competent authorities. Assessments undertaken by FATF and other bodies of 159 countries show that the levels of compliance are very low, particularly with Recommendations 33 and 34 (see appendix A).[3]

This matter has continued to generate considerable debate. At their summit in Pittsburgh, United Sates, in September 2009, the G-20 leaders issued a statement calling on the FATF to "help detect and deter the proceeds of corruption by prioritizing work to strengthen standards on customer due diligence, beneficial ownership and transparency."[4] More recently, in April 2010, a group of leading prosecutors from around the world sent an open letter to the leaders of the G-20 requesting they address this issue as a matter of urgency.[5]

1.2 Objective of This Report

The objective of this report is to contribute to the international policy debate by providing evidence on (a) how corporate vehicles are misused to conceal the identity of their

2. "Economic service providers" or "service providers" is a working term used throughout this report. It encompasses the financial and designated nonfinancial service providers referenced in Recommendation 5 and Recommendation 12 of the FATF 40 Recommendations on money laundering. Absent clarifying or narrowing context, it is used as an umbrella term for the deposit-taking and investment banking institutions, corporate or trust creation and management professionals, and legal and accounting professionals who interact with corporate vehicle clients.

3. In fact, in more than 70 percent of the countries evaluated, the lack of a clear requirement to identify the beneficial owner was mentioned as a key factor justifying a less-than-compliant rating for Recommendation 5.

4. "Leaders' Statement, The Pittsburgh Summit, September 24–25, 2009," accessed at www.g20.org/documents/pittsburgh_summit_leaders_statement_250909.pdf (last accessed August 13, 2011).

5. See a copy of the letter urging the G-20 to call on the Financial Action Task Force to report back on specific actions it has taken to detect and deter the proceeds of corruption by prioritizing work to strengthen standards on customer due diligence, beneficial ownership, and transparency (http://www.globalwitness.org/media_library_detail.php/959/en/open_letter_to_heads_of_state_and_finance_minister).

beneficial owners and (b) the problems that banks, other service providers, and investigators face in attempting to obtain relevant information.

The most significant feature of this report is that its findings and conclusions are based on highly specific data gathered from a wide range of primary sources. These sources include court documents; interviews with investigators, financial institutions, service providers, and corporate registries; and the results of a solicitation exercise. But in providing information on the extent of this type of criminal behavior and the methods most often used by its perpetrators, the report aims to do more than simply raise awareness of the issue. Rather, its ultimate objective is to present policy recommendations for the consideration of authorities as they seek ways to deal with misuse of corporate vehicles within their jurisdictions. A comprehensive strategy at both national and international levels to address the weaknesses in legal and regulatory frameworks—with the aim of decreasing the vulnerability of corporate vehicles to misuse—could contribute toward improving the current situation. Our recommendations are summarized in the Executive Summary and are presented in greater detail in the report.

We choose our words carefully: we do not suggest that policy on its own can provide a solution to this problem. To do so would be to set oneself up for failure. Grand corruption is a criminal problem, and it always will require a response from law enforcement, and certainly, through sheer determination, creativity, and expertise, law enforcement has successfully investigated and prosecuted many cases involving the misuse of corporate vehicles. But even so, law enforcement cannot address this problem alone: a coordinated approach, from both policy and law enforcement perspectives, is required.

Addressing the challenge of identifying the beneficial ownership of corporate vehicles is a multifaceted endeavor. To take this into account, we have gathered data from a variety of sources, including court cases, interviews, and reviews of the activities of relevant institutions:

- ***Court Cases***
  Compilation and subsequent analysis of a database of 150 grand corruption investigations involving the misuse of corporate vehicles. The database identifies the types of illicit assets involved (roughly US$50 billion in total), the professional intermediaries and the jurisdictions involved, and the location of the bank accounts (where available). Analysis of actual cases helps to establish the facts and identifies areas where the genuine problems lie.

- ***Banks***
  An analysis examining how, in practice, 25 banks establish the identity of a beneficial owner, including the information and documents they obtain from their customers and the challenges they face in conducting their due diligence.

- ***Trust and Company Service Providers***
  A study of the extent to which, in practice, TCSPs conduct due diligence when establishing corporate vehicles.

- ***Registries***
  A review of the information collected and maintained by company registries in 40 jurisdictions.

- ***Investigators***
  An examination of the obstacles and challenges faced by investigators[6] in investigating the misuse of corporate vehicles and identifying their beneficial owner(s).

The methods used in the various research activities underlying this study are described in more detail in appendix B. This study makes no claim to assess the full extent of the problem—that would go far beyond its scope and would require different research methods. Instead, the study builds on expert observations and uses these observations to identify and analyze problems that merit the attention of policy makers.

1.3 How to Use This Report

In part 1 of this report, we have sketched the background of the misuse of corporate vehicles and outlined the objectives and scope of this study. The subsequent parts of this report deal with different aspects of the problem. Part 2 examines specific concerns about how we should understand the person hiding behind the corporate vehicle. Then, in part 3, we look at the types of corporate vehicles chosen to hide behind, as well as other strategies used to generate further opacity. Finally, part 4 considers the sources of information available to investigators tasked with uncovering the person hiding behind the corporate vehicle.

The diversity of topics addressed in this report means that at least some readers may encounter unfamiliar content. In that case, they may consult the information provided in the appendixes, which are useful to fill in any gaps in their knowledge needed for appropriate understanding of the report.

6. The term "investigators" used throughout the report encompasses a broad and diverse group of experts we consulted in the course of this study. They include investigators in the traditional sense, those who currently work or formerly worked in law enforcement agencies or other government investigative bodies, such as national anticorruption commissions and financial intelligence units. It also includes prosecutors, in recognition of the fact that, in some jurisdictions, it is prosecutors who lead investigations (or share responsibility for doing so with investigators). Forensic accountants and certified fraud examiners were consulted, as they play critical roles in financial crime investigations. Finally, civil practitioners in the field of international fraud and financial crimes also were consulted, including those with experience in successfully recovering stolen assets on behalf of their client governments or other victims.

Appendix A reviews compliance with FATF Recommendations 5, 12, 33, and 34 and provides an outline of the main issues. Appendix B describes the five component projects that helped to inform this report, including the Grand Corruption Database, Bank Beneficial Ownership, Trust and Company Service Provider, Registry, and Investigator Projects. Appendix C describes the corporate vehicles referred to in this study and Appendix D details ten grand corruption cases. Appendix E provides a detailed comparison of corporate vehicles in selected jurisdictions.