

**Update on the
Misuse of Corporate Vehicles Typologies Project
By
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The issue surrounding the misuse of corporate vehicles gained prominence follow the publication of the Organisation for Economic Co-operation and Development (OECD's) report ***Behind the Corporate Veil***. *“The Financial Stability Forum (FSF) asked the OECD in May 2000 to undertake the drafting of a report to develop mechanisms to reduce the vulnerability of corporate vehicle to misuse for illicit purposes. In particular, the FSF stressed the importance of ensuring that the authorities in each jurisdiction have the ability to share information on the beneficial ownership and control of corporate vehicles established in their jurisdiction.”* The OECD's report was published November 2001.

The International Trade and Investment Organisation (ITIO) and Society of Trust and Estate Practitioners (STEP) jointly commissioned a response to the OECD report. The response ***Towards a Level Playing Field*** provided empirical evidence that corporate service providers are better regulated in a number of non-OECD jurisdictions (including places like the BVI) than in OECD member countries.

Following the publication of the FATF revised Forty plus Nine Special Recommendations, the issue of illicit use of corporate entities has been taken up by the FATF because of a number of high profile corporate scandals.

In November 2005, the FATF held a series of typologies exercise in Brazil. Whilst the BVI was represented at 4 of the 5 typologies projects, the misuse of corporate vehicles project was of particular importance for the Commission. The BVI and two other Caribbean Financial Action Task Force (CFATF) member countries actively participated in this project.

The subject of the misuse of 'corporate vehicles' (defined for the purposes of the Typologies to include corporations, trusts, foundations, partnerships etc) by those engaged in money laundering or terrorist financing is an important but extensive one.

An essential element in the fight against money laundering and terrorist financing is to ‘know the customer’. The successful implementation of the FATF Forty plus Nine Recommendations rests in large part on the effectiveness with which Recommendation 5 on customer due diligence is complied with.

Recommendation 5 states that –

“The customer due diligence (CDD) measures to be taken are as follows:

- a) Identifying the customer and verifying that customer’s identity using reliable, independent source documents, data or information⁴.
- b) Identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner such that the financial institution is satisfied that it knows who the beneficial owner is. For legal persons and arrangements this should include financial institutions taking reasonable measures to understand the ownership and control structure of the customer.
- c) Obtaining information on the purpose and intended nature of the relationship.
- d) Conducting ongoing due diligence on the business relationship and scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with the institution’s knowledge of the customer, their business and risk profile, including, where necessary, the source of the funds.”

A major problem presented through the use of corporate vehicles is gaining information on the ultimate beneficial owner, the source of funds, and the purpose for which the corporate vehicle is being used. This is particularly so when corporate vehicles (e.g. shell corporations) can be created and dissolved in some jurisdictions with few questions asked and few records kept.

⁴ Reliable, independent source documents, data or information will hereafter be referred to as “identification data”.

There are three key elements that were considered as part of the typologies project –

- the creation of corporate vehicles;
- the administration of corporate vehicles;
- the use of corporate vehicles.

However, it was suggested that the key to dealing with the misuse of corporate vehicles is to ensure that in the creation of corporate vehicles there is adequate information provided about beneficial ownership, purpose, source of funds etc; that there is effective access to such information; and that the information can be shared between jurisdictions and between regulatory/law enforcement authorities. To quote from the *Savona Report*, financed by the European Commission, entitled ‘Study of the Regulation and its Implementation, in the EU Member States, that obstruct Anti-Money Laundering International Cooperation’ -

“The incorporation is the initial phase in the ‘life’ of a legal and non-legal structure, in which the structure itself is established through a series of acts aimed at making it operational. The relevance of this thematic area for anti-money laundering international cooperation lies in the fact that lack of checks during the incorporation phase results in greater opacity in company law, which might obstruct the acquisition of information regarding the physical persons participating in its establishment. The less opaque (or the more transparent) the process of incorporation is, the more available should be the information concerning the incorporation of the structures. This facilitates the investigation of their activities and of the persons controlling them, both at the national and international levels.

The aim of the 2005 typologies exercise was to bring practitioners and policy makers together to discuss the work conducted by typologies project teams since June 2005. The aim was to bring together as much expertise and case material as possible to make considerable progress on each of the issues.

Issues:

Criminals have responded to the defences put in place by financial institutions and have sought to use corporate vehicles, and those who provide trust and company services, to disguise and convert their proceeds of crime before entering the traditional financial system.

Trust and Company Service (TCS) activities are sought out by organised crime groups or the individual criminal, keen to profit from the expertise available in setting up schemes to help them launder criminal proceeds. This expertise will include advice on the best corporate vehicles or jurisdictions to use for such schemes. Of particular concern is the ease with which shell corporations can be created and dissolved in some jurisdictions which allows these corporations to be used by money launderers as well as high risk customers such as politically exposed persons (PEPs) to conceal the sources of funds and their ownership.

These are areas where international standards have yet to be clearly defined and where there are potentially important lessons to be learned from a typologies exercise.

Resources Required:

Those with the skills and expertise required to perform the tasks identified below will include individuals from FATF jurisdictions, observer organisations and FSRBs who have skills/experience in the process of corporate vehicle formation and administration, and in particular the formation and administration of shell companies, and in regulatory action and law enforcement in this field. Law enforcement investigators and analysts, as well as other representatives of operational services, who have recently dealt with cases involving the misuse of corporate vehicles, were particularly required to participate. It was also important that there were experts from a sufficiently broad range of countries, including common law and civil law jurisdictions, countries from outside the FATF and countries with a substantial TCSP-industry and/or offshore sector.

Identification and Description

The project group initially relied on information obtained from a questionnaire distributed to FATF members and FSRBs. The information obtained enabled the group to focus on further lines of enquiry and research, as necessary.

Private Sector Consultation

The project group consulted with private sector organisations that have experience of the issues being addressed (e.g. the Society of Trust and Estate Practitioners - STEP).

Overall the scope and complexity of the work requires the presence of specialised experience in the oversight and monitoring of the formation and administration of corporate vehicles, and law enforcement experts engaged in the investigation and prosecution of those engaged in the misuse of corporate vehicles.

It was expected that the exercise overall will be completed within the twelve months.

Project Objectives:

The project sought to identify the areas of vulnerability, and the evidence of malpractice with particular reference to the misuse of corporate vehicles on which the OECD has reported. It was also point to how differences between the national systems for establishing and using corporate vehicles may be exploited, and what steps have been taken by jurisdictions to address this threat.

The project also sought to provide answers to a number of questions including –

- what are the differences in the recognition and treatment of corporate vehicles between jurisdictions;

- how is the formation and administration of corporate vehicles overseen, monitored, investigated and controlled;
- what are the areas of greatest misuse of legal persons and arrangements and what action is taken in different countries to combat that misuse;
- what are the main barriers/difficulties faced by jurisdictions in the effective implementation of Recommendations 33 and 34;
- what lessons can be learnt from the experience of jurisdictions to date in dealing with the misuse of corporate vehicles.

Products:

The project will essentially have two products –

1. A workshop on the misuse of corporate vehicles, which took place during the joint FATF/GAFISUD experts meeting in November 2005. A paper was prepared for the workshop based on the response to the questionnaire distributed to FATF members and FSRBs. This required that the answers to the questionnaire should be received no later than late September/early October.
2. A report on the conclusions of the project team. This report covered the money laundering vulnerabilities identified by the research and would include descriptions of the various typologies supported by relevant case studies as well as issues for consideration regarding the prevention of such misuse. The findings and policy considerations from the report could later become the basis for the future work in the FATF to develop further guidance regarding implementation of Recommendations 5, 6, 8-11, 33 and 34. The most recent draft of the report was received recently and expected to be approved by member of the working group by the end of April 2006 so that it can be adopted by WGTYP and FATF Plenary in June 2006.

