

U.S. DEPARTMENT OF THE TREASURY

Press Center



Written Testimony of Assistant Secretary Daniel L. Glaser before the Senate Committee on the Judiciary, Subcommittee on Crime and Terrorism

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“Combating International Organized Crime: Evaluating Current Authorities, Tools, and Resources”

Introduction

Chairman Whitehouse, Ranking Member Kyl, and distinguished members of this Committee, thank you for the opportunity to appear before you today to discuss the Treasury Department's contribution to the Obama Administration's July 2011 integrated strategy to address the threat posed by transnational organized crime (TOC).

In early 2010, the United States completed a comprehensive assessment of transnational organized crime – the first since 1995 – which concluded that TOC networks have expanded in scope and sophistication, engage in a range of illicit activities, and are taking advantage of the increasingly integrated international financial system. Among the most startling conclusions of that assessment is that these groups' growing infiltration of legitimate commerce and economic activity fundamentally threatens U.S. economic interests at home and abroad and could cause significant damage to the world financial system through subversion, exploitation, and distortion of legitimate markets and economic activity. Terrorists and insurgents increasingly are turning to crime and criminal networks for funding and logistics. Criminal networks are increasingly exploiting vulnerabilities in information technology and are involved in cyber crime. The result is a convergence of complex, volatile, and destabilizing threats to U.S. national security.

To combat this growing threat to U.S. and international security, the Obama Administration announced this past July a national Strategy to Combat Transnational Organized Crime (the “Strategy”). The Strategy lays out five strategic objectives, 56 priority actions, and new and innovative capabilities and tools to mitigate the threat.

President Obama's opening message to the Strategy makes clear that despite a long and successful history of dismantling criminal organizations, not all of our capabilities have kept pace with the expansion of 21st century transnational criminal threats. Shortly before the White House announced the Strategy, President Obama signed Executive Order (E.O.) 13581, thereby providing the Treasury Department a new tool and authority to target the financial underpinnings of the world's most powerful transnational criminal organizations.

This Executive Order supplements an array of the Treasury Department's tools and capabilities that can be used to target TCOs and safeguard our financial system from abuse. Our targeting capabilities include financial sanctions, the imposition of special regulatory measures and requirements, and engagement with at-risk financial institutions and jurisdictions.

In my testimony, I will focus on the Treasury Department's efforts to implement E.O. 13581, as well as the other authorities we have available to use in implementing the Strategy, such as Section 311 of the USA PATRIOT Act. I will also discuss our ongoing work to promote financial transparency domestically and abroad, and the importance of transparency in mitigating the threats posed by TOC and other forms of illicit finance. In particular, I will address the abuse of legal entities as a systemic vulnerability to TOC networks and a chronic challenge to achieving financial transparency. Addressing this vulnerability requires a broad approach, including the adoption of legislation to facilitate the availability of meaningful beneficial ownership information for companies created within the United States.

Targeted Financial Measures

Historically, economic sanctions have been the Treasury Department's primary tool to target the financial networks of illicit actors, including drug trafficking organizations. As these organizations generate hundreds of millions of dollars per year that are often placed in or moved through the international financial system, we have used targeted financial measures to restrict their access to the U.S. financial system. One such authority specifically designed to target drug trafficking organizations is the Foreign Narcotics Kingpin Designation Act (the “Kingpin Act”). Since June 2000, over 1000 individuals and entities have been designated under the Kingpin Act, resulting in the blocking of millions of dollars in financial assets in the United States. The Kingpin Act provided the flexibility necessary to continue targeting Latin American drug cartels over an extended period of time as the drug trade under the control of Colombian cartels gave way to a more segmented market progressively dominated by Mexican TCOs and shifted geographically from Colombia to Mexico. Recognizing the success of measures such as the Kingpin Act, the Strategy proposes that a similar method, with the flexibility to adapt to varying situations, be used to target TOC.

Executive Order 13581

While the Strategy draws from a broad range of tools and authorities to combat the threat posed by TCOs both domestically and abroad, targeted financial sanctions will be employed to help protect the U.S. financial system from these groups. On July 24, 2011, President Obama signed E.O. 13581, “Blocking Property of Transnational Criminal Organizations,” imposing sanctions against significant TCOs that threaten the U.S. national security, foreign policy, or economy and granting the Treasury Department the authority to address TCOs under the International Emergency Economic Powers Act. For the first time, the President recognizes that TOC warrants the declaration of a national emergency and the imposition of economic sanctions.

In the annex of E.O. 13581, the President identified and imposed sanctions on four significant TCOs: the Brothers' Circle (a.k.a. Moscow Center), the Camorra, the Yakuza, and Los Zetas.

The four groups in the annex were chosen because they are large, sophisticated, multi-national organizations engaged in a wide variety of dangerous criminal enterprises ranging from narcotics trafficking, human trafficking, weapons trafficking, murder, complex financial fraud, and intellectual property theft that threaten the U.S. national security, foreign policy, and economy. Let me provide you additional background on these four organizations.

- First, the Brothers' Circle is a multi-ethnic criminal group composed of leaders and senior members of several Eurasian criminal groups largely based in countries of the former Soviet Union, but extending to the Middle East, Africa, and Latin America. The Brothers' Circle serves as a coordinating body for these criminal networks, including mediating disputes between the individual criminal networks and directing global criminal activity.
- The Camorra, Italy's largest organized crime group, is a loose collection of allied and competing local clans in the province of Naples and the Campania region of Italy. The Camorra operates internationally and is involved in serious criminal activity such as counterfeiting and narcotics trafficking. The Camorra may earn more than 10 percent of its

roughly \$25 billion annual profit through the sale of counterfeit and pirated goods – such as luxury clothing, power tools, CDs, DVDs, and software.

- The third group, the Yakuza, comprises the major Japanese organized crime syndicates, and had more than an estimated 80,000 members in 2008. The Yakuza derives a majority of its profits from the drug trade, but is also involved in weapons trafficking, and nearly all aspects of human trafficking and sexual exploitation. The Yakuza is also heavily involved in white-collar crime, often using front companies to hide illicit proceeds within legitimate industries, including construction, real estate, and finance.
- Lastly, Los Zetas, formerly the armed wing of the Gulf Cartel, is an extremely violent transnational group based primarily in Mexico. According to press reporting, the organization is estimated to have thousands of members collectively in Mexico, Central America, and the United States and is specifically responsible for the safe passage of large quantities of illegal narcotics, including cocaine, methamphetamine, heroin, and marijuana from or through Mexico and eventually into the United States. In addition to drug trafficking, Los Zetas is involved in extortion, money laundering, intellectual property theft, and human smuggling. President Obama previously identified Los Zetas as a significant foreign narcotics trafficker under the Kingpin Act in 2009 (its former parent organization, the Gulf Cartel, was similarly identified in 2007). Since that time, 58 individuals and entities have been designated as associates of the two groups. Its listing under E.O. 13581 demonstrates that Los Zetas has expanded its illicit activities beyond drug trafficking.

The President's strategy draws from a broad range of tools and authorities to attack the threat posed by these organizations. As part of this broad strategy, sanctions will complement U.S. law enforcement authorities in the fight against transnational criminal organizations, as they have the in the case of Kingpin Act designations. The Treasury Department intends to build on our close cooperation with the U.S. Department of Justice and other United States Government agencies to identify key nodes of operation for coordinated action in disrupting TOC networks.

In order to implement E.O. 13581 effectively, the Treasury Department has scoped out a series of actions that Treasury will undertake simultaneously in furtherance of the President's Strategy. These actions include: pursuing derivative designations of the four groups, identifying additional transnational criminal organizations, liaising with key foreign partners, and conducting outreach to the private sector.

The Treasury Department, in partnership with law enforcement and Intelligence Community counterparts, will attempt to map out the criminal networks of these groups in order to pursue derivative designations aggressively. As affiliates of the groups do not make transactions under the group name, it is essential to designate the groups' leadership, operatives, associated companies and businesses, and financial facilitators. Designating such individuals and entities owned or controlled by, or providing material support to, these organizations will increase the financial pressure on their networks and affect their ability to conduct financial transactions.

In addition to pursuing derivative designations of groups currently listed in the annex of the E.O., the Treasury Department will work with our interagency partners to identify additional TCOs that pose a threat to the national security, foreign policy, and economy of the U.S. for potential designation.

We will work with like-minded foreign partners to build an international coalition to combat TOC more broadly. Many countries in Europe and Asia have recognized the TCO threat long ago and have taken domestic steps to mitigate the threat. We believe they are natural partners in this initiative. We have already begun outreach to strategic allies to raise awareness of our authorities, to discuss potential information sharing opportunities, and build support for an international effort against TOC. Under Secretary David Cohen was in Europe last week, where he raised TOC as a priority issue with his counterparts there. I will travel to Moscow next week, where I will also raise this as an area where we hope to expand our cooperation with our Russian counterparts.

We will make outreach to the U.S. and international financial community an essential component of our efforts. Our goal will be to ensure that banks understand the risks of doing business with TCOs and are taking appropriate due diligence measures. Our partnership with the private sector on other sanctions programs has amplified the effects of our actions. Our aim, therefore, is to replicate the success of that partnership in order to make it more difficult for these illicit groups to abuse the U.S. and international financial system.

While enacting targeted financial measures against these four groups is our first priority, the Treasury Department is also investigating whether it would be appropriate to use other restrictive measures against TOC.

Section 311 of the USA PATRIOT Act

The Administration's Strategy calls for use of Section 311 of the USA PATRIOT Act, in addition to the new Executive Order, to combat TOC. This powerful tool allows the Treasury Department to take action to protect the U.S. financial system from specific threats. It authorizes the Treasury Department to identify a foreign jurisdiction, foreign financial institution, type of account or class of transactions as a primary money laundering concern, and impose any one or combination of a range of special measures that U.S. financial institutions must take to protect against illicit financing risks associated with the subject of the action. In practical terms, Section 311, where appropriate, enables the Treasury Department to cut off foreign financial institutions from the U.S. financial system on the grounds that they facilitate transnational organized crime or other illicit activity.

For example, in February 2011, the Treasury Department identified the Beirut-based Lebanese Canadian Bank (LCB) as a financial institution of primary money laundering concern for its role in facilitating the activities of an international narcotics trafficking and money laundering network operating across five continents. The LCB action was the product of close coordination and cooperation with the Drug Enforcement Administration. Similarly, in 2005, the Treasury Department identified two Latvian banks (VEF Bank and Multibanka) under Section 311 because they were being used to facilitate or promote money laundering and other financial crimes.

Several of our Section 311 actions against foreign banks have highlighted the role of shell companies in illicit activity. The Multibanka and VEF actions I mention above noted that the banks were involved in transferring funds involving illicit activity by multiple shell companies with no legitimate business purposes. Further, the Section 311 findings against Macau's Banco Delta Asia (BDA) and Infobank in Belarus alerted financial institutions around the world to the role that front companies play in furtherance of a wide array of illicit conduct. In these actions, the Treasury Department exposed the fact that BDA was providing services to North Korean front companies, and Infobank was involved in laundering improper fees derived from the United Nations' Oil for Food Program via shell companies. These findings illustrate the need for enhanced financial transparency, which is also a component of the President's Strategy.

Financial Transparency

The success of our efforts to combat TOC networks through targeted action, including through the application of E.O. 13581, relies on our ongoing work to promote a transparent global financial system. The President's Strategy notes that such transparency is critical to law enforcement's efforts to combat TOC. Enhanced transparency also enables financial institutions, law enforcement and other relevant authorities to implement and enforce the targeted measures described above. More broadly, financial transparency is the cornerstone of our efforts to protect the financial system from abuse. It is the foundation of virtually all of our efforts and successes to date in countering illicit finance, from an increasing reliance on targeted financial measures in addressing global security threats to supporting international efforts to strengthen global anti-money laundering/combating the financing of terrorism (AML/CFT) standards.

The growth and increasing sophistication of the international financial system in recent years has enabled TCOs and other illicit actors to move money, hide assets, and conduct transactions anywhere in the world, exposing financial centers to exploitation and abuse in an unprecedented way. Our success in combating these illicit actors going forward will depend critically on our continued efforts to increase transparency across the international financial system. By requiring the collection of key information regarding the nature of transactions and the relevant transacting parties and beneficial owners, a transparent financial system will compel some criminals to avoid transactions altogether and pose significant obstacles for others who nevertheless seek to move funds in support of their illicit activities. And if, despite our best efforts, these individuals and entities still manage to access the financial system, the information collected by financial institutions enables law enforcement to trace the money and track down criminals and other bad actors.

The stakes are high. Just as financial transparency has helped us combat WMD proliferators, corrupt kleptocrats, and terrorist financiers, it also serves as a powerful weapon against transnational organized criminal networks. Where transnational criminals seek to exploit complexity and opacity, we must seek to untangle and bring clarity. As we enhance financial transparency, we diminish their ability to commit crime.

How we achieve financial transparency

In the broadest sense, our efforts to promote a transparent financial system encompass ongoing work to strengthen financial transparency across the formal financial sector and expand such transparency to the informal sectors, such as hawala and other informal remittance systems. This has not been limited to the U.S. financial system, but has included efforts to strengthen global standards and facilitate implementation of effective AML/CFT regimes in countries around the world. Working through various multilateral bodies, we have promoted transparency throughout the international financial system and have integrated robust systemic AML/CFT safeguards into the international financial architecture. This global AML/CFT architecture has enabled us to systematically identify and address illicit financing vulnerabilities in the international financial system on an ongoing basis. I would like to take a moment to discuss some of these successes in more detail.

Developing a Global AML/CFT Framework

The global threat of transnational criminal organizations and the increasing interdependence of the international financial system require a global approach to combating transnational organized crime. The Treasury Department's Office of Terrorism and Financial Intelligence (TFI) has worked with its interagency and international partners to help create a global AML/CFT framework as a foundation for taking action against criminal networks and for closing down vulnerabilities that they exploit. This framework consists of several intergovernmental organizations that collectively develop, assess and facilitate jurisdictional implementation of measures that are essential to combating various forms of illicit finance, including transnational organized crime. Such organizations include:

- **Financial Action Task Force (FATF)** – The FATF is the premier international policy-making and standard-setting body in the international effort against terrorist financing, money laundering, and other illicit finance. Established by the G-7 Economic Summit in 1989, the FATF is an intergovernmental body that has grown to include 36 members, representing most major financial centers in all parts of the globe. The FATF sets global AML/CFT standards, promotes and assesses compliance with those standards, and, when necessary, promotes compliance through diplomatic pressure and coordination of economic countermeasures through its member governments. Through a combination of technical expertise and political and economic strength, the FATF has been unique among international bodies in its ability to take strong, effective multilateral action to prompt positive change in strengthening jurisdictional AML/CFT regimes worldwide. My office, Terrorist Financing and Financial Crimes (TFFC), manages the FATF program for the U.S. government and heads the interagency U.S. delegation to the FATF. The U.S. delegation to the FATF includes the Departments of State, Justice, and Homeland Security; the Board of Governors of the Federal Reserve System; the Securities and Exchange Commission; other federal financial regulatory agencies; and federal law enforcement agencies.
- **FATF-Style Regional Bodies (FSRBs)** – Through the FATF, TFI and its interagency and international partners have also supported the creation and development of eight independent FSRBs that serve as leaders in their respective regions for advancing AML/CFT policy, including by conducting periodic compliance assessments of member jurisdictions against the FATF's AML/CFT standards. In conjunction with the FATF, these bodies are intended to establish a global framework for ensuring the adoption and implementation of the FATF standards.
- **IMF / World Bank** – The World Bank and International Monetary Fund (IMF) have become strong partners of the FATF and the Treasury Department in assessing global compliance with international AML/CFT standards, and providing high-quality technical assistance. In 2003, the World Bank and IMF officially recognized the FATF Recommendations as one of the 12 Key International Standards and Codes. Since then, the FATF, the World Bank and IMF worked together to develop a joint standardized methodology for assessing countries against the FATF Recommendations. Today, all formal World Bank and IMF Financial Sector Assessment Programs (FSAPs) must contain a full AML/CFT component, and the World Bank, IMF, and the FATF are coordinating to ensure that virtually every country in the world is subject to an AML/CFT assessment using the joint methodology.
- **Group of 20** – The Group of 20 Ministers have endorsed the important work of the FATF in combating money laundering and terrorist financing, including by calling for the FATF to enhance the transparency of the international financial system and to publicly identify countries of concern for money laundering and terrorist financing. TFI works with AML/CFT experts in the G-20 countries to adequately respond to the G-20 calls and facilitate multilateral action in protecting the international financial system from abuse by illicit actors.

To facilitate compliance with global AML/CFT standards, the G-20 has called upon the FATF to continue to publicly identify jurisdictions that fail to meet the international standards and may pose a risk to the international financial system. I have had the privilege of serving as co-chair of the working group within the FATF that oversees this process. Jurisdictions that have been identified by this process must commit to an Action Plan of ambitious reforms. If the reform timelines specified in the Action Plans are not met, the FATF will issue increasingly strong public warnings, potentially culminating in a specific call for regulatory countermeasures from member countries. In response to this process, numerous jurisdictions have passed important AML/CFT legislation, which likely would not have happened so quickly without the encouragement from this FATF process.

Abuse of legal entities as a fundamental challenge to financial transparency

Despite our ongoing efforts and longstanding commitment to promote a transparent global financial system and to combat money laundering and illicit finance, federal law enforcement agencies and other information sources indicate that hundreds of billions of dollars of illicit proceeds are generated each year in the United States from criminal offenses stemming from illicit drug sales, various forms of financial fraud and tax evasion. The challenges in identifying and recovering proceeds of crime laundered through the U.S. and global financial system may be attributed in large part to ongoing and substantial criminal abuse of legal entities and a lack of insight into the beneficial ownership of those legal entities. These challenges, which are applicable to all manner of financial crime perpetrated by TOC networks, have been exhaustively described in various testimonies and publications. The following provide some examples:

- In 2007, the Departments of Justice, Homeland Security and the Treasury jointly issued the National Money Laundering Strategy (2007 Strategy), which in part, identifies current and emerging trends in money laundering, as well as specific vulnerabilities. The 2007 Strategy specifically emphasizes the risks associated with shell companies and trusts, noting that the use of these entities for illicit purposes has become increasingly popular with criminal actors because of the "ability to hide ownership and mask financial details." The 2007 Strategy re-iterates the long-standing concern regarding shell entities by the international community, citing a 1998 statement by the United Nations: "...the principal forms of abuse of secrecy have shifted from individual bank accounts to corporate bank accounts and then to trust and other corporate forms that can be purchased readily without even the modest initial and ongoing due diligence that is exercised in the banking sector." As asserted by a representative of the Asset Forfeiture and Money Laundering Section of the United States Department of Justice (AFMLS), law enforcement faces "considerable difficulties when investigating U.S. shell corporations due to the lack of beneficial ownership information available in the United States."
- Further, in 2006, Congress directed the Government Accountability Office (GAO) to examine vulnerabilities associated with company formation in the United States. The report cites examples of abuse of the financial system by illicit shell company activities and reports that federal law enforcement officials are "concerned that criminals are increasingly using U.S. shell companies to conceal their identity and illicit activities," and that shell companies are also a way of providing access to the U.S. financial system to offshore illicit actors via correspondent account relationships at U.S. banks.

The abuse of legal entities is an international problem; both foreign and domestic legal entities can be used for illicit purposes. Viktor Bout, an international arms merchant who was designated by the Treasury Department's Office of Foreign Asset Control (OFAC), used U.S. shell companies to mask his ownership and facilitate his illegal arms trafficking activities. Law enforcement believes that the Sinaloa Cartel, one of the major Mexican drug trafficking organizations, uses both U.S. and Colombian shell companies to launder drug proceeds. Additionally, illicit actors use foreign shell companies to mask the involvement of designated persons and circumvent U.S. sanctions programs relating to Iran and North Korea.

Treasury's 3-pronged approach

Addressing the ongoing abuse of legal entities to perpetrate all manner of financial crime requires a broad approach. Accordingly, the Treasury Department has developed a strategy on beneficial ownership that has three independent, but interrelated, objectives.

First, we are working to enhance the availability of beneficial ownership information to law enforcement regarding legal entities created in the United States. Together with our interagency partners and with Congress – including, in particular, Senator Levin, who has been a leader in this area – we are working to address this issue through legislation. These efforts, guided by the President's Strategy, also aim to ensure that legal entities can produce a clear statement of their beneficial ownership to any financial institution that is seeking such information as an element of their customer due diligence. Increased transparency in company formation in the U.S. will also improve law enforcement's ability to respond to Mutual Legal Assistance Treaty (MLAT) requests from foreign partners.

Second, we plan to clarify and strengthen customer due diligence (CDD) requirements for financial institutions with respect to the beneficial ownership of legal entity account holders. In March 2010, the Treasury Department, together with the functional financial regulators, issued Guidance to clarify existing regulatory expectations for obtaining beneficial ownership information for certain accounts and customer relationships. We are also working with the regulatory and law enforcement communities, and consulting with the private sector, to determine how such due diligence requirements can be further clarified and strengthened as necessary through rulemaking or otherwise.

Third, we are working with our international partners in the FATF to clarify and facilitate the global implementation of international standards regarding beneficial ownership. As with our domestic efforts, our beneficial ownership work in the FATF focuses on both issues of legal entity formation within jurisdictions, as well as customer due diligence by financial institutions. We continue to work closely within the FATF and support the current ongoing revision to the FATF recommendations in this regard. The FATF hopes to have a new international standard adopted by February 2012. It is particularly important that we do not neglect this international effort as we move forward in addressing the issue of beneficial ownership in the United States. A unilateral solution is an incomplete and ineffective solution. Without widespread global implementation, even if CDD practices at our domestic institutions forbid dealing directly with a particular customer due to beneficial ownership risk, this same customer may nevertheless seek to access the financial system through foreign correspondent channels.

Conclusion

The President's Strategy calls upon the Treasury Department to deploy our targeted tools and to enhance financial transparency in order to close vulnerabilities, disrupt and dismantle illicit financial networks, and apply pressure on transnational criminal organizations. We are committed to disrupting TOC infiltration of the global economy to better protect the financial system, including by freezing the assets of criminal networks under our new sanctions authorities. At the same time, the United States remains intent on improving the transparency of the international financial system, which will benefit our efforts to combat all manner of illicit finance, including transnational organized crime.