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The Honorable Joseph Lieberman
Chairman
Committee on Homeland Security and Governmental Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing on behalf of the American Bar Association regarding the June 18, 2009 hearing on S. 569, the "Incorporation Transparency and Law Enforcement Assistance Act," and respectfully request that you include this letter in the record of the hearing.

The ABA supports all reasonable and necessary domestic and international efforts to combat money laundering, tax evasion, and terrorist financing. However, the ABA opposes enactment of S. 569. Enclosed please find ABA Resolutions 300 (August 2008) and 104 (February 2003), which further outline the ABA's opposition to S. 569 specifically, as well as to any legislation that purports to impose government-mandated suspicious activity reporting (SAR) obligations on the legal profession.

With respect to S. 569, the ABA is specifically concerned with two aspects: the federal mandates regulating state incorporation practices and the creation of a new group of "financial institutions" known as "formation agents" that could include lawyers. The ABA has, ever since the passage of Resolution 104 in 2003, consistently objected to government-mandated reporting obligations for the legal profession, where the reporting would be triggered by suspicion. The Association also reiterated its concerns regarding SAR requirements in Resolution 300, passed in August 2008.

The ABA is concerned that S. 569 would create new federal mandates and regulation of state incorporation practices. The legislation requires states to maintain beneficial ownership information; such information must be obtained, kept current, and made available to law enforcement authorities by the states upon request or subpoena. The ABA recognizes the need for improvement in company formation processes and increased visibility of persons forming nonpublic entities in the United States, but believes that federal legislation regulating this aspect of state incorporation practice is premature and is not the most effective means for addressing the threat of money laundering and terrorist activities in the U.S.

The Permanent Subcommittee on Investigations, through a series of hearings and investigations into tax abuse havens, and the Financial Action Task Force's (FATF) mutual evaluation of the United States have both expressed strong concerns that the U.S. company

formation process is at risk for exploitation by money launderers, tax evaders and terrorist financiers. As the ABA understands the problem identified by S. 569 and by FATF's mutual evaluation, law enforcement often is unable to locate the beneficial owners of privately held entities. Consequently, money laundering, tax evasion, and terrorist financing investigations are difficult to resolve, and the U.S. financial sector is at a heightened risk for abuse. However, S. 569 would impose undue burdens on state authorities and legitimate businesses at a time when the U.S. financial system and the domestic economy are under severe stress.

Despite objections to S. 569, the ABA is supportive of efforts to combat money laundering that do not infringe upon state sovereignty. Alternatives such as the Uniform Law Enforcement Access to Entity Information Act (Uniform Act) are being developed; this legislation holds the potential of providing law enforcement with the necessary information identifying the record owners and key officers of non-publicly traded entities formed under state law. While the ABA has not formally endorsed the Uniform Act, we believe that effective state laws and proposals like the Uniform Act could obviate the need for federal regulation of business entities while still meeting the requirements of FATF's Recommendation 33 (requiring countries to take measures to prevent the unlawful use of legal persons by money launderers).

In addition to our concerns about federal encroachment on states, the ABA also objects to Section 4 of S. 569. Section 4 would establish a new class of "financial institutions" under U.S. anti-money laundering law, covering "any person involved in forming a corporation, limited liability company, partnership, trust, or other legal entity" (formation agents). These formation agents would then be required to adopt certain enhanced anti-money laundering compliance mechanisms, much like U.S. banks have done, in order to detect possible money laundering activities in the formation of entities. While not explicit on its face, the definition of formation agents would appear to include lawyers involved in establishing entities. This legislation would therefore, for the first time, impose new, enhanced, anti-money laundering compliance requirements on the legal profession and would treat lawyers as if they were banks. This treatment is not warranted, nor does it make sense in light of the obvious distinctions between large financial institutions, the resources at their disposal, and their handling of money transactions, as compared to solo practitioners and law firms.

Moreover, designation of formation agents as financial institutions could potentially impose SAR requirements on the legal profession. The Treasury Department, pursuant to S. 569, could have the authority to impose such requirements on lawyers. Government-mandated SAR requirements could erode the attorney-client privilege and create conflicts between lawyers and their clients. A SAR requirement could also alter the client-lawyer relationship, as lawyers would no longer be acting independently of the state and in the best interests of their clients. These requirements could conflict with ethical obligations of lawyers under state confidentiality laws and could create inherent conflicts between lawyers and their clients; that is, lawyers could be acting as informants under pain of criminal prosecution (for failure to file a SAR), and would therefore be required to place their own interests ahead of their clients. Lawyers also would be prohibited from informing their clients of any such reports, creating an even more untenable conflict situation. Therefore, the ABA opposes imposing federally mandated SAR obligations on the legal profession. We have voiced these

objections to the Department of Justice, the Department of the Treasury, and FATF. The concerns underlying the ABA position are shared by legal professionals around the world. Indeed, these types of concerns were at the heart of litigation in Canada successfully challenging the imposition of reporting requirements on Canadian lawyers.

At the same time, the ABA has been working diligently to enhance the ability of legal professionals to identify and avoid illicit money laundering activities. In coordination with the U.S. Treasury Department, FATF, and legal professionals throughout the world, the ABA is educating members of the legal profession on anti-money laundering and counter-terrorist financing compliance. FATF has been actively collaborating with specially designated non-financial businesses and professions, including lawyers, to develop a risk-based system to further minimize the risk that lawyers and other professionals would be used unwittingly by unscrupulous clients to launder illegally obtained money. The ABA and members of other U.S. legal professional associations, along with our counterparts in the United Kingdom and elsewhere, participated extensively in this effort, attending numerous meetings with FATF officials and assisting in the preparation of the draft guidance on client due diligence to avoid money laundering and terrorist financing risks. The FATF adopted and issued this guidance in October 2008. Through the efforts of members of the ABA Task Force on Gatekeeper Regulation and the Profession, as well as others in the ABA, the American College of Trust and Estate Counsel, the American College of Real Estate Lawyers, the American College of Mortgage Attorneys, and other professional organizations in the U.S., additional voluntary good practices guidance on client due diligence is being prepared in consultation with members of the U.S. Department of the Treasury. Members of the ABA active in this area continue to disseminate education material to the profession at large. (See, e.g., Kevin Shepherd, "Guardians at the Gate: The Gatekeeper Initiative and the Risk Based Approach for Transactional Lawyers," 43 Real Property, Trust and Estate Law Journal, no. 2 (Winter 2009).) The ABA will continue to be active in this area and is working to enhance anti-money laundering compliance awareness within the legal profession.

The American Bar Association appreciates the Committee's efforts to combat money laundering and terrorist financing activity. While opposed to premature federal legislation, the ABA will continue to support state efforts countering these illegal activities in ways that minimize the impact on our economy and state regulators. We look forward to working with you on developing a comprehensive solution that addresses the mutual objectives of all concerned.

Sincerely,

A handwritten signature in black ink, appearing to read "Thomas M. Susman", with a long horizontal flourish extending to the right.

Thomas M. Susman

Enclosures

cc: Members of Homeland Security and Governmental Affairs Committee