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November 27, 2017

The Honorable Jeb Hensarling  
Chairman  
Committee on Financial Services  
U.S. House of Representatives  
Washington, D.C. 20515

The Honorable Maxine Waters  
Ranking Member  
Committee on Financial Services  
U.S. House of Representatives  
Washington, D.C. 20515

Re: Joint Subcommittee Hearing on H.R. \_\_\_\_, the “Counter Terrorism and Illicit Finance Act”  
and Concerns Regarding Section 9 (“Transparent Incorporation Practices”)

Dear Chairman Hensarling and Ranking Member Waters:

On behalf of the American Bar Association (ABA), which has more than 400,000 members, I write to express our concerns regarding key provisions in the draft “Counter Terrorism and Illicit Finance Act” that would impose burdensome and intrusive regulations on millions of small businesses and their lawyers. In particular, the ABA opposes Section 9 of the bill, which would require small corporations and limited liability companies (LLCs) and many of their lawyers to submit extensive information about the companies’ “beneficial owners” to the Treasury Department’s Financial Crimes Enforcement Network (FinCEN) and that would require FinCEN to disclose the information to many other federal and foreign governmental agencies and financial institutions upon request.

We ask that this letter be included in the record of the joint hearing on “Legislative Proposals to Counter Terrorism and Illicit Finance” that the Subcommittees on Financial Institutions & Consumer Credit and Terrorism & Illicit Finance have scheduled for November 29.

The ABA has worked diligently for years with the legal community, federal law enforcement authorities, international stakeholders, and states to advance reforms to combat money laundering and terrorist financing. Indeed, the ABA supports reasonable and necessary domestic and international measures to fight these illicit activities, and we commend the sponsors of the draft bill for their efforts in this regard. However, the ABA opposes the proposed regulatory approach set forth in Section 9 (“Transparent Incorporation Practices”) of the bill for several important reasons.

First, the ABA opposes these provisions in the bill because they would impose burdensome, costly, and unworkable new regulatory burdens on small businesses and their lawyers.

Section 9 of the bill would require millions of small businesses to disclose their detailed beneficial ownership information to FinCEN and then update that information continuously during the lifespan of those businesses. Failure to submit this information or to update it within 60 days of any change—regardless of when actual knowledge of the change occurs—could subject the businesses to harsh civil and criminal penalties, including stiff fines and prison sentences, for essentially paperwork violations. The bill would also require FinCEN to maintain the sensitive beneficial

ownership information in a massive database—thus subjecting it to possible cyberattacks—and to disclose it to any federal agency in response to a criminal subpoena or to any foreign law enforcement agency if certain conditions are met.

Many lawyers and law firms that help clients to form companies could also be subject to these burdensome disclosure and recordkeeping requirements—and to the bill’s severe criminal penalties for non-compliance—because many of the bill’s requirements apply to any “applicant” to form a corporation or LLC, a vague, undefined term that could be interpreted to include lawyers involved in the corporate formation process.

In Delaware and most other states, a corporation or an LLC is created by filing the articles of incorporation (for a corporation) or a certificate of formation (for an LLC) with the secretary of state. In the case of a new corporation, the filing is signed by an incorporator, and when an LLC is formed, the filing is signed by a person usually called the organizer, or in Delaware, an “authorized person.” In many of these situations, the incorporator, the organizer, or the authorized person is often a lawyer or a paralegal working under a lawyer’s direction. Therefore, the vague, undefined phrase “applicant to form a corporation or LLC” in the bill could easily be read to include lawyers who help clients to form these new entities.

The bill’s definition of “beneficial owner” is also vague, overly broad, and unworkable. It includes every natural person who directly or indirectly exercises “substantial control” over the company, owns 25 percent or more of its equity interests, or receives “substantial economic benefits” from its assets, subject to several exceptions. The bill further defines the term “substantial economic benefits” to mean a natural person who “has an entitlement to the funds or assets” of the entity that, “as a practical matter, enables the person, directly or indirectly, to control, manage, or direct” the entity. Because the beneficial owner definition is so expansive and unclear and would cover many individuals whose personal information is not even within the businesses’ knowledge or control, it would be almost impossible for many small businesses to comply with the bill’s disclosure requirements.

The new federal regulatory regime created by Section 9 of the draft bill, combined with the broad and confusing definition of beneficial owner, would be costly; impose onerous burdens on legitimate businesses and their lawyers and subject them to harsh criminal and civil penalties for essentially paperwork violations; and sow confusion into the company formation process. In addition, the legislation would not be effective in fighting money laundering, terrorist financing, or other crimes.

Second, the ABA believes that the burdensome and intrusive new reporting requirements in the bill would actually *weaken* the federal government’s current anti-money laundering and counter-terrorist financing tools by suspending FinCEN’s potent new Customer Due Diligence (CDD) rule for banks and other financial institutions until FinCEN can write new regulations transferring the banks’ existing beneficial ownership reporting duties to small businesses as required by the bill.

FinCEN’s new CDD rule, issued in May 2016 after years of painstaking development, will require banks and other financial institutions to collect certain specific beneficial ownership information

regarding entities that establish new bank accounts.<sup>1</sup> Unlike the draft legislation, the CDD rule includes a specific, understandable, sensible definition of beneficial owner consisting of each individual who owns 25 percent or more of the entity and a single individual with significant responsibility for managing the entity. When the CDD rule takes effect in May 2018, it will provide FinCEN with valuable, specific information about the key individuals who own or control virtually every company and other entity with a bank account. This information is expected to greatly assist FinCEN in combatting money laundering and terrorist financing.

Unfortunately, Section 9 of the draft bill would require the Treasury Secretary to revise the CDD rule to conform to the bill by transferring the banks' existing beneficial ownership collection duties to small businesses and would suspend the CDD rule until those changes are made. Therefore, by preventing this valuable law enforcement tool from taking effect as scheduled in May 2018, the draft bill will weaken, not strengthen, FinCEN's ability to fight money laundering and terrorist financing.

Third, the burdensome beneficial ownership reporting requirements in Section 9 of the draft bill are unnecessary because in addition to FinCEN's CDD rule, the federal government and the legal profession have developed other tools and taken other steps that are much more effective and practical in fighting money laundering and terrorist financing than the bill's mandates.

For example, the Internal Revenue Service (IRS) already collects entity-related information needed to fight money laundering and terrorist financing, and that information is currently available to law enforcement authorities. Since 2010, the IRS has required every business that obtains an Employer Identification Number to submit IRS Form SS-4, which includes the name of a "responsible party" within the business—i.e., an individual who is able to "control, manage, or direct the entity and the disposition of its funds and assets." Therefore, because federal law enforcement authorities are already able to access information regarding a business entity's responsible parties or beneficial owners from the IRS, it is simply unnecessary to create a costly and duplicative new regulatory regime that would impose unfair burdens and costs on millions of small businesses and their lawyers.

In addition to these federal law enforcement tools, the legal profession and the states have taken aggressive steps to detect and fight money laundering and terrorist financing in ways that minimize the impact on the confidential lawyer-client relationship, small businesses, state regulators, and the U.S. economy. For example, the ABA developed and is actively promoting the "Voluntary Good Practices Guidance for Lawyers to Detect and Combat Money Laundering and Terrorist Financing" (Guidance)<sup>2</sup>, which is designed to help lawyers fight these problems by taking prudent, proportional, risk-based steps tailored to the individual situation rather than the burdensome and costly rules-based approach of the legislation.

Since adopting the Guidance in August 2010, the ABA has worked diligently to educate lawyers, judges, state and local bars, and the public on how to detect and prevent money laundering and the

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<sup>1</sup> See FinCEN's Final Rule on Customer Due Diligence Requirements for Financial Institutions, 81 Fed. Reg. 29398 (May 11, 2016), available at <https://www.gpo.gov/fdsys/pkg/FR-2016-05-11/pdf/2016-10567.pdf>.

<sup>2</sup> The Guidance and related "Frequently Asked Questions"; ABA Formal Ethics Opinion 463 and the Conference of Chief Justices' Resolution supporting the Guidance; and the ABA/IBA/CCBE Lawyer's Guide are all available at [http://www.americanbar.org/groups/criminal\\_justice/gatekeeper.html](http://www.americanbar.org/groups/criminal_justice/gatekeeper.html).

benefits of following the Guidance. The ABA sent the Guidance to all state and local bars and urged their members to follow it, and the ABA Standing Committee on Ethics and Professional Responsibility issued its Formal Ethics Opinion 463 in May 2013 that expressed support for the Guidance and encouraged lawyers to follow its provisions. Significantly, the Conference of Chief Justices—which is comprised of the Chief Justices of the 50 state supreme courts (and the D.C. and U.S. territorial court systems) that license all lawyers in the U.S.—formally endorsed the Guidance in 2014. The ABA, the International Bar Association (IBA), and the Council of Bars and Law Societies of Europe (CCBE) also jointly published the “Lawyer’s Guide to Detecting and Preventing Money Laundering” (Lawyer’s Guide) in 2014, which provides practical tips to help lawyers around the world avoid inadvertently participating in money laundering activities and to comply with their legal obligations to fight money laundering in countries where they apply.

The ABA has worked closely with the states’ secretaries of state, the Treasury Department, and other entities on alternative solutions to the problem of money laundering and terrorist financing that would not require new federal legislation or regulations. For example, substantive law groups within the ABA worked with the Uniform Law Commission to develop a proposal that would require business entities to collect, maintain, and disclose more information regarding their incorporators, officers, directors, and owners to provide additional useful tools to law enforcement officials, but within the existing state company formation system. Such a proposal would aid law enforcement without creating unnecessary new federal mandates that would preempt or interfere with the confidential lawyer-client relationship or traditional state business formation practices.<sup>3</sup>

For all these reasons, the ABA urges you to oppose Section 9 of the draft bill or any other similar measures. Although the ABA opposes this legislation, we will continue our efforts to disseminate the Guidance, the Lawyers’ Guide, and other important educational materials to lawyers, courts, and the entire legal profession, both in the U.S. and abroad, and to promote these materials through national and local continuing legal education courses. The ABA will also continue to support efforts by federal law enforcement agencies and the states to detect and fight money laundering and terrorist financing in ways that minimize the impact on the confidential lawyer-client relationship, state regulation of the business formation process and legal profession, and the U.S. economy.

Thank you for considering our views on these important issues. If you have any questions regarding the ABA’s position on the draft legislation or any other matter, please contact ABA Associate Governmental Affairs Director Larson Frisby at (202) 662-1098 or [larson.frisby@americanbar.org](mailto:larson.frisby@americanbar.org).

Sincerely,



Hilarie Bass  
President, American Bar Association

cc: Members of the House Financial Services Committee

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<sup>3</sup> Information regarding the Uniform Law Enforcement Access to Entity Information Act is available at <http://www.uniformlaws.org/Act.aspx?title=Law%20Enforcement%20Access%20to%20Entity%20Information%20Act>