February 2007

# Shell Games

**With no federal oversight, the states are helping to shelter crooks, money launderers and, possibly, terrorists.**

Shawqi Omar has been cooling his heels in a U.S. military brig in Iraq since he was arrested in Baghdad in October 2004. The 44-year-old Kuwaiti native with American and Jordanian citizenship was charged, along with the late terrorist and leader of al Qaeda in Iraq, Abu Musab al- Zarqawi, with plotting an aborted chemical attack on the Jordanian intelligence agency. The FBI has also taken an interest: Five of Omar's relatives have been charged with using U.S. shell companies in Utah and California to commit bank fraud and money laundering and possibly to fund terrorist activities in the Middle East. One defendant has copped a plea to accusations of fraud and money laundering and awaits sentencing; three others have pleaded not guilty, and one was dismissed for medical reasons. "The fact that U.S. shell corporations can be used to commit criminal activity is increasingly a major weakness in our system," says Gregory Bretzing, supervisor of the FBI's joint terrorism task force in Salt Lake City.

Once ideal vehicles for tax evasion, shell companies--that is, corporations with no operations, no employees and no physical assets--have lately become shelters for far more nefarious criminal activities, says Stuart Nash, an associate deputy attorney general at the Justice Department. Crooks benefit in several ways. A U.S. company address lends credibility in global trade and painless access to American bank accounts. And thanks to loose laws of incorporation in many states, it's easy for offenders to remain anonymous--and to elude the authorities. Unlike publicly held companies, private entities are not obliged to reveal ownership. And without such information the police come to a dead end, unless they can tease the information they need out of bank records.

How widespread is the problem? No one really knows for sure because the states "have no idea who is behind the companies they have incorporated," says Senator Carl Levin (D--Mich.), who is trying to force the states to insist on greater transparency. "The United States should never be the situs of choice for international crime, but that is exactly what the lax regulatory regimes in some of our states are inviting." The Financial Crimes Enforcement Network, the U.S. Treasury bureau investigating money laundering, says roughly $14 billion worth of suspicious transactions involving private U.S. shells and overseas bank accounts came in from banks from 2004 to 2005, the latest Treasury data available. That's up from $4 billion for the long stretch between April 1996 and January 2004. Now, estimates the FBI, anonymously held U.S. shell companies have laundered $36 billion to date just from the former Soviet Union.

State governments provide plenty of cover for bad guys. Every year they incorporate 1.9 million or so private companies, but no state verifies or records the identities of owners, much less screens ownership information against criminal watch lists, according to a study by the Government Accountability Office. "You have to supply more information to get a driver's license than you do to form one of these nonpublicly traded corporations," says Senator Levin.

In many cases the documents of incorporation require only a company name, an address where official notices can be sent and the names and signatures of folks handling the paperwork--not of the owner or controlling shareholder. You can submit the forms in person, by mail or, increasingly, via the Web in a process that takes from 5 minutes to 60 days, depending on the state. The median fee is $95. A network of registration agents here and abroad help set up a vast number of shells each year. Once the minimal work is complete, the corporation, a perfectly legal entity, can conduct business and, in many cases, open a bank account.

Why doesn't Delaware crack down on anonymous incorporation? It would be a futile gesture; the crooks would just take their business to Nevada. Also note that chartering out-of-state corporations is a big industry in an itty-bitty state, which brought in $4.6 million a year in franchise fees in 2005 and kept many a lawyer occupied in Wilmington. Richard Geisenberger, Delaware's assistant secretary of state, says investigating the owners of new corporations would be untenable. "Costs are tremendous, and benefits are likely to be illusory," he says. "Crooks will give you false information absent a verification system." Then there's a "principle" at stake. "Consensus is that having disclosure of all of the shareholders would violate privacy and be a major burden to the state's resource allocation," says Laurie Flynn, chief legal counsel for the secretary of state of Massachusetts. "We have to stop terrorism, but we need to keep commerce [flourishing]."

Given the paucity of information, nailing criminals means relying on bank records. That's what happened in the Omar case. Shawqi Omar's relatives used two shell companies incorporated in Salt Lake City and San Diego, as well as two other front companies, to defraud local banks of at least $327,000 taken in the form of loans. The FBI says that, in at least one instance, a stateside family member wired $150,000 to an account in Amman, Jordan. The bureau is investigating whether that money was used to fund terror in Iraq.

Sometimes it's a foreign investigator who gets stonewalled. Authorities from overseas, mostly from Russia and Ukraine, sent in 143 demands for private-company data to the Justice Department in 2005. They almost always came away empty-handed. Uncle Sam couldn't investigate, much less prosecute, a Nevada corporation it declines to name that received 3,700-plus suspicious wire transfers totaling $81 million from such locations as the Bahamas, British Virgin Islands, Latvia and Russia. The situation has made a mockery of American demands that other nations do more to stop financial crimes. The U.S. has been pressuring the Financial Action Task Force on Money Laundering, a 33-nation organization Washington helped set up in 1989.

The shell problem was spectacularly demonstrated in the Bank of New York case. Peter Berlin, a Russian immigrant, with the help of his wife, Lucy Edwards, a Russian national as well, and a bank vice president, opened up accounts in 1996 at the bank for two private shells, Benex International and BECS International. According to allegations in a criminal case, they laundered $7 billion over the next three and a half years. The money came from Russian businessmen seeking to duck customs duties and hide profits from tax authorities. Convicted of money laundering, Berlin and Edwards were given five-year suspended sentences and six months' house arrest; they were ordered to pay fines of $20,000 apiece and pay the IRS $685,000.

Bank records helped finger Garri Grigorian, a 44-year-old native Russian. He struggled with a job at a fast-food joint in Sandy, Utah, then opened a deli--and, according to the feds, from October 1998 through January 2001 he laundered $133 million on behalf of customers of Intellect Bank in Moscow. He did it by setting up two U.S. shells and opening bank accounts to give the appearance of legitimate wire transfers to and from Intellect Bank. For his troubles he got $800,000 and interests in an apartment building and a golf course. Grigorian was caught because he made the mistake of using his own name to set up a bank account. He was sentenced in August 2005 to 51 months and ordered to pay $17 million in restitution to Russia for unpaid taxes and customs duties on money transferred out of that country.

Sometimes these schemes imperil strategic interests. Uncle Sam has charged Evgeniy O. Adamov, Russia's former atomic energy minister, and Mark Kaushansky, a onetime Westinghouse engineer, of using a couple of U.S. shells to divert $15 million that was supposed to upgrade nuclear safety at power plants in Russia and eastern Europe. In September Kaushansky pleaded guilty in federal court to conspiracy and tax evasion. Adamov is being tried in Russia.

Incorporation agents are not shy about promoting the privacy offered by U.S. laws. Atrium Incorporators of London promotes Delaware on its Web site as "an offshore tax haven for non-U.S. residents." Advantages: "Owners' names are not disclosed to the state," and "the company is not required to report any assets." Another Web site, corp95.com, promises that for as little as $69, plus filing fees, it can set up a corporation in Nevada, which "may provide for anonymous ownership and bearer shares." The site also offers "shelf" corporations, already incorporated businesses that have sat dormant but have some operating history.

"The upside is, you can develop a credit history easier with a shelf company," says Wayne Andre, 59, who runs Nevada First Holdings in Las Vegas, which offers shelf companies--and much more--to convince creditors that a shell is really in business. Andre also rents out his own employees to serve as directors or officers to a prospective company in order to help the real owners "retain a higher level of anonymity," a company advertisement says. Such execs for hire can use their own names to obtain an employer identification number from the IRS on behalf of the new company's owners. And if you need a business address or telephone services, Nevada First can help there, too; it has already assigned 1,800 addresses for "suites" within its Vegas offices.

As for hanky-panky among his clients, "We don't have a single company we know of that's done criminal activity," says Andre. Yet he himself took a wrong turn. In 1998 he pleaded guilty to embezzling $2 million from his clients and was later sentenced to four years in prison. Using the name Wayne McMiniment at the time, he offered incorporating services and set up bank accounts but retained signature authority over them, diverting funds, supposedly headed for offshore accounts, for his own "lavish lifestyle," says a court document.

Other shell promoters have ended up in the slammer. Paul D. Harris of Elizabeth, Colo. was sentenced in January 2006 to five and a half years in prison on tax fraud charges. Through his company, Tower Executive Resources of Denver, Harris set up shells used to conceal $9 million in taxable income for clients, who sheltered funds in secret bank accounts in the Turks and Caicos Islands and other offshore hideaways.

What's to be done? "The systemic vulnerability we face in the United States from shell companies can only be addressed by Congress through legislation to specifically regulate shell companies," says Dennis M. Lormel, senior vice president of Corporate Risk International in Reston, Va., the former chief of the financial crimes section in the FBI. If the states don't fix the problem themselves, Senator Levin says he will have to introduce legislation seeking a uniform standard. His solution: require states to force owners of companies they incorporate to disclose the owners' names on state incorporation forms. But there seems to be little urgency among his peers.

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