



**NASS**

National Association  
of Secretaries of State

## NASS Company Formation Task Force Report & Recommendations

Approved by the NASS Membership on 7/18/07

Co-Chairs:

Hon. Elaine Marshall (NC)

Hon. John Gale (NE)

## BACKGROUND

At the beginning of 2006, the federal government produced two major reports on the company formation process that raised important questions for Secretaries of State.

At the request of U.S. Senators Carl Levin (D-MI) and Norm Coleman (R-MN), the leaders of the Senate Homeland Security Committee's Permanent Subcommittee on Investigations, the U.S. Government Accountability Office (GAO) released an April 2006 report on the collection of beneficial ownership information during the company formation process. Its conclusion that the laws of incorporation in most states allow company owners to remain anonymous led some to wonder if the process was being used by criminals hoping to elude detection by authorities.

Meanwhile, a separate multi-agency report entitled, "Money Laundering Threat Assessment" raised related concerns about limited beneficial ownership information. Federal agencies contributing to this report included the U.S. Treasury, Internal Revenue Service, U.S. Department of Justice, U.S. Department of Homeland Security, the Federal Reserve and the U.S. Postal Service.

Based upon the findings of these reports, Senators Levin and Coleman arranged for the Senate Permanent Subcommittee on Investigations to hold an oversight hearing in November 2006. The hearing sought to examine how the lack of company ownership information in state files impeded law enforcement efforts in combating criminal activities. Officials from Delaware, Massachusetts, and Nevada joined federal agency representatives in testifying about their state procedures and requirements for forming business entities.

At the time of the hearing, Senator Levin expressed interest in a Massachusetts law that requires companies to maintain their list of beneficial owners and to provide that list to the Secretary of State upon request. In his view, the lack of information gathering practices employed by states could prevent authorities from identifying tax cheats, money launderers, and possibly, terrorists. He also expressed concern over a Financial Action Task Force (FATF)<sup>1</sup> evaluation that gave the U.S. a failing grade in collecting beneficial ownership information. Senator Levin warned that if the states didn't come up with some solutions to address his concerns, he would introduce federal legislation to create greater transparency.

In January 2007, NASS Business Services Committee Chair Elaine Marshall of North Carolina took action. She sent a letter to Senator Levin's office requesting the

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<sup>1</sup> World leaders established the Financial Action Task Force on Money Laundering (FATF) at the G-7 Summit held in Paris in 1989.

opportunity to convene a NASS task force to study the company formation process and to develop meaningful recommendations for federal and state consideration. Senator Levin agreed to postpone the introduction of any legislation until NASS had the opportunity to issue its findings.

The following month at the NASS 2007 winter conference, Secretary Marshall (NC) and Secretary of State John Gale of Nebraska agreed to serve as co-chairs of the NASS Company Formation Task Force. Other Secretaries of State serving on the NASS Business Services Committee volunteered to serve on the task force and some offered to recruit their state director of corporations to assist with this endeavor.

As such, the NASS Company Formation Task Force consisted of the following members:

| <b>Secretaries of State</b>                         | <b>Secretary of State Office Staff</b>                             |
|---|--|
| Hon. Elaine Marshall, North Carolina<br>(Co-Chair)  | Haley Haynes, North Carolina                                       |
| Hon. John Gale, Nebraska<br>(Co-Chair)              | Judy Jobman, Nebraska<br>Colleen Byelick, Nebraska                 |
|   | Rick Geisenberger, Delaware<br>Eileen Simpson, Delaware            |
| Hon. Karen Handel, Georgia                          | Chauncey Newsome, Georgia  |
| Hon. Todd Rokita, Indiana<br>(NASS President-Elect) | Liz Keele, Indiana<br>Marci Reddick, Indiana                       |
|   | Laurie Flynn, Massachusetts  |
|   | Tim Poulin, Maine  |
| Hon. Mark Ritchie, Minnesota                        | Bert Black, Minnesota  |
| Hon. Ross Miller, Nevada                            | Scott Anderson , Nevada  |
| Hon. Lorraine Cortez-Vazquez, New York              | Paul LaPoint, New York<br>Denise Lauer, New York                   |
| Hon. Max Maxfield, Wyoming                          | Tom Cowan, Wyoming<br>Genie Sawyer, Wyoming<br>Barb Boyer, Wyoming |

## MEETINGS

The NASS Company Formation Task Force met via conference call every two weeks from early March through July 2007. Member participation rates were very high and the calls allowed for lively debate and discussion. During the first few calls, the task force decided upon its mission, goals, and process. Members decided early on to limit task force participation to Secretaries of State and/or their designated staff. However, the following stakeholders received notification about the task force and its work:

- Other state agencies responsible for company formation
- International Association of Commercial Administrators (IACA)

- The American Bar Association (ABA) Corporate Laws Committee
- The ABA Partnership Laws Committee
- National Conference of Commissioners on Uniform State Laws (NCCUSL)
- National Governor's Association
- Registered agent community
- Various federal agencies

The NASS Company Formation Task Force held a conference call with several of the stakeholders in early May and followed that with an in-person meeting later that month during the IACA Annual Conference. These discussions provided an excellent opportunity to explore shared goals and to craft reasonable, workable solutions in a short period of time.

Early conference call discussions focused on first identifying issues with potentially simple resolutions. Another key focus was clarifying Senator Levin's exact concerns and addressing those from a state perspective. Meetings between a task force member, NASS staff and Laura Stuber of Senator Levin's office produced two key directives that the task force recommendations needed to address:

1. Find a way to provide a list of shareholders, members, or beneficial owners kept in the state of organization that would be available to law enforcement without a subpoena.
2. During the company formation process, someone must be required to check the Office of Foreign Asset Control's (OFAC) Specially Designated Nationals (SDN) List to ensure that none of the owners, members, or shareholders is on the watch list.

At the IACA Annual Conference in May, the NASS Company Formation Task Force met in person to begin drafting recommendations. Because so many task force participants attended the conference, it was an ideal time for holding a drafting session. In addition to NASS Company Formation Task Force participants, representatives from the registered agents, the ABA, and NCCUSL observed this drafting session. The task force developed draft language for six recommendations at this meeting with more than thirty participants. In addition, the IACA Business Organization Section passed a resolution endorsing the efforts of the task force.

The task force soon notified both ABA and NCCUSL that their assistance would be requested in drafting amendments to the Model and Uniform Business Entity Laws if NASS members approved the task force's recommendations at the association's July

2007 summer conference. Both organizations needed to get a written notification in order to place the request in their drafting queue.

Additionally, the task force developed a survey on state company formation practices. More than thirty states responded, providing a solid framework for members to use during development of their recommendations.

The results of the survey and other useful resources became part of a web-based information page for task force members. It also includes new and pending company formation legislation from Delaware, Massachusetts, and Wyoming.

### **RECOMMENDATIONS OF THE NASS COMPANY FORMATION TASK FORCE**

On July 18, 2007, the NASS Membership Approved the approved the following recommendations developed by the NASS Task Force and amended by the NASS Business Services Committee:

1. NASS will draft a letter to OFAC regarding state promotion of the current obligation that individuals and business entities have to comply with the Trading with the Enemy Act (31 CFR, Subtitle B, Chapter V, as amended), and suggest a meeting to discuss usability issues, public education, etc. (attachment 1)
2. NASS and IACA will compile and periodically update a comprehensive overview of state business entity laws for federal and international law enforcement use. The report would cover how each U.S. business entity statute handles the collection of ownership information, filing requirements, and periodic reporting requirements. It will also explain how law enforcement can access ownership and other relevant information.
3. States are encouraged to engage in educational outreach to the relevant communities about checking the OFAC SDN List. Pending resolution of the issues contained in recommendations 1 and 4, states are encouraged to examine their statutes and other requirements for annual or biennial reporting by business entities and determine what amendments to statutes and additional language may need to be added to the statutes, applicable notices, or forms to advise entities of the OFAC SDN List, and to identify specific individuals who may be contacted by federal law enforcement authorities with regard to investigative concerns about owners of record for their business.
4. NASS will draft a letter requesting that ABA and NCCUSL develop language to amend Model or Uniform Business entity laws requiring entities to file a periodic report that includes a name and address of a natural person in the United States that has responsibility for providing access to the list of owners of record for a business entity. That name would be a part of the public record and therefore available to law enforcement without a subpoena. NASS also recommends that

NCCUSL and ABA consider the historical precedent of confidentiality of company ownership when developing recommended language for Uniform and Model Business Entity Acts.

5. NASS recommends a two-pronged approach to “bearer shares and interests held in bearer form.” First, NASS will include a request in letters to ABA and NCCUSL that they also address clarifying Model and Uniform Entity Laws that bearer shares and interests held in bearer form are not permitted. In the interest of time, states should also examine their statutes to clarify prohibitions on bearer shares and interests held in bearer form. Currently state laws do not allow bearer shares, but language can be vague.

## **NEXT STEPS**

If the NASS membership approves and adopts the task force recommendations, a follow-up letter must be sent to both ABA and NCCUSL containing this language and asking them to begin their drafting processes. The ABA drafting timeline could be complete by April 2008, whereas the NCCUSL process will take until July 2008.

NASS will also request a meeting with Senator Levin and Senator Coleman and other concerned members of the Senate Permanent Subcommittee on Investigations to present them with the recommendations and discuss next steps.

Finally, NASS will convene a meeting of business entity law drafters to define and clarify the differences, if any, between “beneficial owners” and “owners of record.”

For more information on the NASS Company Formation Task Force, please contact:

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<http://www.nass.org>

## Attachment 1



June 8, 2007

Mr. John Smith  
Associate Director, Program, Policy and Implementation  
Office of Foreign Asset Control  
United States Treasury  
1500 Pennsylvania Avenue, N.W.  
Washington, DC 20220

Dear Mr. Smith:

The National Association of Secretaries of State (NASS) has put together a Company Formation Task Force to address issues of ownership information and the company formation process. The NASS Business Services Committee decided to organize this Task Force to respond to and address concerns raised by Sen. Levin and other members of Congress on these issues.

The NASS Task Force has had regular conference calls on the broad issues and regulatory implications of providing ownership information to investigative authorities. We have also addressed the issues of the OFAC Specially Designated Nationals List (SDN). The Task Force has participants from 12 states and has conferred with other organizations including committee representatives from the American Bar Association (ABA) and the National Conference of Commissioners on Uniform State Laws (NCCUSL). Our Task Force met recently during the annual

conference of the International Association of Commercial Administrators (IACA) to begin drafting some recommendations that the NASS membership will consider during our July 2007 Summer Conference.

One of the goals of the NASS Task Force is to find ways to assist OFAC in performing its duty to educate businesses and individuals about the importance of checking the OFAC SDN List.

The states are very willing to provide assistance in the area of public education. However, before we can encourage the public to utilize the SDN List, it is vitally important to clarify and simplify some of the processes first:

1. In earlier discussions with OFAC, we addressed our concerns about the usability and "searchability" of the OFAC SDN List. If states are going to begin referring businesses to the OFAC website and OFAC publications, it will be critical to address the fact that the current SDN List published on OFAC's website is not user-friendly for typical businesses and individuals that are required to check the list. We discussed bringing together a group of filings officers and company formation agents to advise OFAC on ways to make the list searchable and "real-time". We would like follow up on this suggestion. In its current form, the SDN List is not searchable, is not certified by OFAC as accurate and is not updated frequently enough to make any certification that the list has been checked meaningful. Once improvements are made to the list, we think states would be willing to include a link to the SDN list on their website.
2. We would like to help arrange OFAC training seminars for state filing offices. A review of the training seminars on your website indicates that the sessions are targeted to specific industries like banking, international trade and insurance. We would like to work with you to develop a training class that could be done for state officials so that they could assist in educating the business community about their obligations under federal law, including the SDN List and how to use it.
3. We would also like a "talking points" document that could help us to promote compliance with federal law and the specifics and details involved with the OFAC List. We want to ensure that simple, accurate information is provided in print and online that informs individuals and entities of their responsibilities under federal law. Contact information for OFAC so that questions may be answered and clear, simple instructions are essential to ensure compliance by the public. We would also like to work with you to create a list of vendors that might be able to help those states who would like to try and perform searches from their state system.
4. At the above mentioned IACA conference, a representative of the Small Business Administration (SBA) talked about a program they have established through the offices of the Secretaries of State. Representatives from SBA have developed materials and come to the state offices on a regular basis to answer questions for people interested in starting a business. In our discussions with SBA, it became clear that they were not familiar with the SDN List. We would encourage OFAC to reach out to the SBA to include them in any sort of public education campaign.

In short, we are committed to helping OFAC educate the public and the business community at large about the extremely important work you do and the reasons why people need to be vigilant about checking the SDN List. It should not be the duty of the office of the Secretary of

State (or other relevant state agency) to check names of beneficial owners against the OFAC SDN List.

The Senate Permanent Subcommittee members have emphasized the importance of our working together and we take that responsibility very seriously. We would like to meet with you to discuss how to move forward on these very important issues. Please contact Leslie Reynolds (202)624-3525 at the National Association of Secretaries of State to coordinate this meeting.

We appreciate your commitment to this issue and we look forward to working with you.

Sincerely,



Hon. Elaine Marshall, NC Secretary of State  
Co-Chair  
NASS Company Formation Task Force

Hon. John Gale, NE Secretary of State  
Co-Chair  
NASS Company Formation Task Force

cc: NASS Company Formation Task Force  
Hon. Deb Markowitz, Vermont Secretary of State, NASS President  
Laura Stuber, Majority Counsel, Senate Permanent Subcommittee on Investigations