MONEY LAUNDERING

THURSDAY, MARCH 9, 2000
U.S. House of Representatives,
Committee on Banking and Financial Services,
Washington, DC.,

The committee met, pursuant to call, at 10:07 a.m., in room 2128, Rayburn House Office Building, Hon. James A. Leach, [chairman of the committee], presiding.

Present: Chairman Leach; Representatives Roukema, Baker, Metcalf, Barr, Ose, Terry, LaFalce, Waters, C. Maloney, Velazquez, J. Maloney, Sherman, Inslee, Schakowsky, Moore, and Capuano.

Chairman **LEACH.** The hearing will come to order. The committee meets this morning to focus attention on money laundering and the law enforcement and regulatory challenges created by the proliferation, in recent years, of so-called offshore secrecy havens.

We are appreciative that Deputy Secretary of the Treasury, Stuart Eizenstat, is here to detail a legislative proposal announced last week by Secretary Summers to combat the money laundering vulnerabilities associated with some of these offshore centers, as well as to discuss the Administration's other anti-money laundering initiatives.

Later today, the Ranking Member and I will be introducing the Administration-crafted bill, which builds in a constructive, although more limited basis, on the provisions of legislation that I introduced last fall with the co-sponsorship of Mr. LaFalce and thirteen other Members of this committee.

I look forward to working with the Administration, Members of this committee, Members of the other body and other interested parties to pass meaningful anti-money laundering legislation this year.

Last September when the committee met to consider issues relating to the global money laundering threat, our focus was on allegations of suspicious transfers of funds from Russia to accounts at one of America's oldest and most venerated financial institutions, the Bank of New York.

Before turning to the subject of today's hearing, I have several comments on developments in that case.

Last month, the Federal Reserve and the New York State Banking Department took supervisory action against the Bank of New York, requiring it to implement new procedures for detecting suspicious activities.

These were plainly lacking during the three-year period in which some $7 billion flowed through its accounts from dubious Russian sources. Also, former bank executive Lucy Edwards and her husband, Peter Berlin, entered guilty pleas in Federal Court to a variety of charges, including conspiracy to commit money laundering, and aiding and abetting Russian banks in conducting unlawful and unlicensed banking operations in the United States.

Shortly after the guilty pleas were entered, I notified the Department of Justice of my intention to subpoena Ms. Edwards and Mr. Berlin to compel their appearances before the committee.

I did so because of my belief that the Bank of New York matter raises fundamental issues that demand Congressional review, including the extent to which the U.S. financial system has contributed to the impoverishment of the Russian people by processing transactions involving the proceeds of crime and corruption in that country.

Also worthy of Congressional examination are the systemic implications of Ms. Edwards' and Mr. Berlin's acknowledged participation in a scheme whereby Russian banks of questionable legitimacy and with apparent ties to powerful Russian oligarchs operated illegally in this country.

The specter of large-scale infiltration of our financial system by corrupt enterprises abroad is one that Congress cannot lightly ignore.

The Department of Justice, however, has expressed concerns regarding the testimony of Ms. Edwards and Mr. Berlin before Congress at this early stage of their cooperation with the Government. Consequently, I have indicated to the Justice Department that the committee is willing to refrain, at this time, from issuing subpoenas, in deference to the law enforcement interest in conducting a thorough debriefing of the couple.

I have also made clear to the Department that the committee's patience in this regard has its limits, and that we expect the Department to reciprocate the committee's recognition of its legitimate institutional prerogatives by helping to make Ms. Edwards and Mr. Berlin available for Congressional questioning at the earliest possible date.

While the **committee's emphasis today will be on offshore secrecy havens,** rather than the **Russian crime and corruption issues that were the focus of last fall's Bank of New York hearings**, the two subjects are, in fact, highly intertwined, as recent revelations demonstrate.

For example, in testimony during last fall's hearings, it was acknowledged that the then-Russian president Boris Yeltsin's son-in-law was the beneficial owner of two accounts at the bank's Cayman Islands branch, containing in excess of $2 million.

Shortly thereafter, the **Deputy Chairman of the Russian Central Bank was quoted in The Washington Post as estimating that in 1998 alone, $70 billion was transferred from Russian banks to accounts of banks chartered in Nauru, a small island in the South Pacific with a population of approximately 11,000 people.**

Nauru's banking system, characterized by draconian secrecy laws and minimal regulatory oversight, was described in a 1999 State Department report as extending "an open invitation to financial crime and money laundering."

Nauru also figures prominently in the Bank of New York scandal. The criminal information to which Ms. Edwards and Mr. Berlin pled guilty last month states **that several banks registered in various South Pacific islands, including Nauru, were used as ''fronts to facilitate the illegal transfer of money out of Russia and to conceal the Russian origin of money flowing through the Bank of New York pipeline.''**

Offshore jurisdictions have also been at the center of allegations of improprieties involving International Monetary Fund assistance to Russia and other Eastern European countries.

Last year, it was discovered that the **Russian Central Bank had secretly transferred billions of dollars through a thinly capitalized shell company located in the Channel Islands.**

More recently, press reports indicate that the Ukraine Central Bank may have engaged in similar machinations.

The committee expects to examine these issues in greater detail in its March 23 hearing on international financial architecture.

As noted before, money laundering is perhaps best understood as a seemingly modest offense that opens a window onto greater crimes that can have serious geopolitical ramifications.

In the case of Russia, the Bank of New York episode highlights the intractable nature of corruption in that country and underscores the need for U.S. foreign policy to align itself with the interests of the beleaguered Russian people, not the Kremlin elites or the commercial oligarchy.

Corruption, of course, is not exclusively a Russian phenomenon. The recent historical record is replete with instances in which foreign central banks and major money-center banks have served as vehicles for the misappropriation or outright looting of government resources.

Unfortunately, the U.S. banking system is hardly immune from the dirty monies that flow all too freely through the global economy. For someone seeking to confer the appearance of legitimacy on illicitly-derived profits, U.S. and other established financial centers are attractive destinations.

Indeed, there is little doubt that funds representing illegal flight capital or the proceeds of crime and corruption abroad enter the U.S. system in large volumes on a daily basis.

What distinguishes the U.S. from many other countries that criminals or corrupt government officials use as conduits for their ill-gotten gains, however, is our insistence on transparency and the rule of law. When schemes such as the Bank of New York circumstance come to light, institutions and individuals can be expected to be held accountable, and legal mechanisms ensure that the facts, as awkward or inconvenient as they may turn out to be, are exposed, either through the criminal justice process or Congressional hearings, or both.

The same can most assuredly not be said for some of the offshore havens that are the subject of today's hearing, where supervisory controls are either lax or nonexistent and where brass-plate banks and shell corporations are permitted to operate, free from any meaningful judicial or regulatory oversight.

The legal regimes in many of these jurisdictions guarantee a level of secrecy for financial institutions licensed to do business in them that far exceeds what is necessary to satisfy reasonable privacy interests or legitimate commercial concerns.

Moreover, U.S. investigators who follow money trails to some of these jurisdictions often run into dead ends created by statutory provisions making it a criminal offense to release information regarding clients' transactions, even in response to formal requests from duly constituted law enforcement authorities.

Even where cooperation from the local authorities is ultimately forthcoming, it is often only achieved after a period of delay and foot-dragging sufficient to permit the target of the investigation to transfer the relevant assets and records to another secrecy haven.

Recent years have witnessed some progress in introducing transparency and openness in the offshore financial sector. Some jurisdictions previously notorious for offering safe haven to criminal proceeds have executed Mutual Legal Assistance Treaties with the United States, authorizing the exchange of information and evidence in criminal investigations.

A growing number of jurisdictions have enacted meaningful anti-money laundering statutes that conform to internationally recognized standards.

But even with laws on the books, there remains a serious question as to whether there exists either the political will or the legal infrastructure to enforce those laws, particularly given the sheer volume of activity being conducted offshore.

Further complicating the international anti-money laundering effort is the dynamic nature of the offshore market. No sooner does one jurisdiction commit itself to meaningful countermeasures against money laundering than another pops up in some other corner of the globe to service the business flushed out of the first locale.

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Indeed, in recent years, authorities in this country have noted **a migration of unsavory operators from havens in the Caribbean to remote islands in the South Pacific, such as the aforementioned Nauru, that did not even register on their collective radar screen five years ago.**

The ever-changing face of the offshore sector presents enormous challenges for law enforcement officials and regulators struggling to keep pace with international criminal organizations.

It is self-evident that in an interdependent global economy with fewer and fewer barriers to capital flows, the international anti-money laundering regime is only as strong as its weakest link.

Accordingly, the U.S. and its allies in the anti-money laundering fight must embrace aggressive multilateral and bilateral strategies designed to encourage jurisdictions that have been "missing in action" in this fight to adopt the necessary legal reforms, and dedicate the necessary resources to supervising their financial sectors.

In this regard, I welcome the recent announcement by the Financial Action Task Force, formed ten years ago by the G–7 nations to coordinate international anti-money laundering initiatives and hope that it will produce, later this year, a list of so-called "non-cooperative countries" and territories that offer financial services without appropriate regulatory controls and subject to strict bank secrecy.

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And I'm also hopeful that we get greater cooperation in cross-border investigations of financial crimes.

I'd now like to turn to our Ranking Member, Mr. LaFalce.

Mr. **LAFALCE.** Thank you, Mr. Chairman. I'd like unanimous consent to put the entirety of my remarks in the record.

Chairman **LEACH.** Without objection, so ordered.

Mr. **LAFALCE.** Let me just make a few points: Last week, Secretary Summers highlighted three very important reasons to embark on an aggressive fight against money laundering.

First, it helps us pursue criminals who commit the underlying organized crimes that generate tainted money, such as drug trafficking, tax evasion, and fraud.

And it probably enables us to catch these drug traffickers, tax evaders, fraud—you know, better than any other mechanism. Second—and this is very important, too—it helps us fight the foreign corruption that undermines United States and multilateral assistance programs to promote democracy and economic development abroad.

And that is extremely important, not just because the United States programs can be effective, but

because the efforts to bring about democracies will or will not be successful, dependent upon how we can deal with the problem of corruption. And we need to enhance our fight against money laundering in order to fight that corruption, in order to help stabilize those countries. It's extremely important.

And also it helps us protect the stability of our international financial system. And it's great to have the IMF with all the debate going on about international economic architecture, what they've done right and what they've done wrong and what they ought to be doing in the future.

But if the money that they do lend, short-term, long-term, project-specific, whatever it might be, is going to be filtered through money laundering into corrupt hands, it's going to jeopardize the stability of the whole system.

And so as we proceed legislatively, we should keep these three principles in mind. Yesterday's unveiling of the 2000 National Money Laundering Strategy moves all of the stakeholders in this process, the regulators, law enforcement officials, the financial services industry, and the Congress in the right direction.

Frequently, we'll hear from the financial services industry that it self-regulates. It self-regulates well in the area of international and correspondent banking, and that, therefore, no legislation is needed.

But too many examples, too egregious, show that that just hasn't worked, such as the recent one involving the laundering of Russian organized crime funds through offshore centers and United States financial institutions.

We need a much better, targeted, common-sense approach to fill the gaps in current law. Now, last September, Chairman Leach and I introduced a bill, H.R. 2896, and today, he and I and others will be building upon that effort, in large part introducing the bill developed by the Treasury Department.

And I think that it offers the kind of regulatory flexibility that we need to tackle a fast-moving and remarkably adaptable class of criminals.

In crafting the bill, the Treasury Department recognized the need to provide a set of discretionary and targeted tools that could be deployed to address discrete problems in recognized money laundering offshore havens.

For example, the Secretary could identify a particular institution in a foreign jurisdiction as a primary money laundering concern. The entire foreign jurisdiction would not necessarily be singled out as a problem, although it could be, but the institution would be.

The Secretary would have the authority to target the specific threat posed by that institution.

We will attempt to keep in mind the need to protect legitimate commerce—that's essential—and to balance fairly, burden-sharing between regulators and the industry.

In partnership with the Administration and in partnership with the law enforcement community and the regulators and the financial services industry, I think we can enact this bill, perhaps with appropriate amendments and modification, to accomplish our goals, to protect the integrity of our international financial system. I look forward to working with you, Mr. Chairman, and hearing from the Administration. Thank you very much.

Chairman **LEACH.** Mrs. Roukema.

Mrs. **ROUKEMA.** Thank you, Mr. Chairman. I certainly will keep my remarks brief. Certainly

you, the Chairman, and the Ranking Member, Mr. LaFalce, have made the case very clear here in your opening statements. I'd just like to add that money laundering is not a victimless crime.

The money does come from drugs, illegal gambling, and a lot of other criminal activity. And the crimes affect each one of us in our daily lives.

Law enforcement has consistently told us that fighting money laundering will cut down on drugs and other crimes. I believe them. We need to take effective action.

Mr. Chairman, I also want to say, quite frankly—and this is a recurring issue—that I believe we have to look at the issue of correspondent banking more closely.

The Bank of New York Chairman, Tom Renyii, told this committee last year at hearings that correspondent banking opens the door to money laundering, and I think that case has been made.

Once a banker, an entity, has access to the international payments system, the money is as good as laundered, because the money can be whisked around the globe with a touch of a button. I think that case was made.

I will be looking at this issue and other issues relating to banking relationships. Hopefully, I will be holding a hearing in my own district in New Jersey in May.

I had tentatively planned that hearing, even before yesterday's money laundering announcement by the Administration. I believe we'll hear more from Secretary Eizenstat today, but that proposal for the hearing in New Jersey was made before the High-Impact Financial Crime Areas, or HIFCAs, were identified. Sorry to say, one of those high-impact areas is the New York/New Jersey area, which includes my district in New Jersey.

I certainly know that Senator Schumer will be testifying on those related subjects.

I pledge with you, Mr. Chairman, that we must make progress in specific ways this year—that is, legislative progress, and that's the reason I am a cosponsor, original cosponsor of your legislation, and I want to move ahead in a bipartisan way. Thank you, Mr. Chairman.

Chairman **LEACH.** Thank you very much, Mrs. Roukema.

Does anyone else seek recognition for an opening statement?

[No response.]

Chairman **LEACH.** If not, let me turn to Deputy Secretary Eizenstat, with whom this committee is very appreciative of in working of a number of subjects, not the least of which has been that he holds the Administration's principal jurisdiction on holocaust issues.

It is my view that Secretary Eizenstat is one of the preeminent public servants of this last century. Please proceed.

STATEMENT OF HON. STUART EIZENSTAT,
DEPUTY SECRETARY OF THE TREASURY

Mr. **EIZENSTAT.** I appreciate that. Coming from you, it means a lot.

Mr. Chairman, Mr. LaFalce, Members, I'm very happy to be here this morning to present the International Counter Money Laundering Act of 2000.

This committee has been at the center of a growing effort to expose the serious problem of money laundering, and to take effective steps to combat it. There are a variety of measures that have been passed over the last several years which this committee has been at the forefront of leading.

The legislation we're proposing today would fill a crucial gap in our authorities, and significantly enhance our ability to take calibrated, targeted action with respect to money laundering threats posed by foreign jurisdictions, institutions, or transactions.

Quite frankly, our legislative proposal has benefited considerably from proposals that you, Mr. Chairman, and other Members of this committee have made, from which we've liberally drawn.

We look forward to working with you and Ranking Member LaFalce with the aim of enacting effective legislation this year, and appreciate very much, the co-sponsorship that we have already from the Chairman and Ranking Member and from other distinguished Members of this committee.

I would like to point out that this legislation is being proposed in the context of the National Money Laundering Strategy for 2000, which we unveiled yesterday. This comprehensive document reflects considerable progress on a wide range of initiatives since our initial strategy last year.

It also announces a series of new initiatives to combat money laundering in the areas of financial services, international policy, and Federal, State, and local law enforcement.

I would be most appreciative, Mr. Chairman, if the entire 2000 strategy document could be made part of this record.

Chairman **LEACH.** Without objection, sir.

Mr. **EIZENSTAT.** The IMF has estimated that the amount of money laundering worldwide is between 2 and 5 percent of the world's total gross domestic product. By conservative estimates, that would be close to $600 billion, and it is probably more.

Regardless of the exact figures, money laundering is a serious threat to our country; first, because it facilitates drug trafficking, organized crime, and international terrorism.

Second, because it encourages corruption in foreign governments, undermining U.S. efforts to promote democratic institutions and healthy economic development, and, third, because it is a threat, in and of itself, because it risks undermining the integrity of our financial system.

Indeed, perhaps the most important revelation, I think, that we've achieved in the last couple of years is the recognition that it is just not an adjunct to other crime; it, in and of itself, is a danger to the integrity of our whole financial system, both domestically and internationally.

Safeguarding the integrity of the American financial system and protecting it from abuse are fundamental commitments of this Administration, and, we know, of this committee.

We concluded, after a lengthy study, that specific legislative tools that the Government has available to protect our financial system from international money laundering are, frankly, too limited.

At one end of the scale, we have advisories; at the other end, formal economic sanctions under the International Emergency Economic Powers Act, or IEEPA, and nothing in between.

Treasury advisories can be effective. They can encourage financial institutions to pay special attention to transactions involving certain jurisdictions, and to file suspicious activity reports. But,

frankly, they don't impose specific requirements, as an order or a regulation would, and they are simply not a sufficient tool to address the complexity and growing breadth of the international monetary laundering threat.

At the other end of the scale are blocking orders under IEEPA which require a presidential finding of national security emergency, and operate to suspend all financial and trade relations with the offending target. This is, in a sense, a sort of financial atomic bomb.

Such orders can affect legitimate as well as illegitimate commerce in a country, and therefore it is not, in and of itself, particularly well suited to deal with under-regulated foreign financial jurisdictions.

So what this bill seeks to do is to fill in the gaps between only an advisory on the one hand, and IEEPA sanctions on the other. Under our proposed legislation, if the U.S. Government believes that a certain foreign jurisdiction, a specific foreign financial institution, or a particular type of international transaction, poses a primary money laundering threat to the United States, we would be able to take a far wider range of actions.

The Secretary of the Treasury, for example, after consultation with the Secretary of State, the Attorney General and the Chairman of the Federal Reserve Board, could take one or more of the following types of actions:

First, we could require banks or other financial institutions to keep records of transactions and to make them available to the Government on request. This would be invaluable to our law enforcement and would help us better understand the specific money laundering mechanisms at work.

It could result also in pressure on the offending foreign jurisdiction to improve their laws.

Second, another tool would require financial institutions, at the discretion of the Secretary if this was necessary, to ascertain the foreign beneficial owners of accounts in the U.S. where they are different from the owners of record. This would help dig through layers of obfuscation and often plain deceit, and would help us know which foreigners are really holding money in the U.S. banks.

Third, another tool would require identification of those who are allowed to use a bank's correspondent accounts, as well as its so-called "payable-through" accounts, which allow customers of a foreign bank to conduct banking operations through a U.S. bank, just as if they were its own customers.

Many of these are, of course, completely lawful, but they can also be abused by foreign money launderers who seek to clean their dirty money through our financial institutions.

And, fourth, in extreme cases, the Secretary, under the legislation we propose, would have the authority to impose conditions or, indeed, outright prohibit the opening or maintaining of correspondent or payable-through accounts.

It should be clear from this description that this is not a know-your-customer bill. There is nothing in this bill which in any way requires banks to scrutinize or monitor the domestic accounts of U.S. citizens.

This bill only targets foreign jurisdictions, foreign institutions, and international transactions that pose a threat to the United States.

I would note in this regard that the U.S. banking industry has been generally supportive of our approach, and last week, for instance, the American Bankers Association was publicly supportive of

this legislative proposal.

Our proposed legislation, therefore, is designed to be graduated, targeted, and discretionary; graduated so that the Secretary can narrowly target and tailor the action that would be proportional to the threat; target it so that we could focus on the precise threat we confront; and discretionary so that we can integrate these tools into the bilateral and multilateral diplomatic efforts we're engaged in to persuade offending jurisdictions to change their practices.

To the extent to which we rely on multilateral action, we think this will make what we do more effective, but we are prepared to act unilaterally ourselves.

Permit me to briefly outline the process we intend to use to designate foreign jurisdictions as money laundering threats:

First, we would gather data about other countries' laws, regulations, and practices that either combat or facilitate money laundering. We would look at experiences from U.S. law enforcement, and with this we would then assess the scope and type of money laundering problems we face from each jurisdiction. These assessments would made on an annual basis.

Second, we would seek to determine whether each of the problem jurisdictions is primarily a source of criminal funds or primarily a haven for dirty money.

Political will would be relevant in both cases, but the distinction is crucial in terms of the application of specific countermeasures.

Source countries often face continuing problems of political will and capacity in dealing with what are, at root, domestic problems of crime and corruption. Havens tend to be characterized by under-regulated, offshore financial services and excessive bank secrecy.

Third, for each source country and money laundering haven, we shall ask if it has an adequate anti-money laundering regime, based on the global multilateral standards established by the Financial Action Task Force on Money Laundering, or FATF, a 26-country institution created by the G–7.

In addition, our analysis will also take into account the interplay between tax evasion, a serious crime in its own right, and money laundering, since the same organizations and the same havens are also and often used for both activities, often, indeed, by the same criminals.

The answer to these questions would determine whether a jurisdiction abroad, a foreign institution, or an international transaction type is designed as a primary money laundering concern so that the Secretary could then impose one of the new authorities.

We do actively participate in the work of international organizations. In June, as you mentioned, Mr. Chairman, the FATF is expected to publish the names of jurisdictions that substantially failed to meet its criteria for cooperation in resisting money laundering, and we have submitted a number of such countries to FATF to consider.

The Financial Stability Forum, created by the G–7 industrial countries, is also reviewing the role of offshore financial centers, and encouraging them to put sound financial standards into force. We're also working with the OECD countries to publish a list of tax havens, which will also be available in the next several months.

We announced yesterday that the New York/Northern New Jersey region, the City of Los Angeles, and the City of San Juan had been designated as high-risk money laundering and financial crime areas. One money laundering system, the movement and often smuggling of cash in bulk across the

Southwest border, has received this designation. We appreciated Congressman LaFalce's and Congresswoman Velazquez' participation in that.

In each, a money laundering action team would be created and would coordinate the efforts of Federal, State, and local enforcement. State and local authorities operating within each of what we call HIFCA, will also be eligible for grants under the new Financial Crime-Free Communities Support Program.

So, in conclusion, Mr. Chairman, we have a multifaceted strategy, but what we're in front of this committee to discuss primarily is our new Act which is focused on international money laundering.

There are those who believe that in the world of electronic commerce where funds travel so easily and so rapidly, that law enforcement can't possibly keep up with criminals and corrupt officials and those who move their money for them. We strongly disagree.

We have the same information technology they have, we're more motivated and dedicated than they are, and we will work to implement the authority we have and the new laws we need, and we will also seek to work with other countries that realize that the threat of money laundering is a difficulty for their own economic progress and their own stability as societies.

Thank you very much, Mr. Chairman and Members of the committee, and I look forward to your comments and your questions.

Chairman **LEACH.** Thank you very much, Mr. Secretary.

We do have a circumstance; there are two votes on the floor. I think that rather than beginning and then stopping, it might be wiser to recess for these two votes, and then we will reconvene in about twenty minutes.

Mr. **EIZENSTAT.** Thank you, Mr. Chairman.

Chairman **LEACH.** The hearing is in recess.

[Recess.]

Chairman **LEACH.** The hearing will reconvene, and first I would like to request unanimous consent that all Members be allowed to make opening statements, and without objection, it is so ordered.

Second, in terms of questioning, Mr. Secretary, the United States has done more in recent years to seek these mutual legal assistance treaties with other countries. Does it seem reasonable to you to think of having a requirement that countries make these agreements with the United States before they could have reciprocal banking relationships within this country?

Is that a reasonable thing to point toward or not?

Mr. **EIZENSTAT.** I think it is a reasonable thing to point toward. It is an important objective, just as we try to have mutual tax treaties. This would certainly give us the kind of cooperation and additional tools that we would need, and so I think fighting money laundering involves a whole range of things, of which that certainly would be one useful adjunct.

Chairman **LEACH.** There is a lot of concern of two types of level playing field. One relates between banks and other sectors of the financial community within America and the second relates between American financial institutions and those that are foreign.

One of the pluses of the less rigid approach of the Administration's bill, as contrasted to the one that we introduced earlier, is that it is a little more flexible and that this can perhaps have some advantages in dealing with foreign countries in seeking comparable approaches to doing things.

Do you look on international negotiations in this area as being a high priority of the Administration, or is this something that we just are always reacting to?

Mr. **EIZENSTAT.** No, it is a very high priority. We are working through a number of different institutions. We are working with the OECD to identify international tax havens. We are working as one of the leaders of the FATF process and in that FATF process, which is a 26-country effort, there are 25 criteria that have been identified by FATF as criteria by which they would judge along with us as a member those foreign jurisdictions that are lax in their oversight, that have excessive bank secrecy, and that are potential risks to the rest of the financial system, and so that would give us the opportunity to target multilaterally our efforts, so this is something we are very much involved with.

With respect to the issue you were describing of discretion, let me indicate why the absence of discretion could actually complicate rather than advance our goals.

For one thing, it is important to have the kind of discretion so that the response we make is proportionate to the actual problem.

Second, it is important that a jurisdiction that is identified by, for example, the FATF process abroad, or unilaterally by ourselves be given the opportunity to bring their own practices in line with internationally accepted standards. If the first thing you do is hit them over the head with the maximum sanction, you are not giving them the opportunity to do so.

In addition, the automaticity that would come from the absence of discretion could actually complicate your ability to be tough with countries, because it would be less of a likelihood to name a particular country if you knew that the only thing you could do with it before graduated tools was the sort of maximum tool of cutting them off from doing business with the United States.

We have every tool at our disposal in the legislation that you and Mr. LaFalce have cosponsored and we have every intention of using it in the appropriate circumstance, so we think that it is critical to have discretion. Discretion does not mean inaction. There is tremendous pressure from Congress, within our own Administration, across the board—all departments, and through the FATF process to begin taking action.

I think in June, the FATF, for the first time, names actual countries. This will be a real first in the fight against money laundering.

Chairman **LEACH.** A driving concern that I have had is to upgrade the significance of money laundering that is involved in public corruption as it relates to public officials. I just would like to ask the record, as you take a discretionary approach, can I be assured that the Department is going to make this of seminal significance to your efforts?

Mr. **EIZENSTAT.** You can absolutely be assured of that, but may I just add one additional fact to my assurance. That is that we have a companion bill, which we worked with the Department of Justice on, which it has taken the lead, which is also dealing with money laundering. It was introduced in the last day of the last session, and it would specifically amend our existing domestic enforcement authorities, Mr. Chairman, so that we added foreign corruption—corruption by foreign officials—as a predicate offense.

Currently—this may be hard to believe, but it is, unfortunately, the case. If a foreign official, a Mbutu or a Milosevic or any such person, were to take ill-gotten goods stripped from his country and

put them in a U.S. financial institution, we would not be able to go after that as money laundering, because it is not now a predicate offense.

Chairman **LEACH.** I appreciate that. The reason I raise it, this was a provision in the bill that we had introduced, but was taken out of the bill that you have come back with. Would you have objection of our putting this back in?

Mr. **EIZENSTAT.** No, sir, quite the contrary.

Chairman **LEACH.** Fine. Thank you.

Mr. LaFalce.

Mr. **LAFALCE.** Thank you very much.

Secretary Eizenstat, as I look over the Congress—both in the House and the Senate—I am trying to figure out how we are going to proceed. I am concerned with possible difficulties on both the left and the right.

On the right, the difficulties could be from either conservatives or libertarians, and I think our primary difficulty might be—maybe I am wrong—from libertarians who would see your proposals as something similar to the "Know Your Customer" rule and Orwellian in nature.

The potential difficulty I see from the left is a possible distrust of Government. Distrust that if you are given discretion that you won't use it because of political reasons, you won't use it because of personal reasons, you won't use it for whatever reason, and therefore let us apply it across the board in a very automatic pilot, rigid way.

To a certain extent you have addressed in your response to the Chairman's questions that latter concern that I envision from the left. Certainly, if you want to expand upon that, please do so. One thing you didn't mention—it has been my experience that whenever you have mandatory provisions you inhibit the effectiveness of law enforcement, because you inhibit the ability to target your resources.

I will give one example. Right now we have a law on the books passed in 1996, part of the immigration law, that said if you are going to cross the northern or southern border you must stop every single individual and document them. Well, you would have a three to four day wait and you would not be able to target the individuals that you really want to target. You would divert your time, attention and resources, energies, and so forth.

I would be concerned that that might be the case if we just have this automatic pilot approach without discretionary tools. I would like you to comment on that, and then I would also like you to deal with what I anticipate is a libertarian argument, that "Let's get the Government out of this 'Know Your Customer'-type stuff. We had to stop them once, we are going to have to stop them again."

Would you please comment?

Mr. **EIZENSTAT.** Thank you very much, Mr. LaFalce.

Let me respond in the following ways.

First, as I emphasized in my opening statement, there is no fair interpretation of this proposed legislation which would indicate that this is in any way, shape or form a "Know Your Customer" bill.

It does not require U.S. banks to monitor or scrutinize domestic accounts of U.S. citizens. It targets foreign jurisdictions, foreign institutions and foreign international transactions and I think again one validation of that is the support for this approach that the U.S. banking industry has shown.

The persons, therefore, to be identified would be foreign beneficial owners hiding behind false fronts; Americans who own or open accounts at domestic institutions would not be affected.

In addition, we are going through a separate process now in which I think it is clear we have learned the lessons from the difficulties last year of the "Know Your Customer" proposal. That has been completely withdrawn and what we are looking at now is—and then, only with the widest consultation with both privacy groups and banks and financial institutions—first that we do not intend to issue any formal regulations. We are talking about guidance.

Second, unlike the "Know Your Customer" proposal last year, which was regulatory rather than guidance, it also covered virtually all accounts. The guidance we are looking at would only require special scrutiny with respect to high risk accounts, but that is completely separate from the legislation itself. That is something that is being done just domestically. It has no relevance to this.

One additional point is on the privacy point. We recognize obviously the need to protect individual privacy, and the Treasury Department and FinCEN are very sensitive to that. We have built very strong systems to narrow the scope of the data that FinCEN receives to protect its confidentiality. FinCEN has imposed a comprehensive set of legal and technological restrictions to ensure the proper use of the information, and the information which is provided to the Government cannot be used for any purpose other than law enforcement.

We have our own working group on privacy in this area. We have a review which is due in May that will describe our existing protections in the privacy area and we expect in November to have proposals for even stronger, improved privacy protections.

On the other hand, the points you make about automaticity is that when you run anything on automatic pilot you have the potential for real problems. Even airplanes, when they are put on automatic pilot, have a pilot who has got the ability to turn that off. We want to make sure that we don't unwittingly by automaticity put foreign jurisdictions under such a target that they do not have the opportunity to correct their lack of supervision or excessive secrecy, that we don't have a stepped set of tools to encourage them to do so, and that, in fact, the cause of the automaticity there may be in a reluctance to even name such jurisdiction.

So we very much appreciate the leadership that Senator Schumer and others have provided in this area. We want to work very closely with him and those who want legislation in this area, but we have to make sure that it is proportionate to the particular problem. And again, discretion in no way here means inaction.

Chairman **LEACH.** Mrs. Roukema.

Mrs. **ROUKEMA.** Thank you, Mr. Chairman.

I want to go back to this question that I alluded to in my opening statement on how the Bank of New York at a prior hearing identified correspondent banking as opening the door to money laundering. It is my understanding, let me say, that the Administration wants to give Treasury the authority to declare which countries are off-limits to U.S. banks and for correspondent accounts.

You made reference to that in your opening statement I believe. Can you give me a little more specificity about how that would work? Can you describe what examination procedures the U.S.

Federal banking agencies could or would follow for correspondent banking and what changes in legislation do we need in order to permit and implement this approach so that we can close off this avenue from money laundering? We need a little more specificity on that and I do not know whether or not our legislation deals with it adequately.

Mr. **EIZENSTAT.** No, that's fine. First, let me say that Secretary Summers mentioned himself in his March 2nd speech a number of jurisdictions, from Russia to Nauru, and others in between, that are either sources or havens, and to show our seriousness of purpose Secretary Summers has just sent a letter to the First Deputy Prime Minister of Russia in which we stress the critical importance of them enacting any money laundering legislation which comes up to FATF standards. That has literally just been sent.

What we would do with respect to the particular provision you mentioned is that correspondent accounts can be, in many instances, perfectly legitimate. But they also serve as an avenue for abuse, so what we want to be able to do is have the discretion, when our law enforcement authorities, FinCEN and others, believe that it is necessary, to be able to identify those who use a bank's correspondent accounts and, if necessary, to cut those opportunities off in terms of dealing with U.S. institutions. So when necessary, we need to be able to find out who really benefits from the accounts and then, we think, transparency of identifying beneficial ownership can be very important in this instance.

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Mrs. **ROUKEMA.** Well, will you help us with our own legislation as to where that discretion has to be tightened up or more precisely defined? Correct me if I am wrong, but I sense that there is not precision in the law now that gives the Federal banking agencies the authority, so we need your help in defining that statutorily.

Mr. **EIZENSTAT.** That is correct. Our legislation that we have sent up has a very specific provision dealing with this and I think it provides precisely the kind of direction that you would be seeking.

Mrs. **ROUKEMA.** Thank you. Let me just ask briefly, I think you have gone into this, but again, being from New Jersey, and by the way, Senator Schumer, I am sure, will be addressing this, but being from New Jersey, I am deeply interested in what the Administration recommended in terms of increased prosecutors and increased personnel to deal with these high impact financial crime areas, aside from, of course, what Senator Schumer is doing. What is the Treasury recommending?

Mr. **EIZENSTAT.** First, we have for the first time a unified account of $15 million in our budget to deal specifically with money laundering.

Second, we have an existing amount of $2.5 million for so-called C-FIC grants, and we have asked in this budget for double that amount. This would permit technical assistance, computer assistance, analysis, training of local prosecutors to better sensitize them to money laundering, because oftentimes, unfortunately, money laundering is just viewed as an incidental effect of narcotics or organized crime, when in fact, as I stated, it is a problem in and of itself.

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The designation that we made yesterday of New York and Northern New Jersey as a HIFCA area means that we will be creating an action team of Federal, State and local prosecutors who will act in the same way that similar bodies work in the organized crime area to maximize the cooperation of all prosecutors, of all of our intelligence capability, and so we think it will be a very effective tool.

Now, being a so-called HIFCA does not guarantee that you will receive one of these C-FIC grants, but certainly it makes one a strong candidate for it. So the combination of having an action team and, where appropriate, having this kind of grant assistance for training of local officials, for computer assistance, for technical assistance, we think will help the localities deal with this growing problem.

Mrs. **ROUKEMA.** Thank you. That is all very positive and we certainly look forward to working with you and lobbying you on giving us a top priority. Thank you.

Chairman **LEACH.** Thank you, Mrs. Roukema.

Ms. Waters.

Ms. **WATERS.** Thank you very much. I would like to thank Mr. Eizenstat for being here today and for the work that is being done to address an area that many of us have been encouraging the Administration to get more involved in. There are so many contradictions.

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Before talking about the drug trafficking aspects of this, I have been talking with you and your shop about corrupt money and you have defined that a little bit differently, but again, I would just like to say publicly that it is an absolute contradiction for us to talk about debt relief for many of these poor countries, and that includes Africa and many in Central America, when, in fact, some of our own banks are holding more corrupt money in the banks than we can give in debt relief, and I do want very much for your shop, if that is your responsibility, to get that money and get it back to those countries, particularly Nigeria, where we are trying to support democracy, and let us not pretend as if we don't have the power to somehow do that. We have got to work on that.

That is one part of what I consider money laundering, even though it may not be considered drug money laundering. It is corrupt money that has been stolen from countries that needs to be returned to them so that we do not ask our American taxpayers to continue to support a debt relief which we all believe in.

Second, Secretary Eizenstat, I do not see that part of our problem is that we do not know who is laundering the drug money and it is not as if we have to have a lot more money placed into systems to simply identify it. I requested some time ago, and I am looking at a long list of banks and financial institutions that have been identified for laundering drug money and of course they just get fined, and nobody gets put out of business.

We know who they are. Even as we move forward as one of the sting operations that we had, Operation Casablanca, at the same time that we were moving on banks in Mexico because of the laundering of drug money, Citibank was purchasing Confia and Confia was a notorious bank for laundering drug money and at the time that they were purchasing them it is hard for me to believe that a big bank like Citibank—or whatever—does not have enough capability to do due diligence that they would know that that is a dope money laundering bank.

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So I have a whole list of them. We show them doing business in our country. We have fined them and guess what? Paying fines is simply a cost of doing business as it relates to the laundering of drug money in our country. While I am interested in identifying so-called high drug intensity areas, and so forth, I want us to start with home.

I have been working for three years on **Raul Salinas' drug money, $180 million deposited in Citibank. ''Know Your Customer'' was not even thought about. There was not even a card on him to identify where he lived.** He was assigned a private banker. I have been trying desperately to get us to talk about what we are going to do about private banking and understanding how it works in all of these banks, and **concentration accounts where the identity is lost once they pool that money**, and guess what? I also **had an amendment in the money laundering bill, Prevention Act of 1999, that simply said that our banks would not be allowed to do business with offshore banks and others that we know launder drug money.**

We know they launder drug money in Antigua. We know what that is all about, yet part of the monies that were deposited in Citibank by Raul Salinas was into these concentration accounts and off

to the offshore banks.

Whether it is Cayman Islands or Antigua, we can just say no: "if you do business with them, then you are part of them and you should not do business with them, and we are going to penalize you for doing business."

Now again, we can spend a lot of money and talk about how we develop processes for doing—what? We know how to identify them, and again I have got this whole list here. I do not know if you have seen this for 1997 to 1999, of just scores of banks that launder drug money that we penalized and we have, you know, we do some forfeiture and we do some civil penalties and all of that.

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So, I guess my question to you is this: Are we prepared to get tough, and are we going to start at home? Are there banks that are too big to touch?

Where is the case on Raul Salinas and the $180 million, and are we going to get into a period of time where time is going to run out on that case for us to do something?

Are we prepared to get tough, or are we prepared to put anybody out of business, and are we prepared to stop American banks from wire-transferring money out from these banks into offshore banks, knowing that they are just dealing with havens for the drug traffickers?

And let me just add, are we willing, given our—I have so many Mexican banks here who are known for drug trafficking that we have penalized because they do business in our country, and they are just paying money because it's the cost of doing business, but this Administration is going to fight for certification.

I mean, what are we talking about? Are we prepared to get tough?

Let me tell you why I am so adamant and passionate about it: Every day in the inner cities of America, young men are going to prison for having five grams of crack cocaine—mandatory five years in Federal prison—mandatory. We've got undercover agents out there, we've got people getting caught up in this, but guess what? If they weren't able to launder that dope money, that crack would not be in these inner cities.

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And I tell you, it is absolutely unconscionable and immoral for us to keep talking about we have a War on Drugs and we're cleaning up, while we're throwing more and more into a prison system that does nothing but warehouse them, does nothing for rehabilitation, sets them up as the problem, and the problem is the big boys and who's willing to touch them?

I'm really fed up. And it's not you. This is not a personal attack on you. It's not a personal attack on anybody, but it is an identification of the contradictions that exist in this country that allows this stuff to continue, and the victims who are getting caught up in this and overcrowding the prisons and spending more and more money on the prisons, and these big boys are getting away.

Who is willing to take on Citibank? I want to know.

Mr. **EIZENSTAT.** That has two parts: The first, you started off with was on foreign corruption. You and I have both been to Nigeria within a few months of each other, and, indeed, we discussed your trip before you went.

Nigeria is a very good example of a country that was stripped bare by corruption, an impoverished country that's the fifth largest oil producer. You had to wait hours in line for gasoline at a gas station.

And there is in the new administration of President Obasanjo, a real desire to attack corruption. There is a new Coalition for Africa with eleven countries that has proposed a new set of guidelines to attack corruption, because they realize that corruption is the enemy of development.

We are working with those countries to try to support that, but beyond that, we have not only a focused study going on with what we call attacking cleptocracy, which is the use of illegal funds by leaders, but we're going further, and this was the response to the Chairman's earlier question.

In separate legislation that we introduced last year and which has been reintroduced this year, we would like to add foreign official corruption as a predicate crime, because right now, if, for example, President Obasanjo's predecessors had—or Mr. Malosevic—had taken corrupt funds, funds that they stripped bare from their own country, and put them in a U.S. financial institution, we could not go after that under our money laundering laws, because foreign official corruption is not a predicate crime.

So we have suggested adding foreign corruption, as well as arms trafficking and other things that are not currently predicate crimes, so we could use our money laundering authorities to do that.

And we hope will have support from the Congress to add foreign official corruption as a predicate crime.

Second, with respect to the concern you express about going after domestic banks, obviously shutting off a bank, cutting its license off, is an extraordinarily consequential act to take, because of the impact it can have on innocent account-holders.

But I want to assure you, Congresswoman Waters, that we intend to be tough on money laundering. We've charged a number of domestic financial institutions with money laundering and related violations, from the Bank of New England, to the First Bank of Georgia, and many more.

Just on March the 7th, just a couple of days ago, the president of a New York bank, the MTB Bank of New York, was indicted for a money laundering scheme involving defrauding the government of Argentina.

We have a very real intention to make this a major priority. We intend to be tough, and we think that the strategy that we laid out yesterday, which has both this international bill that we're discussing today, as well as a variety of domestic actions, is indicative of our willingness to be tough.

Ms. **WATERS.** Mr. Chairman, I ask unanimous consent for one more minute.

Chairman **LEACH.** Let me say to the gentlelady, while your time has gone over, you have raised some of the most important questions before the committee, and please proceed.

Ms. **WATERS.** Thank you very much.

One, on the monies that are stolen from governments such as Nigeria. What responsibility can Treasury take, without having laws that would perhaps get at that, to use just the power of that important office to say to Citibank, "Abacha boys stole the money; it's in your bank."

They're in prison because, not only did they steal the money, they murdered the wife of one of the leaders who had been elected and thrown in jail. Just give the money back to Nigeria. Let the Abacha boys then try and get it back.

Why can't we say to Citibank, "you ought to give the money back"? And that goes for a number of

other countries, that they have been taking the corrupt money for years from. Why can't we just tell them to do that?

Mr. **EIZENSTAT.** OK, this is a good question. You mentioned the Salinas matter as well, which I know you've had a special interest in.

What we are now doing, and we announced this in our strategy yesterday, is that we're embarking on a very accelerated effort to reach out to our financial institutions. This will lead to guidance that will be provided to them of how to identify high-risk accounts like the ones you mentioned.

It may be private banking accounts, it may be accounts over a certain amount of money. It may be accounts in which people open the accounts with cash, with large amounts of cash.

So we're looking at ways in which we can provide guidance to sensitize banks to look at those precise types of accounts. We hope that very shortly, within the next couple of months, after this outreach program, to be able to announce to you, ways in which that guidance would work, and ways in which these activities could be better looked at.

And last, I want to assure you that the Suspicious Activity Reports, these require—this is mandatory—when a bank, whether it's Citibank or Bank of New York or any bank anywhere in the country, has any reason to believe that a particular transaction or account is suspicious, they are required to file with FinCEN, which is a part of the Treasury Department, a report of that transaction.
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And I want to assure you that those SARs, as we call them, Suspicious Activity Reports, don't go on a shelf and just lie there. They go to all our enforcement.

The FBI gets it, Customs gets it, FinCEN gets it, and I could list to you, one case after another of organized crime, a syndicate that was broken——

Ms. **WATERS.** Will the gentleman yield for one moment?

Mr. **EIZENSTAT.** ——in Chicago, smuggling rings for cigarettes, which these SARs have helped identify.

Ms. **WATERS.** Well, the problem is just what you described, Mr. Secretary. For example, at Citibank, the most notorious—or the most well-known private banker perhaps in the world, indicated that they were not suspicious of Raul Salinas because he was the brother of the president.

And surely, just because he had $180 million in cash, didn't mean that there was anything wrong with that. At the same time, we are watching the reports come out of Mexico, day-in and day-out, about people being murdered on the streets. They even threatened the Drug Czar when he was down there, and they killed, you know, one of our DEA agents.

And people are missing, and it goes on and on and on, but they didn't have any reason to be suspicious about this $180 million cash. So those reports are only generated when you are suspicious. So if they're not suspicious, and they don't generate those reports, then what are you going to do?
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Mr. **EIZENSTAT.** Obviously, our first line of defense against money laundering are the financial institutions themselves. But we hope, again, with this new guidance that we're going to propose, that it will sensitize banks so that that type of situation is viewed from the start as a suspicious activity.

And we share both your concern and your passion.

Chairman **LEACH.** Thank you, Mrs. Waters. Since the Treasury also has a accountability for the

Secret Service, the Chair would certainly entertain having the Secret Service travel with you if you ever go to Mexico.

[Laughter.]

Ms. **WATERS.** I just left. You know, I'm not scared of anybody.

[Laughter.]

Chairman **LEACH.** Mr. Barr.

Mr. **BARR.** Thank you, Mr. Chairman.

In your remarks, Mr. Eizenstat, on page 7, you say that "this summer we hope to issue our final rules for casinos and card clubs. We have also been working with the SEC and we expect to publish proposed rules covering SAR reporting by brokers and dealers and securities later this year."

To what extent do you anticipate those rules regarding reporting by brokers and dealers will track the current SAR rules and requirements regarding banks? Do you anticipate that there will be differences?

Mr. **EIZENSTAT.** Thank you, Congressman. I know this is an area where you have been most interested and have shown a lot of leadership that we have appreciated.

We expect that by the end of the year, working with the Securities and Exchange Commission to have rules out. Because broker-dealers are in a different situation, and because we're still trying to assess whether or not these types of transactions that brokers and dealers engage in are really subject to the same abuses as money and other MSBs, money service businesses or casinos, I don't want to say to you that the SAR requirements would be identical.

We want to make sure we tailor it to the particular need. The SEC has a great sensitivity as well to the industry that it regulates, and we're cooperating with them.

So it is certainly something that is going to be a serious effort. It is a proposed rule by that time, but I wouldn't want to say that it will simply duplicate the others, because we want to tailor it to the particular need and the particular concern of that industry.

Mr. **BARR.** And to the extent that you can, will you be working with this committee in developing those?

Mr. **EIZENSTAT.** Absolutely. We'll be very transparent. Let me just say that one of the reasons that at our roll-out strategy for the strategy for 2000, Jim Sloan, who is the head of FinCEN, announced that our Money Service Business Rules, or MSB Rules, with more to come on casinos and then later on brokers and dealers, is because we want to try to create a level playing field, as well, for banks.

We don't want banks to be the only ones who are required to file SARs. It's not fair to them. It's important that they do so, but it's not fair to them.

Second, and equally important, is that we would only be doing a part of the job if we put the burden on them, because the more we crack down on those who are using our depository institutions for money laundering, the more likely is that money launderers and criminals are going to use these other avenues, MSBs, or casinos, for their money laundering.

So we want to make sure in that respect, too, that we're closing loopholes that exist. And we will work very closely with the committee, and particularly with you, because I know of your interest.

Mr. **BARR.** Thank you. Could you just take a couple of minutes on a different matter, but just sort of think out loud and weigh the policy pros and cons with regard to requiring foreign financial institutions, particularly foreign banks, from being required by U.S. law, if there was such a U.S. law, to make them subject, as a condition of doing business in this country, to the identical recordkeeping regulations and proposals that—laws and regulations that the U.S. banks are subject to?

Mr. **EIZENSTAT.** Well, that, obviously, is the goal. And may I say that we're trying to do it in a variety of ways:

First of all, we're working through what is called the FATF process, Foreign Action Task Force. This is 26 countries, a task force created by the G–7 countries a decade ago.

And this has been an extremely useful process. They have 40 recommendations of actions that should be taken with respect to supervision, with avoiding excessive bank secrecy, and countries are being asked to come up to those standards.

We're working, for example, with Mexico, with Israel, with Russia, to try to come up to those standards. When I was in Israel just a couple of months ago, I met with the Finance Minister, and I pointed out to him that Israel, for example, does not now meet those FATF standards. They have legislation in the Knesset to try to do so.

So we're talking about countries across the board that we want to bring up to these FATF standards.

Second, to show you that there is bite to this, Austria, which is a member of FATF, has been told that if in June, by June of this year, it doesn't begin the process of ending its refusal to identify the names and owners of savings accounts, that it will be expelled from FATF.

Third, by June of this year, we expect that FATF, having taken referrals from ourselves and eight other countries, of countries we believe are potential money laundering havens, that they will list those countries specifically, at least some of them. And once that's done and you have an international spotlight, that will be very consequential.

Last, once that process is completed and countries are listed through the FAFT process, we would then be expected to act on our own to back up that.

One of the reasons that we want this graduated and targeted set of tools in our bill is so that when that list comes out, we have a variety of tools that we can target to the particular country. You couldn't just use one set of tools for all of them and say, "We'll, we're just going to cut you off completely."

But we want a graduated set of tools, including the ones that you asked about.

Mr. **BARR.** But what you're saying then is, you're agreeing with me that as a general policy matter, there should be no problem with making foreign banks, as a condition of doing business in the United States, being subject to the same laws and regulations that U.S. financial institutions are subject to with regard to information that they are required to obtain from depositors and customers and the retention of those records?

Mr. **EIZENSTAT.** In general, again, what we would like to do is bring all countries up to the FATF standards which include that measure of disclosure and supervision.

Mr. **BARR.** Thank you.

Chairman **LEACH.** Thank you.

Mrs. Maloney.

Mrs. **MALONEY.** Thank you, Mr. Chairman, and thank you, Mr. Eizenstat, for appearing before the committee and for your continued work in this area, and in another very important area, the Holocaust asset issue.

As communications tools transform financial services, the United States and this committee must continue to update money laundering laws to contend with these obvious new threats.

In the long term, the ability to transfer capital globally over the Internet or other electronic systems is a revolutionary development. Resources can be increasingly shifted to more efficient uses across the world, spurring competition and benefiting consumers.

But this system is also being used to anonymously move massive amounts of money for corrupt purposes. The ability of launderers to hide their criminal proceeds has a far-reaching effect beyond the financial system.

Money laundering in Russia has greatly complicated international financial institution lending and other aid. The laundering of drug money from South America facilitates a system that undermines democracy in the region, and finances the flow of drugs to the U.S., which my colleague, Ms. Waters, underlined.

And recent laundering cases at some of the most revered institutions in the U.S. should be a warning enough. If large-scale money laundering can occur at institutions like the Bank of New York, other cases are likely going undiscovered, and we are probably just seeing the tip of the problem.

I believe the Treasury proposal, giving the Department discretionary authority to ask institutions to collect detailed information on customers from countries that are considered to be havens is a thoughtful step in the right direction.

But I am a cosponsor of the Leach-LaFalce bill that was introduced last year, and that legislation went a step further in requiring entities that open U.S. accounts for foreign entities to identify all beneficial owners of accounts.

Some critics of the Treasury proposal argue that discretionary authority for the Department to ask for information on customers is simply not enough. They argue that because of the burden associated with determining beneficial owners, regulators may be under great pressure not to institute such burdens, and banks may decide not to ask for the information.

So, how do you address this?

Mr. **EIZENSTAT.** Well, let me mention two aspects of your question: The first is, when you talk about the Internet and the fact that this provides opportunities for additional money laundering, I was struck by Senator Schumer's very excellent point in his testimony in which he mentions how easily his own search through the Internet determined—and he mentions a particular Internet site in which, Senator, if I may, quote your excellent testimony—in which the site offers an offshore bank account in a particular Baltic state and says that no country, especially not the EU or the U.S. has the powers to request or coerce information from the authorities.

So, the Internet is being used to entice people to, in effect, hide ill-gotten goods, and our concern is particularly the use of that then in U.S. financial institutions.

So this is a growing problem. It requires the kind of international response, as well as our own response that our legislation would provide.

Second, with respect to the issue of discretion, again, I very much respect Senator Schumer's legislation and what was last year's, Congressman Leach's and Congressman LaFalce's bill, and I'm very pleased that this year, they are endorsing our legislation.

But let me again go to the issue of discretion versus automaticity. I would first note that the legislation that was introduced last year only covers offshore accounts. Our legislation is, in that sense, broader in that it covers all banks, including, for example, Russia or other countries and jurisdictions.

Second, all the tools that would be in the legislation introduced last year, as you referred to, are tools that would be in our took kit if our legislation, now the new Leach-LaFalce bill, were to be passed. And we have no disinclination to use those tools.

Third, it's important to be able to go up a chain of tools. If you start with an atomic bomb, which is, in effect, saying that no one who has inadequate supervision can do any correspondent relationships with the U.S., you don't give us the opportunity to use a variety of diplomatic efforts and less restrictive tools to change that conduct.

And we ought to be given that opportunity before we take such a dramatic step. Indeed, the step is so dramatic that one danger is that it may encourage other administrations to be unwilling to even name a country, because the consequences of naming are so automatic and so egregious.

This ought to be not the first, but one of the other opportunities, if they show that they are not willing to take action in response to our other tools.

I can assure you as well, that there is a complete agreement in this Administration, including in the State Department as well, where I worked for two years, that this money laundering problem is a detriment, not just to the United States, but to the country itself which is either the source or the haven for it; that it is a destabilizing impact on those countries, that it is a deterrent to their growth.

So I don't think you'll find any disinclination. But we need the discretion to target in a proportionate way—each country is not going to be in the same situation—to target in a proportionate way and raise their level up to that which we think is necessary and adequate.

Chairman **LEACH.** Mr. Secretary, if I could interrupt for a second, and ask if there could be some accommodation for a minute?

We have a vote on, and we have about five minutes before we have to leave for the vote. But, Ms. Velazquez, Senator Schumer has requested that if he could come now, he could give his statement, and then we could turn to you. But that is at your discretion. I think it's important in timing. Senator Schumer has been delayed quite a bit here, and he has another appointment. Would that be all right with the two of you?

Mrs. **MALONEY.** Mr. Chairman, if I could ask him to put in the record, to accommodate you, my second question is how the Treasury proposal would have applied to the Bank of New York case, and how would the Treasury new power under the proposal have prevented the laundering by the Berlins? If we could see an exact example. I understand that we don't have time now, but if you could get that back to the record in writing, if that's possible, to accommodate the great Senator from the great State of New York?

Mr. **EIZENSTAT.** Sure.

Ms. **VELAZQUEZ.** Where is Chuck? He's not here.

Chairman **LEACH.** Then we have a second request, which is that the Senator would ask if we could end with you, and that then he would come after you when we return.

Ms. **VELAZQUEZ.** That's fair.

Chairman **LEACH.** So, let me turn to Mrs.——

Mr. **EIZENSTAT.** May I say that we are pleased to answer that question. I would answer it now, if the time permitted, but we'll obviously do it in writing.

Chairman **LEACH.** And this will be the last question of this round, and we'll excuse the Secretary after Ms. Velazquez.

Ms. **VELAZQUEZ.** Thank you, Mr. Chairman.

Chairman **LEACH.** I apologize that you will only have about four minutes.

Ms. **VELAZQUEZ.** Sure, I've been here all morning, but it's OK. I will be submitting some other written questions to Mr. Eizenstat.

But I'm pleased that New York was selected as one of the first HIFCAs, but I'm concerned that New York City and Northern New Jersey are designated as one HIFCA.

I understand that the criminals know no boundaries, but in my work I have found that investigative resources should be focused where the heart of the problem is. Criminal enterprises such as drug trafficking and money laundering generate about $15 billion per year for New York City underground economies.

And as you know, the New York area, particularly Queens and Manhattan, has been consistently recognized by the Treasury Department as in need of intensive investigative actions.

I just would like to ask you what studies, research or statistics can you point to that indicates the need for the New York-New Jersey area to be designated as a single HIFCA, rather than two separate HIFCAs?

Mr. **EIZENSTAT.** Yes. We went through a very exhaustive study, Congresswoman—and I very much appreciated your participation yesterday in our rollout strategy—to determine that New York and New Jersey should be considered a HIFCA area itself, rather than designating one or the other.

This was very exhaustive, done interagency, done because of the following: You have an integrated economic region. You have things like the Port of New York-New Jersey, which is an entry point for much of the drugs and drug money that comes in.

We have an experience with the Eldorado Task Force, which is a New York-New Jersey enterprise, and it was our belief that you simply couldn't stop at the Hudson River; that this is an integrated economic region, and that means it's not only integrated for lawful activities, but it is integrated, unfortunately, for unlawful activities.

And if we only dealt with New York, we would only be dealing with part of the problem.

Ms. **VELAZQUEZ.** OK, Mr. Secretary, will Treasury place a limit on the amount of grant funds to be dispersed within a single HIFCA?

Mr. **EIZENSTAT.** The only limit to what can be provided is the upper limit of the amount of HIFCA money we have, $2.5 million this year. We've asked for $5 million next year.

But there is no particular limit per applicant.

Ms. **VELAZQUEZ.** Thank you.

Thank you, Mr. Chairman.

Chairman **LEACH.** Let me thank the Secretary, and also to say to Ms. Velazquez, we're going to have two votes in a row. The hearing will reconvene at 12:30, at which point Mr. Schumer will commence.

Ms. Velazquez, I will turn to you first, if you have further comments or questions you want to make after Senator Schumer testifies.

Thank you very much for your testimony, Mr. Secretary.

Mr. **EIZENSTAT.** Thank you, Mr. Chairman.

Chairman **LEACH.** The hearing is in recess until 12:30.

[Recess.]

Chairman **LEACH.** The hearing will reconvene and before doing so, let me make a couple of announcements. One: an apology to Senator Schumer. Let me say that committee protocol is that Senators and Members go first, and it is my understanding that this was not abided to in this circumstance and I am very apologetic, particularly so because Senator Schumer is a graduate of this committee. He has gone on to bigger and better things and more importantly is one of Congress's leading authorities on the issues under discussion, as well as a number of other subjects, and so I apologize to one of Capital Hill's most esteemed Representatives.

Let me just further say in welcoming Chuck that, just personally, I am always appreciative of having such a good friend come and testify before this body, so please proceed as you see fit.

STATEMENT OF SEN. CHARLES E. SCHUMER, A U.S. SENATOR FROM THE STATE OF NEW YORK

Senator **SCHUMER.** Thank you, Mr. Chairman.

First, let me say I appreciate as always your graciousness and courtesy. The committee had offered to let me testify first. It was my decision. I could not do it at 10 o'clock this morning, so I very much appreciate that.

Second, I realize it is a lot better being on that side of the table than this side of the table, having come here and testified, because the schedule is such I have now, after eighteen years on this committee having a great time, I have sympathy for all the witnesses who have sat here and heard the buzzers go off for votes and everything else, and very much appreciate that.

Finally, I want to thank you, Chairman Leach, for your leadership, your decency, your sense of both

moving things forward and bipartisanship. It is an honor to be here before you and so I did not mind—it is great to be back in the same room. It is great to have all the memories back, but it is terrific to see you as Chairman as well.

I also want to commend you for your leadership on this particular issue. It is not an exaggeration to say it is in good part due to your efforts that industry and regulators are finally recognizing the importance of money laundering. I want to thank the whole committee. It is good to be back in the old committee room even for a little while. As I said, I spent many, many hours in this room legislating, and some of the highlights of my career occurred in this room.

I would like to divide my remarks, Mr. Chairman, into three parts. First, outlining the problem; second, a brief discussion of the Leach-Schumer-Coverdell proposal; and third, my comments on the Treasury proposal.

First, the problem. Over the last year this committee has conducted a vigorous and ongoing investigation into money transfers from Russia through the United States financial institutions that has cast a sharp and indicting light on the business of money laundering by U.S. financial institutions. It is important that we do everything we can to fight money laundering domestically if we expect to exercise leadership on this issue internationally, but the reality is that the laundering of money through U.S. banks is really a drop in the bucket compared to the huge sums that are transferred and hidden in offshore banking centers located in places as far-flung as the tiny islands of the Pacific.

It is in these mostly obscure places like Vaunatu and Nauru in the South Pacific, in St. Vincent and Anguilla in the Cayman Islands and the Caribbean that much of the estimated $4.8 trillion in hidden assets is stashed, and according to Treasury's FinCEN unit, nearly all of that money is hidden to cover up some crime, whether it is the more benign, but still pernicious crime of tax evasion or the more ruthless crimes of international drug smuggling, terrorism, organized crime, and the illegal financing of military regimes.

The reason offshore banks are magnets for the lion's share of illegal money is very simple. They offer a service that U.S. banks and other reputable institutions around the world do not, total secrecy. The common thread in these offshore financial centers are not that they do a better job, but they conceal better than anybody else.

There are laws that make it a crime in most of these countries to divulge any information about the bank officers, depositors, transfers or any financial activity relating to banks to law enforcement without exception, so a drug dealer, terrorist or tax evader who wants total inoculation from the law will put his dollars in these banks, not in American institutions where the risk of getting caught is much greater.

In exchange for total secrecy, these offshore jurisdictions charge a fee. **The island of Anguilla, for example, charges $60,000 to open a bank and $20,000 per year to keep it there.** False credit cards, bogus country passports, and even phony nobility titles intended to hide identity and even bestow a thin veneer or respectability are sold a la carte. Today Anguilla, with a population of 11,000, has 300 chartered banks. By comparison, New York State, the financial center of the universe, at least in our opinion, has 154 chartered banks.

The Cayman Islands, which has recently enacted stricter standards in order to stem the flow of illegal money, is still the fifth largest banking center in the world, behind New York, London, Tokyo and Hong Kong. Did the Cayman Islands become such a large banking center because of their proficiency at financial transactions? Absolutely not. Did they even become such a banking center because of tax laws? No. It is very simple. They become these huge centers because they hide all information about the money that goes in and comes out.

One of the reasons for the growth in offshore money laundering is the Internet. The Internet allows fast, anonymous and cheap movement of money around the globe at the click of a mouse. It used to be that if you wanted to launder money in one of these offshore banks there would have to be some kind of personal involvement. Now on the Internet there is not.

Typing "offshore" into the Yahoo search engine produces 30,074 sites designed to attract dirty money. Again, type "offshore" into the Yahoo search engine, 30,074 sites designed to attract dirty money and some of these sites are incredibly brazen. I have blown up the web pages of some of them so that the committee might look at them.

One of them is www.offshoresecrets.com. That is the blue one over there. I am not sure the committee can see it. As you can see, or as you will see in a second, this website offers an offshore coronate bank account in an unnamed, quote: "Baltic state"—and boasts that, quote: "No country, especially not the EU or the U.S. have the powers to request or coerce information from the authorities." And they note that, quote: "The almost universal need for producing documentary proof that you are a fit person to operate a bank account has been virtually eliminated."

There are thousands of these sites that say, quote: "Yes, I want to order my own bank now." I think that is underneath the chart, the green one, it says "Offshore Financial Freedom."

Yet despite the fact that the nexus of every international crime is money laundering—Maxine Waters, I do not always agree with her, but on this issue she is right—very little has been accomplished to stop it, mostly because law enforcement is on its own fight to another country's domestic law. Law enforcement is just completely on its own, but the U.S. has leverage to compel countries to change their laws and the bill that you in the House, and myself and Mr. Coverdell have introduced in the Senate, would apply that pressure.

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There are three fundamental provisions in the law that we have introduced that would give law enforcement the upper hand in combatting money laundering.

First, our legislation isolates offshore jurisdictions. Banks incorporated in countries with complete opaque bank secrecy laws should not be allowed to participate in the U.S. financial system or transact with U.S. financial institutions. Simply put, there is no excuse for giving a jurisdiction that does not have a mutual legal assistance treaty with the U.S. access to the U.S. banking system.

Second, it expands the list of offenses that count as money laundering to include corruption. By broadening the list we can investigate and take action in cases where foreign governments or dictators seek to use financial institutions to plunder and hide assets.

Third, it requires U.S. institutions to determine the true owners of foreign accounts. U.S. banks should follow the same diligence in determining the true identity of foreign account holders as they use with U.S. customers. This provision has, more than any other, generated concerns in the financial services industry. Some are legitimate, some are displaced because of difficulties in determining ownership, and whether these difficulties warrant greater flexibility in the implementation is certainly an open question. But the first two provisions, in my judgment, are not questionable and should be the bottom line for any legislation we produce.

That brings me to the third issue here, the third part of my remarks, the Treasury Department's proposal.

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First, I want to commend the Treasury Department for their efforts to further this debate. This is the first time since I was elected to office twenty years ago that a Treasury Secretary has focused so keenly on this issue and certainly the first time he has gone so far as to propose money laundering

legislation. I respect those efforts.

But as much as I was looking forward to the unveiling of their proposal, I have to admit I was disappointed. Not because I don't agree with their proposal, because I think the proposal includes the tools necessary for a comprehensive strategy to fight money laundering, but because it renders these tools impotent by making their use discretionary. In my years as a legislator I have observed time and time again that in the international arena discretion is usually a code word for delay and avoid.

The drug certification process is a good example of where the best intentions produce the worst outcome. Discretion in evaluating whether a country receives certification means that every year we routinely ignore reality for the sake of diplomacy, and as a result, countries that do not meet standards are recertified and the drug trade continues to flourish.

Why should we not be discretionary? **There is no reason to allow any of these banks to exist, because we know that their sole and only purpose is money laundering**. What discretion do we need? **When the State Department argues against cutting off the Bahamas, saying we will lose their vote in the U.N., they almost always prevail**. Again in the international arena, diplomacy always seems to take precedence—or all too often, seems to take precedence over real domestic needs.

If we were to simply pass the Treasury legislation, based on my past experience and knowledge in this area, the number of countries that have these banks, whose only purpose is to hide money, that would be prohibited from doing so would be minimal and we would allow for all sorts of extraneous reasons other countries to continue and the money would leave from some countries that are prohibited and go to the ones that are not. So if I were to guess I would say that when it comes to money laundering in most Administrations the path of diplomacy prevails, because it is hard to find the strength necessary to buck the interests that benefit from the dollar flow from offshore jurisdictions. So unless we make it mandatory to cut off these jurisdictions that flagrantly violate international standards against money laundering, mandatory, it is my guess that not much will be done.

Despite my opposition to a highly discretionary approach, I think there is a lot we agree on and I do thank Treasury for introducing a bill that we can use as a foundation to build on. I would hope, Mr. Chairman, that you and I and Senator Coverdell could take the Treasury proposal and toughen it up, and I look forward to passing a bill with teeth in it that will put this $800 billion industry out of business once and for all.

I want to thank you again, Chairman Leach, for your leadership on this issue. You have been an excellent ally, a good friend, and I look forward to working with you and your committee.

Chairman **LEACH.** Thank you very much, Chuck, and your testimony is of course exceptional. I am obligated, however to correct you on a perspective, and that is on being the center of the universe. I represent a State with three times as many banks as your State and by all the powers vested in me as a citizen of a State with three times as many banks as New York, I would like to say that we would be happy to sell you a title. I think Baron von Schumer would be very appropriate.

[Laughter.]

Senator **SCHUMER.** I don't know how well that would fly in Brooklyn, Mr. Chairman.

Chairman **LEACH.** Perhaps not well. One of the aspects of this whole issue that is probably as extraordinary as anything I know relates to statistics. That is, in this town we have gotten used to problems, but problems take on different proportions based on size, and it is a classic philosophical issue that sometimes a difference in size can become a difference in kind.

But, if you take the country of Nauru—I asked my staff to relook at a figure, because I could not believe it, in my opening statement—and it is that in one year**, $70 billion was transferred from Russia through Nauru in a money laundering fashion. That represents $640,000 per citizen of Nauru.**

More extraordinarily, and I think we as a world community have to sit up in geopolitical, and not just banking, alarm. That **represents 21 percent of the GNP of Russia**—21 percent of money fleeing the country through one island. And so what we are dealing with here is an issue that is not exactly simply a banking system issue. It is the banking system impinging upon one of the great geopolitical traumas of our time, which is money flight, particularly as encouraged by oligarchies, in nation-states that have become corruptocracies. How do they have a chance to make it in the world if we tolerate this sort of circumstance?

I am pleased to note that—and I do not mean to defend your Administration, Chuck, but the Deputy Secretary agreed in his testimony today that he would welcome inserting in their statute making public corruption a predicate offense for money laundering purposes. This had been left out of the statute. I think that is a strong step forward and a very important one. This is an issue that impinges on the American banking system, particularly in the sense that we do not want to see the practices of foreign countries become dominant in our own society. But it is, at this point in time, principally a matter of how you develop an international system that works in a political and economic way. Therefore, it has become as large an issue in international politics as there is.

That is an inconvenience for the American banking system, because all laws that relate to money laundering are inconveniences, but the importance is nonetheless staggering and your statement today I think summarized that dilemma as well as any.

My question to you is that if we in the House side come forth with a bill, and frankly I think there is some case for a little more discretion as a first step, particularly to achieve the kind of consensus that may be needed to pass legislation, but can we expect legislation to come through the Senate likewise? What do you see as the realistic prospects?

Senator **SCHUMER.** I think there is a great deal of interest in the Senate in dealing with money laundering. As you know, Senator Coverdell and I do not have the same ideological viewpoint, but we have come together on this and received lots of interest from both sides of the aisle in a really tough bill.

I am optimistic that the kind of proposal that we have made can pass the Senate. I would welcome the House sending us a proposal, even if it does not go quite as far as ours, and we will try to pass as strong a provision as we can and then go to conference.

The one thing I guess I would talk about with discretion, I mean some people believe that Treasury has discretion to act now under a whole bunch of different provisions—they have the suspicious activity reporting requirements and things like that—and they have never done it.

I will tell you when I talk to people in the bowels of the Treasury Department who have been involved in these issues. They are the most enthusiastic people about taking discretion away, because they have lived through this, and this, of course, is their lives and the Government has to balance considerations. But they realize that as long as discretion, and particularly the burden of proof, is on cutting things off as opposed to against cutting things off, it is going to be a long, hard road.

So, you know, I think there is room for compromise. I know that some of the U.S. institutions are worried about the beneficial ownership provisions. I think those we can work out and I am open to talk to people on that. Where I feel really strongly, and I am willing to have the fight on the floor of the Senate and I would urge you to have it on the floor of the House, is allowing the kind of discretionary

approach that Treasury has adopted to prevail, because then I think we will not come close to doing what we should.

I would just say one other thing. I think money laundering in this international Internet world is going to get worse. I think the kind of problem we have seen with Bank of New York, which is a fine New York institution that got into trouble, is going to be small in the next few years. So I am confident that the kind of proposal that Senator Coverdell and I have made here, and you have made in the House, is ultimately going to become law and the only question is when. Because if we do not make it law soon there will be other incidents, scandals, call them what you will, that will importune all of us to act in a stronger way than Treasury has proposed.

Chairman **LEACH.** Thank you, Senator.

There are no more panelists, so we appreciate your staying and accommodating your schedule.

Senator **SCHUMER.** Right, and I look forward to working with you on this. We are going to get something good done here.

Chairman **LEACH.** Good. Thank you, Chuck.

Our third panel is composed of Raymond Baker, who is a Senior Fellow at the Center for International Policy at the Brookings Institution; Robert E. Bauman, who is a former Member of the United States Congress; Kenneth J. Rijock, who is a financial crimes consultant and an acknowledged former money launderer; and Mr. Jonathan Winer of the law firm of Alston & Bird, who is a former Deputy Assistant Secretary of the Bureau of International Narcotics and Law of the Department of State.

We will begin in the order of which the recognition was made, and begin with you, Dr. Baker. Please proceed.

First let me say that, without objection, all full statements will be placed in the record, and you may proceed in any manner that you see fit, please.

STATEMENT OF RAYMOND W. BAKER, SENIOR FELLOW, CENTER FOR INTERNATIONAL POLICY, BROOKINGS INSTITUTION

Mr. **BAKER.** Thank you for the opportunity to appear before you. I am Raymond Baker, and after a career in international business, I'm a Senior Fellow at the Center for International Policy, and have recently concluded a three-year assignment as a guest scholar at the Brookings Institution.

Laundered criminal money and illegal flight capital pass out of other countries and into the United States by the hundreds of millions of dollars.

To distinguish money laundering from parallel financial flows, it is useful to add the word, "criminal," when referring to the movement of funds that violate U.S. anti-money laundering legislation.

The term, "flight capital," generally refers to commercial and private funds being transferred from one country to another. It has both legal and illegal manifestations.

The legal component is generally after-tax money that is properly documented. It remains on the books of the transferor and is largely beneficial to investment and trade.

The illegal component is almost always tax-evading and improperly documented, and it disappears

from any record in the country of its origin.

Illegal flight capital, of course, has many forms, such as corruption by foreign government officials, **falsification of prices in import and export transactions, real estate and securities trades mispriced across borders, and the growing problem of wire fraud out of criminally compliant banks.**

I have studied closely **corruption and trade mispricing**, because both are dependent on international cooperation to facilitate their movement. The lowest estimate I can make for just these two sources of **illegal flight capital is $100 billion a year, a trillion in the last decade, at least half coming to the United States**. A broader examination of illegal flight capital would produce substantially higher figures.

The benefits and costs of this $100 billion a year merit clear analysis. The benefit is that it brings that sum of money into Western coffers. The cost can be seen in the impact on both domestic and foreign interests.

One hundred billion dollars a year or more of illegal flight capital provides cover for far larger amounts of criminal money laundering, estimated at $500 million to a trillion dollars a year. These are two rails on the same tracks through the international financial system. Treasury Department officials estimated to me that 99.9 percent of the criminal money that is presented for deposit in the United States gets into secure accounts. The easiest thing for criminals to do is to make their criminal money look like it is merely corrupt or tax-evading money, and when they do, it is readily received.

The domestic cost of illegal flight capital is that it removes anti-money laundering as an effective instrument in the **fight against drugs, crime, and terrorism.**

The impact of illegal flight capital is equally severe on important foreign policy concerns. Russia has been impoverished by history's largest, swiftest diversion of resources, $200 to $500 billion in a decade. Nigeria suffered under the world's biggest thief of the 1990's, Sani Abacha, with some $12 to $15 billion passing illegally abroad. Corruption and tax evasion were so severe in Pakistan as to contribute to a coup d'etat, upsetting democracy. In Mexico, we have given "white-glove treatment" to high-status criminals moving drug and bribery proceeds. China already estimates an illegal flight capital outflow of $10 billion a year, likely to rise.

The foreign cost of illegal flight capital is that it erodes U.S. strategic objectives in transitional economies, and undermines progress and stability in developing countries.

For many years, an implicit cost/benefit analysis has suggested that the inflow of illegal flight capital is beneficial to the United States. I challenge any analyst to make that case successfully.

I've used the word "facilitate" in talking about U.S. and European activities. For example, every known method for generating resource outflows has been utilized by some unscrupulous Russians, working in cooperation with Europeans and Americans. The principal device has been trade manipulation, whereby, through most of the 1990's, 100 percent of the payment for exports shipments was retained abroad, and today, despite limited reforms, exports are being underpriced so that hefty kickbacks are still paid out of the country.

Russia's problems could have been largely avoided through use of the instrument able to prevent such abuses, the confirmed letter of credit. The West should be pushing adoption of the norms of the free market system, instead of accommodating the aberrations in the free market system.

Most of the dirty money out of Russia and other countries is generated transactionally. It is initially deposited into Western banks and is then frequently spirited out to secure havens.

The question to ask is: Why should the United States accept correspondent banking relationships and overnight deposits from such havens?

It is argued, first, that if we don't take the money, someone else will; and second, that a portion of these funds may be legitimate.

If the case cannot be made that these flows, mostly illegal, strengthen our society, then a reversal of U.S. policy recommends itself. We should accept no money from offshore financial centers and bank secrecy jurisdictions unless their regulatory mechanisms meet U.S. anti-money laundering approval. It is not in our interest to remain the world's largest depository for dirty money.

As we distance ourselves from those who harbor ill-gotten gains, we must cease to harvest ill-gotten gains.

Four fundamentals should underlie a revised U.S. position: One, rejection of dirty money as a matter of policy; two, periodic reconfirmation of this policy, given to and received from foreign accountholders; three, consistency of regulatory requirements and oversight; and, four, exceptions made available to foreign friends in situations of potential violence or political harassment.

The combination of criminal money laundering and illegal flight capital constitutes the biggest loophole in the free market system. Drug kingpins and global thugs thrive because money laundering is easy, and money laundering is easy because illegal flight capital is cultivated and maintained.

We will never effectively curtail the one, while at the same time soliciting the other. Success in fighting dirty money can only be achieved when we address the whole of the problem. Thank you.

Chairman **LEACH.** Well, I thank you very much for that very thoughtful perspective. And just to make it clear that this body does want to hear diverse perspectives, we've invited Congressman Bauman, who had one of the most powerful intellects that I have served with. I am delighted you have returned, Bob, and please proceed in any manner you wish.

STATEMENT OF HON. ROBERT E. BAUMAN, JD, FORMER MEMBER OF CONGRESS FROM THE STATE OF MARYLAND

Mr. **BAUMAN.** Thank you, Mr. Chairman. I think that's an uncharacteristic overstatement of the truth on your part in describing me. I want to thank you for accommodating me and allowing me to appear.

As you know, I contacted your office on Friday, basically, because I found this proposal so outlandish and audacious that I felt that as someone who had some acquaintance with the offshore community, that I ought to avail myself of this occasion to come and make some comments.

I'm certainly not going to read my statement, by any means. And I have to comment, too, in the beginning, that I'm not in favor of crime; I'm not in favor of tax evasion. I don't have any money in any offshore accounts. I wish I did. So I'm not speaking as anyone with a self interest, except as one who has now written two major books on offshore finance and banking, and I just finished another one on second passports and dual citizenship.

This is an area that I have been keenly interested in, and although I haven't traveled in many of these countries that are involved——

Chairman **LEACH.** Can I interrupt for a second? You've just been given a new book subject, the selling of titles.

Mr. **BAUMAN.** I think they're available on the Internet, and I'll be glad to give anyone the website if they'd like to order them.

Chairman **LEACH.** Fair enough.

Mr. **BAUMAN.** In fact, I'll give the Chairman a complimentary copy, if he'll promise me that he'll read it.

So I come here with relatively clean hands, and I have really been amazed at the underlying premise on which I have heard the testimony today.

It appears that everything that is offshore is criminal in the minds of the people that are talking about it. Here we are talking about setting up a system that parallels the current State Department Narcotics Annual Evaluation, but in effect is even more powerful, because it would literally destroy some of these countries if it were applied.

In fact, Senator Schumer criticized that current, existing annual evaluation system, and now you're going to set up a new one, parallel, based on banking activities rather than drug activities, which sometimes, obviously, are related.

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I think this is a new form of colonialism. Many of these countries—I wish the gentlelady from California had stayed—are countries that have struggled to gain their independence from colonial powers.

The financial sector is a major part of their income, and I don't mean selling false bank charters; I mean people working in banks in the Cayman Islands and—in fact, if they are so powerful and they have so much money, I wonder why they're not here today?

I mean, they may well feel that if they appeared, they would be tarred with the same brush as all the rest, and came to defend themselves. I should have thought that people from Switzerland and the Channel Islands and other places, the Bahamas, would have been here.

I must say, Senator Schumer's remarks, to me, were highly intemperate, tarring the Bahamas and the Cayman Islands and others as dirty money, simply because they exist. I mean, there are many, many thousands, tens of thousands and maybe hundreds of thousands, for all I know, of Americans who invest in these places, because there are trust arrangements that help protect their assets, that they do value privacy, which they can no longer get here, and yet all of them are lumped together before your committee in this characterization as being criminal.

We have a process in this country—as an attorney, I learned in Georgetown many years ago that if there is a crime alleged, probable cause has to be shown, an investigation is made, and then the prosecutorial power has the power to indict. There is a trial, and that trial is a decision, and then if there is guilt, they're sentenced.

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All of these powers are in this proposal, at least this business of fingering countries and cutting them off from our banking system, all of these powers are brought into one person's hands, and they can be administered at the whim of that person.

So I have great concern about that. And let me say that I had no idea that Mr. Winer was going to be here today, but I appended to my remarks, an article from the Money Laundering Alert.

The Money Laundering Alert, you probably are aware, is a very well thought of, established—it is the report card, monthly, on money laundering around the world.

The owner and editor is **Charles Intriago, who is a Democrat, former Justice Department Official, a large contributor to the Democratic Party. He's never been accused, except in the Wall Street Journal, of minor infractions himself, and his newsletter is quite reliable.**

And yet in the **three pages that I appended to my remarks, it addresses itself to the treatment that was received by the nation of Anquilla last year at the hands of Mr. Winer who was then in the State Department, and others.**

Literally at a time when this country was trying to accommodate itself to the U.S. demands, it was subjected to an alert that probably caused inestimable damage to their banking system, and without any chance to answer.

So I think that we have already seen one case, at least, where questions have been raised about this, and I see the possibility of this multiplying many times over. And you have—none of your witnesses, and I feel compelled to say this—have given any credit to the changes that these jurisdictions have made.

The Cayman Islands has adopted many changes under the pressure of the Foreign Office in London. Of course, it's an overseas territory.

The Channel Islands, which are in a different constitutional status as Crown dependencies, they have adopted many of these changes, Jersey, the Isle of Man and so on.

And these changes are being made in response, not to force administered by Washington, but by the general pressure to change the climate of banking worldwide.

And not all of these jurisdictions are narrowed. I say to the gentleman and the committee, and I hope that they will consider, that there is more than one aspect to this problem.

I know when you're in Congress, you get wrapped up with the jurisdiction that's before you, what your committee has heard. No one denigrates the problem.

But I think this is a major mistake, and it will cause us international problems. I mean, I have never really understood why the United States has to be the policeman of the world, and now the bank regulator of the world.

And I think you have before you already enough laws to be able to administer the proper punishment to those people over whom we have jurisdiction, without having to crush small nations at will, of people that are essentially bureaucrats appointed for a period of time, not even Congressional say.

I thank the gentleman for allowing me to appear.

Chairman **LEACH.** Well, thank you very much, Bob.

Our next witness is Mr. Kenneth W. Rijock, who I have been told is an acknowledged money launderer and now a cooperator with and counsel to various law enforcement agencies. Mr. Rijock.

STATEMENT OF KENNETH W. RIJOCK, FINANCIAL CRIMES CONSULTANT; FORMER MONEY LAUNDERER

Mr. **RIJOCK.** I'd like to thank the committee and Chairman Leach for the opportunity to testify today. My name is **Kenneth Rijock, and I'm a financial crimes consultant in Miami, Florida.**

I teach money laundering techniques to law enforcement, and I teach from the perspective of a **decade of personal involvement in conducting money laundering operations for narcotics trafficking organizations. In other words, I was a career criminal who disposed of the proceeds of crime for my clients.**

Although I utilized a variety of methods, the most difficult to detect was the illegal export of large amounts of currency from the United States into the tax havens of the Caribbean, the so-called **"banking republics**." Located mainly in the tax shelter countries, offshore banks offer the money managers of criminal organizations the opportunity to launder funds with maximum safety and secrecy at minimum risk. I know this from my own experience.

Offshore operations in the tax havens are painstakingly constructed to make investigation literally impossible. For example, a narcotics trafficker may own a corporation formed in the Turks and Caicos Islands where the U.S. dollar is the currency of the realm. But the Board of Directors live in the Channel Islands, the bank accounts are in Lichtenstein, the company does business in Panama, and the aircraft and vessels utilized to transport narcotics and cash are registered in Sao Tome, off the Coast of West Africa.

What criminal investigator has either the time or the budget to untangle this web?

In a free and open society, we are unable to adequately police our borders, especially where outbound flights and cargo are concerned. Even if the United States Customs Service had two million agents and we placed a web cam in every general aviation airport in the country, money and financial instruments would still find a way offshore and into the tax havens.

I was never even stopped in my many trips overseas, carrying cash or cash equivalent instruments.

Money launderers are attracted by a business environment where income, corporate and inheritance taxes do not exist, where there are no exchange control laws, and where bank and corporate secrecy laws prohibit even an inquiry into the ownership of companies and bank accounts.

For over twenty-five years, the tax havens of Antigua, St. Kitts, the Cayman Islands, Anguilla, the British Virgin Islands, and others, have attracted illicit cash on its journey through the wash, dry, and fold cycles of money laundering: Placement, layering, and integration.

These three separate and distinct phases operate to enter the illicit cash into the worldwide banking system, to move it around, thus disguising its true criminal origin, and to invest the sanitized results into the unsuspecting economy.

*** A typical money laundering operation consisted of chartering a Lear Jet in Ft. Lauderdale, dressing up several clients in business suits for a purported meeting in the Caribbean, and leaving U.S. airspace with several million dollars with the ultimate destination being the "banking republics."

After a short refueling stop in St. Martin, a French-Dutch possession that does not perform customs inspections on any arriving visitors, we arrived at the airport in Anguilla, a nation which, at that time, had over 300 banks, for a nation with a population of about 8,000.

There we were met by our local attorney, who held the title of Constitutional Advisor to Her Majesty's Government, as well as the following positions in nearby St. Kitts: Ambassador to the U.S., the U.N. and the OAS, as well as being a Foreign Minister. Needless to say, we had no problem with the authorities.

Once formalities were completed, a short ride followed to a shopping center of the type common to the tax shelter countries: Only banks, trust companies, and management firms, no retail or commercial businesses whatsoever.

The $6 million was deposited into accounts owned by locally formed corporations in a jurisdiction where bearer shares are permitted, and corporation secrecy penalizes inquiring parties with imprisonment and fines, with the penalty enhanced for law enforcement.

Signature cards are passed out, with bank advice that depositors should not sign their real name. The identification of depositors and the origin of funds are never brought up by bank officers.

Two former prominent clients actually visited a toy store and used rubber stamps with the images of Minnie Mouse and Goofy in place of signatures. The names on the accounts were the names of these cartoon characters.

Certificates of deposit would be issued, the originals remaining in the bank to keep them from the subpoena powers of American courts. Bank statements were sent in care of the local attorney, who was one of the bank's owners.

The offshore banks, shielded from American law enforcement inquiry, have operated with impunity and with great success due to one feature: They all have correspondent relationships with many of New York's major banks, allowing them to deposit obscene amounts of cash anonymously, and in the offshore bank's name. The faceless client is never identified.

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Funds deposited into these offshore banks are immediately couriered to correspondent accounts in the United States, where they earn substantial rates of interest. In turn, the drug capital, now comfortably residing as a general deposit of the offshore bank in New York, is available to the American bank to lend out to any credit-worthy corporate borrower at competitive rates.

Therefore, **the narcotics proceeds make a substantial contribution to the profit picture of both the offshore and the American bank. That's why there is such strong opposition to Chairman Leach's proposed legislation.**

Closing the door on dirty money coming into the U.S. depends on requiring offshore banks to maintain the same level of reporting as is required in the U.S., thus forcing identification of the beneficial owners.

This they will never do, as it: one, exposes the criminal client to possible seizure and forfeiture; two, identifies the client; and, three, violates their own secrecy laws.

By holding the offshore banks to the same standards as we hold our own domestic banking institutions, we are not interfering with their internal operations, or seeking to close them down. Rather, we are declining to deal with them until they conform to established banking norms.

For those privacy advocates who see this proposed legislation as some Orwellian intrusion into the right of the individual to conduct business where and when he pleases, I reply: Please feel free to conduct your business worldwide, but know this; you cannot conduct business into or out of the United States with institutions that do not meet our reporting standards.

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If you want to exercise your right of so-called asset protection, and move your assets offshore to limit exposure to creditors, ex-spouses, and the Internal Revenue Service, you may find you are traveling down a one-way street, unable to repatriate funds.

Another reason we must shut down the incestuous relationship between American and tax-haven banks is the rising presence of Russian organized crime in the Caribbean. As many tax havens allow what are known as **economic citizenship**, these well-funded career criminals have been seen obtaining new passports, often with new names, unknown to law enforcement. We are not interested in these individuals corrupting, influencing or attacking our domestic banking and financial system through the tax havens.

An additional reason for closing the correspondent bank loophole is the proliferation of the so-called **portable or traveling trust**, an investment vehicle guaranteeing total secrecy for the grantor, with an additional feature. The trust document provides that, in the event of any inquiry about the trust or any aspect of its holdings, all assets are immediately transferred to another tax haven, often at the other end of the world. Therefore, no information can ever be obtained.

Still another reason is the prevention of the rise of what have been called narco-democracies in the region, the total domination of a local government by successful narcotics traffickers. The recent experiences of St. Kitts are a prime example.

The passage of the Leach bill would strengthen legitimate banks in the offshore region and encourage their development, thus allowing support for emerging democracies supported by legitimate commerce.

Remember, we also stop international white-collar crime from utilizing our banking system through the tax havens. Crooked insurance companies would no longer be able to hide behind the shield that protects against disclosure of their assets and loss reserves, nor could bank fraud be perpetrated from the safety of offshore refuge.

The second major feature of the Chairman's bill is the functional elimination of the payable-through or pass-through account. Simply put, **a pass-through account allows a non-depositor at an American bank to exercise certain privileges, utilizing the offshore bank's account at that institution**.

I couldn't have created a better vehicle for money laundering than this method, where user identification is all but impossible, and the user can effectively effectuate international transfers with little or no risk or exposure.

I recognize that many banks have already prohibited this type of transaction, but we need to close the door on that form of abuse.

Make no mistake about it, money laundering is financial terrorism. To allow it to thrive in the United States will assist immensely powerful individuals and organizations who, having successfully invested huge sums in our economy, will begin to exert financial, political, and even intellectual influence on our institutions. We need to stop this development at this stage.

Unless we slam the door on the tax havens, and deny them access to our banking system and markets, we cannot expect to suppress money laundering in the United States.

If you want to learn more about this subject, come down to Miami next month, sit in on the International Money Laundering Conference, and learn about the problems faced by law enforcement and the American financial services community. Thank you.

Chairman **LEACH.** Well, thank you very much for that revealing testimony.

Mr. Winer.

STATEMENT OF JONATHAN M. WINER, FORMER DEPUTY ASSISTANT SECRETARY, BUREAU OF INTERNATIONAL NARCOTICS AND LAW, DEPARTMENT OF STATE; COUNSEL, ALSTON & BIRD

Mr. **WINER.** Thank you, Mr. Chairman. My name is Jonathan M. Winer. I was formerly the Deputy Assistant U.S. Secretary of State for International Law Enforcement matters. I'm currently counsel to the law firm of Alston & Bird for e-commerce and financial services issues.

I thank you for the opportunity to testify before this committee again regarding your proposed legislation, the Administration's strategy, and the risks created by under-regulated offshore financial services sectors.

Before addressing these issues, I wanted to review aspects of the recent multibillion dollar money laundering case involving the firm Benex, and its accounts at the Bank of New York.

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In the fall of 1998, in the course of my work at State, I learned from the Manhattan District Attorney's Office that Russian organized crime figures were utilizing offshore money laundering mechanisms previously associated with Colombian cocaine traffickers, involving manipulations of publicly traded stock, both to defraud unwitting investors and to turn dirty money into clean money.

The money trail extended into offshore havens in the Caribbean and the South Pacific, as well as major financial services centers like London and New York.

I wanted to know more. The British Government kindly set up a briefing for me.

I went to London, and a year ago learned of shenanigans involving a pretty typical money laundering infrastructure.

An Ambassador from a West African country was involved in selling passports and various other schemes. Members of the French mafia were using it.

They were working with a well known Italian financial institution. There were Canadian lawyers, British solicitors and accountants, all dirty, and offshore banking in Liberia and the Channel Islands. It was interesting, but it was all pretty familiar to me, the kind of thing one sees pretty often in the realm of international money laundering.

The briefing then took on a much more disturbing aspect. **The British officials told me they'd run across a company called Benex International, based in Queens, New York, owned by a Russian named by Peter Berlin.**

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Benex was a small business, they said, nothing more than a couple of people with a couple of personal computers. **Benex intersected in a number of ways with the money laundering infrastructure the British were investigating, and had also apparently sponsored U.S. visa applications for known members of the Semion Mogilevitch crime organization** of Russia, acting in **false receivables scams with a firm known as YBM Magnex and large frauds involving the Toronto stock exchange.**

The Mogilevitch organization, Mr. Chairman, was and is a well known priority target of law enforcement agencies on both sides of the Atlantic. Public accounts concerning Semion Mogilevitch describe the involvement of his criminal organization in almost every major form of organized crime: Contract killings, drug trafficking, prostitution, extortion rackets, and frauds, extending to a substantial number of countries in Western and Central Europe, the Americas, and the Middle East.

Details about YBM Magnex frauds and Mogilevitch's substantial interest in the company were a matter of public record, after regulatory and enforcement actions were taken against the company in the United States and Canada in 1998, leaving innocent investors holding some $500 million in worthless securities before the firm pled guilty to securities and mail fraud.

At the London briefing, **I learned that Benex's accounts at the Bank of New York included not just YBM Magnex activities, but Mogilevitch funds from drug smuggling, extortion, and contract killings.**

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Benex thus appeared to be part of the infrastructure in the United States that the Mogilevitch organization, among others, was using to launder the proceeds of serious crimes, and to commit ongoing serious frauds.

This, in turn, raised for me the question of the volume of funds Benex was moving. **I learned that a Benex account at the Bank of New York had moved more than $4.2 billion, with over 8,000 transactions a month, for an average of one wire transfer every five minutes, night and day, 24 hours a day, for 18 months, a company with just a couple of employees and a couple of personal computers.**

I learned that Benex was operated by Peter Berlin, a Russian, married to a U.S. citizen, herself Russian born, who had divorced her first American husband after acquiring U.S. citizenship.

I learned that Ms. Edwards worked at the Bank of New York, where Benex maintained its account, and through which Benex undertook its money laundering activity.

I learned that Ms. Edwards' job at the Bank of New York was to head the East European Trade Finance Department at the Bank of New York's London offices, and that she remained in daily contact with her husband, Peter Berlin, who was still in New York running the money laundering operation, Benex.

Mr. Chairman, my jaw literally dropped open when I was provided with this information. In the past, I had investigated the Bank of Credit and Commerce International, BCCI, and a lot of other big international money laundering cases, but this case had stunning implications.

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This suggested to me then a year ago that there was a serious possibility that Benex was a multibillion dollar money laundering business operated by a couple of Russians, including one insider at a major U.S. money center bank, and that Benex was, among other things, laundering funds in New York City for some of the worst elements of the Russian mob.

In various capacities, I prosecuted, investigated, analyzed, or have undertaken oversight of major money laundering cases over the previous twenty years. I had never heard of any money laundering case of this magnitude.

I also had national security concerns. I felt that the lack of transparency in Russia's financial system was closely related to Russia's crime and corruption problems, and the poor reputation of its business environment.

I was of the view that Russian's disappearing capital had contributed substantially to Russia's economic problems, and that the concentration of Russian capital in the hands of a small number of people was dangerous.

For several years, I had worked with Russia's Central Bank and with various other Russian agencies seeking to make Russia's banking system more transparent, and to assist Russia in passing and implementing effective laws and structures to combat both money laundering and financial crime.

Those efforts had not been highly successful. If Benex represented a window on billions of dollars worth of Russian funds being laundered through the United States, a successful investigation could have a potentially significant impact in making Russian money movements more transparent, including the movement of funds embezzled by Russian officials and oligarchs.

My concerns were exacerbated by what I heard about law enforcement's ability to proceed in the case. "We're not sure whether or not anyone will make a money laundering case regarding Benex," investigators told me. "Existing laws may or may not cover this case, depending on what people knew about the sources of the money." I asked whether enough investigators were assigned to the case, given its magnitude, so that the answers would be found out.

I learned that the resources were quite a problem. There were a couple of people working on the case in the United Kingdom, and there was only one Federal agent working on the case in the United States, whom I later heard referred to by other law enforcement officials as "Task Force Steve."

"Surely, you have integrated databases, drawing together and analyzing all your information?" I asked. "Surely, you have analysts working for you?" The answer was the British did not, and neither did their American colleagues.

When I returned to the United States, **I took the information I received to senior officials at the Department of Justice, to the National Security Council, to the Department of State, and to other relevant components of the U.S. Government.**

To a person, neither they nor any of their agencies had any information regarding the Benex case. If there was an active case against Benex in New York, no one in Washington had ever been briefed on it, including senior U.S. Government officials who considered the Semion Mogilovitch organization to be a substantial criminal and national security threat.

Officials at the NSC and State concurred that the information on Benex raised potential national security and foreign policy concerns, as well as serious international law enforcement issues.

We, together, asked senior Department of Justice officials to do everything in their power to make sure the allegations were checked out, and to ensure that appropriate resources were devoted to investigating the case.

Mr. Chairman, I know I'm going over a little bit in my time, but if I might continue just for a few more paragraphs?

Chairman **LEACH.** Let me say to you, Mr. Winer, your testimony is of historical significance, and you may take as much time as you want.

Mr. **WINER.** Thank you, Mr. Chairman. I don't want to abuse the privilege granted to me by the committee. I'll continue.

Because of the magnitude of the money allegedly being laundered, I had hoped that once Washington had been alerted to the case, the Benex money laundering operation would be shut down. I also knew that sometimes ongoing criminal enterprises cannot be stopped for a period of time while officials consider whether they have enough information to bring criminal charges, or to undertaken regulatory or other actions.

I also knew that **the Southern District of New York had a history of not wanting the Justice Department in Washington involved in its cases, and did not always share as much information with main Justice as main Justice desired.**

At that point, my role was to take no further action, but to await developments and to **seek updates from time to time, which I did seek repeatedly, as did other components of the U.S. Government in Washington, updates which were not forthcoming.**

As the committee well knows now, the Benex and Bank of New York story broke in the New York Times in August of last year. Peter Berlin and Lucy Edwards have since pled guilty to various Federal money laundering charges and are now cooperating with U.S. prosecutors.

Benex was, indeed, a multibillion dollar money laundering operation, the largest such operation uncovered to date. Benex did apparently handle transactions for many in Russia who took advantage of its services to create false paper trails by which they hid their money from Russian authorities for differing reasons.

Benex's customers appear to have included a number of very prominent Russians, including other criminal organizations besides that of Mogilovitch, and businesses associated with important figures from Russia's financial community, sometimes called oligarchs.

Mr. Chairman, it is my hope that perhaps someday, through one legal process or another, the financial records of Benex will be made public, even put online for the scrutiny of the whole world. I believe some good might come of that.

I believe that there are lessons to be taken from that case that may be relevant to this committee's legislative efforts, and I would be glad to discuss them in response to any questions you may have. I thank you for the opportunity to testify and for your leadership on this issue.

Chairman **LEACH.** Well, first, thank you very much. I just want to return to perspective on numbers, because this is a town that has a tin ear to the meaning of digits.

These two individuals, Peter Berlin and Lucy Edwards, appear to have laundered $7 billion and possibly more. We're not talking about a few hundred thousand dollars, a few million dollars, a few hundred million dollars.

This is an extraordinary sum of money, and it describes the nature of a system that's come into play of a criminal nature in one of the great countries in the world.

And for our law enforcement not to be immediately attentive is a mistake. For this Congress not to be attentive is extraordinary.

And I happen to think that one of our duties as institutions, as representatives of institutions of the United States is to make it clear that we identify with the plight of the Russian people, as contrasted with concerns with relations with any particular leader in a foreign state or any particular economic organization in a foreign state.

Now, you have background from the Executive Branch's perspective. My ongoing negotiation at the moment is to try to get witnesses to come before this committee, most particularly Mr. Berlin and Ms. Edwards.

The Justice Department is balking. I acknowledge some of this balk, because they want to debrief these witnesses for possible criminal trials.

But it strikes me that, far more significant than any criminal trial holding them particularly accountable for any particular act, is what these circumstances signify for the international system, for

American policy, for American law.

And you're a neutral witness. Do you take the Justice Department's perspective, or do you think this committee has a reason to seek these people's testimony?

Mr. **WINER.** Mr. Chairman, I have actually had a number of different roles in connection with this territory. At various times, I have been a journalist, a lawyer in private practice, a prosecutor, a legislative counsel on Senate hearings on this topic, as well as my role in the Executive Branch.

There was never an occasion under any Administration, Republican or Democrat, throughout the whole time I have been in Washington, that failed to resist efforts by any Congressional committee to seek the testimony of people who were going to be witnesses in potential criminal cases.

They do not wish to have—and I have heard the routine many times when I was staffing people in your position—possibly inconsistent statements made before the Congress from statements that may be made later in judicial proceedings.

Now, there are some very important different equities at play here simultaneously. There are real law enforcement equities at play, which the Justice Department is right and proper to point out and to insist upon.

There are also substantial equities for the U.S. Congress, part of its fact-finding and legislative mission which are simultaneously at play.

Here, there may also be foreign policy and national security interests at play. How one balances all of those things in any individual situation, requires a great deal of judgment from the wisest heads available in the particular situation, looking at the particular information, the particular facts, the particular circumstances and trying to balance and weigh those equities.

It's not a simple matter to do so. I recollect that when I was investigating BCCI, the Justice Department, negotiating with us, revealed some materials on the part of the case that had already been closed, and then more materials, and ultimately a fair amount of materials.

But it was an extended negotiation. There are very, very difficult equities to weigh. That's really the best answer I can give you.

Chairman **LEACH.** In your testimony that is written, you've described certain **Internet gambling operations in the Caribbean island of Antigua involving an institution called the Swiss-American Bank. Do you know what Swiss-American's connection is with the Swiss financier Bruce Rappaport?**

Mr. **WINER.** Sure.

Chairman **LEACH.** His name has obviously come up with the Bank of New York probe.

Mr. **WINER.** Yes, sir.

Chairman **LEACH.** Is there anything you can say, both to the underlying Internet gambling issue, as well as the Rappaport connection?

Mr. **WINER. Mr. Rappaport was the founder of Swiss-American and for a number of years was its owner.** Public records in Antigua suggest that he's not the owner of the bank at this time.

The bank's management has been pretty uninterrupted throughout this period. There have been a

variety of changes, but he certainly was the founder of the bank.

The bank was used by European Union Bank of Antigua, which was the first Internet scam bank on the Internet, a Ponzi scheme to defraud American investors, run by Russian organized crime.

Swiss-American was used to capitalize that, together with funds from Menetap, a Russian bank whose senior personnel also became caught up in the Bank of New York's Benex affair.

Swiss-American, in turn, was related to and has had accounts with Intermaritime Bank, which is a bank which I believe was partially acquired by the Bank of New York. Intermaritime Bank was previously Bruce Rappaport's bank.

What's interesting about the Internet gambling casino connection is that most of the Internet casinos that I have found seeking to have Americans engage in Internet gambling, seem to all use the same facilities. There are different websites throughout the web. I've got a couple here, and I have given the committee copies of the sites of "Casino on Top" and "Casino on Net."

Mr. **WINER.** And what they show, oddly enough, is if you want to do casino gambling, you pay your money to Swiss-American Bank in the name of a particular account, Intersafe Global, and account number, and then that money is advertised as being handled by the correspondent bank of the Intermaritime Bank, Geneva, Bank of New York, among others.

Now, what's interesting about that is that that mechanism, in theory, is a perfect example of concentration accounts or correspondent bank activities where you have commingling of funds, and therefore have essentially no way to be able to trace what's going on. So it is potentially a significant opportunity to do money laundering, depending on how it's handled.

Now, when I visited Antigua and met with the Prime Minister there, **we had questions about Swiss-American, because Swiss-American had been used by a drug trafficker whose assets has been seized by the United States Government, and the United States Government owned the assets, and the assets disappeared.**

And we asked the Prime Minister for access to records on the assets we previously asked him for. This is the Department of Justice and State, working very closely together with the Department of the Treasury.

And the Prime Minister said to me and to a senior Justice official, ''We can't get you the records; they were destroyed in the hurricane.''

Nobody else's records were destroyed, just the records belonging to the accounts that the U.S. Government now had an interest in. And this was money held at Swiss-American Bank.

So if one wants to rely on the records of Swiss-American Bank and their integrity and their transparency and their trustworthiness, I would just remember that at any time, apparently, a hurricane can destroy those records, thus making them unavailable, if you believe the Prime Minister of the country. That was the representation made to senior U.S. officials in the fall of 1996, I believe.

Chairman **LEACH.** I want to go into this Internet gambling for a second. Some of us have grave doubts about it and grave doubts about it as a principle.

You have talked about an element of it. Is it possible to do Internet gambling without a credit card or using Western Union?

Mr. **WINER.** Sure. This particular set of instructions on the Internet, available to anybody in the world, tells you exactly how you do it, through Western Union, through credit cards or through wire transfers.

Chairman **LEACH.** We are in the process of looking at legislation, and I want to make this very clear, to prohibit Internet gambling using bank instruments, or actually prohibiting the use of bank instruments for Internet gambling. Would that be devastating to the Internet gambling community?

Mr. **WINER.** It depends on the regs, the sanctions, the mechanism of enforcement, whether it was adopted ultimately multilaterally, as well as by the United States, whether there was consensus in the financial services sector that this was a reasonable approach.

You have to have such consensus in order for things to be both enforced and enforceable over time.

Given the magnitude of the problem here, I believe it's possible you could achieve such consensus, but it would be important to try and build it.

The multilateral approach to this problem has changed enormously over the past decade. I listened with tremendous interest to the comments made by Senator Schumer, because they reflected a position that I previously would have held.

I have been skeptical for many years of the multilateral initiatives that have been underway as too slow and as covers for non-action.

In the last several years, I have participated in relatively few of them. Much of my work was bilateral or in other areas.

These negotiations tend to be led by the U.S. Department of the Treasury. I have been extremely impressed by the progress made in the past two years since the Russian ruble collapse, the Long-Term Capital Management debacle, the hearings you held on that, which I think had a very substantial impact on Treasury.

And I believe that the concatenation of the financial stability issues, Asian malaise, Latin American economic problems, Mexico, Russia, on the one hand, and the major money laundering scandals on the other hand, have created a real change in what the multilateral organizations are now prepared to do.

And I concur very strongly with the approach laid out by Deputy Secretary Eizenstat this morning, for that reason. I'm speaking in my current vocation as a private sector attorney, not as a flack for the Administration. Simply, that is my judgment.

I believe that remarkable progress is being made multilaterally, and that it's essential, as we continue to move ahead unilaterally and bilaterally, that we also move ahead multilaterally, given the fact that there is no difference today between onshore and offshore, except for one thing: Offshore is what you apply to somebody else's citizens; onshore is what you allow your citizens to do.

So, offshore is what you will take. The money you will take from other people, but what you would not apply to your citizens, because it places at risk your own financial sector.

Chairman **LEACH.** Well, I appreciate that. Let me talk about Internet gambling, though, for a second. As a principle, I don't like the idea, just in and of itself, whether it's perfectly legally done, with perfectly legal intermediaries.

But what you are suggesting with regard to the current nexus of Internet gambling is that there are imperfect people who are in the process center of the Internet gambling circumstance.

For example, within the United States, we've got a lot of laws that apply to gambling. And many gambling casinos are owned by reputable corporations and individuals.

But it strikes me that at the Internet level offshore, there are some imperfections that might be analogous to a new Russian mafia playing a role, as contrasted with an old mafia from Sicily.

Is that a valid observation, or is it an exaggeration?

Mr. **WINER.** No, Mr. Chairman. The same as my colleagues on this panel, Mr. Rijock and Mr. Baker, in particular, both already stated**, the infrastructure used for money laundering, for tax evasion, and now for Internet casino gambling is the same infrastructure. The same people use it, it attracts the same kind of people, it's the same mechanism, same everything.**

Guys and Dolls, Nathan Detroit, he's got the oldest floating crap game in New York; that's where the action is. So what happens is that the international bad guys move to wherever the oldest floating crap game in New York has moved.

And the jurisdictions that Mr. Rijock talked about are among the places where they go right now. It changes over the years, but it's always there, and it does move to the jurisdictions that invite it, and they do invite it.

Chairman **LEACH.** Fair enough.

Let me turn to Mr. Baker for a second. You make a rather startling statement in your testimony that 99.9 percent of criminal money presented for deposit in the United States gets into secure accounts, and that twenty-five years of U.S. anti-money laundering efforts are a failure.

That's a very powerful statement. Do you think the new legislation that is outlined by Deputy Secretary Eizenstat is a step in the right direction, or a kind of throwing a small pebble in a big sea?

Mr. **BAKER.** Mr. Chairman, another way of looking at the total problem is in its three principal categories: Criminal, corrupt, and commercial.

We have criminalized certain acts under anti-money laundering legislation. We are now talking about adding the corrupt element to that, and making corruption a predicate offense under anti-money laundering legislation.

We still have hanging out there, the commercial aspect of dirty money. Either under the guise of corruption or the movement of commercially tax-evading money, billions come into the United States, and provide cover for money laundering, which parallels in the same process.

You said my statement was strong. I think the basic idea, the basic fallacy in U.S. policy for some time, has been an effort to control the criminal element, while at the same time, welcoming the corrupt and the commercial elements of these flows.

We are, hopefully, putting the corrupt element into the category of predicate offenses for money laundering purposes.

Ultimately, in order to address the dirty money problem, we have to include the commercial element, the commercial tax evasion that is facilitated through precisely the same paths in the

international financial system.

I said in my testimony that the easiest thing for criminals to do is to disguise their criminal money and make it look as though it is merely corrupt or merely tax-evading. And when they do, we readily receive it.

No, I don't think that we can effectively deal with this problem until we deal with all three parts of it.

Chairman **LEACH.** Interesting. All right, in a recent op ed piece in The Washington Post, a chap named Matthew Brezezinski, who one views as an offspring—I don't know if that's the case or not—of a former Government official, argued that very little of this could have occurred without a lot of advice from sophisticated American professionals.

Do you think that's the case, or have these money launderers figured out things on their own?

Mr. **BAKER.** I don't think it requires sophisticated advice from Americans. On the contrary, I don't think the money launderers have invented any new ways of moving dirty money from one place to another. They have merely stepped into the same positions that have been used by businessmen and bankers in moving flight capital for decades.

Chairman **LEACH.** Would you agree with that, Mr. Rijock?

Mr. **RIJOCK.** I disagree, sir, because without the professional advice, without people with imagination, who are experts in what we call disinformation, old wine in new bottles, coming up with new versions of the old ideas, law enforcement is always two or three steps behind.

You were talking before about the Internet gambling problem, and I have a problem about it, too. As a matter of fact, law enforcement's major question is, is Internet gambling even legal for the purposes of the elements of chance?

In other words, there are a number of unscrupulous types who rig slot machines in the United States. An Internet gambling device, unfortunately, has no checks and balances, and who is to say that the 55/45 split that's common in our gambling industry isn't a 90/10 split in favor of the house?

But let's take Internet gambling to the element of imagination that money launderers do. Why would they be interested in Internet gambling? Because it allows them to mainstream U.S. profits back into the legitimate economy. I'll explain how:

One of the things that people in money laundering do is, they stay up nights and weekends while all you people are home, to dream up new ideas of ways in which to beat you.

One of the things they do is, **they fake accidents, use corrupt doctors, bring millions of dollars coming into the United States from their own captive insurance company to pay themselves tax-free money on a faked injury, and which, as you know, it's compensatory damages**.

They pay nothing to Uncle Sam and they have a $5 million seed capital, and they go out and buy an automobile dealership in Bethesda. The problem with money laundering and the Internet gambling is, all a person has to do is **arrange with an Internet service provider for a very large win, pay United States taxes on this $5 million win, and he had money which apparently was legitimately spun off from a game of chance, and what's going to happen to the proceeds of that money? It's going to be plowed into the United States.**

Any legitimate type of a business that goes on in the United States is perverted by imaginative

people for money laundering purposes. **One of the biggest things that goes on in Puerto Rico is the abuse of their lottery.** This happens to a lesser extent in the continental United States.

Drug traffickers buy the winning lottery tickets at a severe premium. They then come in and say, "Look, here I am. I just won the lottery. I just won $18 million. I know I have to pay 34 percent in taxes, but that's fine; give me my difference."

Right away, I have legitimized and mainstreamed my money back into the civilian economy, and right away, I'm out of the drug business.

So, the problem is that in any legitimate business transaction, there is always a means by which you can pervert it and use it for financial ends. Trust me, the professionals that are involved in this business are all very experienced lawyers, CPAs, tax professionals, people with several degrees, and people with years of experience in their respective professions.

I mean, I **was a bank lawyer,** and I certainly didn't consider that I had any kind of extraordinary talents. There are people who have fifteen and twenty years worth of financial experience out there, drawing sophisticated methods by which the law enforcement community hasn't a prayer of uncovering the tricky trail around the world.

Remember that the problem with money laundering is that it's got three separate and distinct phases, and unless the investigator hits all three of them, there is no way he can get back to the end user. So, yes, professionals do it.

In my **home State of Florida, I regret to say that there are a couple hundred lawyers and CPAs, all of whom have either done Federal time or are doing time now for money laundering crimes. I was just one of them.** Thank you.

Chairman **LEACH.** Mr. Baker.

Mr. **BAKER.** Mr. Chairman, I have never seen a money laundering scheme—and we're talking here about laundering criminal money—I have never seen a scheme for laundering criminal money in which I have not seen very much exactly the same thing done in the commercial world.

The expert advice that you're talking about being given to criminal money launderers is the same expert advice that's being given to people who are tax-evaders and moving corrupt money and what have you.

The money launderers have taken advantage of systems that have been in existence for a long time.

Chairman **LEACH.** Mr. Winer.

Mr. **WINER.** In the Russia context, Mr. Chairman, this is one of the most difficult issues for policymakers, because whenever there were questions about which of this money is money laundering, and which is capital flight, it was impossible to answer the question, because the same infrastructure was used identically for both.

And given the questions about the legitimacy of the sources of funds in Russia, which is particularly murky, it became a very intense ideological issue, because if it's just capital flight, it's the creation of macro-economic conditions and is not something to worry about.

Whereas, if it's money laundering, it's a serious law enforcement issue, and you do have to worry about it.

And there have been years of discussions on that very point, and I think Mr. Baker has illuminated that point very, very well, as has Mr. Rijock, today, about the distinctions that can be drawn. Thank you.

Mr. **RIJOCK.** Mr. Chairman, I just wanted to bring up one point that we haven't yet gotten to, and that is the most important issue about money laundering. Where is all this money right now?

How many hotels in Washington, DC. are owned by narcotics traffickers from Colombia? How many investment vehicles exist in this country which have been perpetuated because of money laundering activities?

Everybody is always in such a hurry to go after the active duty money launderer. He should realize that for every one that we find, there may be 300 who have successfully committed these crimes, and as such, this money has already been mainstreamed or integrated back into the peacetime economy, and as such it can buy power and influence. It can bribe and corrupt people, both in the U.S. and overseas, and it can wield economic influence in any community in the United States.

That should also be a priority. Where is that money now, owned by our major narcotics traffickers? It's not all in hotels in Moscow; there's a lot of it here.

Chairman **LEACH.** Mr. Sherman.

Mr. **SHERMAN.** Thank you, Mr. Chairman. I don't think we'll be able to make money laundering impossible, but we can at least make it risky and make it expensive.

As to making it expensive, it seems that you've described two types of money laundering, those where the money launderer pays the tax and loses a third of the money they're trying to clean; and those where the money launderer does not.

I think it would be particularly difficult for us to stop money laundering where the launderer is willing to pay income tax. There are a whole variety of cash businesses that any fool could run and perhaps lose 2 or 3 percent a year on the money going through.

It's not that hard to lose money in the vending machine business.

And then all you have to do is add cash to that business and it becomes a moneymaking business. All of our tax examiners are there to get you if you under-report your profits.

I don't know how often the IRS looks for the possibility that you're overstating your profits. Likewise, as you gentlemen have pointed out, gambling—and I don't know anybody who can't go into a gambling casino and pretend to make money, whether they do or not, so at least in those cases, taxes are paid.

I want to focus the attention on these tax haven/bank secrecy situations, because here is a situation, first, where I think our European friends have a tradition of accepting tax evasion and bank secrecy to a degree that makes a mockery of the law that they pass for their own books.

They have elections, **they pass laws that are designed to protect working people, middle class people, allocate the wealth, and then they have a system of winking at how very venerable families conduct their financial transactions.**

I don't see how we can deal with the tax haven countries, even if we had an absolute ban on any transactions with any bank or any financial institution in, say, the Cayman Islands or any other country

that had bank secrecy, if the money can be moved from the bank secrecy country to Britain, France, or Germany. We obviously cannot ban financial transactions with Germany.

Do any of you gentlemen have an approach that we could take to cordon off those countries that make a point of—I mean, you know, they install the laundry facilities right there in their financial institutions.

Is there a way for us to respond that would not require the cooperation of the entire business civilized world?

Mr. Rijock.

Mr. **RIJOCK.** Well, Mr. Sherman, we have these rules already and we use them for other reasons. Why do we not trade with Libya, Iraq or Iran? Because those are terrorist countries.

What do we do with those countries? We allow no commerce, one way or the other. We don't even allow our nationals to fly on their airlines into their country.

Why? Because those are terrorist countries.

Well, money laundering happens to be financial terrorism. In all the years that I practiced money laundering—and I did it for ten years—I used to sit out on the veranda in some of these little countries and have a cup of coffee at 6:00 in the morning before I went to the banks, and I used to look out on the horizon.

Do you know what I was looking for? As an old veteran, I was looking for basically, the U.S. military to show up there one day.

Do you know why? Because it's a direct threat to our country.

All of the people that are involved in the offshore services industry, from my own experience, I would say that between 80 and 95 percent of the money in those banks is dirty money.

I know from my own experiences on Anguilla that the number of millions of dollars that I had in one particular bank was more than 51 percent of the total deposits of that bank. And I didn't know about all of the clients of that bank.

My point is that we have to take what we call drastic or radical measures. Nothing short of that will ever work.

The gentleman's agreement about perhaps putting down "in your discretion," well, yes, they're OK, or no, they're not OK; if they are to be called pariahs in the financial world and shut down, and the bank presidents of these banks are to be indicted and tried in Miami for money laundering, and if we're going to make some sort of legitimate commerce in these countries, rather than what's going on, we have to take radical measures.

How do you take radical measures? Well, I'll tell you: There is one other thing these countries have besides financial services, and that is American tourism.

Five days after we cut off American Airlines flying into these countries, and made it impossible for our tourists to go there and spend their money, these people would be at our doorstep, wanting to know what can they do to clean up their financial services industry?

Remember, these islands do not have any manufacturing, any industry, light or otherwise; they are dependent upon financial services and tourism. If you want to break the one, you're going to have to attack the other, in my humble opinion.

Mr. **SHERMAN.** I think you make a point. The concern I would have is, you can probably prevent certain Caribbean islands from continuing to cover money laundering the way they do and tolerate it, but there are countries in the South Pacific that are far away from tourists.

There are little principalities in Europe. There may be—even if there is just one country that chooses money laundering over tourism, because for some reason tourism doesn't work, that would be a problem.

And I want to get to Mr. Winer in just a second, but the problem is compounded by the fact that if we just prohibit financial transactions with a country or two, they can still do their financial transactions with Britain or Germany or whatever, and then move the money here.

Perhaps we could hear from Mr. Winer, first, and then Mr. Rijock.

Mr. **WINER.** This committee is holding hearings, I believe, next month, on the new financial architecture. And one of the issues that is under discussion as part of the new financial architecture is the **possible revisions to the Basle Committee's Risk-Based Capital Accords.**

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There is a market opportunity here, a self-regulatory market opportunity. If the United States, for instance, on its own, or all the members of the Basle group together—and **this proposal is, in fact, in front of the Basle group—were to say "lending from our institutions to an institution based in one of those bad, non-transparent, non-cooperative jurisdictions, is risky, because we don't know what is inside that black box—tax risks, transactional risks, institutional risks, systemic risks, all kinds of risks there—we're going to require a U.S. bank to provision more if it lends to an entity based there."**

Mr. **SHERMAN.** Of course.

Mr. **WINER.** Well, if the major G–7 countries, for instance, were to do that, that would create such a weight against the jurisdictions that were worst regulated by the operation of the forces of the marketplace, by **making lending to them more expensive**, that they would relatively quickly, I believe, improve their standards to international norms in order to avoid the impact of the fact that nobody wanted to use them because it was too expensive.

Mr. **SHERMAN.** I would doubt that these money laundering countries need to borrow money. The amount of capital flowing into these countries—why would——

Mr. **WINER.** It's not for sovereign borrowing.

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Mr. **SHERMAN.** Or commercial enterprises. There's more than enough——

Mr. **WINER.** Long-Term Capital Management was based in the Caymans. If there was a determination made that the Caymans' system had one embedded risk in it, because it was less transparent than the system that would apply to transactions onshore, and if Long-Term Capital's lenders were told they had to put aside further provisions for lending to Long-Term Capital, if it was based in the Caymans, that would be a disincentive for Long-Term Capital to be based in the Caymans, because it would make its lending more expensive.

So this is not directed at the jurisdictions; this is directed against the entities that would be based in

these jurisdictions.

Mr. **SHERMAN.** So even if there is enough dirty money to finance every hotel built in the Cayman Islands, the financial institutions like Long-Term Capital that are borrowing money in Europe to invest it in other places, would be—and the other thing I said, I began my comments by saying that we can't end money laundering, but we can make it more risky and more expensive, and I think your suggestion, at a very minimum, makes it more difficult or more expensive.

Mr. **WINER.** This suggestion was articulated by Secretary Rubin last April in a speech he made, I think, at SAIS. That was the first time that I encountered it. I read it and thought it was very, very interesting, and I think it was a direct response, probably, to Long-Term Capital Management, but it has implications for the money laundering area as well.

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It would simultaneously raise the cost of doing business in those jurisdictions and create a name, blame, and shame approach, which made them less attractive jurisdictions, so, therefore, would want to increase their standards in order to get out of being on a bad list.

It's market-based, and you can do it unilaterally by direction to your own bank regulators, or you can do it multilaterally as a result of concurrence among the Basle Group in Switzerland.

Mr. **SHERMAN.** I hope it's an idea that we pursue with the appropriate legislative vehicles here.

I realize that the Chairman has been extremely indulgent.

Chairman **LEACH.** I'm happy to continue.

Mr. **RIJOCK.** Mr. Sherman, I'd be willing to respond to your question. If I'm only talking about closing down the tax havens in the Caribbean, why am I happy about that?

Well, let's not let the Bank of New York case distract us here. The Bank of New York case is an example of the use of our financial institutions to move cash through the worldwide banking system.

However, most people involved in criminal activity do not use our banking system in the common manner, because they know about our reporting requirements.

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The large percentage of narcotics traffickers and other criminals in the United States have avoided the banks in the past couple of years like the plague. Where do they go? They go to the non-bank financial institutions that are unregulated.

They go to through the efforts to smuggle bulk cash—and that's the other law—out of the country, because there is no record. It's the old, "take the money and run."

We have a logistical issue here. From Miami, it's two-and-a-half-hours to the tax havens of the Caribbean. It's also two-and-a-half-hours to Bogota. It's several hours from anywhere in the United States to the Asian tax havens and the European tax havens, and it exposes the traffickers to interdiction and arrest.

The reason they go to the Bahamas, the reason they go to all the tax havens in the East Caribbean is because the law enforcement in that area is minimal, at best, if it's not U.S., and they have much more safety and security in operating there.

That's why I would be happy to shut down the Caribbean tax havens and then work on the others from a different and less drastic viewpoint. Thank you, sir.

Mr. **SHERMAN.** I would point out how disappointed I was that **the CBI, the Caribbean Basin Initiative, providing massive trade benefits to Caribbean countries, did not address this issue in any adequate way.**

We're in the process of providing trade benefits to countries that shelter drug profits, but that's a different piece of legislation. I yield back.

Chairman **LEACH.** Thank you very much. Following a little bit with what Mr. Winer was saying, with just a slight correction. **Long-Term Capital Management is headquartered in Connecticut. It's incorporated in Delaware, but its funds were established in the Caribbean.**

To add on to the Secretary's point, some of this, frankly, coming from Congress, as suggestions of the Executive Branch, but there is a huge legal risk implicit in that part of the world, if a fund like this had gone under. That was never compensated for.

Ironically, there is a new factor that Long-Term Capital Management brought onto the scene that no one has ever contemplated, and I call it "central bank risk."

That is, it was the central bank of the United States of America that determined that it should intervene in a given kind of way. I asked the Chairman of our central bank, a man named Mr. Greenspan, if he'd consulted with the Central Bank head of the island to which this fund was established, and he indicated that he had not.

But the point is that there are lots of risks associated with this kind of lending that I think should be accounted for. But, on the other hand, as Mr. Sherman indicated, Long-Term Capital Management is not a unique kind of institution and there are others like it. But lots of the activities down there are simply transferring operations involving fees from U.S. banks that are clearly of a profit-making variety for the American institution, and the tax avoidance opportunity for American institutions for certain things they go down there for.

From a safety and soundness perspective, they enhance certain institutions, perhaps at the detriment of the national interest. But they certainly enhance the institutions.

So you put the regulator at a cross purpose with safety and soundness for an institution, vis-a-vis what might be the American national interest.

We have looked at, and several times it has been raised in the testimony today, these distinctions between tax avoidance as somehow being of lesser significance than public corruption.

But we have tax avoidance in the United States, as we all know, and we have this irony in the last several weeks that we have a dispute with the European community on a tax avoidance scheme using these islands that we're trying to defend, at the same time we're saying that we want to crack down on tax avoidance.

And it puts our Government in an awkward theoretical position, but something that I think that this Congress has a lot of reason to be concerned with.

Now, in this particular committee, we have no jurisdiction over tax policy, and so it's beyond our realm of direct impact, at least on a discretionary basis, of issues coming from the committee.

But one of the circumstances that has come to light is always the argumentation that if other jurisdictions don't abide by the rule of law to the same degree that we do, we're disadvantaged as a society. That applies to tax policy as well as all sorts of other policies.

And that comes back to several of the remonstrations of this panel that multilateralism is a technique that ought to be among our concerns at all times.

I just think it's one of the great issues of democracy in the world today, how governments govern. If you develop techniques to avoid certain responsibilities and other societies have them, therefore for a given kind of equity, our society should develop them, or given companies within our society should develop them.

And it would be far better if we just precluded them in their entirety. Then the challenge becomes, for a country like Russia, where tax avoidance is apparently the norm at all levels of society, how to develop a tax structure that is credible enough for people to want to obey it, and not only a tax structure, a government that doesn't steal.

Whatever the tax structure, if you think your taxes are going to go for the theft of a few oligarchs, what incentive do you have to pay?

And that is a challenge for that type of society that is rather seminal. But I'm concerned that because these things exist abroad, you get the impelling aspect that our society might have to copycat. And that is a really profound concern that Russian techniques come to be matters of course for the United States.

And then that when you look at the sums of money that are being developed. They are not trivial. We have in our country, prided ourselves in very small conflicts of interest.

But, it looks as if the criminal nature of other societies is orchestrating sums of money that could well be tempting in an American political system.

Clearly, they have had some sway in the American professional class, and this is partly the case because we pride ourselves that everybody deserves representation, and that criminals deserve representation just as non-criminals.

But I personally think that is something that our professionals are going to want to really think through, whether they want to identify with thugs and thugging techniques.

Mr. Sherman.

Mr. **SHERMAN.** Mr. Chairman, just in response to your comments, I think we should draw a sharp distinction between tax evasion and tax avoidance. A tax avoidance is often very transparent. It is reducing one's taxes in a way sanctioned by that country's tax code.

You pointed out the foreign sales corporations that do involve establishing a basically shell entity, as I understand them, in an offshore jurisdiction. But there, that is not evasion. It is not secret, and is, in fact, reducing one's taxes in a way that has the support of this Congress when they passed the foreign sales corporations provisions.

I realize we can all wonder whether every provision of our code is well designed, but I think that we should not mix evasion and avoidance in talking about the issue of money laundering.

Chairman **LEACH.** Well, I think the gentleman makes a fair point from a legal or moral sense, that the distinction between evasion and avoidance is very real.

From a public policy sense, though, I think we're all obligated to review the issues, and determine whether we want to have as much avoidance in the statute as we currently do.

But certainly from a participant's perspective, there is a radical difference. We have to respect anyone that obeys the law. That is something that is real.

Anyway, let me thank you all. I'd like to ask unanimous consent that Members be given three days to submit questions in writing. We have several requests from Members who might want to write a letter. You are non-public witnesses, but to the degree that a letter is sent to you, I would certainly appreciate your giving it some attention.

And, Mr. Winer, I would also like to suggest—and actually to any of our panelists—we're looking at some legislative approaches to Internet gambling, and perhaps you'd be willing to respond to some questions we might have for you on that subject, and to all of you.

Mr. **WINER.** Yes, sir.

Chairman **LEACH.** Thank you very much. This brings to an end this particular hearing, and it is adjourned.

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[Whereupon, at 2:22 p.m., the hearing was adjourned.]