

Petition to the Delaware Attorney General To Investigate the Delaware Limited Liability Company Act

The Delaware Coalition for Open Government (DELCOG), the Civic League for New Castle County (CLNCC), and other Delaware organizations petition the Delaware Attorney General to appoint an Independent Counsel to examine the language of the Delaware Limited Liability Company Act (the Act) for the purpose of identifying provisions that facilitate the fraudulent formation and use of Delaware limited liability companies (LLCs) as fronts to commit crimes. Thereafter, the Independent Counsel should recommend amendments to the Act for the purpose of preventing and deterring criminal activities that are enabled by the appearance of being a legitimate Delaware company. As part of the analysis, the Independent Counsel should make recommendations for amendments to provisions of the Act that address the issue of separation of liability of a Series Limited Liability Company that permits series LLCs to escape the responsibilities for the debts and obligations of sub-entities within the series.

The stated purpose of a Delaware LLC

The signatories to this petition are not opposed to legitimate use of Delaware LLCs that assist small business owners or promote business development. We are, however, opposed to the misuse of LLCs. The stated purpose of a Delaware LLC is to conduct a legitimate business, as described in the Delaware Limited Liability Company Act, 6 Del.C.18-106:

“(a) A limited liability company may carry on any lawful business, purpose or activity . . .”

The Act, however, has evolved to allow secrecy and is now enabling crimes

The local and national press have reported activity contrary to the purpose of the Act: a pattern of crimes facilitated by Delaware limited liability companies, including:

- 1) money laundering.¹
- 2) narcotics trafficking.²
- 3) embezzlement.³
- 4) bribery.⁴
- 5) securities fraud.⁵
- 6) prostitution.⁶

1. Ed Leefeldt, “How ‘shell’ companies launder dirty money, *CBS News MoneyWatch*, September 8, 2016, <https://www.cbsnews.com/news/how-shell-companies-launder-dirty-money/>; Margie Fishman, “Mueller: Manafort, Gates laundered Ukrainian money through 9 Delaware LLCs and corporations,” *The News Journal*, November 1, 2017, <https://www.delawareonline.com/story/news/2017/10/31/mueller-manafort-gates-laundered-ukrainian-money-through-9-delaware-llcs-and-corporations/818426001/>.

2. Antonio M. DelGado, “U.S. sanctions Venezuelan vice president, accuses him of being a drug kingpin,” <http://www.miamiherald.com/news/nation-world/world/americas/venezuela/article132494809.html>, *Miami Herald*, updated February 14, 2017; Andrea M. Gacki, “Sanctions Actions Pursuant to the Foreign Narcotics Kingpin Designation Act,” *Federal Register*. The Daily Journal of the United States Government, February 17, 2017, <https://www.federalregister.gov/documents/2017/02/17/2017-03209/sanctions-actions-pursuant-to-the-foreign-narcotics-kingpin-designation-act>.

3. Karl Baker, “Documents: Delaware LLCs tied to Malaysian embezzlement,” *The News Journal*, July 20, 2016, <https://www.delawareonline.com/story/news/2016/07/20/court-documents-delaware-llcs-involved-malaysian-embezzlement/87341712/>.

4. Karl Baker, “Delaware LLC involved in international bribery scheme,” *The News Journal*, August 1, 2016, <https://www.delawareonline.com/story/news/2016/08/01/delaware-llc-involved-international-bribery-scheme/87917910/>.

5. “SEC Charges Operators of \$1.2 Billion Ponzi Scheme Targeting Main Street Investors,” *U.S. Securities and Exchange Commission*, <https://www.sec.gov/news/press-release/2017-235>, December 21, 2016; Karl Baker, “SEC fraud investigators demand to know who is behind Delaware LLCs,” *The News Journal*, December 1, 2017, <https://www.delawareonline.com/story/money/business/2017/12/01/sec-fraud-investigators-demand-know-who-behind-delaware-llcs/908586001/>.

6. Office of Public Affairs, “Justice Department Leads Effort to Seize Backpage.Com, the Internet’s Leading Forum for Prostitution Ads, and Obtains 93-Count Federal Indictment,” *Justice News*, <https://bit.ly/2MnCr0C>.

7) facilitation of online child sex trafficking.⁷

Moreover, it is a salient fact that money laundering and foreign (offshore) ownership of LLCs often are common denominators in combination with these other crimes. Greater transparency would be in the public good.

Abuse of the Delaware Limited Liability Company Act

Delaware's tarnished reputation discourages sustainable and ethical economic development.

- The media have cited Delaware LLCs repeatedly for shady operations, including not only money laundering and child sex trafficking, but also payoffs and influence peddling.
- Federal agencies have investigated the pattern of crimes committed by bad actors that formed Delaware LLCs as fronts for their illicit activities.
- Perpetrators' use of LLCs as shell companies for the pass-through of money from one financial institution to another dodges the requirements of the Patriot Act⁸ and interferes with federal efforts to counter money laundering and the financing of terrorism.

LLCs are not transparent, and they attract criminal enterprises whose members wish to remain anonymous. Through years of legal engineering, the Act has evolved and, contrary to the purpose of law, is now clearly enabling crimes.⁹ Since hundreds of thousands of secretive LLCs are now formed in Delaware, and since minimal documentation is required by statute,¹⁰ the Act fosters anonymity on a grand scale. As stated in an article on the website of the Sunlight Foundation – “Why are there so many anonymous companies in Delaware?” – “[Delaware] happens to be one of the easiest places in the world to set up an anonymous company, making it a great place to establish an LLC to do business that you don't want anyone to know about or you don't want to be easily connected to.”¹¹

A position from individuals or institutions that securing tax revenue is justification for maintaining a law that enables criminal activity is not acceptable. The State of Delaware's failure to investigate the flagrant abuses of the Act and to formulate a comprehensive plan to solve the problems could be interpreted as a breach of public trust. The abuses of the Act should be addressed.

Two examples of audacious abuse of the Limited Liability Company Act

In February 2017, after a multiyear federal investigation, two Delaware LLCs were included on the U.S. Treasury's Office of Foreign Assets Control (OFAC) Specially Designated Nationals and Blocked Persons List of sanctioned persons, groups, and companies that are threats to the United States. The two companies are 200G PSA Holdings LLC (its Gulfstream 200 corporate jet, tail number N200VR, was targeted separately by OFAC) and Agusta Grand I LLC, both classified as specially designated narcotics trafficking kingpins.¹² Their principals are two Venezuelan nationals, one of whom is the vice

7. Margie Fishman, “World's top online brothel' is Delaware company in 'good standing,’” *The News Journal*, February 9, 2018, <https://www.delawareonline.com/story/news/2018/02/09/worlds-top-online-brothel-delaware-company-good-standing/308732002/>; Esteban Parra, Josephine Peterson, Margie Fishman, “Sex marketplace website Backpage.com, a Delaware LLC in 'good standing,' seized by feds,” *The News Journal*, April 6, 2018, <https://www.delawareonline.com/story/news/local/2018/04/06/sex-marketplace-backpage-seized-feds/494868002/>.

8. “Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism,” *The USA Patriot Act: Preserving Life and Liberty*, October 26, 2001, <https://www.justice.gov/archive/ll/highlights.htm>.

9. Leslie Wayne, “How Delaware Thrives as a Corporate Tax Haven,” *Business Day, New York Times*, <https://www.nytimes.com/2012/07/01/business/how-delaware-thrives-as-a-corporate-tax-haven.html>, June 30, 2012.

10. <http://delcode.delaware.gov/title6/c018/sc01/index.shtml>.

11. <https://sunlightfoundation.com/2016/04/06/why-are-there-so-many-anonymous-corporations-in-delaware/>.

12. Resource Center, “Kingpin Act Designations; Publication of Counter Narcotics Sanctions-related Frequently Asked Question,” *U.S. Department of the Treasury*, February 13, 2017, <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20170213.aspx>.

president of Venezuela,¹³ a “Senior Foreign Political Figure” and thus subject to oversight pursuant to the Patriot Act.¹⁴

These limited liability companies were formed in Delaware, having the appearance on the Division of Corporations website as “mom-and-pop”¹⁵ domestic companies.¹⁶ In addition, pursuant to the Foreign Narcotics Kingpin Designation Act, anyone who conducts business with a narcotics trafficking kingpin on the OFAC sanctions list is subject to a \$1.4 million civil monetary penalty.¹⁷

An applicant who executes a Delaware LLC certificate of formation, which states the LLC “may carry on any lawful business, purpose or activity,”¹⁸ and then misuses the LLC by engaging in a criminal enterprise should be deemed guilty of committing fraud against the State of Delaware. Perpetrators of fraud should be prosecuted by the State. Future actions by Delaware’s Department of Justice should become an investigative priority of the Independent Counsel and should include recommendations for levying criminal monetary penalties, cancellation of business entity registrations, and disclosure of evidence supporting those recommendations and actions.

A major barrier to proposed legislation to prevent abuse of the LLC Act

We believe it is important that these issues be investigated by an Independent Counsel, free from conflicts of interest, because in recent years the legislative process of proposing amendments to the Act (the “process”) has been controlled by the Section of Corporation Law (SCL) of the Delaware State Bar Association.¹⁹

The sway of the SCL over “the process”²⁰ has resulted in opposition to and blocking of independently proposed legislation intended to make it more difficult for LLCs engaged in criminal conduct to be registered in Delaware, as documented in the June 14, 2017, minutes of the House Judiciary Committee hearing on House Bill 57 (a bill to reform the Act).²¹ Because House Bill 57²² did not go

13. “Treasury Sanctions Prominent Venezuelan Drug Trafficker Tareck El Aissami and His Primary Frontman Samark Lopez Bello,” *U.S. Department of the Treasury*, February 13, 2017, <https://www.treasury.gov/press-center/press-releases/Pages/as0005.aspx>

14. *Financial Crimes Enforcement Network (FinCEN)*, *Department of the Treasury*, “Fact Sheet, Section 312 of the USA Patriot Act Final Regulation and Notice of Proposed Rulemaking,” December 2005, <https://www.fincen.gov/sites/default/files/shared/312factsheet.pdf>.

15. *Investopedia*, [financial education website defines “mom-and-pop business”: a colloquial term for a small, independent, or family-owned business], <https://www.investopedia.com/terms/m/momandpop.asp>; Cited in Governor Carney’s “Budget Reset: A Balanced Approach,” n.d.

16. *State of Delaware*, Department of State: Division of Corporations, accessed June 19, 2018, <https://icis.corp.delaware.gov/ecorp/entitysearch/namesearch.aspx>.

17. David A. Lebryk, “Implementation of the Federal Civil Penalties Inflation Adjustment Act,” Office of Foreign Assets Control, U.S. Treasury *Federal Register, Rules and Regulations*, Vol. 81, No. 127, July 1, 2016, https://www.treasury.gov/resource-center/sanctions/Documents/fr81_43070.pdf.

18. Delaware Code: O6 Del.C.18-106 (a), <http://delcode.delaware.gov/title6/c018/sc01/index.shtml>.

19. Delaware State Bar Association: Corporate Law, “About the Section of Corporation Law,” Accessed June 22, 2018, <https://www.dsba.org/sections-committees/sections-of-the-bar/corporation-law/>.

20. Richards Layton & Finger, for example, proclaims on their website: “We have Delaware’s largest and most active alternative entities practice, and we are acknowledged leaders in the development of Delaware limited liability company, limited partnership, and general partnership law. Our attorneys were actively involved in drafting the Delaware Limited Liability Company Act, the Delaware Revised Uniform Limited Partnership Act, and the Delaware Revised Uniform Partnership Act, and two of our directors serve on the committee of the Delaware State Bar Association responsible for proposing amendments to these laws.”

<http://www.rlf.com/Practices/LimitedLiabilityCompanyandPartnershipAdvisory>.

21. See attached: House Judiciary Committee Hearing on HB 57, June 14, 2017.

22. *Delaware General Assembly, House*, House Bill 57, 149th General Assembly (Present), 2018, “An Act to Amend Title 6 of the Delaware Code Relating to Limited Liability Companies,” Accessed June 19, 2018, <https://legis.delaware.gov/BillDetail?legislationId=25430>.

through “the process,” there was a motion to table the bill. The motion carried. The minutes of this committee hearing show that adherence to “the process” trumps consideration of amendments to reform the Act independently proposed by legislators without the prior approval of the Section of Corporation Law. As quoted from pp. 2-3 of the hearing minutes, which are attached in their entirety:

*Chair [Rep. J. Larry] Mitchell introduced **HB 57, AN ACT TO AMEND TITLE 6 OF THE DELAWARE CODE RELATING TO LIMITED LIABILITY COMPANIES.***

Rep. [John] Kowalko, the bill's prime sponsor, read from a prepared statement that can be found at the end of these minutes. He said HB57 would prevent the use of Delaware's Limited Liability Act by persons and nations identified by federal agencies as a threat to the U.S. . . .

Vice-Chair Smith [Rep. Melanie George Smith]²³ asked Rep. Kowalko if the bill had gone through the Delaware State Bar Association's Section of Corporation Law.

Rep. Kowalko replied no.

Vice-Chair Smith said that she was concerned about this because the correct process was not followed. She said that when the General Assembly wants to take up legislation dealing with corporations, it takes the recommendation of the Section of Corporation Law. This organization is comprised of some of the state's best lawyers who vet all legislation that goes through it. She added that this process sends a message of stability across the world. She concluded by saying she could not support HB 57. . . .

On the surface, “the process” of releasing from committee only those bills recommended by “the state's best lawyers” in the Section of Corporation Law might seem reasonable. It should be recognized, however, that the Delaware State Bar Association's Section of Corporation Law is *not* a public body. Its members are neither reviewed nor approved by the Delaware legislature or by any other state agency.

The interests of corporate law firms may not always coincide with the best interests of the Delaware public, including consumers and the honest owners of small businesses registered as Delaware LLCs, whose reputations are being tainted by the increasingly frequent revelations about criminal conduct perpetrated by bad actors using the secrecy provided by the Delaware LLC Act to facilitate their activities (see footnotes 1 – 12 and 22).

Moreover, Vice-Chair Smith's statement that “the process sends a message of stability across the world” is debatable. Transparency International, a noted global coalition (in more than 100 countries) against corruption, describes Delaware as “a place where extreme corporate secrecy enables corrupt people, shady companies, drug traffickers, embezzlers and fraudsters to cover their tracks when shifting dirty money from one place to another. It's a haven for transnational crime.”²⁴ Is this the ethical stance and the resulting reputation that Delawareans collectively – citizens, business leaders, public officials – want our state to have?

The “process” of proposing and approving amendments to Delaware's LLC Act should not be controlled entirely by the Section of Corporation Law. The Delaware Attorney General's Office also should play an active role in proposing and reviewing amendments to the LLC Act that will prevent the ability of bad actors to conceal criminal enterprise in their corporate activity.

23. “Melanie George Smith, an attorney at Richards, Layton & Finger, began her career practicing in the firm's business and alternative entities department.”

<https://www.globalreporting.org/information/events/reportersummit/Pages/Speakers.aspx>

24. *TransparencyInternational.org*, “Delaware: The US Corporate Secrecy Haven,” Accessed June 21, 2018, https://www.transparency.org/news/feature/delaware_the_us_corporate_secrecy_haven.

The Delaware Attorney General's Mandate

The Delaware Attorney General's mandate is to protect the public, as described on the Attorney General website: "Delaware's Attorney General, the State's chief law enforcement officer, has broad responsibility to combat crime, safeguard families, fight fraud, and protect consumers in the First State."²⁵

The Delaware Attorney General has the authority to appoint an Independent Counsel, free of conflicts of interest, to investigate crimes and corruption. For example, in 2011, Delaware Attorney General Beau Biden appointed an Independent Counsel and Special Deputy Attorney General to investigate Delaware campaign finance corruption. This investigation resulted in the Report of Independent Counsel on Investigation of Violations of Delaware Campaign Finance and Related State Laws.²⁶

Appointing an Independent Counsel appears to be the most effective means of addressing these issues. Neither denial nor laxity nor timing should be an option that distracts the Office of the Attorney General from addressing the issues described in this Petition.

Therefore, DELCOG, CLNCC and all of the Delaware organizations who are signatories to this petition request that the Delaware Attorney General appoint an Independent Counsel, free of conflicts of interest, to accomplish the following:

- Study the language of the Delaware Limited Liability Company Act for the purpose of identifying provisions that facilitate the misuse of Delaware limited liability companies as fronts to commit crimes.
- Investigate the issues of fraud against the State committed by bad actors that form LLCs to commit crimes, prosecute when criminal liability is assessed, and levy monetary and other appropriate penalties.
- Make recommendations for amendments to provisions of the Act that address the issue of separation of liability of a Series Limited Liability Company that permits series LLCs to escape the responsibilities for the debts and obligations of sub-entities within the series.

Respectfully submitted,

Delaware Coalition for Open Government
 Civic League for New Castle County
 League of Women Voters of Delaware
 Delaware Press Association
 Pacem in Terris
 American Promise Delaware
 Delaware Get Money Out
 Network Delaware

25. *Delaware.gov*, Delaware Department of Justice: Attorney General, "About the Office," Accessed June 20, 2018, <https://attorneygeneral.delaware.gov/about/>.

26. E. Norman Veasey and Christine T. Guglielmo, "Report of Independent Council on Investigation on Violations of Delaware Campaign Finance and Related State Laws," Delaware State Bar Association, December 28, 2013, http://media.dsba.org/pdfs/Chief_Justice_Veasey_Report.pdf.