Statement of
ANTONIO GIRALDI
Before The
U. S. Senate Permanent Subcommittee on Investigations
Hearings On
Private Banking and Money Laundering:
A Case Study of Opportunities & Vulnerabilities
November 10, 1999

My name is Antonio Giraldi. I graduated from Culver Military Academy, Culver, Indiana, in 1975; from Baylor University, Waco, Texas, with a B.A. in 1979; and from Georgetown University, Washington, D.C., with an M.A. in 1981. I began my banking career at the Bank of America in 1981 in the International Management training program, where I became a corporate banking officer and, later, a credit review officer for Latin America. In 1984, I was recruited by Riggs Bank in Washington, D.C., to work in the International Division, and in the fall of 1986 I was recruited to join Citibank's Private Banking team in New York City. In 1988, I accepted a position as Vice President/Country Manager for Mexico Private Banking at Bankers Trust, and I joined American Express Bank in 1990 as a First Vice President and Marketing Group Head for International Private Banking in Beverly Hills, California. This written statement is based on my personal experiences, and those of my many former colleagues and friends, in the banking industry.

A historical overview of the private banking industry will help put my remarks into perspective. For much more than a century, private banking was the mainstay of European banks, which managed, with absolute privacy, the assets (currency and specie) and investments of select clients, most of whom possessed political, business, and social status uniformly recognized and accepted within the European community of nations. The experienced European banks exploited the generation of new wealth in the emerging republics, as well as the simultaneous revolutionary developments in communications and transportation, by establishing what we know today as International Private Banking ("IPB"). In so doing, they replaced the concept of "privacy" in their client relationships with the concept of "*secrecy*." Foremost in this field were the Swiss banks, who had the advantage of being domiciled in a politically neutral and stable country. Swiss banks, which actively promoted "numbered accounts" as a marketing tool, obtained billions in deposits of foreign origin. These deposits, which, as circumstances dictated, were kept in liquid assets or invested, generated substantial earnings for the banks. At one point, the inflow of funds was such that the Swiss banks charged *negative* interest on deposit accounts.

IPB clients were motivated to establish their banking relationships for a variety of reasons, both legitimate and illegitimate. These reasons included concealment of assets, tax avoidance and/or evasion, estate planning concerns, avoidance of foreign exchange controls, fear of currency devaluation, fear of confiscation resulting from political upheaval, concealment of ill-gotten gains by corrupt political figures, and concealment of ill-gotten proceeds of illegal activity. Although IPB provides entirely legal and valuable services for its legitimate clients, IPB's

increasing accessibility to the criminal elite and vulnerability to their illegal money laundering objectives have cast a dark shadow on the industry. Foreign political figures, military leaders, and their families and close associates have established substantial IPB relationships, many using funds that were later identified publicly as "tainted." The sources of these extremely profitable IPB deposits, in most cases, were neither requested nor challenged, consistent with the IPB industry's well-developed atmosphere of "quiet, respectable exclusivity and confidentiality" (*i.e.*, "secrecy"), an atmosphere specifically designed, projected, and maintained in order to encourage the ever-increasing and quasi-permanent volume of IPB deposits.

The United States banking community recognized private banking as a desirable and profitable source of business and ventured into IPB as a new market. This decision proved sound, as the potential market in IPB grew to trillions of dollars. The IPB clientele courted by United States banks consisted primarily of customers already served by, or at least familiar with, the services offered by the European banks. To be competitive, United States banks had to extend, and/or improve upon, the treatment and services IPB clients had come to expect from foreign banks in return for the promise of their deposits. A description of the more common products employed by IPB groups at United States banks is attached to this statement as Exhibit "A."

In the 1980s and early 1990s, with money laundering awareness in its infancy, compliance and due diligence procedures were not fully effective. Training for Relationship Managers ("RMs") was limited, and focused on cash transactions in response to regulatory and law enforcement requirements, but that training did nothing to change the IPB "culture" or its product base, which were becoming the primary tools for sophisticated criminals to manage the proceeds of their criminal activities. When the United States' regulatory framework of tightened controls would not permit the same degree of secrecy and tax flexibility enjoyed by many of the United States banks' foreign competitors, the United States IPB groups moved offshore, using island "tax" havens where prevailing legal and regulatory structures made possible the same treatment for IPB deposits as that offered by competing foreign banks. Offshore facilities are now used by European banks as well.

RMs were taught by their superiors that secrecy in IPB transactions was paramount. The obsession with secrecy went far beyond the United States banks' imaginative use of offshore banking "tax" havens. RMs often posed as tourists and were encouraged to travel on tourist visas when visiting foreign clients abroad. RMs and their clients were encouraged to speak in "code" during business-related telephone conversations, and RMs carried account statements that had been reduced in size to avoid being recognized by foreign customs officials for what they actually were. United States financial institutions marketed to IPB clients from offices located abroad and refused to share client information with staff and personnel in their domestic offices. Trust officers continually admonished RMs who inadvertently cross-referenced or otherwise linked their clients' names (the names of the beneficial owners, that is) with the offshore financial structures used to manage those clients' assets. RMs were told that it was not their responsibility to determine whether or not an IPB client had complied with the laws and financial regulations of his/her home country. RMs were far more concerned with "appearance" than with

"substance" when it came to issues of due diligence and what would later become the Know Your Client ("KYC") doctrine. If an "acceptable" level of due diligence could be fashioned with the guidance and encouragement of senior management, then the RM had done his/her job. No RMs known to me consciously attempted to legitimize what was known or believed to be proceeds of specified unlawful activity, but no one *seriously* attempted to determine the *actual* origin of a client's money. Our world (the IPB "culture," that is) was all about playing the "new deposits" game the way our senior management "coaches" insisted we play it, about being rewarded by them when we "succeeded," and about being too naive to realize how dangerous a game we were playing.

Money launderers who are beneficial owners of billions of dollars are aggressive, intelligent, and streetwise individuals who have built successful criminal enterprises. Their wealth is used to purchase legal industries as well as corrupt branches of governments that can be used to their private advantage. They have also learned to use "third parties" to accomplish many of their illegal endeavors. The perceived legitimacy of these "front persons," who typically have no known prior criminal affiliations, helps them manage the vast financial holdings entrusted to them. Ironically, the beneficial owners of tainted IPB assets, and their "front persons," have been encouraged by the financial institutions which hold their assets to "layer" them (the assets) with financial structures which further conceal their true origin and ownership. IPB groups and senior bank managers played the lead role in creating the IPB "culture," where each additional layer of "structure" generates additional earnings for the financial institution, and generates another layer of "exclusivity" (the functional equivalent of "anonymity") for money launderers. United States financial institutions often fire, hire, sell, and/or purchase entire IPB teams, and sell or purchase IPB portfolios. Large banks purchase and/or merge with other financial institutions in order to create mega-institutions. Similar to another layer of financial "structure," each of these types of events also provide opportunities for a sophisticated money launderer to avoid law enforcement scrutiny.

The IPB industry, worldwide, evolved from the substantial flow of funds from non-United States residents, and, in large part, from the geometric growth of the illegal drug industry and the "narco-wealth" it generated. IPB clients' increasing demands for confidentiality, exclusivity, secrecy, and the use of fictitious names unquestionably should have triggered suspicions that substantial portions of these funds had originated from other-than-legitimate business activities. The massive size of these deposits and the income they generated for United States financial institutions, however, weighed against the application of principles of bank "morality."

As governments around the world followed the lead of the United States government in attempting to combat the drug cartels by seizing the proceeds of their illegal activities, drug traffickers were quick to identify the advantages of IPB for processing their ill-gotten gains. The IPB industry was a ready-made haven for money launderers, who sought to emulate the respectability and legitimacy of the "old money," upperclass clients for whom the industry had traditionally provided its services. Money launderers hurried to acquire the talent and skills necessary to funnel their illicit profits into this financial arena. Needless to say, the quasi-

impenetrable fabric of absolute secrecy in IPB relationships which is the cornerstone of IPB "culture" has impeded the efforts of law enforcement agencies everywhere. IPB "culture," reinforced by the Bank Secrecy Act and similar legislation in other countries, has often defended itself with the rationale that "banks should not be obliged to act as law enforcement entities."

The objectives of most money launderers are to legitimize their financial holdings, to gain acceptance to the hallowed halls of international financial institutions as "trusted and valued" clients, and to receive the attention traditionally lavished on such clients by said institutions' senior managers. Money launderers are frequently credited with authorship of their imaginative financial schemes, but the ultimate responsibility for authorship of these schemes properly rests on the shoulders of the financial institutions and their senior managers. A senior bank manager confronted with an RM's decision not to accept a new IPB client was just as likely to chastise the RM for losing the new client to a competitor institution as to congratulate the RM for protecting the integrity of his/her employer. "IPB" says it all – the word "private" means "secluded from sight, presence, or intrusion of others." Money launderers succeed by simply permitting the IPB "culture," which is driven by senior management's pursuit of profit, to dictate the actions of their respective RMs. Everyone "wins" – everyone, that is, but law-abiding citizens everywhere.

The money launderer has shed his/her conventional image and now wears a "chameleon" cloak provided courtesy of the IPB industry. This fact, coupled with the demise of the recently proposed KYC regulations and the arrival of a whole new generation of cyber-savvy money launderers, has compounded the difficulties faced by federal law enforcement agencies and the United States Department of Justice, and bodes ill for their efforts to combat the evils associated with money launderers and their activities. If the issue of money laundering is to be addressed effectively, United States financial institutions, at every level, *must* interface with federal law enforcement agencies. United States financial institutions *must* effect fundamental changes in the prevailing IPB "culture" and product base. And senior bank managers *must* implement supervisory procedures designed to identify "rogue" RMs who manipulate international financial resources and activities for their own personal gain. As long as United States financial institutions continue to use their IPB groups the way they have for years, the managers of international criminal enterprises will continue to use our highly imaginative and flexible banking system and its products to handle the proceeds of their illicit operations, and to legitimize themselves in the eyes of the international business community. United States financial institutions should no longer succumb to the established yardstick, "If we don't accept this account, one of our competitors will."

COMMON FINANCIAL PRODUCTS UTILIZED BY THE INTERNATIONAL PRIVATE BANKING COMMUNITY

The following products, among others, are commonly used by United States financial institutions to manage the assets of private banking customers:

1. Demand Deposit Account and Savings Account –

These are the traditional accounts available to all. Savings accounts are not commonly utilized due to their limited flexibility and interest yield.

2. Money Market Account (MMA) –

The MMA is an attractive vehicle, earning a higher interest yield than checking accounts, and providing a high degree of flexibility for transfers of funds to and from the account and "parking" of funds pending their subsequent utilization and investment. The amounts involved are substantial. MMAs are attractive to banks because of the minimal expense associated with maintaining them. Relationship managers (RMs), with preestablished authorization from their clients, can readily make charges to MMAs for transfers to other accounts, investments, payments of bank fees, and credit card billings, as well as for payments of expenses incurred by their clients outside the bank. MMAs can also be held in the name of PICs (see 4. below).

3. Time Deposit (TD) –

These fixed maturity instruments are often used by conservative clients venturing into a private banking relationship for the first time, and prior to becoming familiar with the full range of available investment options offered by the bank. Fees are not typically charged for establishing TDs.

4. Private Investment Company (PIC)/Trust –

PICs are established via the banks' "offshore" trust companies, and are opened in names other than the clients'. A PIC is administered and managed by the officers of the bank trust company, who typically register as the PIC's officers and directors. Once a PIC has been established, the client's assets are processed in the name of the PIC (as the nominative owner), providing a "layer" of anonymity for the client, who becomes the "beneficial owner." Funds transfers, investments, and other banking services are conducted in the name of the PIC. Additional PICs may be set up in the same or another "offshore" domicile. A client can easily establish a second PIC to administer and manage the assets of his/her first PIC, thereby adding another "layer" of anonymity. PICs generate attractive fees for banks.

Banks' offshore trust companies can also create trusts (which can include PICs among their assets). Many IPB divisions of banks have trust officers domiciled in the United States who interface with their respective "offshore" bank trust companies. These trust officers work extremely closely with RMs in the marketing and structuring of fiduciary vehicles. They also meet with existing and prospective clients to personally identify and review their needs, to sell the bank's fiduciary products, and to generally promote client satisfaction. Extreme caution is taken by the banks' trust specialists to ensure that PIC/trust files, wherever they may appear throughout the bank, are devoid of the beneficial owners' names, and that PIC/trust transactions leave no clues as to the actual identities of their respective beneficial owners.

5. Discretionary Portfolio –

The establishing of discretionary portfolios, a highly profitable activity, is strongly encouraged. Portfolio managers regularly meet with a client and his/her RM to evaluate the client's investment history, risk tolerance, and estate planning requirements. A portfolio is then structured, generally in a PIC and/or trust, to accommodate the client's needs. Once the client consents to a discretionary portfolio, he/she has very little, if any, input into the investment strategy employed for his/her portfolio. Discretionary portfolio investment parameters, however, can be modified as the client becomes better educated or as his/her risk tolerance increases. Equities and fixed income instruments are often purchased in blocks in the name of the financial institution, and then allocated among the various discretionary portfolios under the financial institution's management. Some financial institutions facilitate the establishment of discretionary portfolios in Europe and Asia to enhance confidentiality and investment diversification.

6. Credit –

Lines of credit are almost universally extended to clients. These include loans, letters of credit, and guarantees, any of which can be extended in the name of a client, a company owned and/or controlled by the client, a third party, or a PIC. Credit requests are prepared by RMs and submitted to bank credit officers for their review and approval. In almost all cases, the extensions of credit are 100 percent secured by the assets of the client in question, which results in lower than normal scrutiny of the terms and conditions of the credit, including purpose of loan and borrower source of repayment. These are very attractive (*i.e.*, profitable) products for banks. Clients requesting a partial liquidation of managed assets to generate liquidity are often encouraged to borrow in lieu of disrupting their asset bases.

7. Real Estate –

Several major private banking groups provide real estate products to IPB clients. They utilize real estate specialists within the Private Banking Division to promote real estate products to RMs and to their clients. Specialists representing the bank often purchase commercial property on behalf of a client, and establish domestic and/or offshore PICs to serve as the nominative owners of the property. These specialists will also assist in structuring any financing that is required, and assist clients with property management issues.

It should also be noted that RMs are strongly encouraged to "cross over" to other divisions of their respective banks in order to meet clients' needs. One example of a "cross over" division is the Corporate Division, whose expertise and research can be offered to those clients who express an interest in business acquisitions and/or sales.