The Race Against Los Zetas: How One of The Most Feared Mexican Drug Cartels in History Was Able to Hide Millions in The American Quarter Horse Racing Industry and How the Corporate Transparency Act Could Beat Financial Terrorists to the Finish Line

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“For an illegal enterprise to succeed, criminals must be able to hide, move, and access illicit proceeds—often resorting to money laundering and utilizing the anonymity of shell companies to obscure the true beneficial ownership of an entity.”¹ In other words, for corrupt officials, drug traffickers, terrorists, tax evaders, and other hostile actors, protecting illicit cash in the United States has historically required less than that of a driver’s license.² The existing anti-money laundering regime has traditionally posed several threats to regulators’, law enforcement agencies’, and financial institutions’ ability to identify illicit funding. Consequently, strategic use and abuse of anonymous shell companies has made investigations exponentially more difficult, laborious, and costly.³ However, with the override of former President Trump’s veto of the National Defense Authorization Act and passage of the Corporate Transparency Act effective as of January 1, 2021, criminals will soon lose a significant amount of protection.

The purpose of this article is to address the gap in the American law enforcement system that has not only completely failed to curtail financial terrorism but rather welcome it. In doing so, this article will begin with a brief overview of the structure of shell companies and the attractiveness of their formation to criminals. Next, the article will

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³ D’Antuono, supra note 1.

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highlight the Los Zetas cartel’s use of shell companies within the American quarter horse industry to operate a multimillion-dollar money laundering scheme and the legislative shortcomings that allowed such. The article will then briefly hypothesize differing potential outcomes had laws such as the CTA been in place at the time. Finally, the article will explore how the implementation of the CTA will help to further deter financial terrorists in the future while addressing possible counterarguments to its enforcement and solutions to reiterate its importance and necessity.

I. INTRODUCTION

“For an illegal enterprise to succeed, criminals must be able to hide, move, and access illicit proceeds—often resorting to money laundering and utilizing the anonymity of shell companies to obscure the true beneficial ownership of an entity.” The existing anti-money laundering (AML) regime has posed several threats to regulators’, law enforcement agencies’, and financial institutions’ ability to identify and lessen the use of illicit funding. Consequently, strategic use and abuse of anonymous shell companies has made investigations exponentially more difficult, laborious, and costly.5

As part of the National Defense Authorization Act (NDAA), Congress passed the Anti-Money Laundering Act of 2020 into law on January 1, 2021. One of the legislation’s most significant provisions includes the Corporate Transparency Act (CTA).6 The CTA marks the first significant update to U.S. AML laws in nearly two decades as a bipartisan effort to address the anonymity loophole by requiring businesses in the United States to file “beneficial ownership” information with the Financial Crimes Enforcement Network (FinCEN). In shifting the burden of ownership information collection from financial institutions to companies, the CTA will impose stringent penalties for willful non-compliance and unauthorized disclosures.7

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4 Id.
5 Id.
7 Id.
II. Fatal Attraction

In accordance with the Securities and Exchanges Commission (SEC), a shell company is “a registrant with no or nominal operations and either no or nominal assets, assets consisting solely of cash and cash equivalents, or assets consisting of any amount of cash and cash equivalents and nominal other assets.”

These companies do not create products or provide services nor do they hire employees or generate revenue but, instead, store money and engage in financial transactions. While shell companies typically serve legitimate purposes such as vehicles to raise funds for a startup or to conduct a hostile takeover, they are also frequently misused to facilitate illegal activity by disguising business ownership from law enforcement or the public.

Money laundering is the process of making illegally gained proceeds, or “dirty money,” appear legal, or “clean” and typically involves three steps: placement, layering and integration. First, the illegitimate funds are secretively introduced into the legitimate financial system. Then, the money is moved around to create confusion, sometimes by wiring or transferring through numerous accounts. Finally, it is integrated into the financial system through additional transactions until the “dirty money” appears “clean.” Money laundering can facilitate crimes such as drug trafficking and terrorism and adversely impact the global economy.

As non-traded corporations, shell companies are not listed on any stock exchanges for buying and selling by investors and most exist in name only on paper as a registered financial entity or agent. Under the current AML regime, shell company structures in the United States require simple filing with the SEC and are formed pursuant to state-level requirements. Although required information on officers, directors, and

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11 Id.
managers may vary, no state requires the identity of individuals who ultimately own or control the entities legally formed.\textsuperscript{13} Further, despite decades of legislative efforts, no federal-level systems have existed to consolidate or supplement the information collected by states nor have any federal laws required identification of beneficial owners when opening accounts with financial institutions.\textsuperscript{14} Therefore, U.S. shell companies can legally be set up in a manner that obscures ultimate beneficial ownership and, in turn, establishes a degree of anonymity that can be used to hide illegal funds, evade sanctions, and avoid the AML measures used to detect crimes facilitated by money laundering.\textsuperscript{15} As a result, the known anonymity significantly burdening attempts to uncover true beneficial owners combined with corresponding legal insufficiencies, U.S. shell companies have historically been seen as appealing targets in the eyes of criminals.

III. Effects of Legislative Shortcomings

In its mission to “safeguard the financial system from the abuses of financial crime, including terrorist financing, money laundering and other illicit activity,” the FinCEN acts as the designated administrator of the Bank Secrecy Act (BSA).\textsuperscript{16} The BSA was established in 1970 as the first laws to fight against money laundering in the United States requiring businesses to keep records and file reports determined to have a high degree of usefulness in criminal, tax, and regulatory matters.\textsuperscript{17} Since then, numerous other laws have enhanced and amended the BSA to provide law enforcement and regulatory agencies the most effective tools to combat money laundering.\textsuperscript{18} However, as history has shown, the actual effects of such measures have proven unsuccessful more oftentimes than not.

A. The Treviño Morales Brothers and the Los Zetas Drug Cartel

\textsuperscript{13} D’Antuono, \textit{supra} note 1.
\textsuperscript{14} Id.
\textsuperscript{15} \textit{What is Ultimate Beneficial Ownership?} (April 4, 2015), https://complyadvantage.com/knowledgebase/ultimate-beneficial-owner/ [https://perma.cc/3AN8-YJ4C].
\textsuperscript{16} \textit{FIN CRIMES ENF’T NETWORK} supra note 10.
\textsuperscript{18} \textit{FIN CRIMES ENF’T NETWORK} supra note 10.
The Los Zetas drug cartel (Zetas) began as an enforcement gang for the Gulf Cartel predominantly consisting of former Mexican militiamen. Zetas would evolve for over a decade to become one of Mexico’s most powerful criminal organizations in which the U.S. Drug Enforcement Agency (DEA) described them as “perhaps the most technologically advanced, sophisticated and violent” of its kind. Alejandro Treviño Morales, “Z42,” was a Zetas member and brother to former Zetas leader Miguel Treviño Morales, or “Z40,” who was blamed for some of the worst massacres in Mexico’s drug war. In 2010, the Zetas mercenaries broke away from the Gulf Cartel using its signature violence to build a network of international drug trafficking contacts with reported connections in Venezuela, Europe, the United States, and West Africa. José Treviño Morales (Treviño), third brother to the crime trio, was a U.S. citizen with a far less tainted record. Despite his ‘clean’ reputation as a bricklayer reportedly making only $20,000 per year, in 2011, José seemingly came into a sum of money large enough to draw attention to his entrance into the lucrative American Quarter Horse industry.

Contrary to the toll taken by the recession on the historically lucrative quarter horse industry, one Oklahoma farm was “booming with business.” Treviño had purchased a 140-acre farm along with 522 quarter horses prior to moving his entire family from Balch Springs, Texas, to their new home. Further, despite having entered the industry only a short while before, the farm owner was making waves with his million-dollar prize winnings and record-breaking bids. To the common eye was a legitimate business that bought, bred, and raced American quarter horses instead of the massive multimillion-dollar money laundering scheme that it was. Expounding on the gap crippling the current U.S. AML regime is not only the fact that the Zetas cartel was

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20 Id.
21 Id.
22 Id.
24 Id.
25 Id.
26 Id.
able to continue its extensive illegal activity for so long but that it did so quite literally in plain sight.

The basis of the scheme was simple—drugs would travel north from Mexico while illicit profits earned would travel back south hidden in American shell companies created within the quarter horse industry including the main shell company, “Tremor Enterprises LLC” (Tremor).\footnote{Id.} The brothers in Mexico would purchase and sell vast numbers of race horses from auctions on behalf of and between the shell companies through transactions from Bank of America accounts to make the illicit deposits of drug money appear legitimate.\footnote{D’Antuono, supra note 1.} Once one of the horses began to win prize money, the brothers would back-date the sale of the horse into the name of the known Tremor entity under Treviño.\footnote{Id.} Treviño would then deposit and effectively “wash” the illicit income by moving funds between the Tremor accounts and a separate personal account to demonstrate personal income from his business in order to disguise the criminal earnings as legitimate transactions.\footnote{Id.}

While banks are required to report suspicious transactions of $10,000 or more to federal officials under the BSA, investigations recovered Bank of America filings showing an estimated dozen transactions between the shell account and Treviño’s personal account totaling $1.5 million.\footnote{Dan Fitzpatrick, Bank Accounts Figure in Drug Probe, WALL ST. J. (updated July 9, 2012), https://www.wsj.com/articles/SB10001424052702303292204577514773605576442 [https://perma.cc/G6YN-JV8G].} This was also not the first time Bank of America had been involved with or admitted to such financial oversight. According to Bloomberg, Mexican drug organizations have allegedly used Bank of America accounts to buy planes to transport cocaine and the bank was also the alleged destination for almost $10 million in illicit funds from an influential political family in Equatorial Guinea between 2004 and

In 2006, Bank of America officials acknowledged they had failed to catch South American clients laundering $3 billion through one of its Manhattan branches, according to The New York Times. Consequently, the unlawful use of U.S. shell companies has relied heavily on the element of transparency or lack thereof. As was the case of the Los Zetas cartel, criminal owners of such companies have and continue to remain anonymous while free to open bank accounts, transfer money, and enjoy the legitimacy of being formed in the United States. Contrary to prior failed legislation, the CTA aims to directly remedy this loophole in the American financial system by flushing out criminals operating in hiding. In effect, disallowing individuals to use shell companies as shields to facilitate crime as the Treviño brothers did will result in the culmination of centralized resources within the federal government to help keep up with criminals taking advantage of U.S. financial systems.

IV. APPLICATION OF THE CORPORATE TRANSPARENCY ACT

A. THE CORPORATE TRANSPARENCY ACT IN GENERAL

On January 1, 2021, Congress passed the National Defense Authorization Act for Fiscal Year 2021, including the Corporate Transparency Act. In sum, the CTA is designed to ban the anonymous shell companies used by criminals to hide, move, and access illicit proceeds by requiring U.S. businesses to file certain information with the FinCEN; most notably regarding “beneficial ownership.” As the first significant update to U.S. AML laws in 20 years, the CTA gives FinCEN significant authority to adopt the necessary regulations to implement its provisions.


33 Id.


37 Id.
B. IMPLEMENTATION OF THE NEWLY DEFINED “BENEFICIAL OWNER” REQUIREMENTS

As previously mentioned, no state or federal laws have existed prior to passage of the CTA requiring identification of the true “owners” of business entities created in the U.S. Thus, allowing criminals to create and operate shell companies without revealing themselves. Among the requirements to create a Limited Liability Company in Texas, for example, is the common filing of a registered agent.\(^{38}\) Under state law, this can be an individual Texas resident or organization registered or authorized to do business in Texas with a business office at the same Texas address as the entity’s registered office that is not a P.O. box.\(^{39}\) The Treviño brothers created and filed the illicit shell companies under several different “straw purchasers” or nominated outside agents except for Tremor which was filed under the legal ownership of Texan José Treviño, front man for the company. Treviño had left Mexico decades before the scheme and his U.S. citizenship combined with never having been outwardly associated with the cartel provided a cover that would help secure illicit assets “without arousing too much federal scrutiny.”\(^ {40}\)

Under the new terms of the CTA, however, companies will be required to report information regarding the entity’s “beneficial owner” now defined as an individual who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise: (i) exercises substantial control over a corporation or limited liability company; (ii) owns 25 percent or more of the equity interests of a corporation or limited liability company; or (iii) receives substantial economic benefits from the assets of a corporation or limited liability company.\(^ {41}\) Given this update in the law, it is possible that José would not suffice as the beneficial owner of Tremor under the CTA and his information acceptable for disclosure. This is evidenced by the peak of the brothers’ scheme in which bettors at the 2010 All American Futurity race in New Mexico watched the long-shot Mr. Piloto gallop to the


\(^{39}\) Id.


million-dollar first prize by less than a nose, the second-closest win in the race’s history. While the horse was registered to Tremor, the money to buy him had come from Miguel. Further, authorities received their first tip from an informant in January 2010 at one of the biggest auctions in the quarter horse industry where a horse named “Dashin Follies” had recently sold for a record $875,000. More important to investigators would have once again been the buyer: Miguel Treviño Morales. The provisions of the CTA would therefore likely have made Miguel the beneficial owner of Tremor given his exercise of substantial control over the LLC and the benefit, though illicit, he was receiving from its operation. In addition to the illusiveness caused by Treviño being named the legal owner is the fact that the wide use of shell companies to facilitate the criminal transactions in both the United States and Mexico made it nearly impossible for banks and investigators to associate the cartel with racehorses and American bank accounts.

Many of the United States’ closest partners require beneficial information in order to detect and prevent illicit finance and those with the most effective AML regimes require documentation of beneficial owners for “legal persons,” generally referring to corporations, trusts, and property, held in a centralized database easily accessible by government agencies. If entity owners in the United States, such as Treviño and the other straw purchasers, were required to disclose beneficial ownership, and this information was made available to regulators and law enforcement through a central repository, the United States would more vigorously be able to identify and mitigate illicit actors and protect the U.S. financial system. In other words, placing the burden of information collection on the reporting parties rather than financial institutions or other regulatory agencies will likely increase the probability and efficiency at which illicit operations are discovered. Fortunately, coinciding with increasing efforts to combat financial terrorism for which the American system has simply not had the means

43 Id.
44 CNBC supra note 23.
45 Id.
46 D’Antuono, supra note 1.
47 Id.
48 Id.
to keep up with, the CTA will surely kickstart this new and improved pursuit of protection.

V. **OPPOSITION OF THE CORPORATE TRANSPARENCY ACT AND CONCLUSION**

The purpose of the CTA is:

“to ensure that persons who form corporations or limited liability companies in the United States disclose the beneficial owners of those corporations or limited liability companies, in order to prevent wrongdoers from exploiting United States corporations and limited liability companies for criminal gain, to assist law enforcement in detecting, preventing, and punishing terrorism, money laundering, and other misconduct involving United States corporations and limited liability companies, and for other purposes.”

Reporting this sort of information to law enforcement is necessary because “[v]ery few States require information about the beneficial owners of the corporations and limited liability companies formed under their laws. However, there will inevitably be opponents to its enforcement or manipulation of its purpose or intention.

One of the main concerns involves basic privacy rights and potential violation of such in handing over more personal information to government agencies. The CTA’s mandatory disclosure for beneficial owners within covered corporations and LLCs eliminates a monopoly on the beneficial ownership information that the corporation possesses, letting in the relevant federal authorities. However, these constitutional rights have not quite reached this extent of protection for information as such. Usually, the constitutional right to privacy has been construed specifically to protect an American’s right to an abortion, contraception, or other personal healthcare decisions, not anti-money laundering legislation. However, all remain a balancing act of interests. For example, the right of a beneficial owner to maintain their interest as

51 Id.
52 Id.
53 Id.
private knowledge is balanced against the importance of tracking such information to prevent criminal abuse of the financial system. The issue then becomes a matter of how limited the extent to which the beneficial owner’s privacy is violated. Further, compared to other federal legislation allowing the collection of personal information on Americans, such as the Patriot Act and National Security Act, the CTA requires far less information be reported with such information directly maintained by one federal agency.  

Similar to other American programs such as Social Security, for example, where individuals are required to pay to register their name with the government for certain benefits, beneficial owners are instead paying the price of turning over basic components of their identity to federal authorities in order to incorporate. Further, there are other laws still enforced today, including the Patriot Act, in which the federal government has the authority to recover far more information about beneficial owners, given cause.  

Thus, this common point of contention with the CTA is unlikely to lead to any serious action or support, given the fact that the constitutional right to privacy has not been expanded to the realm where turning over basic personal information to federal authorities in order to incorporate a business entity violates such privacy.

The CTA also raises an issue regarding the First Amendment, specifically the freedom of association. Under the CTA, any beneficial owner of a covered entity would be required to publicize their role in the organization to FinCEN and some believe this infringes upon their freedom of association, as situations may exist where an individual’s association with a group, such as a corporation, can only be expressed if such membership is done anonymously.  

When considering a similar question, the Supreme Court found in 1974 that the original reporting requirements of the BSA did not violate any First Amendment freedom of association rights, as such associational interests were “too speculative to warrant proper consideration.”  

Once again, the issue becomes a balance of government interest for which a case of first impression has not yet occurred. Justice Marshall in his dissent in California Bankers Association v. Shultz stated, “the fact that some may use negotiable

54 Id.
55 Id.
56 Id.
57 Id.
instruments for illegal purposes cannot justify the Government’s running roughshod over the First Amendment rights of the hundreds of lawful yet controversial organizations.”\textsuperscript{59} However, while an argument can be made to this statement, the government likely would be able to make a winning case that anonymous shell corporations are such a menace to society that a relative, compulsory revelation of limited information from small corporations nationwide is a small price to pay for the probable exposure of wrongdoing.\textsuperscript{60}

As is the mission of the Financial Crimes Enforcement Network, safeguarding the American financial system from illicit use and combating money laundering and related crimes is necessary in promoting national security through the strategic use of financial authorities and the collection, analysis, and dissemination of financial intelligence. Though provisions are likely to undergo amendment and tailoring once implemented by law, the Corporate Transparency Act is likely to withstand the scrutiny it will and has already faced, proving to be in the best interest of the country and the security of its citizen.

\textsuperscript{59} Id. at 99 (Marshall, J., dissenting).
\textsuperscript{60} O’Leary \textit{supra} note 51.