

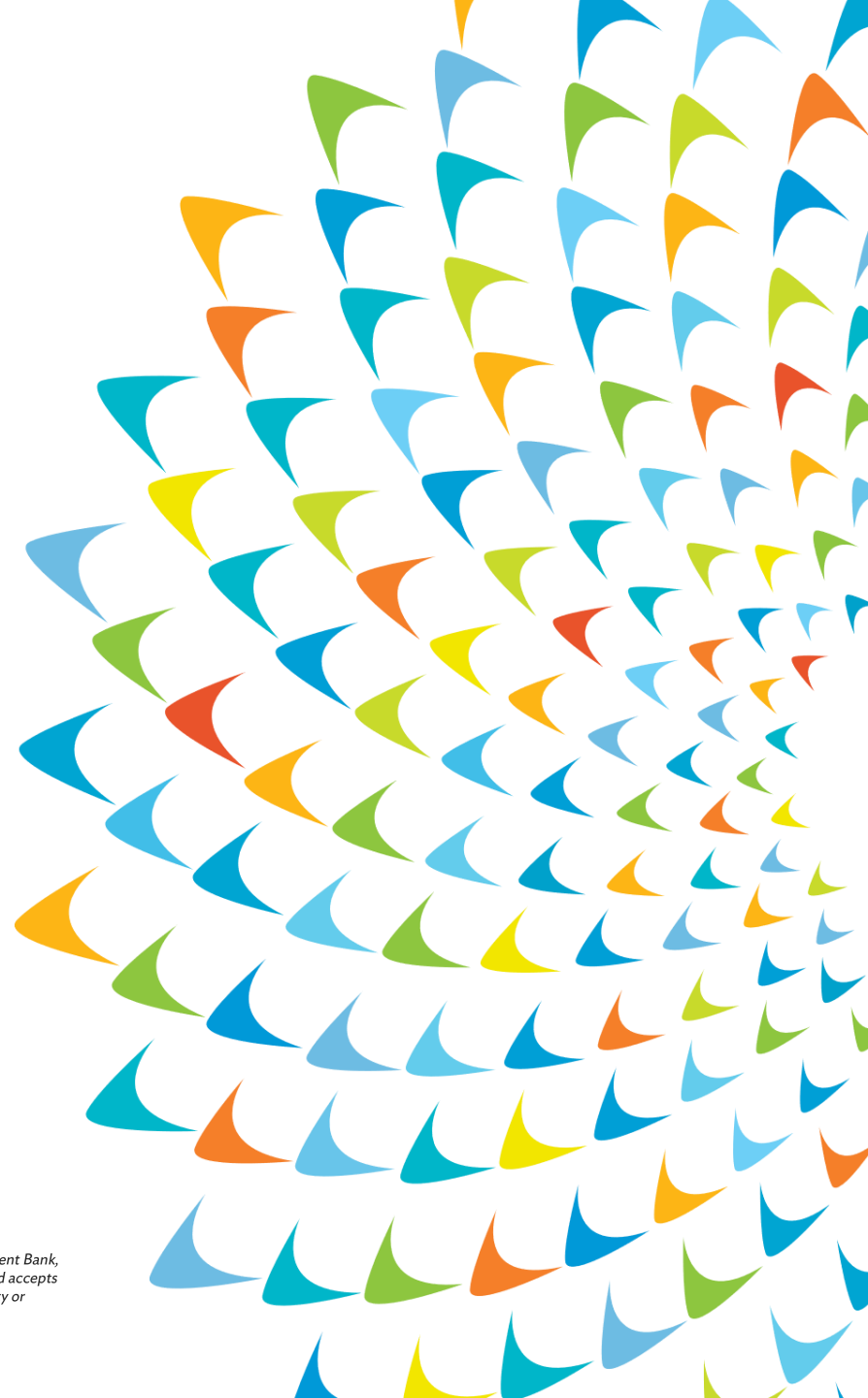


Ultimate Beneficial Owners

International Standards & Practices

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Customer Due Diligence: FATF Recommendation 10 (and 22)

CDD is required when:

- ❖ Establishing business relations;
- ❖ Carrying out occasional transactions above the applicable designated threshold (USD/EUR15,000 for FIs and real estate agents; USD/EUR3,000 for casinos) or qualifying wire transfers; or
- ❖ there is a suspicion of money laundering or terrorist financing; or
- ❖ the financial institution has doubts about the veracity or adequacy of previously obtained customer identification data

Customer Due Diligence: FATF Recommendation 10 (and 22)

Customer Due Diligence (CDD)

- ❖ Identify the customer and verify the customer's identity using reliable, independent source documents, data or information
- ❖ CDD should be applied to:
 - ❖ customers;
 - ❖ persons acting on behalf of customers; and
 - ❖ ultimate beneficial owners
- ❖ For legal persons and arrangements: Also understand nature of business, and ownership and control structure
- ❖ Conduct **ongoing due diligence** throughout course of existing relationship to ensure that the transactions being conducted are consistent with the institution's knowledge of the customer, their business and risk profile (based on materiality and risk)

Customer Due Diligence: FATF Recommendation 10 (and 22)

Steps in identifying beneficial owners of legal persons:

1. Identify natural persons who have controlling ownership interest
2. In case of doubt on controlling ownership interest, identify natural persons exercising control through other means – ex:
 - a) Personal connections
 - b) Financing of the enterprise
 - c) Close and intimate family relations
 - d) Historical or contractual associations
 - e) Control obtained by default on certain payments
 - f) Actual enjoyment of assets
3. Where no natural person can be identified, identify natural person who holds senior management position



Customer Due Diligence: FATF Recommendation 10 (and 22)

Identifying beneficial owners of legal arrangements:

1. Express Trusts: Identity of settlor, trustee/s. any protector, beneficiaries, and any natural person exercising ultimate effective control
2. Other arrangements: persons in equivalent/similar positions

If beneficial owner cannot be identified, then:

- ❖ Do not open the account
- ❖ Do not proceed with the transaction
- ❖ Terminate business relationship
- ❖ Consider filing STR



Beneficial Owner: FATF Definition

The natural person(s) who:

- ❖ ultimately owns or controls a customer; and/or
- ❖ On whose behalf a transaction is being conducted
- ❖ It also includes those persons who exercise ultimate effective control over a legal person or arrangement

“ultimately owns or controls” and “ultimate effective control” – refer to situations in which ownership/control is exercised through a chain of ownership or by means of control other than direct control



Beneficial Owner: Applying the FATF Standard

- ❖ Each time you apply the test of beneficial ownership to a customer you must ask three questions:
 - ❖ Who owns a controlling interest of the customer?
 - ❖ Who has ultimate effective control of the customer?
 - ❖ Who is/are the person/s on whose behalf a transaction is conducted?
- ❖ A beneficial owner is an individual who satisfies any one element, or any combination of the three elements
- ❖ A customer may have more than one beneficial owner
- ❖ Task is to identify and verify the identity of **ALL** beneficial owners of the customer

Beneficial Owner: Controlling Ownership Interest

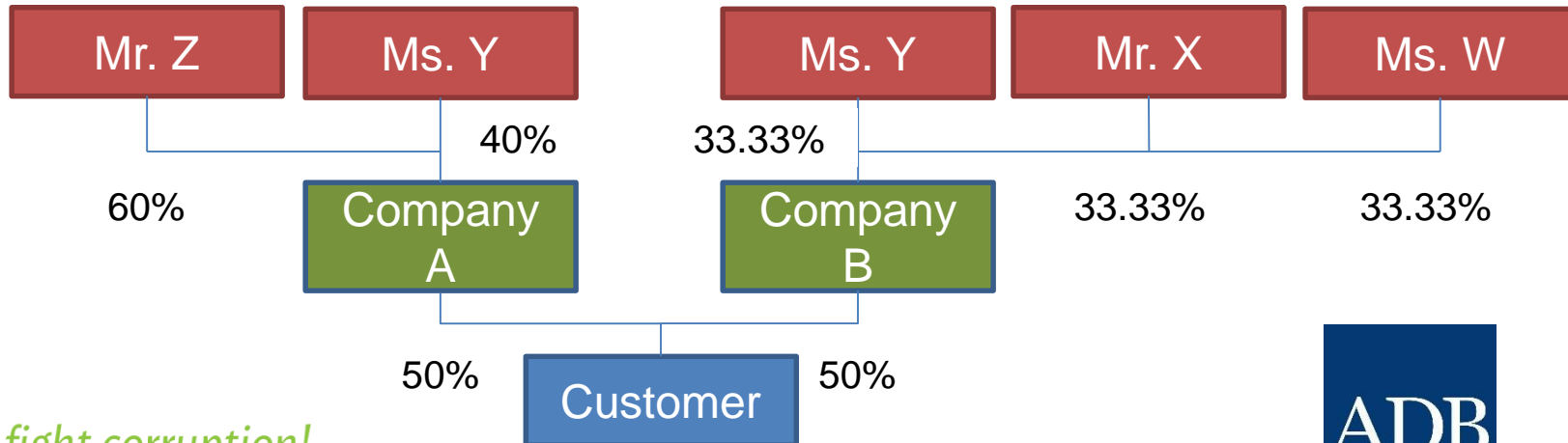
What is a “controlling ownership interest”?

- ❖ The FATF Beneficial Owner definition doesn't tell you... but:
- ❖ Interpretive Notes to FATF Recommendations 10 (Customer Due Diligence) and 24 (Transparency and Beneficial Ownership of Legal Persons) states:
 - ❖ “A controlling ownership interest depends on the ownership structure of the company. It may be based on a threshold, e.g. any person owning more than a certain percentage of the company (e.g. 25%).”
- ❖ EU 4th Directive on AML/CFT: “25% plus one”
- ❖ U.S. Financial Crimes Enforcement Network Rule on Beneficial Owners (2018): “25% or more”
- ❖ Also consider thresholds set in the national law for your specific sector

Beneficial Owner: Controlling Ownership Interest

How do we establish control in an ownership chain?

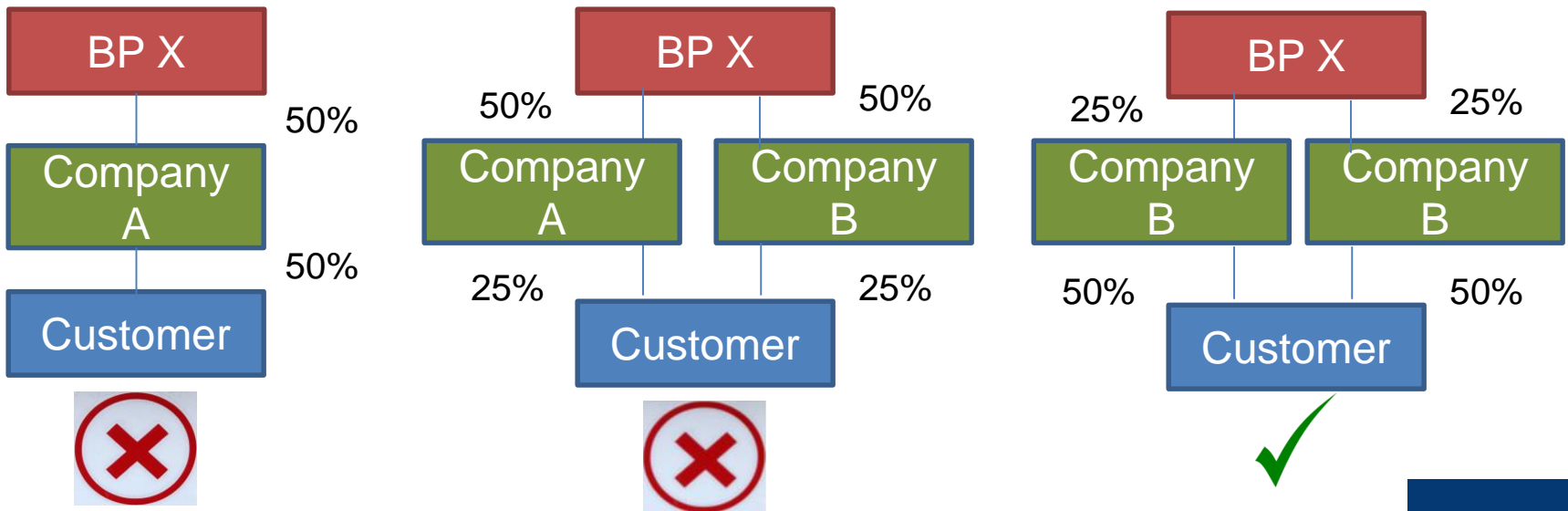
- ❖ U.S. Financial Crimes Enforcement Network Guidance on Beneficial Owners (2018):
 - ❖ Ownership is satisfied either directly or indirectly through multiple corporate structures (applies multiplication criterion)
 - ❖ Example from Guidance:



Beneficial Owner: Controlling Ownership Interest

OFAC's 50% Rule (13 August 2014):

- ❖ Only speaks of ownership, not control
- ❖ Ownership can be aggregated, as well as direct and indirect



Beneficial Owner: Controlling Ownership Interest

How do we establish control in an ownership chain?

- ❖ EU 4th Directive on AML/CFT
 - ❖ Only mentions that a corporate entity can be considered **under the control of a natural person(s)**, or by multiple corporate entities, which are **under the control of the same natural person(s)**
- ❖ Joint Committee of European Supervisory Authorities: “Joint Guidelines on the Prudential Assessment of Acquisitions and Increases of Qualifying Holdings in the Financial Sector” (2016) (Art. 6)
 - ❖ Once a person has reached the control point in a company that – in turn – has a qualifying holding (i.e. substantial influence) in the targeted company, that person is deemed to also have an indirect qualifying holding over such targeted person
 - ❖ If control point is not reached, then apply multiplication criterion

Beneficial Owner: Controlling Ownership Interest

Example using control threshold of >50% and qualifying threshold of 10%:

Figure 1

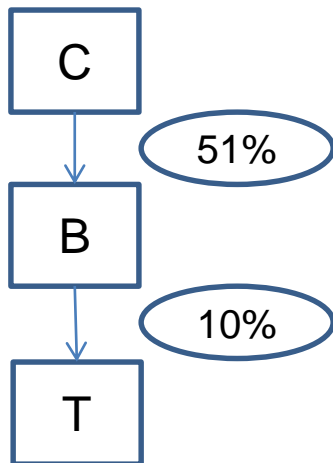


Figure 2

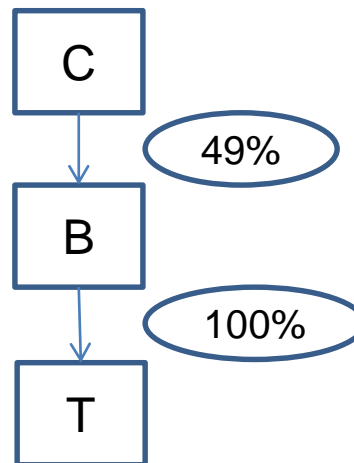
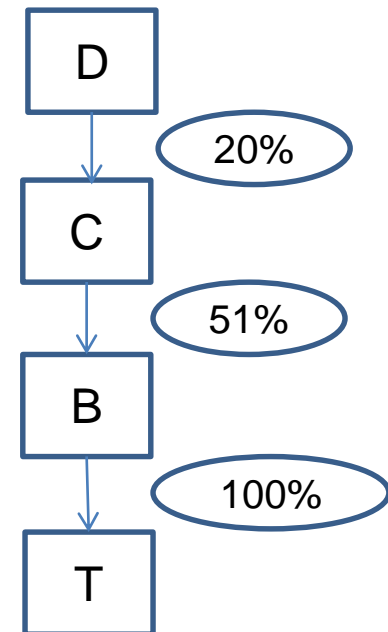


Figure 3



Source: Joint Guidelines on the Prudential Assessment of Acquisitions and Increases of Qualifying Holdings in the Financial Sector

iACT to fight corruption!

Beneficial Owner: Exercise of Control



So, no one owns more than 25%... Now what?

- ❖ Sometimes ownership is spread over a large number of individuals with no individual owning more than 25 percent
 - ❖ Ex.: A co-operative that has a large number of members is likely to have no individual(s) owning more than 25 percent
- ❖ Still must identify a beneficial owner(s)!
- ❖ **DON'T JUST LOOK AT FORMAL SHARE OWNERSHIP!**
- ❖ **Effective control** is the key!

Beneficial Owner: Exercise of Control

Examples of how natural persons exercise control

- ❖ Directly or indirectly holds a minimum percentage of ownership interest in the legal person (threshold approach)
- ❖ Exercise control as a shareholder or together with other shareholders through contract, understanding, relationship, intermediary or tiered entity (majority interest approach) (ex. shareholders agreement, dominant influence to appoint senior management)
- ❖ Exerts control of legal person through other means (ex. personal connections, financing of enterprise, historical or contractual associations)
- ❖ Exerts control through position held in legal person (ex. strategic decisions, executive control, voting rights)
- ❖ **DON'T JUST LOOK AT FORMAL SHARE OWNERSHIP!**

Beneficial Owner: Who really is in control?



Lack of beneficial ownership information **DISGUISES:**

- ❖ **Identity** of known or suspected criminals
- ❖ **True purpose** of an account or property held by a corporate vehicle
- ❖ **Source or use** of funds or property associated with a corporate vehicle

Beneficial Owner: Who really is in control?

Examples of tools to hide true beneficial ownership information

- ❖ Shell companies
- ❖ Complex ownership and control structures
- ❖ Bearer shares and warrants
- ❖ Unrestricted use of legal persons as directors
- ❖ Undisclosed nominator of nominee shareholders and directors
- ❖ Informal nominee shareholders and directors
- ❖ Trusts and other legal arrangements
- ❖ Use of intermediaries in forming legal persons

Beneficial Owner: Shell and Shelf Companies

- ❖ 4 Reasons to establish or control a shell company for ML:
 1. Accomplish the objective of converting cash proceeds of a crime into alternative assets
 2. Create the perception that illicit funds have been generated from a legitimate source (i.e. accounts can be created with FIs) – especially attractive are businesses with high cash volume (retails stores, restaurants, bars, laundromats)
 3. Can operate a wide range of legitimate / bogus business transactions to further ML process (e.g., lending money between criminally-controlled firms, fictitious salaries, disguised payments to suppliers, real estate purchases)
 4. Conceal criminal ownership (i.e. nominees can be used as owners, directors, officers, shareholders, combined with layering)

Problem

- ❖ Dirty money, derived from criminal activities of Belgian Criminal A, is sent to a foreign bank account of Corporation B. Then in Belgium, a new investment Company C is incorporated. Criminal A is appointed as a director of Company C. Company C borrows money from the foreign Corporation B and buys real estate in Belgium. The real estate is rented to third parties. Director (Criminal) A also rents an apartment in the building. With the funds generated by the rent, Company C pays off the loan to Corporation B, and the salary of Director (Criminal) A. Criminal A now converted his dirty money in legal funds. This laundering method is commonly referred to as what?
 - a. Offsetting real estate transactions
 - b. Loan back
 - c. Cuckoo smurfing
 - d. Loan manipulation

* Lifted from ACAMS Study Guide for the CAMS Certification Examination (5th Ed)

Beneficial Owner: Trusts

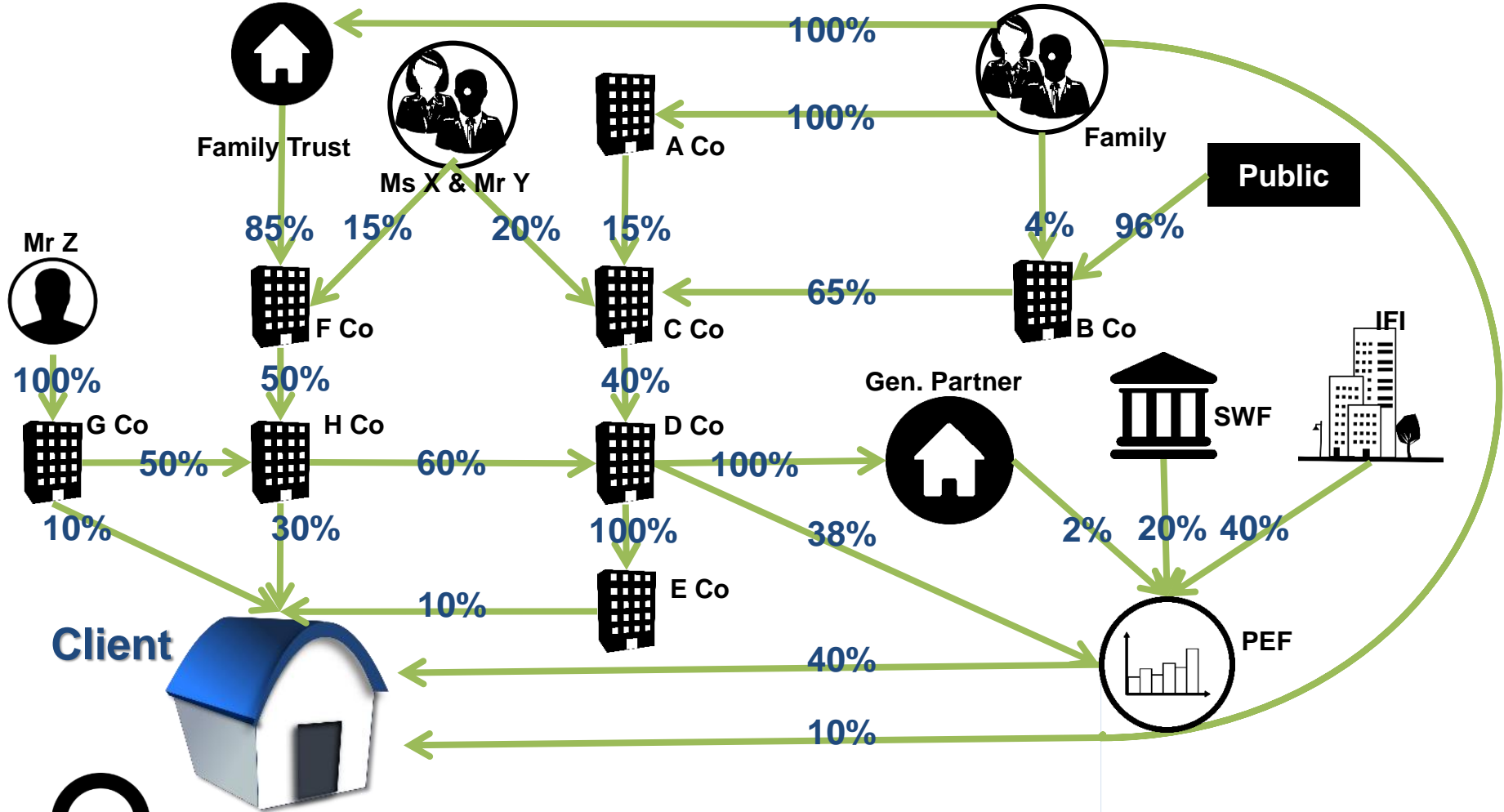
- ❖ Pertains to Express Trusts (as opposed to constructive trusts) – enable property to be managed by one person on behalf of another
- ❖ Since legal title and control of assets are separated from equitable interests, it is difficult to identify the beneficial owner
- ❖ Trustees should disclose their status to FIs and DNFBPs
- ❖ Obtain information on identity of: settlor, trustees, protector, beneficiaries (class of beneficiaries) and other natural persons having effective control

Beneficial Owner: Persons on whose behalf a transaction is conducted

- ❖ May be the individual who is an underlying client of your customer. This concept is important when considering the relationship between managing intermediaries and their underlying clients
- ❖ An example is, if a reporting entity knows that someone (person A) is conducting an occasional transaction on behalf of another person (person B), then person A and person B should both be identified and verified along with any other beneficial owners

Beneficial Owner: Acting on behalf of a customer

- ❖ Not part of beneficial ownership, but it is part of the customer due diligence process.
- ❖ A person might act on behalf of a customer, without being the beneficial owner of that customer
- ❖ “Authority to act” is not the same thing as effective control
- ❖ In some instances, funds from an unidentified third party entering and then exiting an account may be reasonable grounds to suspect that a customer is acting on behalf of another person



Any BOs of Client? How much do they control?
 Other companies controlled by the same ultimate beneficial owners?



If you have questions, contact:

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