



Drilling down to the real owners – Part 1

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“More than 25% of ownership” & “unidentified” Beneficial Ownership: Amendments Needed in FATF’s Recommendations and in EU’s AML Directive

1. Overview

The Panama Papers once again have proven the urgent need for effective rules for the verification of the beneficial ownership (BO) of companies and other legal persons. Central, public, and open registers of this data available online for all types of entities and arrangements is arguably the only promising reform to ensure accountability for and correct filing of beneficial ownership information.

Currently, however, there are serious shortcomings in the international and European framework rules for BO identification, verification and policing of the system, the FATF’s (2012) 40 recommendations and the 4th EU Directive on anti-money laundering (2015) respectively. As we have [explained elsewhere](#)², if this is not addressed, the changes that this European Directive would bring to European anti-money laundering rules by mid-2017 will result in a *weakening* of the rules for the unmasking of the real owners of shell companies.

These shortcomings will be replicated in national laws and therefore weaken or even frustrate anti-money laundering efforts across the globe. Developing country authorities will find it more difficult to pierce through the corporate veil created by shell companies in Europe and elsewhere to recover stolen assets and counter illicit financial flows. Recently announced public registers of company owners in [Afghanistan, France, Kenya, the Netherlands and Nigeria](#) risk falling short of publishing the real owners controlling the companies. These

¹ Please send any feedback on this report to info@taxjustice.net.

² <http://www.taxjustice.net/2016/04/08/panama-papers-break-europe-plans-water-company-ownership-transparency/>; 4.5.2016.

shortcomings will also [prevent the effective verification of BO information for the new global standard on Automatic Exchange of Information](#)³, pursuant to the OECD's Common Reporting Standard (CRS). In contrast, effective public BO registries would even close some of the loopholes⁴ in the CRS.

While there are a number of concerns in the anti-money laundering rules, this first part of a series of analyses focuses on just two, though crucial flaws: high thresholds in the definition of BO ("more than 25% of ownership"), and an escape route to avoid identifying the BO by registering a senior manager instead (by allowing a misinterpretation of situations where "no person is identified as BO"). The likely result of these flaws is the widespread abuse of nominee directors and shareholders that are "mistakenly" recorded as BOs, or the proliferation of entities without a BO. If this is not addressed, both FATF and EU regulations would help protect the veil of secrecy offered by the offshore legal entities exposed by Panama Papers. Urgent amendments are therefore needed.

2. Current Legal Framework

The FATF 2012 Recommendations and the EU 3rd and 4th AML Directives contain a similar basic definition of who the beneficial owner(s) are in the context of a legal entity. The common first step as laid down in the FATF 2012 recommendations entails recording and verifying:

"The identity of the natural persons (if any – as ownership interests can be so diversified that there are no natural persons (whether acting alone or together) exercising control of the legal person or arrangement through ownership) who ultimately have a controlling ownership interest³⁰ in a legal person;" (FATF 2012: 60, 10.C.5.b.i.i).

Footnote 30 on "controlling ownership interest": "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%)." (FATF 2012: 60, FN 30).

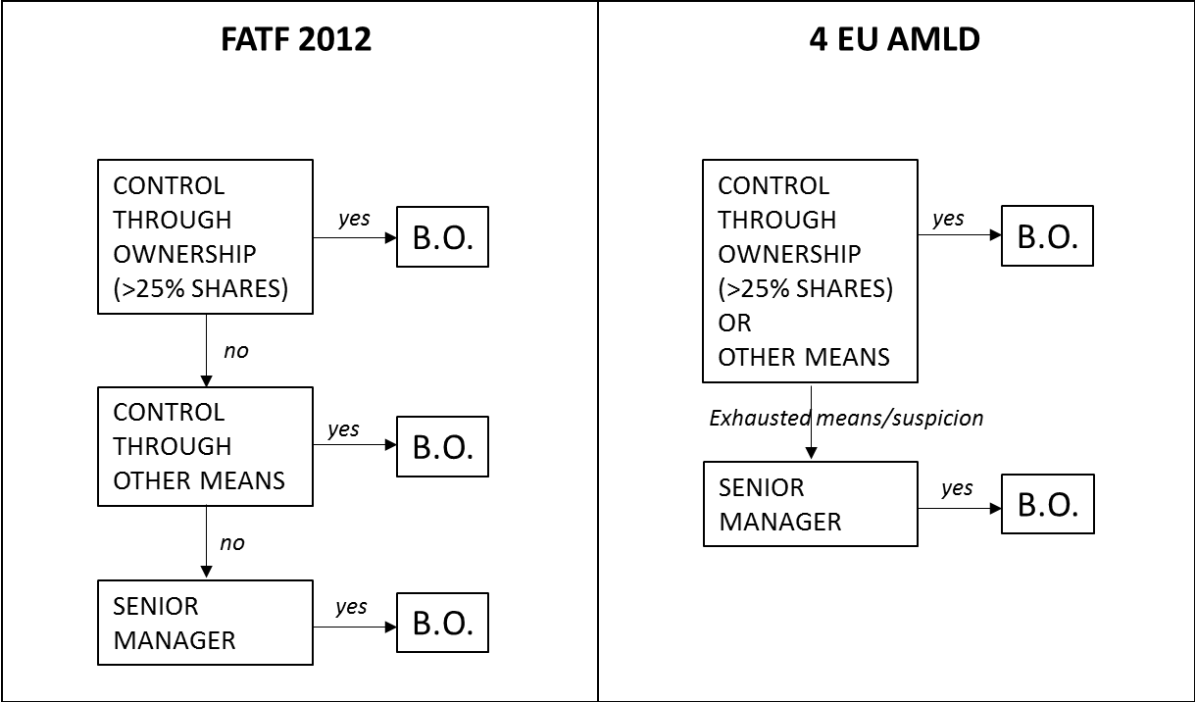
In practice, as confirmed in the EU 3rd and 4th AMLD, this involves a "test" to determine the existence of at least one natural person with an ultimate controlling ownership of more than 25% in the shares of any legal entity

³ <http://www.taxjustice.net/wp-content/uploads/2013/04/CRS-vs-registries.pdf>; 4.5.2016.

⁴ The CRS requires that BOs have to be identified and reported under certain circumstances (i.e. when a bank account is held by a company or trust with "passive" income, such as interests or dividends). For these cases, BO registries would allow verification of BO information. However, public BO registries would also allow BO identification altogether for companies or trusts with "active" income (i.e. income from sale of goods or services), whose BOs need not be identified. This loophole as well as many others are explained here: <http://www.taxjustice.net/wp-content/uploads/2013/04/TJN-141124-CRS-AIE-End-of-Banking-Secrecy.pdf>; 4.5.2016.

("control through ownership"). If tested positive, the natural person(s) are to be defined as the beneficial owners.

After this point, however, the FATF 2012 recommendations and the 4th EU AMLD part ways. While the FATF proceeds by applying a cascading filter, the EU instead offers alternatives.



The FATF states that only if nobody "is identified" using this previous test, the second option applies, where beneficial ownership refers to "the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means" (FATF 2012: 60, 10.C.5.b.i.ii and FN 29). This second test involves thus "control through other means".

The FATF then proceeds to allow the third test which concedes the highly problematic definition of a BO as the "relevant natural person who holds the position of senior managing official" (FATF 2012: 60, 10.C.5.b.i.iii). By allowing this definition of a senior managing official – even if it is only under certain circumstances – this helps blur the concept of beneficial ownership. That legitimises the use of nominee directors, agents, proxies or equivalent, as the last stops in long, secretive and abusive chains of ownership designed to disrupt accountability and traceability. The 4th EU AMLD even allows the use of this third option more easily, as will be shown below under 3-3.2.

3. Flaws in Current Legal Framework and Proposed Solutions

Five problems are salient.

3.1 "More than 25% of ownership"

Both the FATF and the EU AMLD consider an ownership beyond 25% to be the threshold to consider someone as a BO. A typical family of four persons (two

parents and two children or four friends) could appoint every member as a shareholder. In that case, each of them would have only 25% of ownership, so no one would trigger the threshold of more than 25% of ownership to be considered a BO. For this reason, the threshold should be lowered to make it harder to simply appoint a few trusted people as shareholders, as a strategy to avoid identifying the (real) BO. Alternative existing thresholds are “at least 10%” (imposed by U.S. domestic law FATCA to determine ownership of entities by U.S. persons) and “at least 5%” (established by the U.S. Securities Exchange Commission as well as by other regulators of companies listed in a stock exchange). Ideally, however, “any natural person owning directly or indirectly at least one share” should be identified as a BO.

3.2 Control through other means

The definition of “control through other means” (other than through ownership) does not involve only one person with such control, but all the natural persons who meet the condition. Importantly, if no natural person meets the ownership threshold (currently more than 25% of shares, though ideally one share), then every person with control through other means, should be considered a BO. While this provision may be interpreted correctly, the language in the FATF rules does not provide for examples, which would help to correctly interpret this provision. For instance, a provision is missing which clarifies situations in which five natural persons would jointly exercise control over the management of a legal entity. Similarly, no clarification is given about what needs to happen if too many people met that condition (i.e. 20 equal shareholders, each with only one vote to appoint the CEO). In those situations all natural persons with ultimate control through other means should be identified as BOs.⁵

Furthermore, the FATF is even adding the qualifying term “if any” to the control test.⁶ By inserting the condition “if any”, the FATF is suggesting that there may be situations where no person has control neither through ownership nor through other means. However, it appears to be impossible that nobody would have the right to control the company by appointing or removing a CEO, Secretary, Treasurer or CFO.

In order to support the correct implementation of these requirements, it would be advisable to include examples of what constitutes control through other means. The EU AMLD provides some examples: “Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a shareholders' agreement,

⁵ At the very least, if an ownership threshold is maintained, the top 10 or 20 persons with such control should be identified as BOs (for the respective ownership threshold of 10% or 5%).

⁶ “the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means” (FATF 2012: 60, 10.C.5.b.i.ii and FN 29).

the exercise of dominant influence or the power to appoint senior management” (EU AMLD, Whereas 13).

However, the United Kingdom’s law on BO registration for companies (called “Person with Significant Control”) is even more detailed. It includes - in addition to ownership of more than 25% of shares - having 25% of voting rights, the right to appoint or remove the majority of the board of directors, and right to exercise influence or control ([Small Business, Enterprise and Employment Act 2015](#)⁷, amending Companies Act 2006: Schedule 1A, Part 1).⁸

A start-up with one founder and 10 private investors

If a company had one original founder who then got 10 investors, all of which resulting in equal shareholders with equal voting rights, in principle no one would meet the control through ownership test (because no one would have even 10% of the shares, unless the ideal alternative is chosen where any person owning directly or indirectly at least one share would have to be identified and reported). However, this should still trigger the control through other means test. If some of the shareholders could become members of the board, either one or all of them would very likely be considered the BOs. However, if the board only involved independent directors, or if there was no board of directors but only an independent employee-CEO to manage the company, at least 10 out of the 11 owners should be considered BOs, not because they have 10% of ownership, but because they all have control over the company through other means (by appointing the CEO). The senior manager, such as an employee-CEO (only one natural person) seems to only make sense in a truly atomized company – very likely a listed company, which is not covered by the FATF or EU AMLD – where shareholders do not participate in management decisions at all. The “top 10 rule” however, would still include some of those atomized shareholders, either the top largest shareholders and if all have the same amount of shares, any random 10 shareholders.

⁷ <http://www.legislation.gov.uk/ukpga/2015/26/schedule/3/enacted>; 4.5.2016.

⁸ The [Draft Statutory Guidance](#) (https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/498275/Statutory_company_PSC_Guidance.pdf; 4.5.2016) on the latter includes the following examples:

“a) Adopting or amending the company’s business plan; b) Changing the nature of the company’s business; c) Making any additional borrowing from lenders; d) Appointment or removal of the CEO; e) Establishing or amending any profit-sharing, bonus or other incentive scheme of any nature for directors or employees; or f) The grant of options under a share option or other share based incentive scheme.

Where a person has absolute veto rights over decisions related to the running of the business of the company, for example relating to: a) Adopting or amending the

3.3 "is identified" vs "meets the criteria"

Both the FATF 2012 Recommendations and the EU 4th AML Directive refer to cases where no BO exists (because no natural person meets the criteria of 25% or control through other means) using the language "no person was *identified* as a BO". This expression may be correctly interpreted (no BO exists because no one meets the previous test or criteria), but it could also lead to a misinterpretation where a BO that meets the criteria *does exist* (i.e. a controlling ownership interest of more than 25%), but they were not identified or their identities could not be verified, for instance because requested verification documents (e.g. copies of passports, proof of address, ownership structure, etc.) were not provided.

This may be possible because regulated entities are only under a duty to take "reasonable measures" to verify the identities of beneficial owners (FATF 2012: 60, 10.C.5.b). What constitutes "reasonable measures" is highly subjective and opens the door for any regulated entity to record a senior managing official as a beneficial owner.

To avoid ambiguities, the phrase "no person was identified" should therefore be amended to "no natural person meets the criteria", to make sure that if no one was identified nor verified as a BO on the basis of the respective test, it is (exclusively) because no such person exists. However, in a scenario where no thresholds apply anymore for defining the BOs, this language would become redundant.

3.4 Cascade vs interchangeable alternatives

The FATF is explicit⁹ that the first test is to identify the BO who has "control through ownership", and only if no one meets this criterion then the persons with "control through other means" should be identified. Likewise, if no one meets this second criterion, then the person with a senior managing position may be identified.

In contrast, the 4th EU AML Directive, is not explicit that this is a cascading test, and may lead to an interpretation that a person with a senior managing position is a valid substitute for the BO who controls the company through ownership or other means.

3.5 Senior managing position should never be recorded as a BO

Both the FATF and the 4th EU AML Directive allow that, where no person meets the criteria to be a BO (regardless of the cascading test), the person with a

company's business plan; b) Making any additional borrowing from lenders (except as a minority protection)" (UK Draft Statutory Guidance, page 4).

⁹ Footnote 29 of page 60 states: "Measures (i.i) to (i.iii) are not alternative options, but are cascading measures, with each to be used where the previous measure has been applied and has not identified a beneficial owner", available here: http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf

senior managing position will be identified as a BO, but not as a senior manager. Not only would this be inaccurate, but it would also lead others to believe that such a manager (who may be a nominee director, agent or proxy) is in fact a BO. Therefore, if the thresholds and tests would not be abolished or amended as suggested above, and if the first and second tests to identify and verify a BO in case of companies fail (neither an ultimate ownership stake of X% nor control through other means is reported), then at least an explicit public statement about this fact should be required to be disclosed in a register. In addition, the identities of each legal owner of the company and of each director in the board of the company should also be disclosed (as their real status, but not as a "BO").

4. Ideal scenarios

4.1 If the first two tests are amended and at least one natural person-shareholder is always identified as BO

(i) If thresholds that trigger BO identification of the first test ('control through ownership') are lowered to "any natural person directly or indirectly owning at least one share (or the equivalent minimum unit of interest in a legal person)", and/or (ii) if the second test, 'control through other means' is defined indicating that there must always be at least one natural person (or the top 10 or 20 largest shareholders) with control through other means, for example with the power to appoint or remove the CEO, then at least one shareholder (or equivalent) would always be identified, for it would be impossible to have a legal person where no shareholder has any right to appoint or remove a manager.

In spite of this comprehensive test, if there is still no identification of a BO either because the company does not provide this information or because it does not cooperate to verify the information that had already been provided, then:

- companies should not be allowed to be created/exist (existing companies should be "inactivated", so that they cannot operate but their information would still be available – otherwise, those who do not provide information would benefit from their lack of cooperation);¹⁰ and
- regulated entities subject to AML/CDD (i.e. banks) should not be allowed to open accounts in their favour, and they should close those accounts that already exist.

¹⁰ Already existing companies that do not provide BO info, should be sanctioned and blacklisted by UN sanction mechanisms because of a high risk of criminal and terrorist activities, and not be allowed to operate. Their registration info, however, should not be struck off the register, in order to ensure the availability of records and thus accountability in case they have been involved in any wrongdoing.

4.2 If the first two tests are not amended, so there may be situations where no natural person meets the criteria of test one or two

If FATF standards or EU rules are not amended, and no person is identified as a BO because either (i) no natural person meets the criteria to pass the first test (control through ownership) nor second test (control through other means), for example because all shareholders only have 1% of the company, or (ii) the company does not cooperate nor provides information to determine whether a natural person meets the BO definition, then:

a) If the problem refers to lack of cooperation by the company (case (ii)), then the solution should be the same as above:

- companies should not be allowed to be created/exist (existing companies should be "de-activated", so that they cannot operate but their information would still be available – otherwise, those who do not provide information would benefit from their lack of cooperation);¹¹ and

- regulated entities subject to AML/CDD (i.e. banks) should not be allowed to open accounts in their favour, and they should close those accounts that already exist.

b) If the problem refers to no person meeting the (unaltered) criteria of tests one and two, then:

registries of BOs of companies exist, the registry should disclose regarding companies without BOs:

- a statement that no BO exists for this company that meet the criteria of AML rules;

- the identities of all senior managing officials of the company, who should be identified as "senior manager", but not as a "BO"; and

- the identities of all shareholders of the company as "legal owners";

- the whole chain of ownership if many layers of entities are involved as legal owners; and

- describe the actions taken that explain why no natural person related to the company meets the BO criteria.

¹¹ Already existing companies that do not provide BO information, should be sanctioned and blacklisted by UN sanction mechanisms because of a high risk of criminal and terrorist activities, and not be allowed to operate. Their registration info, however, should not be struck off the register, in order to ensure the availability of records and thus accountability in case they have been involved in any wrongdoing.

5. Proposed amendments

5.1 2012 FATF Recommendations

Current Text	Proposed Alternative
<p>“GENERAL GLOSSARY</p> <p>Beneficial owner refers to the natural person(s) who ultimately⁵⁰ owns or controls a customer⁵¹ and/or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.</p> <p>FN 50: Reference to “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.</p> <p>FN 51: This definition should also apply to beneficial owner of a beneficiary under a life or other investment linked insurance policy.”</p>	<p>“GENERAL GLOSSARY</p> <p>Beneficial owner refers to the natural person(s) who ultimately⁵⁰ owns or controls a customer⁵¹ and/or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement. A beneficial owner must always be a natural person (not a legal person), and must refer to the actual and real owner, and not to a nominee, agent, proxy or equivalent.</p> <p>FN 50: Reference to “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.</p> <p>FN 51: This definition should also apply to beneficial owner of a beneficiary under a life or other investment linked insurance policy.”</p>
<p>INTERPRETIVE NOTE TO RECOMMENDATION 10 (CUSTOMER DUE DILIGENCE)</p> <p>[...]</p> <p>C. CDD FOR LEGAL PERSONS AND ARRANGEMENTS</p> <p>[...]</p> <p>(b) Identify the beneficial owners of the customer and take reasonable measures to verify the identity of such persons, through the following information¹²:</p>	<p>INTERPRETIVE NOTE TO RECOMMENDATION 10 (CUSTOMER DUE DILIGENCE)</p> <p>[...]</p> <p>C. CDD FOR LEGAL PERSONS AND ARRANGEMENTS</p> <p>[...]</p> <p>(b) Identify the beneficial owners of the customer and take reasonable measures to verify the identity of such persons, through the following information¹³:</p>

¹² 2012 FATF Recommendations, Pages 60-61, available here: http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf

¹³ 2012 FATF Recommendations, Pages 60-61, available here: http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf

<p>(i) For legal persons:</p> <p>(i.i) The identity of the natural persons* (if any – as ownership interests can be so diversified that there are no natural persons (whether acting alone or together) exercising control of the legal person or arrangement through ownership) who ultimately have a controlling ownership interest³⁰ in a legal person; and</p>	<p>(i) For legal persons:</p> <p>(i.i) The identity of the natural persons (if any – as ownership interests can be so diversified that there are no natural persons (whether acting alone or together) exercising control of the legal person or arrangement through ownership) who ultimately have an controlling ownership interest³⁰ in a legal person; and</p>
<p>IDEAL: BO IS ANY NATURAL PERSON WITH AT LEAST ONE SHARE (++)</p>	
<p>Footnote 30 on “controlling ownership interest”: “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%).”</p>	<p>Footnote 30 on “ownership interest”: “An controlling ownership interest depends on the ownership structure of the company. It includes any natural person ultimately owning more than at least one share or equivalent minimum unit of interest in an entity).</p> <p>If two or more natural persons own, directly or indirectly, a single share (or the minimum unit of interest in an entity), then all of them should be considered the full owners of such single share or unit of interest.”</p>
<p>(i.ii) to the extent that there is doubt under (i.i) as to whether the person(s) with the controlling ownership interest are the beneficial owner(s) or where no natural person exerts control through ownership interests, the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means.</p>	<p>(i.ii) to the extent that there is doubt under (i.i) as to whether the person(s) with the controlling ownership interest are the beneficial owner(s) and the entity does not cooperate to clarify the information, or where the entity fails to provide identity information of any natural person meeting the criteria under (i.i) above, obliged entities shall terminate the business relationship with the client and refrain from executing any transactions.</p>
<p>ALTERNATIVE: IF THE OWNERSHIP TEST IS NOT AMENDED AS SUGGESTED, AND THRESHOLDS REMAIN AT “MORE THAN 25%”, OR ARE AMENDED TO “AT</p>	

LEAST 10%” OR “AT LEAST 5%” (WHERE NO PERSON MAY TRIGGER THE THRESHOLD) (-)

<p>(i.ii) to the extent that there is doubt under (i.i) as to whether the person(s) with the controlling ownership interest are the beneficial owner(s) or where no natural person exerts control through ownership interests, the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means.</p>	<p>(i.ii) to the extent that there is doubt under (i.i) as to whether the person(s) with the controlling ownership interest are the beneficial owner(s) or where no natural person exerts control through ownership interests, the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means.</p> <p>(i.ii) to the extent that no natural person meets the criteria under (i.i), the identity of all the natural persons exercising control of the legal person or arrangement through other means, such as the natural persons with any voting rights, rights to appoint or remove members of the board of directors, and to appoint or remove a senior manager, and with influence or control through other means.</p>
<p>(i.iii) Where no natural person is identified under (i.i) or (i.ii) above, financial institutions should identify and take reasonable measures to verify the identity of the relevant natural person who holds the position of senior managing official.</p>	<p><i>[If either section i.i or i.ii are amended as suggested, it will be impossible not to identify at least one person ultimately beneficially owning at least one share (i.i) or one person being able to appoint or remove senior management (i.ii), therefore:]</i></p> <p>(i.iii) Where no natural person is identified under (i.i) or (i.ii) above, financial institutions should identify and take reasonable measures to verify the identity of the relevant natural person who holds the position of senior managing official.</p> <p>(i.iii) to the extent that there is doubt under (i.i) or (i.ii) as to whether the person(s) meeting the criteria are the beneficial owner(s) and the entity does not cooperate to clarify the</p>

	information, or where the entity does not provide identity information of any natural person meeting the criteria under (i.i) or (i.ii) above, obliged entities shall terminate the business relationship with the client and refrain from executing any transactions.
ALTERNATIVE SOLUTION TO THE CLOSURE OF ACCOUNTS, IF SECTIONS i.i OR i.ii REMAIN THE SAME (--)	
(i.iii) Where no natural person is identified under (i.i) or (i.ii) above, financial institutions should identify and take reasonable measures to verify the identity of the relevant natural person who holds the position of senior managing official.	[<i>If sections i.i and i.ii remain the same and are not amended as suggested:</i>] (i.iii) to the extent that there is doubt under (i.i) or (i.ii) as to whether the person(s) identified are the beneficial owner(s), or where no natural person meets the criteria under (i.i) or (i.ii) above, financial institutions should record that no beneficial owner exists and describe all the (unsuccessful) actions taken to identify them. In addition, they should identify and verify the identity of the relevant natural person who holds the position of senior managing official, who should be recorded as "senior manager" (and not as "beneficial owner"), and record details of all legal owners of the entity, including the full chain of ownership through all layers of legal persons.

5.2 EU 4TH AML DIRECTIVE

The 4th EU AML Directive establishes the different BO tests and allows a senior manager to be considered a BO in two different sections of the Directive. The first is the non-binding "Whereas" section (Paragraph 13), and the second place is in Article 3.6.

5.2.1 Changes in the Introductory "Whereas" section

Current Text ¹⁴	Proposed Alternative
Whereas:	

¹⁴ EU 4TH AML DIRECTIVE, Page 4, available here: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015L0849&rid=1>

[...]	
IDEAL DEFINITION OF BENEFICIAL OWNER (++)	
<p>(13) Identification and verification of beneficial owners should, where relevant, extend to legal entities that own other legal entities, and obliged entities should look for the natural person(s) who ultimately exercises control through ownership or through other means of the legal entity that is the customer.</p> <p>Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a shareholders' agreement, the exercise of dominant influence or the power to appoint senior management. There may be cases where no natural person is identifiable who ultimately owns or exerts control over a legal entity. In such exceptional cases, obliged entities, having exhausted all other means of identification, and provided there are no grounds for suspicion, may consider the senior managing official(s) to be the beneficial owner(s).</p>	<p>(13) Identification and verification of beneficial owners should, where relevant, extend to legal entities that own other legal entities, and obliged entities should look for all the natural person(s) (who cannot be nominees, agents, proxies or equivalent) who ultimately own any share (or equivalent minimum unit of interest in an entity).</p> <p>Where no natural person meets that criterion, obliged entities shall terminate the business relationship with the client and refrain from executing any transactions.</p> <p>Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a shareholders' agreement, the exercise of dominant influence or the power to appoint senior management. There may be cases where no natural person is identifiable who ultimately owns or exerts control over a legal entity. In such exceptional cases, obliged entities, having exhausted all other means of identification, and provided there are no grounds for suspicion, may consider the senior managing official(s) to be the beneficial owner(s).</p>
FIRST ALTERNATIVE: IF THRESHOLDS FOR OWNERSHIP TEST ARE HIGHER THAN "AT LEAST ONE SHARE" AND NO ONE PASSES THE OWNERSHIP TEST, THEN APPLY CONTROL THROUGH OTHER MEANS TEST (-)	
<p>(13) Identification and verification of beneficial owners should, where relevant, extend to legal entities that own other legal entities, and obliged entities should look for the natural person(s) who ultimately exercises control through ownership or through other means of the legal entity that is the customer.</p>	<p>(13) Identification and verification of beneficial owners should, where relevant, extend to legal entities that own other legal entities, and obliged entities should look for all the natural person(s) who ultimately exercises control through ownership or hold an ownership interests, and if no one meets that criterion, then all the</p>

<p>Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a shareholders' agreement, the exercise of dominant influence or the power to appoint senior management. There may be cases where no natural person is identifiable who ultimately owns or exerts control over a legal entity. In such exceptional cases, obliged entities, having exhausted all other means of identification, and provided there are no grounds for suspicion, may consider the senior managing official(s) to be the beneficial owner(s).</p>	<p>natural persons with control through other means of the legal entity that is the customer.</p> <p>Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a shareholders' agreement, the exercise of dominant influence or the power to appoint or remove senior management. There may be cases where no natural person is identifiable who ultimately owns or exerts control over a legal entity. In such exceptional cases, obliged entities, having exhausted all other means of identification, and provided there are no grounds for suspicion, may consider the senior managing official(s) to be the beneficial owner(s).</p> <p>Where no natural person meets the two criteria above, obliged entities shall terminate the business relationship with the client and refrain from executing any transactions.</p>
<p>SECOND ALTERNATIVE: IDENTIFICATION OF SENIOR MANAGER (AS SUCH), INSTEAD OF CLOSING THE ACCOUNT (--)</p>	
<p>(13) Identification and verification of beneficial owners should, where relevant, extend to legal entities that own other legal entities, and obliged entities should look for the natural person(s) who ultimately exercises control through ownership or through other means of the legal entity that is the customer.</p> <p>Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a shareholders' agreement, the exercise of dominant influence or the power to</p>	<p>(13) Identification and verification of beneficial owners should, where relevant, extend to legal entities that own other legal entities, and obliged entities should look for all the natural person(s) who ultimately exercises control through ownership or hold an ownership interests, and if no one meets that criterion, then all the natural persons with control through other means of the legal entity that is the customer.</p> <p>Control through other means may, inter alia, include the criteria of control used for the purpose of preparing consolidated financial statements, such as through a</p>

<p>appoint senior management. There may be cases where no natural person is identifiable who ultimately owns or exerts control over a legal entity. In such exceptional cases, obliged entities, having exhausted all other means of identification, and provided there are no grounds for suspicion, may consider the senior managing official(s) to be the beneficial owner(s).</p>	<p>shareholders' agreement, the exercise of dominant influence or the power to appoint senior management. There may be cases where no natural person meets the criteria of owning or exerting control over a legal entity. In such exceptional cases, obliged entities, having exhausted all other means of identification and verification, and provided there are no grounds for suspicion, should record that no beneficial owner exists and describe all the (unsuccessful) actions taken to identify them. In addition, they should identify and verify the identity of the relevant natural person who holds the position of senior managing official, who should be identified as "senior manager" (and not as "beneficial owner"), and record details of all legal owners of the entity, including the full chain of ownership of layers of legal persons.</p>
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5.2.2 Article 3.6 on the definition of a beneficial owner

The term "beneficial owner" is defined in Article 3.6. In contrast to the 2012 FATF Recommendations, it does not incorporate a cascading test. In addition, paragraph a.ii (Article 3.6.a.ii) seems to be intended to allow for the senior manager to be identified as the BO when no person is identified by using the ownership or control tests, or when there are suspicions regarding the identified person. However, a "stop" to separate the last provision (... companies should record actions taken...) as a different sentence is likely missing. Otherwise, the paragraph does not seem to make sense¹⁵, although it would still implicitly allow the senior manager to be considered as the BO. The resulting ambiguity opens the door for abusive and erroneous interpretations when these provisions are a) translated into the languages of the European Union members and b) applied in practice. The current language is an invitation for creative non-compliance where nominee directors are registered as BOs.

¹⁵ Considering the whole of Art. 3, this is how the sentence should have been written (IN CAPITAL LETTERS), if it had been intended to allow senior managers to be recorded as beneficial owners only in conjunction with the obligation to keep records about the measures taken: : (6) 'beneficial owner' means any natural person(s) who ultimately

Current Text ¹⁶	Proposed Alternative
<p>Article 3 For the purposes of this Directive, the following definitions apply: [...] (6) 'beneficial owner' means any natural person(s) who ultimately owns or controls the customer and/or the natural person(s) on whose behalf a transaction or activity is being conducted and includes at least: (a) in the case of corporate entities:</p>	
IDEAL SITUATION (++)	
<p>(i) the natural person(s) who ultimately owns or controls a legal entity through direct or indirect ownership of a sufficient percentage of the shares or voting rights or ownership interest in that entity, including through bearer shareholdings, or through control via other means, other than a company listed on a regulated market that is subject to disclosure requirements consistent with Union law or subject to equivalent international standards which ensure adequate transparency of ownership information.</p> <p>A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a natural person shall be an indication of direct ownership.</p> <p>A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a corporate entity, which is under the control of a natural person(s), or by multiple corporate entities, which are under the control of the same natural</p>	<p>(i) all the natural person(s) (who cannot be nominees, agents, proxies or equivalent), who ultimately own or control a legal entity (other than a legal entity that is a company listed on a regulated market that is subject to disclosure requirements consistent with Union law or subject to equivalent international standards which ensure adequate transparency of ownership information) through direct or indirect ownership of at least one share in that entity (or equivalent minimum unit of interest in an entity), including through bearer shareholdings;</p> <p>Indirect ownership means that at least one natural person own(s) at least one share in an entity, not directly but via one or multiple entities, spread over one or multiple layers.</p> <p>If two or more natural persons own, directly or indirectly, a single share (or the minimum unit of</p>

owns or controls the customer and/or the natural person(s) on whose behalf a transaction or activity is being conducted and includes at least: (a) in the case of corporate entities: (i) the natural person(s) who ultimately owns or controls [...] (ii) if, after having exhausted all possible means and provided there are no grounds for suspicion, no person under point (i) is identified, or if there is any doubt that the person(s) identified are the beneficial owner(s), the natural person(s) who hold the position of senior managing official(s).[FULL STOP] IN THIS CASE the obliged entities shall keep records of the actions taken in order to identify the beneficial ownership under point (i) and this point;

¹⁶ EU 4th AML Directive, page 14, available here: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015L0849&rid=1>

<p>person(s), shall be an indication of indirect ownership. This applies without prejudice to the right of Member States to decide that a lower percentage may be an indication of ownership or control. Control through other means may be determined, inter alia, in accordance with the criteria in Article 22(1) to (5) of Directive 2013/34/EU of the European Parliament and of the Council (3);</p> <p>(ii) if, after having exhausted all possible means and provided there are no grounds for suspicion, no person under point (i) is identified, or if there is any doubt that the person(s) identified are the beneficial owner(s), the natural person(s) who hold the position of senior managing official(s), the obliged entities shall keep records of the actions taken in order to identify the beneficial ownership under point (i) and this point;</p>	<p>interest in an entity), then all of them should be considered the full owners of such single share or unit of interest.</p> <p>(ii) to the extent that there is doubt under (i) as to whether the person(s) identified are the beneficial owner(s) and the entity does not cooperate to clarify the information, or where the entity does not provide the identity of any natural person meeting the criterion under (i) above, the obliged entities shall terminate the business relationship with the client and refrain from executing any transactions.</p> <p>A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a natural person shall be an indication of direct ownership.</p> <p>A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a corporate entity, which is under the control of a natural person(s), or by multiple corporate entities, which are under the control of the same natural person(s), shall be an indication of indirect ownership. This applies without prejudice to the right of Member States to decide that a lower percentage may be an indication of ownership or control. Control through other means may be determined, inter alia, in accordance with the criteria in Article 22(1) to (5) of Directive 2013/34/EU of the European Parliament and of the Council (3);</p> <p>(ii) if, after having exhausted all possible means and provided there are no grounds for suspicion, no person under point (i) is identified, or if there is any doubt that the person(s) identified are the beneficial owner(s), the natural person(s) who hold the</p>
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	<p>position of senior managing official(s), the obliged entities shall keep records of the actions taken in order to identify the beneficial ownership under point (i) and this point;</p>
<p>FIRST ALTERNATIVE: IF THRESHOLD IS HIGHER THAN "AT LEAST ONE SHARE", THEN APPLY "CONTROL THROUGH OTHER MEANS TEST" (-)</p>	
<p>(i) the natural person(s) who ultimately owns or controls a legal entity through direct or indirect ownership of a sufficient percentage of the shares or voting rights or ownership interest in that entity, including through bearer shareholdings, or through control via other means, other than a company listed on a regulated market that is subject to disclosure requirements consistent with Union law or subject to equivalent international standards which ensure adequate transparency of ownership information.</p> <p>A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a natural person shall be an indication of direct ownership.</p> <p>A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a corporate entity, which is under the control of a natural person(s), or by multiple corporate entities, which are under the control of the same natural person(s), shall be an indication of indirect ownership. This applies without prejudice to the right of Member States to decide that a lower percentage may be an indication of ownership or control. Control through other means may be determined, inter alia, in accordance with the criteria in Article 22(1) to (5) of Directive 2013/34/EU of the European Parliament and of the Council (3);</p> <p>(ii) if, after having exhausted all possible means and provided there are</p>	<p>(i) all the natural person(s) (who cannot be nominees, agents, proxies or equivalent), who ultimately own or control a legal entity (other than a legal entity that is a company listed on a regulated market that is subject to disclosure requirements consistent with Union law or subject to equivalent international standards which ensure adequate transparency of ownership information) through direct or indirect ownership of at least [25%, 10% or 5%] in that entity (or equivalent minimum unit of interest in an entity), including through bearer shareholdings;</p> <p>Indirect ownership means that at least one natural person own(s) at least [25%, 10% or 5%] of ownership interest in an entity, not directly but via one or multiple entities, spread over one or multiple layers.</p> <p>(ii) If no natural person meets the above criterion, then the natural person with control through other means, which may be determined, inter alia, in accordance with the criteria in Article 22(1) to (5) of Directive 2013/34/EU of the European Parliament and of the Council (3), but should include at least the natural persons with at least [25% or 10% or 5%] of voting rights, or, if nobody meets these thresholds, the top ten/twenty largest shareholders with the right to appoint or remove members of the board of directors</p>

no grounds for suspicion, no person under point (i) is identified, or if there is any doubt that the person(s) identified are the beneficial owner(s), the natural person(s) who hold the position of senior managing official(s), the obliged entities shall keep records of the actions taken in order to identify the beneficial ownership under point (i) and this point;

or to appoint or remove the senior manager, or with influence through other means.

Under no circumstance may a natural person be a nominee, proxy, agent or equivalent.

(iii) if the entity fails to provide the identity of any natural person that meets the criteria under point (i) or (ii), or if there is any doubt that the person(s) identified are the beneficial owner(s) and the entity does not cooperate to clarify the information, then the obliged entities shall terminate the business relationship with the client and refrain from executing any transactions.

~~A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a natural person shall be an indication of direct ownership.~~

~~A shareholding of 25 % plus one share or an ownership interest of more than 25 % in the customer held by a corporate entity, which is under the control of a natural person(s), or by multiple corporate entities, which are under the control of the same natural person(s), shall be an indication of indirect ownership. This applies without prejudice to the right of Member States to decide that a lower percentage may be an indication of ownership or control. Control through other means may be determined,~~

~~(ii) if, after having exhausted all possible means and provided there are no grounds for suspicion, no person under point (i) is identified, or if there is any doubt that the person(s) identified are the beneficial owner(s), the natural person(s) who hold the position of senior managing official(s),~~

	<p>the obliged entities shall keep records of the actions taken in order to identify the beneficial ownership under point (i) and this point;</p>
<p>SECOND ALTERNATIVE, WITH NO CLOSURE OF ACCOUNT (--)</p>	
<p>(ii) if, after having exhausted all possible means and provided there are no grounds for suspicion, no person under point (i) is identified, or if there is any doubt that the person(s) identified are the beneficial owner(s), the natural person(s) who hold the position of senior managing official(s), the obliged entities shall keep records of the actions taken in order to identify the beneficial ownership under point (i) and this point;</p>	<p><i>[if section (i) is not amended and remains the same:]</i></p> <p>(ii) if the entity fails to provide the identity of any natural person that meets the criteria under point (i), or if there is any doubt that the person(s) identified are the beneficial owner(s) and the entity does not cooperate to clarify the information, then the obliged entities shall record that no beneficial owner exists and keep records of the (unsuccessful) actions taken in order to identify the beneficial ownership under point (i). In addition, they should identify and verify the identity of the relevant natural person who holds the position of senior managing official, who should be identified as "senior manager" (and not as "beneficial owner"), and record details of all legal owners of the entity.</p>