
NEBOT Paper 4

The Beneficial Ownership Definition for Companies – Challenges and Opportunities

Network of Experts on Beneficial Ownership Transparency, NEBOT



The Beneficial Ownership Definition for Companies - Challenges and Opportunities

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Table of contents

| | | | |
|---|----|---|----|
| Table of contents..... | 3 | 4.1.4 Defining control via other means | 25 |
| Abstract..... | 4 | 4.1.5 Concluding remarks on the proposed BO definitions of the AML package..... | 27 |
| 1. Introduction..... | 6 | 4.2 The most transparent BO definition..... | 28 |
| 2. The policy challenges of defining “beneficial ownership” | 8 | 4.2.1 Removing control as the only prong of the BO definition | 31 |
| 3. The EU framework..... | 10 | 4.2.2 Understandable, implementable, usable, enforceable and proportionate (for simple structures)..... | 33 |
| 3.1 The AML Directive..... | 10 | 5. Conclusion | 34 |
| 3.2 Challenges affecting the implementation of the AML Directive ... | 11 | References | 35 |
| 3.2.1 Unequal transposition of the AML Directive | 11 | Annex: Dissenting Opinion..... | 36 |
| 3.2.2 The definition’s three prongs: control, ownership and benefit..... | 14 | | |
| 3.2.3 Indirect ownership..... | 17 | | |
| 3.2.4 Thresholds | 19 | | |
| 3.2.5 Rules make sense for obliged entities but not for central BO registries | 19 | | |
| 4.... The search for the “adequate” beneficial ownership information..... | 22 | | |
| 4.1 The AML Package..... | 22 | | |
| 4.1.1 Clarifying terms (at least partially) | 22 | | |
| 4.1.2 Removing the ownership element | 22 | | |
| 4.1.3 Thresholds and indirect ownership | 23 | | |

Abstract

Establishing an effective beneficial ownership (BO) definition is essential to ensure the transparency needed to tackle money laundering, tax evasion and other financial crimes. Currently, the BO definitions lack clarity, are subject to different interpretations and implementation by Member States, and most problematically, may not be identifying all the relevant individuals.

This paper analyses how the BO definition has been implemented differently in each Member State and explains the challenges and consequences related to thresholds, indirect ownership and the chosen elements (e.g. ownership, control and/or benefit).

The paper then analyses proposals for an “adequate” definition, assessing the current loopholes of the BO definition in the EU’s proposed Anti-Money Laundering (AML) Package as well as recommending the most transparent definition, considering which elements and thresholds could be used.

While many factors should be considered, e.g. proportionality, clarity, implementation, etc., in the long run, the way to check most of the boxes would be to have a highly comprehensive BO definition that covered as many individuals as possible. Once many IT and legal challenges are resolved, the BO definition could apply no thresholds in the BO definition for legal persons. This would

allow authorities to have all the information they need and make it clear how the rules are to be applied regardless of the complexity of the structure (so as not to decide how to consider indirect ownership or control). To make the definition enforceable, the criteria on control should also become more “mechanical”, i.e. similar to following a simple check list, such as identifying every natural person with a power of attorney, anyone with control over the bank accounts, anyone who participates in the board of directors, etc. While this may end up covering many individuals, it will be easier to implement and understand, rather than relying on how each individual country or user will interpret the concept of “sufficient voting rights”. However, such an approach may significantly increase the cost for obliged entities to perform their customer due diligence processes.

On the other side of the spectrum, keeping a definition with thresholds and open rules on control may make it easier to approve politically and reduce costs for the private sector, but may hinder the provision of much-needed information to determine who is currently controlling, benefitting from or owning Europe’s legal persons.

If governments are to follow an approach towards effective beneficial ownership transparency, they need to pay the costs of setting up efficient BO registries with advanced IT systems and proper verification that can be relied upon by the private sector and especially obliged entities so as not to increase their compliance costs. In other

Civil Society Advancing Beneficial Ownership Transparency

words, it should be the responsibility of governments to set up fully reliable BO registries where the private sector can find the full ownership chain up to each beneficial owner. If commercial and BO registries do not collect all relevant ownership information, governments cannot expect third parties (e.g. obliged entities) to produce this information. Instead, once central BO registries make the full ownership chain of each legal vehicle available, obliged entities and other stakeholders will be able to use this information to assess its accuracy based on more sophisticated checks and data that are only available to them, such as data on the person who withdraws money from an ATM or those with power of attorney over the account.

1. Introduction

Before the 4th AML Directive (AMLD), identifying the beneficial owner was primarily the task of a relatively small group of professionals in the service of obliged entities. An obliged entity (e.g. a financial institution, lawyer, accountant) has to carry out due diligence of customers requesting particular services or products in the course of its business. Due diligence measures are a necessary condition for the provision of these services. As part of the due diligence process, the beneficial owner of the customer is ascertained. From a general point of view, the beneficial owner is determined in an endeavour to uncover the possible existence of individuals behind a legal vehicle (e.g. a company, foundation, trust) who may be linked to money laundering, terrorist financing and related criminal activities (e.g. corruption, tax crimes, drug trafficking, human trafficking).

Recently, however, the task has also been entrusted to a wide range of legal entities and their representatives. Legal persons must now identify and record their beneficial owner in order to comply with the general registration obligation, regardless of their activities or characteristics.

Although many people have a notion of what a beneficial owner is, defining the term and the criteria to determine how to identify beneficial owners in a way

that is understood and agreed upon by all stakeholders is a challenging endeavour. The more technical and specific the regulation on beneficial ownership, the more differences arise.

If legal persons are to be successful in their efforts, i.e. if they are to come up with accurate, up-to-date and complete information, it is essential that they first understand what information they are actually required to register. Moreover, the concept of beneficial ownership must also be understood much more precisely and consistently by the obliged entities in order to avoid frictions or conflicts. Obligated entities must regularly check the BO registries to confirm the existence of discrepancies between the information contained in the register versus the information that they have collected as part of their due diligence process. The consistency in the understanding and implementation of the BO concept will also be crucial to competent authorities as they will increasingly be using BO registers and the information they hold to gather usable and comprehensible information.

In the EU, this challenge is exacerbated by the fact that the BO framework was established by a Directive which is a European legislative instrument that needs to be transposed into national legislation for its provisions to be

integrated in the legal frameworks of the Member States. There is also the ambitious requirement that all Member States' BO registries will become interconnected, requiring agreements not just at the IT level but especially on whose and what information is being registered. This creates a need to harmonise the interpretation of the BO concept in order to avoid having inconsistent, contradicting or conflicting national frameworks. The 2021 [AML Package](#)¹ tries to partially resolve this issue by proposing a Regulation (that is directly applicable in Member States, as opposed to Directives) to address some of the inconsistencies observed during the national transposition process. The provisions of said proposed Regulation are yet to be formally agreed upon by the co-legislators.

This paper presents a list of challenges that have been faced by different stakeholders in relation to the BO definition. Section 2 describes the policy challenges of the BO definition. Section 3 refers to the EU framework, including a comparison of each Member State's provisions. Section 4 offers possibilities for improving the BO definition.

¹ https://ec.europa.eu/info/publications/210720-anti-money-laundering-counteracting-financing-terrorism_en

2. The policy challenges of defining “beneficial ownership”

A BO definition (and more broadly, any BO disclosure framework) needs to strike a balance among opposing factors, including the need to be:

- Understandable by all stakeholders (e.g. competent authorities, obliged entities, legal persons).
- Implementable both by central registries as well as by the private sector in charge of collecting and filing BO information.
- Usable both in terms of the dataset it covers and the technical means through which said information is to be gathered, stored and accessed by each stakeholder (e.g. competent authorities, obliged entities, civil society organisations, journalists, investors, business people).
- Enforceable by central registries, supervisors and all competent authorities.
- Effective towards achieving all relevant goals (e.g. the fight against money laundering, tax evasion, sanction enforcement, financing of terrorism, etc.) and approaches (e.g. “reactive” in response to an investigation, or “preventive” before suspicions have arisen).

Depending on the choice of BO definition, different consequences will arise. A definition resulting in hundreds of registered beneficial owners of a single

entity may provide a great deal of transparency, but at the same time some may argue that it constitutes an intrusion into the privacy of a large number of persons (persons with no real influence or significance) and represents an administrative burden for the legal entity the private sector as well as for the registering authority (unless the available and fully-tested technological solutions are applied – otherwise noise and inaccuracies could be added, affecting the use of data). On the other hand, it is neither useful nor efficient to try to identify as few persons as possible, because even relatively important individuals in a legal entity could fall through the sieve and remain hidden.

To understand the tension among all factors, consider for instance a BO definition which required only the top shareholder to be registered. While this definition is easily understandable, implementable and enforceable, it may lack effectiveness towards achieving any relevant goal given that a criminal could control or benefit from an entity in other ways aside from being the top shareholder. On the other side of the spectrum, a BO definition could simply require the identification of “the person who is really in charge, who would be considered responsible and liable by the

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court in case of a prosecution for money laundering”. This definition would surely address the goal of tackling money laundering. While it may be understandable by many, its effectiveness may be very low, because it would depend on what each country or actor considers “being in charge”. A BO definition must strike a balance between easily implementable (mechanical) rules and more flexible principles that may adapt to the infinite types of structures of any entity.

Moreover, the chosen definition must also accommodate other general policy constraints including the need for proportionality (considering the burden for the private sector and for registry authorities) as well as efficiency (e.g. how easy it is to comply, file and register information, and then how easy it is for relevant stakeholders to use it). Although privacy concerns may also be raised, these tend to be related to public access to information, while this paper deals only with BO registration (i.e. concerning information that will be made available to authorities).

3. The EU framework

3.1 The AML Directive

The EU framework decided to strike a balance among all the contradictory factors mentioned above by incorporating the BO definition based on the Financial Action Task Force (FATF) Glossary and by applying the criteria to determine a beneficial owner based on the customer due diligence rules (CDD) of FATF Recommendation 10.

However, unlike the CDD of Recommendation 10 which applies a cascading test, the AMLD considers as the beneficial owner of a legal entity or legal arrangement anyone who meets any of the criteria. In essence, the definition covers “any natural persons who ultimately own or control the customer and/or the natural persons on whose behalf a transaction or activity is being conducted.” The criteria to determine a beneficial owner for legal persons similar to companies (i.e. corporate entities) involves identifying any individual with a direct or indirect ownership above 25% of shares or sufficient votes, or with control via other means:

(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:
(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.

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, 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);

3.2 Challenges affecting the implementation of the AML Directive

The EU AMLD's BO definition faces several challenges. First, the transposition of the Directive has not been equal and consistent across the various Member States. Second, there is criticism of the current framework from stakeholders (e.g. the private sector, civil society organisations) including issues on clarity, simplification, thresholds, and details to be registered.

3.2.1 Unequal transposition of the AML Directive

Based on the Tax Justice Network's [Financial Secrecy Index](#) published in 2022, the following table describes the differences between EU Member States on the beneficial ownership registration for companies in relation to the conditions that trigger registration; the definition's elements and thresholds on ownership, voting rights and benefits; the threshold to appoint or remove directors; and whether the definition includes cases of control via other means.

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Table 1: The BO definition in each Member State

| Country | Trigger | Ownership threshold (%) | Voting threshold (%) | Benefit threshold (%) | Appoint/Remove Board | Control via other means? |
|--------------------|----------------------|-------------------------|----------------------|-----------------------|----------------------|--------------------------|
| Austria | Multiple | 25 | 25 | - | Majority | Yes |
| Belgium | Local companies | 25 | 25 | - | Majority | Yes |
| Bulgaria | Local companies | 25 | - | - | Majority | Yes |
| Croatia | Local companies | 25 | 25 | - | Not clear | Yes |
| Cyprus | Local companies | 25 | - | - | Majority | Yes |
| Czechia | Local companies | - | “Exceeding majority” | 25 | Majority | Yes |
| Denmark | Local companies | 25 | 25 | - | Majority | Yes |
| Estonia | Local companies | 25 | 50 | - | Majority | Not clear |
| Finland | Local companies | 25 | 25 | - | - | Yes |
| France | Local companies | 25 | 25 | - | Majority | Yes |
| Germany | Multiple | 25 | 25 | - | Majority | Yes |
| Greece | Multiple | 25 | 25 | - | Majority | Yes |
| Hungary | Other | 25 | 25 | - | Majority | Yes |
| Ireland | Local companies | 25 | Not clear | - | Majority | Yes |
| Italy | Local companies | 25 | “Majority” | - | - | Yes |
| Latvia | Multiple | 25 | 25 | - | Majority | Yes |
| Lithuania | Local companies | 25 | - | - | - | Yes |
| Luxembourg | Multiple | 25 | “Majority” | - | Majority | Yes |
| Malta | Local companies | 25 | 25 | - | Majority | Yes |
| Netherlands | Multiple | 25 | 25 | 25 | Majority | Yes |
| Poland | Local companies | 25 | 25 | - | Majority | Yes |
| Portugal | Being (tax) resident | 25 | Not clear | - | - | Yes |
| Romania | Local companies | 25 | - | - | - | - |
| Slovakia | Local companies | 25 | 25 | 25 | Any | Yes |
| Slovenia | Multiple | 25 | 25 | - | Majority | Yes |
| Spain | Other | 25 | 25 | - | Majority | Yes |
| Sweden | Multiple | - | 25 | - | Majority | Yes |

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References:

Trigger: **Austria:** domiciled in Austria and foreign companies intending to acquire land. **Germany:** local companies and foreign ones which acquire land or interests in companies which own land. **Greece:** companies that have a permanent establishment and file tax returns, or which are based in Greece. **Hungary:** It is not clear if only bank account managers or any obliged entity can register the beneficial owners of the entities they engage with. While not all companies must engage with a bank, they must all engage with a notary (obliged entity). **Latvia:** local incorporation and apparently having a permanent establishment. **Luxembourg:** local incorporation and foreign subsidiaries registered in the commercial register. **Netherlands:** companies established in the Netherlands, and all legal entities with their statutory base in the Netherlands. **Slovenia:** being registered in the commercial register or the tax register. **Spain:** the headquarters of their effective management or their main activity in Spain, or that are administered or managed by natural or legal persons resident or established in Spain, or domiciled in Spain which deposit accounts. **Sweden:** Swedish legal persons and foreign ones which conduct business in Sweden.

Voting threshold: In **Ireland** and **Portugal**, while the law doesn't refer to a specific threshold, the guidance mentions 25% of voting rights. In **Belgium**, the law refers to a sufficient threshold (25% being a sufficient but not necessary condition to meet the "sufficient" condition).

Appoint/remove the board: In **Croatia**, while the translation of the law is not clear, the Peer Review report by the Global Forum described that it would include "powers for appointing the high-level management", but it is not clear if this refers to any senior management or the majority of them.

Control via other means: In **Estonia**, while the BO definition refers to "control via other means", this is not specifically mentioned among the criteria to determine who must be identified as a beneficial owner.

As the table shows, the Directive has been transposed in very different ways. As regards triggers for when BO information must be filed with a government authority, most countries require local companies to register their beneficial owners consistent with the AMLD. Many countries have "multiple" triggers, which include registration of local companies (as required by the Directive) as well as other situations, such as companies with a permanent establishment. Portugal requires registration based on the tax residency (which apparently also covers local companies because tax residency is based on having the legal seat in Portugal). Spain requires registration based on having the headquarters and the main activity in Spain, and it is unclear if this would cover all companies incorporated in the country. In Hungary, it is not clear if only bank account managers or any obliged entity can register the beneficial owners of the entities they engage with. While not all companies must engage with a bank, they must all engage with a notary (obliged entity). If only banks are able to file BO information, this would result in another implicit condition: being a local company plus having a local bank account.

With regard to the prongs and thresholds, while most countries apply the 25% ownership threshold (Hungary and Slovakia establish it as "at least", most others as "more than"), Czechia and Sweden do not apply an ownership threshold per se. Belgium provides that beneficial owners are those natural persons with a sufficient

Civil Society Advancing Beneficial Ownership Transparency

percentage of shares owned or voting rights under control. Most countries apply a threshold for the voting rights of 25% (although the AMLD refers just to “sufficient” voting rights), while Estonia applies a threshold of 50% and some countries refer to a “majority” of votes (e.g. Luxembourg or Italy) or even “significantly exceeding the shares of voting rights of other persons” (e.g. Czechia). Other countries do not set a specific threshold for voting rights (e.g. Bulgaria, Cyprus, Lithuania and Romania). As for the benefit element (e.g. rights to dividends), only Czechia, the Netherlands and Slovakia apply a 25% threshold. Many countries also consider a beneficial owner to be an individual who may appoint or remove a majority of the board of directors. Slovakia is the only country that has made the appointment or removal of any director (not the majority) a qualifier, while Finland, Italy, Lithuania, Portugal and Romania do not apply this element. In the case of Croatia, it is not clear what the threshold is. Finally, most countries also require the identification of any individual with other means of control, except for Romania (in Estonia, while the BO definition refers to control via other means, it is not clear if this is part of the criteria to determine who the beneficial owner is).

3.2.2 The definition’s three prongs: control, ownership and benefit

The way the AMLD incorporates the BO definition from the FATF creates confusion because it is too specific to obliged entities’ customer due diligence. For instance, it

refers to “customer” and “transactions”. The consequence of this is that the BO definition could have two possible interpretations. One is “literal”, resulting in part of the BO definition that refers to “transactions” as being irrelevant and inapplicable to BO registration of legal persons. The other interpretation is “holistic” and thus giving a more “applicable” interpretation to the part on “transactions”, by considering it to refer to anyone benefitting from the legal vehicle (the “benefit” element).

Specifically, the AMLD definition, stemming directly from the FATF, states: *“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”*.

Assuming that “customer” refers to “legal person”, a literal interpretation of the remaining part of the definition would suggest that the BO definition covers only anyone who ultimately owns or controls the legal person (ownership and control prongs), while the rest of the definition regarding “transaction or activity” would only make sense for an obliged entity but is inapplicable to the BO definition of legal persons as part of BO registration. In other words, a bank should identify cases where a bank transfer is on behalf of an individual who has no ownership or control over a customer, but this would be irrelevant for BO registration in central registries.

On the other hand, a “holistic” interpretation considers that the full

Civil Society Advancing Beneficial Ownership Transparency

definition is relevant (in fact, the term “customer” must already be interpreted as “legal person”). In this case, the last part of the BO definition on “*and/or the natural person(s) on whose behalf a **transaction or activity** is being conducted*” should refer to a natural person who benefits from a legal person.

In fact, the [FATF](#) seems to use this sentence to refer to cases when the ownership and control structure is deliberately created to avoid identifying a person who is indeed benefitting, and should thus be identified as well: “Another essential element to the FATF definition of beneficial owner is that it includes natural persons on whose behalf a transaction is being conducted, even where that person does not have actual or legal ownership or control over the customer... This element of the FATF definition of beneficial owner focuses on individuals that are central to a transaction being conducted even where the transaction has been deliberately structured to avoid control or ownership of the customer but to retain the benefit of the transaction.”²

Given the relevance of “ownership”, “control” or “benefit” as relevant elements to determine “beneficial ownership” (in other words, authorities should know the

identity of anyone with either ownership, control or benefit over a legal person), this paper considers that the BO definition in the AMLD should be interpreted as referring to these three elements. This is also explicitly considered in the BO definitions of some countries including the Netherlands, Slovakia (see the table above) or the US.³

Based on the explanation above, while the AMLD’s BO definition suggests that three elements (ownership, control and benefit) have equal worth in the definition, the criteria to determine who a beneficial owner is focuses on ownership and control, but not on benefits.⁴ It is based on passing a threshold of direct or indirect sufficient number of ownership (above 25%, but Member States may establish lower ones) or having control based on a direct or indirect “sufficient number of votes” or having “control via other means” (this may be determined based on Directive 2013/34/EU).

As for the hierarchy of ownership and control, they appear to be equal, where anyone meeting any condition is considered a beneficial owner, rather than applying a cascading test where only one condition is

² FATF Guidance “Transparency and Beneficial Ownership” 2014, pp 8-9.

³ The US Corporate Transparency Act of 2019 is clearly based upon similar line of thought, as its definition of a beneficial owner includes a person who “(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.” Available online [here](#) on the US Congress website.

⁴ The criteria to determine beneficial owners is also based on the FATF customer due diligence rules which face the same contradiction. While the BO definition refers to ownership, control and anyone on whose behalf a transaction or activity is being conducted, the due diligence rules only refer to ownership and control, but not to activities or transactions.

checked, and the second one is considered only if no one has passed the first condition.

Therefore, the AMLD definition departs from the FATF CDD of Recommendation 10⁵ because the FATF only focuses on the “control” element and because such control is established based on a cascading test: the first test is anyone with control through ownership (“ultimately having a controlling ownership interest in a legal person”, which may be based on a threshold, e.g. more than 25%). The second test, in case no one has been identified or in case of doubt, requires the identification of anyone exercising “control through other means”.

It is not clear if the AMLD deliberately tried to differentiate itself from the FATF, or if this was an innocent choice of words by legislators. By establishing two elements, ownership and control, the AMLD solves one of the criticisms against the FATF which only focuses on control. By disregarding the cascading test, it also expanded the number of beneficial owners that may be identified.

The criticism of the FATF is that it appears to focus only on “control”, and it suggests a threshold “e.g. more than 25%” to determine the presence of control. However, it results in anyone passing that

threshold being identified as a beneficial owner, even if they have no control at all, which is supposed to be the focus of the FATF. To understand this criticism, imagine a company with two shareholders. John has 26% of the shares and votes, while Mary has the remaining 74%. Based on the FATF thresholds, both individuals would have to be identified as beneficial owners, even though it is clear from the structure that only Mary has control, because with 74% of the votes she can make all decisions regardless of John’s opinion. [If John’s 26% share is to be manifestation of control (controlling ownership interest), the term control must be understood against its common meaning. That is, a “control” in the sense of the FATF is something that is not actually a control at all.]

In the case of the AMLD, it would make sense to identify both individuals because the definition doesn’t suggest that “more than 25%” is an indication of having a “controlling ownership” or “control”. The AMLD simply requires the identification of anyone passing the ownership threshold. The criticism, however, is that 25% becomes an arbitrary number and there is no explanation of how this threshold enables the identification of anyone involved in

⁵ “For legal persons: (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 interest in a legal person; and (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. (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.

* 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%).”

Civil Society Advancing Beneficial Ownership Transparency

money laundering, either from a reactive or preventive approach. In addition, the threshold is considered too high by some, as will be explained below.

As for the control element, the AMLD fails to set a threshold to determine a “sufficient number of votes”. It does offer examples of what “control through other means” may be. These open provisions have the consequence, as illustrated by the Table above, that every EU country may legally choose different thresholds for voting rights or to determine control via other means, such as requiring a threshold of removing or appointing either a majority or just one director. The fact that the AMLD does not define the term “control” also generates confusion.

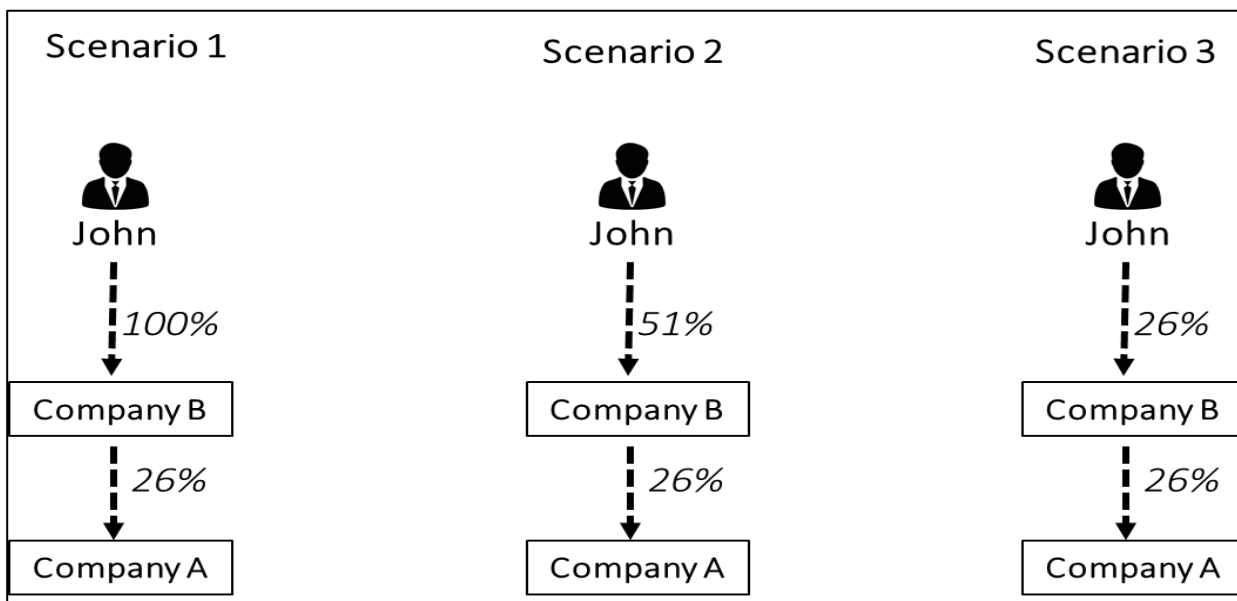
Assuming the AMLD intended to include the “benefit” element in the definition by referring to “on whose behalf an activity or transaction is conducted”, there is a contradiction in the fact that the “benefit” element is not mentioned in the criteria, nor are any thresholds for benefits established.

3.2.3 Indirect ownership

Another criticism is the lack of clarity on the determination of indirect ownership. The AMLD establishes: “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.”

The next figure (on the following page) illustrates three possible scenarios, and the question is whether John would always have to be identified as a beneficial owner of Company A or not.

- In the first scenario it is obvious that John would have to be identified as a beneficial owner: he indirectly owns more than 25% of Company A and he has full control of Company B.
- In second scenario, John would likely be considered a beneficial owner based on the AMLD definition which requires a “shareholding of more than 25% held by an entity under the control of the individual”. Although John indirectly holds just 13.26% of Company A (51% x 26%), Company B holds more than 25% of Company A and Company B is under the control of John because he has more than 50% of the shares and votes.
- Finally, in the third scenario, John would be unlikely to be considered a beneficial owner, unless a country required the “more than 25%” threshold to be tested at every level. In this case, although John indirectly holds just 6.76% of Company A, he would be considered a beneficial owner of Company B for holding more than 25% of Company B’s shares.

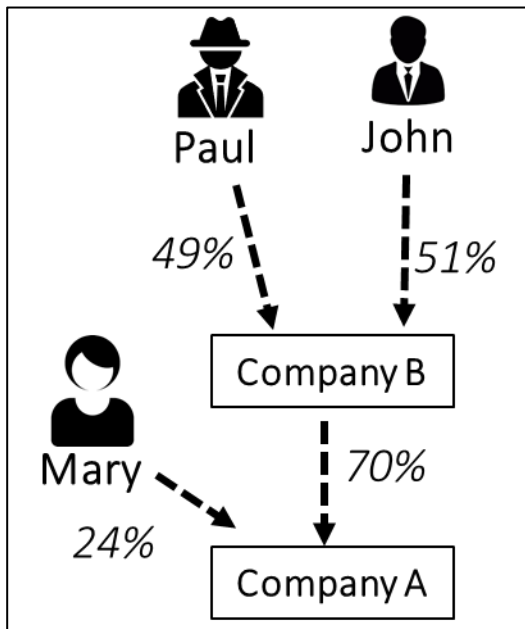


In addition to determining which scenario the AMLD definition applies to (most likely scenarios 1 and 2), identifying John as a beneficial owner in scenarios 2 and 3 may lead to another contradiction. Suppose that Company A is also owned by Mary, who directly holds 24% of the shares and votes of Company A. In all three cases, Mary would not be considered a beneficial owner of Company A, even though she holds more shares than John in scenarios 2 and 3. In other words, in scenario 2, John would be considered a beneficial owner with an indirect ownership of 13.26% while Mary would not be considered a beneficial owner despite holding 24% of the shares and votes. The situation is more extreme under scenario 3, because in this case John is the beneficial owner with only 6.76% while Mary is still excluded despite having 24%.

An even more extreme situation is illustrated by the next figure (on the following page). In this case, John would likely be considered the beneficial owner

because he controls Company B with 51% and indirectly holds 35.7% (51% x 70%) of Company A. Mary, still directly holding just 24% of Company A, would not be considered a beneficial owner. The question is what happens with Paul. He holds only 49% of Company B, so he is clearly not in control, which appears to be the AMLD's criterion. However, by holding 49% of Company B, not only does he meet the threshold of holding more than 25% of Company B, but he indirectly holds 34.3% of Company A (49% x 70%), yet he may still not

be considered a beneficial owner of Company A.⁶



3.2.4 Thresholds

The criticism on thresholds considers whether a “25% threshold” is adequate to address the risk of money laundering and other illicit financial flows. There seems to be no rationale of how that threshold would lead to identifying the relevant individuals. In fact, as it has been widely warned, a basic ownership structure of four shareholders with equal holdings would result in having

no beneficial owners (no one would pass the “more than 25% threshold”).

In fact, an [investigation](#) by Kroll into the Moldovan Laundromat proved that even a threshold of 5% was easy to circumvent:

“On 17 August 2012, all of the bank’s shares were sold and transferred to 21 new shareholders, each with a stake between 4.5% and 4.99%. A shareholder who held a stake of at least 5% was classified as a significant shareholder, with their acquisition subject to formal approval by the NBM [National Bank of Moldova]. The process was therefore circumnavigated by this scheme.”

3.2.5 Rules make sense for obliged entities but not for central BO registries

The AMLD BO definition for BO registration in central registries is based on and adapted from the FATF CDD rules of Recommendation 10. Not only is this clear from the almost identical wording, but also by the retention of terms which do not make sense in the central register context.

⁶ On the one hand, by indirectly holding 34.3% of Company A, Paul may be considered a beneficial owner. However, for indirect ownership, the Directive refers to having “control” over the entity (Company B) that holds more than 25% of the Customer (Company A). Given that Paul has no “control” over Company B, one could interpret that he is not a beneficial owner of Company A: “an ownership interest of more than 25 % in the customer [Company A] held by a corporate entity [Company B], which is **under the control of a natural person(s)** [John, but not Paul]... shall be an indication of indirect ownership.”

Civil Society Advancing Beneficial Ownership Transparency

The AMLD definition refers to anyone “*who ultimately owns or controls the customer*”.

An obliged entity has customers, but a central register does not. The main problem is much more serious than the nuance of the term “customer” or “entity” (which is in any case widely understood). The problem with this shortcut of copy-pasting from a different context is that the FATF BO definition and CDD regulations are actually “principles” which are supposed to be applied by obliged entities and designated non-financial businesses and professionals (DNFBPs) such as lawyers and notaries when engaging with a new customer.

A bank employee is supposed to take the time to analyse the customer’s documents and, based on their expert opinion, consider who is a beneficial owner in terms of having a controlling ownership. The [FATF](#) itself is very clear that using a threshold is just one possibility to determine controlling ownership. If a threshold is chosen, then the figure of “more than 25%” becomes just one possibility within that first possibility, or to put it differently, an example within an example:

“The identity of the natural persons...who ultimately have a controlling ownership interest³⁵ in a legal person.

35. 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%).”

In other words, the bank employee may use a threshold as a reference point, but the “principle” obligation is to determine who has a controlling ownership in each specific case, based on all the specific circumstances of each customer.

In contrast, the EU needed a definition and criteria to be applied by central registries, many of which would never engage with the entity that is registering its beneficial owners. In other words, especially in cases of remote incorporation, there would be no person checking the documents or the structure, or trying to understand the specific circumstances of each entity. For registration of entities *en masse*, principles cannot work. Mechanical and clear rules are necessary. In this case, thresholds must become compulsory, not just indicative.

The EU rightly transformed the principle-based FATF recommendations into applicable rules that can easily be checked. However, by making the 25% threshold set in stone rather than a reference point, it created too much rigidity, making circumvention very easy, as explained in the point above.

Establishing rules rather than principles was the right approach to make them implementable. However, they result in thresholds which are too high to achieve the goal of identifying anyone who may be responsible for money laundering or other financial crimes.

Civil Society Advancing Beneficial Ownership Transparency

Both the FATF and the AMLD also offer a residual to identify “anyone with control through other means”, in case the real beneficial owner is not determined through the ownership threshold test. However, expressed in this way, it becomes a principle which is capable of capturing the right beneficial owner (if properly complied with), but it becomes impossible to be easily implementable in practice. For this reason, as the table above indicates, many countries transformed the “control via other means” into practical rules such as considering a vote threshold (more than 25% of votes) or the right to appoint or remove a majority of the board of directors.

The criticism here is that having two or three conditions may help as reference points for a “principle”, giving sufficient flexibility to whoever is applying it in practice. However, when the conditions become part of mechanical rules, just having two or three conditions may be insufficient, especially if thresholds are high. To put it in perspective, it would be one thing to allow an employee to buy a used car for the company by allowing them to use their judgement but giving them some reference point such as: “try not to spend more than \$10 000, make sure the car is working fine, i.e. as no strange noises when you drive and ideally not too old”. It would be quite different for the company to tell the employee to “buy any car that costs less than \$10,000, doesn’t make noise when you drive and is not more than 5 years old”.

4. The search for the “adequate” beneficial ownership information

The previous section described criticisms to the current AMLD BO definition. This section will explore various alternatives to improve the definition.

4.1 The AML Package

On July 20, 2021, the European Commission presented a package of legislative proposals to strengthen the EU’s rules to tackle money laundering and to counter the financing of terrorism known as the AML Package. The package includes, among other things, a proposal for a Regulation on anti-money laundering and combating the financing of terrorism (AML/CFT) and a proposal for a new AML Directive which would replace the current one.

4.1.1 Clarifying terms (at least partially)

The new BO definition under Art. 2(22) of the AML Package’s Regulation corrects the AMLD definition by referring to a “legal entity or express trust or similar arrangement” instead of a “customer” (which stemmed from the CDD of FATF Recommendation 10). It also explicitly refers to “benefit”, although it still makes reference to a transaction or activity. It would be clearer if the definition were changed to refer to “benefitting from the legal entity or express trust” to clearly

confirm the “benefit prong” of the definition. The table on the following page shows the differences (in bold) between both definitions.

4.1.2 Removing the ownership element

The proposed criteria to determine the identity of the beneficial owner gets closer to the FATF CDD of Recommendation 10 by removing “ownership” as an element that could be present in isolation (even without control) and leaving only the focus on “control”, which can be exercised either through ownership or through other means. This could be consequential if lower thresholds were to be chosen. For instance, if a country were to choose a “no threshold” approach (assuming the proposal changes its current provisions on thresholds and allows for this choice), someone could argue that such a “no threshold” approach is contrary to the Directive, because a person with just one share would have (just) “ownership” but not “control”. In other words, while “ownership” is still kept as an element in the proposal, it only works if that ownership also involves control, but not if it refers to mere ownership without control.

Unlike the FATF, the proposed Regulation does not apply a cascading test, and either manner of control (through ownership or

Civil Society Advancing Beneficial Ownership Transparency

through other means) is equally applicable to identify an individual as a beneficial owner.

The next table shows the differences (in bold) between both definitions.

Table 2: Prongs in the BO definition of the AMLD and the AML Package

| AMLD | AML Package's Regulation |
|---|--|
| Art. 6(3)(a) in the case of corporate entities: (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... | Art. 42(1): In case of corporate entities, the beneficial owner(s) as defined in Article 2(22) shall be the natural person(s) who control(s) , directly or indirectly, the corporate entity, either through an ownership interest or through control via other means. |

By removing “ownership” as an independent element from the criteria to determine a beneficial owner, the proposed Regulation is subject to the same criticism that applies to the FATF. First, it creates a contradiction with the definition which covers “ownership” and “control” (and maybe “benefits”), while the proposed criteria now focus only on “control”.

As will be explained below, by focusing on “control”, it creates a confusion where a person passes the threshold to be considered a beneficial owner based on ownership, but lacks control, e.g. the example of a beneficial owner with 26% of shares while the other beneficial owner has total control with 74%. One solution would be to use a term different from “control”, e.g. “exercise power over the corporate entity”, or adding an explanation that

“control” in the BO definition has a special meaning and should not be considered equivalent to the “control” used in other frameworks, e.g. under commercial companies regulations.

4.1.3 Thresholds and indirect ownership

In an attempt to establish consistency, the proposed regulation removes the option for Member States to establish lower thresholds. On the positive side, the proposed regulation clarifies the ambiguity on indirect ownership by establishing that the threshold test has to be applied to each level of ownership. This also reduces costs for obliged entities and companies operating in more than one country because the same threshold applies in all EU countries.

Table 3: Thresholds in the BO definition

also increases the number of beneficial

| AMLD | AML Package’s Regulation |
|---|---|
| <p>Art. 6(3)(a) in the case of corporate entities: ...</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. 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.</p> | <p>Art. 42(1): In case of corporate entities...</p> <p>For the purpose of this Article, ‘control through an ownership interest’ shall mean an ownership of 25% plus one of the shares or voting rights or other ownership interest in the corporate entity, including through bearer shareholdings, on every level of ownership.</p> |

The negative aspect of the consistency on the threshold is that now all Member States will have to implement a threshold of “more than 25%” which has already been described above as too high to allow for the identification of all the relevant individuals who may be involved in a financial crime (recall the previous case of the Moldovan Laundromat where thresholds were artificially kept below 5%). In addition, some countries (e.g. Hungary and Slovakia) were already implementing the slightly lower threshold of “at least 25%”. In this regard, in other regions, e.g. Latin America, countries have established much lower thresholds such as 15%, 10%, 5% and even no threshold at all.

owners that can potentially be identified. As described in the example above, the proposed Regulation is opting for scenario 3, where “John” would be a beneficial owner just for holding 26% of Company B which in turn holds 26% of Company A. However, this does create a contradiction against a direct shareholder. While John will have to be identified as a beneficial owner despite having indirectly just 6.76% of Company A, Mary would not need to be identified despite directly holding 24% of

By requiring the indirect ownership threshold to be applied in every case, the proposed Regulation becomes clearer and

Company A.⁷ The proposed approach involves a certain randomness in the result.

4.1.4 Defining control via other means

While the current AMLD gives examples of cases involving “control through other means” only by referring to articles of the Directive on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, the proposed Regulation keeps the reference to the articles of that Directive but it adds specific criteria to determine “control through other means”.

⁷ This problem can also occur on higher levels of the structure. e.g. when the direct shareholder is company A with 30%, whose shareholders are John with 25% and company B which has 30% and its shareholders are Mary with 70% and Paul with 30%. John will not be the beneficial owner (with an indirect interest of 7.5%) because of his insufficient 25% share, but Mary (with an indirect interest of 6.3%) and Paul (with an indirect interest of 2.7%) will.

Table 4: Control via other means

| AMLD | AML Package's Regulation |
|--|--|
| <p>Art. 6(3)(a) in the case of corporate entities: ...</p> | <p>Art. 42(1): In case of corporate entities...</p> <p>For the purpose of this Article, 'control via other means' shall include at least one of the following:</p> <p>(a) the right to appoint or remove more than half of the members of the board or similar officers of the corporate entity;</p> <p>(b) the ability to exert a significant influence on the decisions taken by the corporate entity, including veto rights, decision rights and any decisions regarding profit distributions or leading to a shift in assets;</p> <p>(c) control, whether shared or not, through formal or informal agreements with owners, members or the corporate entities, provisions in the articles of association, partnership agreements, syndication agreements, or equivalent documents depending on the specific characteristics of the legal entity, as well as voting arrangements;</p> <p>(d) links with family members of managers or directors/those owning or controlling the corporate entity;</p> <p>(e) use of formal or informal nominee arrangements.</p> |
| <p>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>Control via other means may be determined also in accordance with the criteria of Article 22(1) to (5) of Directive 2013/34/EU.</p> |

The proposed regulation adds many relevant criteria to determine control through other means, such as the right to appoint or remove the majority of the board of directors (as Table 1 shows, most Member States already apply this, though some use lower thresholds than the majority), rights to veto or decide on profit distribution or changes in assets, formal or informal agreements to vote or control in other ways, control through family links or the use of formal or informal nominees.

By referring to “at least one of the following” (criteria) as control via other means, the proposal could be interpreted as an exhaustive list rather than an illustrative list of examples which allow for other cases not contemplated in the lists. (An alternative would be to write “control via other means’ ~~shall~~ **may include, for illustrative purposes, one or more of the following (as well as other criteria):**”). In addition, while these are relevant criteria and are rightly open and flexible, they lack a more mechanical rule that would make it easier to implement, such as disclosing anyone with a power of attorney. On the

one hand, the Regulation could clarify that this is not an exhaustive list and add the residual “or any other forms of control” in case any other form of control is developed in the future. On the other hand, adding this residual could lead to divergences across countries and obliged entities, creating more inconsistencies and discrepancies.

An alternative would be to offer an explicit definition of control and then determine when control is deemed to exist (e.g. whenever an individual has more than X % of the shares) and when control may exist (control via other means).⁸

4.1.5 Concluding remarks on the proposed BO definitions of the AML package

Overall, the proposed BO definition of the Regulation clarifies some terms (e.g. “legal entity or express trust” to replace “customer”) and scenarios (e.g. applying the threshold test to each level of ownership). It also explicitly adds extensive criteria to determine control through other means and promotes consistency by eliminating some

⁸ One proposal to rearrange the BO definition on control would to say for instance: “Control” is the possibility of exercising directly or indirectly significant/decisive influence on the decisions taken by the corporate entity, including veto rights, decision rights and any decisions regarding profit distributions or leading to a shift in assets, based on one’s own discretion, regardless of whether and on the basis of which legal fact it is exercised. Control is always deemed to exist (without the possibility to prove otherwise) when an individual has the direct or indirect ownership (or voting rights) of xx% of the interests in a legal person (if there is to be a threshold) or the right to appoint or remove more

than half of the members of the board or similar officers of the corporate entity. Control may be shared by several persons and may be exercised for example through/with: a) formal or informal agreements with owners, members or the corporate entities, b) provisions in the articles of association, partnership agreements, syndication agreements, or equivalent documents depending on the specific characteristics of the legal entity, as well as voting arrangements and trust agreement or deed; c) links with family members of managers or directors/those owning or controlling the corporate entity; d) use of legal arrangements; e) use of formal or informal nominee arrangements.

choices by Member States (e.g. to apply lower thresholds).

However, the last point may be the most negative from an implementation perspective. One could argue that at the end of the day, countries all over the world face challenges in terms of compliance, enforcement and verification of BO registration. This means that despite current definitions being open enough to require the identification of anyone with control via other means, the vast majority of companies simply apply in practice the threshold test and identify those with more than 25% of shares or votes. This is also the easiest to check and validate with a system, whereas confirming who is in control through other means would require analysing all corporate documents, shareholder meetings and knowing all informal relations within a company. For this reason, the key criterion that determine how many individuals will be identified as beneficial owners in practice may relate to the ownership or voting threshold. By requiring all Member States to apply the “more than 25%” threshold, the Regulation may be going against implementing the needed transparency that is easier to check.

Support for lower (or no) thresholds has also been mentioned by the FATF. However, the FATF suggests this only in cases of higher risk, but not by default for all legal vehicles. The Interpretative Note to Recommendation 10 states that in cases with money laundering risk, no thresholds should be applied:

If, during the establishment or course of the customer relationship, or when conducting occasional transactions, a financial institution suspects that transactions relate to money laundering or terrorist financing, then the institution should: (a) normally seek to identify and verify the identity of the customer and the beneficial owner, whether permanent or occasional, and irrespective of any exemption or any designated threshold that might otherwise apply. (emphasis added).

The AML Package could also include the possibility of applying lower thresholds in cases of high risk, e.g. for certain types of legal vehicles, or for legal vehicles where a politically-exposed person is an owner, or for companies in certain sectors, e.g. extractives.

4.2 The most transparent BO definition

In response to the criticism of the BO definitions of the current AMLD definition, the FATF and the proposed Regulation of the AML Package, there is a more comprehensive definition that could be proposed in the long term, as long as central BO registries are required to collect and make available this information to stakeholders, rather than requiring third parties such as obliged entities to produce this data.

A rule on how to identify a beneficial owner without thresholds addresses all the issues

Civil Society Advancing Beneficial Ownership Transparency

raised on the other definitions and rules while also increasing the chances of being understood, used and enforced. However, it may result in challenges in terms of implementation and proportionality, and it would increase the compliance costs by the private sector, unless governments make this information available.

The most transparent BO definition has the following elements:

1. It covers all elements in equal hierarchy: ownership,⁹ control or benefit.¹⁰
2. It applies no thresholds (anyone with at least one share should be a beneficial owner).
3. It adds mechanical rules to the determination of “control via other means”, e.g. having a power of attorney to manage the entity or its bank account.

The main criticism against this comprehensive approach is that it is not proportional, that it would increase costs both for the legal entity and obliged entities, and that the IT systems of most obliged entities and BO registries may be unable to accommodate so many beneficial owners. In such a case, this most transparent approach would add high costs while lowering effectiveness (there may be too much noise, creating challenges to

verify information or to determine the relevant beneficial owners).

From a “conceptual” perspective, although this approach may sound too ambitious, the reality is that it is precisely the approach applied by the AMLD and the FATF in the BO definition for trusts and for private foundations which are legal persons. For these, all the parties of the trust/foundation must be identified (mechanical rule) without applying any thresholds (point 2) and covering all elements (point 1): “ownership” over the trust assets held by the trustee and by the settlor (formerly) and by the beneficiaries (in the future); “control” over the trust management held by the protector and potentially the settlor or the trustee; and “benefits” over the trust assets in favour of the beneficiaries.

Another benefit of the most transparent approach is that by applying no thresholds, there are no further contradictions in case of indirect ownership, or when a company is a party to the trust.¹¹ All the individuals with any share, vote or rights to dividends in every layer would have to be identified.

Nevertheless, even if the most transparent approach is considered the ultimate means of achieving complete transparency, some practical factors must be considered.

⁹ This should include having interests through financial instruments, e.g. call/put options, futures, convertible stock, etc.

¹⁰ This should include having contracts or arrangements to obtain profits, dividends, etc. from a legal person.

¹¹ Otherwise, if a party to the trust, e.g. the beneficiary is a company, then instead of identifying all the shareholders of the company as beneficial owners of the trust, it would only be necessary to identify those individuals with more than 25% of shares or votes over the corporate beneficiary as beneficial owners of the trust.

Civil Society Advancing Beneficial Ownership Transparency

On the one hand, the main factor relates to the IT capabilities. This comprehensive approach may need to wait until BO registries are equipped with appropriate IT systems that can collect and process much more information (e.g. identifying hundreds of entities and individuals involved in a complex ownership chain, rather than identifying just one single senior manager).

Another consideration is discrepancy reporting by obliged entities. In the case of customers with complex ownership structures, discrepancy reporting covering hundreds of individuals instead of just one senior manager may indeed increase costs. However, it will be necessary to determine the proportion of customers that have complex ownership structures. In other words, if most of the customers of a bank are entities with a very simple structure, expanding the definition to cover any individual with at least one share would not make a difference. If an entity has two individuals as the only shareholders and beneficial owners, then the bank will need to identify those two individuals, either where the BO definition applies a 25% threshold or where “any individual with at least one share” has to be identified.

To tackle the potential costs to the private sector, especially for obliged entities, it should be the responsibility of the central BO register to collect and make available the full ownership chain of each legal vehicle up to each beneficial owner (without applying thresholds) and ensuring that this information is verified. This way, third

parties, including obliged entities, will be able to obtain from BO registries the full ownership structure of their customers. Instead of merely checking for costly discrepancy reporting involving typos and honest mistakes, the complementary verification by the private sector would be based on more sophisticated checks which are not available to BO registries, such as considering who is withdrawing money from the ATM or managing the account, or analysing transfers of money or relationships among bank accounts. In other words, before expanding the BO definition as a cost shifted to obliged entities, countries should invest in establishing effective BO registries with the right IT and verification capabilities which make the full ownership information available to relevant stakeholders.

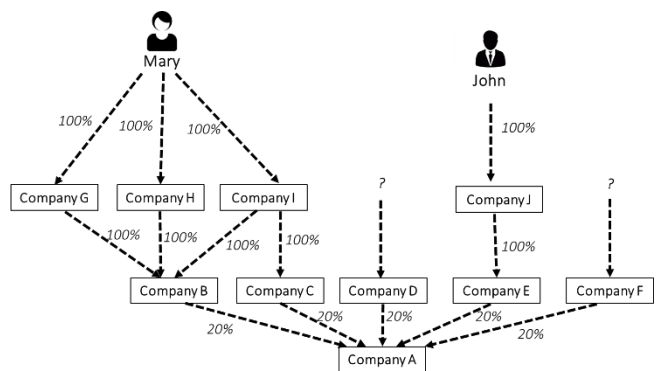
In a way, regardless of the BO definition established by a country, either “more than 25%” or “anyone with at least one share”, **both legal entities and obliged entities must already identify all individuals with at least one share**. The only difference is that in the narrow approach, after identifying all individuals with at least one share, legal entities and obliged entities must only “register or collect information about” the individual with “more than 25% of the shares”, while in the most comprehensive approach, “all individuals with at least one share” must be registered.

Consider a company with a very complex structure. Company A is owned by five other companies, each of them with 20%:

companies B, C, D, E and F. If the BO definition required the identification of just “direct” holders of more than 25% of the shares, then Company A would simply say that no beneficial owner exists and instead identify a senior manager. However, the definition covers both direct and “indirect” ownership. It may be the case that beneficial owner Mary has “indirectly” more than 25% control over Company A through companies G, H, and I which own companies B and C. The only way to know that Mary exists (or to check if any other individual has indirectly more than 25% over Company A) is to know the entire structure of Company A up to every natural person shareholder, so as to then aggregate all of their shareholdings to see if they pass the 25% threshold. It could be the case that John owns 20% of Company A through companies E and J. However, it is not possible to discard John as a beneficial owner (for “indirectly” having “merely” 20%) unless the ownership structures of companies D and F are determined too, because it could be the case that John owns an extra 6% through companies D and F.

In conclusion, regardless of the BO definition, as long as indirect shareholdings are relevant, all individuals with at least one share must be identified to ensure that none of them have directly or indirectly more than 25% of the shares.

The problem is that if central registries do not collect and make this information available, then obliged entities must request this from their customers. This would



demand more resources from obliged entities to significantly expand their due diligence checks and dilute their ability to dedicate the necessary resources and focus on areas of high risk, thereby rendering the requirements less effective. In addition, even if the customer provides the data, obliged entities have no way to check this information at the corresponding register. That is why the information should be given to obliged entities (as well as other stakeholders) from central registries.

4.2.1 Removing control as the only prong of the BO definition

First, even if identifying “the individual who is really in control” were the only goal of the BO definition, its enforcement as such would be impossible. The law could command the BO data collector, either an obliged entity or a BO registry, to register the individual who is really in control. Prescribing this in the law is very easy and generic. On the contrary, complying with this requirement and supervising compliance is extremely difficult if not impossible.

Second, most BO data collectors lack the means or incentives. For instance, a bank

Civil Society Advancing Beneficial Ownership Transparency

has to find a balance between the goal of having more customers and transactions to make more profits and the compliance risks of enabling money laundering. Even if AML regulations and sanctions are applied to reinforce the compliance department of financial institutions, the bank may not be able to obtain all the relevant data from the customer (e.g. a secret letter of intent, etc.) to know who is really in control.

Moreover, determining the person who is really in control may make more sense for a financial institution given the requirement to conduct customer due diligence in addition to having financial information about the account during the whole bank-client relationship: who manages the account, how much money they receive and transfer, and to whom, etc. In contrast, a BO register lacks the staff or the requirements to conduct due diligence and more importantly, they do not receive any more details on the company until the filing of accounts or annual returns (which cannot be analysed, except for the missing of fundamental formalities). In other words, while a financial institution must (and could) spend more resources to determine who is in control, this becomes impossible for a BO register.

Another reason why focusing only on the real BO with control is insufficient is because this only serves as a “reactive” approach once a legal vehicle is already found to be involved in illegal activity and authorities are looking for the person who is ultimately responsible. Instead, a much

more useful approach is to use BO information preventively, before suspicions even arise. By having information on as many BOs as possible, authorities may run analytics to find red flags such as nominees pretending to be the BOs of hundreds of companies. In addition, this comprehensive approach also allows for the detection of unknown relationships to other legal vehicles and individuals. If one of these entities or individuals is found to be committing illegal activities, authorities will already hold information on all the other persons or entities that they are connected to, allowing the full network to be prosecuted and dismantled.

The solution is thus to identify as many individuals as possible hoping that the real controller will also be identified among them. Having information on all individuals related to an entity could be considered proportionate if it is the only way for authorities to conduct preventive analysis (e.g. whether a BO owns or controls thousands of companies, indicating that this may be a nominee). In addition, once authorities are investigating an entity, they would already have information on all potential responsible individuals as well as all the other individuals and entities that they are connected to (e.g. for sharing a director, BO, shareholder, address, IP address, etc.).

4.2.2 Understandable, implementable, usable, enforceable and proportionate (for simple structures)

A BO definition with the goal of identifying as many individuals as possible is very easy to understand both for entities and obliged entities that need to comply as well as for authorities in charge of supervision and enforcement. While it would be almost impossible to verify that every BO register collected information on the “real BO” of each entity, it is easier to check whether have they obtained information on all the individuals who passed a given threshold. Such an approach becomes mechanical: very easy to implement and check. Of course, obliged entities should also use their skills to identify who among those registered individuals they believe to be in charge or to have control, even if they have little ownership or voting rights. Even if this extra check fails, the comprehensive approach at least allows supervisory authorities to eventually conduct the checks themselves among all the registered individuals. On the contrary, if the initial BO collector attempted to find only the real BO and failed to do it, authorities will have very little data to work with, for instance only the identity of a senior manager.

Additionally, the approach of identifying as many individuals as possible helps to discourage complex ownership chains, given that the longer and more sophisticated the structure, the harder it will be for them to obtain information on all the relevant

individuals. In contrast, identifying “all the individuals” becomes very easy for a simple structure of one or two shareholders who are also the BOs.

5. Conclusion

Establishing an effective BO definition is essential to ensure the transparency needed to tackle money laundering, tax evasion and other financial crimes. Currently, the BO definitions lack clarity, are subject to different interpretations and implementation by Member States, and most problematically, may not be identifying all the relevant individuals.

While many factors should be considered, e.g. proportionality, clarity, implementation, etc., in the long term, the best way to check most of the boxes would be to have a comprehensive BO definition that covers as many individuals as possible, e.g. by applying no thresholds in the BO definition for legal persons. This would allow authorities to have all the information they need and make it clear how the rules are to be applied, regardless of the complexity of the structure (so as not to decide how to consider indirect ownership or control). To make the definition enforceable, the criteria on control should also become more “mechanical”, e.g. anyone with a power of attorney, anyone with control over the bank accounts, anyone who participates in the board of directors, etc. While this may end up covering many individuals, it will be easier to implement and understand. However, to enable the implementation of this effective BO definition without thresholds, countries should ensure that their BO registries collect and make

available the full ownership chain of each legal vehicle and that verification mechanisms are applied to make this information reliable. Otherwise, lowering thresholds would only increase compliance costs for obliged entities. In addition, governments should invest in proper IT systems that are able to collect and process the necessary amount of information. This way, once stakeholders, such as obliged entities, can obtain from BO registries the full ownership chain of their customers up to the beneficial owner among those holding at least one share, banks and other obliged entities will be able to apply more sophisticated checks. Instead of merely checking for typos and other honest mistakes in discrepancy reporting, obliged entities could use the information that is not available to BO registries, such as the person withdrawing money from an ATM, managing the account or transferring money in order to complement BO verification.

On the other side of the spectrum, keeping a definition with thresholds and open rules on control may make it easier to approve politically, but may hinder the gathering of much-needed information to determine who is currently controlling, benefitting from or owning Europe’s legal persons.

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Annex: Dissenting Opinion

5 October 2022



European Banking Federation

Dissenting Opinion

on the recommendations set out in NEBOT Paper 4 on the definition of beneficial ownership for companies

The experts representing the European Banking Federation (EBF) in the Network of Experts on Beneficial Ownership and Transparency (NEBOT) appreciate the efforts put in by the drafters of the report to accommodate the different views expressed in the network. Nonetheless, due to the fundamental divergences between the proposed recommendations and the views of the EBF, which could not be reflected to a sufficient extent, we put forward the present dissenting opinion.

Main findings of the report

1. In its essence, the report stipulates that while different factors should be considered, in the long term the most effective approach would be to have a very comprehensive BO definition that would cover as many individuals as possible. It further argues that such an approach would make the definition easier to understand and implement.
2. The EBF experts expressed their concerns with regards to the plausibility of such a proposal given the immense burden this would place on obliged entities. Following a discussion with the drafters of the report, they proposed supplementing the report in order to address these concerns. In doing so, it was suggested that, to be able to implement a BO definition without thresholds, countries should ensure that their BO registries collect and make available the full ownership chain of each legal vehicle and that verification mechanisms are applied to make information reliable. In addition, it was stated that governments should invest to have the proper IT systems that are able to collect and process so much information.

EBF dissenting opinion

Despite all the efforts to find a solution with regards to the opposing views expressed, the EBF experts in NEBOT cannot support the aforementioned conclusions for the following reasons:

- 1. The recommendations lie on a (for the time being) unattainable premise of central registers which can collect and verify BO information**

The EBF experts appreciate the drafters' suggestion to alleviate the enormous burdens a lowered BO threshold would entail for obliged entities by calling for stronger central

5 October 2022



registers with verified and reliable information and for obliged entities to be allowed to fully rely on the information contained in these registers. However, the attainment of such registers is at this stage too far from becoming a reality.

Building strong central registers requires strong political will. Although such registers already exist at the national level (e.g. in Latvia), this is far from being the norm. Political commitment is needed at both EU and national levels to set them up, as well as beyond the EU. Our understanding is that there is no indication of such developments at the EU level. In addition, although the EBF supports the call for the obliged entities to be allowed to fully rely on the information that is contained in the registers, this approach has so far not been adopted by policy-makers.

At the same time, a lowered BO threshold would have huge operational implications on obliged entities. The reporting of discrepancies which is currently imposed on obliged entities would become an overwhelming exercise. The increased operational burden would demand more resources to significantly expand their due diligence checks and would as a result dilute their ability to dedicate the necessary resources and focus on areas of high risk, thereby rendering the requirements less effective and not aligned with the risk-based approach. The lack of interconnectedness of central registers in the EU dramatically exacerbates the problem.

2. Divergence from international standards and other frameworks

Lowering the threshold for beneficial ownership below 25% would, importantly, result in a departure from established international standards and is not in line with the FATF requirements to adopt a risk-based approach.

The FATF, through its assessment procedure and in its 2012 Recommendations, has found 25% to be an acceptable threshold. While it does not mandate a set threshold for determining controlling participation, the recommendations state that it is necessary to record and verify 'the identity of natural persons ... who ultimately have a controlling ownership interest in a legal person'. A 'controlling ownership interest', according to footnote 35, '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%).' In practice, most jurisdictions globally employ the 25% threshold.

A lowered threshold would result in a situation where most non-EU obliged entities will continue to apply the 25% threshold for beneficial ownership under the FATF recommendations. The increased operational burden for transacting with EU entities would place the EU at odds with other jurisdictions without a sound principled basis for departing from best practice established by the FATF. The divergence from international best practice would thus lead to competitive disadvantages of internationally operating obliged entities compared to those from third countries. Even assuming that, in the EU, central registers would collect and verify BO information, this would still not solve the potential problems related to transacting with third-country entities.

5 October 2022



The lowering of the threshold of BO for AML purposes makes it even more difficult to create any potential synergies with the tax reporting frameworks resulting from the Common Reporting Standard, the Directive on Administrative Cooperation (DAC2) and FATCA, as well as the Double Tax Conventions and withholding tax procedures.

3. Control vs ownership: the person controlling a corporate is the one who has authority over it

Beneficial ownership is not synonymous with mere ownership. According to FATF, it refers to the natural persons who exert effective control over the entity regardless of whether they occupy a formal position within the establishment. A lowered or even fully removed threshold as suggested by the drafters of the report does not necessarily point to a natural person having control over a legal entity. It would fundamentally change the concept of beneficial ownership from being indicative of control to instead establishing a 'look-through' approach whereby those with a minimal ownership interest in the company are identified irrespective of their ability to exercise control over its affairs. The EBF experts maintain that this runs completely counter to the risk-based approach, which is the backbone of the AML/CFT framework.

Individuals falling below the current 25% ownership interest are already captured within the definition of beneficial owner by virtue of the second aspect of the beneficial ownership test – i.e. 'control via other means'. This will be the case where the individual exercises control by virtue of, for example, indirect ownership, a veto right or other arrangements (formal or informal). It is appropriate for individuals with a less than 25% ownership interest to be caught by the second aspect of the test and not the first. This is because it is clear that a lower ownership interest with no 'other means' of control will not entitle an individual to exercise control over a company. Such an individual would need 'other means' in order to exercise such control in reality.

4. Risk of 'white noise': operational constraint without benefit for the fight against money laundering

The draft AML Regulation already introduces a number of new obligations with respect to determining the ultimate beneficial owners of legal entities, including new data points (nationality, residential address, tax identification number) and standard verification of identity (instead of risk-based). A proposal to lower the threshold indicative of beneficial ownership would risk overwhelming both obliged entities and competent authorities with white noise which holds little meaning in determining those individuals who actually exercise control over customer entities.

EBF position

The EBF experts stress once more that the goal of strengthening transparency is not to know who all the shareholders of an entity are but to identify criminals that might hide their identity behind a corporate structure. This goal is best achieved by enabling obliged

5 October 2022



entities to look through the increasingly sophisticated means employed by financial criminals to obscure their identities using complex legal structures. This is recognised by recital 13 of the fourth AML Directive which states that “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”.

The ability to trace through complex ownership structures will best enable obliged entities to identify the true beneficial owners of their clients, i.e. the persons who exercise control over the decisions of the corporate entity and not the persons who have an ownership interest which does not permit them to intervene in the life of the corporation. Creating an enabling legal framework for enhanced information exchange for AML/CFT purposes in a way that respects personal data protection rules could support this objective. It would allow obliged entities to obtain a more complete picture of their customers' behaviour. We believe that the report could have explored certain best practices in that domain, including national initiatives on data pooling and KYC utilities. The findings in the recent report by FATF on “Partnering in the Fight Against Financial Crime: Data Protection, Technology and Private Sector Information Sharing” would have been an appropriate basis for discussion.

In contrast, this goal would not be achieved by simply altering the definition as to who qualifies as a beneficial owner to include individuals who may exercise no such control.

Conclusion

In conclusion, the EBF experts once more acknowledge the work of the drafters and we show understanding about the ultimate goal they aim to achieve, namely enhanced transparency. However, we are unable to support the final recommendations in the report. We believe that regrettably, the unattainability of the premise of strong central registers collecting and verifying BO information, coupled with the significant operational burden a lowered BO threshold would otherwise entail, renders the recommendations impractical. Even more, applying in practice a lower BO threshold could even be counter-productive by shifting focus away from real money laundering and terrorist financing risks.

We reiterate that, in our view, the best way to improve transparency is by enhancing the framework for sharing information for AML/CFT purposes while striking a balance with the pertinent personal data protection and privacy framework.

Civil Society Advancing Beneficial Ownership Transparency

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