

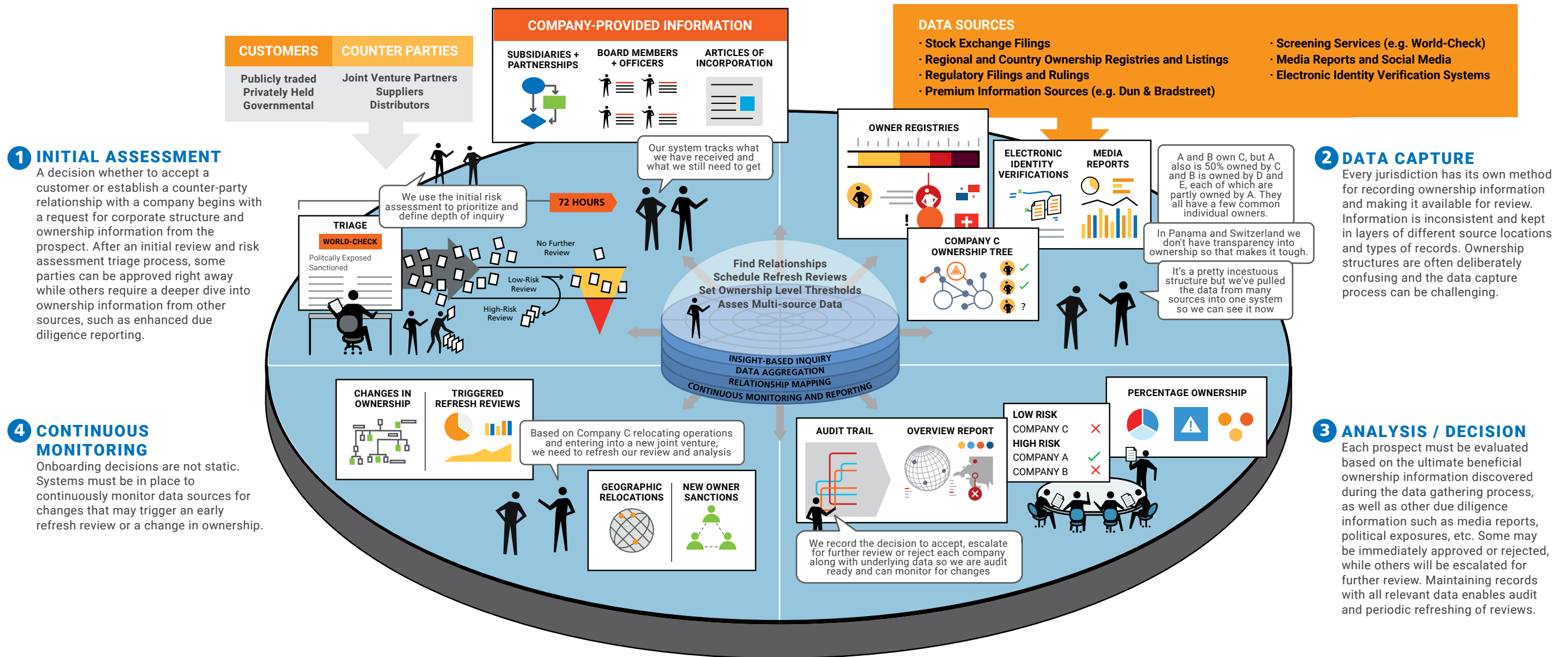
Identifying Beneficial Owners for AML and ABC Compliance

Identifying the real beneficial owners of an entity is essential for ensuring anti-money laundering (AML) and anti-bribery and corruption (ABC) compliance, but it isn't easy. Business ownership information is fragmented, stored in different forms and locations, and often difficult to find. Each jurisdiction has its own method for defining and recording ownership and complex corporate structures, often deliberately making it difficult to identify the real owners. This illustration outlines the key steps in identifying beneficial owners and demonstrates how technology can help to cut through the morass with speed, safety and a uniform approach.

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MANUAL PROCESS CHALLENGE	BENEFITS OF A CENTRAL MANAGEMENT SYSTEM
<ul style="list-style-type: none"> Missed Data Sources Analyst Error Inconsistency Lack of Audit Trail Wasted Resources Out of Date information Taking too Long Lost Opportunities 	<ul style="list-style-type: none"> Consolidated and reconciled data from multiple sources Consistent methodology applied by all using the same system One source of information on each company, owner and related parties Reports with views of decisions, scheduled refresh reviews, outstanding requests Ongoing monitoring of changes at every level and of any type requiring new review

{AN OCEG ROUNDTABLE}

Who is a beneficial owner?

Switzer: New Financial Crimes Enforcement Network (FinCEN) rules on customer due diligence came into force in May this year, adding new obligations for banks to ensure that they know who their actual customer is—what is commonly known as the ultimate beneficial owner or UBO. Why was it necessary for FinCEN to spell out this requirement at this time? Why were existing know-your-customer (KYC) rules insufficient? Are there changes in Europe as well?

Swenson: Recent global events such as the Panama Papers have clearly identified the inability, or unwillingness, to identify ultimate beneficial ownership in corporate structures as a foundation to the proliferation of financial crime and tax avoidance through the international banking system. While trusts and other shell companies may be used for legitimate purposes, these structures are also clearly used by criminals to divert illicit funds. While identifying customers may seem like a fundamental component of even rudimentary know-your-customer processes, the new rules aim to deploy additional discipline around collecting beneficial ownership information up front as part of the onboarding process.

Johnson: In the European Union, regulated firms have had to comply with requirements to identify UBOs since 2005, when the 3rd EU Money Laundering Directive came into force, but ambiguity around these requirements resulted in an inconsistent approach to UBO identification that the 4th EU Money Laundering Directive (4MLD) has now addressed. This has, in part, been achieved with a new definition of a UBO, and clarification on how to apply the recommended 25 percent ownership threshold. It also brought in the require-

ment for all member states to develop and maintain ownership registers to improve transparency and facilitate KYC.

Switzer: What are some of the greatest challenges in identifying beneficial owners?

Johnson: One of the first challenges of identifying beneficial owners is the lack of a commonly agreed-upon definition. While the EU's 4MLD has gone some way toward bringing consistency to what constitutes beneficial ownership across member states, there are still significant differences by jurisdiction. And to add to the complexity, different regulations have set different ownership-level thresholds. Both the FinCEN Rule and 4MLD require UBO identification to a 25 percent threshold, whereas FATCA (Foreign Account Tax Compliance Act) has a threshold of just 10 percent.

The next challenge is data. Building out the full picture of a customer in order to identify beneficial ownership requires access to multiple data sources. The process of accessing and gathering data from multiple sites is time consuming and low skilled, yet precious hours of analyst time are spent on this activity. Once the data is gathered, the challenge of manually analyzing and reconciling data from a range of sources begins. For large corporate customers this is complex work, but with analysts under immense time pressure it is also prone to human error. Inaccurate UBO identification and verification can leave an organization exposed to significant risk.

And finally, there's the challenge of providing a smooth customer experience while all of this is going on in the background. A slow and arduous onboarding process could see organizations lose customers before

they even start transacting. The good news is that technology, specifically robotic process automation, offers a solution and valuable benefits, including cost reduction, consistency and significant time savings.

Swenson: Another key challenge is the complexity criminals can use to disguise beneficial ownership by relying on an increasingly sophisticated network of professionals to architect corporate structures that banks and investigators are unable to decipher. After the Panama Papers scandal broke, Thomson Reuters performed an informal survey to determine the level of transparency of jurisdictions where companies can be registered. Out of 235 countries, territories, and overseas dependencies where a company could be registered, only 58 percent have online corporate registries where basic company verification can be performed. Only 45 percent publicly provide information on company directors, and even fewer offer shareholder details.

Even if a jurisdiction discloses ownership information, this will not necessarily lead to the ultimate beneficial owner. Complex structures, multijurisdictional ownership, out-of-date information, and incomplete or inaccurate details further complicate the unwrapping exercise.

Switzer: How can a financial institution with tens or hundreds of thousands of customers conduct triage to risk rank customers and determine where resources should be applied to identify beneficial owners?

Johnson: As regulation has moved toward a risk-based approach, most organizations will already have an initial risk assessment process in place to triage customers according to perceived risk. Specifically, when it comes to UBO discovery, certain criteria will be more relevant than others in assigning a risk ranking. The type of legal entity is, of course, an important consideration. Shell companies, trusts, foundations and family offices may all represent a higher risk of an undesirable end customer. Country risk is also important, and companies registered in secrecy jurisdictions should be looked at more closely. Conversely, regulated and listed companies that are already subject to various compliance and corporate governance regulations will be low risk.

Swenson: In terms of ownership unwrapping, organizations may apply a higher risk ranking to companies registered in opaque jurisdictions. Additional risk may be applied to certain entity types like trusts. This pro-

cess allows regulated institutions to demonstrate an appropriate level of due diligence was applied to higher-risk customers. Enhanced due diligence may also be applied to higher-risk profiles. Banks may need to reach out to potential customers on several occasions to obtain appropriate documentation to demonstrate to a regulator ownership was confirmed, which may delay the account opening process.

Switzer: Technology is an essential tool in this process, but is there work that needs to be done to “clean” data or establish consistent data management procedures for the technology to work most effectively?

Swenson: Many organizations are investing in technology, data acquisition tools, and analytics to help facilitate their KYC and beneficial ownership unwrapping obligations. The current manual processes used by most organizations are not sustainable for large-scale banking, and the cost of compliance is escalating rapidly. Technology, however, is dependent on good-quality data and some form of standardization across multiple jurisdictions. In developed financial centers, registry data can be queried in bulk and analyzed by technology. In developing economies, this may be more challenging due to the unstructured nature of the data required.

Johnson: Absolutely ... clean, accurate, and complete data on a customer is critical for technology to perform effectively. To start with, if the data you're collecting from the customer is inaccurate, KYC and UBO identification will be difficult to complete effectively, with or without technology. As an example: When a new customer is to be onboarded, a relationship manager will collect certain information from them to start the KYC process. If this data is inaccurate—let's say the legal entity is incorrect (a common mistake considering the number of legal entities that can make up a large, global brand—an analyst could end up identifying beneficial ownership of the wrong company entirely.

Additionally, as multiple data sources are used to gather information on a customer, you also have to bring different formats into a unified, structured format that your technology solution can digest and interpret. Data really is like the oil to the technology engine. Good-quality data—by that I mean complete, up-to-date and accurate—will ensure you can automate manual processes and achieve high straight-through processing rates. ■

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Hidden ownership in high-end real estate

This column accompanies the illustration on the facing page fold-out, which is part of OCEG's GRC Illustrated Series. To download a copy of the illustration and others in the series, visit the OCEG Eebsite at www.oceg.org/resources or go to www.complianceweek.com and select "GRC Illustrated" from the "Topics" pull-down menu on the toolbar.

by Carole Switzer

We often think that money laundering involves the use of offshore accounts in places with opaque banking systems, but the truth is that money laundering is often hidden in plain sight in developed countries with strong banking regulations. This can be accomplished through investment in high-end real estate.

Transparency International reports that investment in luxury property through shell corporations is one of the most common ways money is laundered. A 2016 Transparency International Canada study of high-end properties in Vancouver, B.C., Canada found that 45 percent of the properties are held through corporate structures that hide the owners. The "No Reason to Hide" report found that nearly half of the 100 highest priced properties—together valued at more than \$1 billion—did not have transparent ownership structures. Instead, they were owned by holding companies, or were owned by "nominees," who were unemployed students or home-makers or were held in trust for anonymous beneficiaries.

Investigative reports have found that a large part of the problem arises from Chinese money laundering activity. A recent article, for example, notes "Criminal syndicates that control chemical factories in China's booming Guangdong province are shipping narcotics, including fentanyl, to Vancouver, washing the drug sales in British Columbia's casinos and high-priced real estate, and transferring laundered funds back to Chinese factories to repeat this deadly trade cycle, a *Global News* investigation shows."

In June of this year, the problem of massive money laundering through B.C. casinos was outlined in a detailed independent report undertaken on behalf of the provincial government and work is underway to implement the recommendations for better control. In the final report, known as the "Dirty Money Report," the author notes that those laundering money through the casinos are also using the high-end real estate sector to clean their criminal gains and teaching others how to do so as well. This has led to plans for a second investigation, this time into the workings and weaknesses of the real estate industry that allow for money laundering to continue.

Just days before the public release of that report, the provincial government began to take steps to tackle the problem by trying to increase the transparency of beneficial owners. On June 21st, the Minister of Finance for B.C. announced that the province intends to create a first-of-its-kind publicly accessible

registry of beneficial owners, requiring declaration of such information from trustees and corporations acquiring property. The Land Owner Transparency Act Whitepaper issued with the announcement outlines the legislation that must be enacted to establish the registry and reporting requirements and ensure privacy of owners at the same time.

Recognizing that identifying beneficial owners is not always an easy task, given intentionally complex corporate structures, the whitepaper states, "The legislation recognizes that corporate or other structures used to own land can be very complicated and, in some cases, the reporting body may not be able to determine or confirm the identity of the individuals who ultimately own or control the corporation. In these cases, the reporting body is required to take steps to try and determine the identity of the individuals who control the corporation, outline the steps that were taken to identify the appropriate individuals, and provide the reasons the identity could not be confirmed."

While this type of registry is a good first step, I do not believe it is enough to address the problem of money laundering in high-end real estate. When the buyer is a part of a criminal enterprise, the self-reporting aspect of the registry presents an insurmountable limitation. Where large real estate developers or brokerage firms are involved in sales, there must be a know-your-customer style review and anti-money laundering regulations must be clarified and expanded to require such. Whether the companies involved are publicly traded developers and brokerages or are privately held, the same risks exist. Well-documented reports of money laundering activity involving condos in The Trump Ocean Club International Hotel and Tower make the case for regulation of privately held developers.

The use of opaque and extremely complex ownership structures is not limited to the real estate sector, and there may well be tax planning or other legitimate (or illegitimate) reasons for such structuring. The use of such structures in the real estate sector to support criminal activity by the laundering of ill-gotten funds has overtaken legitimate uses, however, as revealed in Transparency International's "No Reason to Hide" report, and it must be addressed and stopped as an essential element in fighting the underlying corruption, drug trafficking, and other crimes that are the source of the invested funds. ■

Carole Switzer is the co-founder and president of OCEG, the global non-profit think tank that issues GRC standards and certifications. [Learn more at OCEG.org.](http://www.oceg.org)



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