

Risks and Challenges of the Use of Corporate Vehicles (CVs) and Identifying Ultimate Beneficial Owners (UBOs)

By Mark McKenzie

1. Background

The recent publication of the Panama Papers by Washington, D.C.-based International Consortium of Investigative Journalists covering the massive leak of 11.5 million documents from a Panamanian law firm, covering four decades, has renewed world attention on tax havens, offshore companies and beneficial ownership.¹ The Panama Papers provides insight into the methods used by criminals and corrupt individuals to launder money, evade taxes and finance arms and drug deals. The Panama Papers revelations prompted renewed calls from the United States, the United Kingdom and others to make beneficial ownership information public, especially in international financial centres or so-called “secrecy jurisdictions,” some of whom have exhibited vulnerability to criminal misuse in the past.

Asian governments and regulators have adopted standards set by the intergovernmental Financial Action Task Force (FATF) to strengthen their anti-money laundering (AML) and combating the financing of terrorism (CFT) regimes.⁴ However, a number of factors including social, cultural and legal factors and business traditions can pose obstacles to effectively enforcing international AML/CFT rules. In addition, rigid confidentiality rules and privacy laws in some jurisdictions can prevent access by regulators and other authorities to information on suspicious transactions. The continued acceptance of nominee ownership (where an entity holds assets for the actual owner) in some economies prevents the proper identification of beneficial ownership, reduces transparency, and makes it difficult to enforce “know your customer” requirements.⁵

The objective of this article is to explore the issues of money laundering and other financial crimes facilitated by the use of corporate vehicles (CVs) and the absolute need for banks and other financial institutions to do due diligence to identify ultimate beneficial owners (UBOs). The article looks at some requirements in China, Singapore, Hong Kong, Malaysia and South Korea, as well as approaches being taken in the U.S. and EU.

2. Relevancy of AML/CFT to financial stability and supervision in Asia Pacific Economies

Money laundering and terrorist financing are widely recognized as factors that may undermine financial stability.⁶ As stated by Min Zhu, Deputy Managing Director of the IMF:

“Money laundering and the financing of terrorism are financial crimes with economic effects. They can threaten the stability of a country’s financial sector or its external stability more generally. Effective anti-money laundering and combating the financing of terrorism regimes are essential to protect the integrity of markets and of the global financial framework as they help mitigate the factors that facilitate financial abuse. Action to prevent and combat money laundering and terrorist financing thus responds not only to a moral imperative, but also to an economic need.”

Money laundering, terrorist financing and other financial crimes can adversely affect foreign investment and distort international capital flows. There may also be negative consequences for a country’s macroeconomic performance as result of money laundering and other financial crimes. This may result in welfare losses, draining resources from more productive economic activities, and can even have destabilizing spillover effects on the economies of other countries.

Money launderers and terrorist financiers exploit both the complexity inherent in the global financial system as well as differences between national AML/CFT laws and systems, and they are especially attracted to jurisdictions with weak or ineffective controls where they can more easily move their funds without detection. Moreover, problems in one country can quickly spread to other countries in the region or in other parts of the world.

Strong AML/CFT regimes enhance financial sector integrity and stability, which in turn facilitate countries’ integration into the global financial system. They also strengthen governance and fiscal administration. The integrity of national financial systems is essential to financial sector and macroeconomic stability both at the national and international levels.

In recent years, Asian economies have made significant progress towards implementing AML/CFT standards promulgated by the FATF. To combat risks associated with money laundering and other financial crimes, economies in the region have strengthened AML laws, established financial intelligence units, developed AML/CFT supervisory frameworks for financial institutions, and improved coordination and cooperation between national agencies and across economies.

However, compliance with these standards across the region has been uneven. The Asian Development Bank conducted a reviewed of ADB developing member

countries based on mutual evaluations completed between 2008 and 2012. The ADB found that there is much scope for improvement in dealing with money laundering and terrorist financing risks.¹¹

3. FATF Recommendations and Guidance on Transparency and Beneficial Ownership

The FATF Recommendations are recognised as the international standard for combating of money laundering and the financing of terrorism and proliferation of weapons of mass destruction. They form the basis for a coordinated response to these threats to the integrity of the financial system and help ensure consistency and adherence to at least minimum standards. The FATF monitors the progress of its members in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally. In collaboration with other international stakeholders, the FATF works to identify national-level vulnerabilities with the aim of protecting the international financial system from misuse.

3.1 Corporate Vehicles and the Definition of Beneficial Owner

Corporate vehicle such as companies, trusts, foundations, partnerships, and other types of legal persons and arrangements have legitimate commercial purposes. However, corporate vehicles have been misused for illicit purposes, including money laundering (ML), bribery and corruption, insider dealings, tax fraud, terrorist financing (TF), and other illegal activities.

The lack of beneficial ownership requirements and anonymity can inhibit law enforcement. For criminals trying to circumvent anti-money laundering (AML) and counter-terrorist financing (CFT) measures, corporate vehicles are an attractive way to disguise and convert the proceeds of crime before introducing them into the financial system.

The FATF definition of beneficial owner in the context of legal persons must be distinguished from the concepts of legal ownership and control. On the one hand, legal ownership means the natural or legal persons who, according to the respective jurisdiction's legal provisions, own the legal person. On the other hand, control refers to the ability of taking relevant decisions within the legal person and impose those resolutions, which can be acquired by several means (for example, by owning a controlling a block of shares). However, an essential element of the FATF definition of beneficial owner is that it extends beyond legal ownership and control to consider the notion of ultimate (actual) ownership and control. In other words, the FATF definition focuses on the natural (not legal) persons who actually own and take advantage of capital or assets of the legal person as well as on those who really exert effective control over it (whether or not they occupy formal positions within that legal person), rather than just the (natural or legal) persons who are legally (on paper) entitled to do so.

For example, if a company is legally-owned by a second company (according to its corporate registration information), the beneficial owners are actually the natural persons who are behind that second company, or ultimate holding company in the chain of ownership, and who are controlling it. Likewise, persons listed in the corporate registration information as holding controlling positions within the company, but who are actually acting on behalf of someone else, cannot be considered beneficial owners.

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.

To get to the heart of beneficial ownership information, the FATF requires each jurisdiction to collect and maintain the following information pertaining to legal persons:

- the company name,
- proof of incorporation,
- legal form and status,
- the address of the registered office,
- basic regulating powers (for example, memorandum and articles of association), and
- a list of directors.¹²

In addition to the above, companies should be required to obtain and record basic information which should include the following:

- a register of their shareholders or members, and
- the number of shares held by each shareholder and categories of shares (including the nature of the associated voting rights).

The beneficial ownership information of legal persons should be determined as follows:

Step 1

- a) 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, who exercise control of the legal person through ownership) who ultimately have a controlling ownership interest in a legal person, and
- b) to the extent that there is doubt as to whether the persons with the controlling ownership interest are the beneficial owners, or where no natural person exerts control through ownership interests, the identity of the natural persons (if any) exercising control of the legal person through other means.

Step 2

Where no natural person is identified under (a) or (b) 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.

FATF Recommendation 24 also requires countries to implement the following fundamental requirements to enhance the transparency of legal persons:

- a) Keep beneficial ownership information on all legal persons accurate and updated on a timely basis.
- b) Have sanctions for failing to comply with requirements for collecting and maintaining beneficial ownership information.
- c) Implement measures to overcome specific obstacles to the transparency of companies.

Countries must also take specific measures to prevent the misuse of other mechanisms that are frequently used to disguise ownership of companies, including bearer shares, bearer share warrants, nominee shares and nominee directors.

The FATF definition of beneficial owner also applies in the context of legal arrangements, meaning the natural person(s), at the end of the chain, who ultimately owns or controls the legal arrangement, including those persons who exercise ultimate effective control over the legal arrangement, and/or the natural person(s) on whose behalf a transaction is being conducted.

However, in this context, the specific characteristics of legal arrangements make it more complicated to identify the beneficial owner(s) in practice. For example, in a trust, the legal title and control of an asset are separated from the equitable interests in the asset. This means that different persons might own, benefit from, and control the trust, depending on the applicable trust law and the provisions of the document establishing the trust (for example, the trust deed). In some countries, trust law allows for the settlor and beneficiary (and sometimes even the trustee) to be the same person. Trust deeds also vary and may contain provisions that impact where ultimate control over the trust assets lies, including clauses under which the settlor reserves certain powers (such as the power to revoke the trust and have the trust assets returned). This may assist in determining the beneficial ownership of a trust and its related parties.

Under FATF Recommendation 25, “legal arrangements” means express trusts or other similar arrangements. Much of Recommendation 25 focuses on how to apply comprehensive AML/CFT due diligence measures to trusts.¹³

Trust law countries should require the trustees of any express trust governed under their law to obtain and hold adequate, accurate, and current beneficial ownership information regarding the trust. This information should be kept as accurate, current

and up-to-date as possible by updating it within a reasonable period following any change. In this context, beneficial ownership information includes:

- a) information on the identity of the settlor, trustee(s), protector (if any), beneficiary or class of beneficiaries, and any other natural person exercising ultimate effective control over the trust, and
- b) basic information on other regulated agents of, and service providers to the trust, including investment advisors or managers, accountants, and tax advisors.

Recommendation 25 places specific requirements on all countries, irrespective of whether the country recognises trust law. In particular, all countries should implement the following measures:

- a) Require that trustees disclose their status to financial institutions and designated non-financial businesses and professions (DNFBPs) when forming a business relationship or carrying out an occasional transaction above the threshold. The trustee needs to actively make such disclosure (and not only upon the request of a competent authority). Trustees should not be prevented from doing this even if, for example, the terms of the trust deed require them to conceal their status. The only source of information on the trustee often available comes from the business relationship of a financial institution/ DNFBP and the trustee.
- b) Require professional trustees to maintain the information they hold for at least five years after their involvement with the trust ceases. Countries are also encouraged to extend this requirement to non-professional trustees and the other relevant authorities, persons and entities.

3.2 Wire Transfers

In relation to wire transfers, the circumstances covered by the Interpretive Note to FATF Recommendation 16 include wire transfers above USD/EUR 1000. This means that financial institutions should undertake customer due diligence (CDD) when carrying out cross-border wire transfers above USD/EUR 1000, including the requirement to identify and take reasonable measures to verify the identity of the beneficial owner of the originator or beneficiary, as outlined above. In addition, Recommendation 16 also requires financial institutions to take further measures such as collecting certain originator information and ensuring that this information accompanies a wire transfer.

4. EU's Fourth EU Anti-Money Laundering Directive (4AMLD)

On June 5, new EU's anti-money laundering (AML) rules, namely the Fourth EU Anti-Money Laundering Directive (4AMLD) and a new Regulation on the information accompanying transfer of funds were published in the Official Journal of the European Union. EU Member States will have until June 26, 2017 to transpose the requirements of the 4AMLD into national law.

A key feature of the new Directive is the introduction of a central UBO-register, a public register which identifies the ultimate beneficial owners (UBOs) of companies and trusts. The AMLD defines a UBO as any natural person(s) who ultimately owns or controls the customer (i.e. a corporate entity or other legal entity) and/or the natural person(s) on whose behalf a transaction or activity is being conducted. In respect of corporate entities this definition of a UBO is further specified as a natural person who ultimately holds a shareholding, controlling interest or ownership interest over 25% of the shares or voting rights in a corporate entity. If no UBO can be identified, the natural person(s) holding the position of senior managing official are in principle registered as UBO. At least the following information on the UBO would be included in the UBO-register:

- name;
- month and year of birth;
- nationality;
- country of residence; and
- nature and extent of the beneficial interest held.

The UBO-register will be accessible to:

- competent authorities and EU Financial Intelligence Units, without any restriction;
- obliged entities (such as banks, notaries and lawyers conducting their “customer due diligence” duties); and
- a member of the public that can demonstrate a “legitimate interest” (i.e. in respect of money laundering, terrorist financing and the associated predicate offenses – such as corruption, tax crimes and fraud).

EU member states are authorized to deny access to obliged entities, or the public, part or all of the UBO-information in exceptional circumstances, on a case-by-case basis, e.g. when there is a high risk of fraud, kidnapping, blackmailing, etc.

In case of trusts, a separate arrangement will apply, whereby the EU member states must provide for a central register for UBOs of trusts governed by their law that will, in principle, only be accessible to competent authorities, EU Financial Intelligence Units and obliged entities that are conducting customer due diligence, but not to the public. EU member states must include UBO-information in this register in respect of trusts and comparable legal arrangements that are governed under the law of this respective EU member state if the trust generates tax consequences. However, the meaning of the term “tax consequences” has not been clarified yet.

The information included in this trust register should include the identity of:

- the settlor;
- trustee(s);
- protector(s) (if any);
- beneficiaries or class of beneficiaries; and
- any other natural person exercising effective control over the trust.

Other elements of the 4AMLD include, for example, a reshaping of the risk-based approach for customer due diligence concerning the obligation of obliged entities to check the identity of their customers and to report suspicious transactions; new and increased administrative sanctions for serious, repeated or systematic breaches of the 4AMLD's requirements; and, new requirements for traceability of fund transfers, including information on the payee (and not only the payer).

5. The UK's The Register of People with Significant Control Regulations 2016

New UK laws, which came into force on April 6th, impose an obligation publicly to disclose the ultimate beneficial owners or controllers who have "significant control" over UK incorporated companies.

The UK is the first country in the European Union ("EU") to implement this new disclosure regime through the Small Business, Enterprise and Employment Act 2015, which amends the Companies Act 2006. However, under the Fourth EU Money Laundering Directive, all member states in the EU are required to introduce an Ultimate Beneficial Owner register by June 26, 2017 to record "adequate, accurate and current" information about a company's beneficial owners.

What do the new UK laws mean for companies incorporated outside the UK which have a subsidiary in the UK?

From April 6th this year, the law requires most UK companies, Societates Europaeae (public companies registered in accordance with European law), ("SE's"), and Limited Liability Partnerships ("LLP's") to keep a register of persons or entities that have significant control over them. Companies subject to chapter 5 of the Disclosure and Transparency Rules including those listed on the main market of the London Stock Exchange or AIM will not be required to do so, on the basis that they are already required to disclose significant shareholdings. Furthermore, from June 30th 2016, companies must deliver this information to UK Companies House when filing their Confirmation Statements (the new equivalent to Annual Returns). Persons of significant control ("PSC's") are defined as an individual who meets one or more of the following conditions in relation to the UK company, SE or LLP:

- directly or indirectly holding more than 25% of the shares;
- directly or indirectly holding more than 25% of the voting rights;
- directly or indirectly holding the right to appoint or remove a majority of directors;
- otherwise having the right to exercise, or actually exercising, significant influence or control; or
- having the right to exercise, or actually exercising, significant influence or control over the activities of a trust or firm which is not a legal entity, but would itself satisfy any of the first four conditions if it were an individual.

Although a PSC is by definition an individual, legal entities can own and control companies, and must be put on the PSC register if they are "relevant and registrable".

“Relevant” is defined as fulfilling any one of the five PSC criteria above plus one or more direct criteria described as follows:

- it keeps its own PSC register; or
- it is subject to Chapter 5 of the Financial Conduct Authority’s Disclosure and Transparency Rules (DTRs); or
- it has voting shares admitted to trading on a regulated market in the UK or European Economic Area (other than the UK) or on specified markets in Switzerland, the USA, Japan and Israel.

And an entity is “registrable” if it is the first relevant legal entity in your company’s ownership chain. Venture capital funds or other investors may be “relevant and registrable” and therefore trigger the PSC disclosure requirements to identify their beneficial owners.

Relevant UK Companies, SE’s or LLP’s must take reasonable steps to identify if they have a PSC. The legal guidance suggests that the company also record the steps it has taken to make that identification: doubtless with a view to producing this evidence if a regulator subsequently comes calling.

6. FINCEN’s Final Rule on Beneficial Ownership Requirements

On May 6, 2016, the U.S. Department of the Treasury’s Financial Crimes Enforcement Network (FinCEN) released a final rule (the “Final Rule”) requiring banks, brokers or dealers in securities, mutual funds, futures commission merchants, and introducing brokers in commodities (collectively, “covered financial institutions”) to obtain and record beneficial ownership information as part of their anti-money laundering (AML) obligations under the Bank Secrecy Act (BSA). The Final Rule will become effective 60 days after its publication in the Federal Register. However, covered financial institutions will have a two year implementation period to comply with the new requirements.

The Final Rule requires covered financial institutions prospectively to identify and verify the identity of beneficial owner(s) of each legal entity customer when a new account is opened. Beneficial owners are persons meeting either the “ownership prong” or the “control prong” of the definition of “beneficial owner.” The Final Rule does not apply to existing customers or retrospectively. However, the Final Rule is applicable if pre-existing customers that open new accounts after promulgation of the rule and this means covered financial institutions must obtain beneficial ownership for all new accounts.

The Final Rule only applies in relation to beneficial ownership information for “legal entity customers,” which are defined to include any corporation, limited liability company, or other entity that is created by the filing of a public document with a Secretary of State or similar office, a general partnership, and any similar entity formed under the laws of a foreign jurisdiction that opens an account.

FinCEN clarified that this definition does not include sole proprietorships or unincorporated associations because neither is an entity with legal existence separate from the associated individual or individuals. The definition also does not include natural persons opening an account on their own behalf. Nor does it include trusts (other than statutory trusts created by a filing with a Secretary of State or similar office). With regard to so-called “intermediated account relationships,” (such as, for example, when a broker-dealer opens an account with a mutual fund to engage in transactions on behalf of its customers) FinCEN explained that in cases where existing guidance provides that a financial institution shall treat an intermediary (and not the intermediary’s customers) as its customer for purposes of the Customer Identification Program (CIP) rules, the financial institution should likewise treat only the intermediary as its customer for purposes of the new beneficial ownership requirement.

The Final Rule defines beneficial owners as those individuals meeting either the ownership prong or the control prong. Beneficial owners identified under the ownership prong are defined as “[e]ach individual, if any, who, directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, owns 25 percent or more of the equity interests of a legal entity customer.” FinCEN stated that it intended the term “equity interest” to be “broadly applicable” and declined to further clarify the definition beyond describing it as “an ownership interest in a business entity.” FinCEN confirmed that the phrase “directly or indirectly” meant that the covered financial institution’s customer must identify its ultimate beneficial owner[s] and not their nominees or “straw men.” Covered financial institutions may establish a threshold below 25 percent based on their own assessment of risk in appropriate circumstances.

Special circumstances involving trusts and entities excluded from the definition of “legal entity customer”. The Final Rule specifies that if a trust owns directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, 25 percent or more of the equity interests of a legal entity customer, the beneficial owner for purposes of the ownership prong shall mean the trustee. The Final Rule also specifies that where one of the entities holding 25 percent or more of the equity interests of a legal entity customer is itself excluded from the definition of a “legal entity customer,” no individual need be identified under the control prong.

Beneficial owners identified under the control prong are defined as “[a] single individual with significant responsibility to control, manage, or direct a legal entity customer,” including:

An executive officer or senior manager (e.g., a Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, or Treasurer); or any other individual who regularly performs similar functions.

FinCEN further stated that “the control prong provides for a straightforward test: the legal entity customer must provide identifying information for one person with significant managerial control.”

It should be noted that there could be variations on the number of beneficial owners identified under the ownership and control prongs. FinCEN recognized that, under the ownership prong, depending on the factual circumstances, as few as zero and as many as four individuals may need to be identified. All entities, however, would be required to identify one beneficial owner under the control prong. It is also possible that in some circumstances the same person or persons might be identified under both the ownership and the control prongs. FinCEN further noted that covered financial institutions had the discretion to identify additional beneficial owners as appropriate based on risk.

FinCEN noted that it would be impracticable for covered financial institutions to monitor the equity interests and management team of legal entity customers on an ongoing basis and continually update this information. It “emphasize[d] that the obligation for identification and verification should be considered a snapshot at the time that a new account is opened, not a continuous obligation.” However, FinCEN does expect covered financial institutions to update this information episodically based on risk, generally triggered by a covered financial institution learning through its normal monitoring of facts indicative of a change in beneficial ownership relevant to assessing the risk posed by the customer. This presents a second way that a pre-existing customer of a covered financial institution might have to provide beneficial ownership information, in this case even if no new account has been opened. This obligation to update arises from the general CDD obligation FinCEN codifies in the new rule that covered financial institutions must update all customer information on a risk basis, i.e., when customer information changes in a way that may affect its risk profile.

In addition to the Final Rule, the U.S. governmental authorities also announced a series of other related initiatives that target the key points of access to the international financial system. That is when companies open accounts at financial institutions, when companies are formed or when company ownership is transferred, and when foreign-owned U.S. companies seek to evade their taxes.

First, the U.S. governmental authorities reported that they have sent a legislative proposal to Congress that would require all corporations formed in the U.S. to report their beneficial ownership information at the time of formation. Such a national requirement relating to corporate formation has long been resisted by states that are popular places of incorporation, such as Delaware. The legislation also reportedly would “clarify” the scope of FinCEN’s authority to gather information using geographic targeting orders, in particular with respect to the collection of wire transfer information.

Second, the Internal Revenue Service issued a proposed rule to require foreign-owned single member limited liability companies and other so-called “disregarded entities” to obtain a tax identification number from the IRS, thereby requiring these entities to report ownership and transaction information.

Third, U.S. authorities proposed legislation that would enhance the Department of Justice’s authority in money laundering and anti-corruption cases. The administration’s proposal would, among other things, expand foreign money laundering predicates to include violations of foreign law that would be money laundering predicates if committed in the U.S. It would also authorize the use of administrative subpoenas for money laundering investigations and enhance prosecutors’ ability to access foreign bank or business records by service branches located in the U.S.

Finally, the administration urged Congress to amend financial reporting requirements to establish full reciprocity with U.S. Foreign Account Tax Compliance Act (FATCA) partners and to approve eight tax treaties that are currently pending with the Senate.

The legislative proposal with respect to beneficial ownership in particular may also help to satisfy FATF as it conducts its review of U.S. AML practices in ways that the new Final Rule does not, because it speaks specifically to FATF’s longstanding concern that beneficial ownership information be obtained at the time of company formation.

7. Requirements for Identifying Ultimate Beneficial Owners in Selected SEACEN Member Economies

a. Malaysia

In Malaysia, the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 requires financial institutions to conduct customer due diligence on beneficial owners. There are no requirements for a public registry.

Under the AML Guidelines, legal arrangement means an express trust or other similar legal arrangement. Legal person means any entity other than a natural person that can establish a permanent customer relationship with a reporting institution or otherwise own property. This can include companies, body corporates, foundations, partnerships, or associations and other similar entities.

Beneficial owner means the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes that person who exercises ultimate effective control over a legal person or arrangement.

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

b. China

China is a member of FATF as well as the Asia/Pacific Group on Money Laundering and the Eurasian Group on Combating Money Laundering. Chinese AML regulations establish a comprehensive system that is broadly comparable with EU rules. The main activities of money laundering are criminalized in China, with sanctions including imprisonment, dependent on degree of misconduct, confiscation, and compensation. There are strict rules relating to customer due diligence, including the identification of beneficial ownership of assets, and financial institutions are also required to report suspicious activity of customers as well as large value transactions. Also, Chinese AML law requires financial institutions to establish internal AML control programs, designate specialist AML units, establish a customer identification program, and provide appropriate staff training.

c. South Korea

In South Korea, the Trust Act applies to personal trusts and under Article 33 obliges a trustee of a personal trust to keep books and clarify the management affairs of the accounts pertaining to each trust and prepare a list of inventory at least once a year. Personal trusts are required to file tax returns but personal information contained therein is limited to the trustee. According the 2009 Mutual Evaluation Report, Korean officials state that “there are few personal trusts in Korea.” Korea does not have a central trust registry for personal trusts and consequently, it is difficult to know the full dimensions personal trust activities. Trust companies may be banks or other financial institutions licensed under the Trust Business Act to engage in trust business.

When entering in trust contract, trust companies are required to include information as below in the contract (Article 37-4 of the Trust Business Act and the Article 18 of the Presidential Enforcement Decree of the Trust Business Act).

- Names of truster, beneficiary and trust company.
- Information on designation and changes of beneficiary.
- Type, amount and price of property in trust.
- Purpose of trust.
- Information that shows trusted properties of securities, stock certificate and bond certificate.
- Type of trusted properties that would be granted to beneficiary and methods and timing of delivery.

Law enforcement agencies have powers to obtain information on both personal and business trusts, including the “truster” (i.e. settlor), and to some extent beneficiaries,

in business trusts, in criminal investigations. Given the absence of a central registry for personal trusts, the information is limited to what is required under Article 33 of the Trust Act (as noted previously). And, while personal trusts are obliged to file tax returns, given the strict Korean laws on tax secrecy, that information is not available to other agencies except for a criminal investigation in relation to tax matters or pursuant to a court order.

Trust companies are regulated by the Financial Supervisory Service (FSS) which has a full range of administrative powers of access to information held by trust companies (see earlier discussion in Section 3.10 of this report). The Financial Services Commission (FSC) which oversees the FSS, may supervise the business of trust companies, and issue an order required therefore (Article 24-2 of the Trust Business Act). And the FSC may, where it deems necessary, have a trust company report on the status of business and assets or submit documents or accounting books (Article 25 of the Trust Business Act). In addition, the FSC may entrust the FSS with supervision and have officials of the FSS inspect the business and assets of trust companies. The FSS may request trust companies to submit documents and ask an interested party to attend and state his opinion (Article 26 of the Trust Business Act).

Law enforcement authorities have the authority to obtain or access available information on beneficial ownership on trusts in these trust companies only in case of criminal investigations or pursuant to a court order.

There are no requirements for financial institutions to obtain information on the intended nature and purpose of the business relationship, identify beneficial ownership beyond the direct beneficiary and to conduct ongoing due diligence on all customers, and to subject higher risk customers/transactions to enhanced due diligence. Thus, while law enforcement agencies and supervisory authorities have access to information, little exists which relates to beneficial ownership and control of legal arrangements.

d. Hong Kong

Based on Hong Kong's Guideline on Anti-Money Laundering and Counter-Terrorist Financing, where there is a beneficial owner in relation to the customer, financial institutions are required to identify and take reasonable measures to verify the beneficial owner's identity. In addition, in the case of a legal person or trust, the financial institution is to take measures to enable that it understand the ownership and control structure of the legal person or trust.

A beneficial owner is normally an individual who ultimately owns or controls the customer or on whose behalf a transaction or activity is being conducted. In respect of a customer who is an individual not acting in an official capacity on behalf of a legal person or trust, the customer himself is normally the beneficial owner. There is no requirement on FIs to make proactive searches for beneficial owners in such a case, but

they should make appropriate enquiries where there are indications that the customer is not acting on his own behalf.

The obligation to verify the identity of a beneficial owner is for the FI to take reasonable measures, based on its assessment of the ML/TF risks, so that it is satisfied that it knows who the beneficial owner is. In determining what constitutes reasonable measures to verify the identity of a beneficial owner and reasonable measures to understand the ownership and control structure of a legal person or trust, the FI should consider and give due regard to the ML/TF risks posed by a particular customer and a particular business relationship.

FIs should identify all beneficial owners of a customer. In relation to verification of beneficial owners' identities, the AMLO generally requires FIs to take reasonable measures to verify the identity of any beneficial owners owning or controlling 25% or more of the voting rights or shares, etc. of a corporation, partnership or trust. In "high risk" situations, the threshold for the requirement is 10%.

For legal persons, the principal requirement is to look behind the customer to identify those who have ultimate control or ultimate beneficial ownership over the business and the customer's assets. FIs would normally pay particular attention to persons who exercise ultimate control over the management of the customer.

In deciding who the beneficial owner is in relation to a legal person where the customer is not a natural person, the FI's objective is to know who has ownership or control over the legal person which relates to the relationship, or who constitutes the controlling mind and management of any legal entity involved in the funds. Verifying the identity of the beneficial owner(s) should be carried out using reasonable measures based on a risk-based approach.

Where the owner is another legal person or trust, the objective is to undertake reasonable measures to look behind that legal person or trust and to verify the identity of beneficial owners. What constitutes control for this purpose will depend on the nature of the institution, and may vest in those who are mandated to manage funds, accounts or investments without requiring further authorisation.

For a customer other than a natural person, FIs should ensure that they fully understand the customer's legal form, structure and ownership, and should additionally obtain information on the nature of its business, and the reasons for seeking the product or service unless the reasons are obvious.

An FI should obtain and verify the following information in relation to a customer which is a corporation:

- (a) full name;
- (b) date and place of incorporation;

- (c) registration or incorporation number; and
- (d) registered office address in the place of incorporation.

If the business address of the customer is different from the registered office address in (d) above, the FI should obtain information on the business address and verify as far as practicable.

In the course of verifying the customer's information for a corporation, an FI should also obtain the following information:

- a) a copy of the certificate of incorporation and business registration (where applicable);
- b) a copy of the company's memorandum and articles of association which evidence the powers that regulate and bind the company; and
- c) details of the ownership and structure control of the company, e.g. an ownership chart.

Beneficial owner in relation to a corporation is defined as an individual who:

- a) owns or controls, directly or indirectly, including through a trust or bearer share holding, not less than 10% of the issued share capital of the corporation;
- b) is, directly or indirectly, entitled to exercise or control the exercise of not less than 10% of the voting rights at general meetings of the corporation; or
- c) exercises ultimate control over the management of the corporation; or (ii) if the corporation is acting on behalf of another person, means the other person.

e. Singapore

Based on the Monetary Authority of Singapore Notice 626 issued 24 April 2015 to banks under MAS Act, CAP. 186 Prevention of Money Laundering and Countering The Financing of Terrorism – “beneficial owner,” in relation to a customer of a bank, means the natural person who ultimately owns or controls the customer or the natural person on whose behalf a transaction is conducted or business relations are established, and includes any person who exercises ultimate effective control over a legal person or legal arrangement.

For this purpose “legal arrangement” means a trust or other similar arrangement and “legal person” means an entity other than a natural person that can establish a permanent customer relationship with a financial institution or otherwise own property.

For AML customer due diligence purposes a bank shall inquire if there exists any beneficial owner in relation to a customer. In the case there is one or more beneficial owner in relation to a customer, the bank shall identify the beneficial owners and take reasonable measures to verify the identities of the beneficial owners using the relevant information or data obtained from reliable, independent sources. Reasonable measures means appropriate measures which are commensurate with the money laundering or terrorism financing risks.

The bank shall:

- a) for customers that are legal persons:
 - i) identify the natural persons (whether acting alone or together) who ultimately own the legal person;
 - ii) to the extent that there is doubt under subparagraph (i) as to whether the natural persons who ultimately own the legal person are the beneficial owners or where no natural persons ultimately own the legal person, identify the natural persons (if any) who ultimately control the legal person or have ultimate effective control of the legal person; and
 - iii) where no natural persons are identified under subparagraph (i) or (ii), identify the natural persons having executive authority in the legal person, or in equivalent or similar positions;

- b) for customers that are legal arrangements:
 - i) for trusts, identify the settlors, the trustees, the protector (if any), the beneficiaries (including every beneficiary that falls within a designated characteristic or class), and any natural person exercising ultimate ownership, ultimate control or ultimate effective control over the trust (including through a chain of control or ownership); and
 - ii) for other types of legal arrangements, identify persons in equivalent or similar positions, as those described under subparagraph (i).

Where the customer is not a natural person, the bank shall understand the nature of the customer's business and its ownership and control structure.

8. Recommendations

Relevant national authorities should review their AML requirements for legal persons and legal arrangements and identification of beneficial ownership, and consider establishing comprehensive public registries for ultimate beneficial ownership information.

The following steps may strengthen AML/CFT requirements and allow law enforcement to better track illicit use of financial services:

- 1) Set up a public registry for beneficial ownership information
- 2) Financial institutions identify and verify the identity of beneficial ownership information
- 3) Financial institutions establish procedures for making and maintaining a record of all information obtained under the procedures implementing the identification and verification requirements of beneficial ownership information. At a minimum the record must include the following:
 - i) any identifying information obtained by the financial institution, and

- ii) a description of any document relied on (noting the type, any identification number, place of issuance and, if any, date of issuance and expiration), of any non- documentary methods and the results of any measures undertaken, and of the resolution of each substantive discrepancy.

Further, financial institutions have in place adequate custom due diligence measures including:

- 1) customer identification and verification,
- 2) beneficial ownership identification and verification,
- 3) understanding the nature and purpose of customer relationships to develop a customer risk profile, and
- 4) ongoing monitoring for reporting suspicious transactions, and, on a risk-basis, maintaining and updating customer information.

9. Conclusions

The recent publication of the Panama Papers has renewed world attention on tax havens, offshore companies and beneficial ownership. The Panama Papers revelations prompted renewed calls from the United States, the United Kingdom and others to make beneficial ownership information public, especially in international financial centres and so-called secrecy jurisdictions.

Corporate vehicle such as companies, trusts, foundations, partnerships, and other types of legal persons and arrangements provides useful commercial purposes. Despite their usefulness, corporate vehicles have been misused for illicit purposes, including money laundering (ML), bribery and corruption, insider dealings, tax fraud, terrorist financing (TF), and other illegal activities.

The lack of beneficial ownership requirements and anonymity inhibits law enforcement. For criminals trying to circumvent anti-money laundering (AML) and counter-terrorist financing (CFT) measures, corporate vehicles are an attractive way to disguise and convert the proceeds of crime before introducing them into the financial system. Money laundering and other financial crimes can expose a country to financial instability and macroeconomic risk by accelerating the growth of domestic credit and create market volatility that threatens sustainable economic growth and price stability.

An effective domestic AML/CFT regime requires the existence of certain structures, such as a robust regulatory framework, the rule of law, government effectiveness, a culture of compliance, and an effective judicial system. While most regional economies have made substantial progress in the implementation of global AML standards, some have room for improvement. Some economies do not have fundamental structural elements in place, while others have significant weaknesses or shortcomings that impair the implementation of an effective AML/CFT framework. In

some cases, policies on taxes, currency controls and trade restrictions serve as incentives for individuals to circumvent formal financial channels and drive the demand for money laundering.

Asian financial systems continue to increase in complexity over time as they develop. From this perspective, it is imperative that regulatory regimes, including AML/CFT oversight, need to be sufficiently broad and comprehensive to cover the entire spectrum of the financial system. Regulatory regimes need to be integrated so that issues of market transparency and interconnectedness of financial firms are covered. Finally, authorities need to continuously upgrade technical and analytical capacity to effectively regulate and supervise financial institutions and markets to promote financial innovation and stability.

Endnotes

1. Read more about the Panama Papers at <https://panamapapers.icij.org/>
2. <http://www.scmp.com/news/hong-kong/article/1943463/chinese-dominate-list-people-and-firms-hiding-money-tax-havens-panama>
3. <http://atimes.com/2016/04/south-korean-links-to-panama-papers-spread/>
4. The Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its Member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is therefore a “policy-making body” which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas. First issued in 1990, the FATF Recommendations were revised in 1996, 2001, 2003 and most recently in 2012 to ensure that they remain up to date and relevant, and they are intended to be of universal application. In 2001, the development of standards in the fight against terrorist financing was added to the mission of the FATF. In October 2001 the FATF issued the Eight Special Recommendations to deal with the issue of terrorist financing. The continued evolution of money laundering techniques led the FATF to revise the FATF standards comprehensively in June 2003. In October 2004 the FATF published a Ninth Special Recommendations, further strengthening the agreed international standards for combating money laundering and terrorist financing - the 40+9 Recommendations. In February 2012, the FATF completed a thorough review of its standards and published the revised FATF Recommendations. This revision is intended to strengthen global safeguards and further protect the integrity of the financial system by providing governments with stronger tools to take action against financial crime. They have been expanded to deal with new threats such as the financing of proliferation of weapons of mass destruction, and to be clearer on transparency and tougher on corruption. The 9 Special Recommendations on terrorist financing have been fully integrated with the measures against money laundering. This has resulted in a stronger and clearer set of standards.
5. Federal Reserve Bank of San Francisco. “Asia Focus: Anti-Money Laundering Reforms and Trends in Asia,” by Birgit Baxendale. July 2007.
6. For definition of financial stability see Schinasi, Garry J. “Defining Financial Stability”, International Capital Markets Department, IMF Working Paper, October 2004, “Financial stability may be defined a state in which the financial system, i.e. the key financial markets and the financial institutional system is resistant to economic shocks to ensure the smooth functions such as the

intermediation of financial funds, management of risks and the arrangement of payments. Financial instability may be caused by a range of different factors such as rapid liberalisation of the financial sector, inadequate economic policy, non-credible exchange rate mechanism, inefficient resource allocation, weak supervision, insufficient accounting and audit regulation, poor market discipline.”

7. Furusawa, Mitsuhiro “Building Financial Sector Stability to Ensure Asia’s Continued Success” Opening remarks for Conference on Banking Supervision and Regulation, September 14, 2015
8. Chairman Ben S. Bernanke, At the Federal Reserve Bank of San Francisco’s Conference on Asia and the Global Financial Crisis, Santa Barbara, California, October 19, 2009
9. Chairman Ben S. Bernanke, At the Federal Reserve Bank of San Francisco’s Conference on Asia and the Global Financial Crisis, Santa Barbara, California, October 19, 2009
10. Furusawa, Mitsuhiro “Building Financial Sector Stability to Ensure Asia’s Continued Success” Opening remarks for Conference on Banking Supervision and Regulation, September 14, 2015
11. See ADB’s “Second Review of Enhancing the Asian Development Bank’s Role in Combatting Money Laundering and the Financing of Terrorism,” November 2012
12. FATF Interpretive Note to Recommendation 24
13. Trusts enable property to be managed by one person on behalf of another, and are a traditional feature of common law. They also exist in some civil law countries or are managed by entities in these countries, and have a wide range of legitimate uses (for example, the protection of beneficiaries, the creation of investment vehicles and pension funds, and the management of gifts, bequests or charitable donations).