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## AFME Consultation response

### FATF – Amendments to Recommendation 24 on Transparency and Beneficial Ownership of Legal Persons

6 December 2022

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The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the Public Consultation on FATF amendments to Recommendation 24 (R24) on Transparency and Beneficial Ownership of Legal Persons.

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors, and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

AFME is registered on the EU Transparency Register, registration number 65110063986-76.

#### High level summary

AFME welcomes the opportunity to respond to FATF's draft text of the guidance paper to Recommendation 24 and have the following high-level comments:

- **Standardised Baseline Threshold** - AFME supports a standardised threshold for Beneficial Ownership for all countries of more than 25% as opposed to individual thresholds set by different jurisdictions<sup>1</sup>. Our members note that different thresholds create additional complications, unnecessary costs, and complexity for firms with global booking models. Furthermore, our Members consider that the baseline threshold should be no lower than 25%, with lower thresholds defined by Obligated Entities on a risk-based approach.
- **Primary Role of the National Company Registry/Beneficial Ownership registers** - Whilst AFME understands the benefits of a "multi-pronged approach to Beneficial Ownership information" (Ref 5.), Members do not consider that Obligated Entities should be required to primarily verify information held on Beneficial Ownership registers. Our Members view is that there is no substitute for a primary source, centrally administered, accessible, adequately resourced Company Registry. Central Company Registries should have systems and controls in place to verify company information in order to ensure the accuracy and adequacy of the Beneficial Ownership information.
- **Risk/ Threat Assessments** - We also welcome greater clarity on the approach to legal entity type risk assessments (Ref. 2.3). We would support a harmonised approach, which acknowledges that in an exceptional threat-based situations (for example, from FIU intelligence) it may be deemed necessary to adopt a lower threshold for a specific legal entity type.
- **Harmonised Guidance:** AFME recognises that some countries provide harmonised guidance via private industry bodies. For example, the UK has the Joint Money Laundering Steering Group, whose guidance is endorsed by the UK FCA and UK HMT and typically aligns with the FATF. Given

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<sup>1</sup> We note that certain jurisdictions have lowered their beneficial ownership threshold (to 10%) for high-risk clients, specifically in Hong Kong.

developments at the EU level as part of the EU AML package, we anticipate that the role of the Anti-Money Laundering Authority (AMLA) will be to develop and issue harmonised guidance which is preferable to guidance instead by national supervisors. We are concerned that guidance produced at a country level, which is not aligned will result in discrepancies and undermine the benefits of a harmonised approach

- **Beneficial Ownership registers:** We advocate for reliable and accurate Beneficial Ownership registers, which is particularly helpful for Obligated Entities identifying low risk individuals.
- **Additional reporting obligations:** We are also concerned that the number of recommendations contained within the guidance could create additional reporting obligations for Obligated Entities. The proposals on the treatment of a global client could for example, prove particularly difficult. We also note that there is an existing centralised system for corporate registry and welcome a streamlined approach.
- **Control through debt instruments (or other convertible financial instruments):** AFME acknowledges the potential Beneficial Ownership utility afforded by certain debt instruments to the extent they can be converted into voting equity shares reflecting control, however such instruments only confer Beneficial Ownership through control once the conversion clause is activated within an executed agreement. AFME requests that this is explicitly clarified within the guidance.
- **Multi-pronged approach to Beneficial Ownership information:** We are concerned that the multi-approach as specified in sections 5, 6 and 7, may introduce greater burdens on Obligated Entities and wish to emphasise that these requirements rely on financial institutions having adequate resources available to them. It is our view that the public sector has a responsibility to provide accurate and adequate information for Obligated Entities to utilise.

Having reviewed the draft guidance carefully with our members, we propose the following recommendations to support the FATF's objective to prevent the misuse of legal persons for money laundering or terrorist financing. We have also identified a series of areas, where we welcome further clarity.

We would be happy to discuss any of the raised in our response with you if that would be helpful.

## I. Response to draft guidance to Recommendation 24

### Question 1. Whether the Guidance is clear or are there any issues which need further clarification.

#### AFME response:

- **Section 2.2: Foreign legal persons:** This section suggests that countries may determine what is considered a sufficient link on the basis of risk. Examples of sufficiency tests may include, but are not limited to, when a company, on a non-occasional basis, owns a bank account, employs staff, owns real estate, invests in the stock market, owns a commercial/business insurance, or is a tax resident in the country. On what is considered a 'sufficient link' based on the examples given above, except for tax residence, AFME Members consider that the definition of links to country is too broad. For example, where an entity (e.g., a Private Investment Vehicle (PIV)) may be used to hold properties in the UK and bankable investments in various jurisdictions' bank accounts) the general principle of looking through to the individual Ultimate Beneficial Owner (UBO) on Source of Wealth (SOW) is currently applied without further understanding of where the assets are held. We welcome further guidance or confirmation if exclusions are to be considered, if the country links of the assets held are to be assessed and if they should be applied on an account holder entity level instead of the UBO SOW.

- **Section 2.3, Risk assessments :** We also welcome greater clarity on the approach to risk assessments. Our Members are of the view that risks are identified via threat-based risk assessments and intelligence and not determined by the entity type. Therefore, we welcome an approach that will facilitate utilising real time intelligence information obtained from public-private partnerships (PPPs) and from firm's intelligence data. We would support a harmonised approach, which acknowledges that in an exceptional threat-based situation it may be necessary to adopt a lower threshold.
- **Section 4: Definition of Beneficial Owner:**

The FATF definition of Beneficial Owners appears in Box 2 (*"beneficial owners refers to the natural person(s) who ultimately owns or controls a customer .... It also includes those natural persons who exercise ultimate effective control over a legal person or arrangement*).

- We note however that the distinction between ownership interest and control is unclear as voting rights and outstanding debt convertible into voting rights/debts instruments are mentioned in both definitions (point 35 and 44).
- While in Box 2, the identity of the natural persons exercising control through ownership interests should be done "to the extent that there is a doubt about whether a person with a controlling ownership interest in the Ultimate Beneficial Owner of where no natural person exerts control through other means", our understanding of point 31 is that both methodologies (ownership interests/control via other means), must be applied in parallel. Furthermore, point 52 states that information on more than one form of Beneficial Ownership (e.g., through both ownership and control) could be considered by countries as useful. We would welcome clarity on the process of identification to understand whether it is a one or two step process with two investigations in parallel.
- We welcome the usage of an ownership threshold to determine Beneficial Ownership based on ownership interest (as stated in point 36) but we are not in favour of the possibility given to countries to apply different thresholds as mentioned in point 36 (*a threshold should not exceed...*) and point 38 (*countries ... apply different thresholds e.g. across different sectors of the economy or for different types of legal persons*). Examples of factors to be considered in setting a threshold in point 39 should be qualified by reference to the RBA and should be used at the FI level when assessing the client's relationships risk and not for specific legal entities.
- We also note that the threshold for determining beneficial ownership based on ownership interests should not exceed a maximum of 25% (point 36) whereby the interpretative note of recommendation 10 refers to person owning more than a certain percentage (e.g., 25%). In order to prevent jurisdictions which have adopted a 25% plus one share rule to re-evaluate their requirements, we suggest maintaining the threshold of more than a certain percentage of the legal person (e.g., 25% or more).
- We also welcome confirmation that in scenarios where Obligated Entities can reasonably satisfy themselves that a Beneficial Owner cannot be identified that there is no further expectation to perform disproportionate verification activity that this is the case. As outlined in (32.), the Obligated Entity should identify a natural person who holds the position of senior managing official and record him/her as holding this position. This supports a risk-based approach to non-Beneficial Owners further due diligence requirements in order to avoid practical challenges. For example,

when operationalising source of wealth requirements for individuals who may be identified as Politically Exposed Persons (PEPs) are acting as decision makers within a corporate client but are not meeting the Beneficial Owner definition. Furthermore, in verifying Beneficial Owners we welcome the guidance that *“a risk-based approach should be adopted in determining the reasonableness of the verification measures”* and suggest that Obligated Entities should have a degree of risk-based flexibility in deciding what steps need to be taken to identify and verify the identity of a key decision maker (rather than a Beneficial Owner), particularly when it comes to highly scrutinised, audited, regulated, listed or state owned corporates in appropriately regulated jurisdictions/markets.

- **Section 4.3: Control through debt instruments (or other financial instruments):** AFME notes that it is particularly challenging and impractical for firms to identify Beneficial Ownership and control through debt instruments, and we are unclear what specific concern the FATF is seeking to address in the draft guidance. Whilst asking a firm if they have issued a debt instrument may not appear problematic, where a firm has a client who is a corporate, for example, it is likely that the structure of their securities holdings will be confidential information which they are not currently required to disclose. The guidance infers that firms would need to ask corporates for confidential information, in order to determine if such instruments have been issued in a way that breaches the Beneficial Ownership threshold.

As we explain on our high-level summary, there are significant proportionality, practical and financial information confidentiality concerns pertaining to Obligated Entities being advised to view convertible financial instruments as reflecting Beneficial Ownership when they have not been activated for conversion to voting equity and may not ever be activated. It is likely that the structure of a corporate/wholesale client’s complex capital financing arrangements and securities issuances/holders will be confidential financial information which clients are not legally obliged to disclose unless already made public. In addition, as the guidance is drafted, this would require Obligated Entities to undertake and resource a forensic-level financial analysis of capital financing arrangements (including complex calculations of % un-activated debt holding counterparty distribution) of each client, in order to determine potential Beneficial Ownership through control/other means. AFME views this as a disproportionate approach, which would divert resources away from focusing on the true controlling Beneficial Owners, on a risk-based approach.

Furthermore, whilst AFME welcomes the caveating statement that *a bank providing financing to a legal person will rarely be considered as exercising control over the legal person by the act per se*, it is unclear what the parameters of a *rare* context might look like in practice. AFME does not consider that bi-lateral/syndicated financing arrangements (with no convertible contractual options) would ever amount to Beneficial Ownership, therefore AFME requests further specificity and explicit clarification on this point within the guidance.

- **Section 5: Multi-pronged approach to Beneficial Ownership information:** We are concerned that the multi-pronged approach as specified in points 45-49 may introduce greater burdens on Obligated Entities and wish to emphasise that these requirements rely on financial institutions having adequate resources available to them. It is our view that the public sector has a responsibility to provide accurate and adequate information for Obligated Entities to utilise. This is also the case for Adequate Beneficial ownership information in **section 6** and Accurate information – means of verification of Beneficial

ownership information in **section 7**. We also wish to make a general point that the FATF position on verification and adequate resources is insufficiently clear.

- **Section 7.3: Discrepancy Reporting Mechanisms:** We note that Section 7.3 of the proposed recommendation suggests that in order to support the accuracy of Beneficial Ownership information, countries should consider complementary measures as necessary to support the accuracy of Beneficial Ownership information, e.g., discrepancy reporting. We welcome further guidance is provided on the definition of discrepancy and how it would be applied to entities with multi-layers across multiple jurisdictions with private trusts for example. For multi-layer structures involving multiple jurisdictions, this may be challenging for firms to determine which discrepancy reporting should be made to the respective authorities.
- **Section 8: Up to date basic and Beneficial Ownership information:** We note that the Interpretive Note to Recommendation 24 refers to “up-to-date information” as information, which is as current and up to date as possible, and is updated within a reasonable period (e.g., within one month) following any change. We welcome further clarification as to whether the expectation is that financial institutions would be expected to update information within one month as well. Our Members consider that the current one-month expectation may be operationally challenging for complicated structures and may pose an additional burden.
- **Section 10: Data protection:** AFME welcomes more guidance for Obligated Entities accessing Beneficial Ownership registers. We are also mindful of the November ruling of the Court of Justice of the European Union. It is our view that access to Registers of Beneficial Ownership should, at a minimum, include FI’s so that they can meet their obligations under the EU Anti Money Laundering Regulations.

**Question 2. Are there case examples of registries and alternative mechanisms for holding of accurate, adequate and up-to-date beneficial ownership information?**

**AFME response:** Our Members also wish to reinforce the value of utilising the corporate registry. Please also see our response to Q1 on the FATF’s proposed multi-pronged approach and the importance of not placing additional burdens on financial institutions to maintain the accuracy of information in Beneficial Ownership registers. We are also keen to stress the importance of continued access to registers in order to comply with obligations under EU Money Laundering Regulations.

**Question 3. Are there case examples of mechanisms to verify Beneficial Ownership information in low-risk scenarios?**

**AFME response:** We are unable to provide examples of alternate mechanisms. We do however suggest that for listed companies it is possible to use information that is contained within an annual report. For unlisted companies who are regulated entities in the UK, their Beneficial Ownership information is submitted to the local supervisors e.g., the close links reports submitted to the UK PRA and the FCA.

**Question 4. Are there case examples of the use of information held by stock exchanges for listed companies to meet Beneficial Ownership information obligations?**

**AFME response:** We have no comments on this question.

We have also reviewed the proposal relating to Recommendation 25 and welcome the additional clarity that they provide.

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