AML Beneficial Ownership Register in Ireland – Who's Holding the Baby?

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AML Beneficial Ownership Register for Irish Funds – Who's Holding the Baby?

Background

If you've been involved in the funds industry, you will be well aware of the ever-increasing focus on anti-money laundering and "know your customer" requirements by national and supranational regulatory bodies alike. In fact, the Central Bank of Ireland (**Central Bank**) has consistently listed anti-money laundering as an enforcement priority every year since 2012. A new addition to these obligations is the implementation of the European Union (Anti-Money Laundering: Beneficial Ownership and Corporate Entities) Regulations 2016 (**Regulations**), which implemented Article 30 of the Fourth Anti-Money Laundering Directive EU 2015/849 (**4 AMLD**) and which took effect in Ireland on 15 November 2016. As of that date, all companies and legal entities established in Ireland (**Companies** and each a **Company**) were required to take all reasonable steps to gather and maintain adequate, accurate and current information of their "beneficial owners" on an internal beneficial owner register (**Internal Register**).

The Regulations dealt with one aspect of 4 AMLD which was due to be transposed into Irish law in full by 26 June 2017. Meanwhile, a proposal for a Fifth Anti-Money Laundering Directive (**5 AMLD**) which will amend 4 AMLD is at an advanced stage and is currently scheduled to be discussed by the EU Parliament later this year. It is likely therefore, that the remainder of 4 AMLD will not be implemented into Irish law until the proposals for 5 AMLD are settled, although EU Member States will be required to enable public access to information about the beneficial ownership of companies from 1 January 2018.

The requirement to maintain an Internal Register is the first of a two-stage process required by all EU Member States in relation to putting in place national provisions around beneficial ownership information. In due course, all Companies will also be required to file this information with a central beneficial ownership register (**Central Register**) which for corporate entities is in the process of being established by the Companies Registration Office (**CRO**) and is expected to be populated in Q4, 2017. By implementing the Regulations, Ireland adopted an early implementation approach to Article 30 of 4 AMLD to allow entities an appropriate lead in time to gather the necessary data required in order to complete the information required for the Central Register.

The Regulations do not provide for any transitional arrangements and, therefore, all Companies were expected to be in compliance of the requirement to maintain an Internal Register as of 15 November 2016.

For a number of reasons which are set out below, it is proving difficult from a practical perspective for Irish funds to achieve compliance with the requirement to maintain an Internal Register.

The Problem

The requirement to identify the beneficial ownership is nothing new so on a first view there should be no problem. The issue is that in most cases, such identification and verification is done indirectly through reliance on third parties in accordance with the existing AML regime which sets the bar in relation to such reliance at a high level.

Third party reliance allows a designated person to rely on relevant third parties to complete certain Customer Due Diligence (CDD) requirements whereby the third party undertakes the CDD information in relation to the underlying client and enters into a written agreement under which it agrees to provide within a certain time frame all CDD documentation in relation to its underlying client and/or its beneficial owner.

The process of identifying the beneficial owner is also reliant on customer self-certification and information held in company registries and financial institutions. However, most of these sources have limited or no access to offshore entities or contain unreliable, incomplete data.

The difficulty with the Regulations is that it does not take account of such third party reliance meaning that notwithstanding the well established procedures for third party reliance which are generally implemented either through the investment manager or through a distributor, the fund itself must exercise all reasonable steps to carry out its own investigation of beneficial ownership in order to construct the Internal Register.

This is a significant shifting of the goalposts with regard to AML compliance and one which Irish funds and their administrators who typically rely on third parties to undertake AML functions are struggling with. Irish funds are therefore examining the ways in which they can minimise the impact of the Regulations while adhering to full and rigorous compliance with all applicable AML law.

The Regulations apply at Company level meaning that for umbrella funds, the Company will have to aggregate the information from the share registers of each fund up to umbrella level.

As collective investment schemes, most funds are broadly owned, with shareholders generally owning, directly or indirectly, relatively small stakes in fund Companies. For the limited number of funds that are impacted, compliance in many instances should be quite straightforward as funds that have a small number of shareholders, will generally be in that position for specific reasons. This may be due to the fact that the fund was created with a relatively small numbers of investors in mind or because it is comprised of a small number of seed or initial investors. In such circumstances, the identity of the beneficial owners will be a relatively straightforward exercise. The public policy dimension of requiring investors to effectively disclose details of their investments simply because they are in corporate form is questionable.

Application

Given the various types of legal structures in which Irish funds can be established, one of the key questions that has arisen is “are we caught by this?” The Regulations apply to Companies which is defined as a corporate or other legal entity incorporated in the State and includes a company and any other body corporate so incorporated. Therefore, the Regulations would appear to apply to all Irish funds structured as corporates (i.e. investment companies and ICAVs) and also to Irish management companies whether structured as AIFMs or UCITS management companies.

The Regulations do not apply to non-corporate structures such as unit trusts, investment limited partnerships or common contractual funds although, in line with Article 31 of 4 AMLD, there are proposals to implement similar regulations to deal with trusts later this year.

Also exempt from the Regulations are corporate entities which are:

- listed on a regulated market that is subject to disclosure requirements consistent with EU law, or
- subject to equivalent international standards which ensure adequate transparency of ownership information.

In a funds context, it would appear that this exemption would only apply to closed-ended funds as these are subject to the Transparency Directive and would satisfy the "listed on a regulated market that is subject to disclosure requirements consistent with the law of the European Union" exemption.

Who is a Beneficial Owner?

The Regulations refer to the definition of "beneficial owner" contained in Article 3 of 4 AMLD. The term means a natural person who ultimately owns or controls a legal entity through direct or indirect ownership of a sufficient percentage of the shares or voting rights in that entity or through control by other means. A percentage of 25% plus one share held by a natural person is stated to be evidence of direct ownership, and a shareholding of over 25% held by a corporate entity under the control of a natural person, or by multiple corporate entities which are under the control of the same natural person, is stated to be an indication of indirect control.

Where the beneficial owners are not known, Companies must take "all reasonable steps" to ensure the beneficial ownership information is gathered and recorded on the Internal Register. Where no beneficial owners can be identified, Companies are required to enter the names of the directors/senior managers of the Company on the Internal Register as the "beneficial owners". In a funds context this will typically be the board of directors on the basis that they are the controllers of the Company.

The purpose of these requirements is to enable the determination of the natural persons who are the real owners/controllers of a Company. In many cases, this is clear as the legal owners and beneficial owners are one and the same. In other cases, the ownership may be so diluted that it is not possible to identify a particular beneficial owner. As noted above, funds are generally broadly held and from a practical perspective, the identification of the "beneficial owner" will likely be most relevant in the context of funds which have a small number of investors and funds which are (initially at least) capitalised with seed investment.

In most other circumstances, the directors of a fund are most likely to be listed as the beneficial owners on the register of beneficial ownership of a fund.

Internal Register – Information to be Held

The following is a summary of the information that Companies are required to hold in relation to their beneficial owners under Section 4 of the Regulations:

- name, date of birth, nationality and residential address;
- statement of nature and extent of interest held;
- date of entry as a beneficial owner on the register; and
- date of entry of ceasing to be a beneficial owner.

Central Register – Information to be Filed

Once established, the above information will be required to be filed on the Central Register, which will be done through an online portal with the CRO. It is expected that the Department of Finance will make a Statutory Instrument in the coming months assigning separate legal responsibility to the CRO for the establishment and maintenance of the Central Register. Companies will have at least 3 months once the Central Register is established to file without being in breach of their statutory duties.

The CRO has produced a helpful template of the data to be entered in the Central Register. The information to be filed with the CRO is respect of each beneficial owner will include the following:

- forename & surname
- date of birth
- nationality
- residential address
- a statement of the nature of the interest held by each beneficial owner
- a statement of the extent of the interest held by each beneficial owner
- the date on which each natural person was entered in the register as a beneficial owner of the Company
- the date on which each natural person who has ceased to be a beneficial owner of it, ceased to be such an owner
- if no natural persons are identified there shall be entered in the register the names of the natural persons who hold the positions of senior managing officials of the Company

It is not clear yet whether the Central Register will be publicly accessible or if access will be restricted to appropriate parties such as entities carrying out customer due diligence, EU regulatory and financial intelligence units and other that can demonstrate a legitimate interest. As it stands, 4 AMLD provides that the information on the Central Register must be accessible to:

- competent authorities and financial intelligence units;
- “obliged entities” (including investment funds and banks), when carrying out customer due diligence measures; and
- those who can demonstrate a “legitimate interest” in the information.

Member States may provide for wider access to the Central Register, and it remains to be seen whether Ireland will avail of this option. The Regulations do not deal with this aspect of 4 AMLD.

Furthermore, it has yet to be decided what if the Central Bank as registrar will maintain the Central Register on behalf of ICAVs.

Acquiring the Information

Companies may send a "Regulation 6 Notice" to any individual that the Company has reasonable cause to believe is a beneficial owner. The individual must confirm within one month of receipt whether they are in fact a beneficial owner of the Company and if so, whether the details on the Notice are correct.

A Regulation 6 Notice is not required if a Company knows an individual is a beneficial owner, and the necessary information relating to that individual has been provided either by the individual or with his or her knowledge.

Companies can issue a similar notice - a "Regulation 8 Notice" to any entity, such as a distributor or intermediary that they have reasonable cause to believe is aware of the identity of any individuals who may be beneficial owner of the Company.

In a funds context, the appropriate representations could be sought from individuals through the subscription form process for example.

Issuing such notices in a funds context is especially problematic as an investor in a fund will not likely be aware if they are a "beneficial owner" of the fund and in the case of daily dealing funds the holding has the potential to change frequently.

Furthermore, data protection issues may arise as the beneficial owner may be non EU domiciled and Companies will need to access whether they have the appropriate date protection consents before they transfer data to the Central Register.

Obligation on Individuals to Notify Changes

Individuals who are beneficial owners are obliged to notify Companies in which they hold a beneficial interest of such beneficial interest where the required information has not already been provided and to notify them of any change in the future.

Ongoing Obligations

The Internal Register must be updated when there has been a relevant change in beneficial ownership, (i.e. where a natural person ceases to be a beneficial owner, or when there has been a change in the information contained in the Internal Register). Where a Company learns of such changes or has reasonable cause to believe that such a change has occurred, it must serve notice on the natural person concerned seeking updated information, unless the information has already been provided by or on behalf of the natural person.

So who holds the Baby?

The beneficial ownership requirements represent a significant development for Companies and their ultimate beneficial owners as, before now, the identity of the beneficial owners for Irish Companies could remain largely private where such persons were not direct shareholders of the company. Under Irish company law, the legal name entered on the share register is conclusive evidence of the shareholding.

While the Regulations have given rise to many challenges for funds and their management companies, the obligation to keep information up to date in the context of daily dealing funds and intra-day dealing funds poses a particular challenge. In addition, Irish investment funds are commonly distributed on a global basis and these requirements may prove problematic for third country investors who may not be familiar with such requirements. It may be appropriate to treat the information required to maintain the Internal Register in a similar fashion to

other AML documentation so that a subscription may be accepted, but a blocked placed on redemptions until all relevant information is received.

The board of directors of an Irish fund or management company, while having overall responsibility for ensuring that the fund complies with its legal and regulatory obligations, typically delegates the shareholder dealing function, the maintenance of the register and AML compliance to the fund's administrator. In the context of its role as transfer agent of a fund, it is the administrator who maintains the fund's share register and is arguably, therefore, best placed to maintain the Internal Register. The administrator should reasonably expect to be remunerated for this role.

However, administrators have been reluctant to take on this role given the degree of uncertainty around the requirements, the manual nature of the processes necessary to ensure compliance and the operational risk that it may expose them to.

In other instances, we have seen the company secretary or the fund's MLRO undertake this role based on data provided by the administrator. In addition and unlike the approach taken in other countries, for example, the UK which issued detailed statutory guidance in relation to how to deal with this requirement, Ireland has not to date issued any such guidance.

The manner in which the Regulations were transposed into Irish law has created a number of ambiguities and open questions which industry are seeing to have addressed by the Department of Finance. One potential solution which is being sought by industry is that there should be no requirement to look beyond intermediaries, given the fact that intermediaries are subject to their own due diligence standard in respect of its underlying customer base. However, until the Department of Finance provide industry with some comfort in relation to whether they can rely on this approach, Irish funds will need to ensure compliance with the Regulations.

It might be more appropriate to adopt a risk based assessment on a case by case basis which is central to the effectiveness of AML compliance.

While the "all reasonable measures" test provides a certain flexibility as a regulatory minimum standard, a risk based approach should be adopted to ensure that Companies move beyond compliance with the Regulations as a box ticking exercise.

While the absence of any guidance has certainly compounded the uncertainty around how fund boards should comply with these requirements, given the length of time that has now elapsed since the Regulations became effective and the fact that no transitional arrangements are afforded, fund boards now need to take proactive steps to ensure compliance.

The funds industry, while having so far adopted a "wait and see" approach generally, will need to agree a consistent approach to dealing with fund Internal Registers and decide whether this is a service offering that is appropriate for the administrator/registrar solely, or if there are systems and mechanisms that can be put in place to allow real-time updates to a third party in relation to shareholder dealing to allow the Internal Register to be updated upon a change.

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