Ultimate Beneficial Owners (UBO) Between Identification and Verification

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I. Executive Summary

Establishing effective policy and processes to identify an ultimate beneficial owner (UBO) is essential in combating money laundering and terrorist financing. All UBOs should be identified, declared, verified (where applicable) for all new and changes to existing accountholder accounts and financial services and products provided to occasional (walk-in) accountholders. These procedures must require proper due diligence and may identify unusual transactions, and possibly report the suspicious transactions. International AML standards and regulations (i.e., the Financial Action Task Force [FATF] Recommendations, the Financial Crimes Enforcement Network [FinCEN] and the Basel Committee principles), and local regulatory requirements impose legal and regulatory obligations on financial institutions (FIs) to identify UBOs, these obligations will be discussed in this white paper.

FATF defines¹ UBOs as natural person(s) who ultimately owns or controls an accountholder and/or the person on whose behalf a transaction is being conducted. It also incorporates those persons who exercise ultimate effective control over a legal person or arrangement.

1. 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.
2. This definition should also apply to a beneficial owner of a life or other investment linked insurance policy.

Money launderers, terrorists and sanctioned parties try to access the financial system by hiding their existence (i.e., true identity) during account opening and service request processes, through using individual or non-individual accounts opened by their association’s or family members’ names, or opening accounts for legal entities with complex ownership structure, or any other tactics to avoid detection.

UBO identification and verification can be very difficult due to a lot of challenges, for example:

1. Complex ownership structures of the legal entities
2. Legal entities established in high secrecy jurisdiction (i.e., Samoa, Cayman Islands, Panama)
3. False accountholder’s declarations on UBOs
4. Limited information available on offshore accountholders
5. Unqualified staff

FIs have the ultimate responsibility to identify UBOs and verify them (where applicable). It is worth to mention that UBO verification for individual accounts is not possible in most cases, as FI’s depend on the accountholder’s declaration only. On the other hand, FIs could be verified the

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¹ Source: Glossary of the FATF Recommendations (http://www.fatf-gafi.org/pages/glossary/)
identified UBO for non-individual accountholders, through reviewing the client’s know your customer (KYC) documentation.

Therefore, appropriate policy, procedures and controls must be established to comply and mitigate the legal, compliance and regulatory risks. The methodologies of identifying UBOs vary among FIs. Some identify UBOs through obtaining a Declaration Form specifying the UBO and signed by the accountholder. Others verify the UBO through obtaining formal documents that identify the UBO.

II. Methods of Identification and Verification for UBOs
   A. Possible UBOs of Common Types of Accountholders

Possible UBOs of common types of individual and non-individual accountholders (legal entities/arrangement) could be identified in detailed in the table below.

<table>
<thead>
<tr>
<th>Accountholder Classification</th>
<th>Account Type</th>
<th>Possible UBO</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual</td>
<td>Adult Accountholder Account</td>
<td>1. Third party</td>
</tr>
<tr>
<td></td>
<td>Adult Accountholder Account opened through Power of Attorney (POA)</td>
<td>1. Power of Attorney (POA) holder 2. Third party</td>
</tr>
<tr>
<td></td>
<td>Minor Accountholder Account opened by Guardian</td>
<td>1. Guardian 2. Third party</td>
</tr>
</tbody>
</table>

2 Third party: anyone that has direct/indirect control over the account holder
B. The identification and verification process for UBOs should be performed during account opening, while updating KYC information, when obtaining banking services/products forms. Policy, procedures and processes must clearly ask the accountholder to declare the UBO, with imposing an obligation on the accountholder to update the FI, if the declared UBO is changed.

The following must be obtained, before providing the financial service, activating the account, or issuing banking self-services to the accountholder for individual and non-individual accounts:

1. Reason of having a third party as a UBO and the relationship between the accountholder and the declared UBO.
2. Full KYC documentation and information (full name, nationality, resident address, source of funds/wealth, etc.)
3. If the accountholder is a citizen of the U.S., it is required that they complete the appropriate form, to comply with Foreign Account Tax Compliance Act (FATCA) requirements, for individual accounts only.

UBO verification can be conducted through several different ways, as explained in Figure 1.

![Figure 1 Verifying UBO](image)

The above methodology may differ between institutions and accountholder types, but the UBO must be clearly identified and verified by the FI as an essential part of KYC requirements.
III. The Importance of Compliance with UBO Requirements

A. The grounds of regulations imposing the obligation of identifying UBOs is addressed in various manners by the Department of the Treasury of the U.S., U.K. Money Laundering Regulations 2007, the European Commission, FATF Recommendations and the Basel Committee’s customer due diligence (CDD) paper. These are all summarized as:

1. **Sections 325 and 326 of the USA Patriot Act 2001**, issued by Department of the Treasury of the U.S., requests FIs to take additional steps to identify UBOs of the accountholder by seeking information about individuals with ownership or control over the account, and verify it.

2. **U.K. Money Laundering Regulations 2007**, regulation numbers 7.4.b and 9.2 (2) requires FIs to identify and verify beneficial owners when it: A) Establishes a business relation; B) Carries out an occasional transaction (which is defined as a transaction outside of a business relationship amounting to EUR 15,000 or more, whether the transaction is carried out in a single operation or several operations which appear to be linked); C) Suspects money laundering or terrorist financing; D) Doubts the veracity or adequacy of documents, data or information previously obtained for the purposes of identification or verification.

3. **EU Fourth Anti-Money Laundering Directive**: The new EU anti-money laundering (EU 2015/849) directive became effective on June 26, 2015. The Directive applies to a range of businesses, from FIs to auditors and accountants, and generally defines “beneficial owners” as “any natural person(s) who ultimately owns or controls the accountholder and/or the natural person on whose behalf a transaction or activity is being conducted.” Furthermore, the beneficial owner “shall at least” include, for corporate entities, the natural person who “owns or controls a legal entity through direct or indirect ownership or control over a sufficient percentage of the shares or voting rights.” Retaining the Third Directive threshold, a percentage of 25 percent plus one share constitutes sufficient evidence of ownership or control.

4. **FATF Recommendations** related to transparency and beneficial ownership of legal persons/arrangements (24 and 25) encourage identifying and verifying the UBO, and requires countries to ensure that competent authorities have timely access to adequate, accurate and up-to-date beneficial ownership information. Also, Recommendation 10, which addresses the CDD measures that are expected from FIs, specifically states that

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3 The European Commission is the EU’s executive body. It represents the interests of the European Union as a whole (not the interests of individual countries). website (http://ec.europa.eu/about/index_en.htm)

4 Department of Treasury of United States (FinCEN) website (http://www.fincen.gov/statutes_regs/patriot/)


7 FATF Recommendations - Transparency And Beneficial Ownership of Legal Persons And Arrangements-Page 22 (http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/fatf_recommendations.pdf)
“Identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner, such that the FI is satisfied that it knows who the beneficial owner is.” For legal persons and arrangements, this should include FIs understanding the ownership and control structure of the account holder.

5. Basel CDD paper (sections 2.2.1, 2.2.2, and 2.2.4)\(^8\) and Wolfsberg principles\(^9\) encourages FIs to identify and verify the UBO for account holders and establish the beneficial ownership for all accounts. This general principle is then elaborated in the context of natural persons, legal entities, trusts, nonprofit organization and pool funds.

Most FIs can comply with the above requirements through the development and implementation of policy, procedures and controls. In addition, FIs can comply by providing the required training to concerned staff, in order to understand the UBO of any proposed account holder, the ownership structures for different types of legal entities, and appropriate forms to use to allow account holders to properly identify the UBO. These mandatory internal forms must be completed by the account holder during account opening and the KYC update process. The ultimate responsible parties of complying with these requirements are business operations, oversight functions (i.e., regulatory compliance and risk), and independent assurance (i.e., internal audit, external audit and other independent assurance providers).

B. Consequences of Not Complying with the UBO Requirement

Serious consequences for noncompliance can be imposed as mentioned in Figure 2. In order to ensure compliance, an organization should prepare an action plan, follow-up, validation and rectify existing account holders accounts opened without identifying UBO. This is in addition to the typically incurred costs and resources required for AML compliance. Moreover, all AML/regulatory regulations prohibit FIs from maintaining anonymous/nominee/numbers accounts, which are controlled by or held for the benefit of another person; the identity of that person is not disclosed.

IV. Challenges of Identifying and Verifying UBO

A. Identifying and Verifying UBOs

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\(^8\) Basel Committee on Banking Supervision- Account holder due diligence for banks issued on October 2001 ([http://www.bis.org/publ/bcbs85.pdf](http://www.bis.org/publ/bcbs85.pdf))

\(^9\) The Wolfsberg Group is a private association of eleven global banks, founded in 2000 at the Château Wolfsberg, (Switzerland). Its goals have been to develop financial industry standards for Know Your Account holder (KYC), Anti-money laundering (AML) and Counter Terrorist Financing (CTF) policies, similar to what the Financial Action Task Force (FATF) on Money Laundering does on a government level, the Wolfsberg Standards consist of the various sets of AML Principles, as well as related Statements, issued by the Group since its inception, for more information refer to Wolfsberg Group’s website ([http://www.wolfsberg-principles.com/index.html](http://www.wolfsberg-principles.com/index.html)).
FIs are facing a lot of challenges and obstacles when trying to comply with UBO requirements. The major ones as follow:

1. The complex ownership structures of multinational companies, the actual UBO might be identified and verified through reviewing the entity's ownership structure, which requires for digging in the ownership structure until determining the natural person with real interest for whom the Business relationship or on his behalf is conducted or who has ultimate or effective control over a legal person or has the right to conclude a legal entity on its behalf. In case the beneficial owner is a legal person, reasonable measures must be taken to verify the ownership structure and the controlling management of the legal person.

   This obstacle is outlined further below in Section VI (Case Study).

2. UBOs are difficult to identify for legal entities incorporated in high secrecy jurisdictions (i.e., Samoa, Cayman Islands and Panama), the ownership structure of legal entity might be not available in the registration certificates (Certificate of Incorporation, Memorandum and Articles of Association, etc).

3. False declaration of a UBO provided by the accountholder, or the accuracy of such information cannot be verified in some cases.

4. Most countries do not publish on public domains the ownership structures of the companies incorporated in their jurisdiction, which makes the verification of any UBO very difficult.

B. Observations on the Current Audit Process of UBOs

Line of business, compliance and internal audit departments should perform the following:

1. Review KYC documentation for new and existing accountholder accounts, to ensure that UBO has been identified and verified. Self-assessment is recommended to be conducted by the compliance department using a variety of means to validate the UBOs; such as a review of completed KYC forms, risk/breach logs, participation in account opening/KYC interviews and workshops involving business managers;

2. Create system controls into the organizations’ core systems to make identifying UBO on the system mandatory before account activation and before issuing self-service items (cheque books, ATM card, Internet banking, phone banking, etc.). Periodic validation should be conducted by an independent party on such controls to make sure they are effective and sufficient;

3. Review the justifications for having a UBO (different than accountholder) for account holders’ accounts, and checking the availability and accuracy of KYC documentation related to identified UBOs.

C. Lack of Independent Testing to comply to UBO Policy and Procedures
Most ad-hoc and periodical testing conducted by external/internal auditors are missing detailed and real assessments of the entities’ compliance with identifying and verifying UBOs, identifying the weakness of current processes and the opportunities for control enhancement.

The tests and assessments conducted are limited to ensuring that the UBO forms are complete without checking the accuracy of identified UBOs and reasons the UBO is different than the accountholder/shareholder/authorized signatory, “if any.”, without checking that AML risk score rating and full KYC documentation of identified UBO have been obtained.

V. Identify Effective Policy, Procedures and Controls to Identify and Verify the UBO

A. Risk Assessment

Risk assessment should documents what staff and relationship managers have to do to verify different types of accountholders. For example, when a national resident individual wants to become an accountholder, the front staff must identify both the accountholder and the UBO and obtain standard KYC documentation. The risk assessment may lead you to treat this accountholder as a low-risk customer.

If the accountholder is rated as a moderate or high-risk customer, enhanced due diligence (EDD) should be applied/conducted. In this case, EDD must be obtained and the information relating to the source of funds or wealth of the accountholder, expected nature of transaction, turnovers and the countries that the accountholder will receive/send transfers from/to, must be maintained. On the other hand, EDD for nonindividual account holders should be conducted by obtaining the following:

1. KYC documentation showing the UBO (i.e., memorandum/articles of association, or bylaws of the accountholders and the related parties that have direct/indirect control on the accountholder);
2. Check the UBO by reviewing credit reference/information bureau
3. Latest audited financial statements; and
4. Source of cash, “if any,” expected nature of transaction, turnovers, countries that the accountholder will receive/send transfers from/to.

B. Developing and Implementing Effective Policy and Procedures

Anti-money laundering (AML) and compliance policies and procedures should contain a clear process on for identifying and verifying the UBO. All new and existing accounts are subject to verifying the identifying UBOs during account opening or KYC updates processes.

The policy should identify the concerned parties which are responsible of conducting the process.

Moreover, policy and procedures should provide a clear guidance for complex/complicated scenarios related to individuals and nonindividual accounts. The same should be reflected in the policies and procedures related to the institution’s products and services. It is necessary to
provide adequate training and awareness among concerned employees, from time to time, via training seminars, conferences and emails in order to:

a. Keep all parties current on the processes for identifying and verifying UBOs;
b. Provide solutions to comply with UBO requirements for complicated/complex cases;
c. Keep open communication between front staff and compliance to answer questions and provide assistance/advice.

The related policies and procedures should be reviewed and updated frequently by concerned parties (compliance, legal, line of business management, audit, etc.), in order to make sure they are still up-to-date, and all laws and regulations are reflected and addressed.

C. Creating Core System Controls

System controls are essential to decrease human error and comply with the defined UBO requirements. Some fields can be created in the organization’s KYC system, making entering the identified UBO and related information into the system mandatory before activating the accountholder’s account, or prior to providing the required service. The validation process should be performed before launching such controls on the system, before being used by accountholders or internally by employees, and must be reviewed periodically to make sure they are valid and up-to-date. This should occur since criminals always come up with new tactics and tricks to circumvent such controls.

It is possible to use an AML risk rating for accountholders, as mentioned in Figure 3. Moreover, this will help auditors and compliance officers maintain accumulated lists of accountholders and their UBOs, for auditing and reporting purposes.

With oversight by the board of directors, and development by management and other personnel. Creating a system of controls is on of effective way to meet the following objectives:

1. Effectiveness and efficiency of operations
2. Compliance with applicable laws and regulations
3. Reliability of regulatory reporting

Control activities encompass the policies and procedures that help ensure that management directives are carried out.
D. Matrix of KYC Requirements

Using a matrix showing KYC requirements for a proposed account holder, especially for the nonindividual account holders, is an efficient way to make sure that front staff and relationship managers have a clear and documented checklist to obtain the required KYC documentation and information, for different types of account holders. This also helps them verify the UBO of a company with a complex and multilayer structure by reviewing the commercial registration extract, memorandum/articles of association, bylaw documents, or trust deed.

E. Qualification and Knowledge

Employees that obtain identification and perform the verification of the UBO should be qualified and have the knowledge for dealing with legal entities, tracking the ownership in complex structures that may be located in offshore jurisdictions (Cayman Islands, Panama, etc.). These employees should have sufficient education and experience to qualify them with dealing with legal structures and documentation for legal entities and those entities that are incorporated and registered in different regions of the world.
Compliance officers should provide periodic training to concerned employees that handle account opening and KYC processes. Special attention for UBO identification and verification processing should be provided to personnel with a matrix showing the required actions on possible scenarios and examples on how to identify and verify UBOs in complex ownership structures is recommended. Moreover, special training should be conducted for concerned parties on any controls installed in the systems to keep them up-to-date and to ensure that the required information has been accurately input in the system.

Personnel should also be trained on how to use the public registers and websites to verify the UBO. It is very important for FIs with significant exposure to offshore entities that usually do not provide official documents showing the actually UBO for different reasons.

F. Other Controls for Identifying and Verifying the UBO

There are a lot of solutions that could be conducted or performed to comply with identifying UBO requirements. For instance:

1. Enhanced KYC forms through developing declaration forms making the account holder acknowledge on the existing of UBO, the accuracy of the provided information, and imposing an obligation against the account holder to update the FI immediately when identified UBO or the provided information has been changed.

2. Verifying the identified UBO for legal entities should be conducted through matching it with information available on private or public databases (i.e., Companies House register—U.K., 10 World-Check list, 11 Bankers Almanac, 12 or Zawya 13), or by reviewing governmental authorities websites (i.e., European Business Register, 14 or the local authority’s registration of the legal entity).

It is worth mentioning that the new EU AML Directive (EU 2015/849) instructs EU countries to set up registers to record the UBOs of businesses. The registers must be accessible to the authorities within each country, to obliged entities, such as FIs performing due diligence on accountholders, and to others, such as investigative journalists who can demonstrate a "legitimate interest" in gaining access to the information.

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10 Companies House register-UK website (https://www.gov.uk/government/organisations/companies-house)
11 Part of the Thomson Reuters Risk Management Solutions suite, the World-Check database of Politically Exposed Persons (PEPs) and heightened risk individuals and organizations is used around the world to help to identify and manage financial, regulatory and reputational risk.
12 It is a leading provider of reference data on the banking industry, its portfolio of solutions aims to help financial decision-makers make payments, conduct due diligence, assess credit risk and conduct financial research on the world’s banks. Containing comprehensive information on financial institutions worldwide.(http://www.accuity.com/financial-counterparty-kyc/bankersalmanac/)
13 Zawya is the preeminent source of Middle East and North Africa business intelligence and is now part of Thomson Reuters, the world’s leading source of intelligent information for business and professionals.
14 European Business Register website (http://www.ebr.org/)
VI. Case Study

The following case studies are examples and are not live cases. The names, nationalities and ownership structures mentioned in the ownership chart below are representative information for example purposes only, in order to provide ideas on the identification and verification of UBOs.

The following chart illustrates the UBO for a proposed account holder that wants to open a depository account with a bank. Based on the hypothesis that the account holder is not a public shareholding company, the regulatory requirement is to identify the UBO as any natural person(s) who ultimately owns 20 percent or more of entity's capital, or controls an account holder.
VII. Conclusion

International entities are an important part of today’s world and FIs find it attractive to offer theirs banking products and services as a great business opportunity. As international organizations have access to most jurisdictions in the world through the financial systems, by conducting remittance, issuing letters of credit, guarantees and bills of collection. FIs are required to make reasonable efforts to identify and verify the UBO, in order to avoid being used as conduit to launder illicit proceeds and to fund terrorism.

Identifying UBOs behind legal entities is possible, and verifying that information is attainable in the current situation; however, it is conducted more effectively and efficiently by utilizing technology solutions and reviewing publicly available registers published by governmental entities.

Complying with UBO requirements is essential and mandatory for all FIs around the world, as AML regulations, principles and recommendations have a common objective to identify the UBO. This requirement could be done through obtain a signed statement from account holder acknowledge on the existing of UBO. This undertaking must be obtained prior to conducting/providing any transactions/services with/to the accountholder.

Finally, FIs must obtain and document the account holders’ declarations, the result of due diligence conducted during the creation of relationship. Moreover, FIs should ask the accountholder if the UBO has been changed on any of the following cases:

1. During investigations on unusual transaction
2. During the periodic review of the accountholder’s KYC
3. During a significant change that occurred on corporate ownership and/or the legal structure
4. During others reasonable grounds
I. Glossary of Defined Terms

<table>
<thead>
<tr>
<th>Term</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accountholder</td>
<td>The individual or Entity that is assigned to the Financial Account (“the account holder” or “the policyholder”)</td>
</tr>
<tr>
<td>Bylaw</td>
<td>It is a rule or law established by an organization or community to regulate itself, as allowed or provided for by some higher authority. The higher authority, generally a legislature or some other government body, establishes the degree of control that the by-laws may exercise. By-laws may be established by entities such as a business corporation, a neighborhood association, or depending on the jurisdiction, a municipality.</td>
</tr>
<tr>
<td>Guardian</td>
<td>a person who looks after and is legally responsible for someone who is unable to manage their own affairs, especially an incompetent or disabled person or a child whose parents have died</td>
</tr>
<tr>
<td>Indicia</td>
<td>FATCA identifies a number of signs or indications that an Account Holder or Principal Party has a reportable US connection. For example:</td>
</tr>
<tr>
<td></td>
<td>1. U.S. Citizenship (US Passport Holder) or lawful permanent resident (“green card” holder).</td>
</tr>
<tr>
<td></td>
<td>2. U.S. Birthplace.</td>
</tr>
<tr>
<td></td>
<td>3. U.S. Residence address or correspondence address.</td>
</tr>
<tr>
<td></td>
<td>5. U.S. “care of” or “hold-mail” address that is the sole address for the account holder.</td>
</tr>
<tr>
<td></td>
<td>6. Power of Attorney or signatory authority granted to a person with a U.S. Address.</td>
</tr>
<tr>
<td></td>
<td>7. Standing Instructions to transfer funds to U.S. accounts.</td>
</tr>
<tr>
<td>Mutual Fund</td>
<td>An investment vehicle that is made up of a pool of funds collected from many investors for the purpose of investing in securities such as stocks, bonds, money market instruments and similar assets. Mutual funds are operated by money managers, who invest the fund's capital and attempt to produce capital gains and income for the fund's investors. A mutual fund's portfolio is structured and maintained to match the investment objectives stated in its prospectus. From Investopedia website (<a href="http://www.investopedia.com/terms/m/mutualfund.asp">http://www.investopedia.com/terms/m/mutualfund.asp</a>)</td>
</tr>
<tr>
<td>Reliable and independent electronic data</td>
<td>Data are published and available on a reliable, independent, or governmental source (Credit Reporting Information, Credit Reference Bureau, Commercial Registration Databases, world-check online/ Zawya Limited “Thomson Reuters”, etc.)</td>
</tr>
<tr>
<td>Sanctioned parties</td>
<td>Persons and companies with whom trade is prohibited by law.</td>
</tr>
<tr>
<td>Trustee</td>
<td>It is refer to any person who holds property, authority, or a position of trust or responsibility for the benefit of another, also a trustee can be a person who is allowed to do certain tasks but not able to gain income. Although the strictest sense of the term is the holder of property on behalf of a beneficiary, the more expansive sense encompasses persons who serve, for example, on the Board of Trustees for an institution that operates for the benefit of the general public. Also a person in the local government. A trust can be set up either to benefit</td>
</tr>
</tbody>
</table>
particular persons or for any charitable purposes (but not generally for non-charitable purposes): typical examples are a will trust for the testator’s children and family, a pension trust (to confer benefits on employees and their families) and a charitable trust. In all cases, the trustee may be a person or company, whether or not they are a prospective beneficiary. From Wikipedia website (https://en.wikipedia.org/wiki/Trustee)