

August 1, 2022

Ms. Violaine Clerc
Executive Secretary
Financial Action Task Force (FATF)
2 Rue André Pascal 75116
Paris, France



RE: Revision of Recommendation 25 - White Paper for Public Consultation

Dear Ms. Clerc:

The Institute of International Finance (“IIF”) is grateful for the opportunity to comment on the Financial Action Task Force (“FATF”) consultation on revisions to Recommendation 25 (“R.25”) on the transparency and beneficial ownership (“BO”) of legal arrangements (the “Consultation”)¹. We greatly appreciate the FATF’s iterative outreach on changes in this important area and we very much support its wider work in mitigating and preventing the effects of financial crime globally.

The focus on beneficial ownership information is critical. As we all know, identifying the true beneficial owner or individual exercising control in a business relationship is vital for both the public and the private sectors in the fight against financial crime. Access by competent authorities and financial institutions to reliable and verified beneficial ownership information remains a global priority.

In this regard, we support the FATF’s goal to improve R.25 and its Interpretive Note (“INR.25”) to better meet its stated objective in preventing the misuse of legal arrangements for money laundering or terrorist financing. The FATF has an important opportunity with these revisions to reduce complexity, enhance legal certainty, ensure global consistency and effectiveness in the reporting of beneficial ownership information, and address shortcomings regarding access to that information. This involves instituting standards for mechanisms which establish registries of such data, held by public authorities and accessible to relevant stakeholders, including financial institutions. The content of the registry must be verified by public authorities. Importantly, financial institutions should be able to rely on the information therein.

However, it should be considered that the implementation of new rules and definitions can also lead to extensive administrative issues for financial institutions without concomitant benefits to the goal which is being pursued. Placing additional requirements on the private sector without addressing the role the public sector plays in holding and verifying beneficial ownership information should be obviated.

As such, we reflect herein on important points for access and reporting which would be helpful for standardization at the international level through the FATF and we offer specific input to the questions outlined by the Consultation. Overall, any final changes to R.25 need to be commensurate with the relevant risks being addressed, given the wide range of legal arrangements which exist. We also note that the FATF should further consider conflict of law issues which could arise in the context of jurisdictional implementation of R.25 and INR.25.

Lastly, given the relatively short timeframe for comments on these changes, the final revisions would benefit from a second round of consultation on updated drafts of revisions and further engagement by the FATF with relevant stakeholders. We very much understand the urgency in the need to address opacity

¹ FATF, *Revision of Recommendation 25 - White Paper for Public Consultation*, June 2022

in the beneficial ownership of legal arrangements, especially given the potential for such arrangements to contribute to the circumvention or evasion of financial sanctions in the current geopolitical environment. However, a truncated period of review risks unintended consequences arising during the implementation phase of the changes.

We look forward to engaging with you further as beneficial ownership reform efforts continue at the FATF and around the world and we would be pleased to help facilitate further dialogue with our members on these issues. If you have any questions, please do not hesitate to contact me or Matthew Ekberg (mekberg@iif.com).

Very truly yours,

A handwritten signature in black ink, appearing to read 'Andres Portilla'.

Andres Portilla

Revisions to FATF Recommendation 25 - Responses to the FATF Questions

I. Scope of Legal Arrangements, risk assessment and foreign trusts

Question 1: *Are the following concepts sufficiently clear? If not, how could they be improved? a “governed under their law”, b “administered in the jurisdiction”, c “trustee residing in the jurisdiction”, and d “similar legal arrangements” (as compared with express trust).*

Answer: Question One raises’ issues of legal terminology and potential conflict of law issues dependent on the interpretation of the terms during jurisdictional implementation. We specifically recommend that the FATF consider descriptive terms or explanations of terms which ensure full understanding of the meaning behind the revisions, as discussed further in our answers to subsequent questions.

Question 2. *What could be the pros and cons associated with the new suggested risk assessment? What could be the potential “sufficient links” for foreign-created legal arrangements (e.g., residence of trustee, location of asset etc.) for the purpose of risk assessment?*

Answer: Under the new suggested risk assessment, countries will need to be familiar with the associated risks and evaluate what is happening in their area of responsibility, which will have risk management benefits and could be integrated into national risk assessments. Such a requirement could prove useful; however, it will be important that the assessments were not too onerous and will not lead to an increased administrative burden without clear, useful outcomes.

Nevertheless, in order to fully understand the risk posed by trusts and similar legal arrangements governed under jurisdictional law (or which are administered in jurisdictions or whose trustees are residing in such jurisdictions), it will be essential to first and foremost ensure the requirements are in place in the relevant jurisdictional legislation and associated regulatory guidance, where applicable.

Countries may determine what is considered a sufficient link based on risk. Examples of sufficiency tests may include - but are not limited to - when a trust, on a non-occasional basis, owns a bank account, employs staff, owns real estate, invests in the stock market, or owns commercial/business insurance. It could also include the residence of the settlor and/or trust protector who has the power of terminating a trust or removing a trustee in the interest of the beneficiaries, and not just the residence of the trustees. There is currently not enough emphasis on the settlor under the draft revisions, though the settlor may be the one who accumulated wealth illegally, and not the beneficiaries.

Question 3. *Are there any other considerations with respect to scope of legal arrangements or risks posed by legal arrangements that FATF should factor into its review of R.25?*

Answer: In order to address issues with the Consultation in terms of application of the risk-based approach, we believe that low risk trusts or similar legal arrangements should be excluded from R.25. This should include such entities as institution trusts (e.g., pension plans), publicly traded trusts, and widely held trusts. The focus should be on arrangements that seek to complicate/obfuscate ownership and which do not have an objectively reasonable personal, business, or tax purpose.

II. Obligations of trustees under R.25

Question 4. *What are the pros and cons of expanding the extent of information which trustees should hold to include the objects of power in the context of discretionary trusts? Is the concept of “objects of power” sufficiently clear and reasonable? Are there any other terms that you would recommend FATF use instead of “objects of power”?*

Answer: Question Four raises’ issues of legal terminology and potential conflict of law issues which we noted at the outset of this submission. For example, “objects of power” may already have a legal meaning in certain jurisdictions which could conflict with the intent of the FATF revisions. We specifically recommend that the FATF consider more descriptive terms which ensure full understanding of the meaning behind the revisions. For instance, in the context of purposes of the exclusion, the FATF might consider “individuals who may benefit from the trust property but are neither named nor vested beneficiaries”.

In addition, when addressing the information that trustees should hold, it may be useful for the trustee to keep information on the individuals who may benefit from the trust property but are neither named nor vested beneficiaries, as well as default takers. However, it is important to note that we believe it is still reasonable for financial institutions to limit their customer due diligence (“CDD”) to those beneficiaries who are known, determined, and vested. It is still possible that contingent/undetermined beneficiaries, by the very nature of their interest, receive nothing at all from the trust. As such, we would argue that they are not relevant for the purposes of CDD, nor would we necessarily view them as significant risk factors.

Question 5. *Do you agree with the proposed nexus of such obligations based on residence of trustees or location where the trusts are administered? Compared to the current obligation incumbent on countries that have trusts governed under their law, do you see pros and cons from such a change, (e.g., would there be a difference in terms of efforts to collect the information in cases where a trust may have trustees that are resident in more than one jurisdiction, and where a trust may be administered in a country in which a trustee is not resident)?*

Answer: Question Five raises issues concerning interpretation of control across jurisdictions. In some cases, if the legal residence of the trust (registration location) and the location of the trustee are in different countries, the record keeping duties of the trustee must cover the requirements of both countries. In other circumstances, a jurisdiction should apply measures to the extent that a trust has a trustee resident in that jurisdiction. If the trustees reside outside of the jurisdiction, then measures should apply to the extent that the trustee enters a financial relationship in the name of the trust in that jurisdiction, or the trust acquires real estate in the name of the trust in that jurisdiction. A similar legal arrangement to a trust would have related obligations based on where the controlling party resides.

As such, we believe this question would benefit from further discussion with stakeholders to ensure the interpretation of this change across jurisdictions does not result in conflict between legal regimes or an unnecessary administrative burden in implementation.²

² We also note that all examples concerning types of trusts and other such legal arrangements which are made throughout this letter may differ across jurisdictions and these examples are given to assist in explaining relevant suggestions concerning revisions to R.25 and INR.25.

Question 6. *Do you see challenges in respect of record-keeping obligations for non-professional trustees noting that all other obligations under R.25 apply to such trustees?*

Answer: Due to the risks associated with these types of entities, the non-professional trustees should not be exempt from the record keeping requirements as the attendant risks do not turn on the affiliation of the trustee. Indeed, in most cases, the trustees should have this information and so this revision should not present an onerous burden.

III. Definition of Beneficial Owners

Question 7. *Would you support the insertion of a standalone definition for beneficial owner in the context of legal arrangements (distinct from that for legal persons)? Or would it risk creating confusion with the definition of beneficial owners applicable to legal persons? What relevance should control have in the definition of beneficial ownership of legal arrangement to address AML/CFT risk?*

Answer: A standalone definition for beneficial owners in the context of legal arrangements may be useful to overall risk management efforts in the context of the Consultation. Trusts and other legal arrangements are diverse in nature and manifest themselves in many forms and shapes. An example of this is a self-settled trust where the settlor is also the beneficiary - in which the concept of beneficial ownership is decoupled from control, and therefore there is no risk of confusion in treating the definition of beneficial owners differently from the legal entities. Furthermore, it is quite conceivable that the beneficiaries are intentionally left unaware of their status as a beneficiary of the trust.

Control is very relevant in trusts and other legal arrangements because it can be exercised at different levels and by different stakeholders regardless of ownership. For example, in discretionary trusts, trustees have discretion over the asset distribution to the beneficiaries, but the settlor may revoke trustees and exert ultimate control over the corporate trustee. It is also important that any obligation to understand the control structure and obtain appropriate evidence does not result in new and additional responsibilities such as forcing a financial institution to act as a protector of a trust with all the legal/liability risks attached to that role.

However, we note three caveats to the creation of a standalone definition which the FATF should consider:

First, it is likely that extensive interpretation support will be needed for a standalone definition in terms of explanatory notes or guidance. This could include, *inter alia*, an explanation of areas where treatment of beneficiaries with subsidiary or contingent interests is not clear³, or where clarification is needed on issues which arise regarding the interpretation of the class of beneficiaries.

Second, the new definition should not conflict with long standing legal definitions, which could lead to confusion, misalignment in implementation, and conflict of law issues, as noted in other areas of this submission where the FATF seeks to redefine or create terms. Another way of addressing this issue could be to include in the obligation of the trustee the requirement to hold information on the additional categories of individuals. Control with respect to trusts seems relevant to an AML/CFT risk assessment as an individual with control can direct the disbursement or transfer of property to persons within the authority of the trust deed.

³ However, when considering issues of CDD for contingent interests, please see our answer to question 4 for further clarity.

Third, it should be considered that the implementation of new rules and definitions can lead to an extensive administrative burden for financial institutions. Therefore, any new definition of beneficial ownership in this context should be balanced against those consequences. For example, the definition of the beneficial owner is not only the connecting factor in many financial institution procedures, but also a very important factor for the risk framework of financial institutions. As such, changes to the beneficial owner definition can have further knock-on effects and unintended consequences which should be avoided.

Question 8. *Does limiting the information regarding beneficiaries to only those who have the power to revoke the arrangement or who otherwise have the right to demand or direct (that is, without the consent of the trustee) distribution of assets seem reasonable?*

Answer: We would recommend differentiating between the situation when the trust is the direct customer/client/contractual partner of the financial institution and the situation when a trust is part of the ownership structure of a customer/client/contractual partner. In cases where the trust is the direct customer, all beneficiaries should be regarded as beneficial owners. This would also allow the financial institution to monitor the outgoing payments from the trust's accounts.

In cases where the trust is part of an ownership structure of a customer (*e.g.*, a corporate client), only the person that can exercise the voting rights/control in the name of the trust should be treated as the beneficial owner in the ownership structure (if the trust holds ownership or control above the legal threshold).

Question 9. *Do you have any specific suggestions for a different standalone definition?*

Answer: Please see comments in question 7.

IV. Obstacles to transparency:

Question 10. *What features of legal arrangements do you see being used for obscuring ownership? Are these linked to their involvement in the creation of broader complex structures or inherent to legal arrangements?*

Answer: Obstacles to transparency can take different forms and are often seen in abuse of nominees and trusts structured with the intention of ensuring that property gets to contingent beneficiaries - such as individuals who may benefit from the trust property but are neither named nor vested beneficiaries - as a means of frustrating transparency. Trusts or similar legal arrangements are used in ownership structures due to the fact that there is only very limited public information available on the trusts, their trustees, their beneficiaries, and their founders.

However, we think it is important to clarify that such structural arrangements are not unlawful *per se*, and broad complex structures are not necessarily unique to these arrangements. It is the opacity in the ownership chain with unjustified or anomalous complexity that should trigger additional verification.

Question 11. *What are the legitimate uses of flee/flight clauses? What are the challenges associated with these clauses?*

Answer: We believe that the FATF should consider examples and empirical evidence of the abuse of flee/flight clauses before taking any further action in relation to revisions to R.25. However, we note that in the era of increased cross-border reporting and transparency and changing geopolitical circumstances, a “flee/flight” clause may seem potentially archaic.

Question 12. *What are the key obstacles to transparency of trusts and other legal arrangements?*

Answer: Obstacles are evident when trusts and other legal arrangements appear as an “additional layer in the middle” of a complex corporate arrangement. Legal arrangements are often layered in complex structures registered in offshore jurisdictions as intermediary entities to further obscure beneficial ownership. There are also issues concerning limited official information sources or public information/public records available for such entities, along with a lack of regulation aimed to create transparency for trusts and similar legal arrangements.

When misused, a trust can conceal the sources and uses of funds, as well as the identity of beneficial and legal owners, specifically in cases where it is set up in one jurisdiction and used in another, with the intention to avoid cross-border scrutiny. Customers and account beneficiaries may try to remain anonymous, benefitting from lack of cross border transparency requirements in order to move illicit funds or avoid further examination.

A fundamental issue that exists with a trust or similar arrangements is the lack of consistency necessary concerning forms/terms/documentation and the absence of a registry of interests. It is therefore necessary for fundamental requirements to be raised to protect the financial system. This could be done by expanding the scope of relevant parties involved - *e.g.*, nominee companies and corporate directors – who should come under increased scrutiny and reporting obligations.

V. Approach in collecting beneficial ownership information

Question 13. *Can such an approach ensure that competent authorities have timely access to beneficial ownership information in the context of legal arrangements?*

Answer: Mechanisms such as a public authority or body holding information on the beneficial ownership of trusts or similar legal arrangements, asset registries, or the collection of information by other competent authorities would be important steps forward in increasing transparency around legal arrangement which may conceal beneficial ownership, particularly if the collected information were available to relevant public/private sector stakeholders including financial institutions and was internationally accessible/interoperable.⁴

To further increase transparency, the proposed mechanisms under Section V(i) of this consultation could include additional elements such as ensuring a trust shall be valid only after registration with such a public authority. Similarly, a beneficiary may only be entitled to receive payments out of a trust after registration with the relevant public authority. Actions such as these, coupled with ensuring a mechanism for policing

⁴ Please also see our comments in relation registries and Recommendation 24: IIF, *RE: Revisions to Recommendation 24 - White Paper for Public Consultation*, August 2021.

and sanctioning entities who do not provide accurate and up to date information, would improve the timely access to beneficial ownership information in the context of legal arrangements.

In the absence of a registry, we recommend that an attestation of the accuracy of the information from the trustee should be acceptable in terms of verification. Financial institutions should not be expected to obtain a copy of the trust deed for verification. It should also be sufficient for an obliged entity to obtain its due diligence information from a representative of the trust.

Question 14. *Have you seen any issues/challenges with including information collected by other agents or service providers including trust and company service providers, investment advisors or managers, accountants, or lawyers as a mechanism?*

Answer: As widely reported by transparency investigators⁵, foundations and trusts, company formation agents, law firms and related gatekeepers may in some cases not fulfill a sufficient duty of care concerning limiting the opacity of corporate structures. As in other areas of FATF standards or guidance, it is important that the risk posed by such gatekeeper entities from an AML/CFT perspective is well considered and addressed and we would support further attention to this in the context of revisions to R.25.

Question 15. *Do you think that a multi-pronged approach should be followed for accessing beneficial ownership information of legal arrangements, consistent with Recommendation 24? Or would the features of legal arrangements make a single-pronged approach preferable instead? What are the pros and cons, including in relation to administrative burden, from these approaches?*

Answer: As we stated in our feedback to the revisions of Recommendation 24 (“R.24”)⁶, access to beneficial ownership information should be made available first and foremost to those who have a legitimate purpose for needing this information, such as financial intelligence units (“FIU”), regulatory bodies, law enforcement agencies, and financial institutions. Security of information and genuine data privacy/protection concerns are key considerations which the FATF should take into account when considering amendments to R.25 as well.⁷

However, when considering access to this information, it is important to also consider the aspects of collection of information concerning legal arrangements. If the use of a combination of different mechanisms for collecting beneficial ownership information on legal entities will produce the expected benefits, it is appropriate to extend that to legal arrangements as well and ensure eventual consistency between R.24 and R.25. However, given the complexity and challenges around certain legal entity structures, further guidance around which beneficiaries need to be captured as beneficial owners and when would be useful. In principle, standards around collection and access via a common registry should achieve the desired objectives.

Question 16. *Are there any other mechanisms that FATF should consider as a reliable source of beneficial ownership information for competent authorities?*

⁵ Please see, for example, “The Ownership Monitor” produced by the Università Cattolica del Sacro Cuore and investigations undertaken by the International Consortium of Investigative Journalists, Inc. (“ICIJ”).

⁶ IIF, *RE: Revisions to Recommendation 24 - White Paper for Public Consultation*, August 2021

⁷ Based on this, tiered access for legitimate interest by other stakeholders beyond competent authorities and financial institutions could be considered.

Answer: Competent authorities should perform the cross-checking of beneficial ownership information with other public and private databases in their verification process, especially when identifying persons and entities designated in sanctions lists or when identifying patterns for illicit financial activities. Registries rely on the underlying input data. In this vein, they often cannot be qualitatively more advanced than the data that companies themselves submit to the register. It is therefore often important and desirable to have an independent party that checks and validates the data to improve the data quality. As such, we believe a new structure is needed that supports technical elements that confirm a minimum level of interoperability in order to increase efficiency and data quality to ensure that stakeholders have timely access to adequate, accurate and up-to-date beneficial ownership information.

We would support innovative and stronger cooperation between government agencies and private undertakings that provide and benefit from a breadth of their data management capabilities who can assist in filling gaps that remain in the effective identification of beneficial owners. We believe the overall legal and operational guidance needs to be improved regarding international cooperation and the exchange of data. Countries should rapidly, constructively, and effectively establish international cooperative guidelines for public-private partnerships as well as allowances for private-private data sharing with appropriate data protection safeguards that ensure secrecy in accordance with financial crime compliance standards.

The FATF has already engaged on these topics in its 2017 information sharing guidance and in its 2021/2022 digital transformation workstream, and specific reference to beneficial ownership registries, and the inclusion of information on trusts and other legal arrangements would be beneficial. National registry sharing and access is a very important component for increasing efficiency given the cross-border nature of crime.

VI. Adequate, accurate and up-to-date information

Question 17. *Do you see any concerns with the suggested requirements?*

Answer: The main issues concern the sources of information; however, this can be mitigated by the introduction of a registry of beneficial ownership interests, as noted above. Nevertheless, it is the role of public authorities to ensure high standards are in place which include a regular review of registries to ensure weak spots are mitigated. There should be further work to examine the role of interoperability and international cooperation with and across domestic and regional registries to identify where complex international corporate structures may be shielding criminal activity. Registries must also be sufficiently staffed and resourced to validate the beneficial ownership information provided.

It should be recognized by the FATF that financial institutions have limited means to verify beneficial ownership information and heavily depend on publicly available information (or in some cases restricted information sources). Registries (as sources for information as well as documentation) would help rectify this issue and should be actively policed and backed by the government as a trustworthy source of due diligence material. Lastly, it should be clear that the public sector should stand by the contextual reference data they provide, ensuring it is a source upon which the regulated sector can rely both practically and legally if the integrity of the verification information is appropriate for effective risk management. Financial institutions should not be expected to ensure the quality of information maintained in a registry.

Question 18. *In addition to trustees, who could play a role in the verification of BO information in the context of legal arrangements?*

Answer: We believe adding the protector (if any) for the BO verification would be helpful. Additionally, a designated public authority could hold and verify BO information. (as proposed under Section V (i) of this Consultation).

Question 19. *Can the notion of “independently sourced/obtained documents, data or information” in the definition of accurate information pose any issues for the private sector and, if so, how?*

Answer: In absence of official information available to relevant stakeholders, including financial institutions, it is difficult to assess the data quality and reliability of independently sourced/obtained documents. Currently, the main source of information is a category of persons/organizations (*inter alia*, trustees, lawyers, accountants) which can create a conflict-of-interest situation generated by the fact that their income often is tied to such trusts or similar legal arrangements. To produce sources of information that is indeed independent, new mechanisms as per Section V of the Consultation must be created to ensure “independently sourced/obtained documents, data or information”.

VII. General questions

Question 20. *What are the potential issues/challenges for the private sector regarding implementation of the R.25 requirements?*

Answer: As we have outlined herein, there is too much onus placed on the private sector currently in the context of R.25 and further work should be considered to ensure the public sector adequately collects, verifies, and provides access to underlying beneficial ownership information in legal arrangements. Any final changes to R.25 also need to be commensurate with the relevant risks being addressed, given the wide range of legal arrangements which exist⁸, and we note that the FATF should further consider conflict of law issues which could arise in the context of jurisdictional implementation of R.25 and INR.25. Taken together, this will assist in obviating a situation where the implementation of new rules and definitions leads to an extensive administrative burden for financial institutions without concomitant benefits to the goal which is being pursued.

Question 21. *Do you see any challenges in obtaining information regarding beneficial ownership information of legal arrangements when the trustee (or equivalent) resides in another jurisdiction or when the legal arrangement is administered abroad?*

Answer: Significant challenges can arise in obtaining information regarding beneficial ownership information of legal arrangements when the trustee (or equivalent) resides in another jurisdiction or when the legal arrangement is administered abroad. These include different interpretation of terms in accordance with deviating market practice per country, different standards of publicly available information, and the potential for conflicting data protection laws.⁹

Question 22. *Are there any suggestions to improve R.25 and its Interpretive Note to better meet its stated objective to prevent the misuse of legal arrangements for money laundering or terrorist financing?*

⁸ We highlight the July 2018 FATF/Egmont Group paper on Concealment of Beneficial Ownership in this regard, which noted that trusts are not particularly attractive to criminals - at least not in the same way as a shell company - because they give up legal ownership/control of the assets and involve a trustee who must be involved.

⁹ Please see IIF/Deloitte, *The Effectiveness of Financial Crime Risk Management Reform and Next Steps on a Global Basis*, November 2021 for further discussion on information sharing and data privacy.

Answer: Please see answers to the questions outlined herein regarding revisions to R.25 and INR.25 for suggestions on specific improvements.

Question 23. *What are the areas in particular where the private sector would benefit from guidance regarding implementation of R.25 requirements, including suggested revisions described above?*

Answer: Issues which would benefit from further guidance will largely depend on the final standards; however, we believe that the FATF should consult widely with stakeholders on the ultimate guidance documents concerning R.25. In particular, if the timeframe remains unaltered concerning finalization of the revisions, we anticipate a number of areas may require further clarification to prevent any potential unintended consequences arising in jurisdictional implementation.