

The Wolfsberg AML Principles:

Frequently Asked Questions with Regard to Beneficial Ownership in the Context of Private Banking

Questions sometimes arise with regard to the term “beneficial ownership” as used in the Anti-Money Laundering Principles (AML) for Private Banking (the “Principles”). Some of these questions, as well as answers, are noted below.

Q. 1. What does “beneficial ownership” mean for AML purposes?

A. The term “beneficial ownership,” when used to refer to beneficial ownership of an account in an AML context (such as the Principles), is conventionally understood as equating to ultimate control over funds in such account, whether through ownership or other means. “Control” in this sense is to be distinguished from mere signature authority or legal title.

The term reflects a recognition that a person in whose name an account is opened with a bank is not necessarily the person who ultimately controls such funds. This distinction is important because the focus of AML efforts – and this is fundamental to the Principles – needs to be on the person who has this ultimate level of control. Placing the emphasis on this person is typically a necessary step in determining the source of wealth.

Generally, the process of determining who should be viewed as the beneficial owner does not pose any particular challenges. For example, as noted in the answer to Question 3 below, it is readily apparent that an individual who establishes a personal investment company (“PIC”), transfers his own assets into the company, and is the sole shareholder, should be viewed as the beneficial owner. There may be situations, however, in which determining what “beneficial ownership” is for AML purposes may not be as straightforward as a conceptual matter. To accommodate these situations, beneficial owners should, for money laundering purposes, be broadly conceived of as including the individuals (i) who generally have ultimate control over such funds through ownership or other means and/or (ii) who are the ultimate source of funds for the account and whose source of wealth should be subject to due diligence.¹ An example of the application of this framework to the different roles involved in the creation and management of trusts is discussed below in the answers to Questions 4 to 4C.

What “beneficial ownership” is intended to mean for purposes of the Principles should therefore be seen as dependent on the circumstances of the account involved. The Principles, consequently, do not seek to define the term “beneficial ownership” in the abstract; rather, the focus in the Principles is on identifying persons, in particular circumstances, who should be viewed as having the requisite “beneficial ownership.” Accordingly, Paragraph 1.2.3 of the Principles begins with the general statement that beneficial ownership must be established for all accounts, sets forth general characteristics of beneficial owners (as per (i) and (ii) in the prior paragraph), but then qualifies these general principles by elaborating, in the particular contexts of (i) natural persons, (ii) legal entities, (iii) trusts and (iv) unincorporated associations, what the private banker should seek to understand so that he is in a position to determine the persons who warrant due diligence.

In the context of private banking relationships – which is what the Principles address – it should be noted that in circumstances in which the account holder is not a natural person, the general objective is to establish the identity of the natural person(s) who, ultimately, has the requisite beneficial ownership. In other contexts – e.g. lines of business of the bank in which the clients are operating corporate entities with many shareholders – this objective, of course, would not make sense.

Generally, for purposes of the Principles, it would be inappropriate to equate “beneficial owner” with “beneficiary” or “holder of any beneficial interest.” To define the term “beneficial ownership” in this manner would yield a result that is too inclusive. See Questions 2-5 for a more concrete, practical approach.

These FAQs focus on beneficial ownership of accountholder assets in the typical private banking contexts (e.g. when the accountholder is a PIC or a trust). These situations are to be distinguished from those situations, not addressed in these FAQs, in which the accountholder is (i) a legal entity that is an operating company or (ii) an intermediary (e.g. an investment manager) acting on behalf of its clients. For a more detailed consideration of intermediaries in the context of private banking, see the Wolfsberg Frequently Asked Questions with Regard to Intermediaries and Holders of Powers of Attorney/ Authorised Signers in the Context of Private Banking.

Q. 2. What does the term “beneficial ownership” mean in the context of natural persons?

A. When a natural person seeks to open an account in his/her own name, the private banker should inquire whether such person is acting on his own behalf. If such person responds affirmatively, then, in the ordinary case, it is reasonable to presume that he/she is the beneficial owner.

There are circumstances, however, when this presumption may no longer be reasonable, that is, when “doubt exists” as to whether the apparent account holder is acting on his own behalf. In the client acceptance process, for example, such doubt could arise if there are inconsistencies in the information gathered in the due diligence process. For example, if a prospective client’s explanation as to the sources of his/her wealth does not, on its face, make sense, further due diligence would be appropriate.

Moreover, after the account has been opened, subsequent activity in the account may become inconsistent with the originally anticipated account activity, in which event, it may be reasonable to revisit the initial presumption that the account holder was acting on his/her own behalf. For example, if it is anticipated that the client, after the account is opened, will have occasional transfers of US \$100,000, and there are suddenly frequent transfers substantially in excess of that amount, further due diligence may be warranted, including further inquiry as to beneficial ownership.

Q. 3. What does “beneficial ownership” mean in the context of a legal entity, such as a Personal Investment Company (PIC)?

A. There are situations in which the client (i.e. the accountholder) is a legal entity, but in which it is appropriate, for due diligence purposes, to understand the identity of the beneficial owners of the entity. In the event an individual wishes to hold assets through a PIC, the PIC is the client, and the individual is the beneficial owner of such company and appropriate due diligence would be done, including, for example, ascertaining the ownership and control structure, database checks and inquiring as to the beneficial owner’s source of wealth. If appropriate, the banker should consider verifying the identity of the beneficial owner by reference to official identity papers or other reliable, independent source documents, data, or information.

The case of a PIC is to be distinguished from that of a corporate entity that is a typical operating company with many shareholders, with regard to which it would make no sense to do due diligence on the shareholders. Indeed, this type of entity would not ordinarily have a relationship with a private bank because such a client is institutional or commercial in nature and would presumably have relationships with other business units of the bank.

There may be situations where there is more than one beneficial owner. For instance, a successful entrepreneur may organise a private holding company in which he and his spouse are the shareholders, but in which he is the provider of funds. In this situation, due diligence as

to the source of funds and wealth should be done on him, not his spouse. It may, however, be appropriate to engage in some due diligence with respect to the spouse's background and reputation.

It is appropriate for the private banker to develop an understanding of the company's structure. In the event, for example, there are shareholders owning a substantial amount of shares who are not related to the apparent provider of funds, the private banker should seek to understand why this is so. Similarly, if there are individuals who are in a position to exert control over the funds held by the company (e.g. directors or persons with power to give direction to the directors) and such individuals are not related to the apparent provider of funds, the private banker should consider why this might be so. In these types of situations, this further inquiry may disclose that the apparent provider of funds is not to be viewed as the beneficial owner with respect to such funds. If so, the focus of due diligence should be redirected to the beneficial owner, or indeed, the propriety of opening an account at all may be called into question.

Q. 3A. What implications, if any, are there if corporate entities are not legally required to disclose, as a matter of public record or otherwise, who their ultimate beneficial owners are?

A. There may be situations in which applicable law does not require corporations to disclose publicly (e.g. in a registry) or otherwise who their beneficial owners are. If such a corporate entity were a potential client of the private bank, such law, however, would not preclude, as a matter of AML due diligence, an understanding of the beneficial ownership of the company. The private banker should conduct the appropriate due diligence with respect to the principal beneficial owners, regardless of the disclosure laws applicable to the company.

Q. 3B. What implications, if any, are there, for due diligence purposes, if shares of a PIC are held in bearer form?

A. The fact that shares of a PIC are in bearer form does not preclude the usual due diligence standards with respect to the beneficial owner of assets held within the PIC. The initial inquiry should be to identify the beneficial owner of the assets held within the PIC (regardless of whether the shares are held in bearer form). In addition, given that in the case of bearer shares the ownership interest may be readily transferred, a bank should take measures to prevent the misuse of bearer shares by applying, for example, one or more of the following mechanisms: (i) certification as to beneficial ownership at the outset of the relationship and when there are changes in beneficial ownership structure; (ii) immobilisation of the shares by requiring them to be held by an appropriate party; (iii) conversion of such shares to registered shares; or (iv) prohibiting bearer shares.

Q. 4. What does "beneficial ownership" mean in the context of trusts?

A. In the typical case, it would be clear which person has "beneficial ownership" for the purposes of the Principles. For instance, in the case of an industrialist who establishes a trust for the benefit of his wife or minor children, the "beneficial owner" would be the industrialist settlor, namely, the "provider of funds," as contemplated by Paragraph 1.2.3 of the Principles. The appropriate due diligence should be conducted with regard to the industrialist, including background checks and the requisite inquiry as to the source of wealth. If appropriate, the banker should consider identifying the beneficial owner by reference to official identity papers.

Even though the wife and children have a beneficial interest in the trust for trust law purposes (indeed for such purposes they might appropriately be referred to as "beneficial owners"), they should not be treated as "beneficial owners" for AML purposes. That is, it would not make sense to conduct due diligence with respect to the wife's or children's source of wealth, although it may be appropriate to do some due diligence with respect to their background and reputation.

This result, incidentally, highlights the consequences of a typical feature of trusts, the separation of legal title and beneficial interest. The person having legal title, i.e. the trustee, typically has control with respect to the assets; however, the parties to the arrangement who have beneficial interests, i.e. the beneficiaries, would typically not have control. As the prior example illustrates, it is yet a third party, the settlor, as the provider of funds (who may neither have control, nor a beneficial interest in the assets of the trust) who should, from an AML point of view, be the object of due diligence. Control in these circumstances is not the determinative criterion for AML purposes, nor is beneficial interest.

The fact that the settlor is deceased does not preclude the need for due diligence with respect to his/her reputation and source of wealth. In this regard, it is presumptively reasonable to look to the trustee for information regarding the source of wealth, assuming the trustee is reputable.

Q. 4A. Why is it appropriate for the private banker to understand who has control over the funds held in the trust structure or who has the power to remove the trustee, even if the person having such control or power is not the source of funds?

A. If there is a person who has this level of control or power, it is appropriate for the private banker to seek an explanation for this arrangement and to undertake further inquiry, if, on its face, the arrangements are not plausible.

Moreover, a person who has this level of control or power may present reputational risk to the bank, even if the ultimate explanation for the arrangement is plausible and due diligence as to such person's reputation is warranted, if such person is not already known by the bank to be reputable.

Q. 4B. Why is it appropriate for the private banker to determine the persons for whose benefit the trust is established?

A. The private banker should consider for whose benefit the trust is established in order to determine whether more inquiry would be appropriate. As noted in the answer to Question 4, in the typical case, in which the beneficiaries are, for example, members of the settlor's family, applying the same level of inquiry to the beneficiaries that would be applied to the settlor would not be warranted. This would not ordinarily be a situation posing money laundering or terrorist financing risk. If, however, the private banker determines that a beneficiary exercises control over the arrangement, the beneficiary should be treated as a beneficial owner for AML purposes, i.e. as a person subject to due diligence. Furthermore, if the private banker, in his consideration of the circumstances, determines that the arrangement is unusual (e.g. the beneficiaries' relationship to the settlor is atypical), the private banker should conduct further inquiry.

Q. 4C. What should the private banker review in seeking to understand the structure of the trust sufficiently for purposes of 1.2.3?

A. The private banker may rely on declarations or attestations given by the trustee as to the "provider of funds, those who have control over the funds (e.g. trustees) and any persons who have the power to remove the trustees" as well as persons for whose benefit the trust is established, if the trustee is an institution or individual who is well-known to the private banker. If the private banker is not familiar with the institution or individual, then the private banker should undertake due diligence with respect to such institution or individual with a view to establishing a basis for reasonably accepting such declaration or attestation. It is not necessary for the private banker to obtain a copy of the trust instrument. In atypical circumstances, the private banker may determine to engage in further inquiry.

Q. 5. What does beneficial ownership mean in the context of partnerships, foundations and unincorporated associations?

A. Establishing beneficial ownership in these contexts generally entails the same principles as discussed above.

Partnerships: Partnerships are comprised of partners (sometimes referred to as general or equity partners) and sometimes include limited partners. Ordinarily, the principal general or equity partners would be considered to be the "beneficial owners" for purposes of Paragraph

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1.2.3. In the event the partnership includes limited partners, there may be circumstances in which a limited partner could be considered to be a “beneficial owner.”

Foundations: In some jurisdictions, “foundations” may be used by clients as investment or wealth planning vehicles, much as private holding companies are used for such purposes in other jurisdictions. Foundations, however, are not “owned” by particular individuals. The private bankers should understand who the founder (typically, the client) is. The private banker should do so even if the identity of the founder (i.e. the source of funds) is not discernible from the public record.

Unincorporated Associations: If such organisations are used by clients, the private banker should understand the structure of the association (which may not be “owned” by particular individuals) and identify who provides the association with its funds and subject such person to appropriate due diligence.

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