# Beneficial Ownership Monitoring

The Challenges and Practicalities

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# Contents

An Ultimate Beneficial Owner (UBO) is defined as 'The natural person(s) who ultimately gains from, owns or controls a legal entity'. A beneficial owner can either be a direct shareholder of a given company, or have an equity holding in another entity that has ownership in the given company.

**Understanding UBOs is** a fundamental regulatory requirement in EU Money Laundering Directives, which forms part of a risk-based approach to Anti-Money Laundering (AML), Know Your Customer (KYC) and Customer Due Diligence (CDD) efforts. It is backed by G20 initiatives to build transparency, good corporate governance and ultimately trust in organisations that sit within regulated industries.

**Establishing UBOs ensures** brand reputation is maintained through screening for unlawful behaviour such as bribery, corruption, sanctions, politically exposed persons (PEPs), litigation and adverse media.

**Understanding and verifying** Ultimate Beneficial Owners (UBOs) is a challenge due to multiple metrics, missing links and conflicting information. Now that it's a regulatory recommendation to monitor UBO information for any changes, this is an additional effort for compliance teams.

**In this whitepaper,** we explore how to overcome the challenges of UBO verification and monitoring, including:

- Approaches for consistent calculation of ownership and control
- Summarising the complexities of monitoring
- How technology can help organisations to embrace monitoring and assess the impact of changes

## Beneficial Ownership: The Background

**As has been** the case for some years now, the European Union has led the way from a regulatory perspective, specifically regarding beneficial ownership. Member States are making registers of Ultimate Beneficial Owners (UBOs) of companies and other legal entities more accessible and transparent to the general public; going beyond the regulatory requirement to demonstrate legitimate interest.

**Perhaps most significantly** for operational leaders and compliance teams, The EU Commission has been tasked to connect the various registers at EU level by 10th March, 2021, to provide a consistent and transparent pool of information on UBOs across the region.

**The theory is** that information provided should comprise, as a minimum: the beneficial owner's month and year of birth, country of residence, nationality, and the nature and extent of the beneficial interest held.

**Of course, as** with all directives, each member state has, or will, implement directives in the way that best suits their unique frameworks and political needs – ultimately adopting different approaches with broadly the same set of criteria. Whether countries will support transparency of disclosure to meet the widening needs in understanding ownership and control during the onboarding cycle, and ongoing client engagements, remains to be seen.

**With lack of** consistency in the registration approach across EU countries, differing levels of data and complex regulatory changes – juxtaposed with the chains of command of companies becoming more diluted – how do compliance professionals tackle the establishment of beneficial ownership and control?

| 25 june 2015 | 26 june 2017 | 9 july 2018 | 10 jan 2020 | 10 mar 2021 |
|---|---|---|---|---|
| Fourth AML Directive | Fourth AML Directive Implemented by Member States | Fifth AML Directive | Fifth AML Directive Implemented by Member States | Interconnection of "UBO" registers at EU Level |

## The challenges of establishing ultimate beneficial owners

**There is a** shift towards multiple metrics of beneficial ownership and control. This can mean that, instead of following one path, businesses may need to investigate multiple paths – for example, one for voting rights, one for traditional ownership, one for influence and control. This can lead to many more people being identified as beneficial owners.

**When beneficial ownership** is discussed, simple examples with full information are often used to show linkages and business relationships between companies. However, these usually show just a handful of levels and provide examples of how dilution of holdings is calculated. Often the reality is much different. Some of the common challenges are described here.

## Ownership going overseas

**This is probably** by far the most common issue. The UK may have good disclosure but this is rarely matched in jurisdictions abroad, and there is also likely to be many instances where the entity in question is not UK-based. For many institutions, having an international client base poses the most challenges as contact with officers and owners is often more difficult to achieve, so beneficial owners can be many layers removed from the starting entity in question.

**Companies House covers** around four million limited companies in the UK and quotes around 95% accuracy on UK Persons of Significant Control (PSC) data. That still leaves 200,000 entities where there are questions, or data is incomplete. With some 50 million businesses in Europe and a further 55 million active business covering the rest of the globe, the UK PSC is just a fraction of the challenge.

## Loss of granularity in ownership

**There are many** jurisdictions in which ownership can be established from available data, but it's not necessarily possible to obtain a precise percentage of ownership. Some ownership links may be undisclosed or simply state that they are majority owned.

**This can cause** problems in trying to establish the correct diluted percentage

### Ownership going overseas
- Opaque jurisdictions
- Tax havens

### Loss of granularity of ownership percentage
- Undisclosed percentages
- Only required to state majority owners

### A range of ownership rather than specific percentage
- PSC register approach

### Conflicting information
- Timing of filings
- Differing views of controlling party

figure all the way through the chain of ownership nodes. This can be an issue in the United States, where SEC (Security and Exchange Commission) filings only mandate disclosure of significant subsidiaries, and don't necessarily disclose the actual percentage.

## Range of ownership

**In the UK,** the PSC register is a valuable resource, yet it only provides defined ranges of ownership, such as 25–50%, 50–75% and 75–100%, whereas the Confirmation Statement gives an actual percentage. Using the PSC information can make it difficult to calculate the diluted percentage, especially where multiple relevant legal entities are filed, rather than natural persons.

## Conflicting information

**Where ownership structures** span the globe, we often see discrepancies in information. This can be due to some registers requiring information that skips some levels, like the PSC register, or where jurisdictions have differing requirements. There are differing combinations of asking for or sharing information on the legal, or immediate owner and the beneficial owner. If a natural person in China is seven layers removed from a UK business and makes some changes in his ownership interests, will they really consider their obligations as a UK PSC? Alternatively, companies may state their ultimate owner in an Annual Return, which could differ from the PSC, which in turn could differ from confirmation statements, depending on the timing.

**As a precursor** to monitoring it is important to systematically establish the end state for comparison. So what methods or techniques can we employ to help with this?

## 'Spidering'

This involves starting with an input company and following every single link to the end, then returning the entire structure.

By splitting the spidering of the network from the algorithm to calculate the metric, different views or calculations can be applied. This can be done quickly on the same data-set returned, as spidering is not conditional.

Graph database technology has matured so that high volumes of data can be processed and returned quickly – in a matter of seconds.

## Algorithms

A flexible suite of algorithms is available depending on the use case. One example is to apply a worst-case scenario algorithm, others may involve using control metrics as well. This method usually provides a reasonable amount of detail, but may leave some areas without a specific percentage, and hence can't carry a true calculation through to the end. This means the beneficiaries or owners can be identified but there is a lack of information on the precise quantity of their holding.

In a worst-case scenario approach, it is possible to proxy in remaining percentage amounts to at least give some indication on whether owners should be considered or not. If all the owners and their inferred percentages are totalled up, a calculation could produce over 100%. However, this approach can lead to a vast reduction in the number of beneficial owners that meet a threshold; in most cases there is likely to be a tenfold reduction in nodes even when considering the worst-case scenario.

## Ultimate beneficial ownership monitoring

**Understanding and verifying** UBOs is difficult but there are ways to overcome this, as we have just explored. Monitoring UBO information for change within an appropriate time frame is also imperative – due to regulatory expectations – to mitigate risk and improve transparency.

**However, figuring out** how to monitor and maintain up to date UBO information, without sacrificing efficiency and inviting increased operational pain is a real challenge. Monitoring is often done as part of a risk-based approach, through periodic reviews, when organisations start from scratch each year

**It is normally** the case that a periodic review leads to key information, and sometimes significant levels of change being updated on the client and the counterparties in three main areas.

- Firmographic changes (addresses names etc.)
- Principals information
- Ownership

### Why review the ultimate beneficial ownership of third parties?

- The Fifth Money Laundering Directive (5AML) set the expectation for monitoring and keeping UBO information up to date
- Ownership structures are complex and change often happens in multiple layers
- Percentage changes might go over or under the risk threshold set in the organisation's policy
- Entities in the structure might change to be registered in countries deemed a higher risk
- Keep the most up to date view of owners for third parties

**The ability to** consume 'Master Data Management' style updates on records for firmographic data and principals associated with clients has been available for many years. Large quantities of data can be supplied quickly and easily, instantly updating records and offering the chance to build rules sets around the materiality or otherwise against this change.

**The direction of** travel is clear. More and more, the onus is on organisations to automate. This is for several clear reasons:

- The need to continually scale; manual reviews are hard to scale without investment in people, which are a costly resource that needs continuously upskilling
- Growing amount of information available
- An increasing number of requirements added to the 'check and validate' list; as this happens, it becomes increasingly harder to keep up to date and to deliver service levels expected by customers both internally and externally

## Moving to systematic monitoring

**Many organisations are** now looking seriously at how they can systemise the monitoring aspects of ongoing customer and third-party due diligence, moving from periodic review to continuous assessment. There are potential benefits to doing so, including a saving of time and a level of consistency not provided by manual reviews, particularly when driving automation and rules to resolve hidden complexities.

> With continual assessment, a much faster understanding of real risk with each client or counterparty can be achieved, ultimately leading to quicker time to realising additional revenue potential with the client.

**Although automation offers** a potential reduction in overall cost, there is still a need and value in some level of human intervention. With continual assessment, a much faster understanding of real risk with each client or counterparty can be achieved, ultimately leading to quicker time to realising additional revenue potential with the client.

**However, the realisation** of monitoring and continual assessment on true ownership – legal or beneficial or control – has not been so simple to execute.

**Dun & Bradstreet** believe ownership should be treated like any other assessment criteria and needs to be seen in the framework of three simple questions:

1. **How can we establish if there has actually been a change?**
   Without a baseline or end state, understanding real change is problematic. If an end state is established, it can then be compared to that same calculation day-to-day, or month-on-month, and see if they appear the same. There are certain areas that seem obvious when viewed with a human's eyes, but small details can be problematic when considering a machine's view.

   As an example, another entity could simply be inserted into a group structure, but with the end shareholders being the same. If shareholders are recorded in a different order, it could create a "noise" change – a change in the strictest sense, but not actually a change in a material sense.

   Depending on regulatory drivers, industry differences and the organisation's risk appetite, teams may also want to consider what to do if there is a change in the path of ownership from legal to beneficiary, but the end people don't change. It's vital that there is standardisation, a comparison of apples with apples and that 'real' changes are identified. Teams could also choose to filter out anything that is not a beneficiary, if that suits their risk appetite.

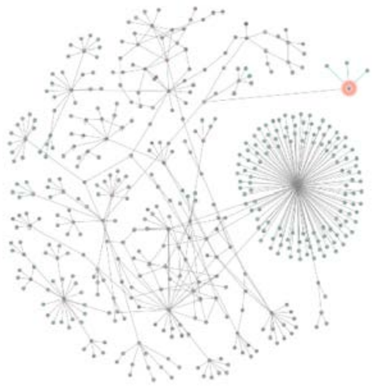
   In the ownership context, organisations should consider how they want to represent UBOs and be clear whether change in route, but not a change in persons, is important to their organisation.

2. **How do we establish what that change was?**
   Most systems that are implemented to detect change rely on a unique key for each record, then simply check each attribute associated from old to new – effectively, looking at subset of data that is tied together in a row, then comparing that same row in the same way every time will identify change.

   However, a different approach is needed for beneficial ownership as attributes that are not part of a standard row of data, but are connected through relationships, also need to be checked. For example, a person is unlikely to change their name or Date of Birth, but they could change their percentage holding in a business. In this case, the beneficial owner has not changed, but their attributes have. In reality, the most likely scenario is that a beneficial owner is either added or removed.

   By its nature, ownership is an elastic data structure, and changes in just one single node can have a large knock-on effect. Whatever mechanism an organisation uses to detect changes needs to be able to compare old vs new and accommodate potentially big differences created downstream from one event.

3. **Does the established change have an impact to the compliance professionals, the customer, the policy or the organisation?**
A single change within a connected ownership structure can have different effects depending on the starting point. So, the actual change requires context.



A change at the highlighted node will have a different impact in relation to all the other nodes in the graph. So, propagating the change and its impact requires a high capacity tech stack to calculate all the individual changes and the downstream variations.

To process and make sense of these changes, compliance teams need to set up some rules – the most obvious being a threshold check. This would monitor for instances whereby there have been no additions or deletions of beneficial owners, but a percentage attribute change.
If new beneficial owners have been identified, teams should understand if they go over a threshold and move to the next step – screening.

There could be instances whereby many beneficiaries are identified, even with a worst-case scenario, if we have a large customer or supplier base. Different clients may choose to apply different rules in terms of impact dependent on their use case. For example, a financial services business may want to send all new owners for screening. An industrial company assessing suppliers may choose to apply some more pragmatic measures, such as averaging out unknown ownership or deciding that, if there are potentially hundreds of beneficiaries, that it's unlikely that anyone has total control.

Any professionals that have been involved with screening for sanctions, PEPs and adverse media will know that the task of evaluating false positives can be very onerous, so being as tight as possible will reduce downstream effort. Therefore, applying thresholds and rules, and deciding on a risk appetite, will determine what goes forward to the next stage.
If no screening hits are received during screening, then the assessment of a UBO change could be fully automatic. For cases where hits have been encountered, once any necessary manual false positive reviews are completed, a true picture of the impact of the change can be seen. Naturally, the converse should be applied for owners that have been removed, it could well be that this has a positive impact on risk if these people had associated screening hits.

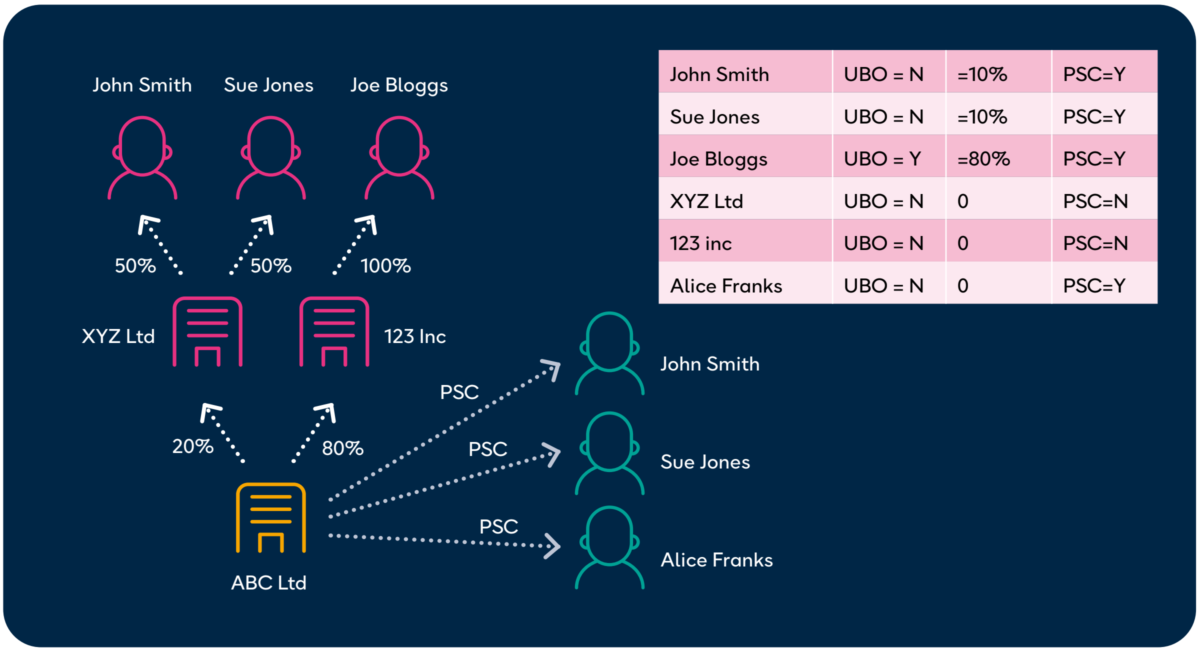
With an increase in data points comes more choices on the rules that can be applied – for example, one risk-based approach may choose to stop at a listed business on a recognised exchange. Some organisations may attach increased significance on state owned entities, others may want to apply some factors such as Transparency International's Corruption Perceptions Index to the jurisdiction. There are many additional attributes that can be attached to the nodes to help in deciding if they are relevant, then what level of risk they may pose; and whether they should be screened or not.

Finally, teams can assess if the results of all these combined rules actually change the internal risk level assigned to the entity in question.

## Covering Different Metrics

**Up to now,** we have very much concentrated on beneficial ownership, but there is an increased focus on other reviews and metrics, including who influences or has control over a business. In addition to calculating actual ownership percentages, compliance teams also need to consider what the future will bring in terms of other views of control.

**Since the UK** is one of the first to create such a register (Companies House PSC data) some additional PSC links are shown below:




| | | | |
|---|---|---|---|
| John Smith | UBO = N | =10% | PSC=Y |
| Sue Jones | UBO = N | =10% | PSC=Y |
| Joe Bloggs | UBO = Y | =80% | PSC=Y |
| XYZ Ltd | UBO = N | 0 | PSC=N |
| 123 inc | UBO = N | 0 | PSC=N |
| Alice Franks | UBO = N | 0 | PSC=Y |

**These could include** existing known people, by nature of ownership, but can include additional individuals, in this case Alice Franks, who has no ownership at all, but can exercise control over the business.

**Therefore, in terms** of future proofing it would be advisable to anticipate having to store these kinds of attributes or data, so that these can also be taken into consideration for monitoring.

## Conclusion

1. **Look to future proof your approach and systems to handle future control requirements as well as ownership**

2. **Have a systematic and consistent approach to calculation of ownership and control**

3. **Understand the complexities of monitoring and the elastic nature of the data and changes**

4. **Embrace emerging technologies to automate and provide the capabilities to assess the impact**

## How Dun & Bradstreet can help

**Reduce the operational** pain associated with reviewing ownership of third parties.

**UBO Monitoring from** Dun & Bradstreet allows you to monitor your entire network in near real-time. From a single starting entity, you will be able to monitor ownership calculations all the way up to UBO, through all nodes and regardless of where organisations sit geographically.

**Receive automatic alerts** when there are shifts in the UBO structures of your customers, suppliers and other third parties. Take control and be proactive in your management of change.

- Monitoring information is updated daily
- Change history helps you to understand the current and previous data position on all owners over the last 12 months
- Receive information on direct, indirect and informational changes (e.g. % change)
- Understand when owners are removed or added to the structure
- Option to receive alerts via API into your current workflow

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