

What is an Ultimate Beneficial Owner? An Investigation on Actual Literature

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Abstract

The purpose of the article is to describe an aspect that has appeared frequently in recent years, in the banking financial field: Ultimate Beneficial Owner (UBO). The concept or phenomenon is important for developing a safety and trustful business environment on one hand, and for minimizing the banking risks, money laundering and terrorism finance. “There is an industry-wide expectation for banks and corporations to know the individuals they do business with. Any institution within the scope of Anti-Money Laundering and Anti-Terrorist Financing regulations needs to disclose the UBO’s identity for any of their business transactions” (according to the Society for Worldwide Interbank Financial Telecommunication, SWIFT). Through the research undertaken on the specialized literature (precarious in this field) only vague, not current, and exhaustive attempts to investigate the UBO phenomenon were identified. In addition, the legal framework has been studied. Finally, there is presented the way banks identify UBOs.

Keywords: Ultimate Beneficial Owner (UBO), banking risks, risk mitigation, money laundering, anti-terrorist financing regulations

INTRODUCTION

The purpose of the article is to describe an aspect that has appeared frequently in recent years, in the banking financial field: Ultimate Beneficial Owner (UBO). The concept or phenomenon is important for developing a safety and trustful business environment on one hand, and for minimizing the banking risks, money laundering and terrorism finance (Koster, 2020); Crama et al., 2021). According to the Society for Worldwide Interbank Financial Telecommunication, SWIFT, “there is an industry-wide expectation for banks and corporations to know the individuals they do business with. Any institution

within the scope of Anti-Money Laundering and Anti-Terrorist Financing regulations needs to disclose the UBO's identity for any of their business transactions" (Swift, 2024).

Furthermore, regulators' major concerns in recent years have been the stopping of terrorists funding and money laundering. Investigators sometimes link suspicious transactions to fictitious addresses, PO boxes, or the private residences of unwary citizens. Some dishonest actors may conceal their activities using offshore accounts. The individual who is the ultimate beneficiary when an institution starts a transaction is known as the UBO. Although the exact definition of a UBO varies from country of jurisdiction, in general, a UBO is someone who owns at least 10% to 25% (depending on the jurisdiction) of the capital or voting rights in an organization (Swift, 2024).

Through the research undertaken on the specialized literature (precarious in this field) only vague, not current, and exhaustive attempts to investigate the UBO phenomenon were identified. In addition, the legal framework has been studied. Finally, there is presented (as a case study) the way banks identify UBOs.

AN OVERVIEW OF THE CONCEPT DEFINITION

General considerations

When it comes to UBO, the most common meaning refers to the natural person who is ultimately responsible for, owns or controls a 'customer'. In most cases, this 'customer' is an institution, business, or legal entity: of which the UBO has 100% direct ownership. They are the Ultimate Beneficial Owner or ultimate interested party on whose behalf a transaction is carried out. It also includes a person who has ultimate effective control over another person or an arrangement (LexisNexis, n. d.).

This UBO definition is according to the Financial Action Task Force (FATF, 2024). The regulatory body is responsible for fighting criminal activities such as terrorist financing and money laundering schemes. However, there is no global standard for how the UBO definition is applied across different regions around the world. Another complex factor is that UBOs can be transitive, and they may not stay in one location for an extended period. Because ultimate beneficial ownership regulations are constantly evolving, it is often challenging to uncover the identity of a UBO (LexisNexis, 2024).

The concept of "Beneficial Ownership" was first developed in the 1933 United States Securities Act in relation to the ownership of securities (such as shares in a company) (Voynarenko et al., 2020; KycHub, 2024a). This concept was then adopted by several national and international laws and is now applied not only to the ownership of securities but to the ownership of all sorts of other goods whose ownership is subject to registration in legal records (for instance, real properties and vessels). As the name suggests, an Ultimate Beneficial Owner (UBO) refers to the individual or entity that ultimately benefits from the ownership of a business or organization (Théaud, 2023).

UBO could be a single individual or a group of individuals, depending on the ownership structure of the company. They may have a direct or indirect interest in the company, such as through a trust or a nominee arrangement.

According to the Money Laundering Act (Geldwäschegesetz – GwG, 2024), a beneficial owner is a person who:

- Owns more than 25% of the company's equity (shares);
- Has more than 25% of the voting rights and can exercise, directly or indirectly, such voting rights at the general meeting of shareholders of the legal entity;
- Or who can similarly exercise significant control over the company.

On this point, it is worth mentioning that banking practice goes beyond legal and regulatory requirements here. When identifying UBOs, banks will indeed retain a 10% threshold as opposed to the 25% one provided by the regulations (Théaud, 2023).

UBO laws and regulations

Various laws and UBO regulations govern the identification and reporting of UBOs in a transparent way (Konovalova et al., 2023). Companies are required to report information about their ultimate beneficial owners to relevant authorities, including financial institutions and government agencies, under UBO legislation. This act is intended to increase the transparency of firm ownership arrangements and prevent financial crimes, including money laundering and terrorism. Various nations have their own UBO laws, but in general, they require firms to identify and disclose the individuals or entities who ultimately own or control them. This can include information such as the UBO's name, address, and ownership percentage. In many instances, UBO information must be provided to a central register or database that may be viewed by the appropriate authorities. As part of their anti-money laundering (AML) and know-your-customer (KYC) responsibilities, financial institutions like banks are obligated to collect UBO information from their customers (Théaud, 2023).

UBO identification

It is very important to correctly identify the Ultimate Beneficial Ownership. Identifying the Ultimate Beneficial Owner (UBO) of a company can be quite a puzzle, especially in organizations with intricate structures. A structured approach can be as follow:

- Gather Company Credentials: Start by collecting essential information about the company, such as its registration number, address, and key management personnel.
- Research Ownership Chain: Investigate who holds shares or interests in the company, and whether this ownership is direct or indirect.

Identify and Verify the UBO(s) means to determine the individuals who ultimately have a significant share or control over the company. This might involve looking beyond the immediate shareholders to those indirectly influencing the company. Conduct AML and KYC Checks: All identified UBOs must undergo Anti-Money Laundering (AML) and Know Your Customer (KYC) checks to ensure compliance and legitimacy. In every case, identifying the UBO is more than a regulatory formality – it's a critical step for ensuring transparency and integrity in business dealings (Théaud, 2023).

THE ROLE OF TECHNOLOGY IN SIMPLIFYING UBO COMPLIANCE

Because it is quite difficult to discover UBO the use of Artificial Intelligence (AI) and regulatory technology can simplify the research of UBO. AI and other technologies can improve the accuracy and reliability of UBO identification and can transform the manual process into an automated one. The FATF (2024) plays a major role in establishing the regulatory environment for UBO compliance as the

worldwide standard setter for AML and CTF procedures. To ensure that its member nations adopt efficient measures to fight financial crimes, the FATF routinely evaluates and updates its recommendations to meet growing risks and difficulties in the financial sector (KycHub, 2024b).

The following is the role of technology in simplifying UBO Compliance (KycHub, 2024c):

- Automated Data Collection and Analysis: advancements in technology, such as artificial intelligence (AI) and machine learning, can streamline the UBO identification process by automating data collection and analysis. AI-powered tools can rapidly scan and analyze vast amounts of data from multiple sources, such as public registers and commercial databases, to identify UBOs and assess potential risks;
- Enhanced Verification Processes: technology can also enhance the UBO verification process by enabling financial institutions to access a wider range of data sources and cross-reference information more effectively. For example, blockchain technology can provide a secure and transparent platform for sharing beneficial ownership information, reducing the reliance on customer-provided data and improving the accuracy of UBO verification;
- Ongoing Monitoring and Risk Assessment: sophisticated technology solutions can help financial institutions monitor changes in beneficial ownership and continuously assess potential risks. By automating the monitoring process, banks can more efficiently detect and respond to changes in their customers' ownership structures, ensuring that their UBO records remain up-to-date and accurate.

CASE STUDY – DESCRIPTION OF THE UBO APPROACH IN PRACTICAL BANKING

The theory and the legislations define UBO as a person who owns at least 10-25% (depending on the jurisdiction) of the capital or voting rights in an entity. In theory, it is not specified which legal documents can be analyzed in such a way as to result in UBO. In practice, the method of identifying UBO is different from one bank to another. For some banks it is sufficient to consult the register of the real beneficiary, for others a statement from the analyzed company, but for many banks the UBO analysis must be documented.

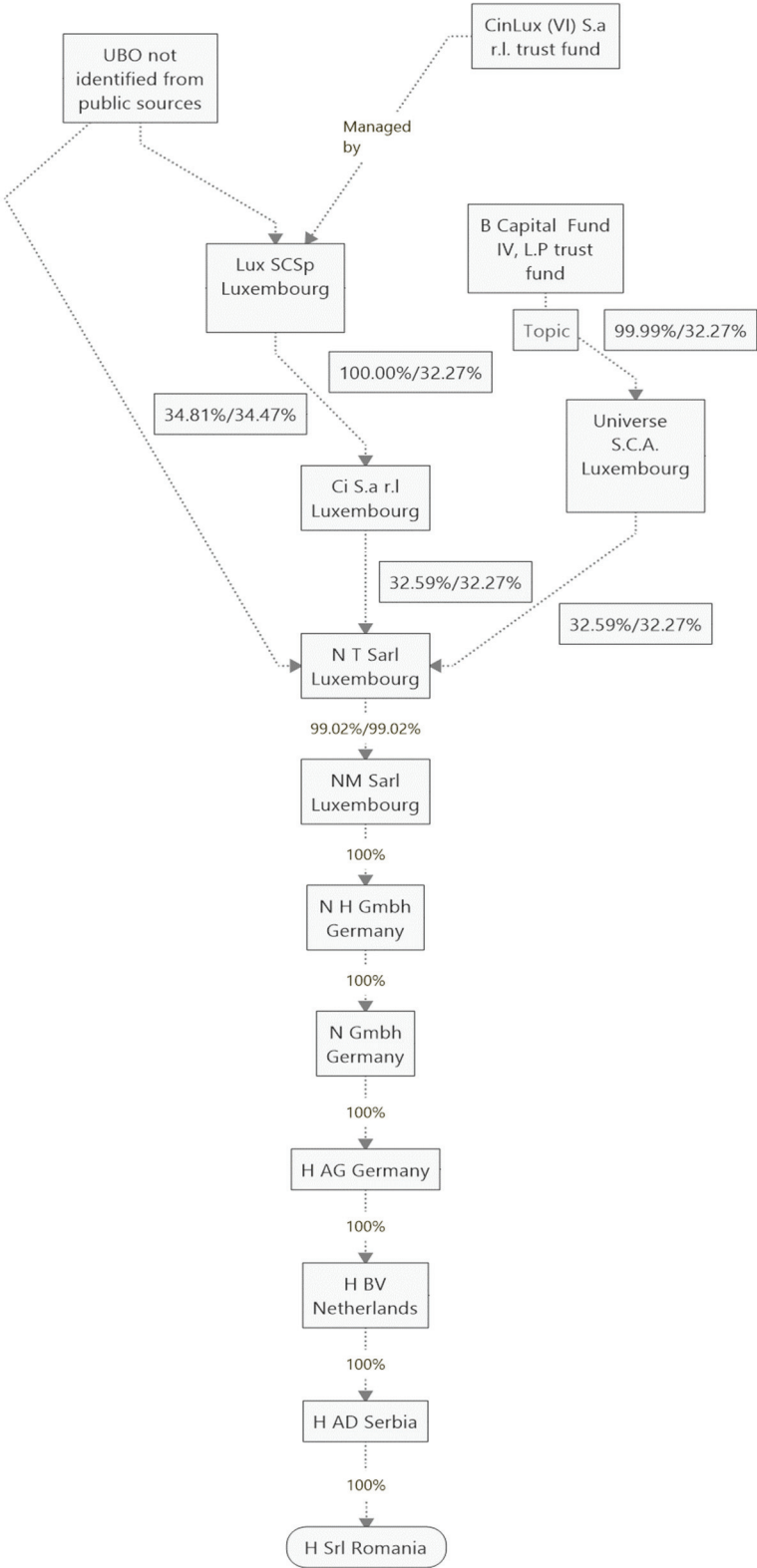
The documents, from case to case, can be:

- Legal documents on the UBO chain up to the last holding,
- Company's extract from the country of residence,
- Audit reports,
- Legalized declarations from third parties (notaries, lawyers) who, following the analysis of all legal documents, identified UBO without limiting themselves to these.

In our case study, the bank wants to identify the UBO for the company H SRL Romania. As we can see in figure 1, our company is ultimately owned by two funds: CinLux (VI) S.a r.l. trust fund and B Capital Fund IV, L.P. trust fund. We do not have the entire set of legal documents for the entire chain, we cannot obtain all the extracts from the countries of origin, nor can the UBO register be consulted many times. In most cases, banks encounter problems such as: unauthorized external access to the UBO register, consultation for a fee of the register or the extracts, insufficient documents published on the official

websites of the countries in which they operate, publication information with the character of confidentiality for third parties, the lack of audit reports. The biggest problem here is the client's refusal to provide documents (the bureaucracy).

Picture 1: Ownership chain



In our case, because the ownership is a complex one, and the company is part of a multinational group, we identify the UBO from the last audit report of the parent company, N H Gmbh Germany. The audit was drawn up and published to third parties by a big consultancy company. In the report it is mentioned, at one point, that although big part of the assets was transferred to be administered by the two funds, all decisions and control remain the responsibility of the Executive Board of the N H Gmbh Germany. After the detailed analysis of the audit report, we came to the conclusion that UBO can be identified, in that case, only on the control criterion - CEO, CFO, COO. The conclusion was also strengthened by the transparency register that we finally obtained, those three being declared real beneficiaries. Finally, after 6 months of continuous work, the company's legal file was validated by KYC Aml.

Because the time needed to do the analysis was very long, if the AI and regulatory technology were to function globally, UBO could be identified and documented more easily, down to minutes.

CONCLUSION

Identifying and verifying Ultimate Beneficial Owners (UBOs) is not a one-time thing, it is an ongoing process, complex and complicated, that requires financial institutions to monitor their customers' ownership structures and update their records accordingly. Ongoing monitoring enables detecting changes in beneficial ownership that may signal potential risks or start additional checking requirements. In conclusion, UBO identification is a critical tool in the fight against financial crimes. Refining and improving the system is a step closer to minimizing illicit activities.

Identifying the Ultimate Beneficial Owner (UBO) of a company can be a tricky task, and there are a few key hurdles that make it difficult:

- Data Availability and Accuracy: In some countries, there simply aren't public registries that list a company's UBOs. Even when registers do exist, the information might be incomplete, outdated, or even inaccurate.
- Complex Ownership Structures: Companies can be set up with multiple layers of ownership, using shell companies, nominee shareholders, and other mechanisms to obscure who ultimately controls the company (Fernando & Berkhout, 2022, chapter 2). This makes it difficult to untangle the web and find the real person at the end (Moody's (2022)).
- Keeping Up to Date: Even if you manage to identify the UBO initially, there's no guarantee that information will stay current. UBOs can change hands, and keeping track of those changes requires ongoing monitoring and effort (Greville,

Furthermore, the preliminary research done states that AI and other technologies (e.g. datamining, blockchain etc.) can improve the accuracy and reliability of UBO identification and can transform the manual process into an automated one. Through the research undertaken on the literature, which we find to be precarious, vague and not current in this field, an attempt to investigate the UBO phenomenon was identified. In addition, the legal framework has been studied.

Future research will be oriented on UBO process in the financial-accounting and banking ecosystem in association with the general concern of risk management.

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