

RIA BENEFICIAL OWNERSHIP

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HM TREASURY/DTI

REGULATORY IMPACT ANALYSIS
DISCLOSURE OF
BENEFICIAL OWNERSHIP OF UNLISTED COMPANIES

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1. MANAGEMENT SUMMARY

1.1 Background

1.1.1 In its Report of June 2000 entitled "Recovering the Proceeds of Crime" the Cabinet Office Performance and Innovation Unit (PIU) studied how the UK anti-money laundering regime might be tightened as part of the fight against serious and organised crime. A key conclusion was the need for measures to improve use of disclosures in helping law enforcement to attack criminal finances. In particular, shell companies were seen as often involved in complex money laundering operations, with criminals benefiting from the ease of incorporation in the UK and the ability to keep secret the actual beneficial owners of UK companies. It concluded that "a Regulatory Impact Assessment (RIA) should weigh the clear law enforcement benefits of publicly registering beneficial owners against the burden that it would place on companies, as well as the relative benefits of a lesser burden, e.g. making details of beneficial owners available to law enforcement officers".

1.1.2 In late 2000 Her Majesty's Treasury ("HMT") and the Department of Trade and Industry ("DTI") drafted a range of outline policy options and commissioned this RIA from Compliance Chain Limited ("CCL"). The RIA covers all unlisted UK companies because the UK Listing Authority is already listed companies and the greater risk is felt to lie in unlisted companies.

1.1.3 In June 2001 the OECD issued a report on the misuse of corporate vehicles which is the spearhead of international action in the sector. This RIA has also been written with a view to implementing the recommendations contained in the OECD report and ensuring that the UK is unequivocal in its fight against international organised crime. The RIA, which identified at an early stage the value establishing beneficial ownership in counter-terrorism, may well be of relevance to the measures being taken by the international community in the wake of the 11 September attacks in the USA.

1.1.4 The RIA is based on desk research and interviews held with a wide range of sources in public and private sectors in the summer of 2001. It focuses on the position under English law and, rather than following the Cabinet Office suggested format, is structured to focus on specific detailed issues. However, a Table of Conformity (App. 1) with the suggested format is provided.

1.2 Base Case

1.2.1 There are a wide range of business forms in the UK half of which are variants of the company structure. The *bona fide* reason for forming a company is to gain protection from unlimited liability. Compared with other countries the UK

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offers advantage of speed price, corporate infrastructure and a good judicial environment - See *Sections 3.1 - 3.3*.

1.2.2 Companies are owned by their members, who are usually their shareholders. Defining ownership can be problematic and for the purposes of the RIA a strict definition of ownership has been made. From the point of view of anti-money laundering policy, control is also an important consideration, as recognised in the existing attention paid to shadow directors. A company can be controlled by persons who are not its owners or beneficial owners and whose role is not revealed by the current ownership and control disclosure regime - See *Sections 3.4 - 3.6*.

1.2.3 Details on companies, their ownership and control are held by companies themselves, Companies House and private sector data providers. The extent of data held is governed in the public sector by policy and in the private sector by commercial considerations, such as the need to establish creditworthiness. Such information can be used by a wide range of law enforcers using their respective powers. However, data obtained under the current disclosure regime does not easily support inquiries into beneficial ownership, or produces information that is incomplete and/or out of date and which may risk warning suspects they are under investigation. There is currently no system that allows the depth of regulatory data found in the public sector to be searched effectively and efficiently or easily matched against data held in the private sector - See *Sections 3.7 - 3.10*.

1.2.4 Action on disclosure of beneficial ownership of small companies would underline the UK's tough stance on money laundering in the UK and dependencies. The question of beneficial ownership is closely linked to two of the Financial Action Task Force's key areas of concern – trusts and the role of professionals and other intermediaries in the establishment and management of companies. These concerns are also shared by other multilateral and private sector bodies - See *Section 3.11*.

1.3 Current Proposals

1.3.1 The five cumulative options identified by HMT and DTI are set out in detail in Section 4 and summarised in Table 1. The three variants of Option 1 cover imposing a duty on beneficial owners of private companies to identify themselves and their level of interest to the company involved with various degrees of detail and timeliness. Option 2 extends this duty to require reports to be made on beneficial and legal ownership from private and unlisted companies to Companies House in annual returns, whilst Option 3 requires changes of legal and beneficial ownership to be submitted to Companies House as they occur. Option 4 looks at the creation of a searchable database on legal and beneficial ownership and Option 5 extends this to include directorships and shadow

directorships. The option of making such information available to the public (as opposed to just law enforcers) is also set out. See sections 4.1 – 4.9 and Table 1.

1.4 Benefits

1.4.1 Benefits identified included not only higher recovery rates, but also other law enforcement benefits such as better deterrence and prevention and meeting international treaty obligations. Private sector benefits included reduced credit costs and higher business confidence. Important assumptions made in obtaining such benefits included that Companies House would collect and chase, but not validate, disclosures. In addition to a light touch regime for benign non-disclosure, a serious arrestable offence would need to be created covering intent, recklessness or gross negligence in assisting with laundering money - See Section 5.1.

1.4.2 Potential beneficiaries identified include law enforcers and civil experts engaged in recovery, law enforcers engaged in other investigations and private sector credit reference agencies and their clients. Direct recovery benefits would accrue through shorter investigation times, more investigation capacity and the ability to attempt more complex investigations with a greater chance of success. Options that result in timely data and allow automatic links to data held in the private sector offer higher levels of benefits. Secondary recovery benefits would accrue from making it harder for intermediaries (lawyers, accountants and company service providers) who help criminals to continue to do so. The proposals would also offer wider benefits to those investigating terrorism, drug trafficking and organised crime, helping to demonstrate the UK's intention to prevent abuse of corporate vehicles. Under the open register options industry would also benefit from better access to credit information and less credit risk. See Sections 5.2 – 5.6.

1.4.3 Arguments in favour of making disclosure information public centre on the advantages gained from cross-referencing it to private sector data. Arguments against include *bona fide* grounds for privacy such as the political vulnerability experienced by Huntingdon Life Sciences. Whilst ultimately a political decision, the advantages are thought by those interviewed to outweigh the disadvantages. The creation of a serious arrestable offence may be compared to similar or tougher penalties established for tipping off or failing to report, and those proposed under the Company Law Review for fraudulent trading. See Sections 5.6 – 5.8.

1.4.4 In quantifying and attributing benefits, the analysis identifies the key factors of providing better legal and beneficial ownership disclosure, increased personal data detail, data timeliness, system user-friendliness and links to other data sources. These are used to identify three orders of economy in investigation effort estimated at 5%, 15% and 30% respectively available according to the various option involved. These are in turn applied to the estimated cost of just one part of UK financial investigation activity. Further savings are identified in additional recoveries, crime prevention and reduced business risk. Taking a strict

view of benefits and beneficiaries result in estimated savings of £5.1 million, £15.2 million and £30.3 million for the first second and third orders of economy respectively. Each option is then analysed in term of which order of economy was generated. The open register version of Options 3, 4 and 5 generate the greatest benefits. See *Sections 5.9 – 5.17 and Tables 2, 3 and 4.*

1.4.5 Sensitivity analysis shows the benefits would be decreased unless full name, date of birth and post code were all required as personal identification data, and increased if this were extended to national insurance, driving licence or passport number. The need for a civil penalty to ensure filing at Companies House (Options 2 and above) is also highlighted. The effects of non-compliance are found to be greatest where wide-scale non-reporting or reporting of indistinct data occurred. However, this extent of non-compliance is thought to be unlikely given the compliance profile of the target group, and non-reporting would in any case be easily detectable under Options 2 and above. Were criminals to go abroad outside the scope of UK legislation, benefits would still accrue in terms of quicker determination that an operation was based offshore, the consequent release of investigation assets to intensified pursuit or more rewarding duties, and the collection of evidence on non-co-operative jurisdictions for use at a political level. Tax considerations play an important role in decisions to site businesses and the crime business is no exception. See *Sections 5.18 – 22 and Table 5*

1.5 Costs

1.5.1 The proposals affect just under 1.5 million companies. The report estimates the number of legal shareholders at 5.25 million and beneficial owners at around 125,000. However, the large majority of firms have small fixed shareholdings and are little affected by the proposals. By analysis of the nature and number of filing transactions each option would generate the report identifies direct and compliance costs for each option in respect of both open and closed register options. As the cost are cumulative Option 1 has the lowest costs and Option 5 (Open) the highest. The closed register costs are only slightly lower, if at all, than the open register costs. Company House IT capital costs are assumed to be covered by the blanket budget put aside for new systems arising from the Company Law Review. Other potential costs identified but not calculated include the time needed by lawyers and accountants to study the proposals. See *Sections 6.1 – 6.11 and Table 4*

1.5.2 Costs are sensitive to the number of shareholders in private companies in the UK, which is not known. Company formation agents consider the estimates used in the report to be reasonable. Legal expenses might increase the cost to companies and shareholders significantly, but only if the proposals were poorly drafted and explained. See *Section 6.12*

1.5.3 There may be small costs arising from the need to obtain licence under the Data Protection Act 1998. The final form of the proposal will need to be checked

for conformity with both the DPA and the Human Rights Act 1998 to confirm the relevant exemptions do in fact apply. With regard to the protection of privacy, the report distinguishes between the need to protect privacy and the need to guarantee anonymity. It highlights the dilemma that protecting against one threat might necessarily create exposure to another threat. Whilst showing how it would be possible to adopt disclosure based on service addresses, it concludes such a system would cost at least £1 million p.a. and risk creating indistinct data – a major risk to obtaining the full benefit of the proposals. The report suggests that a much stricter system would provide better protection to a few highly vulnerable people, cost less to operate and preserve the integrity of the proposed measures. See 6.13 – 6.14.

1.6 Alternatives

1.6.1 The report examines the option of a database containing details of legal ownership and the fact of beneficial ownership, updated yearly. This Option is found to be of limited value, especially with regard to criminal intelligence, having costs similar to Option 4 but benefits closer to Option 2. The possibility of a semi-open register is discussed. This would enable the public policy problem of privacy to be overcome whilst allowing public access to anonymised data via carefully screened credit reference agencies. The effects on cost would be small and the superiority of benefits over costs maintained in all cases.

1.7 Conclusions and Recommendations

1.7.1 The report concludes that Option 3 Open offers the best functionality and long term benefits at least cost. Option 5 offers the best closed register route. Option 3 Open offers the best protection in case of wide scale non compliance, whilst Option 5 Open is the best if money is no object, as it creates unifies public sector data, thereby simplifying inquiries handled and creating a back up system in case private sector systems fail.

1.7.2 Rather than adopt a closed register route the report recommends adopting a semi open system. If the proposals overall are felt to be worthy but sensitive then the minimum viable system would be Option 2 Open with the reporting threshold possibly raised to 10%. It would only be worth taking this route if it were intended to tighten the regime in due course. The semi open register option should be looked at in detail before a closed register option is chosen.

2. BACKGROUND

2.1 Legal and illegal payment flows

2.1.1 Every day, billions of payments are made and received by businesses, a large proportion of which are companies, in the UK. The overwhelming majority of such payments are in respect of bona fide goods and services. However, a significant minority of transactions represent the transfer of the proceeds of crime as the profits from illegal activities are surreptitiously shifted from the illegal to the legal economy. Once laundered they can be used by those who control them without fear that the criminal origins of the funds will come to light.

2.2 PIU report and disclosure

2.2.1 The Cabinet Office Performance and Innovation Unit (PIU) studied "the effectiveness of pursuing and removing criminal assets as part of the fight against crime and particularly against serious and organised crime" and "how to maximise effective use of such techniques". In its Report of June 2000 entitled "Recovering the Proceeds of Crime" it looked (Chapter 9) at how the UK anti-money laundering regime might be tightened, emphasising that "attacking money laundering has been recognised internationally as key to undermining criminal activity". A key conclusion was the need for measures to improve use of disclosures in helping law enforcement to attack criminal finances.

2.2.2 Chapter 9 of the PIU Report noted that "almost all complex laundering operations involve UK shell companies" and that the launderers' task was made easier by the ability to install nominee directors and keep secret the actual beneficial owners of the company.

2.2.3 The PIU Report also highlighted the fact that "ease of incorporation is seen as one of the strengths of the UK's competitive regulatory environment" and that there were bona fide reasons why small privately held companies do not necessarily wish details of their ownership to be made public. It also pointed out the difficulty in some cases of attributing beneficial ownership of companies to individuals other than trustees.

2.2.4 The PIU Report concluded that "a Regulatory Impact Assessment (RIA) should be carried out to establish whether the clear law enforcement benefits for financial investigation and prevention of money laundering of publicly registering beneficial owners justifies the burden that it would place on companies". It also concluded that the RIA should consider the relative benefits of a lesser burden "e.g. that details of beneficial owners should be made available on enquiry by a law enforcement officer". The PIU Report did not explain, however, what was meant by a "beneficial owner".

2.3 Follow up by HMT & DTI

2.3.1 Her Majesty's Treasury ("HMT") and the Department of Trade and Industry ("DTI") took responsibility for the RIA and in late 2000 drafted a range of outline policy options. They commissioned this RIA of the options from Compliance Chain Limited ("CCL"), a leading consultancy firm specialising in the analysis of compliance issues.

2.3.2 In line with the Terms of Reference set by HMT and DTI, this RIA does not cover all UK companies, but only those which are unlisted. This is because, as set out in section 3.3.10 below, the UK Listing Authority is already charged with records of listed companies. It focuses on the abuse of corporate vehicles to hide ownership of assets, addressing how companies may be used by criminals, and the advantages and value offered by them to criminals. The RIA further assesses various options relating to precisely what information on beneficial ownership might be disclosed, by and to whom, and the optimum timing of disclosure. It also looks at how the information disclosed can be collected, collated, analysed and used by law enforcement and other third parties both to reduce the scale of criminal activity and money laundering, as well as to improve the record on confiscation of assets.

2.3.3 This RIA is a timely one in terms of both UK and international developments in the reduction of crime. In the UK the Proceeds of Crime Bill is currently undergoing passage through Parliament. Comprehensive of English company the Company Law Review was published in July. A radical overhaul of UK financial market regulation is due to come into force at the end of November. On the international scene the OECD has recently released an extensive report on the Misuse of Corporate Vehicles for Illicit Purposes, the Financial Action Task Force is to commence a review of its Forty Recommendations, and many countries are stepping up their money laundering deterrence regimes.

2.3.4 Of the international initiatives, the most germane to this RIA is the OECD Report on Misuse of Corporate Vehicles. In a key passage, its finding was that:

"...in order to successfully combat and prevent the misuse of corporate vehicles for illicit purposes, it is essential that all jurisdictions establish effective mechanisms that enable their authorities to obtain, on a timely basis, information on the beneficial ownership and control of corporate vehicles established in their jurisdictions for the purpose of investigating illicit activities, fulfilling their regulatory/supervisory functions, and sharing such information with other authorities domestically and internationally. This requires adherence to three fundamental objectives...:

- 1) beneficial ownership and control information must be maintained or be obtainable by the authorities;*
- 2) there must be proper oversight and high integrity of any system for maintaining or obtaining beneficial ownership and control information; and*

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3) non-public information on beneficial ownership and control must be able to be shared with other regulators/supervisors and law enforcement authorities, both domestically and internationally....

In addition, it is desirable that policymakers in each jurisdiction consider ways to make it possible to grant access to beneficial ownership and control information to agents with authority delegated by the government or the judiciary (such as insolvency administrators) and financial institutions seeking beneficial ownership and control information in order to comply with their customer identification and due diligence requirements under anti-money laundering laws.”

2.3.5 The OECD found the mechanisms for obtaining such beneficial ownership and control information fall into three categories, namely:

- 1) up front disclosure to the authorities
- 2) disclosure by intermediaries involved in the formation and management of corporate vehicles
- 3) use of an investigative system

2.3.6 The OECD also highlighted the role of information sharing. Member States can tailor the above three mechanisms (or a combination of them) as they see fit, provided the solution complies with the three objectives set out in section 2.3.4 above. The OECD did not, however, differentiate the value of such information as between intelligence, investigation and evidential purposes.

2.3.7 This RIA refers to the position under English law. The position under the laws pertaining to Scotland and to Northern Ireland will in most respects be the same or fairly similar, but any differences are not covered here. As the title to this Report suggests, and as required by HMT and DTI, it focuses on beneficial ownership, though issues relating to control are covered in sections 3.5 and 3.6 below.

2.3.8 Lastly, due to the complexity and range of the issues involved and the specific requirements of HMT and DTI, this RIA does not follow the Cabinet Office suggested format for RIAs. A Table of Conformity (App. 1) shows where issues usually treated separately under various RIA standards are covered in this text.

3. BASE CASE

3.1 Types of businesses and companies

3.1.1 Businesses in England and Wales may take a number of forms:

- unincorporated association
- unlimited company
- public limited company
- public limited listed company
- private limited company
- private limited listed company
- company limited by guarantee without share capital
- company limited by guarantee with share capital
- company formed by Royal Charter
- company formed by letters patent
- company formed by Act of Parliament
- overseas company
- partnership
- limited partnership
- limited liability partnership
- European Economic Interest Grouping
- friendly society
- industrial society
- provident society
- sole trader

3.1.2 Of these, the principal forms are unincorporated businesses, partnerships and public and private limited companies. Companies may also be formed in Scotland and overseas companies may also register a presence as a branch, or a place of business (its residence for tax purposes may well be different).

3.1.3 Friendly, industrial and provident societies have a separate registry administered by the Registrar of Friendly Societies and are outside the scope of this RIA, as are companies formed by Act of Parliament, charter and letters patent.

3.1.4 Companies are different from individuals and sole traders in that they have separate legal personality. Companies do not have to limit the liability of their members towards creditors (S1(2)(c) CA 1985) but almost all do so, either by share or guarantee. There are roughly 1.5 million companies currently registered in the UK. They fall into two principal types of company, public and private. A public company may offer its shares to the public. It may also be quoted on a stock exchange or securities market, but does not have to be: of the 12,000 public companies registered in UK, only 2,200 are quoted on the London Stock

Exchange. Certain private companies may have their shares publicly traded (e.g. on AIM or Ofex).

3.1.5 A public company must have two directors and a suitably qualified secretary. A private company may have just one member and one shareholder (S1(3A) CA 1985), but at least two people must be involved in running it, one of whom must be the company secretary, and the other a director. As seen from the above figures, nearly all companies are private companies.

3.1.6 Unlimited companies can be formed with or without shares. Companies limited by guarantee do not normally have a share capital (since 22nd December 1980 a company cannot be formed which is both limited by guarantee and has a share capital). Companies limited by guarantee are small in number and are usually formed by operators of clubs and associations for charitable, social or non-profit making purposes. In the event of liquidation, the members of such a company pay whatever sum they have guaranteed to pay (usually £1). Such companies are not the main focus of this RIA.

3.1.7 Unlimited companies are also rare since the liability of the shareholders is unlimited and thus defeats the usual purpose of incorporation. However, as they have unlimited liability they can reduce their share capital in any way, much easier than limited companies can. Unlimited companies are sometimes formed for sporting events. Again, such companies are not the main focus of this Report.

3.1.8 Businesses may establish themselves as sole traders, but do not have separate legal personality or limited liability.

3.1.9 Lawyers, accountants and architects all traditionally use partnerships, but recently such professionals are moving towards usage of Limited Liability Partnerships. Partners are jointly and severally liable for the debts of the partnership, though procedural rules allow partnerships to sue and be sued in the name of the partnership. Limited Partnerships under the Limited Partnership Act 1907 are relatively rare, as are European Economic Interest Groupings (EEIGs), traditionally used by associations of professional firms as they are taxed on a flow-through basis.

3.2 Reasons for company formation

3.2.1 The original intention in allowing the creation of companies was to afford some measure of protection to entrepreneurs. Up until then UK industry depended on entrepreneurs risking the whole of their assets with no protection at all.

3.2.2 The earliest commercial corporations were chartered companies whose members traded with their own stock, subject to the regulations of the company. These regulated companies were later replaced by "joint stock companies" whose shares were freely transferable by any one of their members without the

consent of all the members. From the 18th century onwards, the promoters of undertakings such as turnpike roads or canals obtained incorporation by private Acts of Parliament, usually because they needed authority to acquire land. Statutory incorporation became more common in the 19th century with the development of railways and private gas, electricity and water undertakings. Both chartered and statutory incorporation however, were very slow and expensive and many unincorporated companies sprang up outside these restrictions. It became necessary for the Board of Trade to institute a method of incorporation which was easily available and which at the same time allowed the public some measure of protection by regulation. This resulted in the method of incorporation by registration. Nowadays nearly all commercial companies are registered companies.

3.2.3 Companies formed by Royal Charter, letters patent or Act of Parliament do not appear on the register of companies, although the Companies Act 1948 made provision for them to register if they so choose. The only chartered company records which are held in the Public Records Office are those of the various colonial chartered companies. There remain approximately 400 active incorporated companies which were created by Charter, which consist mainly of worthy institutions such as universities and guilds. There is no consolidated record of companies created by Act of Parliament, but it is believed that there are few of them left, though some of them are powerful companies. Some have gone through a number of forms of incorporation (e.g. Royal Bank of Scotland, founded by Royal Charter in 1727, before being merged by private Act of Parliament and then becoming a plc).

3.2.4 The creation of the joint stock company allowed entrepreneurs to invest a certain amount of their capital with lesser risk, the effect on the UK economy being dramatic, with some commentators ascribing the development of an industrial economy in the UK to this reason alone. The key reason for the formation of a company is still the protection from unlimited liability that the corporate veil allows shareholders. Those in the position of directors are charged with the running of the company and the protection of shareholder value, and nowadays have rather more risk and obligation as discussed below.

3.3 Reasons for choosing company formation in the UK

3.3.1 Company formation in the UK is now a smooth and efficient process. Indeed it has become a key attraction to establishment in the UK (as recognised in the PIU Report), coupled with the fact that the process of law in the UK is seen as relatively fair and efficient by global standards. For example, it is estimated that over 40% of the world's commercial contracts are governed by English law.

3.3.2 Companies in the UK may be formed on a "tailor-made" basis or "off the shelf", the majority of UK companies being formed on the latter basis. If the entrepreneur has all the requisite details to hand to enable the company to be formed, the established company can be handed to him in under 24 hours at a

cost of £1000 or less (see below). This is seen as a major attraction to establish business in the UK.

3.3.3 Formation of corporate vehicles in other countries is often slower and more expensive. Some “offshore” jurisdictions allow the formation of companies at a cheaper rate (see Appendix 2 for a comparative table of company formation fees in certain key and popular jurisdictions). Others offer more “protection” for entrepreneurs by offering for example greater confidentiality, through swingeing secrecy laws, the use of bearer shares, and the use of “international business companies”. The latter, though registered in the jurisdiction concerned, are not allowed to carry on business there. This is in stark contrast to financial institutions across the EU which are required to locate their registered office in the same country as their principal place of business pursuant to the EU “BCC1” Directive (95/26/EC). In relation to all companies, the test of EU personality is a two stage test – the first stage being formation under the laws of an EU Member State, the second stage being one of registered office, seat, or principal place of business, (depending on the Member State concerned) being within a Member State.

3.3.4 An entrepreneur is not obliged to use a UK corporate vehicle in order to do business in the UK, and can use a vehicle established anywhere in the world. If he maintains a place of business in the UK, then he is required to register a branch of an “overseas” (as defined in the Companies Act 1985) company with Companies House. If he merely carries on business on a cross-border services basis, then no such registration is required, and the entrepreneur is bound only by the reporting obligations of the home state.

3.3.5 There may, however, be other requirements for registration depending on the type of business carried on (e.g. registration with the Financial Services Authority). In general, in order to carry on business in the UK a business will be required to comply with laws on a wide variety of matters from data protection and advertising, to health and safety. Generally speaking, the requirements applied in the UK do not have extraterritorial effect, i.e. the obligations applicable to business carried on in the UK do not necessarily apply in other countries.

3.3.6 Virtually anyone may establish a company, either by direct application to Companies House, or by going through an intermediary such as a company formation agent, lawyer, accountant or other advisor. The majority of businesses choose the latter route. Up to 10% of current company formations via formation agents are thought to involve foreign interests.

3.3.7 The advantages of going through a company formation agent or other intermediary are that they have familiarity with the process, can assist in avoiding pitfalls for the unwary, and can often offer other related services such as provision of a registered office, company secretary, directors, officers and nominee shareholders, establishment of bank accounts, provision of fax and mail forwarding services, E mail addresses, telephone answering services, etc.

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3.3.8 The cost of establishing a company directly by going to Companies House comprises the registration fee of £20 (£80 if same day registration is required) plus postage, stationery and time. The applicant would also have to file a memorandum and articles of association, which it would either have to draft itself, or use a standard set. A standard set usually costs around £20. Completing the same process using a company formation agent would cost around £125 – £295. Completing the same process using a lawyer or accountant would usually cost £300 – £1,000.

3.3.9 Compared with forming a company in other countries, therefore, the UK has the advantage of speed, price, corporate infrastructure services and a good business and judicial environment. There may well be tax implications and indeed, access to the UK tax regime may be a prime consideration in establishing a UK company in the first place.

3.3.10 As mentioned in section 2.3.2 above, the key focus of this RIA is on the private limited company as this is where the greater risk is felt to lie. Hitherto, criminal organisations have not been found to use other more arcane forms of business (such as some of those mentioned above) since they would be conspicuous. Accordingly, they and the question of harmonising disclosure across the various forms of business are not discussed in detail in this Report

3.3.11

3.4 Ownership of companies

3.4.1 Under English law the owners of a company are its members, usually its shareholders. The legal owner of a share is either the registered shareholder, or the bearer of a related share warrant. Legal owners can be legal or natural persons and shares may be jointly owned.

3.4.2 By issuing a share certificate showing a named person as entitled to certain shares, a company represents that he is so entitled, and if anyone deals with him in reliance on the certificate and suffers a detriment, the company may not deny the truth of its representation. The falsity of a share certificate does not of itself give rise to a cause of action unless the directors issued it knowingly or carelessly.

3.4.3 Where the legal owner of a share holds that share under a contractual agreement with and on behalf of, another person, then the legal owner is often referred to as a "nominee shareholder".

3.4.4 The legal owner of a share in a company may therefore not necessarily be the beneficial or equitable (i.e. real) owner of the shares. The definition of a member of a company under the Companies Act 1985 is entirely concerned with the legal owner of a share, that is, the person appearing on the register. The legal and beneficial ownership of shares is, however, frequently separated, both because shares are a common form of investment for trustees and because it is often commercially convenient for shares to be held by a trustee or nominee.

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Currently, beneficial owners have no special status in relation to companies. A company is not bound by, nor compelled to recognise, any interest in a share other than an absolute right to the whole share vested in the registered holder, even where the company has notice of some other interest.

3.4.5 English law defines an owner as “the person who enjoys or who is entitled to the benefit of property”, and a “beneficial owner” as “a person who holds or is entitled to a beneficial or equitable interest in property, such a person for whose benefit a trust is created”. Thus a beneficial or equitable owner may own some, the majority or all of the shares in a company by means of a formal or informal agreement with the legal owner or owners, which may be in the form of an individual, a trust, or another company.

3.4.6 There is no definition of “beneficial owner” in the Companies Acts. SS 203 - 205 Companies Act 1985 create a “wider” definition of notifiable or disclosable interest (which some would consider to be a “beneficial interest”) in relation to public companies, and Schedule 2 to the Companies Act 1985 contains an interpretation of references to “beneficial interest” included in certain sections of, and schedules to, the Act. This schedule is complex, but as it adds little to the discussion here, it is omitted, though parts of it would be of use to the parliamentary draftsman in defining a “beneficial owner”. S444(2) contains a definition of a person deemed to have an interest in shares, which may also assist the draftsman’s purpose.

3.4.7 In the event of the proposals set out in this RIA being implemented, this definition of beneficial interest might have to be reinterpreted to conform to the narrower definition of real owner used (after discussions with HMT/DTI) in this RIA.

3.5 Control of companies

Concepts of control

3.5.1 The concept of control of a company is an interesting one, as for some of those we interviewed in the course of this RIA, this is the key issue at stake, rather than a strict focus on who the beneficial owner of the company may be. Thus the controllers may in actual fact be shareholders, beneficial shareholders, directors, shadow directors, creditors, or some third party behind the scenes who is controlling the company by blackmail, extortion, coercion or some other means. Those behind criminal activities have used all such positions to control businesses.

3.5.2 Recovering the proceeds of crime will necessitate an examination of those controlling the criminal activity, and establishing a link between them and the criminal assets. However, as this RIA mainly concerns small private companies, as requested, the narrower definition is examined here, as stated above.

Levels of Control

3.5.3 The issue of control also occurs in related areas. For example, the Financial Services Authority tries to establish who is behind a financial institution and whether they are fit and proper to be authorised to act as a controller of a financial institution in the UK, when deciding whether or not to authorise that financial institution. It also requires to be provided with information as to changes in controllers so as to decide upon the continuing authorisation of the financial institution. It is therefore useful to set out the controller test as used by the UK financial sector regulators:

“Controller means:

(a) in relation to a body corporate:

- (i) a person, who alone or with any associate or associates...has a direct or indirect holding in the body corporate which represents 10% or more of the capital or of the voting rights; and*
- (ii) any person who has a direct or indirect holding in the body corporate which makes it possible to exercise a significant influence over the management of the body corporate; and*

(b) in relation to an unincorporated association:

- (i) any person in accordance with whose directions or instructions the officers of the association are accustomed to act (but disregarding advice given in a professional capacity);*
- (ii) any person who is entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of the association; and*
- (iii) any person who has a direct or indirect holding in the association which makes it possible to exercise a significant influence over the management of the association.”*

3.5.4 Other areas of English law define the concept of “control” differently. For example, the City Code on Take-overs and Mergers defines the concept as “Control means a holding, or aggregate holdings, of shares carrying 30 per cent or more of the voting rights...of a company, irrespective of whether the holding or holdings gives de facto control”.

3.5.5 The Income and Corporation Taxes Act 1988 (S840) states “for the purposes of, and subject to, the provisions of the Tax Acts which apply this section, “control”, in relation to a body corporate, means *“the power of a person to secure:*

- a. by means of the holding of shares or the possession of voting power in or in relation to that or any other body corporate; or*
- b. by virtue of any powers conferred by the articles of association or other document regulating that or any other body corporate,*

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that the affairs of the first-mentioned body corporate are conducted in accordance with the wishes of that person and, in relation to a partnership, means the right to a share of more than one half of the assets, or more than one half of the income of, the partnership”

3.5.6 With regard to the current RIA the options are to require the reporting of the fact, degree or precise amount of, or changes in, beneficial interest. The terms of reference have followed percentage holdings rather than the fact of ownership with regard to both thresholds and intervals, for the sake of consistency with monitoring public companies. It should be borne in mind that these levels were geared towards the regulation of the take-over of larger companies with a wider shareholder structure than the companies involved here. Under alternatives the option of monitoring the simple fact of beneficial ownership is also reviewed.

Directors secretaries and shareholders

3.5.7 Directors are responsible for the management of a company for the benefit of the shareholders, but do not have authority to commit the company to any contract unless acting as a board or individually under powers delegated by the company or the Board. Under such circumstances directors can do anything subject to the limitations of the law, the company's memorandum and articles, and provided it is in the company's best interests.

3.5.8 The law currently states that all companies must have company secretaries but does not specify their duties. The following list (which is not exhaustive) includes both those duties which are legal obligations of the company and those resulting from best practice according to the Institute of Chartered Secretaries and Administrators:

- board meetings (ensuring the smooth operation of the company's formal decision making and reporting machinery through organising meetings, formulating agendas, information management, minutes, etc.)
- shareholder AGMs, EGMs and communications (circulars, dividends, documentation concerning shares generally, such as share transfers, and notices of meetings, annual report)
- ensuring compliance with the company's Memorandum and Articles
- maintenance of the statutory registers (shareholders, mortgages and charges, directors and secretary, directors' interests, etc.)
- filing of statutory returns at Companies House (annual returns, report and accounts, amendments to incorporation documents, returns of allotments, notices relating to officers and auditors, change of registered office, Companies Act resolutions)
- share administration (managing and supervising the register of members, share transfer matters generally, requests for information from shareholders, issue of share certificates, notice of allotments, employee share option schemes, share capital restructuring)

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- shareholder monitoring (stake building, “making appropriate enquiries of members as to the beneficial ownership of holdings”)
- corporate governance
- maintaining communication links between shareholders and the board and non-executive directors
- making documents required by law available for inspection by third parties
- managing the security of the company seal, share certificates and stock transfer forms
- administering the registered office
- ensuring corporate identity requirements are complied with
- administration of subsidiaries, liaison with the holding company, maintaining records of group structure
- general compliance

3.5.9 The traditional functions of company secretaries are important when it comes to regulation on disclosure of beneficial ownership, not least as the Company Law Review has recommended that, in respect of private companies, the mandatory appointment of a company secretary should be abandoned.

3.5.10 This is because at present a company secretary of a private company is not required to have appropriate qualifications or experience. In practice, except in the case of sole director companies, directors usually carry out the role of company secretary, or contract out this role to external advisors, or appoint a family member to fill the position. Accordingly it is felt that the current requirement imposes a burden to very little effect, and that the market should make the decision to use a company secretary, not the law.

3.5.11 However, the recommendation to abandon the mandatory appointment of a company secretary would not remove the obligation on the company to carry out the functions that a company secretary normally carries out, but it would provide greater flexibility to companies in their internal administrative arrangements. Private companies could then appoint a company secretary to carry out those functions that are ascribed to either a director or company secretary in the Act, or performed by the company secretary as a matter of practice. When appointed, the company secretary will be able to carry out these functions with the full authority that he has under the current law.

3.5.12 For the purposes of this RIA, the key point is that if the requirement to have a company secretary is indeed abolished, directors may become more closely involved with processing declarations of beneficial ownership and reporting the same to Companies House.

Shareholders

3.5.13 Depending on the size of their shareholding, and whether or not they are company employees, shareholders, the legal owners of a company, can influence its actions by:

- acting as officers or employees
- informal dialogue with the officers of the company
- formal resolutions passed at shareholders' meetings.

3.5.14 By contrast, beneficial owners may have agreements with the legal owners and/or officers of the company, whereby the company is run either on a discretionary or non-discretionary basis by the legal owners and/or officers with any profits flowing back to the real owner. Directors in such cases are sometimes called "nominee directors".

3.5.15 However, where beneficial owners are in a position to influence a company's operations then they themselves may become "shadow directors". The Companies Act defines a shadow director as a person in accordance with whose directions or instructions the directors of a company are accustomed to act (S741(2) CA85, S22(5) CDDA86).

3.6 Disclosure of ownership and control

Ownership

3.6.1 With company status comes the duty for a company to disclose certain information. Routine disclosure of information on ownership and control of companies is governed principally by the Companies Act 1985 and subordinate legislation (such as the Companies (Registers and Other Records) Regulations 1985, SI 1985/724). The Act sets out the information that companies and their officers must provide on themselves, their shareholders and the company's financial situation. This is done principally by means of company registers and company submissions to Companies House.

3.6.2 Allotment of shares must be notified to Companies House within one month (S88(2)). Under Section 352(1) these details must be entered into the register that every company is required to maintain (Register of Members) giving details of each member's name, address and the date of their becoming or ceasing to be a member and the class of share held. The fact that a share certificate must be complete and ready for delivery within two months (S185 (1)) in effect creates a time limit.

Transfers and changes

3.6.3 Every company must complete and have ready for delivery the certificates of all shares within two months after the shares have been allotted, or from the date on which the transfer of such shares is lodged with the company (unless the conditions of issue of the shares provide otherwise). This requirement does not apply in the case of a transfer to any persons where, by virtue of regulations

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under section 3 of the Stock Transfer Act 1982, they are not entitled to a certificate or other document of, or evidencing, title in respect of the securities transferred (regulation 25 Table A 1985 - 2000 and SS183, 185 & 352). Transfers of shares are not registered as they occur at Companies House but the next annual return must contain a list of members at the return date. Section 352(6) allows for the deletion of former members 20 years after a person ceases to be a member.

3.6.4 Before proceeding with any transfer of shares, the company secretary will have to check the Articles of Association. The transfer of legal title to shares can only be effected in writing and a stock transfer form is usually used for this purpose (unless an exemption applies). The transferor must complete and sign the stock transfer form. If the shares being transferred are nil or partly paid, the transferee will also need to sign the stock transfer form. The full procedure for transferring shares is set out in Appendix 2.

3.6.5 If shareholders change their addresses, then they inform the company secretary or registrar as appropriate and the company secretary amends the details.

Register of Members

3.6.6 The Register of Members must be kept at the offices of the company or at another address in the UK registered with Companies House. It must be open to public inspection, though it may be closed for up to 30 days per annum. Except for companies with registered offices in Scotland, no notice of any trust over shares can be registered. The register of members is prima facie evidence of any matters which are directed or authorised to be inserted into it. The details required are:

- name
- address
- date of registration
- date of cessation of membership
- type, class and number of shares held
- amount paid
- amount and class of stock held
- class to which member belongs

3.6.7 The details of the company's shareholders need to be up to date so that any notices for general meetings and dividends are sent to the correct address.

3.6.8 Companies are also required to submit to Companies House an Annual Return (Form 363a/363s), by reference to a yearly date ("legal return date") specific to each company. Form 363a requires a full list to be sent to Companies House with every third return, with changes notified annually. The turn-around (Shuttle) version of this form (Form 363s) contains the name and address of

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shareholders already notified as at the legal return date, and provides space to record the name and address of any persons who became or ceased to be members over the intervening year.

3.6.9 A pre-shuttle version of this procedure also exists with companies submitting details annually and receiving a list of shareholders for confirmation every three years. Companies with many shareholders ("Bulk List" companies) submit data annually, often on CD-ROM, using a different system. However, these are almost exclusively listed companies.

3.6.10 Information on certain private share transfers is also submitted to Inland Revenue on Stock Transfer Forms, if they attract stamp duty, of which just over half a million were submitted last year.

Public Companies

3.6.11 Part VI Companies Act 1985 requires persons with an interest (i.e. legal and beneficial owners) in the unrestricted voting shares of a public company to disclose such interest to the company within two days of it crossing a specified threshold of the company's issued share capital. The starting threshold is usually 3% and disclosure must also be made at 1% intervals above this level. Certain less material interests (e.g. interests held by bona fide investment vehicles) must only report above the 10% level. Companies must keep a register of disclosures received.

3.6.12 Section 212 of the Companies Act also gives a public company the power to investigate the ownership of its shares. Companies do this by sending a written notice ("S212 Notice") to any person or company whom they have *reasonable cause to believe* has, or had, an interest (i.e. *owns, controls or has certain rights over shares*) in their relevant share capital at some time in the three years immediately preceding the issue of the notice.

3.6.13 The recipient of the notice is then required to inform the company making the enquiry whether they have or had such an interest, and to give details. The recipient may also be required to inform the company of anyone else whom they know to have or to have had, an interest in the shares in question.

Disclosure of Control

3.6.14 A company's initial directors and secretary are recorded on Form 10 and submitted upon application for registration of the company. Form 12 operates as a statutory declaration and must therefore be sworn in front of a solicitor, or completed and signed by one. A solicitor may therefore be seen as acting as a gatekeeper. The S288 series of forms allows for subsequent adding, amending and deleting of details of company directors and secretaries. The details of a shadow director or *de facto* director must be notified as per S741(2) CA 1985 in the same way as any other company officer. S723(B-F) CA 1985 & S45 Criminal Justice and Police Act (CJPA) 2001 provide for confidentiality of such data to be granted to directors and secretaries where such disclosure might put their

persons or property in jeopardy. Regulations under S45 CIPA 2001 are in the process of being drafted.

3.6.15 A company must keep a register of directors (including shadow directors) and company secretaries available for public inspection (S288(1) CA 1985).

Enforcement

3.6.16 All companies must deliver an annual return to the Registrar each year. Company directors are personally responsible for ensuring that they are delivered on time. Failure to deliver statutory information is a criminal offence. The consequences can be that directors risk a criminal record and a fine. The company can be struck off for persistent failure. Failure to deliver on time may also be a conduct matter to which the court may have regard under the Company Directors Disqualification Act 1986.

3.6.17 This duty is difficult to evade as Companies House tracks both Annual Returns and annual accounts and can identify non-compliance within a few days. Annual Return compliance is believed to be around 90-95%. In 1990-00 the DTI brought 683 prosecutions under S365(3) for failure to deliver annual returns. 360 convictions were obtained and 29 cases adjourned. The conviction rate over the last five years has ranged between 27% and 50%. The majority of charges where convictions were not obtained were as a result of the annual returns and accounts being filed and the prosecutions not being proceeded with.

3.6.18 As company registers of members and directors are so rarely checked, it is not known how well they are kept, and the obligation is easy to avoid. It is generally thought that the requirement to keep registers up-to-date is not observed, especially among companies established directly with Companies House. Where a company is formed via an intermediary or agent, registers of members and directors may be provided as part of the service, as is also the case with company secretarial software packages. Companies House and the DTI will investigate complaints concerning refusal of inspection of the members' or directors' registers under the Companies Act (S288 and S354). There were no prosecutions in 1999-2000. The number of complaints made about members' or directors' registers is not published, but is held by Companies House.

3.6.19 Changes in company secretaries and directors and their details must be notified within 14 days under S288 CA. This is not believed to be rigidly enforced, but non-compliance is highlighted each year by differences between the Form 363 details and the reality. In such cases companies often file the relevant S288 series form to regularise the position.

3.7 Public and private records

Companies House

3.7.1 Annual accounts and Annual Returns (with shareholder details) for all registered companies are openly available from Companies House upon payment of the relevant fee. Those who have set up an account can obtain this

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information in hard copy form or immediately by on-line inquiry. This includes many law enforcement units. Certain basic information about a company, but not its directors or shareholders, is available over the internet for free.

3.7.2 Companies House also maintains a register of individuals disqualified under the Company Directors Disqualification Act 1986, including their full name and address, as well as the period of, and reason for, disqualification. This information is available free of charge.

Private systems

3.7.3 In addition to official data held by Companies House, a number of company information services and private credit reference agencies hold data on companies often based on extracts from Companies House records backed up by their own research. These databases include shareholder details, usually the ten top shareholders of larger unlisted public and private companies, and can operate as relational databases as opposed to the corporate registry maintained by Companies House. This means that details on shareholders can be obtained without knowing the name of the company; merely inputting the name of the suspected shareholder will produce details of actual shareholdings of that person and of persons with similar names. For example, one such firm, Dun & Bradstreet produces a CD ROM called DASH – Directors and Shareholders which contains such information.

3.7.4 An important point about such companies is that they collect information on a wide range of issues on an international basis. Thus, Dun & Bradstreet bases its products and services on a global database of reputedly over 64 million companies worldwide. Its services, which include debt collection and credit reports, usually include information on the principals behind the business.

3.7.5 Another important feature is the fact that such databases are frequently updated. Thus Experian, a subsidiary of the GUS group and reputedly the UK's largest credit reference agency, makes over 20 billion updates each year to consumer credit files. The importance of such companies in credit making decisions is evidenced by Experian's claim to facilitate lending to customers equivalent to 20% of GDP in certain countries.

3.7.6 Data is held about all UK limited companies, including full financials, credit information and document images, all UK directorships, past and present, details of over 2.2 million UK non-limited businesses, county court judgements, payment trend information, credit ratings and risk scores, as well as on companies trading overseas. This is one of the largest and most detailed database of limited and non-limited companies in the UK.

3.7.7 In addition to business information companies, there are also a number of registrar companies, mostly operated by the main UK clearing banks, though independents such as computershare.com exist too. They hold a large amount of information on shareholders and shareholdings, principally on listed companies,

but also on unlisted companies. In a number of cases, information held by them may help to identify individuals who are believed to be associated with a company, e.g. as a signatory on cheques or letters, or as a shareholder. Such information may also be accessed on a relational as opposed to a registry basis.

3.7.8 Data services are often referenced by law enforcers and regulators as a standard procedure, should they know of their existence and have the budget and political will to use the data. They are also used extensively by financial institutions and others acting under an obligation to “Know Your Customer” for the purposes of compliance with Financial Services Act 1986, money laundering requirements pursuant to the Money Laundering Regulations 1993, as well as credit control.

3.8 Obtaining information using investigative powers

DTI

3.8.1 Under the Companies Act 1985, the Secretary of State for Trade and Industry has various powers to scrutinise both ownership and control of a company including:

- (S442) to establish company membership and investigate arrangements and understandings which though non-legally binding are or were likely to be observed and relevant to the investigation. This the appointment of inspectors to investigate and report on company membership.
- (S444) to require any person to provide information they have or may be able to obtain on past and present interests in a company's shares. This power does not require the appointment of inspectors.
- (SS431 and 432) where there is a request by the company itself or a number of its members, a court order or suspicion of fraud, the Secretary of State may (S431) or shall (S432– subject to certain conditions being met) appoint inspectors to investigate and report on the affairs of the company.
- (S447) to obtain production of company records, and in case of non-compliance or risk of destruction, to search and seize the same.

3.8.2 Under S445 shares in suspect companies may be subject to issue and trading restrictions and rights and payments arising from the shares may be frozen, whilst S446 allows investigation of dealings by directors and their families. These powers might be of secondary use in an inquiry into beneficial ownership.

3.8.3 SS82-84 of the Companies Act 1989 also give the Secretary of State wide powers for the purpose of assisting an overseas regulatory authority which has requested assistance in connection with enquires being carried on by it or on its behalf, subject to HM Treasury's confirmation that the application is from a valid authority. Such powers can also be used to look into beneficial ownership.

The Serious Fraud Office

3.8.4 The Serious Fraud Office has extremely broad statutory powers under S2 of the Criminal Justice Act 1987 to obtain information and documents for the

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purposes of an investigation into serious or complex fraud. These powers are exercised by written notice issued by staff designated by the director in any case where there appears there is good reason to do so for the purposes of investigating the affairs (or any aspect of the affairs) of any person.

National Criminal Intelligence Service (NCIS)

3.8.5 The Economic Crime Unit at NCIS is the central unit responsible for receiving, analysing and disseminating financial disclosures relating to money laundering to law enforcement authorities for investigation. It has an establishment of 60. It is not vested under the Police Act 1997 with any special powers over and above those possessed by its officers in the normal course of events.

National and Regional Crime Squads

3.8.6 The National Crime Squad (NCS) deals with serious crime and has 3 branches, each with a Financial Investigation Unit (FIU). They handle many of the disclosures made to NCIS. NCS is not vested under the Police Act 1997 with any special powers over and above those possessed by its officers in the normal course of events.

Police Forces and Constabularies

3.8.7 There are 53 police forces or constabularies in the UK. This figure does not include non-geographic forces such as MOD Police, nor does it include those forces in the Channel Islands or Isle of Man, nor does it include other bodies having a law enforcement function, such as NCIS, NCS, etc.). Under Association of Chief Police Officers (ACPO) arrangements, each of them has a unit to handle NCIS money laundering disclosures. Such units operate mainly under powers set out in the Police and Criminal Evidence Act 1984, which enable those investigating a crime or suspected crime to obtain information from companies they suspect of involvement in illegal activities and from those it has dealings with, such as banks and suppliers.

3.8.8 Orders under the Police and Criminal Evidence Act require financial institutions to disclose the information requested to the requesting enforcement authorities within seven days (this time period may in certain circumstances be extended to 14 days). The application for the order is made *ex parte*, i.e. in such a manner that the person to whom the order relates should not know who has made the request. Explanation Orders require the financial institution to explain the transaction to the enforcement authorities. General Bank Circulars require banks to disclose information (in a broader sense than that set out above) under the Terrorism Act 2000. This procedure needs the authorisation of a police superintendent or above.

3.8.9 Police forces also rely on S29 Data Protection Act 1998, Memoranda of Understanding with regulators and human intelligence sources.

Financial Services Authority

3.8.10 Where a business is regulated by the FSA, information on beneficial ownership, control or corporate structure material can be provided from the authorisation, supervision and intelligence areas of the Financial Services Authority. This information is acquired as part of the application process for firms requiring authorisation or entering into a regulatory environment and whenever a "change of controller" (or controlling share) in a regulated firm occurs.

3.8.11 The FSA may also investigate the beneficial ownership of any regulated business, and unregulated business which appears to be operating illegally within the UK, when investigating any actual, potential or suspected transgression within its area of responsibility. These powers may also be used to assist an investigation by an overseas regulatory authority.

Customs and Excise

3.8.12 HM Customs & Excise exercises similar powers to trace beneficial ownership. It works to the Drugs Trafficking Act 1994, the Criminal Justice Act 1988, the Customs and Excise Management Act 1979, the VAT Act 1994 and various Finance Acts.

Inland Revenue

3.8.13 Inland Revenue exercises similar powers to trace beneficial ownership. Powers are exercised by tax inspectors in the normal course of business, and by the Special Compliance Office, which investigates complex tax evasion schemes.

Department of Work and Pensions

3.8.14 The Department of Work and Pensions also has investigation powers under the new Social Security Fraud Act, for example to access the records of credit reference agencies in individual cases, and investigative powers under the Insolvency Act 1986, the Company Directors Disqualification Act 1986 and the Companies Act 1985. It has a special unit "BASIS" which looks at organised benefit fraud.

Use of Civil Action

3.8.15 A search order (formerly known as an Anton Pillar order) is an order of the court made without notice, granted under Section 7 of the Civil Procedure Act 1997, authorising entry of a defendant's premises and the inspection and detention of documents or items on those premises.

3.9 Problems with the current disclosure system

Forming a company

3.9.1 The UK system of direct access to company formation means there are no mandatory "gatekeepers" (e.g. regulated company formation agents, law firms and accountants) to screen new companies, other than the requirement for a Form 12 to be sworn before a solicitor or to be completed by one. Thus it is possible for criminals to form companies themselves or make use of a small number of company advisers who, knowingly, recklessly, negligently or

unwittingly, assist or collude in the establishment of companies for criminal purposes.

3.9.2 Often an intermediary will simply not have the resources to check on identity of those behind a company. Due diligence procedures, if required, would force up the price of registration of such companies from a few hundred pounds to well over £1,000 depending on the locations where due diligence would need to be carried out. Often, the client will merely give sufficient detail to establish the company and nothing more, and may instruct other intermediaries to carry out certain other aspects of the business, which means an intermediary may not have the full picture of the situation.

3.9.3 The Second EU Money Laundering Directive will subject company formation agents and other intermediaries (e.g. accountants and lawyers) to the Know Your Customer obligations of the Money Laundering Regulations. Company formation agents may be subject to a lighter touch regulatory regime in certain EEA Member States. This Directive has yet to be agreed, though agreement is expected shortly, with implementation aimed for by the end of 2002.

3.9.4 Companies House itself exercises a registry function only and does not validate new company data other than for completeness and disqualified directors, though certain postcode validation takes place. Provided these are satisfactory and the fee has been paid, incorporation is automatic.

3.9.5 Thus, from the money launderer's point of view, as well as facilitating the use of fictitious shareholders, the rules allow companies to be registered to people who, unlike fictitious shareholders, actually exist yet have no apparent link to criminal activities. In reality, however, they are under the influence of third parties.

Ownership

3.9.6 The minimum disclosure information required by law falls short (intentionally) of identifying all other people who may have an interest in a company. However, by allowing nominees to be registered as legal owners, an immediate hurdle is created to the identification of beneficial owners.

3.9.7 The barrier may be relatively low where the nominee is a UK person. It can be insurmountable where the legal owner or nominee is a foreign company in a jurisdiction where the corporate veil cannot be pierced, except by order of the court and then only to the extent that the company is prepared to divulge information. It would remain so even if full disclosure requirements were introduced, if the beneficial owner is a non-UK (registered) natural or legal person.

3.9.8 Trusts pose a particular identification problem. Professional advisers seeking to protect the legitimate confidentiality rights of their clients will utilise UK and offshore discretionary trusts to hold shares in UK companies. The

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discretionary beneficiaries of such trusts have no constitutional or other control over the shares, they have no direct or indirect interests in the share capital and are not directors. Where trustees act with absolute discretion over which individual beneficiaries shall be granted benefits and within normal professional guidelines, the discretionary beneficiaries may neither be “persons who can influence the company’s operations at will” nor the real owners.

3.9.9 Only in certain sectors, such as in the financial markets example described above, can a regulator be expected to make *ex ante* investigations regarding beneficial ownership and control.

3.9.10 The basic requirement contained in section 352 Companies Act 1985 is believed to be more honoured in the breach than the observance. This requirement is merely to keep a register of members, there being no explicit requirement to update the register, nor inform anyone of new members. Whilst annual returns may be accurate in the period soon after they have been filed, register searches thereafter become increasingly out of date. The information contained therein is not required to be validated by Companies House. Court action is required if any person is entered into or omitted from the register, or there is default or unnecessary delay in entering onto the register the fact that a person has ceased to be a member. Such court action has to be instigated by complaint of an aggrieved person, shareholder, or the company. There is no active policing of the requirement by Companies House who will only respond to complaints received.

3.9.11 Trying to establish ownership by asking to see a register of members thus has several limitations. It may be non-existent, inaccurate, or legally unavailable without an order for up to thirty days. Moreover, and more importantly, the mere act of asking for the information may tip criminals off and thus prejudice further inquiries.

3.9.12 Moreover, where a company authorises share warrants to bearer to be issued, the transfer of those shares will be valid even where the company intentionally fails to notify Companies House of the resolution to issue such securities. The level of criminal sanction faced for non-reporting will not deter the professional launderer from this course.

Control

3.9.13 As with shareholders, directors can again be nominees or companies and the same problems regarding identifying control of nominee shareholders applies to identifying who controls directors. Whilst S741(2) Companies Act 1985 requires shadow directors to be notified it is impossible to force people to declare their existence who may have no intention of doing so. The only remedy is to hold the nominee directors to account for the submission of false or misleading details.

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3.9.14 In the UK, no explicit qualifications are required to be a company officer, except for the position of company secretary to a public company. Even then a public company secretary need have no formal qualification if the directors think he or she is capable of doing the job (section 286(1)(e)). However, there are many duties and liabilities (including potential disqualification) which the law brings to bear on such officers and which in effect introduces some form of requirement for qualifications and expertise.

3.9.15 Though Companies House maintains a database of disqualified directors, it is difficult to establish with absolutely certainty if a person has been disqualified, due to the disqualified director's ability to use an alias or simply variations on their own forenames, initials and surname.

3.9.16 The problems described above in relation to inspection of the register of members also relate to inspection of the register of company officers.

Disclosure

3.9.17 Shareholder details on annual returns are filed annually by reference to the company's legal return date. Shareholder details only consist of name and address and this does not always allow for unique identification of individuals, for which an additional personal identifier (e.g. date of birth or National Insurance number) would be required.

3.9.18 Key data on Companies House forms, Annual Returns and annual accounts are not authenticated e.g. signatures and authority of company officers or accountant's identity. Civil penalties for late filing of annual accounts (introduced in 1992) have reduced non-compliance from over 50% to just 4% in 2000. There is no equivalent regime for Annual Returns, even though it is a criminal offence in both cases. The compliance regime for directors and company secretaries is even weaker. A duly registered and up-to-date company can thus have recorded out of date directors and non-existent auditors.

3.9.19 At present Companies House has a database of directors (including shadow directors whom it does not differentiate) and has shareholder data entered in field format, but it does not hold a readily available database combining shareholders and directors.

Open Record

3.9.20 Whilst knowledge of beneficial ownership may be of interest to the general public, placing information on individuals' names and addresses has led to policing problems, such as in the case of Huntingdon Life Sciences (HLS). It is very likely that public domain information was used by activists to locate and attack individuals associated with HLS and their property. Thus the very concept of public registers has come under scrutiny. Shareholders may, however, currently use any address. Matching ownership would therefore require a relational database which supports cross-referencing by a wide number of fields, such as those offered by credit reference agencies.

3.10 Problems with investigative powers

3.10.1 Information on beneficial owners may assist law enforcement in many different respects, but principally by:

- providing intelligence (trying to identify criminal activity)
- assisting investigation (of suspected criminal activity)
- facilitating evidence gathering (to lay charges which will stick, convict perpetrators and recover the proceeds of crime)

3.10.2 At present, the difficulties faced by company investigators and law enforcement officials mean that a significant proportion of police time and effort in reduction of financial crime and money laundering is wasted trying to identify beneficial owners. Not only is information hard to come by but hard to come by at an early enough stage when its value is greatest. Information gleaned under the various powers set out above may therefore be useful in the evidential phase, but of no use earlier on at the intelligence gathering and investigation stages. Worse still, many cases are dropped (sometimes after considerable time and expense) simply because the trail leads to a beneficial owner who cannot be identified.

Particular problems with investigations under the Companies Act

3.10.3 Whilst the DTI has wide powers to launch investigations, they can be costly in terms of time and money. DTI currently has an investigation department of 60 staff. This number has fluctuated only slightly over the last few years. With over 24,000 NCIS disclosures in 2000, it would be difficult for the DTI investigations branch to undertake S442 investigations on all the companies involved without a substantial increase in resources. In the year 1999-2000, DTI undertook one S432, and no S442 or S444 investigations. This may well be because the DTI's investigative powers focus on the company not the individual, and unless the connection between the two can be made the powers are of little use.

3.10.4 Whilst S447 inquiries (by far the most common undertaken – 167 in 1999-2000) are usually meant to be completed in three months, section 432 and 442 inquiries may take longer. Section 447 inquiries also have to be conducted so as to avoid the risk of harming the company.

3.10.5 These limitations can restrict the efficiency of S447 enquiries, as questions to third parties regarding beneficial ownership cannot be asked without a risk of detrimental effect on the company. A company can use the same argument to drag out the investigation process whilst covering its tracks or even continuing to commit crime. Moreover an investigation is not always made public and information it produces is confidential and can only be revealed in certain circumstances to outside regulatory and professional bodies (S449). The confidential nature of the process, whilst protecting the innocent, diminishes its deterrent effect.

3.10.6 Where matters in an investigation suggest that a criminal offence has been committed, referral must be made to the prosecuting authority. All these steps may delay the discovery of beneficial ownership or control and certainly will have flagged the interest of the authorities to the company concerned.

Investigations under other powers

3.10.7 As with the Companies Act, use of other powers may not always produce the desired results in terms of obtaining details of beneficial ownership. Information requested may not be held by the company concerned or may be useless by the time it is retrieved. The length of time records are kept by companies is falling despite legal requirements to the contrary.

3.10.8 Exercising the powers may also be counterproductive in that the company may find out, directly or indirectly, that it is under suspicion and sue the person providing the information to the authorities.

3.10.9 Law enforcement authorities sometimes have problems in getting certain of their powers (e.g. to obtain intelligence, investigate or collate evidence) to work because the powers are cumbersome or hard to use with the precision and discretion needed for full effect. Lack of training in how to use powers, lack of information sharing (particularly cross border), lack of resources and low priorities given to white collar crime are also cited as reasons why enforcement in this area is weak.

3.10.10 There is also great frustration that current powers allow little scope for action against the handful of corrupt company advisers who help set up false front companies, and without whom the underlying criminals would have great difficulty in operating.

Quality of Information

3.10.11 Private registries are also that their own databases, which often rely on Companies House data, need further checking. This involves further cost to them and to clients. Businesses will often therefore decide against conducting proper due diligence due to the costs involved. As private registry data is used for credit scoring purposes, this has much wider implications for the rest of industry in terms of cost of credit and loss experience. Awareness of the capability of credit reference agency information systems does not appear to be as great as it might

be among some enforcement agencies. This may be both the cause and effect of the lack of money and resource available for using such systems, even though cost of individual searches is low.

3.11 International considerations

3.11.1 The UK is in the forefront of developments in international initiatives on money laundering deterrence, not least the EU's proposed Second Money Laundering Directive. It has long supported OECD initiatives, the FATF Forty Recommendations, United Nations, Council of Europe and Commonwealth initiatives and has been held up by the FATF as a model for other countries. The UK is also actively involved with the G7, G8, Basle Committee on Banking Supervision, IOSCO, IAIS and Financial Stability Forum, especially its Off-shore Financial Centres working group. The UK also has responsibilities in relation to the Crown Dependencies and Overseas Territories. It has been seeking to ensure they meet international standards of regulation and best practice, as evidenced by, in particular, the UN Report, the Edwards Report, the KPMG Report on Overseas Territories and the recent OECD Report on Misuse of Corporate Vehicles. By these means, HM Government is showing its determination that such territories shall not be used for moneylaundering.

FATF

3.11.2 The FATF 1998-99 Annual Report noted that problems in obtaining information from certain jurisdictions on the beneficial owners of shell companies, international business corporations and offshore trusts were the primary obstacles in investigating cross-border money laundering.

3.11.3 The FATF 2000-01 Annual Report typologies section focused, *inter alia*, on trusts, other non-corporate vehicles, lawyers, notaries, accountants and other professionals. From the FATF examination it became clear that the concern of the anti-money laundering authorities is the seemingly impenetrable anonymity which a trust may provide to the true owner or beneficiary. This anonymity is enhanced by the fact that documentation of trusts is not public information. Certain types of trust appear to be more misused than others, such as the blind or black hole trust and the asset protection trust, perhaps enhanced by "flee clauses" and may therefore warrant specific action to address their use. Other possible solutions range from establishing a strict regulatory regime for trust formation agents (subjecting them to licensing, customer identification, record keeping and reporting requirements), to imposing some sort of public or semi-public registration requirement on trust creation.

3.11.4 The FATF is likewise concerned that lawyers, notaries, accountants and other non-financial professionals often play the role of gatekeepers. Professionals have the ability to create corporate vehicles, trusts and other legal arrangements that facilitate money laundering. Moreover, professional confidentiality, which has traditionally applied to the relationship between the lawyer and the client for advocacy purposes, also extends to other non-advocacy "gatekeeper" functions. This makes the use of these professionals attractive to

those individuals wishing to hide assets or launder money. One solution is to include these professions under the same or similar money laundering deterrence obligations as financial intermediaries.

3.11.5 Other international initiatives include the Council of Europe Action Plan on Transnational Organised Crime 1997, which emphasised the need for data exchange between countries. This was echoed by the UN which also noted that the principal forms of abuse of secrecy have shifted from individual bank accounts to corporate accounts and then to trusts and other corporate forms.

3.11.6 The October 2000 ECOFIN meeting called for further work on developing mechanisms to identify the beneficial owners of legal entities. This built on the EU Action Plan to Combat Organised Crime 1997 which called for Member States to collect information on the physical persons involved in the creation, direction and funding of legal persons registered in their countries.

3.11.7 Another EU backed initiative is the European Business Register (EBR), providing input on ten countries, but not yet including the UK. By creating and making available to other countries a standardised database on businesses, their directors, shareholders and controllers (the very system covered by the options under review here) the UK would at least meet in part the criteria set out in the EBR.

Private sector

3.11.8 In the private sector, international financial institutions are also reflecting these developments, as the recent release of the Wolfsberg principles shows. The proposals under review would reinforce measures being taken at national level and at operational level (e.g. Egmont Group), which are of use in overcoming the barriers to law enforcement posed by bureaucracy, language, culture, lack of resources and differential powers. Likewise, the Asser Institute report on Prevention of Organised Crime concluded that the ability of legal entities to conceal the identity of their beneficial owners stimulates their use for criminal activities.

3.11.9 Whilst the UK regime has been praised for its business friendliness and pragmatism in attracting foreign companies to establish themselves here, it also has its critics at home and abroad. Indeed, centres once considered disreputable by UK standards now have stricter company regulation, in certain respects, than the UK (see, e.g. the Jersey and Bermudan laws on beneficial ownership). Thus the current system raises issues of how to balance the interests of the national economy and international leadership.

4. CURRENT PROPOSALS

4.1 *The five options*

4.1.1 HM Treasury and DTI have identified a range of five options to be assessed to meet the PIU Report conclusions with regard to disclosure of beneficial ownership, filing and publication. In addition, the TOR of this RIA requires assessment for all five options of *"the cost and benefits of placing the information disclosed on a register open to the public"*. The options are set out in tabular form in Table 1 and discussed in detail in this section.

4.1.2 For all options described it has been assumed that, in line with Part VI Companies Act 1985:

- the shares in question are those of a class carrying rights to vote in all circumstances at general meetings of the company, and that
- changes in percentage are by reference to the issued capital of the company.

4.1.3 In terms of the disclosure requirement, it is envisaged that legal owners would not be under a duty to disclose the identity of the ultimate beneficial owners of their shares, which they might not know. Instead, they would be asked to disclose the identity of the person "next in line" i.e. exercising immediate control over them. Such disclosures could then be compared with other disclosures, including any by the "next in line", allowing discrepancies to be followed up. The "next-in line" would either need to show that the initial declaration was false, or disclose in turn on whose behalf they were exercising influence. By means of this iterative process, investigators would have better powers to home in on the core behind complex corporate veils.

4.1.4 Further details about the workings of each option are set out below. The options are cumulative and therefore each section addresses only the extra considerations relevant to that option.

4.2 *Option 1a*

"A person should be obliged to disclose to a private company if they hold a beneficial interest in an unspecified percentage of that company's shares which is more than 3%. Such persons should also disclose to the company when their beneficial interest drops below the 3% threshold. This information should be held by the company and made available on enquiry to law enforcement and regulatory authorities."

4.2.1 This option applies primarily to beneficial owners of private companies. As set out above, persons with an interest in public companies already have to disclose such an interest within two days on a much stricter movement basis and with a wider definition of beneficial interest.

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4.2.2 It is necessary to consider both the form of disclosure required from the beneficial owner, and the form of holding and making available disclosures received. At the very minimum, beneficial owners would need to provide a one line statement describing their shareholding, and the company would need to store all such disclosures where they could be found within a reasonable time limit.

4.2.3 An alternative approach tracking arrangements for legal owners of public company shares would be for the company to be sent a formal notice akin to the DTI's recommended Form 212 disclosure consisting of name, address, number and class of shares beneficially owned and details of any agreement and arrangements under S204.

4.2.4 These details would then be entered by the company in a subsection of the register of members which it is already required to keep under S352 CA 1985 and open to inspection by the public at its registered office or other location notified to Companies House, as well as via Companies House itself. Provision would need to be made for intermediaries (lawyers, accountants, company formation agents and registrars, etc.) to submit the same information.

4.2.5 For both of the above options the beneficial owners or their agents would need details of the company's share structure to be able to ascertain if they were above or below the threshold. Capital structure would be seen every year from the Annual Report but changes in structure during the year might be harder to monitor where the legal owner did not pass on details of, for example, any rights issues or stock splits.

4.2.6 Complex share structures might make it difficult to calculate percentages, but the general assumption is that a shareholder or its advisers should know or want to know such details in the course of the routine management of its investments.

4.3 Option 1b

"In addition to the above, persons holding beneficial interests above the 3% threshold should disclose to the company at the outset the percentage of the company's shares in which they have a beneficial interest, and disclose on an annual basis to what extent their beneficial interests have changed. This information should be held by the company and made available on enquiry to law enforcement and regulatory authorities."

4.3.1 This option again applies primarily to beneficial owners of private companies and is still less strict than the regime for public companies. It allows the extent of beneficial ownership to be established by a private company once the beneficial interest is acquired and monitored annually thereafter.

4.3.2 As with Option 1a, disclosure could be very simple - as for Option 1a, but with an additional yearly disclosure. Where there was no change it might not

even be necessary to make a disclosure, provided it was made clear that a non-return was equivalent to disclosing no change. The same record-keeping and percentage calculation considerations apply as for Option 1a.

4.4 Option 1c

"In addition to the above, persons holding a beneficial interest above the 3% threshold should disclose to the private company, within a specified period (such as two days), each time that their holding rises by one percentage point. This information should be held by the company and made available on enquiry to law enforcement and regulatory authorities."

4.4.1 This option, which again applies primarily to beneficial owners of private companies, allows the extent of beneficial ownership to be monitored by a private company on a continual basis. Save for the definition of beneficial ownership, it tracks closely the regime for public companies (indeed it may be that the same distinctions regarding holdings by investment vehicles in public companies should apply here).

4.4.2 The option only requires disclosure of rises of 1%, whereas notification of both rises and falls would be necessary to monitor the extent of beneficial ownership accurately between yearly reporting dates established under Option 1b. Otherwise, the same observations as with Options 1a and 1b apply to this option.

4.5 Option 2

"In addition to the above, information on beneficial interests exceeding the 3% threshold held in private and unlisted companies should be disclosed by those companies to Companies House via annual returns. This notification made by the company to Companies House should give the name of each beneficial shareholder and the percentage of their shareholding. This information should be made available on enquiry to law enforcement and regulatory authorities."

This option to private and unlisted companies the same duty to report beneficial interests to a regulatory reporting point - here Companies House - as affect public companies under Part VI Companies Act 1985

4.5.1 As specified in the TOR, and unlike notification of legally owned shares which starts at one share, this option starts at the 3% threshold. It only requires the name of a shareholder to be submitted to Companies House, not the address as required when notifying legal ownership of shares, e.g. in Form 353. To make this option workable it has been assumed that a principal residential address is also supplied.

4.5.2 Where legal owners are also the beneficial owners, a simple additional box tick question in Section 4 of Form 363s would enable the facts required under this option to be established. Otherwise, names of beneficial owners and their percentages could be entered under Section 5 of Form 363 (with or without slight modifications). As shareholder details are checked every 1-3 years, only changes

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in beneficial ownership or in the details of beneficial owners would involve extra work by the company.

4.5.3 Alternatively, notification could take the form of a simple hard copy or electronically filed list with the same data.

4.5.4 It is assumed that processing beneficial ownership data would simply entail extending the processing to which an Annual Return is already subject at Companies House. For the most part this would consist only of checking a few additional boxes, with occasionally the need to enter extra shareholder details. Accordingly, training would be required by Companies House staff. There might be a small rise in the number of forms to be rejected as a result of failure to enter details of beneficial owners to Companies House standards. These are discussed under *Section 6. Costs* below.

4.6 Option 3

"In addition to the above, all changes in legal share ownership and in beneficial interests exceeding the 3% threshold should be disclosed to Companies House as and when they occur rather than via annual returns. Disclosure should be made when ownership changes by at least one percentage point. A time leeway should be introduced to avoid unnecessary reporting whilst changes in legal ownership are being cleared and settled. This information should be held by the company and made available on enquiry to law enforcement and regulatory authorities".

4.6.1 This option applies only to private and unlisted public companies. It would enable changes in the legal and beneficial ownership of such companies to be monitored as they occur. The time leeway for clearing and settlement would need to be at least 14 days to allow for postage processing and a margin of error.

4.6.2 Upon receipt of notification on the basis of Option 1c above, the company would need to forward the document to Companies House (if it was in a set format) or transpose the information supplied onto an electronic or hard copy form similar to Section 5 of the S363a Annual Return to Companies House. Companies House would then log the details in its computer.

4.6.3 Using c. 500,000, the number of stock transfers submitted in hard copy to Inland Revenue, as an estimate for private company share transfers (not all stock transfer forms attract stamp duty), were they all hand-entered then Companies House would need to process on average upwards of 2,500 share transfers a day. This amount would be the equivalent of a 10% addition to Companies House' daily document processing total, and would be a new document for them to process.

4.7 Option 4

"In addition to the above, Companies House should establish a modern database which allows the name of a person to be inputted and then reveals which shareholdings and beneficial interests that person holds. This information should be held by the company and made available on enquiry to law enforcement and regulatory authorities."

4.7.1 Option 4 applies to all companies. It entails Companies House establishing a database capable of supporting two-way inquiry (companies associated with names and vice versa) on the legal and beneficial ownership of all shares.

4.7.2 Such a database could be built up using:

- the data Companies House currently holds
- allotment data submitted on Form 88
- transfer data submitted under Option 3 (from Form 363a)

4.7.3 As data would already be in electronic format from work under previous options, it would only be necessary for Companies House to validate the format (e.g. data submitted in electronic format), code the inquiry applications and provide relevant links.

4.7.4 The main assumption here is that shareholder names are entered in a consistent way that uniquely identifies the person concerned, or which lists all similar names. Address, postcode and date of birth may help in this respect and it has been assumed that shareholder details can be entered consistently by using these details.

4.8 Option 5

"In addition to the above, this modern database should allow the name of a person to be inputted and then reveal which directorships and shadow directorships that person holds. This information should be held by the company and made available on enquiry to law enforcement and regulatory authorities."

4.8.1 Companies House already maintains a database of company directors, including shadow directors. This option foresees a one-stop shop where all aspects of ownership and control can be established. It would entail extracting data from the existing directors database and the new shareholder database

according to simple search parameters, and merging it in an on-line or hard copy report format.

4.8.2 The main assumption here is that directors' names are entered in a consistent way that uniquely identifies the person concerned. Unlike shareholders, directors also have to provide details of nationality and their date of birth. We have assumed these are also search parameters.

4.9 register options

4.9.1 As stated, the TOR of this RIA requires assessment of "the cost and benefits of placing the information disclosed on a register open to the public". There are two sub options:

- *First, that the register should be held by the company (this would apply to options 1a, 1b and 1c).*
- *Secondly, that the register should be held by Companies House (this would apply to the other options 2,3,4 & 5)*

4.9.2 For Options 1a-c, we believe the proposal would be met by simply requiring the existing register of members to be suitably updated, with a clear distinction made between legal and beneficial ownership.

4.9.3 For Options 2-5 we consider this requirement to be met by making the details stored in this option available in the same way as annual accounts and Annual Returns are made available.

4.10 Other considerations

Government information campaign

4.10.1 It is assumed that the government would make known the duty to report beneficial ownership from time to time, using a range of instruments to inform companies, shareholders and intermediaries, and explain the requirements and how to report suspicions.

Other initiatives

4.10.2 The options described above are not the only proposals currently affecting the question of money laundering. Parallel initiatives include the Proceeds of Crime Bill and the establishment of the new Civil Asset Recovery Agency, the new Computer Crime Unit, and the Partners Against Crime initiative (though we understand that there was no referral from the public to the private sector in the latter's first year of operation). The effect of the Proceeds of Crime Bill in particular will be to consolidate important aspects of money laundering legislation. A major review of company law has just been completed.

Enforcement

4.10.3 The role of establishing beneficial ownership in tackling money laundering is a crucial one these proposals are seen more as criminal than company law

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initiatives. Tipping off and failure to disclose are key 5 year offences in the Proceeds of Crime Bill and there is a strong case for including failure to disclose beneficial ownership with intent (or recklessness or gross negligence) to launder as a third such offence. A key issue discussed in the assessment of costs and benefits below is therefore the nature of the enforcement regime for the proposed regulation, 5.18 Sensitivities below. Enforcement would not be the responsibility of Companies House (or the DTI), but of the agencies which investigate financial crime.

5. BENEFITS

5.1 Methodology

Consultees

5.1.1 As the proposals have a wide potential impact we consulted a wide range of experts, most of whom we engaged in a detailed informal dialogue. The organisations represented included government departments and agencies, law enforcement, regulators, industry bodies, private sector firms, and academics (see Appendix 1 for the full list).

Recovery benefits

5.1.2 We wanted to establish who would benefit from the various options and how the proposals would help to improve recovery of the proceeds of crime. Regarding the marginal value of each option to the recovery process, we asked interviewees how each increase in the amount, frequency and accessibility of information on company ownership and control would help, how the information might be used and what effect this would have.

5.1.3 To identify any other critical factors that would help improve recovery rates, we asked interviewees if there were any other unmet needs or concerns linked to disclosure of beneficial ownership and control, for example regarding the level of detail on individuals required, ownership thresholds, timings, inquiry systems and enforcement considerations. Some of this information was also used for the sensitivity analysis (see below).

5.1.4 Those engaged in civil recovery were asked similar questions, with special emphasis on the value of record.

Other law enforcement benefits

5.1.5 As the information gathered under the options would be available for purposes other than recovery, we also asked what these processes might be and what benefits might accrue from information on beneficial ownership and control being available. Specifically we asked if there would be any benefits in deterrence and prevention of crime and securing the conviction of criminals, as all these activities share the same ultimate goal as asset recovery, namely reduction of crime. As with recovery, we asked if there were any other critical factors that would improve the effect of the options in these areas.

International obligations

5.1.6 Analysis of benefits with regard to international obligations was based on comments by policy officials and comparison of the UK's position with relevant international standards.

register

5.1.7 To identify the benefits of an open, as opposed to a semi-open or closed register, we asked law enforcers and industry representatives which option they preferred and why. Access to information about beneficial ownership and control also affects decisions to enter into business relationships and/or extend credit to clients. We therefore asked banking representatives and credit reference agencies how they might use such information and what benefits might accrue to industry in general, and to the clients of credit reference agencies in particular.

Sensitivity analysis

5.1.8 We asked respondents what impact changes to key parameters disclosed would have (e.g. level of detail and timing of data). We also asked respondents how they thought recovery and other important processes supported by the proposals would be affected by evasion of the obligations, and what form this evasion might take.

5.1.9 As HMT and DTI expressed concern that the proposals should be enforceable we asked for comments on the minimum level of enforcement regime that would have the desired effect. On the basis of initial responses, specific comments were sought on the creation of a serious arrestable offence where money laundering was suspected.

5.1.10 The full sensitivity analysis is to be found at 15.18 below.

Assumptions

5.1.11 In assessing benefits, both generally and for particular options, it has been assumed that:

- reporting and recording beneficial ownership and control is carried out along the minimum lines set out in Section 4
- no verification of forms submitted to Companies House or routine checks of company registers is undertaken (as with the current base case)
- Annual Returns are due within 30 days of an annual legal return date (except Option 1a where no annual obligation applies)
- individuals and companies failing to make a declaration/return on beneficial ownership or control or making a false or misleading declaration /return *in benign circumstances* would face civil penalties
- where there was *intent, recklessness or gross negligence* to launder or assist with laundering, the same transgressions would be serious arrestable offences with a maximum sentence on indictment of five years' imprisonment
- no 'smurfing' takes place, i.e. thresholds (if introduced) for declarations of beneficial ownership are not avoided by setting up a series of beneficial owners each holding an amount below the threshold.

5.2 Beneficiaries

5.2.1 Many experts in both public and private sectors agreed with the view expressed in the PIU Report that many large money laundering schemes (in

excess of £100,000) involve private companies, or thought that the use of private companies is a serious option for money launderers to consider. They were able to cite specific examples of past cases and allude in general to cases currently under investigation. Being able to determine the real owners or controllers (alleged or otherwise) of such companies is a major obstacle to recovering assets and thus proposals for a duty to disclose beneficial ownership and control were welcome.

5.2.2 Responses suggested there is a wide range of potential beneficiaries and four groups were thought to benefit in particular:

- criminal law enforcers engaged in asset confiscation or other investigations
- civil law experts engaged in asset recovery, and within industry as a whole
- credit reference agencies and their clients as well as those engaged in prevention and deterrence, and
- those undertaking KYC and due diligence as part of money laundering identification and verification procedures and compliance with other similar regulation.

Law enforcers engaged in confiscation

5.2.3 It is difficult to determine precisely the number of people in this group and thus the number of potential beneficiaries. Whilst the PIU Report estimated there were 1,700 financial investigators working in the police, NCS, NCIS, SFO, Inland Revenue, DWP and DTI, information received in the course of this study suggest there are now nearly 1,600 financial investigators in the police alone.

5.2.4 Moreover, just as not all financial investigators work on confiscation (about one in three in the case of the police) not all those working on recovery are financial investigators. Whilst the DWP is only cited by the PIU Report as having three financial investigators, it has 2,600 investigators overall. Likewise, qualified financial investigators account for just under 10% of the 2,000 strong Customs & Excise National Investigation Service. The DTI has approximately 60 staff engaged on Companies Acts and Financial Service Act investigations more generally (as opposed to specialised money laundering investigations and beneficial ownership enquiries).

5.2.5 Inland Revenue is cited as having 103 financial investigators, but the number of staff working on dedicated non-compliance, evasion and special investigation teams that may lead to the identification and recovery of unpaid tax liabilities varies according to the nature of strategic initiatives targeting high risk areas. 2,000 staff were involved in the Save and Spend programme in 1999/2000. Thus, nationwide in these key institutions alone, as many as 7,000 specialist staff may be potential beneficiaries of the proposals.

5.2.6 Those interviewed suggested units engaged in the numerous middle-sized operations (which constitute the bulk of routine confiscation cases) would benefit in particular. These include police FIU's, HM Customs & Excise special

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investigation units, and tax inspectors whose current powers are limited or restricted to a specific purpose, e.g. establishing a tax liability.

5.2.7 However, even though large-scale recovery cases tend to be handled by specialist units with superior powers to obtain information, it was thought that the proposals would ultimately benefit specialist units as well. The examples of such units are SO6 and SO12 (Metropolitan Police), Special Compliance Office (Inland Revenue), BASIS (DWP's organised crime unit), as well as HM Customs & Excise which recently made interception of drugs money a key part of its current strategy.

Law enforcers in other investigations

5.2.8 Many respondents thought the proposals would also be generally useful to law enforcers working in the criminal intelligence, crime prevention and investigation areas, for example by helping to find money being accumulated for serious criminal purposes or terrorist purposes, using a corporate front. Likewise, HM Customs and Excise, Inland Revenue and DWP inspectors conducting routine investigations into duties, tax and benefit irregularities would find routine if low-grade use for a beneficial ownership database. The number of potential beneficiaries in this group is clearly a multiple of the 7,000 specialist staff identified above.

Civil experts engaged in recovery

5.2.9 The third group comprises private sector firms and individuals engaged in civil recovery. Many of the larger accountancy and law firms are engaged, to a greater or lesser degree, in the recovery of assets on behalf of clients who have been the victims of crime or other irregularities. Such clients, as the PIU Report points out, prefer the civil recovery as opposed to the criminal proceedings route as it is the former that focuses on recovery of their assets. The latter focuses on arrest and imprisonment of the perpetrator. A number of smaller specialist investigation firms play a significant role in this area, and there is an active second tier of around 130 debt collection agencies with over 22,000 full and part-time staff.

Credit reference agencies and their clients

5.2.10 The fourth group comprises private sector firms who provide data to help identify and assess the creditworthiness of potential business partners. It also includes the clients of such companies - potentially all financial and other institutions subject to the Money Laundering Regulations, and all firms offering to supply goods or services on credit. It also includes firms and individuals who need information on the reliability and wider connections of business partners, lest they unwittingly deal with disreputable or competing counterparties, or otherwise in breach of the law.

5.2.11 Thus the range of potential beneficiaries extends well beyond law enforcement to encompass much of UK industry. How it does so is explained in the next section.

5.3 Asset recovery benefits

5.3.1 Successful recovery of the proceeds of crime depends on being able to identify and locate assets and link them to criminal activity or civil wrong. This will involve reconstructing a chain of transfers and possession, involving multiple natural and legal persons and transactions. Without this evidence, courts can neither freeze suspect assets, nor seize them on conviction of those responsible for the crime and/or laundering proceeds or proof of the civil case.

5.3.2 Enforcement officials were unanimous in their view that the and inquiry systems resulting from these proposals would help in the recovery process by establishing more quickly, easily and comprehensively, links between individuals and companies, as well as the real or alleged identity of other persons associated with those individuals and companies. Either by itself, or in combination with other evidence, data on beneficial ownership would help to eliminate innocent parties from enquiries, focus attention on suspicious behaviour and even provide direct evidence of the ownership or control of an asset or activity. Four primary benefits were highlighted. These benefits could be evaluated in terms of intelligence, assistance to investigation and assistance in building the evidential case.

Primary recovery benefits

5.3.3 First and foremost, access to a single system showing all the corporate connections of a given individual – legal and beneficial – would produce economies at the operational level in terms of shorter investigation times and thus more investigation capacity. Importantly, by enabling key information to be available at the time an investigation was planned, more and more complex investigations could be attempted with a greater chance of success. In short, provided the proposals resulted in a sufficient degree of disclosure of readily useful information they would open the way to ordinal improvements in recovery resource allocation decisions.

5.3.4 Secondly, the proposals offered the prospect of more timely and relevant information. Whilst units working on old cases where proceeds had come to rest (i.e. in property or other assets) might be able to use data collected annually, those working on fresher cases or closing in on trails need as up to date information as possible as some of the options offered. This is especially the case where, for example, assets and individuals were about to leave the country and an application to freeze assets and arrest individuals needed to be made. Russian money laundering schemes, for example, are felt to be relatively ephemeral, planned to last for a maximum of 18 months. To combat such operations, information on beneficial ownership and control would need to be provided on a timely basis.

5.3.5 With regard to the level of detail and relevance, consultees thought that the degree of beneficial ownership that needed to be disclosed would vary according to the purposes for which the information was required. For obtaining initial evidence, proving or disproving connections between individuals and companies, disclosure of the mere fact of beneficial ownership may be sufficient to pursue other forms of inquiry. However, much higher levels of detail are needed for evidential purposes, for example to prove a controlling interest (the FSA uses a 10% threshold) or to link a cash flow to the purchase of a specific degree of interest in a company. Again, some of the options offered this higher level of detail. This also depends on the type of case being pursued. For example, criminal cases need proof beyond all reasonable doubt, whereas civil cases require proof of an outcome on the basis of a balance of probabilities.

5.3.6 Thirdly, by allowing more data on individuals to be collected, the proposals would help to identify legal and beneficial owners more accurately than at present or at least force criminals into more easily checked statements. The minimum data needed in addition to full name and home address are postcode and date of birth.

5.3.7 Fourthly, the proposals opened the way for additional officially collected data to be linked automatically to other systems, especially those in the private sector held by credit reference agencies, which are often consulted by those units which can afford them. The extended information and user-friendly inquiry mechanisms thus enabled would allow totally new approaches to investigation, as well as an extra form of routine screening.

Secondary recovery benefits

5.3.8 In addition to primary recovery benefits attributable to new data and systems, interviewees also identified secondary benefits which might result from the proposals. By applying to intermediaries legislation to make the provision of false or misleading statements a new serious arrestable offence (as envisaged in the latest OECD initiatives), lawyers, accountants, company formation agents and other company service providers who help establish and maintain suspect businesses would be less likely to co-operate with criminals and more likely to co-operate with enforcement officials.

5.3.9 Moreover, even if the underlying crime, a handling or a money laundering charge could not be proven, the unwary criminal or intermediary might still be convicted of the new offence. The consensus was that the combination of more effective recovery, denial of technical resources and raising the risk stakes would create a virtuous circle, leading ultimately to deterrence of crime being committed in the first place.

Assessment of arguments for benefits

5.3.10 Whilst there is no study which proves conclusively that confiscation or recovery deters crime, the arguments for secondary benefits are supported by literature which suggests that criminal risk-reward assessments are similar to

legitimate ones. Not unreasonably, given the sophistication of large schemes, current policy assumes that those involved in money laundering are rational actors and will not take part in schemes where the risks outweigh the rewards. A major tenet of current crime reduction policy is that by driving up the risk of facilitating a crime, the cost of committing crime will become prohibitive as accomplices demand higher risk premia. The conclusions usually drawn from such arguments are that criminals will abandon crimes entirely, delay them until cheaper schemes are found locally, or take advantage of cheaper opportunities offered by offshore schemes.

5.3.11 Given that, in comparison with the UK, the cost of laundering through other offshore centres is increasing, thus reducing the alternatives available, it is quite possible that the benefits of the proposals will make it harder to accumulate funds for crime and from crime. This meets two key crime reduction messages in the PIU Report.

5.3.12 The same arguments which apply to law enforcement confiscation activity also apply to civil recovery procedures. Were civil enforcers to have access to the data available under the proposal they would be able to undertake more efficient and effective civil proceedings in a wider range of circumstances. The nature and timeliness of data required by civil investigators is very similar to that required by law enforcement officials, though focusing more on the assets than the perpetrator.

5.3.13 One advantage here is the lesser burden of proof required, as mentioned above, the burden of proof in criminal cases being beyond all reasonable doubt, as against the burden of proof in civil cases being on a balance of probabilities. The value of the system is evident from the fact that whilst this group currently receives significant income from establishing the same information the proposed system would provide, many of them welcomed the proposals on account of the increase in recovery rates made possible.

5.4 Wider law enforcement benefits

5.4.1 Experts emphasised how the ultimate objective of recovery, reducing crime (especially terrorism, large-scale organised crime and drug trafficking), is also shared by other law enforcement processes. Three key areas are deterrence, prevention and arrest, and in all three the proposals were thought to assist by providing additional and more up-to-date intelligence on suspicious actors and activities and providing additional powers. The proposals are thus particularly timely for anti-terrorist units, HM Customs & Excise (which recently promoted intelligence to a core function), and DWP (where the Fraud Intelligence Unit, established after the Scampton report, is taking an increasingly intelligence-led approach).

5.4.2 In addition to the benefits described under asset recovery, other ways in which the information might help included providing an early warning or evidence

of the presence of a person in a particular place, or the acquisition of assets. From Option 3 onwards, the proposals opened the way for a database which might be easily further primed to flag transactions involving key individuals shortly after they occurred. This important, relatively cheap and simple additional function is discussed under Section 7 Alternatives, below.

5.4.3 Specialist units emphasised a precondition for this benefit to accrue would be timeliness of data. The intelligence of greatest value is "lead intelligence", which enables counter measures that deter crime e.g. by making it prohibitively difficult (placing the target assets out of reach), too risky (increasing security), or by enabling arrest on suspicion.

5.4.4 Similarly, only an up-to-date system would support the prevention of crimes currently being executed, especially complex frauds where connections between individuals need to be established, e.g. to prove conspiracy. The need for timely information was also important in combating terrorism, where the window of opportunity for reaction once a criminal presence or move has been established might be small.

5.4.5 The system might also help to convict known criminals simply by capturing their details. With law enforcers checking data for a wider range of purposes, the chance of coming across a wanted person or fortuitously establishing a link to crime would increase.

5.4.6 Law enforcement benefits are summarised in Table 2.

International standing

5.4.7 Policy officials thought that the measures would send a clear signal internationally of the UK's intention to prevent the abuse of corporate vehicles for illicit purposes. Options 3, 4 & 5, with their ability to provide information within the normal lifetime of schemes, would show the UK's commitment to the deterrence and prevention of money laundering, as well as helping to raise standards internationally by setting an example.

5.4.8 The proposals may also have a foreign policy premium in assisting to open up certain of the jurisdictions on the FATF blacklist, and those close to being blacklisted, as well as improving control over the dependent and overseas territories. By implementing a system close to international best practice (e.g. Asser Institute Recommendations), the UK would once more set a major benchmark for reducing crime. It would also have the benefit of complying with international best practice, as set out in the OECD report, etc.

5.5 Benefits to industry

5.5.1 Industry representatives highlighted potential benefits to business generally under the open record options in terms of better decisions and higher business confidence.

5.5.2 The proposals would correct information asymmetries by providing more information on companies and those connected to them, and generate further economies by providing it in a user-friendly fashion. As a particular result, credit decisions by banks and companies would more accurately reflect underlying risk. This would improve the profitability of extending credit as well as putting downward pressure on its cost.

5.5.3 Both of these benefits would be of particular value to small companies for whom establishing credit standing (either their own or that of key suppliers and clients) is proportionately greater and more critical than for larger firms with less vulnerability to bad decisions.

5.5.4 A further benefit to companies where both legal and beneficial ownership details were held on open record would be not having to answer repeated requests for standard information. Whilst some register inspections might still take place, it would be possible for companies to refer most inquirers to the open record. The more comprehensive and up-to-date the open record, the fewer requests for data and updates a company would have to handle. Creating a centralised and easy point of reference would also reduce costs for inquirers. In hard cash terms, savings would come from reductions in fraud and fraud insurance premia, bad debts, loan losses, borrowing charges and reduced company running costs.

5.5.5 The proposals would also be of value to those who have to check identity and credit standing in detail for legal reasons such as meeting FATF based client identification requirements, and financial institutions that must regularly review counterparty credit standing in detail to meet banking supervision requirements. In the UK, several million accounts are opened annually, all of which require more or less complex customer identification procedures to be undertaken.

5.5.6 Within a company, knowing the full extent of those involved in a company would provide internal benefits for companies and their members, by enabling shareholders to make more informed share transaction and voting decisions, and allowing managers to make better management decisions in their shareholders' interests. A further benefit of open record is that either party could obtain information without having to inconvenience or alert the other party unnecessarily.

5.5.7 Industry representatives generally agreed with the argument that these benefits are in addition to the safer environment created for business by the proposals, which would result in less direct and (often overlooked) opportunity

costs from crime, as well as more chance of recovery and downward pressure on insurance premia.

5.6 Open (Public) register

5.6.1 Our interviews highlighted both financial and non-financial arguments for and against an open register with regard to both improving asset recovery and wider uses. This section focuses on the high level arguments.

Recovery arguments in favour of open register

5.6.2 The major benefit of an open register in asset recovery is that it allows credit reference agencies to link beneficial ownership data to other information they hold on individuals and companies. This in turn enables name-based searching of wider databases, with the possibility of fuller lists of legal and beneficial corporate interests and more links to associated information. Without access to the open register detail, the credit reference agencies cannot construct the wider databases or make the wider links.

5.6.3 A further advantage of open register is that it facilitates recovery investigations of a company and its legal and beneficial owners without raising suspicions. Where it avoids, or at least provides a plausible excuse for, the need to inspect a document at a company's offices, an open record would reduce the risk that criminals would be alerted to an investigation closing in on them. As described in 5.4 above, this in turn reduces the risk that individuals and assets are moved on.

5.6.4 Civil recovery efforts would only be improved under open register options giving the same access as law enforcement officials and regulators enjoy under the closed record option. Without such access, they would be no better off and the government's aim of making better use of private sector resources would be frustrated.

5.6.5 The arguments for open register are strongest in respect of Options 2 – 5 because under these options data would be submitted routinely by the company to Companies House and thus easily incorporated into private sector databases. By contrast, under Options 1a-c data would have to be obtained from the companies themselves. This might still help in individual recovery cases, but sheer complexity would preclude credit reference agencies from collecting and routinely cross-referencing beneficial ownership data to other information on a national basis.

Wider arguments in favour of open register

5.6.6 The same arguments in favour of an open register for recovery purposes also apply to general law enforcement efforts to deter and prevent crime. The principal reasons are that deterrence and prevention rely heavily on output from intelligence and investigation activity, which an open register would support in very much the same way as set out above for recovery. With regard specifically to intelligence, open record also increases the chance that third parties will notice

and reports suspicions and inconsistencies regarding ownership and activities of a person or company.

5.6.7 With regard to the benefits for industry, the principal benefit of an open register is to provide the mechanism whereby data made available under these proposals can be communicated to the wider public and credit reference agencies to generate the benefits set out above. Without the open register the mechanism would not function and the benefits would not accrue. Conversely, and as with recovery, the wider benefits of open register are greatest where the information is most detailed and centrally reported.

Arguments against open record

5.6.8 Arguments against open record were expressed by a number of law enforcement officials and industry representatives. From an overall crime reduction point of view, a small number of law enforcers believed a restricted database would create (the illusion of) an information advantage over criminals, which would have a deterrent effect.

5.6.9 A number of industry representatives expressed the reservation that making data publicly available might make companies less forthcoming with public declarations than ones destined for private record. In effect, open register might force companies either to surrender commercial advantages currently enjoyed or face breaking the law.

5.6.10 It is accepted that as things currently stand, beneficial owners may have a *bona fide* commercial interest in veiling their interests, for example, wanting discretely to use the products or services of a company in which they hold a beneficial interest. A company may want to hide behind a corporate veil for fear of negatively affecting the availability, quality and cost of goods and services which it wants to obtain, or flagging commercially sensitive information to competitors.

5.6.11 A further reservation expressed by both industry and law enforcement representatives was that publication of some details of legal and beneficial ownership might have public order implications. These arguments draw on the experience of companies whose shareholders and officers had been subject to menace and physical attack on account of the legal but controversial nature of their business. This is best illustrated by the problems recently experienced by Huntingdon Life Sciences and the consequent proposals to protect the details of company directors (see Section 6 Costs below).

5.6.12 Individuals with a high public profile, politically exposed persons, those under witness protection schemes and members of family trusts, might also have valid reasons for not wanting their identity or level of interest disclosed.

Weighing the pro's and con's

5.6.13 It is possible that closed record might provide law enforcement authorities with a real or apparent information advantage over some criminals. However, law enforcement officials with all the machinery of state behind them probably do not need to rely on this particular system to claim information advantage when there are more credible grounds for making such a claim. One such ground would be the tasking of the intelligence services in the fight against organised and serious crime, which might reasonably be expected to have a greater deterrent and prevention value. Another is that open register options allow the private sector to produce a wider range of related on-line information that is of more practical value to law enforcement in proof or disproof of suspicions than the deterrent effect of (real or illusory) data superiority.

5.6.14 The *bona fide* business confidence argument against open record has much stronger roots in tradition. One possible compromise is to provide information to commercial inquirers only on the basis of name give up, which information would be available to the company or individuals themselves. This option has not been costed.

5.6.15 With regard to arguments based on potential non-compliance, the reluctance of companies and individuals to submit returns is closely linked to the perceived quality of the enforcement regime. Companies House has shown how submission rates can be dramatically improved by applying principles of restorative justice, involving a combination of education, compliance friendly reporting procedures, warnings and, only as a last resort, civil and criminal penalties. Whilst Companies House cannot guarantee the quality of the information it collects has shown it can secure its delivery within a certain timeframe.

5.6.16 Public and private sector sources agreed that on balance, with certain safeguards, advantages to society at large from open register were greater than the disadvantages, with the advantages of linking public and private sector data presenting a particularly compelling argument in favour.

5.7 Serious arrestable offence

5.7.1 With relatively little risk of automatic detection of false reporting, enforcement would rely heavily on sanctions. Importantly, some of those most at risk of transgressing () are deterred not so much by the sentence faced, but by the prospect of committing an arrestable offence and its impact on their reputation if arrested, even if only on suspicion. The ability of the police to obtain a search warrant is also a major deterrent. Thus, a maximum prison sentence of five years would need to be attached to failure to disclose or report with intent to assist money laundering. Five years is the time required for an offence to be

classified as a serious offence which in turn enables arrest without warrant. The offence a lesser term, but the offence nonetheless specified in the relevant legislation as arrestable without warrant. Lesser would greatly reduce the impact of the proposals.

5.7.2 Currently, failure to submit an Annual Return can lead to a fine on, and ultimately disqualification of, directors. However, offences such as tipping off, or failure to disclose knowledge or suspicion of money laundering, which might also be looked upon as essentially administrative offences, carry a penalty of up to five years in prison. Sentences of four years' imprisonment have been passed in a number of cases where bank managers have tipped off their clients that they have made a report or that an investigation is being carried out. The current Company Law Review also envisages increased penalties, with imprisonment for up to ten years mooted for fraudulent trading.

5.7.3 The prospect of severe penalties might also encourage compromised intermediaries to denounce their principals. Other options that might be considered include voidness or unenforceability for unreported transfers of both forms of ownership.

5.8 Quantifying and attributing benefits

Allocation and Quantification Considerations

5.8.1 Quantifying financial crime, and the effects of financial crime measures, reliably, is notoriously difficult. It is not possible to establish a precise value of each option in the proposals. By the nature of the underlying phenomena, it is quite possible that data obtained under the minimum option 1a might lead to a large recovery whilst a sophisticated operation based on maximum option 5 might recover very little. Moreover, an important element of the benefit derives not from the options themselves but from the enforcement regime that accompanies them, notably the creation of the serious arrestable offence.

5.8.2 Instead we have constructed a hierarchy of benefits based on the consensus among enforcement and industry representatives that the value of the benefits generated by proposals builds up progressively with each option.

5.8.3 In terms of increasing potential for reduced operating costs, recoveries, and crime prevention we isolated, on the basis of comments received, the following factors of benefits:

- legal ownership coverage
- beneficial ownership coverage
- personal data detail
- data timeliness
- system user-friendliness
- links to other data

5.8.4 Under the proposals, personal data detail is common to all options, so the remaining five factors determine the quantum of benefit.

Orders of Economy

5.8.5 Analysis of comments further suggested that the marginal benefits of the proposals accrue in three stages according to the numbers of factors coming into play.

5.8.6 An initial order of economy is linked to increased effectiveness, efficiency and value for money of operations generally, and recovery in particular. It results principally from access to information (especially fresh information) on beneficial ownership and from timesaving and higher quality investigation of individual cases. Such access may be due to the development of entry-level user friendly inquiry systems by private sector providers. Based on estimates by individual enforcement units the order of economy involved is around 5 – 10% and we have used the lower figure.

5.8.7 Options attracting first order benefits are:

- 1a-c, 2 (in both cases open and closed)
- 3 (closed)

NB. Option 2 Open is included in this order as access to data would not be timely and this might further affect access to wider data via the entry-level computer inquiry systems mentioned above. Option 3 is included because of the lack of link to wider data and user friendly inquiry systems.

5.8.8 A second order of economy is achieved where the proposals allow operations of greater scope and complexity. It results from having user-friendly systems that can manipulate data on legal and beneficial ownership on a large scale, and from the ability to search a unified ownership database by company or person to establish matches and links. Based on estimates by individual units the order of economy involved is around 15 – 25% and we have used the lower figure.

5.8.9 Options attracting second order benefits are:

- 4 and 5 (closed)

5.8.10 A third order of economy is obtained where the proposals allow entirely new strategic approaches to operations. This occurs where databases on company ownership can be linked to other databases. It results from the ability to monitor and match routinely a much wider range of behaviour of people and companies. An example of this is the use of data matching by the DWP to identify fraud and error across a range of benefits and which resulted in downward adjustment of benefits of over £70 million in the year to April 2000. Based on

estimates by individual units the order of economy involved is around 30 – 50% and we have used the lower figure.

5.8.11 Options attracting third order benefits are:

- 3, 4 and 5 (open)

5.8.12 We believe these ranges are consistent, if not modest, compared with rates of improvement recently achieved by individual units and overall. HM Customs & Excise confiscation of drugs proceeds increased by 47% between 1999 and 2000, whilst the total value of non-drug confiscation orders and money laundering prosecutions doubled between 1998 and 1999.

5.8.13 Factors of orders of economy are also set out in Table 3.

5.9 Quantum of benefits

Cost Reductions

5.9.1 To establish the order of potential cost reductions, we looked at the cost base of the law enforcement units most likely to use these powers and the total beneficiaries established above.

5.9.2 Police officer salaries in England and Wales in 1999-2000 amounted to approximately £4.2 billion. The number of police officers was just under 122,000. This produces expenditure per officer of c£34,000 p.a. Based on an estimated salary outturn in 2000-01 of £593 million and staff of c22,000, HM Customs & Excise average expenditure per head of staff is around £27,000 p.a. We have therefore assumed that the average expenditure per head of a law enforcer specialising in recovery is around £30,000.

5.9.3 Taking the basic PIU Report figure for qualified financial investigators in UK law enforcement of around 1,700 and applying the first, second and third order of economy to their average cost produces savings for financial investigators of £2.55 million, £7.65 million and £15.3 million respectively. However, as the ratio of formally qualified to unqualified investigators can be as high as 1:10, the proposed system might well be used by many more investigators, meaning the total potential savings at unit level are much higher.

5.9.4 These figures exclude the benefits to other law enforcers who might use the proposed system for routine inquiries but who do not work in FIUs. They also exclude increases in fines and penalties, of which HM Customs & Excise alone collected over £146 million in 1999-2000. The effect of the orders of economy here would be an increase in fines and penalties of £7.3 million, £21.9 million and £43.8 million respectively

Recoveries

5.9.5 Units could not offer firm estimates of the likely increased volume of recoveries. One problem is that there is no reliable figure for the volume of

underlying funds involved. On the basis of the activity of one unit handling 25% of NCIS disclosures we estimate that, in the case of detected drug crime alone, the annual order of magnitude is at least several hundred million pounds. Of this total, and based on the same unit's experience, only a few tens of millions of pounds are being recovered every year and (for lack of resources) units are only investigating a fraction of cases referred to them.

5.9.6 This supports the PIU Report's observation that whilst the estimated outflow from the UK of proceeds from the sale of drugs was £970 million in 1994, the recovery of drug proceeds in the UK in 1999/2000 was just £4 million. Its estimate of the value of proceeds from drugs, prostitution, gambling and stolen goods in 1996 is £6.5 – £11 billion. The Report also highlights that court orders to recover assets currently follow <1% of convictions and that confiscation orders have been raised in just 20% of drugs cases and 0.3% of other crime, even though 70% of recorded crime is acquisitive. Collection rates average 40% or less of amounts ordered.

5.9.7 More recent figures (NERA & Home Office RDS, 2000) suggest underlying fraud and forgery of £16 billion alone but with confiscation order values now approaching £50 million.

5.9.8 As the proposals were seen to increase both the chance of identifying proceeds of crime and the probability of recovering them, the expectation that recovery rates will increase is not unreasonable. Applying the first order of economy percentage to the current value of confiscation produces an increase of £2.5 million. Applying the second and third order of economy percentages produces increases of £7.5 million and £15 million.

Prevention

5.9.9 Because of variations in the way terms are defined, units were not able to give standardised estimates of the value of crime that would be prevented by the proposals. Nor could they allocate reductions between the greater deterrent effect of recovery, less potential offenders in circulation due to more arrests or better protection of assets due to intelligence work. However, they emphasised that with such a large value at risk to crime, small increases in prevention would still have a large cash effect. Two illustrations of this are HM Customs & Excise and DWP:

- HM Customs & Excise estimate that £2 in 2000. A 1% efficiency increase in this unit alone would be worth over £20m. In the same year NIS closed down 76 criminal organisations, the very type of organised crime activity targeted by these proposals.
- In the year to March 2000, benefit fraud and error amounted to £1.32 billion and 10,000 prosecutions took place. Whilst much of this concerned individuals, organised benefit fraud is a major problem in areas such as counterfeiting and sophisticated multiple claim scams run on an industrial basis by various gangs. Estimates of value at risk are as high as £2 – 3

billion. Because of calculation methods, fraud prevented by BASIS is roughly the same as recoveries - £10 - 20 million. Economies of the first order (5%) would lead to increased recoveries of at least £500,000 and savings of at least £1 million if also applied to the (narrowly defined) BASIS figures for prevention.

Industry and society

5.9.10 Whilst it is reasonable to assume the proposals would have a beneficial effect in these areas, no estimates have been made of the full value of the proposals to industry as the range of potential effects are so wide.

5.9.11 In terms of improved business confidence, the market for data from credit reference agencies is about £175 million per year, implying that the potential losses their clients seek to avoid are a multiple of that figure. Indeed, the yearly value of bad debts referred to debt collection agencies is c£3.5 billion, whilst non-mortgage credit in 1999 was £500 billion. A very small impact on the quality and cost of corporate credit would have significant value.

5.9.12 Estimates produced for the FSA of the cost of account opening identification procedures suggest the cost to industry and individuals is up to £14 million per year. Again, even benefits of the first order of economy would be worth £750,000 p.a.

Total Benefits

5.9.13 Taking a strict view of beneficiaries, recognising only cost savings by financial investigators, and allowing reasonable expectations of improvements in recoveries produces the following benefits:

1. Options with first order of economy £5.1 million
2. Options with the second order of economy £15.2 million
3. Options with the third order of economy £30.3 million

5.10 Benefits of specific options

5.10.1 The extent of benefits for each option is discussed below. As law enforcement officials emphasised the need for a name-based, user-friendly and accurate means of establishing all corporate interest of a given person, analysis focuses on Option 2 onwards as it is from this option onwards that a centralised system on both legal and beneficial ownership can put together. However, it is also necessary to analyse earlier options as they introduce many of the duties upon which later options depend.

5.10.2 In line with the Terms of Reference, the benefits are reviewed on the basis of both a closed register (open to law enforcers only) and an open register. It should be noted that the major difference between Options 2 & 3 (open register) and Options 4 & 5 is that in the former case it will be left to the private sector to establish the database, but in latter to Companies House.

5.11 Option 1a

Closed register

5.11.1 The two principal features of this option are the introduction of a duty on individuals to report beneficial ownership and a duty on companies to maintain records of the same.

5.11.2 From a law enforcement perspective the major benefit of this option is the enforcement regime, including the serious arrestable offence. The first option of the proposals immediately brings the actions of not only beneficial owners but also company officers and intermediaries within the scope of the law. This would have immediate benefits across a wide range of enforcement agencies, who would now be able to check real or alleged beneficial ownership declarations, question or charge individuals regarding their declarations, and question or charge company officers regarding false record keeping in connection with moneylaundering.

5.11.3 The information itself reveals only the fact of beneficial ownership and would only be obtained by direct inquiry. Both of these points limit its value. More positively, the option does open the way for honest company officials to express their suspicions about ownership as per the company's books of record. It would also enable them to report on their company's activities becoming suspicious in the light of beneficial ownership. Both forms of whistle blowing may produce useful intelligence.

5.11.4 Overall, the option would generate some benefits for law enforcers engaged in confiscation openly seeking basic information on historical links. Examples are police fraud investigation units, tax and DTI officials who would otherwise have to use other powers (e.g. S442 & 447 CA85). It would also help in routine other investigation and evidence gathering in other enforcement activity, for example by revealing a *modus operandi* over a number of years.

5.11.5 The principal benefit to beneficial owners is having their interest, though not the degree of interest, recorded in the company records, which may be of use in the case of disputes. The benefit for companies is likewise knowledge of the existence of such interest. The current proposals thus go further than the CLR, which recommended that in some circumstances beneficial owners would be able to register their interest with the company. However this was to be on a voluntary not compulsory basis.

Open record

5.11.6 Placing the data on open register introduces the basic ability for the general public, including company stakeholders, to obtain a more informed view of the company's situation, though the disclosure is less than required for legal owners of shares. From a law enforcement point of view it offers weak cover for obtaining information using a pretext and in theory increases the number of people in a position to inspect records and thus to spot and report inconsistencies.

5.11.7 The open register is probably of most use to those making occasional routine background checks on individual companies, and civil recovery experts working on long running cases below law enforcement thresholds of interest.

Benefits

5.11.8 On a closed register basis the principal law enforcement benefits of this option are:

- savings in time made possible by access to information by simple inquiry rather having to conduct an investigation, and
- the value of information obtained on actual and alleged beneficial ownership from records or interviews.

5.11.9 With the prospect of committing a new serious arrestable offence it is not unreasonable to assume those questioned will provide more, or more accurate, information, leading to more, and more successful, investigations and even the higher orders of economy highlighted above. The closed register option offers no benefit to industry, other than to contribute at the very margins to the weeding out of potentially dubious business partners.

5.11.10 There are similar benefits for company stakeholders under the open register option, which are limited by the low level of declaration required, but which may be of significance in individual cases where the existence of beneficial ownership was not known to the company or other legal and/or beneficial shareholders.

5.11.11 The open and closed register versions of Option 1a both attract *benefits of the first order* of economy.

5.12 Option 1b

Closed record

5.12.1 Option 1b introduces the ability to know the extent as well as the fact of beneficial ownership, and to receive details on an annual basis. It therefore has value in determining whether an individual's involvement constitutes full or part ownership or another legally-defined interest in a company, and in tracking and monitoring situations.

5.12.2 The option would especially benefit those in general investigation and historical evidence gathering, where the additional information data would now

make it possible to reconstruct the nature and approximate periods of control. The annual data supply would also fit in with the review cycle of organisations working on an annual basis, such as Inland Revenue.

5.12.3 As there would be more reports and more specific disclosure made by beneficial owners under this option, there would be more chance for honest company officials to develop and report suspicions. Beneficial owners would have the benefit of an official record of the extent of their interest with a mirror benefit for the companies in question.

Open record

5.12.4 The open record version of Option 1b is almost the same regime as for Option 1a, but with the advantage of more timely and detailed information. However, the data which a company would hold on beneficial ownership would still not be as extensive as that on legal ownership. The option extends to the private sector the ability to look into aspects of ownership and control, putting civil recovery experts on a par with law enforcers.

Benefits

5.12.5 Over time, this option would allow investigators to establish and monitor patterns of real and alleged corporate interests by simple inquiry, as opposed to quite complex historical investigation. In addition to simple efficiency gains, the new ability to demonstrate control or ownership is important as it not only increases the chance of linking a person to a company or transaction, but of linking them in a more important role.

5.12.6 Therefore, the option improves not only the chance of conviction and confiscation but also the potential seriousness of the charge and the scope of recovery. As the beneficial owner must declare, and the company record, the extent of change in relation to specific dates, there is also more scope for enforcers to question owners, company officials and intermediaries about statements made and records kept, and to identify material inconsistencies.

5.12.7 In the private sector, benefits would similarly come from better credit scoring, client identification and civil recovery possible with the additional information. Thus the benefits of Option 1b are of the same kind as those of Option 1a, but the increased information available provides a significant increase in potential effect.

5.12.8 The open and closed register versions of Option 1b both attract *benefits of the first order* of economy.

5.13 Option 1c

(NB It has been assumed that the obligation is to report changes of 1%, not rises of 1% as stated in the Terms of Reference).

Closed register

5.13.1 This option introduces the requirement to report and record precise percentage changes to a company's ownership structure as they occur. It is the first option in the proposals oriented towards current developments as opposed to the *ex post* nature of previous options. This is important as both money laundering operations and other crimes may take place within a time frame of just a few weeks or even days. The average length of time of a benefit fraud is c.32 weeks.

5.13.2 The stricter timing requirement means the option is the first to support fast moving investigations. It would also improve support for longer standing historical reconstruction of asset and possession trails by enabling the review of recent history. The more detailed record of past beneficial ownership that would emerge over time would also provide a source of information in starting and progressing less urgent investigations. However, there is still no cover for inquiries and no cross-linking to the wider interests of the individuals concerned.

5.13.3 The option allows beneficial owners to register their interests sooner, and companies would have the benefit of full and timely transparency over alleged beneficial ownership. There would be more frequent scope for whistle blowing by company insiders, increasing information available to law enforcement authorities, and heightening the chance of more convictions and recoveries.

5.13.4 As officials would not have to obtain information using other powers (or at worst, wait a year), quicker, wider and deeper investigations would be possible than under Option 1b and the opportunity created for quicker and more substantial proof to be gathered. Obtaining equivalent information from other sources (e.g. production orders and bank circulars) might involve substantial delays, assuming such information was available at all (some consultees were concerned that several recent bank information system designs have failed to support the information needs of criminal inquiries).

Open register

5.13.5 The marginal added value of open register for law enforcement in this sub-option is the possibility of access using a pretext. As with Option 1b, the open register puts private sector recovery experts on a par with law enforcers.

5.13.6 Principal industry beneficiaries would be businesses that regularly review counterparty credit standing in detail. Information available under this option would also be of more benefit to companies having to meet FATF-based client identification requirements, as the information would be more current and match disclosure requirements for legal shareholdings. From the shareholder viewpoint there would be almost complete transparency with regard to their company's true ownership though, as with law enforcement, no easy way to drill deeper.

Benefits

5.13.7 The power to get alongside events as opposed to the *ex post* nature of the earlier options has important morale value for enforcers as it overcomes the sense of always being many steps behind criminals and allows a more proactive response. It therefore is of special value in rapidly moving investigations where success depends upon speed and precise calculation of beneficial ownership. Late stage support to long-running investigations is also important, as this is the point where assets and their current possessors are located.

5.13.8 The increased opportunities to question beneficial owners and company officials more often about the timing and content of recent declarations and records provides more opportunity for inconsistencies to emerge. The greater detail of historical record that would arise would make more complex analysis possible, for example linking cash flows to timings. Once more there would be more chance of success and bigger possible successes.

5.13.9 The open and closed register versions of Option 1c both attract *benefits of the first order* of economy.

5.14 Option 2

Closed record

5.14.1 The main features in Option 2 relate to the introduction of a duty to report beneficial ownership at company level and the extension of the duty to unlisted public companies. The three principal marginal effects of the option are that:

- The company and its directors are brought into the frame of responsibility with respect to reporting as well as recording
- The serious arrestable offence is widened to cover any failure to report annually and reporting false or misleading data
- A central reporting and inquiry point is established at Companies House

5.14.2 By making more comprehensive and centralised historic data available, and more accessible, the marginal effect of the provision's environment would be similar to Option 1b (open register), namely to:

- increase the number of people that can be held to account, and the range of their behaviour that can be investigated
- improve the opportunities to spot inconsistencies
- improve the likelihood that those questioned will co-operate with inquiries
- provide an alternative source of historical information of a known format and age on company structure

5.14.3 The opinion among law enforcers was that the option was the first to offer the possibility of a new approach to planning long-term operations, and that its value would grow over time as data built up. The critical marginal benefits for recovery were that:

- making company 'gatekeepers' for the purposes of determining company ownership allows more scope for intermediaries and accomplices to deny criminals opportunities for abusing companies and to report them if they do
- a central reference point would allow more sensitive investigations to be undertaken with less risk of interest being flagged to companies and thus possibly to individuals under suspicion or surveillance that attaches to Options 1a-c
- Having a central reference point would also save time by allowing easier physical access to data through Companies House than via individual inquiries to companies (as under Option 1a-c)

5.14.4 It is with this option that the proposals also begin to be of practical value to other law enforcement units, by saving them using more complex powers to obtain information, as well as the time and effort involved in so doing. Checks on this basis might become routine, as with land registry searches in HM Customs & Excise inquiries. The option would also reduce the risk of prejudicing an investigation by being seen to be asking questions. This would benefit, for example, SFO, HM Customs & Excise investigation teams and Special Branch.

5.14.5 As a result, more and complex investigations could be attempted with more chances of laying charges and more chance of successful convictions and confiscation. In particular, by making it riskier for company officers and intermediaries to act on behalf of criminals and thus harder for criminals to control companies, fewer corporate vehicles would be available as conduits.

Open register

5.14.6 The marginal effect of open register would be to extend the closed record benefits to a much wider audience. Importantly, it is the first option that allows private sector data suppliers access to routine comprehensive data on beneficial ownership from official sources and to match it with other information held on individuals and companies. Placing the information obtained under Option 2 on open register would allow these companies to establish user-friendly databases on beneficial ownership.

5.14.7 Public information held by Companies House is used extensively by credit reference agencies. Many of the companies offer on-line or CD ROM/DVD based inquiry systems which allow searches by name of individual. Moreover, as these companies already hold details on all UK private and unlisted public companies and most of their shareholders, they would be in a position to provide and maintain a combined database on shareholders and directorships, foreshadowing some of the proposals under Options 4 & 5. The database could be linked to

other information held by credit reference agencies on the individuals and companies concerned.

5.14.8 This option would therefore allow more sophisticated historical linkages to be established and thus more complex cases to be identified and investigated by those law enforcement officials with sufficient resources to access private sector systems. It establishes the principle of using open record options to generate significant advantages for law enforcement from better use of private sector resources.

5.14.9 As with the closed record, the benefits for both law enforcement and civil recovery experts would be the ability to undertake more cases, make better investigation decisions, exploit the value of automatic access to information and the reduced need for visits to companies to obtain information. More litigation and prosecutions would lead to greater chances of successful recovery and conviction.

5.14.10 Stakeholders would also obtain similar benefits but with regard to the creditworthiness of the company or individuals under consideration, not to possible criminality. The improved information environment would still increase the chance of irregularities being identified and reported. This option would also be the first to provide widespread benefits to industry, as the improvements in the quality of private sector data on companies and individuals enabled better credit decisions, thus lowering loan loss and bad debt experience. The improved systemic confidence possible through this would tend to push credit costs lower and profit margins higher.

5.14.11 However, the information available under the open option would not always be timely, and this might in turn adversely affect ability to access wider data. Thus both the closed and open register versions of Option 2 attract benefits of the *first order* of economy.

5.15 Option 3

Closed record

5.15.1 The main features in Option 3 relate to the introduction of a duty to report changes in beneficial ownership to a central reporting point as they occur, and the extension of the same duty to cover changes in legal ownership. The principal marginal effects of the option are that:

- more timely information is available at the central reporting point
- a fuller range of legal and beneficial interest is covered
- the serious arrestable offence net is extended to company reporting of legal ownership declarations where money laundering is suspected.

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5.15.2 By making more comprehensive and up-to-date data available, and more accessible, the provision's environment works like Option 1c (open register), in that it would:

- widen the range of behaviour that can be investigated
- increase the opportunities to identify inconsistencies
- increase the timeliness of information available
- provide an alternative source of current information of a known format on alleged company structure
- improve the likelihood that those questioned will co-operate with inquiries

5.15.3 The opinion among law enforcers was that, as with Option 1c, the option would especially benefit fast-moving operations. The critical marginal benefits for recovery units were that anonymity obtained in Option 2 was now combined with data obtained up to a year earlier than otherwise possible. This would allow an earlier response to short-lived money laundering schemes, which previously might have fallen through the net.

5.15.4 This benefit was also thought to have wider enforcement value in terms of easier identification and elimination of suspects, getting closer behind suspects, and creating more time and information for case building. The option also offered the possibility of a better approach to investigation planning and management based on knowledge of the existence and accessibility of the data.

5.15.5 Once again, this would contribute to a virtuous circle of capacity for more and more complex investigations with more chance of successful outcome in terms of convictions and recoveries. The risks and costs of using corporate vehicles would continue to rise and the attraction of doing so would fall further.

Open Record

5.15.6 Placing the same details on open register would give stakeholders, including legal and beneficial holders, creditors and clients, almost full transparency on corporate structure and the additional benefit of being able to check on time sensitive matters, such as transfers in legal ownership, at any stage of the year.

5.15.7 This would give businesses more flexibility in planning their routine reassessment of counterparties, e.g. annual credit reviews, and allow more accurate checks of information provided in client identification procedures. It would allow those requiring such information a known point of easy reference with the established benefit of accessing official figures. The open register option would likewise save individual firms from having to make available updated routine details of beneficial ownership repeatedly.

5.15.8 As with previous option, the principal benefit of open register would be to make more data available to company data holders who would then be in a

position to offer a better range of services to bulk public and private sector users, including law enforcers.

5.15.9 In particular under this option, leading credit reference agencies could offer continually updated information and search facilities at the name level, based on the open register details and combined with the full director data and some shareholder data that they already have on their systems. The system would have the advantage over Option 2 of being more complete and up to date. A comparable official integrated system is not provided by these proposals until Option 5.

5.15.10 This would be of direct benefit to all law enforcers with access to such systems as well as private sector due diligence and recovery work. It is the first option that allows recovery and investigation strategies to be based on comprehensive and user-friendly database screening. It would also support the type of Watch List system discussed in Section 7 *Alternatives*, below.

5.15.11 The closed register version of Option 3 attracts benefits of the *first order* of economy. The open register option attracts benefits of the *third order*.

5.16 Option 4

Closed register

5.16.1 This option introduces the ability to search an officially held database at name level for legal and beneficial shareholdings. It creates a legal requirement for a system which would allow law enforcement to drive investigations according to the name of the individuals involved and not according to the companies involved, which may not be known.

5.16.2 It is important to realise that, as the options are cumulative, Option 4 closed register enjoys all the benefits of Option 3 closed register. By requiring Companies House to create a searchable database, Option 4 provides some of the advantages of name-based search and listing that private sector systems might supply using data available from the open register under Option 3. Option 4 would allow similar searches to Option 3 (Open) but would not produce as wide a range of data on directorships and wider credit-related data. The option would come close to providing the complete closed record framework if used in conjunction with the existing Companies House database of directors and private sector systems, each on a standalone basis.

5.16.3 Though the system would be cumbersome for large-scale screening (because of the need to search two databases for details of all corporate interest), it would be adequate for large scale individual investigations. It is the first of the closed record options that would make it possible to drive investigation strategy by name and allow higher orders of efficiency to be achieved. This would be expressed in terms of the increased complexity and scope of investigations that could be undertaken, and create the benefits described in Option 3 (open) above, but on a lower scale.

Open register

5.16.4 As Option 4 Open enjoys the cumulative benefits of Option 3 Open, the value of this sub-option is greatest for private sector parties without access to commercial data sources. It allows fuller investigation of an individual's wider interests which may not otherwise be available or available only at some cost via credit reference agencies. Whilst bulk data users may have other sources of such information, the open register would also be a good cross check of the completeness of private sector systems, and competition between the two fostered by this option would increase consumer choice.

5.16.5 The open register would again save companies and individuals having to ask for, and companies and individuals having repeatedly to provide, data to third parties and keep it updated. These benefits would accrue in the same areas as for other options, but especially for bulk client identification and review purposes where files based on open register data could be created for batch processing rather than individual checks.

The closed register version of Option 4 attracts benefits of the *second order* of economy. The open register version of Option 4 attracts benefits of the *third order*.

5.17 Option 5

Closed and Open Register

5.17.1 Again Option 5, because of the cumulative effect, attracts all the benefits as Option 4 but with the increased efficiency of providing all company structure data on one system. The marginal benefits of this system relate mainly to efficiency through avoidance of the need to install or access multiple systems and undertake multiple searches, first for shareholders and secondly for directors. There is also the benefit of government having a system which is not reliant on commercial pressures and provides a guarantee of continuity of availability. Changes in market forces might lead to the private sector deciding to withdraw a service which law enforcement had come to rely on. Also, a system within the government sphere provides a degree of backup in case of technical or security failures in the private sector.

5.17.2 The open register version would allow data providers to offer a one-stop shop, taking advantage of the wider coverage of Companies House data obtained in Option 4 and linking it to the directors details. It would improve the

access to, and manipulation of, data obtainable from Companies House in other formats. All other benefits mentioned in previous options would attach and be greatly improved by system unity.

5.17.3 The closed register version of Option 5 attracts benefits of the *second order* of economy. The open register version of Option 5 attracts benefits of the *third order*.

5.18 Sensitivities

5.18.1 This section looks at the effects of changes to assumptions made in identifying benefits and other factors effecting the likelihood of their benefits being realised in part or in full.

Changes to level of detail of identity reporting

5.18.2 The above analysis assumes the type of personal information required is the minimum described above (See 4.2 Option 1a). The benefits of the system would be greatly enhanced by requiring only two extra details - mandatory date of birth and post code. These could be used to speed identity checks in closed record investigations under Options 1 – 3 and would have even more benefit as potential additional search fields in any future private sector or Companies House inquiry database which enabled search and listing by name. Not having these details would result in having to revert in some cases to more labour intensive methods of inquiry. This would reduce the value of benefits by about one order of economy. The precise special details required for overseas residents would have to be determined on the basis of detailed input from potential users.

5.18.3 Conversely, much higher benefits would accrue from a requirement to use a passport identity, driving licence, tax or National Insurance number.

Changes to level of ownership declaration thresholds

5.18.4 Some industry representatives thought the proposals would be defeated by dividing beneficial ownership and share trades into parcels below the declaration thresholds ('smurfing'). This method of circumvention cannot be excluded, but it would require establishing at least 34 shareholder identities for a private company, and the mere number of shareholders would stand out. Smurfing would impact least on Options 4 & 5 where cross checks on e.g. directors and shareholders are possible and indeed provide the very tool to tackle this problem.

5.18.5 Some enforcers argued that the thresholds were in fact too low and that thresholds in stages of 10% would be equally effective for less effort. Others suggested that reporting should be in absolute numbers of shares, as this would enable direct reconciliation of legal and beneficial ownership levels for the same or less effort.

5.18.6 The option of declaring the fact of beneficial ownership only is discussed under Section 7 Alternatives.

Changes to timing

5.18.7 These are addressed by the structure of the options. The fact that information disclosed annually might have lost its relevance by the time it is needed has been shown to increase the value of Options 1c and 3 - 5. The value of timely information is at least one order of economy.

Changes to controls of company registers.

5.18.8 It has been assumed that the proposed duties on companies to keep additional records will not be subject to routine controls, reflecting the current enforcement of S352 CA85 in the case of the register of members. If controls were established then there is a greater chance that information would be current and available, increasing the efficiency of the proposals and thus benefits. Further investigations might also arise from the spot checks, increasing the value of the proposals by an order of economy.

Annual declarations/returns are due within a month of the legal return date.

5.18.9 The benefits assume that a modified Form 363a is used for annual declarations to Companies House within a month of the legal return date. There are advantages (relevance) and disadvantages (non-compliance) to shortening and lengthening this period, which are assumed to cancel each other out.

Changes to civil penalties

5.18.10 As in the case of penalties on directors for late filing of Annual Returns, the regime would be significantly impacted by insufficient penalties for benign non-filing. However, there would have to be scope for discretion in collecting the penalty where the circumstances merited (especially in the case of small companies with limited resources) avoidance of the system falling into disrepute. This is an important area, as wide-scale non-filing or late filing, whilst rewarding in terms of penalties collected, would seriously impact the proposals (i.e. benefits would fall by at least one order of economy). The question of civil penalties will require careful consideration to achieve a fair balance.

Changes to serious arrestable offence

5.18.11 This has been discussed under Section 5.7 above.

Data Protection Act

5.18.12 It has been assumed with reasonable confidence that it will be possible to store, manipulate, retrieve and in certain circumstances publish data based on exemptions and licences granted under the Data Protection Act 1998. It will be important to confirm this still applies to the detailed specification of any system resulting from these proposals.

5.19 Effect of non-compliance

5.19.1 The proposals target criminals and their accomplices who are by definition non-compliant. The question arises as to whether in such circumstances the benefits of the proposals can still be obtained.

5.19.2 These proposals have been analysed in a manner that takes such non-compliance into account, as it would be irrational to design a system that relied on self-denunciation by criminals in order to be effective. In analysing sensitivities it should be borne in mind the system is designed to produce data that highlights discrepancies when checked against other facts and opinions.

5.19.3 Indeed, as the section on Serious Arrestable Offence points out, a major purpose of the proposals is to require statements to be made which remain available for use as evidence. Another purpose is to allow patterns of reporting to be analysed across individuals, companies and time, enabling suspicious patterns of behaviour to be identified. It is for the investigator to then establish if non-compliance is benign or malign. In analysing the effect of non-compliance we have once more assumed that non-compliance will only come to light if looked for.

Detection and correction of non-compliance

5.19.4 In reality, as the options are structured, non-collusive failure to report and misreporting by individuals would be detectable by comparing the records of legal and beneficial ownership with each other and with any evidence which contradicts either or both of them. Inadequate reporting would render the individuals concerned liable to a civil penalty. Where a malign motive was established, further investigation would be possible and the proposals would have met their immediate objective.

5.19.5 Collusive false reporting by a company or individual would, again, not be detected unless the information given was checked and found to be wrong. However in such circumstances ownership declarations on record would provide evidence of guilt, increasing the chance of conviction for e.g. a money laundering offence and attaching a confiscation order to assets. Where this failed, the authorities would have the option to pursue the serious arrestable offence and even if this failed, the company and individuals would be recorded as suspicious, building up evidence that might be useful were they to come to the attention of the authorities again.

5.19.6 Where a company failed to maintain a record of beneficial ownership, such failure would be apparent when checked against other evidence as available on inquiry under Options 1a-c and provide grounds for further investigation. Where suspicions of money laundering were later confirmed, more charges would be available.

5.19.7 Where failure was innocuous, the company's subsequent reporting performance could be monitored with a view to e.g. disqualification of directors,

thus contributing to orderly markets balance by weeding out unfair competition from non-compliant businesses. Here again non-compliance allows action to be taken which has positive benefits and which might not have been possible under the base case.

5.19.8 Where a company failed to report beneficial ownership, such failure to submit consistent data on legal and beneficial ownership despite having information to hand (i.e. from Options 1a - c) would be apparent from return forms. In the case of Option 2, discrepancies would only be apparent annually, allowing a window for non-compliance to go unnoticed unless specially investigated. Option 3 allows non-compliance to be apparent immediately if investigated.

5.19.9 Thus failure to report and misreporting by individuals and companies does not *per se* put law enforcement at a disadvantage, but rather, where it comes to light, it provides leads that can be followed up and extra charges that can be considered. It stands to reason that misreporting is more likely to come to light under open rather than closed systems as there is more opportunity for discrepancies to be detected.

5.19.10 The impact of failing to report beneficial ownership (as opposed to false or misleading disclosure) depends on the motives. Where it is an attempt to hide the true nature of beneficial ownership it in fact does the opposite - as and when other evidence becomes available, it draws attention to it. Where the motive is innocuous, it provides the same basis for monitoring company behaviour and weeding out unfair competition as failure to maintain records.

5.19.11 From a business confidence perspective, very similar arguments apply. By having information in the open, individual businesses can perform the checks they think necessary and take a commercial view where evidence of false reporting is encountered. This view might include whistle blowing.

5.19.12 An even more effective approach would be to make companies responsible for confirming that shareholders have fulfilled their declaration duties. However, on account of the complex issues involved, this avenue has not been analysed.

Wide scale non-reporting and indistinct data

5.19.13 As already mentioned under penalties, the most serious threat to the system is not where data is wrong, but where it is absent or provides inconclusive identification on a wide scale. This would especially be the case where details relate to individuals and companies overseas.

5.19.14 It is difficult to predict the level of non-compliance and to distinguish between involuntary and voluntary non-compliance in such cases. The former would be highly influenced by the simplicity or complexity of the final legislation as well as the amount and quality of instructions and information provided by

DTI/Companies House. The latter might constitute a transgression whilst not being criminally motivated.

5.19.15 Where non-compliance did occur, its effects would be determined by its extent and the resulting effect on the individual option involved, as the nature of the option determines the order of economy achieved. Generally speaking, the more developed the option, the greater the effect of non-compliance is likely to be.

5.19.16 This is because there is a steep increase in benefits between the first and second orders of economy as well as the second and third. The steep rises are related to two key factors, access to wider data (Order 2 to Order 3) and user friendly inquiry and timely data (Order 1 to Order 2). Thus, non-compliance which seriously impacted on one or more of these areas would, depending on the option involved, have the ability to reduce benefits by one or two orders of economy. In the worse case, however, for the benefits of the proposals to be completely lost, non-compliance would have to extend to a wide scale failure simply to submit any data at all. This is difficult in Option 2 and above where non-submission would be detected by Companies House. It is therefore unlikely that non-compliance would void benefits completely.

5.19.17 Indistinct data, such as misspelling of name, date of birth and postcode, would tend to reduce access to wider data either by limiting the searches that could be made of private sector databases or by producing more results than could be usefully processed (e.g. too many people called "John Smith"). It would thus have the effect of reducing the benefits of the open register versions of options 3, 4 and 5 by one order of economy.

5.19.18 Lack of data would impact the closed versions of Options 4 and 5 as lack of data would mean there was nothing at all to enter into user friendly systems. This would reduce their benefits by one order of economy. Both versions of the lower Options 1 (a, b, c) and 2, and the closed version of Option 3 are vulnerable to wide scale failure to submit timely information, and to provide legal details. This would reduce benefits back to the status quo.

5.19.19 Wide scale failure would require a long term wide scale rejection of the proposals which is at odds with the law abiding profile of the majority of the target group which external studies have shown to be one of the more compliant business communities in Europe.

5.19.20 Table 5 shows reduced benefits against constant costs.

5.20 Use of overseas fronts and other schemes

5.20.1 A possible effect of the proposals is to lead criminals to give overseas addresses or use overseas firms to circumvent the disclosure requirements. Some argue that, by encouraging the transfer of proceeds of crime and criminal operations offshore, assets would be harder to seize and criminals harder to

convict. Thus the immediate benefits of the proposals would be lost and the underlying objective of the proposals (to reduce serious crime) defeated. Crime would still occur in the UK, but simply be masterminded from abroad. With no UK companies involved, the features of these proposals would have nothing to analyse and thus produce no benefits at all.

5.20.2 The opposite case can also be argued. Where a person or company is suspected of involvement in a crime, it is critical to establish if they are connected to companies in the jurisdiction or not. The Options under these proposals allow this to be done with varying degrees of ease and timeliness and in the higher options to search wider databases as well. Even under the least of the proposals, an investigator is better off knowing that an individual is not active in the UK or connected with a UK company.

5.20.3 Likewise, knowing that a company has a beneficial owner registered offshore is better than not knowing who the beneficial owner is. In both cases it saves time looking in the wrong place, and this time can be re-employed more usefully in more selective domestic and overseas investigations.

5.20.4 There seems to be a suggestion that where an individual or company goes offshore it then becomes impossible to establish beneficial ownership. Whilst investigations offshore can be difficult, they are not impossible, especially where high level political will promotes lower level co-operation. An example of this is the recent closing down of various web-based paedophile rings having part of their operation in such jurisdictions. Indeed, in certain offshore jurisdictions, it may be easier to establish details of beneficial ownership than in the UK (e.g. Jersey, Bermuda). The sooner it is known that a person is probably offshore, the sooner a decision can be taken whether or not to pursue them. Where they are linked to a country it is easier to decide when further investigation has a chance of success. According to this argument the proposals retain their value by increasing the efficiency of resource allocation.

5.20.5 As the proposals become more thorough, they enable more detailed searching and screening which increases the chance of detecting patterns of avoidance. Even if crime has been pushed offshore, the system would enable more complex criminal intelligence analyses helping to identify the jurisdictions where suspicious actors are concentrated and allowing further pressure to be exerted, for example by political pressure and input to, e.g., FATF blacklist discussions.

5.20.6 Once crime is forced offshore to blacklist countries, their unwitting counterparts in the UK will also be obliged to undertake extended due diligence which may raise suspicions or simply add too much cost and trouble to make business worthwhile. In any case, the objective of ensuring UK companies are not abused as vehicles for crime will have been met.

Intermediaries

5.20.7 Criminals might seek to use company service providers (accounting and legal professionals or company formation agents, etc.) to establish and front companies for them and thus circumvent the proposals. Thus the level of demand for, and profitability of, professional services also affects the vulnerability of such professionals when a criminal approach is made. The quality of entry standards, training, compliance systems, professional standards and regulation are also important factors in maintaining the integrity of the market for professional services.

5.20.8 The significance of the role played by intermediaries is that they are the potential weak and strong points of deterrence and prevention systems, as recognised in recent OECD literature. By their stature they lend credibility and transfer knowledge. They can advise on illegal acts in other countries from jurisdictions where it is perfectly legal to do so. A small minority is simply corrupt. Intermediaries are believed to play a major complicit, unwitting, reckless or grossly negligent role in front company formation and management and interviewees highlighted the particular problem of debarred professionals.

5.20.9 Where these fail, sanctions-based policy must take over, as discussed in serious arrestable offence, above.

5.20.10 The proposals are more sensitive to circumvention by two other methods, use of bearer share warrants, and use of other forms of registered business not covered by these proposals.

5.20.11 Where a company issues bearer share warrants it may not be possible for the company to identify their holder if the holder failed to identify themselves to the company. Law enforcers and private inquirers would have to form a judgement on whether the issuance of bearer share warrants was suspicious and react accordingly, which might include having to abandon the investigation. Wide scale use of bearer share warrants would need to be watched for very carefully, and if necessary, subjected to further controls.

5.20.12 The proposals also fail to cover all forms of registered business status. By not extending to the other forms of businesses described in the base case, the way is left open to use these vehicles instead of private companies. Registration of LLPs has increased significantly recently with many sole traders who might have formed a private company opting for the LLP route. Close attention needs to be given to further harmonising disclosure across the various possible forms of business.

5.21 Other items impinging on policy effectiveness

Public awareness

5.21.1 The general public tends to associate the question of money laundering with the regulation of banking rather than with the regulation of companies, and with cash rather than cash substitutes or other assets. Thus, money laundering is seen as a risk that exists between financial institutions executing customer

orders, and then very much at the retail end. It is not seen as involving the corporate payer or payee, even though without them transactions would not exist.

5.21.2 This perception has been heightened by a series of large-scale scandals where publicity has focused on the financial institution involved (e.g. Bank of New York) and not the many small companies on the other side. Moves by UK authorities to crack down on poor controls in the financial sector, including custodial sentences for bank managers (usually four years for tipping off), have reinforced this view.

5.21.3 The public does, however, associate the use of companies for other illegal or marginal purposes such as fraud and tax evasion. To establish fully the relevance of these proposals, it would be necessary to extend public awareness to the other criminal uses of small companies and the severity of the risks posed by money laundering. This would help to explain the extension of state monitoring of the affairs of companies and individuals.

Target group awareness

5.21.4 To promote spontaneous compliance with the proposals, publicity and education effort would have to address the mechanics of the reporting system to ensure those with a duty to report knew they had such a duty and knew what that duty entailed. An immediate question is the definition of beneficial ownership, where uncertainty over interpretation of the term together with the ownership patterns of small companies (80% husband and wife) might lead to unintentional over or underreporting.

5.21.5 A further factor from the company point of view is that they incur two compliance duties, to store information and, in certain cases, to report as well. Where companies do not know or have not been able to contact or receive data from beneficial owners they may be forced into unwilling transgression.

5.21.6 Failure to set out the requirements and responsibilities of all parties involved in respect of the law and each other clearly and consistently will be critical here less large legal bills are incurred by target groups members seeking to clarify their position.

Controls

5.21.7 The proposals generate data which would be checked in detail only in the event of some other interest in the company. A crucial point here is that Companies House' mandate currently only extends to checking the completeness of data collected rather than validating it or checking it for discrepancies. Investigators or private sector data users would need to be, or become, familiar with what to look for and be able to assess if reports indicated a link to moneylaundering or just bad filing or bad data entry.

Distortions

5.21.8 There are several ways in which, assuming information is obtained, the proposals could fail to function properly. Firstly, cash-strapped investigation units might not be able to pay for access to the systems. Companies House operates as a trading fund and has a duty to recover costs (its sister registry of land is self financing). Private sector firms might levy charges for some searches which, whilst important, are simply unaffordable if other policing levels were to be maintained. Low police use of currently available private sector systems is mainly attributable not to unwillingness, but inability to pay or indeed ignorance of the existence of such systems and their possible use in intelligence and investigation.

5.21.9 With a relatively limited number of trained financial investigators in the country, it might also be possible that whilst data might be produced, it could not be analysed effectively. Similarly, it might be that police priorities meant that financial investigators, who are often detectives trained in a wide range of investigations, have to deal with other crimes. No police officers in the UK now have a financial industry qualification.

5.21.10 When investigating companies and beneficial owners in detail, enforcers could find companies and beneficial owners playing each other off with mutual recriminations and constructive obstruction tactics, which may give the impression of being a screen for money laundering but in fact relate to struggles over power and money.

5.21.11 As the range of size of money laundering schemes is so wide, the benefits of the measures might easily be greatly increased by a single large success. Whilst higher recovery levels may lead to more deterrence, they may actually indicate a higher incidence of underlying crime. Where recovery does have a deterrent effect, recovery levels may tail off, whilst deterrence benefits continue to accrue.

Time and change

5.21.12 With money launderers always seeking arbitrage opportunities, it might be that new and more efficient ways of laundering were developed. In this case the proposals would lose their immediate relevance and value. However they would still make it difficult to return to the use of small companies for money laundering were the new windows of opportunity to close. Moreover, the proposals are far reaching and involve measures, which reflect current best practice in anti money laundering policy. They may reasonably be expected to provide protection over the foreseeable time horizon.

Tax regimes

5.21.13 A comment from company formation agents was that, in addition to disclosure, a major factor in companies locating in a particular country was the tax regime, specifically the rate of tax and the taxation treaties in operation. Changes to either of these might have an effect on the number of money laundering schemes and criminals based in the country. The effects of changes

have not been calculated, but as the PIU Report says, money laundering operations are businesses. Bad ones as well as good ones are attracted by lower corporate tax rates and favourable tax treaties.

5.22 Concluding remarks on benefits

5.22.1 Especially when used in conjunction with other information, the proposals will have immediate effect in the evidential area but have their full desired effect if Option 4 upwards is implemented with the open register option and the accuracy of the data held by Companies House can be assured.

5.22.2 The proposals raise the barriers to money laundering across the board. At the entry level, the proposals will help in low and middle order crime prevention by making smaller criminals easier to target effectively. This would help prevent them from graduating to larger, harder to identify and more organised criminals. At the top end the proposals also provide a second layer of powers for combating the very serious offences both in money laundering and other forms of crime.

5.22.3 Overall the proposals will add to a range of measures the UK Government is introducing to tackle serious/financial crime in the UK and make the UK less attractive as an operating base or hiding place to both UK and non-UK criminals. They will enable the UK to lead international initiatives to share data in this area and stop jurisdictional arbitrage by criminals.

6. COSTS

6.1 Methodology and assumptions

6.1.1 This section identifies the major costs of the proposals to government, industry, companies and individuals. The costs we focused on were:

- Direct costs. The costs of establishing and running the system
- Compliance costs. Individuals' and companies' costs of obeying the rules
- Effects on sales. Changes to the quantity, quality and volume of goods sold
- Effects on competition. How companies might enter or leave the market as a result of the proposals
- Unfair costs. The element of the above costs which might affect individuals or groups disproportionately.

6.1.2 The direct costs and compliance costs of each option have been estimated in detail. The other costs have been analysed in more general terms but where possible they have also been estimated.

Businesses and individuals affected

6.1.3 There are approximately 1.5 million companies registered in England and Wales. Of these, 13,000 companies are public limited companies, of which only 2,200 are listed on the London Stock Exchange. Thus in the UK a small (private or unlisted public) company and covered by these proposals. Companies House figures show that 1.1 million of them have authorised share capital of £100 or less.

6.1.4 Potentially affected are the registrars, company formation agents, corporate company secretaries, software firms, lawyers and accountants who advise and assist these firms.

6.1.5 To estimate the number of legal shareholders affected we took the number of companies in England Wales and multiplied it by 3.5 - the Companies House estimate of the number of shareholders per company (excluding bulk list companies which are mainly listed companies). Accordingly we estimate that up to 5.25 million legal shareholders across the UK would be effected by the proposals. By way of comparison, listed public companies are estimated to have 12 - 13 million shareholders.

6.1.6 We next wanted to establish the number of companies that might have beneficial shareholders as well as legal owners. Companies House estimates that roughly 80% of companies are "" style small businesses. Figures from Companies House likewise suggest that 65% of companies have up to two members each and 80% have up to three members each. We therefore assumed that 80% of companies are likely to have only legal owners, because of the close shareholding structure, and that they have an average of two and a half

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shareholders each. The remaining 20% of companies (300,000) have the greater potential of including companies with beneficial owners.

6.1.7 There was no data available on which to derive firm estimates of the number of purely beneficial owners themselves. Instead, we have made assumptions based on the best available evidence – the experiences of experts (mainly credit reference agencies and company formation agents). They suggested that up to 5% of the 20% of companies with greater potential of having beneficial owners might in fact have them (i.e. 1% of all companies). The 20% of companies identified above were calculated to have 2.25 million shareholders (5.25m total shareholders – (1.5m companies x 80% “” companies x 2.5 shareholders per company)). This produces a figure of up to 112,500 beneficial owners (2.25m shareholders x 5%). We have rounded this figure up to 125,000 to allow for errors and omissions and facilitate calculations.

6.1.8 No adjustments have been made for multiple ownership of companies and group structures. The effect of such adjustments would be to reduce this number, but this is likely to be only very slightly since not many small companies are involved in group structures.

Registration and inquiry processes involved

6.1.9 To establish the impact on Companies House expenditure we wanted to identify the type and number of possible new transactions involved. The principal processes are:

- declarations of beneficial ownership on allotment
- transfers of beneficial ownership
- changes in beneficial ownership details
- entries and amendments to company registers of beneficial ownership
- company reporting of beneficial ownership details via annual returns
- company reporting of transfers of beneficial and legal ownership
- company reporting of changes in legal and beneficial ownership details
- company register inspections and company searches

New beneficial owners per year

6.1.10 By applying the percentage of companies likely to have beneficial owners (20%) to the number of new incorporations per year (2000-2001: 236,000) we estimated there would be up to 2,500 declarations of beneficial ownership on allotment by companies with beneficial owners who are not simultaneously legal owners of the same company.

6.1.11 There are about half as many dissolutions a year as incorporations. The cost of processing them has not been calculated as it has little impact on the overall picture.

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Transfer of beneficial ownership per year

6.1.12 To estimate changes in ownership we took the Inland Revenue figure of 500,000 annual transfers of legal ownership of shares in private and unlisted public companies, a ratio of c.1 transfer to every ten legal shareholders. This figure excludes exempt transfers such as family trusts and gifts, which cannot be established. Assuming beneficial ownership transfers occur at the same (c.10%) rate as legal ownership transfers, there would be 12,500 transfers of beneficial ownership to be recorded each year.

6.1.13 In its last financial year Companies House also processed just under 100,000 changes in directors' particulars, or a change rate of 3% on the total number of appointments. We applied the same change ratio to the number of beneficial owners (125,000) to obtain the maximum number of changes in beneficial ownership details – c.4,000.

6.1.14 Thus the maximum number of change of particulars to be processed by companies and (under Option 3) possibly Companies House would be around c.530,000 (2,500 + 500,000 + 12,500 + 4,000 = 519,000 *plus* rejections and re-submissions, *less* non-compliance).

6.1.15 Using the same 3% change rate we estimate that c.157,500 changes (3% x 5.25 million shareholders) to legal ownership details are reported annually via Annual Returns.

6.1.16 It is not known how many companies received requests to inspect their registers of members. Company searches at Companies House are running at 1.5 million per year. It is not known if the proposals would increase or decrease the number of such searches and inquiries and accordingly no analysis has been made of these processes.

Notification

6.1.17 In calculating costs we have made the following assumptions as to registration activity.

6.1.18 A duty would be placed on legal shareholders to confirm they were the beneficial owners of a share or to give the details of the person to whom they had assigned beneficial ownership. Notification procedures would thus focus on the immediate beneficial owner and not the ultimate beneficial owner at the end of a long and possibly complex chain.

6.1.19 Form 88(2) would be amended to allow the initial legal owner of shares to include any beneficial ownership details. Subsequent changes to ownership details would be notified to the company by a notice similar in content to the Stock Transfer Form. Changes to shareowner details would be by notice similar in content to the S288 series of forms. The company register would provide the basis for updating the Annual Return. Where immediate notification of

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subsequent changes was required, the company would forward the details to Companies House.

6.1.20 In the overwhelming majority of cases (companies with no beneficial owners or no changes to beneficial ownership details) annual confirmation of beneficial ownership details would be possible by means of a box tick against legal or beneficial owner details. Changes would be effected by amendment of the same pre-printed details on Form 363s. A separate section (cf. current Section 5) would allow details of other beneficial shareholders to be recorded on this form in identical fashion to the current other legal shareholder details.

6.1.21 The duty of beneficial shareholders to identify themselves and report changes to the company would track the current arrangements for legal shareholders. The regime for both would be tightened by specifying the period within which notification of changes had to be made to the company (we have assumed seven days), and implementing the requirement for residential address and date of birth details discussed above.

6.1.22 Were the closed register regime to be adopted, beneficial ownership details would be incorporated in a special section of the register of members and the sections of Forms 88 (2) and 363a/s with beneficial ownership details would be easy to separate from the current open record data. These sections could be copied to allow beneficial and legal ownership details to be submitted and/or processed separately.

6.1.23 Arrangements under the open register option for the protection of the privacy of individuals are discussed in *Protection of Privacy* below.

Enforcement

6.1.24 We have assumed that, as with the existing regime, there would be no active enforcement of the duty of legal and beneficial owners to notify companies, but active enforcement of the duty of companies to inform Companies House. We have also assumed that a publicity campaign would make clear the possibility of legal and beneficial shareowner non-compliance being subject to a civil penalty if detected from company records, and companies being subject to a standard late filing regime.

6.1.25 We have assumed the publicity campaign would also make clear the possibility of penalties and charges under other provisions, including the serious arrestable offence (where intent, recklessness or gross negligence in laundering or assisting to launder was proven). It would likewise warn of the wide range of enforcement officials including tax and VAT inspectors, able to check the register. The combination of heightened detection probability, sanction certainty, and potential sanction severity would substitute for a lack of dedicated enforcement effort (see also *Sensitivities* below).

6.1.26 In 2000/2001 Companies House collected civil penalties for late filing of accounts in excess of £25 million. These receipts went to the Consolidated Fund. In the same year Companies House received £2.2 million from the DTI to cover associated costs. Using the same penalty-to-cost ratio a 5% non-compliance rate with Option 3 would produce penalties of £3 million and costs of just over £250,000. Costs of justice have not been estimated.

Validation

6.1.27 As with the existing regime we have assumed that Companies House undertakes completeness checks but does not perform any validation checks. Where the generation of street addresses from postcodes resulted in different addresses being shown than the one supplied, the fact would be noted but not used as grounds for rejection, in line with current Companies House policy.

Companies House Cost Base

6.1.28 Estimating the costs involved at Companies House under these proposals has been complicated by a major programme of systems replacement and business change. The CHIPS (Companies House Information Processing System) initiative will involve the replacement of Companies House core mainframe systems (database and applications) and significant changes to many storage and retrieval methods over a three-year period. A key function of CHIPS is to meet requirements resulting from the Company Law Review (CLR), as well as the Government's policy objective of 100% electronic capability by 2005.

6.1.29 Accordingly, it is difficult to base estimates on alterations to current systems as these are the very systems facing substantial reengineering. It would only be possible for Companies House to provide such figures on the basis of a full and thorough exercise, which in any case might not be able to take into account the impact of wider developments the CLR.

6.1.30 We have therefore approached the problem of Companies House costs by looking at the number of forms processed by Companies House against its overall cost base. We have estimated the impact for each option in terms of additional forms, and additional form content, generated in approximate percentage terms, and applied these figures to the cost base. This produces an indication of the order of additional Companies House costs.

6.1.31 In the financial year ended March 2001 Companies House processed around 6 million forms in connection with registration activity, including 1.5 million Annual Returns and 1.8 million changes in directors particulars. Its expenditure was c. £38 million, giving a cost per form of £6.33. We have used this figure as a base for our calculations of costs to Companies House. Whilst this base figure is based on historic processing costs, it has the advantage that it can be adjusted at a later stage to gauge the impact on these proposals of changes to average cost per form e.g. as a result of the CHIPS system.

6.1.32 Where appropriate we have also provided private sector estimates for undertaking similar work. It should be borne in mind that such companies often use overseas labour for data entry at costs much lower than those that apply to Companies House, and do not have its public service obligations. They also have access to more modern equipment.

Other cost bases

6.1.33 We have assumed a labour rate of £5 hour for company secretarial duties, on the basis that maintenance of a register, though requiring checks by a company secretary or director, or even if completed by them, is in itself a task of a clerical nature. Postage rates reflect first class post. The possible cost of any legal/accounting advice sought is discussed below - see 6.12 Sensitivities above.

6.2 Costs of options

6.2.1 Estimates of the costs of various options are set out below, and should be read in conjunction with Table 1 Summary of Options. The descriptions of cost also build on descriptions of options contained in Section 4.

6.3 Option 1a

6.3.1 Direct costs to central government would comprise informing the public about changes to the law by notices to companies and media campaigns. The one-time cost of this has been assumed in talks with HMT and DTI to be around £1 million. As no routine controls are assumed, inspection of company registers would be in the course of other inquiries and therefore have zero marginal costs. Costs of penalising benign non-compliance is assumed to be zero or positive as set out above.

6.3.2 Legal owners would be mostly untouched by this option, except for the need to beneficial owner's details at the outset, which in the vast majority of cases would be by means of a box tick advise of change address, which they would need to do anyway to receive communications from the company. Their cost is therefore marginal.

6.3.3 Legal and beneficial owners will need to monitor their holdings in relation to the 3% threshold. This is a consideration a prudent person would take into account in any case and thus does not lead to marginal costs.

6.3.4 Transfers of legal ownership are in any case notified to the company and certification of beneficial ownership in such cases would involve negligible (box tick) additional effort or cost.

6.3.5 The only marginal costs are therefore beneficial owners' one-time notices of identification and occasional updates regarding transfers and changes of address. We have allowed £25,000 for ownership transfer reporting (12,500 transfers x £5/hour x 15 minutes plus £0.50 postage per report) and £7,000 for

detail changes (4,000 changes x £5/hour x 15 minutes plus £0.50 postage per report).

6.3.6 The compliance cost to the relevant companies is that of very minor changes to the company register and the time involved a matter of minutes for each. We have assumed costs simply mirror those of owners.

6.3.7 As the company register would provide an open register there is no extra cost for the public register option.

6.3.8 The direct and compliance costs that can be estimated are thus £1 million up front and £32,000 p.a. for both the closed and open register options.

6.4 Option 1b

6.4.1 The direct and compliance costs of Option 1b are of the same type as for Option 1a. There will be greater chance that more data will lead to more detection of transgression and higher costs of justice.

6.4.2 Extra reporting costs will result from the duty of beneficial owners to declare ownership annually. An estimate of the costs for beneficial owners would be c£220,000 (125,000 beneficial owners x £5/hour x 15 minutes £0.50 postage per report).

6.4.3 The corresponding company time involved in updating the company register would be c£160,000 (125,000 companies x £5/hour x 15 minutes). As the company register would provide an open register there is no extra cost for this option.

6.4.4 The marginal direct and compliance costs that can be estimated are thus £380,000 p.a. and apply to both open and closed registers.

6.5 Option 1c

6.5.1 The direct and compliance costs of Option 1c are of exactly the same type as for Options 1a & 1b. The marginal direct costs of Option 1c are again assumed to be zero or beneficial.

6.5.2 If all estimated transfers of beneficial ownership broke a 1% shareholding interval, the cost for beneficial owners would be an extra £25,000 (12,500 transfers x £5/hour x 15 minutes plus £0.50 postage per report).

6.5.3 The corresponding company time involved in updating the register would mirror this cost (i.e. a further £25,000). As the company register would provide an open register there is no extra cost for this option.

6.5.4 The marginal cost of option 1c is therefore c£50,000 for both open and closed register options.

6.6 Option 2

6.6.1 The marginal direct costs of Option 2 in respect of Companies House will include more expenditure on public education and guidance, alterations to the Annual Return form, data entry, checking, postage and handling costs, handling inquiries, processing rejections, enforcing compliance, and staff training. There might also be implications for systems maintenance costs, electronic filing and dissemination systems, contracts with suppliers and service providers as well as the mainframe systems investment program. All these costs are assumed to be reflected in the average cost per form calculated above.

6.6.2 The opinion of professionals and company data holders is that the changes to the Share Allotment and Annual Return forms would be relatively minor. Most declarations and confirmations of beneficial ownership would relate to legal owners and be effected by means of a box tick. The addition of details relating to persons who were only beneficial owners would involve a change of around 10% in form content. Applied to the approximate number of such forms submitted per year (236,000 + 1.5 million = c.1.75 million) the additional cost would be c£1.2 million (£6.33 x 10% x 1.75 million).

6.6.3 Entering beneficial ownership transfer details included on Annual Returns would involve a similar level of effort (12,500 x £6.33 x 10% or c£10,000). Entering changes in ownership details would have minimal cost impact.

6.6.4 Using private sector data capture costs of £25,000 per annum per 1,000 forms processed in a day (based on a 220 day year and overseas processing). The cost of data entry for just the additional or amended details on all 15,000 (12,500+ 2,500) annual forms involving beneficial owners would be c£2,000.

6.6.5 Company costs would be those of transferring beneficial ownership data held from Option 1b on to the shuttle form 363s and keeping it updated annually. This equates to an initial cost of c£160,000 (125,000 beneficial ownership details x £5/hour x 15 minutes) plus a yearly £16,000 (12,500 transfers x £5/hour x 15 minutes). Change of particulars would cost companies c£5,000 (4,000 changes x £5/hour x 5 minutes). The existing annual return postage costs would apply as there is no need to submit additional forms.

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6.6.6 It may be that private sector company data providers decide to add links to annual beneficial ownership details to their existing product range. According to representatives of such companies, the database and standard inquiry infrastructure is already in place. The principal costs involved would therefore be limited to purchasing data from Companies House and the adapting the search request, reporting and distribution systems.

6.6.7 The cost of obtaining data from Companies House, especially under the new CHIPS system, would be a commercial issue depending on a wide number of variables. No estimates have been made as any such charges might also offset Companies House costs. With regard to system development costs, company data providers thought that the type of systems envisaged might well be developed and offered as part of routine upgrades, i.e. at no additional cost. However we have allowed £300,000 upfront and £250,000 p.a. for the development and running of one such system.

6.6.8 The marginal costs estimated for Option 2 are therefore c£460,000 up front and c£283,000 p.a. for companies and data providers, and c£1.2million p.a. for government. As we have based costs on expenditures under an open register regime, this is taken to be the public register cost option. The private register cost would be slightly lower on account of the lesser number of inquiries and queries from the general public to be handled by Companies House. We have used totals of £125,000 up-front and £1 million p.a.

6.7 Option 3

6.7.1 Option 3 involves processing legal and beneficial ownership details as they occur, rather than via the Annual Return as in Option 2. As a result, companies would have to submit more forms during the year but have less data to write up on the Annual Return.

6.7.2 The total number of transfers to be notified by companies would be c512,500 (500,000 legal and 12,500 beneficial). Using a labour cost of £5/hour, 15 minutes time per transfer and £0.50 postage the total cost to companies for notifying transfer is £640,000 +£256,000 = c£900,000.

6.7.3 The total number of change of ownership details would be c162,000 (157,500 legal + 4,000 beneficial) On the same basis the cost to companies of these notifications is c£285,000.

6.7.4 The total cost to companies is thus £1.2 million but it is partially offset by the lower effort required to complete the Annual Return, as some of the details submitted during the year would already be included in the shuttle form.

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6.7.5 The total number of forms to be processed by Companies House would be c.675,000 (512,500 + 157,500 + 4,000). At the full average form rate of £6.33 the cost to Companies House is estimated at £4.3 million. Again, this would be partly offset by the reduced number of details to be processed in the Annual Return.

6.7.6 The open register cost is assumed to be covered by the assumed cost of form processing and may be offset by charges made for access, as with the current system for obtaining annual accounts and returns. The marginal cost for a private sector database operator would be the increased frequency of updates in respect of which an additional £100,000 p.a. has been allowed.

6.7.7 The marginal cost of Option 3 is therefore estimated at c£5.6 million p.a. Again these are costs under an open register regime and the private register costs would be slightly lower (we have used £5.3 million p.a.) for the same reason as Option 2.

6.8 Option 4

6.8.1 As all data is already captured, the costs of this option relate solely to the provision of database maintenance and search facilities and the additional cost of making the information available to the general public under the open register option.

6.8.2 This is the type of system that might be introduced under the new CHIPS system and the cost of doing so depends on too many variables to enable a meaningful detailed estimate. Those we talked to at Companies House expressed the view (but we stress not an official Companies House opinion) that systems such as those covered by Options 4 and 5 cost several millions of pounds.

6.8.3 Private sector establishment costs for a similar system using the data from Option 3 were estimated by credit reference agencies to be around £100,000 - £250,000 with annual maintenance costs of about half these levels. To allow for the higher cost base of Companies House and the other duties it performs we have estimated Companies House future IT costs conservatively at £1 million up front and £500,000 p.a. for the open system. The closed system costs would be lower.

6.8.4 We do not have figures for the cost of data obtained from Companies House by credit reference agencies. Some agencies thought the cost of additional beneficial ownership details to end-users for routine purposes would be very low as it would probably form part of routine system upgrades for which budgets already exist. Prices for special analysis of data would be agreed with users on an ad hoc basis.

6.8.5 The marginal cost of Option 4 is therefore estimated at c£1 million up front and £500,000 p.a. for the closed system and £1.25 million up front and £625,000 p.a. for the open system.

6.9 Option 5

6.9.1 The costs of this option relate solely to the extension of the beneficial and shareholder database to cover directors and shadow directors. As both categories of director are already collected by Companies House (without distinction) the costs involved are the technical costs of system unification. We would estimate these conservatively at a further £1 million up front and around £500,000 p.a. based on the costings set out in Option 4. This includes the cost of making the information available to the general public under the open register option, so the closed register option would cost slightly less.

6.9.2 The availability of a single Companies House stream of data on shareholdings and directors would probably lessen the costs of processing for credit reference agencies. However we have allowed the same figures as before for private sector costs. The same points regarding cost of data from Companies House and to Customers apply.

6.9.3 The marginal cost of Option 5 is therefore a further c£1 million up front and £500,000 p.a. for the closed system and £1.25 million up front and £625,000 p.a. for the open system.

6.10 Quantity, quality and variety of goods sold

6.10.1 Whilst probably negligible at the macro level, the theoretical effect of compliance costs and direct costs, passed on to companies as taxes and higher fees, may be to increase prices of goods and services and thus reduce sales. There may be less quality and/or variety of goods as production standards and/or product range are cut to maintain prices. It is not possible to allocate these effects to individual options but they are a larger risk in the case of the more costly options and will affect companies operating on small profit margins more than those on high ones.

6.10.2 By providing vendors with greater transparency about their purchasers and vice versa the proposals may lead to decisions to raise prices to cover risks or not to purchase goods. A fall in sales may result. Transparency is a feature of the open register options and more likely to be associated with the higher open register options.

Competition

6.10.3 Increased transparency may also persuade some companies with valid reasons for wanting to retain anonymous beneficial ownership to leave the registry and likewise discourage similar companies from establishing themselves. It would appear that 5 - 10% of current company formations through company formation agents have overseas links and some of these companies are attracted

to the UK by virtue of the disclosure regime. The exit from the market of such firms would lead to a decrease in competition and loss of income from their investment in UK goods and services.

6.10.4 There may be a knock-on effect on company service providers who will experience less demand for their services from those from that decide to go or remain offshore, though many company service providers may be able to help their clients establish elsewhere.

6.10.5 Given the low compliance cost to 80% of businesses, it is highly unlikely that companies will not be able to absorb the marginal cost of the regime. Some small, inefficient companies may not be able to comply with the regime and be wound up.

6.11 Additional costs

6.11.1 The additional costs mentioned below may arise in connection with the proposed measures. The likelihood of their arising rises with the complexity of the options.

6.11.2 The need for the data captured by the system to be accurate may require Companies House to improve its procedure with regard to information checking. As this is already the subject of another Companies House initiative we have assumed there are no marginal costs involved. The same may be required of the police national computer before its data can be usefully combined with that obtained via the proposed measures.

6.11.3 Where a company noticed and reported a discrepancy it might become involved in an investigation that would divert its resources from production of goods and services.

6.11.4 Company service providers will need to update their procedures to cope with the new regime. Software providers will need to update turnkey company formation and secretarial packages. However, Companies House has pointed out the use of such packages to effect filing has been disappointingly low, which Companies House attributes to the high cost of the software involved.

6.11.5 Legal and accounting firms would have to learn and study the implications of the proposals. Given the number of firms and individuals involved, the effect of this over a number of professions might amount to several millions of pounds. In terms of the amount of effort that has to be given to the CLR as a whole, the time involved is very small.

6.12 Sensitivity of cost estimates

Shareholders

6.12.1 There are other ways of estimating the number of shareholders which produce both smaller and larger numbers. The numbers used here represent the

figures felt to be most reasonable by company formation agents and are based on one particular set of Companies House figures.

6.12.2 There large number of owners and companies. Relatively small additional expenses on each shareholder can result in much larger cost increases overall. One potentially large cost is legal fees for advice on how to stay within the new rules. It is not possible to say what the legal costs to companies and individuals would be without knowing how, and how well, the proposals would be framed, and the extent and efficiency of the public information campaign that would accompany the measures.

6.12.3 We have assumed that the stricter definition of beneficial ownership analysed here would be clearly and unequivocally defined in law and that Companies House would put out similar plain language information, so that both legal and beneficial owners would know their position and duties. This being the case, most companies and individuals would have, as now, little need to take legal advice, or would obtain it free of charge through business association and other business literature.

6.12.4 However, it is possible that a small percentage of companies and individuals might still do so. Cost would accrue at just over £1 million for every 1% of the 300,000 companies and 125,000 potential beneficial owners that spend £250 on legal advice.

6.12.5 Another large potential cost is communications with shareholders. Where these are included in the Annual Report package usually sent to shareholders by companies the marginal cost is limited to the cost of producing the memo itself which would depend on the subject. The postage cost of mailing shareholders in non "" firms would be just over £1 million per mailshot.

CHIPS

6.12.6 Over time, Companies House' electronic filing initiative may reduce direct costs. However, there might be a corresponding increase in compliance (systems) costs and thus zero net effect.

6.13 Human rights costs

6.13.1 By intent, the proposals affect unlisted companies most of which are small and medium sized firms. As set out above the burdens are not inconsistent or disproportionate. However, they do raise issues of fairness and possible conflict with other regulation. The areas involved include the Human Rights Act 1998, Data Protection Act 1998, Public Interest Disclosure Act 2000, Regulation of Investigatory Powers Act 2000, Freedom of Information Act 2000 and sections 723B-F Companies Act 1985 as inserted by section 45 Criminal Justice and Police Act 2001.

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6.13.2 Data protection considerations should not give rise to any real concern. Some companies still that all those holding information on others, electronically, need to be registered with the Data Protection Commissioner, save for certain limited exemptions.

6.13.3 It may be that beneficial ownership information can be dealt with under the exemption in Section 29 DPA, the exemption for data processed for the prevention or detection of crime. In any event all those holding information on their directors should already be covered by a DPA licence. Adding a register of beneficial owners will not involve significant additional cost, other than provisions to grandfather in those already registered under DPA, and to amend the admission procedures for companies seeking a DPA licence. The precise nature of the final provisions is unknown, the costs have not been calculated.

6.13.4 For similar reasons we believe that Article 8 of the Human Rights Convention, as implemented by the Human Rights Act 1998, the right to privacy, will not pose any problem since it also contains in relation to the detection or prevention of crime to the data protection regime

6.13.5 Another issue is whether creation of a criminal offence in an area where the majority of those affected are law abiding will create opportunities for unintentional, unavoidable or reckless drift into crime. The provision for warnings and lesser penalties for the lesser crimes should provide a safety for the inept as opposed to the criminal transgressor.

6.14 Protection of privacy

6.14.1 With regard to the other Acts, there are a number of valid reasons why certain target group members would not want beneficial ownership information disclosed publicly. The dilemma for government is that a disclosure system to protect society from one threat may be abused by those representing the same or a different threat. Striking a balance between level of disclosure and effectiveness of a system on one hand and cost and complexity on another can be difficult or impossible. A system that is fair to all parties may risk protecting neither. The analysis we present below focuses on protecting those in real danger to life and limb at the lowest reasonable cost, whilst ensuring the beneficial ownership disclosure system produces the breadth and depth of disclosure required to function effectively.

6.14.2 In other fields, accepted reasons for limiting disclosure include:

- witness protection, though presumably identities can be created which cater for witnesses with beneficial ownership
- family trusts that have family “political” issues tied up in their structure
- companies that do not want employees or customers to know exactly what shareholders have a stake in them
- commercial confidence (e.g. planning a legal takeover). Here, however, it can also be argued that a transparent environment would foster more business than it would prevent, owing to the greater market confidence generated.

6.14.3 In particular, it might not be in the public interest for ownership details of politically vulnerable companies and individuals to be in the public domain. Radical activists have targeted members of the UK fur trade as well as shareholders and officers of animal testing laboratories using addresses obtained from Companies House. We were asked to estimate the cost of a separate system to allow such data to be kept confidential.

6.14.4 We talked to a number of experts on such incidents. They confirmed that, whilst many cases involved listed companies outside the scope of this project, there was a need to protect vulnerable smaller companies and importantly, vulnerable shareholders in non-vulnerable smaller companies. This is because shareholders in a politically sensitive company might be targeted using details of their shareholding in another company.

6.14.5 Concerns were also expressed that the allow company directors to service addresses would not prevent their residential addresses soon being established by other means. Proposed limitations on the use of such data would also be ineffective in such cases. thus provide an element of privacy to the many but no anonymity to the few—based on police estimates around 250 companies and 250 individuals nationally are under real threat of attack.

6.14.6 Notwithstanding these reservations, one option to preserve the privacy of shareholders is to extend to them measures similar to those proposed in the Company Law Review for directors, giving them too, the option to provide a service address in addition to a residential address.

6.14.7 Accordingly under the closed register option of these proposals, beneficial owners and legal owners would supply a residential address and, if so desired a service address to the company. Only the details of legal owners would appear in the company register and Companies House records, with the service address used, where supplied. Residential addresses of legal shareholders and full details of beneficial owners would be kept separately and made available to law enforcers and regulators.

6.14.8 Under the open register option, the same system would apply except that the names and residential or service addresses of beneficial owners would be included in the open records.

6.14.9 Under the open register option, to obtain the benefits to industry from better credit scoring, and to law enforcement from matching public and private sector data, arrangements would be made to give approved parties access to restricted address data. Arrangements for controlled private sector access to electoral role data provide a precedent for so doing.

6.14.10 As "" companies account for over half of all companies, and usually operate from a registered address which is often the residential address, the

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take-up of the service address option offers little advantage and is unlikely to be exercised in such cases. However, a solution would have to allow for double the number of shareholder addresses supplied to companies and Companies House, and subsequent changes.

6.14.11 Assuming the addition of such data constituted a 20% change to forms submitted by half of all companies, the cost would be at least £1 million (1.5 million companies x 50% x £6.33 x 20%). However it is possible this amount might be covered in the several millions of pounds figure that Companies House experts thought a system with annual update and transfer notification would cost.

6.14.12 Two factors support this argument or would at least tend to reduce the costs involved. First, as the solution would track the regime for directors there would be opportunities for synergies and economies of system design between the two systems. Secondly, Companies House's intention to move towards direct electronic data entry would likewise reduce costs to Companies House and companies concerned by obviating the need for data entry at Companies House and possibly enabling companies to produce registers automatically.

6.14.13 Though no scheme can guarantee anonymity, an alternative to tracking the is that, on police advice companies in politically sensitive fields might apply to the DTI for exemption from public filing for their shareholder details. Politically exposed individuals might similarly apply for an exemption with regard to their shareholdings generally.

6.14.14 Exempt companies would simply maintain the records as usual but without public access. In addition to shareholder details, the company would file a copy of the exemption with Companies House, which would then be put on public register. The number of shareholders and the size of their holdings (individually or in total) might also be shown. Records at the company and Companies House would be available for inspection by regulators and law enforcers and by court order for genuine inquirers, but not passed on to the private sector under controlled access schemes.

6.14.15 Exempt individuals would furnish their personal data to any non-exempt company concerned, accompanied by details of their exemption. The company would keep the data confidential from the public, and report them as usual to Companies House along with details of the exemption. Companies House would also keep the data confidential but publish the number of shareholders holding exemptions and the size of their holdings (individually or in total) as supplied by the company. All records would be accessible directly by law enforcement, and by genuine inquirers via the courts

6.14.16 The cost to government of administering the tighter system would be relatively low, as applications would be subject to clear and strict criteria which would be easily verifiable by the police investigating the underlying public order issue, who would thus be able to act as a filter for such applications at a low

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marginal cost. As stated above, in the long run we have assumed that Companies House would be able to establish a confidential area of its database and the procedures for maintaining it. In the short run, we have assumed that a stand-alone system would be set up (e.g. on a PC using a proprietary database program such as Access) which can handle all standard database tasks with negligible record and file length limitations.

6.14.17 To estimate the cost of a limited system, we allowed £50,000 one time costs for hardware and software (assuming one live system and one backup), allowing one working day per application, and assuming 500 applications were reviewed every year, the time involved is 500 working days per year. Using lower, median and upper gross salary bands for non-industrial staff (as per Civil Service Statistics 2000 Page 47), the basic DTI/Companies House gross salary cost of such a system is around £30,000 p.a. The minimum annual running costs to government of a basic system (excluding any other capital costs) might be reasonably assumed to be in the order of £100,000 -£200,000 p.a.

6.14.18 The major cost for the companies and individuals involved would be the time spent applying for the exemption. The application might easily consist of a one-page letter. In view of the small number of persons and individuals involved with diverse cost bases, we have not calculated the cost of this activity. As these companies and individuals represent a high risk it may in any case be necessary to undertake these actions to obtain insurance cover. We would estimate it as a matter of a few tens of thousands of pounds. The government time spent separately recording and storing such exemption details is already allowed for in the estimates for the basic system.

6.14.19 would greatly reduce the volume of data processing, but would result in more addresses being published than under the . As an additional measure it would help close the risk gap for those most vulnerable.

6.14.20 Provided due attention is given to justifying the introduction of these proposals, setting out a clear definition of beneficial ownership and making the nature of the disclosure obligation known, then the obstacles to spontaneous compliance are low for Options 1a, 1b and 2 which carry only an annual disclosure burden. As most companies involved see little transfer of their shares compared to listed companies, obstacles to spontaneous compliance for Options 1c and 3 are not that much higher.

6.14.21 Options 1a, 1b and 1c would be cheapest to enforce, controls being probably covered in the course of other enquiries and Option 3 the most expensive. If money were no issue, Options 2 and 3 would be easiest to enforce, as non-disclosure would be tracked by Companies House.

7. ALTERNATIVES

7.1 Alternative 1: Annual disclosure of any beneficial ownership

7.1.1 We were asked to consider the alternative of establishing a database which records the details of legal ownership, the fact of beneficial ownership and which is updated annually.

7.1.2 This alternative would require nearly the same reporting requirements on legal and beneficial shareholder as Option 1b, save that beneficial owners would not have to monitor and report levels and changes in beneficial holdings. This would make reporting by beneficial owners and recording by companies slightly easier. We have therefore reduced the cost given in Option 1b from £380,000 to £300,000 p.a.

7.1.3 Companies would submit the information on beneficial ownership to Companies House by including it in the Annual Return. In similar fashion to Option 2. The costs involved to companies are £160,000 up-front and £25,000 p.a. Again, as less data is required we have reduce these to £150,000 and £20,000. The cost involved to government is c£1.4 million which we have left unadjusted.

7.1.4 The cost of the database is similar to the costs under Option 4, or £1 million up front and £500,000 p.a. for the closed system and slightly higher (£1.25 million and £625,000 p.a.) for the open system.

7.1.5 The alternative would therefore have up-front costs of around £2.4 million up front and £820,000 p.a. for the closed system and £2.65 million up front and £945,000 p.a. for the open system.

7.1.6 As the data would only be available annually, and thus lose much of its intelligence value, this alternative lies closest to Option 2 and attracts at best first order benefits, and only then if the data were placed on open record. Like Option 2 it would be of most benefit in long running inquiry cases and could not be relied on in the case of late stage investigations or current threats where current data is vital.

7.2 Semi open record

7.2.1 Public policy may preclude the open register route, for fear of placing individuals at risk. Allowing trusted credit reference agencies access to closed data on condition the information was kept confidential and anonymised would provide a means of preserving many of the benefits of the open register options without the risk of information obtained under the proposals being abused. The effects on costs would be small and the superiority of benefits over costs would remain in all cases unaffected.

7.3 Status Quo

8. CONCLUSIONS AND RECOMMENDATIONS

8.1.1 As can be seen from Tables 4a & 4b, for each option the intentionally limited scale of benefits exceed the costs, in the higher options by a wide margin.

8.1.2 The option that best meets law enforcement requirements at least cost and with the greatest potential long term benefit is the Option 3 Open register version. This costs £1.5 million up front and £7.6 million p.a. whilst producing £30.3 million p.a. in benefits. Functionally, the best closed register solution is Option 5 would cost more both up front (£3.2 million) and p.a. (£7.8 million) and bring benefits of £20 million p.a. The next best closed register option is Option 2 Closed.

8.1.3 If money is no object then the next best open register solution is Option 5 Open, which would create a full database under government control as well as enabling links to private sector systems. Option 4 Open, though slightly cheaper, would fail to unify the shareholder and director databases. If money *is* an issue then Option 2 Open is the next best choice.

8.1.4 If wide scale non-compliance is thought to be a risk then the choice is between Option 3 Open, where the greater benefits form a cushion, and Option 2 Open which offers the greatest possible gain for the least possible loss, whilst still offering very basic functionality. By the same criteria Option 2 offers the best choice if the closed route is selected.

8.1.5 To be effective, all options will require the serious arrestable offence outlined in this RIA to be introduced. The move from annual change reporting under Option 2 to reporting changes as they occur (Option 3) does require a firmer enforcement regime than at present. However, because of the shareholding structure of most private companies, tighter proposals will not affect as many companies as might be thought.

8.1.6 Moreover, any marginal burdens imposed are relatively small in size, not unreasonable in nature and more than compensated for in the greater scheme of things by the creation and preservation of a safer society and business environment.

8.1.7 More generally, law enforcement in the UK is moving away from reactive investigation after the events to targeting active criminals on the balance of intelligence. To quote Sir David Phillips, QPM Chief Constable of Kent:

"Intelligence usually means making inferences from large amounts of data. This process is only possible if we can mix and match data from across the board....We should be able to aggregate the national picture on a much more informative way.

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8.1.8 Without the data and databases created by the higher options, the proposed systems will not be able to contribute to this process or fulfil the requirements of the guidelines in the OECD Report on Misuse of Corporate Vehicles. We therefore recommend that Option 3 (open register) be implemented to create a system which uses the resources of the private sector and to leverage data that can only be collected by the public sector.

8.1.9 If a "soft landing is wanted, Option 2 Open offers a route to introduce the regime gradually. Disclosure could be introduced on an annual basis to start off with, possibly using a 10% initial threshold, and then tightened at a later date (e.g. to coincide with new systems at Companies House). However it is only worth going this route if it were intended to upgrade the level of disclosure in the not too distant future to gain third order economies.

8.1.10 Before choosing a Closed Option, the semi-open option should be looked at in detail on account of the substantial added benefits it would most likely bring.

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Appendix 3	Principal organisations contacted
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TABLE 1: SUMMARY OF OPTIONS FOR DECLARATION OF BENEFICIAL OWNERSHIP						
OPTION	KEY POINTS OF DUTY				ENQUIRY MECHANISM	COMMENT
	ON WHOM?	DISCLOSE/DO WHAT?	TO WHOM?	WHEN?		
1a	Beneficial owner of > 3%	a) Unspecified holding above threshold b) Holding now below threshold	Company	Not specified; Assume upon settlement	Made available to law enforcers and regulators	Private companies
1b	Beneficial owner of > 3%	a) Percentage at outset b) Change over year	Company	Annually	Same	Private companies; In addition to 1a
1c	Beneficial owner of > 3%	Each time holding rises by 1%	Company	2 days (?)	Same	Private companies; in addition to 1b
2	Company	Name of beneficial shareholder >3% and percentage held	Companies House (via annual return)	Annually	Same	Private and unlisted public companies. In addition to 1c
3	Company (?)	Changes of >= 1% in: a) legal share ownership b) beneficial ownership	a) To Companies House	Upon settlement	Same	Private and unlisted public companies in addition to 2
4	Companies House	Maintain database of shareholdings and beneficial interest	n/a	n/a	Same; search and listing by name	In addition to 3. All companies.
5	Companies House	Maintain database of directorships and shadow directorships	n/a	n/a	Same; search and listing by name	In addition to 4. All companies.
Closed	Company	Publish relevant data	Public	As above	Public register	(Options 1a, 1b 1c)
Open	Companies House	Publish relevant data	Public	As above	Public register	(Options 2 - 5)

OPTION	TABLE 2: SUMMARY OF LAW ENFORCEMENT BENEFITS			
	AREA/NATURE OF BENEFITS			
	Intelligence	Investigation	Evidence Gathering	Deterrence
1a	Basic screening Open Register allows tipping off	Detailed screening. Easier linking to past crime	Easier proof of links to past crime	Limited displacement
1b	Change data may be useful Open Register allows tipping off	Change data may suggest active links	Change data might help prove active links	Limited displacement
1c	May increase number/value of suspicions reported Open Register allows tipping off	May allow wider/ quicker/ deeper investigations	May allow quicker and more substantial proof.	Some deterrence due to higher risk of detection
2	As all above. Easier access wider data No tip off risk Limited mix and match*	As all above Easier access to wider range of data No tip off risk	As all above Easier access to wider range of data No tip off risk	All the above. Easier access to wider range of data No tip off risk
	Open register allows limited mix and match with private sector databases. Some improvement in all areas from easier informal access to larger amounts of data on beneficial ownership and company officers			
3	As all above Easier lead intelligence.	As all above. Easier monitoring of suspects	As all above Easier to get key details.	Beginning of crime displacement due to real time data
	Open register allows limited mix and match with private sector databases. Large improvement in all areas from easier informal access to larger amounts of timely data on legal and beneficial ownership and company officers. Smart systems possible.			
4	Reverse search and smart systems for shareholdings become possible under a closed system. Open system may benefit from single data feed and back up.			
5	Reverse search and smart systems for shareholdings and company officers become possible under a closed system. Open system may benefit from single data feed and back up in case of critical event.			

TABLE 3 FACTORS OF ORDERS OF ECONOMY AND OPTIONS CONCERNED				
<u>BENEFIT OBTAINED</u>	<u>BASE CASE</u>	<u>1ST ORDER</u>	<u>2ND ORDER</u>	<u>3RD ORDER</u>
BENEFICIAL OWNERSHIP DETAILS	NO	YES	YES	YES
LEGAL OWNERSHIP DETAILS	YES	YES	YES	YES
USER FRIENDLY INQUIRY	NO	LIMITED (2 Open) NO (Rest)	YES	YES
ACCESS TO WIDER DATA	NO	LIMITED (2 Open) NO (Rest)	NO	YES
TIMELY DATA	NO	YES (3 Closed) NO (Rest)	YES	YES
OPTIONS CONCERNED	N/A	<i>1a – c Open and Closed 2 Open and Closed 3 Closed</i>	<i>4 Closed 5 Closed</i>	<i>3 Open 4 Open 5 Open</i>

TABLE 4a: SUMMARY OF COSTS AND BENEFITS – OPEN RECORD

OPTION	MARGINAL COST (£)		RUNNING TOTAL (£)		ORDER OF ECONOMY ATTRACTED	VALUE OF BENEFITS (£)
	UP FRONT	PER ANNUM	UP FRONT	PER ANNUM		
1a	1M	0.03M	1M	0.03M	1	5.1M
1b	-	0.4M	1M	0.4M	1	5.1M
1c	-	0.05M	1M	0.5M	1	5.1M
2	0.5M	1.5M	1.5M	2M	1	5.1M
3	-	5.6M	1.5M	7.6M	3	30.3M
4	1.3M	0.6M	2.8M	8.2M	3	30.3M
5	1.3M	0.6M	4.1M	8.8M	3	30.3M

TABLE 4b: SUMMARY OF COSTS AND BENEFITS – CLOSED RECORD

OPTION	MARGINAL COST (£)		RUNNING TOTAL (£)		ORDER OF ECONOMY ATTRACTED	VALUE OF BENEFITS (£)
	UP FRONT	PER ANNUM	UP FRONT	PER ANNUM		
1a	1M	0.03M	1M	0.03M	1	5.1M
1b	-	0.4M	1M	0.4M	1	5.1M
1c	-	0.05M	1M	0.5M	1	5.1M
2	0.2M	1.0M	1.2M	1.5M	1	5.1M
3	-	5.3M	1.2M	6.8M	1	5.1M
4	1M	0.5M	2.2M	7.3M	2	15.2M
5	1M	0.5M	3.2M	7.8M	2	15.2M

TABLE 5a: SUMMARY OF REDUCED BENEFITS AT CONSTANT COSTS – OPEN RECORD

OPTION	MARGINAL COST (£)		RUNNING TOTAL (£)		BENEFITS AFTER NO. OF REDUCTIONS IN ORDER OF ECONOMY DUE TO NON-COMPLIANCE (£)			
	UP FRONT	PER ANNUM	UP FRONT	PER ANNUM	NONE	ONE	TWO	THREE
1a	1M	0.03M	1M	0.03M	5.1M	0M	0M	0M
1b	-	0.4M	1M	0.4M	5.1M	0M	0M	0M
1c	-	0.05M	1M	0.5M	5.1M	0M	0M	0M
2	0.5M	1.5M	1.5M	2M	5.1M	0M	0M	0M
3	-	5.6M	1.5M	7.6M	30.3M	15.2M	5.1M	0M
4	1.3M	0.6M	2.8M	8.2M	30.3M	15.2M	5.1M	0M
5	1.3M	0.6M	4.1M	8.8M	30.3M	15.2M	5.1M	0M

TABLE 5b: SUMMARY OF COSTS AND BENEFITS – CLOSED RECORD

OPTION	MARGINAL COST (£)		RUNNING TOTAL (£)		BENEFITS AFTER NO. OF REDUCTIONS IN ORDER OF ECONOMY DUE TO NON-COMPLIANCE (£)			
	UP FRONT	PER ANNUM	UP FRONT	PER ANNUM	NONE	ONE	TWO	THREE
1a	1M	0.03M	1M	0.03M	5.1M	0M	0M	0M
1b	-	0.4M	1M	0.4M	5.1M	0M	0M	0M
1c	-	0.05M	1M	0.5M	5.1M	0M	0M	0M
2	0.2M	1.0M	1.2M	1.5M	5.1M	0M	0M	0M
3	-	5.3M	1.2M	6.8M	5.1M	0M	0M	0M
4	1M	0.5M	2.2M	7.3M	15.2M	5.1M	0M	0M
5	1M	0.5M	3.2M	7.8M	15.2M	5.1M	0M	0M

TABLE OF CONFORMITY WITH COMMON RIA HEADINGS

The following generic RIA topic headings are based from various international RIA formats. The location of where they are mainly covered in this RIA is given in italics underneath the respective heading.

- Background
Section 2
- Base case
Section 3
- Risks
Appendix 2
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Section 3
- Proposals
Section 4
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Section 4
- Assumptions
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- Alternatives to regulation
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- Impact of consultation:
Next stage
- Conclusions as to the likely impact of the regulations
Section 8
- Recommendations
Section 8

RISK ANALYSIS

Set out below is a description of the risks the proposals address. As money laundering is a derivative crime, i.e. another crime must be committed before money laundering is possible, it is important to distinguish between the risks relating to beneficial ownership and risk relating to money laundering and underlying crime generally.

Risks relating money laundering generally

In extreme cases, money laundering schemes are associated with risks to life and limb such as terrorism, kidnapping, and threats of violence. The victims are often innocent third parties targeted because they are in positions of trust and can facilitate money laundering. It is also associated with murder, serious assault and damage to property, the victims here being more likely to be criminal themselves.

The scale of these risks is outside the scope of this RIA. However, it is probable that a small number (units) of the violent deaths in the UK each year involve disputes about laundering proceeds as distinct from committing the underlying crime.

Money laundering also has an effect on the financial institutions used to carry out money laundering. It does so by:

- Creating the illusion that more bona fide business exists than in reality
- Distorting market pricing mechanisms by creating false demand for products and services
- Damaging the reputation of institutions unwittingly or negligently involved

Ultimately, money laundering can damage the reputation for integrity of financial centres and the regulatory systems involved. Studies have shown that countries with a high reputation for integrity are generally more successful in attracting business than those with low reputations.

Again it is very hard to quantify the risk involved here and the proposals below relate only to one aspect of measures to prevent money laundering. Given the crucial role of trust in enabling business and government to take place, any risk to the reputation of the UK as a financial centre and as a competent regulator is a matter of prime concern. Historically and in extreme cases, the effect of money laundering scandals on companies (e.g. EF Hutton, BCCI,

Bank of New York), markets (e.g. tin, copper) and countries (e.g. Czech Republic) can be catastrophic

Risks relating to underlying crime

The major forms of crime underlying money laundering are drug trafficking, fraud, organised crime, terrorism, tax evasion, tobacco smuggling, people trafficking and prostitution. At this level, crime is an issue of national importance and the government's ability to retain public confidence a key factor in upholding the rule of law.

PRINCIPAL ORGANISATIONS CONTACTED

ACPO
Avon & Somerset Police
British Chambers
CBI
City of London Police
Companies House
CRG
D&B
DWP
DTI - Investigations
DTI - SBS
Experian
FSA
FSB
HM Customs and Excise
HMT
Home Office
ICAEW
ICSA
Inland Revenue
IoD
IPSA
Jordans
KPMG
Law Society
Metropolitan Police
National Crime Squad
NCIS
Norfolk Police
OCRA
PWC
SFO
Special Branch

UK SHARE TRANSFER PROCEDURES - PRIVATE COMPANIES

First the stock transfer form must be completed, signed and dated by the transferor. The completed form, the share certificate and any fee (e.g. including stamp duty) should then be sent to the company secretary or registrars who deal with the share transfers of the company. In certain circumstances for share transfers, no duty is payable to the Inland Revenue as stamp duty. The stock transfer form is handed to the transferee in exchange for the consideration and the transferee is responsible for meeting any stamp duty payable. Once stamped, the stock transfer form can be passed to the company secretary for processing.

The company secretary will then:

- Check the stock transfer form
 - name given on the form should agree with the register of members
 - name on share certificate should agree
 - address is as expected
 - ensure share details are correct and agree with the certificate
 - where the transferee has a liability, they should also sign
- Ensure the consideration given is “reasonable”
- Check share certificate is original
- Check appropriate transfer fee has been enclosed
- Transfer form may need to be stamped by Inland Revenue
- Check register of members that no legal restraint on transfer, does the number of shares being transferred agree with the entry in the register of members
- If shares are partly paid, ensure amount paid up is correct and if remainder should be paid before transfer, ensure it has been
- Cancel old share certificate, where the certificate is for more than is being transferred, a balancing certificate must be prepared and sent to the transferor
- Registration of the transfer and the stock transfer form should be approved by the board, authority also being needed for the use of the company seal, if appropriate
- Make the necessary entry in the register of transfers
- Make the necessary entry in the register of members, closing account of transferor and opening the account of the transferee, with details of the holding
- Issue new share certificate and send to transferee or his representative
- File stock transfer form and cancelled certificate

APPENDIX 5**COMPANY FORMATION COMPARATIVE COST DATA**

Jurisdiction	Company	Shelf Co.	Licence Fee/Tax (£UK)	Fees (£UK)	
				Annual Filing	Incorp'n
Anguilla	IBC	Yes	155	Nil	500
Bahamas	IBC	Yes	245	Nil	500
Belize	IBC	Yes	75	Nil	335
Bermuda	Exempt	No	1120	Nil	2850
BVI	IBC	Yes	225	Nil	335
Cayman Is	Exempt	Yes	390	Nil	1000
Cook Is	International	No	335	Nil	1500
Costa Rica	SA	Yes	100	Nil	530
Cyprus	IBC	Yes	4.25%	Nil	1000
Denmark	Holding	No	Varies	Nil	3450
Gibraltar	Exempt	Yes	250	45	530
Hong Kong	Private Ltd	Yes	400	135	535
Hungary	Offshore Kft	No	3%	45	3450
Hungary	Offshore RT	No	3%	45	3450
Iceland	ITC	No	800	Nil	3470
Ireland	Private Ltd	Yes	Varies	150	400
Isle of Man	Exempt	Yes	430	50	530
Isle of Man	International LLC	Yes	430	50	530
Isle of Man	Resident	Yes	20%	50	530
Israel	Non Resident	Yes	Nil	135	1250
Jersey	Exempt	No	600	130	800
Labuan	Offshore trading	No	0, 3% or \$8000	570	1835
Liberia	Non Resident	Yes	100	Nil	635
Liechtenstein	Corporation	No	4% div tax	Nil	1670
Luxembourg	1929 Holding	No	0.2% capital	Nil	2750
Luxembourg	1990 SOPARFI Hldg	No	Varies	Nil	2750
Madeira	Limitada	Yes	670	Nil	Varies
Malta	Non trading	No	Varies	135	2670
Mauritius	International	Yes	75	Nil	500
Mauritius	Offshore	No	1000	Nil	1000
Netherlands	BV	No	Varies	335	3450

Netherlands Antilles	Offshore trading	No	c 30%	45	2000
Nevis	NBCO	Yes	150	Nil	530
Niue	International	Yes	100	Nil	530
Panama	Non Resident	Yes	100	Nil	530
Samoa	International	Yes	225	Nil	530
Seychelles	IBC	Yes	75	Nil	335
St. Vincent	IBC	No	75	Nil	530
Turks & Caicos	Exempt	Yes	225	Nil	530
UK	LLP	Yes	Fiscally transparent	50	295
UK	PLC	Yes	20-30%	15	295
UK	Private Limited	Yes	20-30%	15	295
Uruguay	Non Resident	No	0.3% capital	Nil	2000
Vanuatu	International	No	225	Nil	800
Arkansas	LLC	Yes	Nil	45	335
Delaware	LLC	Yes	Nil	75	335
Florida	LLC	Yes	Nil	35	535
New Jersey	LLC	Yes	Nil	35	335
Oklahoma	LLC	Yes	Nil	Nil	335
Oregon	LLC	Yes	Nil	75	335
Washington DC	LLC	Yes	Nil	35	335
Wyoming	LLC	Yes	Nil	75	400
New York	LLC	Yes	Nil	Nil	635
California	C Corp	No	Varies	535	935
Delaware	C Corp	Yes	Varies	35	335
Florida	C Corp	No	Varies	100	400
Nevada	C Corp	No	Varies	60	535
New Jersey	C Corp	No	Varies	30	400
Oregon	C Corp	No	Varies	35	335
Wyoming	C Corp	No	Varies	75	335

EXEMPTIONS FROM STOCK TRANSFER FORMS

- Vesting of property subject to a trust in the trustees of the trust on the appointment of a new trustee, or in the continuing trustees on the retirement of a trustee
- Conveyance or transfer of property the subject of a specific devise or legacy to the beneficiary named in the will (or his nominee)
- Conveyance or transfer of property which forms part of an intestate's estate to the person entitled to intestacy (or his nominee)
- Appropriation of property within S84(4) Finance Act 1985 (death: appropriation in satisfaction of a general legacy of money) or S84(5) or (7) of that Act (death: appropriation in satisfaction of any interest of surviving spouse and in Scotland also of any interest of issue)
- Conveyance or transfer of property which forms part of the residuary estate of a testator or beneficiary (or his nominee) entitled solely by virtue of his entitlement under the will
- Conveyance or transfer of property out of a settlement in or towards satisfaction of a beneficiary's interest, not being an interest acquired for money or money's worth, being a conveyance or transfer constituting a distribution of property in accordance with the provisions of the settlement
- Conveyance or transfer of property on and in consideration only of marriage to a party to the marriage (or his nominee) or to trustees to be held on the terms of a settlement made in consideration only of the marriage
- Conveyance or transfer of property within S83(1) Finance Act 1985 (transfers in connection with divorce etc.)
- Conveyance or transfer by the liquidator of property which formed part of the assets of the company in liquidation to a shareholder of that company (or his nominee) in or towards satisfaction of the shareholder's rights on a winding-up
- Grant in fee simple of an easement in or over land for no consideration in money or money's worth
- Grant of a servitude for no consideration in money or money's worth
- Conveyance or transfer of property operating as a voluntary disposition *inter vivos* for no consideration in money or money's worth nor any consideration referred to in S57 Stamp Act 1891 (conveyance in consideration of a debt, etc.)
- Conveyance or transfer of property by an instrument within S84(1) Finance Act 1985 (death: varying disposition)