

|  |  |                                    |  |
|--|--|------------------------------------|--|
| <b>Title:</b><br>Transparency & Trust – Enhanced Transparency of Company Beneficial Ownership<br><br><b>IA No:</b> RPC13-BIS-1990<br><br><b>Lead department or agency:</b><br>Department for Business, Innovation & Skills<br><br><b>Other departments or agencies:</b><br>Companies House, HMT, HMRC, Cabinet Office, MoJ, Home Office, SFO, NCA, CPS, Attorney General's Office, DFID, FCO | <b>Impact Assessment (IA)</b>                |                                    |  |
|  | <b>Date:</b> Published early 2014            |                                    |  |
|  | <b>Stage:</b> Enactment                      |                                    |  |
|  | <b>Source of intervention:</b> International |                                    |  |
|  | <b>Type of measure:</b> Primary legislation  |                                    |  |
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| <b>Summary: Intervention and Options</b>   |  | <b>RPC Opinion:</b> Green at Final |  |

| Cost of Preferred (or more likely) Option |                            |  |   |
|---|----------------------------|--|---|
| Total Net Present Value                   | Business Net Present Value | Net cost to business per year (EANCB on 2009 prices) | In scope of One-In, Measure qualifies as Two-Out? |
| -£970.6m                                  | -£968.8m                   | £85.9m   | No   NA   |

**What is the problem under consideration? Why is government intervention necessary?**

Opacity of the control of corporate structures can firstly facilitate illicit activity, and secondly lead to a deficiency in corporate governance which can erode trust and damage the business environment. Both can ultimately hold back economic growth. Government intervention is necessary to correct the regulatory failure underpinning the first, and the information asymmetry reflected in the second. A lack of knowledge around the beneficial ownership of UK companies – i.e. around the individuals who really own and control the company – can contribute to corporate opacity. The central problem under consideration is therefore the scope for misuse and poor corporate behaviour as a result.

**What are the policy objectives and the intended effects?**

The policy intends to enhance transparency around the ultimate owners and controllers of UK companies. The chosen option implements the UK's G8 commitment to prevent the misuse of companies, specifically to implement a publicly accessible central registry of company beneficial ownership information. It also meets international standards on tackling the misuse of companies. We intend that enhanced transparency will deter illicit activity and improve enforcement outcomes where misuse does take place, and promote good corporate behaviour. We intend to implement a system that is both proportionate and effective.

**What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)**

0) Firstly, we consider the 'Do Nothing' option and conclude that this would not meet the policy objectives.

1) Implementation of a **central registry of company beneficial ownership information**. Although this has higher costs to business and individuals than Option 2, this is our preferred option as it is the most cost effective way of meeting our policy objectives and UK G8 commitments – particularly in terms of delivering benefits to enforcement agencies and wider society through tackling illicit activity.

2) A **Government-led campaign** to promote the importance of corporate transparency (non-regulatory option). Although costs would be lower than Option 1, this is our least preferred option as it is unlikely to deliver significant benefits in terms of reducing crime through tackling company misuse (as the information provision would be voluntary) or meet the UK's international commitments.

**Will the policy be reviewed?** It will be reviewed within three years of the requirement to file beneficial ownership information at Companies House coming into force.

|  |                     |                       |                       |                      |                           |
|--|---------------------|-----------------------|-----------------------|----------------------|---------------------------|
| Does implementation go beyond minimum EU requirements?   |                     |                       | N/A                   |                      |                           |
| Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.                       | <b>Micro</b><br>Yes | <b>&lt; 20</b><br>Yes | <b>Small</b><br>Yes   | <b>Medium</b><br>Yes | <b>Large</b><br>Yes       |
| What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent) |                     |                       | <b>Traded:</b><br>N/A |                      | <b>Non-traded:</b><br>N/A |

**I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.**

Signed by the responsible SELECT SIGNATORY: ..... Date: .....

# Summary: Analysis & Evidence

# Policy Option 1

**Description:** A publicly accessible central registry of company beneficial ownership information: Preferred Option

## FULL ECONOMIC ASSESSMENT

|                      |                   |                      |                                       |            |                       |
|----------------------|-------------------|----------------------|---------------------------------------|------------|-----------------------|
| Price Base Year 2014 | PV Base Year 2015 | Time Period Years 10 | Net Benefit (Present Value (PV)) (£m) |            |                       |
|                      |                   |                      | Low: -1761.7                          | High: -683 | Best Estimate: -970.6 |

| COSTS (£m)    | Total (Constant Price) | Transition Years | Average (excl. Transition) (Constant Price) | Annual (Constant Price) | Total (Present Value) | Cost |
|---------------|------------------------|------------------|---|-------------------------|-----------------------|------|
| Low           | 338.9                  | 1                | 40.7  |                         | 682.9                 |      |
| High          | 775.4                  |                  | 111.4                                       |                         | 1716.7                |      |
| Best Estimate | 458.9                  |                  | 60.5  |                         | 970.6                 |      |

### Description and scale of key monetised costs by 'main affected groups'

Costs to Government are estimated to be **£72k-112k** for the IT development of the registry and communication to industry; and **£225k** pa on-going for the maintenance. Costs to businesses are estimated to be **£458.9m** set up cost in 2015 (familiarisation, identification, collation, initial storage of data and responding to a request for information), and **£67m** pa on-going costs for updating information and providing returns to Companies House (starting in 2016).

### Other key non-monetised costs by 'main affected groups'

It is also expected that the proposal will have costs to individuals as a result of having to report their beneficial ownership status to companies of which they are a beneficial owner, and update this information as it changes. These costs have not been monetised as it is not possible to estimate the level of costs they will incur. There might be an adverse impact on UK investment from increased disclosure and business costs. Additional court costs might also be incurred.

| BENEFITS (£m) | Total (Constant Price) | Transition Years | Average (excl. Transition) (Constant Price) | Annual (Constant Price) | Total (Present Value) | Benefit |
|---------------|------------------------|------------------|---|-------------------------|-----------------------|---------|
| Low           | 0                      | 1                | 0   |                         | 0                     |         |
| High          | 0                      |                  | 0   |                         | 0                     |         |
| Best Estimate | 0                      |                  | 0   |                         | 0                     |         |

### Description and scale of key monetised benefits by 'main affected groups'

### Other key non-monetised benefits by 'main affected groups'

There is little quantified data about the benefits from this policy proposal. Benefits will be associated with: (1) reduction in crime and increased efficiency by law enforcement agencies, reduced due diligence costs for regulated entities and from these, efficiency and welfare gains to the economy; and (2) increased transparency which could potentially have an impact on economic growth.

Key assumptions/sensitivities/risks

Discount rate (%) 3.5

100% compliance. All UK companies in scope (3.43m) experience at least some familiarisation and on-going costs. Almost by definition, corporate opacity is challenging to evaluate; we have taken considerable steps to identify material to support quantification of the costs and benefits of the proposals, and have used evidence derived from a survey of almost 600 companies. We received a large number of both high and zero cost estimates in the survey so the sample was truncated to arrive at more robust and representative estimates. We have conducted some sensitivity analysis around our estimates and assumptions.

## BUSINESS ASSESSMENT (Option 1)

|   |                   |                      |
|---|-------------------|----------------------|
| Direct impact on business (Equivalent Annual) £m: | In scope of OITO? | Measure qualifies as |
| Costs: 85.9                                       | No                | NA                   |
| Benefits: 0                                       |                   |                      |
| Net: -85.9  |                   |                      |

# Summary: Analysis & Evidence

# Policy Option 2

**Description:** Government-led campaign to encourage enhanced transparency of company ownership: Non-regulatory option

## FULL ECONOMIC ASSESSMENT

| Price Base Year 2014 | PV Base Year 2015 | Time Period Years 10 | Net Benefit (Present Value (PV)) (£m) |             |                      |
|----------------------|-------------------|----------------------|---------------------------------------|-------------|----------------------|
|                      |                   |                      | Low: -1.01                            | High: -0.97 | Best Estimate: -0.99 |

| COSTS (£m)    | Total (Constant Price) | Transition Years | Average (excl. Transition) | Annual (Constant Price) | Total (Present Value) | Cost |
|---------------|------------------------|------------------|----------------------------|-------------------------|-----------------------|------|
| Low           | 1.0                    | 1                |                            |                         | 1.0                   |      |
| High          | 1.0                    |                  |                            |                         | 1.0                   |      |
| Best Estimate | 1.0                    |                  | 0                          |                         | 1.0                   |      |

### Description and scale of key monetised costs by 'main affected groups'

There are likely to be costs to the public sector associated with promoting the voluntary approach. For example, communications campaigns and business engagement. The cost of **£894,000** is from a previous Companies House information campaign and is meant to be merely indicative of possible cost. There will also be one-off costs of **£72k-112k** incurred by Companies House in terms of changes to their IT systems.

### Other key non-monetised costs by 'main affected groups'

Any private sector costs derived from this policy change cannot be fully monetised as both the likely take-up rate and the likely effort expended in the collection of data and reporting (including possible external advice bought in) are uncertain.

| BENEFITS (£m) | Total (Constant Price) | Transition Years | Average (excl. Transition) | Annual (Constant Price) | Total (Present Value) | Benefit |
|---------------|------------------------|------------------|----------------------------|-------------------------|-----------------------|---------|
| Low           | 0                      | 1                | 0                          |                         | 0                     |         |
| High          | 0                      |                  | 0                          |                         | 0                     |         |
| Best Estimate | 0                      |                  | 0                          |                         | 0                     |         |

### Description and scale of key monetised benefits by 'main affected groups'

Any benefits derived from this policy change cannot be fully monetised. It is expected that the impact on crime reduction would be considerably lower in this Option, as would the impact on transparency, however this will depend on the level of take-up of voluntary collection and reporting and the consequent behavioural change of companies.

### Other key non-monetised benefits by 'main affected groups'

Few benefits from reduced crime are expected under this Option, given that a voluntary approach would not fully help to deter, disrupt and penalise criminal activity. There might be some gains from increased vigilance from the publishing of information on the misuse of companies for crime. There might also be some deterrent benefits in terms of individuals choosing to incorporate a company or conduct illicit activity outside the UK, but these are expected to be limited. In addition there might be some increase in transparency which could feed through into more economic transactions. It will not however meet our G8 commitments or international standards. Overall this option is not likely to achieve the desired objective of the policy fully.

|                                     |                   |      |
|-------------------------------------|-------------------|------|
| Key assumptions/sensitivities/risks | Discount rate (%) | 3.5% |
|-------------------------------------|-------------------|------|

## BUSINESS ASSESSMENT (Option 2)

|   |                   |                      |
|---|-------------------|----------------------|
| Direct impact on business (Equivalent Annual) £m: | In scope of OITO? | Measure qualifies as |
| Costs: 0  | No                | NA                   |
| Benefits: 0                                       |                   |                      |
| Net: 0  |                   |                      |

# Evidence Base (for summary sheets)<sup>1</sup>

## Transparency and Trust – Enhanced transparency of company beneficial ownership

### Executive summary

#### Problem under consideration and rationale for intervention

- At the UK-chaired G8 Summit in 2013, the G8 Leaders<sup>2</sup> recognised the problem of corporate opacity. They agreed common Principles<sup>3</sup> to tackle the misuse of companies and legal arrangements and to publish National Action Plans setting out the concrete steps they would take to implement them. Central to the Principles was that companies should obtain and hold information on their beneficial ownership (i.e. on the individuals who ultimately own and control the company), and that this information should be accessible onshore to relevant authorities. The UK committed to do this by creating a publicly accessible central registry of company beneficial ownership information, maintained by Companies House<sup>4</sup>.
- Measures to implement these reforms are contained within the Small Business, Enterprise and Employment Act 2015 (SBEE Act). The legislation refers to the central registry as ‘the register of people with significant control’ or ‘PSC register’.
- Corporate opacity can facilitate illicit activity, and lead to poor corporate behaviour which erodes trust and damages the business environment. Both crime and a lack of trust can impede economic growth.
- Where there is a lack of transparency around corporate structures which facilitates illicit activity and hinders the criminal justice system, there is **regulatory failure** with respect to the company law framework and enforcement. Where there is a lack of transparency, there is an **information asymmetry** which damages trust and hinders transactions and investment. Therefore there is a dual rationale for government intervention to address the problems of corporate opacity.
- The central problem under consideration here is where opaque company ownership structures, in which the registered directors and legal owners of the company are not the individuals who ultimately own and control the company, are used to: facilitate illicit activity; or create scope for reduced levels of trust in UK business.

#### Policy Objectives and options

- The overarching policy objectives for the *Transparency and Trust* package are to reduce crime and improve the business environment so as to facilitate economic growth.
- Specifically, this policy aims to implement the UK’s G8 commitment to ensure that UK companies obtain and hold adequate, accurate and current information on their beneficial ownership; and that this information is publicly accessible onshore in a central registry. We want to implement reform that is both effective and proportionate, and that maximises the potential benefits to be gained by UK and overseas enforcement authorities; financial institutions and other regulated professional bodies; and the wider community that engages with UK companies.
- The options considered to achieve this objective include:
  - **Option 0:** ‘Do Nothing’. This does not meet the stated policy objectives.

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<sup>1</sup> This IA updates the information and estimates in the 2014 Transparency and Trust – Enhanced Transparency of Company Beneficial Ownership Final IA

<sup>2</sup> Now G7.

<sup>3</sup> G8 action plan principles to prevent the misuse of companies and legal arrangements (June 2013): <https://www.gov.uk/government/publications/g8-action-plan-principles-to-prevent-the-misuse-of-companies-and-legal-arrangements/g8-action-plan-principles-to-prevent-the-misuse-of-companies-and-legal-arrangements>

<sup>4</sup> UK action plan (June 2013): <https://www.gov.uk/government/publications/uk-action-plan-to-prevent-misuse-of-companies-and-legal-arrangements/uk-action-plan-to-prevent-misuse-of-companies-and-legal-arrangements>

- **Option 1:** The creation of a publicly accessible central registry of company beneficial ownership information. This is our preferred option, as it fulfils the UK's G8 commitments and is the most effective Option by which to tackle company misuse.
- **Option 2:** Government-led campaign to encourage greater company ownership transparency (non-regulatory option). This is our least preferred option. Whilst it may deliver some benefits in terms of reducing crime through enhanced corporate transparency, increased awareness/vigilance of the misuse of companies and the deterrent effect on setting up companies in the UK for illicit purposes, this is not expected to be as significant as Option 1. It will also not meet our G8 commitments or international standards.

## Costs and benefits

- **Option 1:** Delivers benefits to Government, individuals and business through a reduction in illicit activities and potentially some increased economic activity arising from increased transparency. There will be public sector costs in setting up a registry; and costs to business and individuals in implementing the new requirements.
- **Option 2:** Whilst the costs of Option 2 (in terms of costs to business, individuals and the public sector) would be much lower than Option 1, we anticipate that the benefits would equally be much lower relative to Option 1. For example, Option 2 would not deliver significant benefits in terms of a reduction in illicit activities given the voluntary nature of the data provision.
- The costs and benefits described in this Impact Assessment (IA) are based on the most robust analysis available.

## Implementation

- The SBEE Act contains measures to implement the registry. Secondary legislation is also required. We have prepared separate Impact Assessments to consider the costs and benefits of secondary legislation where these costs and benefits are not reflected within this Enactment Impact Assessment<sup>5</sup>.
- We intend that companies will be required to keep their own registers of beneficial ownership information from January 2016. They will be required to start filing this information at Companies House from April 2016. This 'staggered' approach will provide companies with a period of at least three months in which to obtain the required information before they need to submit it to the central registry.
- The SBEE Act requires the Secretary of State to review the legislation implementing the central registry within three years of the requirement to file information at Companies House commencing.

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<sup>5</sup> See 'Costs and benefits of making a company's own PSC register publicly available' and 'A Register of People with Significant Control over a Company – Protection Regime'

## A. Background

### *A lack of corporate transparency*

1. Under the Presidency of the UK, G8 Leaders agreed at Lough Erne in June 2013 that a lack of corporate transparency was a problem they were determined to address. They agreed common Principles<sup>6</sup> to tackle the misuse of companies and legal arrangements and to publish national Action Plans setting out the concrete steps they would take to implement them. Central to the Principles was that companies should obtain and hold information on their beneficial ownership (i.e. on the individuals who ultimately own and control the company), and that this information should be accessible onshore to relevant authorities. The UK committed to do this by creating a publicly accessible central registry of company beneficial ownership information, maintained by Companies House<sup>7</sup>.
2. The G8 and UK commitments are in line with the recommendations of the Financial Action Task Force (FATF), which sets the global standards on combating money laundering and terrorist financing: “*Competent authorities should be able to obtain, or have access in a timely fashion to, adequate, accurate and current information on the beneficial ownership and control of companies [...]*”<sup>8</sup>.
3. This reform has been taken forward in the UK through measures in the Small Business, Enterprise and Employment Act 2015. The legislation refers to the central registry as ‘the register of people with significant control’ or ‘PSC register’.
4. This Enactment Impact Assessment (IA) considers the costs and benefits of implementing a publicly accessible central registry of company beneficial ownership information in line with the UK’s G8 commitments, made in June 2013<sup>9</sup>. Other IAs in the *Transparency and Trust* package cover proposed action to improve the transparency of ownership and control of companies through other means. Taken together, these measures should meet the overarching G8 objectives to tackle the misuse of companies.
5. The UK’s G8 commitments capture the two sides of the problem under consideration – firstly, that of opacity facilitating illicit activity, and secondly that of a deficiency in good corporate behaviour which erodes trust and damages the business environment. Both elements can ultimately hold back economic growth.

## B. Problem under consideration

### *Corporate opacity and illicit activity*

6. Estimates vary on how much criminal money is generated and laundered within and through the UK. A 2012 EU-sponsored study estimated that about €25bn a year is laundered from UK

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<sup>6</sup> G8 action plan principles to prevent the misuse of companies and legal arrangements (June 2013): <https://www.gov.uk/government/publications/g8-action-plan-principles-to-prevent-the-misuse-of-companies-and-legal-arrangements/g8-action-plan-principles-to-prevent-the-misuse-of-companies-and-legal-arrangements>

<sup>7</sup> UK action plan (June 2013): <https://www.gov.uk/government/publications/uk-action-plan-to-prevent-misuse-of-companies-and-legal-arrangements/uk-action-plan-to-prevent-misuse-of-companies-and-legal-arrangements>

<sup>8</sup> The FATF Recommendations (February 2012): <http://www.fatf-gafi.org/topics/fatfrecommendations/documents/internationalstandardscombatingmoneylaunderingandthefinancingofterrorismproliferation-thefatfrecommendations.html>

<sup>9</sup> UK action plan to prevent misuse of companies and legal arrangements (June 2013): <https://www.gov.uk/government/publications/uk-action-plan-to-prevent-misuse-of-companies-and-legal-arrangements>

crime<sup>10</sup>. The Home Office judges that in 2010/11, UK organised crime generated about £13bn, of which they estimate about £10.5bn is laundered. This figure excludes 85% of fraud and other non-organised crime<sup>11</sup>. Furthermore, the social and economic costs of organised crime in the UK are estimated to be £24bn<sup>12</sup>, of which £8.9bn are associated with fraud.

7. Globally, the European Commission's 2013 IA of *Anti-Money Laundering and Terrorist Financing*<sup>13</sup> points to global criminal proceeds potentially amounting to some 3.6% of GDP; around US\$2.1 trillion in 2009. The best available international estimate of the amounts used in just money laundering would be equivalent to some 2.7% of global GDP or US\$1.6 trillion in 2009<sup>14</sup>. And illicit flows out of low income countries, particularly in Africa, are often claimed to be more than the aid the developed world provides. The Africa Progress Panel chaired by Kofi Annan<sup>15</sup> highlighted the problem, citing research suggesting that the annual loss to Africa between 2008 and 2010 was \$38bn, and that between 1970 and 2008 \$1.8 trillion were lost from the continent - with obvious human consequences<sup>16</sup>.
8. There is a clear link between such illicit financial flows and company structures, described with concern by a range of international expert organisations. The Organisation for Economic Co-operation and Development (OECD; 2011)<sup>17</sup> has observed that: "*almost every economic crime involves the misuse of corporate vehicles [i.e. companies].*" A World Bank review<sup>18</sup> reported that 150 of the 213 grand corruption cases investigated involved the use of at least one corporate vehicle to hide beneficial ownership and the true source of funds; the World Bank has confirmed that 26 of these cases involved UK corporate vehicles. In these 150 cases, the total proceeds of corruption were approximately \$56.4bn. Meanwhile, the World Economic Forum (WEF; 2013)<sup>19</sup> highlighted the increasing number of problematic cases confronting law enforcement agencies involving illegitimate business activity co-mingling with legal business activity, and illicit funds with licit funds.
9. These issues are systemic and relate in many ways to the essence of the company form, which is largely replicated throughout international legal systems. Given the significant international issues, and the high profile association of some jurisdictions with illicit financial flows, the UK is driving change on a wider stage. The Government has and is continuing to pursue this not only through the G7, but also in the G20, in FATF, in Europe, and with the UK's Overseas Territories and Crown Dependencies. In parallel, there is a strong case for domestic action to reduce the vulnerability of the company form.
10. UK law enforcement and tax authorities have in addition provided case studies which give an indication of the scope and scale of the misuse of companies. Whilst some of these cases will involve non-UK companies, the City of London Police estimated that around 99% of company

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<sup>10</sup> Project 'ECOLEF', the Economic and Legal Effectiveness of Anti-Money Laundering and Combating Terrorist Financing Policy (November 2012)

<sup>11</sup> Home Office (2013): *Understanding organised crimes: estimating the scale and the social and economic costs*

<sup>12</sup> Home Office (October 2013): *Serious and Organised Crime Strategy*. This estimate does not include money laundering.

<sup>13</sup> European Commission (2013) for revision of the third money laundering directive: *Impact Assessment – proposal on the prevention of the use of the financial system for the purpose of money laundering, including terrorist financing*

<sup>14</sup> UNODC (October 2011): *Estimating illicit financial flows resulting from drug trafficking and other transnational organized crimes: Research report*. This estimate would be within the IMF's original 'consensus range', equivalent to some 2.7% of global GDP (2.1 – 4%) or US\$1.6 trillion in 2009.

<sup>15</sup> Africa Progress Panel (2013): *Africa Progress Report 2013: Equity in Extractives*

<sup>16</sup> Global Financial Integrity and the African Development Bank (2013): *Illicit Financial Flows from Africa: Hidden Resources for Development*

<sup>17</sup> OECD (2011): *Behind the Corporate Veil: Using Corporate Entities for Illicit Purposes*

<sup>18</sup> World Bank Publications (2011): *The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to do About It*.

<sup>19</sup> World Economic Forum (2013): *Organised Crime Enablers: "Law enforcement agencies have been handling an increasing number of cases in which legitimate businesses co-mingle with illegal businesses, and legitimate funds with illicit funds. Reconstructing these complex corporate schemes and identifying who lies behind them, i.e. identifying their beneficial owners (BO), is considered to be essential to reveal the full extent of the criminal infrastructure and to prevent future criminal activities."*

fraud cases they investigate involve UK companies. The Serious Fraud Office (SFO) and Metropolitan Police Service (the 'Met') have highlighted a number of cases in which UK and/or overseas-incorporated companies are used to channel illicit funds through the UK; hold UK assets such as property; or perpetuate fraud involving UK citizens. Amounts up to £50m can be involved in such crimes. Recovering the proceeds of such crimes can be incredibly difficult - if not impossible - not least because of the multi-jurisdictional nature of the various companies involved in the ownership chains. Further examples are provided at **Annex D**.

11. These authorities have made a strong case for action to increase corporate transparency. The SFO, the National Crime Agency (NCA)<sup>20</sup>, the Crown Prosecution Service, the Attorney General's Office, HMRC and the City of London Police and the Met have been engaged in the development of the *Transparency and Trust* package generally, and this IA specifically, and have described the problems the package could address and the benefits these measures could bring for them, and crucially for business and the public from a potential reduction in crime<sup>21</sup>.
12. In the UK, there are currently circumstances in which a company's beneficial owners should already be identified. For example, under the UK's anti-money laundering (AML) regime<sup>22</sup>, banks, lawyers, accountants and other professional bodies ("regulated entities") are required to apply customer due diligence measures before entering into a business relationship with a company, including identification of the beneficial owner(s). However, regulated entities have told us they can struggle to fulfil this requirement, finding it difficult to obtain the information from the company or through other means. If the regulated entity cannot obtain this information to its satisfaction, it should not enter into the business relationship (irrespective of whether criminal activity is suspected). This clearly has the potential for sub-optimal outcomes for the regulated entity, which loses the potential client. The regulated entities go on to say that where services are refused, the company may look to find a service provider who does not apply due diligence, or does so to a lesser degree. It is also possible the company may simply give up, with an unquantifiable potential reduction in legal UK economic activity.
13. Law enforcement agencies have statutory powers of investigation which they can use to try and identify beneficial ownership. However, where illicit activity is suspected it can be very difficult to prove that the person suspected of benefiting from the shares or company in question is actually the beneficial owner. This can have an adverse impact in terms of the amount of time and resource expended in investigating a case; but also in terms of the ultimate case outcome (e.g. the ability to prosecute successfully). Law enforcement agencies say the opacity of current beneficial ownership arrangements is a significant barrier to tackling money laundering and successfully recovering stolen assets:
  - **NCA:** At any one time in the 2012/13 financial year, SOCA (now NCA) was involved in over 400 significant operations. Nearly all of these had a financial investigation element. The NCA estimated that in around 70% of such investigations issues around beneficial ownership arise. In 2013 the NCA had approximately 60 cases where civil recovery powers were used to retrieve criminal assets. Again, beneficial ownership issues arose in about 70% of those cases.
  - **SFO:** The SFO has stated that establishing the beneficial ownership of assets is almost always a key element of confiscation investigations. They note that at any one time there will be around 50-60 active criminal investigations by the criminal case teams. The Proceeds of Crime Division will also have around 100 individuals under investigation plus around 40 individuals already subject to confiscation orders (where enforcement action is

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<sup>20</sup> And previously the Serious Organised Crime Agency (SOCA)

<sup>21</sup> Including evidence provided by SOCA prior to the launch of the National Crime Agency in October 2013.

<sup>22</sup> See the Money Laundering Regulations 2007 (No. 2157)

being taken to make them pay what the court has ordered). One case involved a UK company as well as overseas companies, and took a team of four around two years before a confiscation order was obtained.

- **The Met:** estimate that in cases where hidden beneficial ownership is an issue, 30-50% of an investigation can be spent in identifying the beneficial owners through a chain of ownership “layers”.

14. Discussions with enforcement agencies and private sector fraud investigators have indicated that many cases of company misuse will involve complex webs of companies and other corporate structures incorporated in numerous different jurisdictions. This is supported by relevant literature on the misuse of companies<sup>23</sup>. This necessarily increases the time and cost of obtaining beneficial ownership information, for both UK and international enforcement agencies.
15. Aside from the problem of opacity of company ownership hindering AML due diligence checks and enforcement action, the general lack of transparency of UK company ownership may also have an adverse impact on levels of trust in UK business, and perceptions of the UK as a clean and open place to do business. This may result generally in companies doing less business with the UK. Similarly, without this transparency, where one company wants to identify with whom they are really doing business, they may have to spend more time or resource in obtaining this information, or be more reluctant to engage with the company in the first place.
16. The Financial Reporting Council, the UK’s independent regulator responsible for promoting high quality corporate governance and reporting to foster investment has noted that: *“High quality corporate governance helps to underpin long-term company performance. The UK has some of the highest standards of corporate governance in the world, which makes the UK market attractive to new investment.”* However, keeping the UK’s position secure requires continual evaluation of improvements that can be made.
17. Linked to this is the need to meet relevant international standards on company beneficial ownership transparency in the context of anti-money laundering and counter-terrorist financing. If the UK is not assessed as effectively meeting these standards, it could have an adverse impact on our international reputation and standing. This may in turn have a detrimental effect on the UK’s attractiveness and competitiveness.
18. The problem of opaque company ownership structures can therefore be summarised as increasing the potential for criminal activity and potentially also reducing levels of trust in business. Without Government intervention, there is unlikely to be sufficient collective action by industry to address these issues; particularly given that much of the activity we are aiming to address is criminal.

### C. Rationale for intervention

19. There are two facets to the economic rationale for Government intervention through the policy changes described in the *Transparency and Trust* package. Firstly there is the **regulatory failure** associated with the current corporate governance and company law frameworks, which enable those that control companies to remain anonymous and hence allow or even facilitate financial crime. Secondly, and linked to that, there is an **information asymmetry** with respect to company ownership and control, between those that control companies and those that trade with them or invest in them, which inhibits economic activity. The inefficiency and reputational damage that

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<sup>23</sup> For example, World Bank Publications (2011): *The Puppet Masters : How the Corrupt Use Legal Structures to Hide Stolen Assets and What to do About It*

crime introduces to the economy, as well as the lost business and reduced investment from information asymmetry, could negatively impact on economic growth.

### **(1) Regulatory failure and the potential facilitation of crime**

20. There is a well-established role for the State in addressing criminal behaviour. This includes the introduction of laws which form a central part of the UK's institutional infrastructure and business environment. By upholding the law and enforcing property rights, the State facilitates economic activity. The State's role also includes the provision of criminal investigation and law enforcement, not least where there are externalities and the potential for free-riding. It could be argued that there is a regulatory failure where there is a deficiency in the legal framework, or in the functions of associated institutions, which facilitates crime (which in turn imposes costs on society). There is therefore a clear rationale for intervention where the net benefits of Government action outweigh the cost of inaction.
21. Companies and other corporate entities have separate legal personality, meaning they can enter into contracts and business relationships in their own name. Importantly in addition, many companies take advantage of the option to have limited liability. Alongside these advantages, which facilitate entrepreneurship<sup>24</sup>, a company is required to put more information in the public domain (e.g. their accounts, and information on their shareholders and directors) compared to other business forms (e.g. sole traders). However there still remains scope for opacity around corporate ownership structures and company control. This is because various aspects of the current corporate ownership system (e.g. bearer shares, opacity of beneficial ownership, the use of certain arrangements involving directors) can be used to conceal an individual's interest in a company.
22. This potential for anonymity means the individuals who 'stand behind' the company can then use the company as a front, for example, to launder the proceeds of crime and to finance organised crime and terrorism<sup>25</sup>. A Home Office rapid evidence review (February 2014) concluded that corporate entities can be used to enable or assist criminality, to launder money or to provide prestige or perceived legitimacy. UK enforcement agencies have provided examples of the types of activity that can be facilitated using opaque corporate structures. These include tax crimes such as Missing Trader Intra Community (MTIC) fraud<sup>26</sup>; hiding stolen assets and the proceeds of crime; fraud; and drug and people trafficking.
23. The anonymity afforded by the corporate structure also means law enforcement agencies cannot always readily identify the individuals really responsible for the criminal activity - resulting in less efficient and effective investigations; and potentially sub-optimal outcomes. Where the corporate governance and company law frameworks do not ensure sufficient transparency to prevent this opportunity, and hence also fail to reduce the need for risk mitigation measures by counterparties or inefficient corporate activity, it can be viewed as a **regulatory failure**.
24. Thus, in this case, regulatory failure facilitates crime which can lead to costs to the economy and more widely to society. These costs include the welfare damage to the victim; inefficient resource allocations and a forced redistribution of income; lost economic activity/output; inefficient insurance expenditure; and costs to the criminal justice system, including the police<sup>27</sup>. The aim of

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<sup>24</sup> Brian Brougham (2011): *Entrepreneur Wealth and the Value of Limited Liability*

<sup>25</sup> That is to say the money passing through the company can be of criminal origin, and / or can be used to support further crimes, and through the relative anonymity of the company structure the individuals involved can be concealed.

<sup>26</sup> Missing Trader Intra Community (MTIC) fraud contains two elements: a missing trader and an intra-community supply. There are two types of MTIC fraud - acquisition and carousel - as well as one variant - contra trading. For more information go to:

<http://www.hmrc.gov.uk/manuals/vatfmanual/vatf23300.htm>

<sup>27</sup> See Brand and Price (2000): *The economic and social costs of crime*, Home Office Research Study 217. London: Home Office. And

this policy to address the regulatory failure affecting corporate ownership and transparency of control is to reduce the opportunity for financial criminal activity and thus reduce these costs to the UK.

25. Opaque corporate structures can not only facilitate crime but also hamper the law enforcement response. Firstly, during the investigation phase where time and resource can be used to establish basic facts, such as who are the individuals owning particular assets or who control a company, and secondly, during prosecution or after a conviction, by preventing confiscation of the proceeds of crime by the authorities and return of assets or compensation to the victims.
26. Reducing opportunities for crime could also help support conditions for growth. Each US\$1 billion laundered reduced overall economic growth by 0.04-0.06 percentage points in 17 OECD countries, prompting the UN to comment on the findings that: *“financial centres have developed a self-interest of not being associated with ‘tainted money’ and have signed relevant international instruments to avoid the inflow of such criminal finance<sup>28</sup>.”*
27. There is a strong body of evidence highlighting how crime acts as a drag on investment, job creation and ultimately economic growth. For instance, Goulas and Zervoyianni (2013)<sup>29</sup> find that in times of macroeconomic uncertainty, a 10% increase in the crime rate is associated with a reduction in annual GDP per capita growth of 0.49%-0.62%. Although these studies<sup>30</sup> do not directly identify the mechanism, they highlight that reducing crime will support growth.

## **(2) Imperfect/asymmetric information affecting the operation of the business environment**

28. Opaque corporate ownership structures are also associated with **imperfect/asymmetric information**. In all economic transactions, one party to the transaction must acquire information about the other party to understand sufficiently the quality and risks associated with the goods, service or investment opportunity on offer. In particular, when engaging in high cost and long term economic relationships involving complex goods (“experience” or “credence” goods), services or investments (e.g. long term investment in corporations or purchasing high-end professional services), the information asymmetry between parties is likely to be large and significant.
29. The corporate form helps mitigate the impact of information asymmetry. This is because the company has separate legal personality: *“As a separate legal entity [...] the company must be treated like any other independent person with rights and liabilities appropriate to itself<sup>31</sup>.”* In other words, a person may engage with the company without needing to satisfy himself or herself of the nature of the persons *behind* the company - they simply need to be satisfied with the ‘credentials’ of the company itself, which is evidently a less onerous and more efficient process than needing to satisfy themselves with respect to all the individuals who might be associated with a company in various ways.
30. However, corporate opacity – created, for example, by a distinction between the legal owners of a company as recorded on the company’s register of members and the ‘beneficial owners’ on whose behalf company shares are held – can nevertheless lead to **two** sub-optimal outcomes.

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Dubourg et al (2005): *The economic and social costs of crime against individuals and households 2003/04*. Home Office Online Report 30/05. London: Home Office.

28 UNODC (October 2011): *Estimating illicit financial flows resulting from drug trafficking and other transnational organized crimes: Research report*

29 Goulas and Zervoyianni (2013): *Economic growth and crime: does uncertainty matter*. Applied Economics Letters, Vol 20, issue 5, pp420-427

30 See also Detotto and Paulina (2013): *Does more crime mean fewer jobs and less economic growth?* European Journal of Law and Economics, Vol 36, Issue 1, pp183-207 and Detotto and Otranto (2010): *Does crime affect economic growth* International Review of Social Sciences, Vol 63, Issue 3, pp330-345

31 Hannigan, B (2003): *Company Law*, Clays Ltd

31. The **first** is in terms of the ability of the members of the company to hold the directors to account. An individual holding 15% of the company's shares will not, on their own, be able to influence materially a key company vote. However, that individual can look to other members to support their position, thereby gaining a much greater ability to support or block the vote. This process is facilitated by the member's ability to access the company's register of members – giving them the means to identify to whom else they need to talk.
32. However, this register of members may not of itself be sufficient. For example, where a bank holds shares on behalf of a client, it will be the name of the bank that is recorded in the register – not that of the client. In this cases, an ability to identify the beneficial owner would improve the ability of the shareholders (understood here as the individuals and companies investing in the company, whether directly or through an intermediary) to hold the company to account, and ultimately drive more successful outcomes.
33. This enhanced transparency, enabling shareholders to hold companies to account could be expected to have a positive impact on economic growth. As discussed in the Kay Review (2012)<sup>32</sup>, greater shareholder unity enables shareholders to hold companies to account more effectively, which is thought to generate efficiency, corporate profit and therefore economic growth<sup>33</sup>. Essentially, by reducing the information asymmetry between the company board (agent) and the shareholders (principal), this enables the shareholders to align more effectively the board's incentives to generate positive outcomes from the company.
34. As noted in the seminal paper by Hirschman (1970)<sup>34</sup>, shareholders have two means to influence company boards; 'voice' (lobbying management and voting) and 'exit' (selling their shares). The additional transparency resulting from our package of policies gives shareholders more 'voice' to influence the board, hold it to account (particularly with respect to the company's ownership chain) and therefore drive corporate growth and long-term development.
35. The **second** sub-optimal outcome is in terms of those who engage with a company wanting to know with whom they are actually dealing.
36. Irrespective of the 'protection' that the corporate form affords in an economic sense; we might expect investors, suppliers and customers to want to know who actually owns and controls the company (again, its beneficial ownership) – not least as a means to mitigate reputational risk incurred as a result of transacting with a company subsequently found to have, for example, established links to terrorist groups or money launderers.
37. Arguably, knowledge of a company and its owners is therefore important in helping those who engage with a company to assess the risk of company transactions, and therefore their own engagement with them, more accurately. Not knowing who ultimately owns/controls a company means that there is a greater inherent risk of making sub-optimal investments, not being paid correctly for goods/services or inadvertently financing crime. This can make economic transactions/activities less attractive<sup>35</sup> and hence less likely to go ahead or they might go ahead but at a higher cost or lower level. For instance, Easley and O'Hara (2004)<sup>36</sup> find that companies which keep a greater proportion of their information private require a greater compensating return

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<sup>32</sup> BIS (2012): *The Kay Review Of UK Equity Markets And Long-Term Decision Making*

<sup>33</sup> Bilych, G. (2012): *Profit and economic growth*. Macrothink Institute vol. 2 no. 2

<sup>34</sup> Hirschman, A. O. (1970) *Exit Voice and Loyalty: Responses to Decline in Firms, Organisation and States* Harvard University Press

<sup>35</sup> Furthermore, considering adverse selection, if the share of 'bad' companies exceeds a certain threshold, the market will cease to exist as 'good' companies are driven out of business.

<sup>36</sup> Easley, D. and O'Hara, M. (2004): *Information and the Cost of Capital*. The Journal of Finance, Vol. 59, No 4.

for the lack of transparency, i.e. they face a higher cost of capital. This is a common finding in the economic literature<sup>37</sup>.

38. Also when corporate information is not readily available, other parties must incur greater costs from conducting due diligence to mitigate this risk. They must, for instance, actively seek to determine the trustworthiness of the company and also write, complete and monitor contracts<sup>38</sup>. Therefore a lack of information will increase transaction costs, which can serve as a serious barrier to entry in the market, discouraging economic activity and harming growth.
39. Whilst both the higher cost of capital and greater risk mitigation represent a market response to a lack of information, they can also be inefficient. This raises the question of why all companies do not volunteer such information proactively. One possibility is that an individual's rationality is bounded<sup>39</sup> by the information they have, the finite amount of time at their disposal and limits to their ability to process and analyse all the information available. It is plausible that even though information about the business advantages of corporate transparency exists, companies may be unaware of it. Alternatively, the costs of identifying, accessing, understanding and applying this information (e.g. the opportunity cost of a director's time) outweigh the perceived benefits. Furthermore, evidence may be available only in an abstract sense, and not easily accessible to many companies. Therefore, many companies may not volunteer relevant corporate information in these circumstances.
40. Given that such bounded rationality is likely to be pervasive, firms behaving in this way (i.e. not revealing relevant corporate information) might not necessarily be forced out of the market by more competitive rivals in the long run, even if we assume that markets are rational and competitive.
41. Opacity could also drive adverse selection<sup>40</sup>. Here the potential investor/lender/customer/supplier of a company cannot distinguish between a low-risk transaction and a high-risk one because of asymmetric information around ownership and control. Therefore they offer 'average' terms and conditions for that transaction. This means that some mutually beneficial business will only go-ahead at a sub-optimal quantity, or not at all. Over time, standard economic theory suggests that less mutually beneficial business will take place as fewer high quality offers are put to the market on the supply side and risk averse firms and investors start to opt out of the demand side. A market for 'lemons' is the result<sup>41</sup>. On this basis, a lack of transparency and trust can inhibit optimal economic activity.
42. Finally, there is a broader point around the role of trust in the smooth operation of the economy. The literature commonly identifies a significant and positive relationship between trust and overall economic growth, which emerges because trust motivates innovation, investment and more entrepreneurship<sup>42</sup>.

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37 See Barry, C., and S. J. Brown (1985): *Differential Information and Security Market Equilibrium*. Journal of Financial and Quantitative Analysis 20, no. 4: 407-22 for a model, which demonstrates that securities with relatively little information are of a higher systemic risk. See Merton, R. (1987): *A Simple Model of Capital Market Equilibrium with Incomplete Information*. Journal of Finance 42, no. 3: 483-510. Finds that in a model where investors are not aware of all stocks available i.e. suffer from incomplete information, the equilibrium value of each company is always lower.

38 Nonetheless, knowledge is always imperfect to some extent: as noted by Miller and Whitford (2002): without all encompassing contracts, which account for every eventuality, some element of trust is implicit in every business contract.

<sup>39</sup> Gigerenzer, Gerd and Selten, Reinhard (2002): Any benefits derived from this policy change cannot be monetised. *Bounded Rationality*. Cambridge: MIT Press.

40 It refers to a market process in which undesired results occur when buyers and sellers have access to different information; the "bad" products or services are more likely to be offered and selected.

41 Akerlof G.A. (1970): *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*. The Quarterly Journal of Economics, Vol. 84, No. 3., pp. 488-500

42 For instance, see Knack S, (2001): *Trust, associational life, and economic performance*, World Bank; Dincer and Uslander (2010): *'Trust and Growth'*; Knack, Stephen and Paul Zak (2001): *Trust and Growth*, Economic Journal, 111(470): 295-321 and Knack & Keefer (1997): *Does Social Capital Have an Economic Payoff? A Cross-Country Investigation* The Quarterly Journal of Economics, Vol. 112, No. 4, pp. 1251-1288.

43. Whilst trust alone will not drive growth, it feeds into the stability of economic systems which are key to economic activity. In terms of its relative importance, Whiteley (2000)<sup>43</sup> finds evidence suggesting social capital, defined as the extent to which people are prepared to co-operate based on interpersonal trust, has a highly significant impact on growth, at least as strong as education or human capital. More broadly, enhancing trust will act to improve the prospects, reputation and stability of UK businesses and financial services.
44. In summary, the *Transparency and Trust* policy proposals around increasing the transparency of corporate ownership and control have the potential to:
- reduce crime, by addressing a regulatory failure in the corporate governance and company law frameworks; and
  - reduce the risks around economic activity and increase trust by reducing information asymmetry between those who do business with, or invest in, the company and those that control it.

#### **D. Policy objective**

45. We want to know who really owns and controls UK companies to tackle the potential for misuse and promote good corporate behaviour. In so doing we want to fulfil the UK's G8 corporate transparency commitments, and meet international standards on anti-money laundering and counter-terrorist financing. In the UK's G8 Action Plan we stated our intention to implement reform via primary and secondary amendments to company law. The SBEE Act contains the primary legislative measures needed to implement the register. We are currently preparing secondary legislation in advance of planned implementation in 2016. We will also take forward reform through amendments to money laundering legislation and other relevant bilateral and multilateral agreements.
46. The chosen option should contribute to the two main objectives of the *Transparency and Trust* package, which are to:
- reduce crime, and
  - improve the business environment so as to facilitate economic growth.
47. Company beneficial ownership reform should, in line with the UK's G8 commitments:
- ensure UK companies obtain and hold adequate, accurate and current information on their beneficial ownership; and
  - ensure this information is publicly accessible onshore in a central registry. The registry should provide a single source of information to support national and overseas law enforcement and tax authorities' investigations; support financial institutions and other regulated professional bodies as they carry out AML due diligence checks on companies; and allow all those who engage with a company (e.g. investors, suppliers, customers) to identify with whom they are really doing business.
48. The chosen policy option should also:

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Bjørnskov (2012): *How Does Social Trust Affect Economic Growth?* Southern Economic Journal, Working Paper 06-2, shows that trust has a direct impact on schooling, which in turn feeds into the investment rate and ultimately economic growth.

43 Whiteley, P. (2000): *Economic Growth and Social Capital*, Political Studies 48, 443-466.

- stimulate global, collective action to tackle the misuse of companies. Investigations into abuses of company structures will often cross borders and so coordinated international action is vital. In leading by example, UK and G8 action should encourage other jurisdictions, including the UK's Overseas Territories and Crown Dependencies, to follow suit. This should deliver better outcomes in terms of reducing crime in the UK as well as elsewhere;
- deliver benefits for developing countries who suffer as a result of tax evasion, corruption and fraud. By allowing them access to information on UK companies, they should be more easily able to identify the individuals really responsible where a UK corporate entity has been used to facilitate the crime; and
- ensure full UK compliance with relevant international standards in advance of the UK's next FATF peer review (expected to take place around 2017) to maintain and enhance the UK's reputation as a clean and trusted place to do business and invest.

49. We want to achieve these objectives by developing a policy solution that:

- is effective and proportionate and the most cost effective way to achieve the policy objectives;
- maximises the potential benefits to be gained by UK and overseas enforcement authorities, financial institutions and other regulated professional bodies, and the wider national and international community that engages with UK companies;
- minimises the potential for an adverse impact on the competitiveness of the UK business environment and the desirability of the UK as a place to set up and operate a company;
- minimises the potential for unintended consequences as a result of enhanced transparency (e.g. the potential for an adverse impact on companies or individuals); and
- is straight-forward for UK companies to understand and apply.

## **E. Description of options considered (including 'Do Nothing')**

### ***Option 0 - Do Nothing***

50. Under the 'Do Nothing' Option the UK will have ways to identify the beneficial ownership of UK companies. For example: enforcement agencies can obtain production orders for this information; the Business Secretary can use his powers under the Companies Act 1985 to investigate company ownership; and regulated entities are required to obtain beneficial ownership information before entering into a business relationship with a UK company. In addition, public companies can use provisions in the Companies Act 2006 to investigate their own membership (i.e. shareholders).

51. These measures are however not effective enough in dealing with the problem because:

- if companies are not required to provide beneficial ownership information by law, the only way for enforcement agencies to obtain the information is via production and court orders. As an example, the SFO applies for around 30 production orders from the courts each year, and this takes some two staff-days per order to prepare, review and authorise. This process would not be aided by more extensive use of their current powers. In addition, these methods alert the company to the fact that they are under scrutiny. Enforcement agencies have noted this can be counterproductive in investigations – as the company may then take steps to conceal their illicit activity or transfer the illicit funds before the investigation is complete (potentially preventing the individuals from being sanctioned);
- similarly, regulated entities have reported it can be difficult to obtain beneficial ownership information. Simply requiring them more effectively to carry out their due diligence obligations without supporting them to do so (e.g. by placing a statutory obligation on companies) is

therefore insufficient to meet the stated policy objectives. Furthermore, UK companies could continue to avoid having to provide their beneficial ownership information by using a service provider who is not subject to the UK or EU AML regime (e.g. an overseas bank). This means the potential for misuse will remain;

- it will remain difficult for those engaging with a company to identify who they are really doing business with; and
- the UK will not meet its G8 commitments and will not be compliant with FATF standards, which may ultimately impact the UK's reputation as a clean and trusted place to do business and invest.

**Option 1 – A publicly accessible central registry of company beneficial ownership information: Preferred option**

52. At the G8 Summit in June 2013, all G8 countries committed to tackle the problem of hidden company beneficial ownership:

*“Companies should know who owns and controls them and their beneficial ownership and basic information should be adequate, accurate, and current. As such, companies should be required to obtain and hold their beneficial ownership and basic information, and ensure documentation of this information is accurate<sup>44</sup>.”*

To do this, the UK committed to place a requirement on companies to obtain and hold beneficial ownership information in a publicly accessible central registry, maintained by Companies House. There were a number of variables as to how the registry could be implemented, and BIS sought views on these options in the *Transparency and Trust* discussion paper.

53. The UK model, which takes account of consultation responses to the *Transparency and Trust* discussion paper, is set out below. This is reflected in the primary legislative measures. Further detail as to the variables that we have discounted is provided at **Annex D**. The policy model is outlined in further detail in BIS' Government response to the *Transparency and Trust paper* and in the legislation.

54. We are now taking forward secondary legislation to implement some of the detailed aspects of reform. As the primary and secondary legislation are so interlinked – both are required to implement the register - the costs and benefits of the policies contained within the secondary legislation are largely covered in this Enactment Impact Assessment. However, we have prepared separate Impact Assessments to look at:

- the costs and benefits of companies making their own beneficial ownership registers available for public inspection; and
- the costs and benefits of the regime for suppressing information of individuals at serious risk of physical harm from public disclosure.

55. Guidance will be prepared to help companies and others understand the new requirements.

**(1) The definition of beneficial ownership**

56. As set out in the Final Stage Impact Assessment for the policy, we have maintained consistency with the principles of the beneficial ownership definition currently used in AML legislation. The register will hold information on the individuals who ultimately own and control UK companies.

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<sup>44</sup> G8 (June 2013): <https://www.gov.uk/government/publications/g8-action-plan-principles-to-prevent-the-misuse-of-companies-and-legal-arrangements/g8-action-plan-principles-to-prevent-the-misuse-of-companies-and-legal-arrangements>

The legislation sets out five conditions for being a 'person with significant control' or beneficial owner – any individual meeting one or more of those conditions must be entered in the PSC register. These conditions are:

- directly or indirectly holding more than 25% of the company's shares;
- directly or indirectly holding more than 25% of the company's voting rights;
- directly or indirectly holding the right to appoint or remove a majority of the board of directors;
- otherwise exercising significant influence or control over the company; or
- exercising significant influence or control over a firm or trust which would itself meet one of the above conditions were it an individual.

57. Further detail on the interpretation of these conditions is included in the legislation. Statutory guidance will be prepared on the meaning of "significant influence or control". Companies and others must have regard to that guidance in deciding whether someone exercises significant influence or control.

58. For the purpose of this policy, corporations sole, governments and certain other organisations are treated as individuals. This means that where they meet one of the above conditions, they will be recorded as the company's beneficial owner.

59. In certain circumstances a legal entity must be recorded in the register instead of an individual. This is described below.

## (2) *The scope of the registry*

60. We will require all UK bodies corporate that currently register information on their members at Companies House to hold their beneficial ownership information and provide it to the central registry. This will include companies and Limited Liability Partnerships as well as some lesser used corporate forms (for example, Societas Europaea).

61. We will exempt companies with securities listed on a UK regulated or prescribed market from the requirement to maintain this information and provide it to Companies House. This is because these companies already comply with more stringent ownership disclosure rules under Chapter 5 of the Financial Conduct Authority's (FCA) Disclosure and Transparency Rules (DTRs). We also intend to exempt companies with securities listed on an EEA regulated market subject to equivalent disclosure requirements. Exempt companies will be required to inform Companies House why they are not required to provide beneficial ownership information in the context of the new check and confirm process<sup>45</sup>.

62. As indicated in the Final Stage Impact Assessment, we have sought to avoid duplicative and burdensome reporting for private companies owned by other companies. The legislation therefore introduces the concept of 'relevant legal entities' or 'RLEs'. Where a company is owned by an RLE, the company may provide details of the RLE in its register rather than details of the people who own and control the RLE.

63. RLEs are entities which already make information about their ownership and control publicly available. They are:

- entities which are required to keep a beneficial ownership register; and
- entities which are exempt from keeping a beneficial ownership register.

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<sup>45</sup> The 'check and confirm' process will replace the Annual Return. This means that the company will be required to update all relevant information – including beneficial ownership information – at least once in a 12 month period (for further detail, see the Government response to the *Company Filing Requirements* consultation).

64. This approach will still allow the beneficial owner of UK companies to be traced but should reduce the costs incurred by companies in obtaining the information.

*(3) How beneficial ownership information is obtained*

65. As set out in the Final Impact Assessment, disclosure obligations will be placed on both companies and beneficial owners to ensure that all relevant beneficial ownership information is disclosed without placing a disproportionate administrative or cost burden on the company.

66. Companies will be required to take reasonable steps to identify their beneficial owners. Where the company does not already hold the required information it will be required to serve notice on the beneficial owner and others to obtain it. Those in receipt of such a notice will be statutorily required to reply. If a company cannot, having taken reasonable steps, identify its beneficial ownership it will be required to state that fact in its register.

67. A company that cannot identify its beneficial ownership must consider whether to impose restrictions on the shares or rights in question ('the restrictions regime'). The intention is that this will encourage people to provide the required information. Where restrictions have been imposed, we intend to require this to be annotated in the company's register.

68. Beneficial owners will be required to disclose their interest in the company to the company unless they know the company already has this information stated in its register, or they have received a notice from the company to request this information. Beneficial owners may wait a month to see whether they receive a notice from the company before they are required to proactively discharge their notification obligation. After a month has elapsed, they must disclose the information to the company. They have another month in which to do this.

*(4) Providing and updating information in the central registry*

69. Having obtained beneficial ownership information, companies will be required to maintain a register of this information at their registered office, or other specified location which in future will for some private companies - if they wish - include Companies House. This register must be kept available for public inspection. A separate Impact Assessment sets out the costs and benefits to companies of making their register publicly available.

70. Companies will be required to hold information on their beneficial owners' full name, date of birth, nationality, country or state of usual residence, residential address, a contact (or "service") address, the date on which the beneficial owner acquired the beneficial interest (and ceased to hold it, where applicable), details of how the beneficial owner exercises control over the company and whether the person has applied for their personal information to be protected from public disclosure.

71. If a company has been unable to identify its beneficial owners or gather the necessary information it will need to annotate its register accordingly.

72. With the exception of residential addresses, all of this information will be made available for public inspection by the company. The costs and benefits of this element of the policy are covered in the separate Impact Assessment looking at making PSC registers publicly available.

73. The company will be required to provide all of this information to Companies House. With the exception of residential addresses and the 'day' of the dates of birth<sup>46</sup>, this information will be publicly accessible via Companies House. Residential addresses and the full date of birth will be available to specified public authorities and organisations on request.

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<sup>46</sup> Unless the company has opted to hold its register of beneficial owners at Companies House (for further detail, see the Government response to the *Company Filing Requirements* consultation).

74. We recognise concerns around the potential for fraud and other criminal activity through the public disclosure of this information. This would have, amongst other adverse consequences, a cost and time impact on enforcement agencies dealing with the crime. However, we carefully considered the balance between the information made available publicly and privately; and think that it should limit the risk of fraud whilst ensuring that sufficient information is made available publicly to derive anticipated benefits.
75. We will also put in place an exemptions framework for individuals at risk. This means that all of their details will be made unavailable for public inspection at the company and Companies House. This information will still be available to specified authorities. The costs and benefits of this element of the policy are covered in the separate Impact Assessment looking at the protection regime.
76. We will require companies to provide a statement of intended beneficial ownership ('initial significant control') at incorporation<sup>47</sup>. Thereafter, they will be required to update the register they hold if they know or have reasonable cause to believe that a change to their beneficial ownership has occurred. For example, if 25% of a company's share capital was acquired by a single member of the company, the company should take steps to identify whether the beneficial ownership of those shares had also changed because it might reasonably expect this to be the case.
77. We will also require beneficial owners to inform the company of any changes to the information held by the company, for example, if they change their name. They will be required to make this notification if they haven't heard from the company within one month of the change occurring.
78. The company will be required to update beneficial ownership information held by Companies House in the context of the 'check and confirm' process<sup>48</sup>. This means beneficial ownership information held will need to be confirmed and updated with any changes at least once in a 12 month period.
79. Option 1, as outlined above, is our preferred option.

***Option 2 - Government-led campaign to encourage enhanced transparency of company ownership: Non-regulatory option***

80. We have considered the non-regulatory option of a Government-led campaign encouraging companies to obtain, report and have published their beneficial ownership information. We would work with business representative bodies and regulated professional bodies to support and encourage their members and clients to take positive action in this space. We would continue to push for changes to be made and implemented to national and international standards or best practice on, for example, corporate governance.
81. In parallel, as under Option 0, the UK will still have ways to identify the beneficial ownership of UK companies. For example; enforcement agencies can obtain production orders for this information; the Business Secretary can use his powers under the Companies Act 1985 to investigate company ownership; and regulated entities are required to obtain beneficial ownership information before entering into a business relationship with a UK company. In

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<sup>47</sup> Because the company does not exist prior to incorporation, it can only be a statement of intended beneficial ownership.

<sup>48</sup> The 'check and confirm' process will replace the Annual Return. This means that the company will be required to update all relevant information – including beneficial ownership information - at least once in a 12 month period (for further detail, see the Government response to the *Company Filing Requirements* consultation).

addition, public companies can use provisions in the Companies Act 2006 to investigate their own membership.

82. However, we do not think that a non-regulatory approach would be sufficiently effective in meeting our policy objectives to reduce crime significantly and improve the business environment so as potentially to facilitate economic growth. This is considered further in the costs and benefits section below.

83. This is our least preferred option.

#### **F. Monetised and non-monetised costs and benefits of each option (including administrative burden)**

84. In order to gather evidence of the impact of these proposals on UK businesses, individuals and the public sector, and to inform thinking around policy and implementation, BIS has undertaken: a literature review; a call for evidence in a public discussion document; various focus groups, discussions with academics; a self-selection online survey; and a fuller representative survey and follow-up survey both using company interviews (see **Annex A** for the methodology). The results from these are used to inform the analysis below.

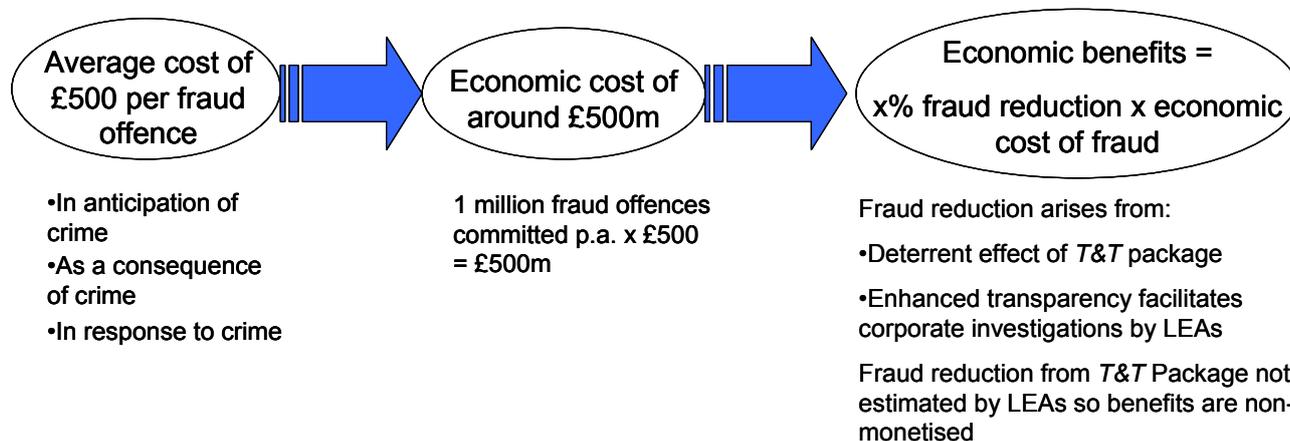
#### ***Option 1 – A publicly accessible central registry of company beneficial ownership information: Preferred option***

##### ***Benefits***

85. The benefits of Option 1 are expected to be associated with the impact that increased transparency could have on the reduction of illicit activity and potentially increased economic activity. We have not, however, attempted to include any estimate of the benefits in the EANCB calculation as the causal link is, ex ante, unquantifiable.

##### ***B1. Benefits to government, individuals and business of a reduction in illicit activities***

86. To identify the economic benefits arising from a reduction in illicit activity, we first quantify the total economic cost of illicit activity. The proposed beneficial ownership reform will help to tackle crime by enhancing corporate transparency. It should result in a situation where apprehending criminals is both cheaper and easier for law enforcement agencies. It should also have a deterrent effect (i.e. criminals less likely to misuse UK companies). Based on our understanding of the impact this policy will have on crime, we derive illustrative estimates of the benefits using a range of assumptions about the scale of the crime reduction. These are based on 2013 data, merely as an indicative year.



**Figure 1: The logic chain behind the benefits of the Transparency and Trust package**

87. In discussion with UK enforcement agencies, including the NCA (formerly SOCA), the SFO, the Met, the City of London Police, the Crown Prosecution Service, the Attorney General’s Office and HMRC, there has been unanimous agreement that greater transparency of UK company ownership will be beneficial. They have highlighted the potential deterrent effect on criminals who might otherwise seek to form or use UK companies for illicit purposes and the potential for a positive impact on the timeliness and efficacy of investigations and outcomes (e.g. recovery of stolen assets, disruption of criminal activity).
88. The SFO has commented that the overall Transparency and Trust package would “*make UK corporate vehicles less attractive to criminals as a means to commit fraud or facilitate money laundering*”. Similarly, the Met indicated that all of their major grand corruption/money laundering cases and their “smaller” financial crime investigations had the tracking down of the beneficial owners at the core. Whilst much of the criminal activity took place overseas, the UK, due to being a major financial centre, could be a conduit for funds, thus knowledge of UK company beneficial ownership would be a key additional tool. They estimated 30-50% of an investigation could be spent identifying the beneficial owners through a chain of ownership.
89. An increase in transparency could therefore reduce the financial and labour resources spent by law enforcement agencies on investigating and prosecuting this particular sort of offence. This means enabling law enforcement agencies to have faster/easier access to beneficial ownership information, or getting that information without tipping off the criminals, could have an economic benefit in terms of freeing up these resources to be re-allocated elsewhere (potentially into additional investigations). This is equally the case in respect of overseas authorities, who may need to make fewer formal requests for information to UK authorities as a result of a public register of beneficial ownership. As well as being of benefit to them, we might expect corresponding resource efficiency benefits for UK authorities as they would need to expend less time and effort in responding to these information requests.
90. In 2002 a Government IA<sup>49</sup> on similar proposals (though with real time updates to Companies House on beneficial interests exceeding 3%) was produced. It based its analysis on desk research and interviews with 30 key public and private sector sources. This estimated benefits to the police of £30m in cost savings and improvements in recoveries. Up-rated over the last 11 years, this leads to a benefit of some **£40m** pa.

<sup>49</sup>HMG (July 2002): *Regulatory Impact Assessment: Disclosure of beneficial ownership of unlisted companies*

91. It is not just law enforcement agencies that expect to derive benefits from enhanced transparency around company beneficial ownership. HMRC, for example, has indicated a number of potential benefits to having a central source of beneficial ownership information. Further information on the potential benefits to law enforcement and tax authorities is provided at **Annex D**.
92. Since the opacity of company beneficial ownership facilitates criminals' engagement in serious crime such as fraud and terrorism, it follows that increasing transparency could lead to a reduction in the total amount of this detrimental activity committed in society due to: the successful prosecution of those committing the crime; the deterrent effect of the measures introduced; and/or through the disruption of the criminal activity. For example, if a key member of an organised criminal gang is imprisoned, the activity of the rest of the gang may be restricted or stopped.
93. This benefit could take the form of a reduced number of crimes and/or a reduction in the average value of a crime. The existence of crime could result in a reduction in economic activity (e.g. agents engage in less economic activity to avoid fraud; and resources are spent on non-productive/inefficient activity, insurance expenditure and the Criminal Justice System, including the police/other criminal investigators).

#### *Total Economic Cost of Fraud*

94. On this basis, we have below sought to monetise partially the benefits arising from reduced crime through enhanced transparency of company beneficial ownership. It is not possible to monetise fully the benefits of the policy to society from a reduction in crime, nor the benefits to law enforcement agencies in terms of reduced costs (in part because there is no systematic distillation of the investigation data to identify the impact of a single factor, such as hidden beneficial ownership).
95. The crime associated with a lack of transparency of company control, including through hidden beneficial ownership, imposes significant direct costs on society. These costs include the physical, financial and emotional damage to the victim<sup>50</sup>; insurance expenditure; lost output; and costs to the Criminal Justice System, including the police. The economic cost of crime for a full range of offence categories has been estimated by Brand and Price (2000)<sup>51</sup>. We have selected fraud as a key crime on which to focus here; it is a financial crime of the sort that could be facilitated by the use of opaque company ownership structures and Brand and Price's fraud data also encompass money laundering. In pulling out this strand for further analysis, we should bear in mind that there is also the breadth of potential criminal activity linked with financial crime and hence opaque corporate structures.
96. The methodology used places a value on the opportunity cost of resources used:
- in anticipation of crime (e.g. insurance<sup>52</sup> or security expenditure);

<sup>50</sup> Economic theory would normally dictate that theft, for instance, is a transfer from one individual to another, so is not considered a loss to society. However, given that the transfer is unwanted and moves the stolen item from the legal economy to the illegal economy, following Brand and Price (2000), we consider this part of the costs of crime.

<sup>51</sup> Brand and Price (2000): *The economic and social costs of crime*. Home Office Research Study 217. London: Home Office. Although this is not a recent publication it set the standard for robust analysis in this area, and as set out below prices have been adjusted for 2013. The NERA (2000) crime figures are disaggregated slightly differently to ONS data but we have arrived at a reasonably close match between the two data sources.

<sup>52</sup> In a purely economic sense, when an insurance claim is made, it is a transfer. As such 'insurance expenditure' in our estimates only includes insurance administration costs (i.e. the running costs for insurance companies – staff, ICT, property etc) because without crime these costs would be deployed elsewhere in the economy (See Brand and Price (2000) for more detail). Companies might, for instance, purchase fidelity guarantee insurance to protect against fraud by an employee, or crime protection insurance. The Fraud Advisory Panel currently advise small businesses to consider such products, as part of their advice to reduce the impact of fraud on small and medium sized businesses. *Fraud Facts*. 2009: [https://www.fraudadvisorypanel.org/pdf\\_show\\_112.pdf](https://www.fraudadvisorypanel.org/pdf_show_112.pdf)

- as a consequence of crime (e.g. to the victim); and
- as a response to crime (e.g. to the criminal justice system<sup>53</sup>).

97. Below, we estimate the total economic cost of fraud. This figure is then used to give illustrative examples of the potential economic benefits resulting from the crime reduction associated with this policy.

98. We have updated the average cost estimates for inflation to arrive at estimates in 2013 prices, using standard HMT GDP deflators<sup>54</sup>. We have also removed the cost of benefit fraud which, as a conservative step, could be considered the subset of fraud less likely to be related to abuse of company structures. This gives us two estimates of the cost per fraud offence of approximately **≈£500** and **≈£1400** in 2013 prices as shown in the table below:

**Table 1: The Economic Cost of Fraud – A report from the Home Office and Serious Fraud Office (NERA, 2000)**

|   |   | 1999<br>Cost (£m) | 2013<br>Cost (£m) |
|---|---|-------------------|-------------------|
| Resource Costs                                    | Criminal Justice System (including SFO) | 579               | 776               |
|   | Other public sector                     | 412               | 553               |
|   | Private sector                          | 156               | 209               |
| Transfer Costs                                    | Public sector                           | 2682              | 3595              |
|   | Private sector                          | 1377              | 1845              |
|   | SFO                                     | 1138              | 1524              |
| Other misallocation of resources (tax distortion) |   | 1858              | 2490              |
| Number of offences                                |   | 7.7m              | 7.7m              |
| Total Economic Cost (Excluding transfers, £m)     |   | 3006              | 4028              |
| Average Cost Per Offence (£) Excluding transfers  |   | ≈400              | ≈500              |
| Total Economic Cost (Including transfers, £m)     |   | 8202              | 10992             |
| Average Cost Per Offence (£) Including transfers  |   | ≈1100             | ≈1400             |

\* Average costs have been rounded to the nearest £100 but the original values are used in calculations.

99. The two estimates differ because the lower figure of ≈£500 excludes transfer costs. A transfer is a redistribution of a good or income from one party to another party such that the recipient's gain exactly offsets the donor's loss and no resources are used. In a pure economic sense, when a criminal steals a victim's property this is a transfer. In reality, however, it is an unwanted transfer, and victims suffer the emotional and physical impact of crime; indeed, the Ministry of Justice *Criminal Justice System Cost-Benefit Framework* considers the victim's losses but not the offender's gains from crime. Including transfer costs gives a figure of ≈£1400 per fraud offence.

<sup>53</sup> The estimated impact on the Criminal Justice System (CJS) is based on the Home Office 'flow and costs model'. The model estimates the long run costs of a criminal flowing through the system from prosecution and trial to probation or imprisonment. This is based on an active sample of resource costs from staff in the CJS and any associated agencies.

<sup>54</sup> HMG (December 2013): <https://www.gov.uk/government/publications/gdp-deflators-at-market-prices-and-money-gdp-march-2013>

100. We consider ≈£500 as our ‘best,’ and most parsimonious estimate, while providing the estimate of ≈£1400 for further context as the cost of a fraud offence. While we cannot directly relate a number or proportion of such offences to the use of hidden beneficial ownership, we can estimate, for illustrative purposes, the overall economic cost of fraud, and seek to understand how it might be changed.

101. To arrive at an estimate, we multiplied the average cost of fraud offences by ONS (2013)<sup>55</sup> crime figures. We estimate that there were **1 million fraud offences** across the UK in 2012/13<sup>56</sup> as an indicative year.

102. On the basis of 1 million fraud offences being committed in 2012/13 with an average cost of ≈£500<sup>57</sup> we estimate that the total economic cost is **£523m**, of which £496m falls on the public sector<sup>58</sup> and £27m falls on the private sector. This is calculated as follows:

$$\approx£500 \times 1\text{million} = £523\text{m}^{59}$$

*Average cost per offence x number of offences*

#### *The potential impact of this policy intervention*

103. One might expect the impact of the *Transparency and Trust* package, which contains a series of targeted measures including enhanced transparency of company beneficial ownership, would impart a deterrent effect on criminal activity. This could potentially be reinforced by a further deterrent effect from additional law enforcement capacity on the basis of greater investigation efficiency or capability if companies are more transparent. For example, enforcement agencies may be able to match up beneficial ownership data held by Companies House against their own systems and databases to identify trends or patterns highlighting criminal activity. This could in turn have a deterrent effect which could then reduce costs for law enforcement agencies.

104. In terms of wider reductions in costs for law enforcement agencies, enhancing the transparency of company beneficial ownership would remove a layer of complexity in investigations seeking to identify the natural person ultimately owning or controlling a company, resulting in expedited and more efficient processes.

105. As noted above there is no reliable or systematic way of attributing reductions in law enforcement agencies’ costs or the consequences directly and exclusively to enhanced transparency of company beneficial ownership. For this reason, the benefits resulting from reduced costs to law enforcement remain non-monetised. We should also note that beneficial ownership reform is only one part of the *Transparency and Trust* package. While it is difficult reliably to predict change in the crime rate related to any one part of the package, we could consider that the overall combined effect from implementing the comprehensive package is likely to be greater than the sum of its parts.

55 Office for National Statistics (2013): *Crime in England and Wales, year ending June 2013 – Appendix tables*

56 Since the ONS data are only for offences committed in England and Wales and the NERA figures cited in Brand and Price (2000) split all UK recorded offences into those committed in each devolved administration, we applied the same proportional distribution as Brand and Price (91% of fraud offences committed in England and Wales; 8% committed in Scotland; and 1% committed in Northern Ireland) to arrive at an estimate of the total offences committed in the UK. This overall figure of 1 million excludes cheque and credit card fraud and accounts for the number of unreported offences, using the crime multiplier in NERA (2000).

57 To note unit costs are rounded for presentation in the text, with original figures used for calculation to give overall estimates.

58 Public sector costs include costs to the Criminal Justice System, the NHS, Customs & Excise & VAT, Inland Revenue and Local Authorities. The public:private sector cost distribution is calculated based on the distribution in the above table.

59 To note unit costs are rounded for presentation in the text, with original figures used for calculation to give overall estimates.

*The scale of the economic benefits*

106. Whilst law enforcement agencies are not in a position to quantify the direct or deterrent benefits that the *Transparency and Trust* package might have on fraud offences, we can offer some illustrative examples of the likely economic benefits associated with reducing crime:

| Reduction in crime     | Economic benefit      |
|------------------------|-----------------------|
| 2% reduction in crime  | £10.5m (2% of £523m)  |
| 5% reduction in crime  | £26.1m (5% of £523m)  |
| 10% reduction in crime | £52.3m (10% of £523m) |

107. For further context, as mentioned, we can use the average cost estimate of ≈£1400, which includes transfers, to give an overall cost of fraud. On this basis, the total cost estimate rises to approximately £1.43bn pa. Of this figure, around £1.16bn pa falls on the public sector and £270m pa falls on the private sector. The benefit of reducing corporate opacity to reduce this crime would similarly be derived from the reduction in these indicative costs. In this case, for example:

| Reduction in crime     | Economic benefit         |
|------------------------|--------------------------|
| 2% reduction in crime  | £28.5m (2% of £1,427m)   |
| 5% reduction in crime  | £71.4m (5% of £1,427m)   |
| 10% reduction in crime | £142.7m (10% of £1,427m) |

108. Feeding into or stemming from illicit activity associated with companies are a range of organised crime and potentially terrorism offences beyond fraud. As noted in Brand and Price (2000), the crime multiplier associated with organised crime is substantial because it sustains and creates other criminal markets, which impose further costs on society. The Home Office analysis which accompanied the launch of the National Crime Agency (Mills et al 2013) highlights that organised crime cost the UK £24bn in 2010/11, with drugs supply, for instance, costing the UK £10.9bn within that total<sup>60</sup>. The Home Office analysis excludes money laundering, which as mentioned above has a significant global impact.

109. The above analysis represents just one potential source of benefits of reducing crime. Subjective wellbeing benefits should also be considered. As Brand and Price (2000) set out, there are a range of potential emotional and physical impacts on victims of crime, which might leave a legacy of problems. Reducing crime based on corporate opacity, including through enhanced transparency of company beneficial ownership, will therefore realise benefits to national well-being, as measured by the National Well-being programme led by ONS<sup>61</sup>.

110. Action will also help to develop an environment conducive to economic growth in the UK, and attendant benefits. There is a strong body of evidence highlighting how crime in itself acts as a drag on investment, job creation and ultimately economic growth. For instance, Goulas and Zervoyianni (2013)<sup>62</sup> found that in times of macroeconomic uncertainty, a 10% increase in the

<sup>60</sup> Home Office analysis cost estimates presented do not include SOCA costs of preventing and responding to organised crime (Mills et al (2013): *Understanding organised crime: estimating the scale and the social and economic costs*, Home Office, Research Report 73) [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/246390/horr73.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/246390/horr73.pdf). Any benefits derived from this policy change cannot be monetised.

<sup>61</sup> <http://www.ons.gov.uk/ons/guide-method/user-guidance/well-being/index.html> This includes measures of the crime rate, happiness, anxiety and mental well-being.

<sup>62</sup> Goulas and Zervoyianni (2013): *Economic growth and crime: does uncertainty matter* Applied Economics Letters, Vol 20, issue 5, pp420-427

crime rate is associated with a reduction in annual GDP per capita growth of 0.49%-0.62%. Although the literature<sup>63</sup> does not directly identify the mechanism through which crime affects growth, it has repeatedly been highlighted that reducing crime will support growth.

111. There are also benefits to reducing crime which accrue not just in the UK but internationally. These are not within scope of the process of assessing the impact of the policy change for these purposes, but are nevertheless important. As set out in the 'problem under consideration', illicit flows out of low income countries, particularly in Africa, will often be channelled through company structures. They are extremely significant, and often claimed to be more than the aid the developed world provides. Reducing the potential for abuse of the company structure should therefore derive benefits not only for crime in the UK, but for the UK's international reputation and for its international partners.
112. In addition to benefits to individuals through crime reduction, there will also be benefits to regulated entities<sup>64</sup> who will have more ready access to information on beneficial ownership, either through Companies House, credit reference agencies or through the companies themselves being better able to respond to enquiries. We would therefore anticipate some cost savings here in terms of carrying out due diligence. Similarly credit reference agencies<sup>65</sup> have indicated that they may also gain from increased transparency through better risk assessment of companies. Also for private sector organisations engaged in asset recovery and fraud investigation, they might find their costs of investigation reduced. However we have not been able to determine the magnitude of the cost savings. For example, in discussions between financial institutions and HM Treasury, the former have explained that they are unable to monetise the costs they incur in obtaining beneficial ownership information as separate from the total costs incurred in carrying out AML due diligence. This means it is not possible to estimate the potential cost saving if they were to have a central source of information as a starting point for beneficial ownership due diligence checks.
113. No additional data on costs and benefits were provided though the responses to the formal BIS discussion document. 80% of responses to the questions in the discussion document around beneficial ownership were however positive about changes to the obligations, with some wanting the proposals to go further – in terms of the scope and nature of any new requirements - than outlined here. Benefits mentioned included: reducing tax evasion, corruption and money laundering; lowering the costs to regulated entities' in terms of conducting due diligence; supporting developing countries in their efforts to tackle the misuse of companies and tax evasion; increasing the UK's integrity; deterring criminals from operating in the UK; reducing the UK's cost of capital; and providing more information about who does business with whom.
114. In summary, **there is little quantified data about the benefits resulting from this policy proposal**. However, based on the responses to the discussion document and the focus groups, it could be expected that: law enforcement agencies would experience increased efficiency; regulated entities might experience reduced costs; there could be reduced criminal activity and, from this, efficiency and welfare gains to the economy; and potentially a non-negative impact on economic growth.

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<sup>63</sup> See also Detotto and Paulina (2013): *Does more crime mean fewer jobs and less economic growth?* European Journal of Law and Economics, Vol 36, Issue 1, pp183-207 and Detotto and Otranto (2010): *Does crime affect economic growth*. International Review of Social Sciences, Vol 63, Issue 3, pp330-345.

<sup>64</sup> Regulated entity refers here to an entity subject to the Money Laundering Regulations 2007 (No. 2157), as defined in Regulation 3. This includes: credit institutions, financial institutions, auditors, insolvency practitioners, external accountants, tax advisors, independent legal professionals, trust or company service providers, estate agents, high value dealers and casinos.

<sup>65</sup> Business Information Providers Association

## **B2. Benefits to companies and individuals from corporate transparency supporting the business environment**

115. As outlined in the ‘rationale for intervention’ section, greater transparency of company beneficial ownership will make it easier for those who engage with a company to identify with whom they are actually dealing and for company shareholders to hold the company to account.
116. In the representative company survey undertaken for BIS by IFF Research 10% of respondents indicated that the proposed reform would ensure they know with whom they are doing business, thereby increasing trust and confidence in their organisation, creating a level playing field, exposing companies that are breaking the law and improving their own peace of mind. As noted by the RPC, this implies that the benefits around increased transparency might in practice be less than set out in the rationale above. We accept this comment and the implication that the non-monetised benefits arising from increased transparency should not be overstated in size.
117. This is however to some extent mitigated by other consultations. In a Focus Group of representative industry bodies, participants recognised the potential benefit to the UK in being seen to have fully met international standards around company beneficial ownership (and the potential adverse impact if the contrary were true). Furthermore, representatives of business information providers highlighted in discussion the potential economic benefits of having company beneficial ownership information in the public domain. They noted their customers (lenders, insurers etc) would be likely to use information of this nature to inform decisions about whether to do business with a company, and on what terms, as it would help build a picture of the company. Providers could look at trends and patterns in the data to improve the quality of their own analysis. In this way they felt that a central registry of company beneficial ownership would have the potential to facilitate or improve the terms of economic transactions.
118. Economic theory suggests this increase in transparency is likely to reduce information asymmetry and increase trust, and therefore increase economic activity including trade and investment (see ‘rationale for intervention’ section) although the level of the increase is highly uncertain. Empirical evidence in this area, whilst informative, relates to the general relationship, observed across the economy, rather than beneficial ownership specifically.
119. Ultimately, enhancing trust in the business environment serves to “grease the wheels” of economic activity and facilitate economic growth. Greater transparency is associated in the literature with greater investor confidence, alongside trust in companies and between companies. This enables economic transactions to go ahead more readily since, for instance, a buyer will not be discouraged or delayed by a lack of transparency and trust in a seller; this enables them safely to simplify the contracting process between them<sup>66</sup>. Therefore increased corporate transparency can increase economic growth through the mechanism of increasing trust and reducing transaction costs. A more detailed explanation of the theoretical and empirical framework linking trust, transparency and growth is set out in **Annex D**.
120. By increasing corporate transparency, including through the creation of a central registry of company beneficial ownership information, benefits to trust, and therefore the business environment and potentially economic growth, could potentially be realised but the level and specific policy causal link are uncertain and hence are unmonetised here.

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<sup>66</sup> The importance of trust in economic transactions is highlighted in Fukuyama, F. (1996): *Trust the social virtues and the creation of property*

## Costs

121. The cost estimates below are based on results from a survey of companies undertaken by IFF Research (2013)<sup>67</sup> (see **Annex A**). The costs identified through the survey have been processed - using statistical techniques and in the light of subsequent discussions/interviews with companies - before being applied to wider populations of companies to arrive at estimates of the overall impact of the policy. This processing has included the removal of implausible high values that could make the dataset less robust and the re-coding of zero wage cost values (again, see **Annex A**)<sup>68</sup>. We intend that companies will be required to start keeping their own registers from January 2016 and that they will need to start filing this information at Companies House from April 2016.

## Corporate entities in scope

122. We intend to require all bodies corporate that currently register information on their members at Companies House to hold their beneficial ownership information and provide it to the central registry. This would include companies and Limited Liability Partnerships as well as some lesser used corporate forms (for example, Societas Europaea).

123. However, we intend to exempt companies with securities listed on a UK regulated or prescribed market from the requirement to maintain this information and provide it to Companies House. We also intend to exempt companies with securities listed on an EEA regulated market subject to equivalent disclosure requirements. These companies would simply be required to state their exemption in the course of routine information provided to Companies House.

124. In order to identify the number of companies in scope we have used the FAME company database (which uses, amongst other sources, Companies House data). This is because, unlike Companies House data, the FAME database allows us to identify company size by turnover, assets and employees.

125. The FAME database reports that there are **3.47m UK companies**<sup>69</sup>. This figure includes active and dormant companies, and companies in the process of being dissolved.

126. The proposal exempts companies with securities listed on a UK regulated or prescribed market<sup>70</sup> and those on regulated EEA markets subject to equivalent disclosure requirements. We would also intend to exempt Limited Partnerships, European Economic Interest Groupings, industrial/provident companies and foreign companies. Applying these exemptions to the FAME population gives an estimated number of companies in scope of 3,429,549<sup>71</sup>. Of these 3,381,941 **are small or micro companies**, 30,277 are medium and 17,381 are large. The population is highly skewed towards small firms where we might expect the costs to be lower (this a priori judgement accords with results from the survey BIS undertook, as set out in the SaMBA below).

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67 IFF Research (2013): *Transparency and Trust Company Survey* – <https://www.gov.uk/government/publications/company-ownership-transparency-and-trust-survey-and-follow-up-research>

<sup>68</sup> Please note: costs have been rounded in this section to avoid spurious accuracy. Also the costs have been updated in the main body of the IA to 2014 prices.

<sup>69</sup> Company population estimates were extracted from the FAME database (Bureau Van Dijk Electronic Publishing, 2013). This figure includes Limited Liability Partnerships.

<sup>70</sup> We assume that we will be able to exempt companies listed on prescribed markets from the requirement to maintain a PSC register. This is subject to the outcome on the EU's Fourth Money Laundering Directive which may require companies listed on prescribed markets to report beneficial ownership information to a central register.

<sup>71</sup> FAME database Bureau Van Dijk Electronic Publishing, 2014 data extracted the 11/03/2015.

Companies House register statistics show that there are around 59,000 Limited Liability Partnerships (LLP) on the ‘LLP Total Register’<sup>72</sup> (included in the 3.43m figure above).

127. It is expected that the costs to companies will depend on the number of shareholders but also its size and ownership structure. According to FAME data, out of the 3.43m UK companies, there are **3.2m with fewer than 4 shareholders**. It is likely that, for these companies, the overall costs associated with identifying and reporting beneficial ownership would be lower than for companies with more shareholders. In addition, the table below sets out the number of firms broken down by the complexity of their ownership structure. Ex ante, we also expect those with more layers/more complexity of ownership to face the greatest costs in identifying their beneficial owners.

| Complexity of ownership                  | Number of companies |
|--|---------------------|
| One or fewer layers of ownership         | 3,235,424           |
| Two or three layers of ownership         | 107,847             |
| Four or more layers or foreign ownership | 86,278              |

128. As set out in our description of the policy option, some companies (A) will be owned by entities (B) that are exempt from maintaining a register (e.g. because they are listed), or already maintain a register of beneficial ownership. Entity B is deemed to be a ‘relevant legal entity’ or ‘RLE’. In such cases, A will only be required to place details of B on its register, rather than details of B’s beneficial owners. Analysis using the FAME database indicates that 322,213 UK companies are wholly or partly owned by a RLE. In such cases we anticipate the costs to A could be lower than might otherwise be the case as the amount, and difficulty of gathering, data might be lower.

129. Nevertheless, the proposals, to a greater or lesser extent, will impact on all companies in scope regardless of size or complexity of ownership.

## **C1. Public sector costs**

### One-off costs

#### *a.1. IT development*

130. Costs to Government will involve increased costs to Companies House in setting up and administering the register, including the cost of setting up systems both for making information publicly available and protecting certain information from public disclosure (the “protection regime”). All of these public sector costs are included in this Enactment IA.

131. Companies House has indicated that they will experience a one-off cost ranging from **£60k-99.6k** (with a mid-point of £79.7) for IT development to set up the registry<sup>73</sup>. This will involve collecting and storing beneficial ownership data in new fields and tables within the existing system. It is estimated that it will cost £40k to update the information in the context of the new ‘check and confirm’ process. Making the information publicly accessible will cost a further £20k. Companies House also adds £40k contingency to the range. These costs only account for

<sup>72</sup> Companies House (November 2013): *Companies Register Statistics for November 2013*

<sup>73</sup> We expect there to be transition costs to software providers associated with updating their standard packages to reflect the changes in the Transparency and Trust and Company Filing proposals. Software companies provided a single cost estimate for the policy proposals collectively rather than broken down by proposal. Discussion of these cross-cutting costs is included in the Company Filing Requirements validation IA. Therefore we have not included the costs here to avoid double counting.

development and do not include any other business costs such as training or communication. If there is insufficient internal development resource external resource may be required which would cost significantly more.

#### *a.2. Communication and publication costs*

132. Companies House will issue communications to all companies to ensure they are fully aware of the regulatory changes associated with beneficial ownership disclosure and indeed the rest of the *Transparency and Trust* package.

133. It is likely Companies House would use a wide range of cost effective and targeted communications to companies such as including 'inserts' (i.e. an information page in another document) with standard reminders. Companies House has indicated the anticipated costs of sending an insert on *Transparency and Trust* reforms to 3.19m companies (as estimated in the *Transparency & Trust Final IA*) would be minimal, at around £23k. Using the most recent estimate of the number of companies affected and uprating the cost data for 2014, this cost rises to £25.3k. This cost would cover the communication for the Corporate/Shadow Directors' part of the package of reforms as well as for beneficial ownership, thus we have assumed that the £25.3k would be split evenly between the two policies. Hence the cost for beneficial ownership is **£12.7k**.

134. This would be supplemented by website notices and guidance, FAQs and social media information. Engagement with company agents and representatives through Focus Groups and events would also be helpful in ensuring that the requirements are understood. In addition, BIS will produce statutory and non-statutory guidance on the policy, supported by a voluntary Expert Working Group made up of representatives from business, civil society and professional service providers.

**The overall monetised one-off costs to the public sector are estimated to be £92.4k (£12.7k + mid-point between £60k and £99.6k) with a range of £72k and £112k.**

#### Ongoing costs

##### *a.3. Staff costs to support the registry*

135. On the basis that beneficial ownership information will be submitted at incorporation and in the context of the 'check and confirm' process (i.e. at least once in a 12 month period) there will be very little additional cost in terms of staff resources (relative to total Companies House costs) as 98% of incorporations and returns are handled electronically.

136. There will however be ongoing staff costs of approximately **£225k** pa to support the closed system for beneficial owners' residential addresses and full dates of birth, and for all of the information on those beneficial owners who are deemed at risk (the "protection regime"). This figure is based on the current costs of seven people administrating the (closed) usual residential address system for company directors<sup>74</sup>. Companies House estimate that the costs will be roughly the same for setting up the closed register for beneficial ownership information. However the number of applications will ultimately affect the costs to Companies House.

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<sup>74</sup> Company directors are required to provide a usual residential address and a service address to Companies House. The former is not available for public inspection, other than to specified authorities and Credit Reference Agencies and is maintained on a closed system. Currently an individual or company may apply to the Registrar of Companies to make an address unavailable for public inspection (£55 per document to be suppressed); or to make usual residential address information unavailable to a Credit Reference Agency (£100 per application).

137. As described in the separate IA on the protection regime, beneficial owners who consider themselves at serious risk of physical harm will be able to apply to Companies House for all of their information to be protected from public disclosure. On receipt of an application for information to be protected, Companies House may need input from a relevant authority, such as the police, to help them decide whether the application should be granted. There would be costs to those authorities in providing that advice/confirmation but we do not know how long this might take or how much it might cost.
138. Although it is not a like for like comparison, the anecdotal evidence provided by the National Crime Agency and the Metropolitan Police's National Domestic Extremism and Disorder Intelligence Unit in their risk assessment of individuals seeking police protection could act as a proxy. This suggests that the time and cost taken are specific to the circumstance of each application. For example, complex cases could take over 6 months to assess.
139. We also do not know how many applications to Companies House for information to be protected there might be. As an indication, in 2013/14 there were around 500 applications to Companies House for information to be suppressed on the public register or not provided to Credit Reference Agencies. We anticipate more applications in the context of beneficial ownership.
140. Following standard IA methodology, this IA assumes 100% compliance, thus court costs will be zero. However, where this turns out not to be the case, as the policy will introduce new criminal sanctions there may be additional costs for the criminal justice system (Justice Impact Test provided separately and summarised below).
141. **The total Net Present Value monetised costs to the public sector are therefore expected to be £1.8m over 10 years**<sup>75</sup>. Companies House operates as a trading fund and would need to recover the costs of those services. For statutory activities they do this by charging fees. Companies House have noted that, based on the current level of information, they do not anticipate an increase to existing fees to companies as a result of this proposal.

## **C2. Private business costs**<sup>76</sup>

142. One of the policy drivers for beneficial ownership reform is the opacity associated with company ownership – the fact we do not know who really owns and controls UK companies. There are therefore methodological challenges associated with estimating the cost to business with a high degree of certainty because we do not know how many beneficial owners of UK companies there are, or to what extent UK companies already know and hold this information. The RPC asked for clarification on the sources of data used in the consultation IA and for sensitivity analysis using alternative sources. The analysis in the final IA (and therefore this Enactment IA) used results from a one-off bespoke representative company survey commissioned by BIS but validated/informed by other sources as set out below (**Annex A** provides more detail on the methodology used and **Annex C** provides some sensitivity analysis on the key assumptions).
143. Responses to the *Transparency and Trust* discussion document were mixed with respect to the costs to business from this reform. 30 of the 199 responses which set out views on the

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<sup>75</sup> 10 years is the expected life of the policy and the NPV uses standard Green Book discount rates.

<sup>76</sup> The estimate of costs in this section uses the survey results and methodology reported in Annex A, uprated to 2014 prices.

costs and benefits indicated that the costs would be minimal; a further 16 indicated that costs would be burdensome.

144. A 2013 report for Global Witness by J Howell & Co Ltd<sup>77</sup>, based on a 2002 government RIA, estimated the costs to be a £24m one-off cost plus £2.3m ongoing costs. These equated to less than £10 one-off cost and less than £1 annual costs per company. We have considered this report, and its findings, carefully. However, the approach is largely based on assumptions and expert opinion, rather than direct engagement with the business community. The assumptions used may not therefore reflect the actual cost to companies (e.g. the cost of collating and processing the relevant information). In addition, the research does not fully consider familiarisation costs, which we would expect to form a significant proportion of the total cost to companies, nor the cost of identifying the beneficial owner.
145. BIS also undertook an online non-representative company survey as part of the consultation process for the proposed measures. 32 responses were received. Around half of respondents said that the cost of gathering the information would be zero or negligible but other estimates ranged from £100 pa to £50k pa and 5% of operating costs.
146. A sample of published IAs was analysed but provided little relevant cost information for this specific proposal. For example, the most closely related assessment was made for the Anti-Money Laundering IA<sup>78</sup>. This notes that complying with the requirements for newly obligated entities would cost 0.16%-0.29% of operating expenses (though it offers no specific monetised cost estimates). It also noted that additional beneficial owner information requirements are not expected to entail significant burdens to individual companies but that, because a large number of entities would be affected, there would be significant cumulative impact. The Companies Act 2006 evaluation<sup>79</sup> provided estimates of costs associated with **all** the changes for the Companies Act – both internal wage costs and additional costs of external advice. Time spent internally over three years ranged from 0 to 40 hours; external professional services were bought in by only 52% of companies; 64% of those reporting purchasing external services incurred under £500 of costs and 32% did not know the cost. The total cost of all the Companies Act changes is estimated at £1.11bn pa<sup>80</sup>.
147. Also, in 2007, PWC were commissioned to produce an Administrative Burdens Measurement Exercise. This exercise estimated administrative burden (compliance costs) of regulations across a number of policy areas including business environment. PWC estimated the cost of completing, signing and returning Companies House form 692b (for the return of alteration in the directors or secretary of an overseas company or in their particulars)<sup>81</sup> to be £10.73 per company, which uprated to 2014 prices is £12.66.
148. Modelling from Companies House<sup>82</sup>, indicates that the familiarisation costs for a broadly comparable measure are substantially lower; modelling indicated it would take companies 20 minutes to familiarise themselves with a comparable policy, which was multiplied by £19 – the

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<sup>77</sup> John Howell & Co. Ltd. (April 2013): *Costs of Beneficial Ownership Declarations*

<sup>78</sup> Impact assessment on the prevention of the use of the financial system for the purpose of money-laundering, including terrorist financing, 2013

<sup>79</sup> <http://www.bis.gov.uk/assets/biscore/business-law/docs/e/10-1360-evaluation-companies-act-2006-volume-1.pdf>

<sup>80</sup> Our calculations based on the data provided in the Companies Act 2006 Evaluation (which did not formally calculate a total cost to business) gave a total cost per company of £343 p.a. in 2010 prices, which includes both additional costs and wage costs. This gave a total cost of £1.11bn p.a. To arrive at this we used a total company population of 3,238,890; a director's wage of £48.36 taken from ASHE data as above (and transformed into 2010 prices (£46.58) using the GDP deflator); and we used a mid-point of the categories displayed for compliance time and for total cost of external services

<sup>81</sup> The form deals with any alteration made in the Directors or secretary of an overseas company or the particulars contained in the list of the directors and secretary.

<sup>82</sup> Detail in cost benefit analysis within consultation on Company Filing Requirements.

mid point between the median wage and the wage of a company director – to give a total familiarisation cost of around £6.

149. The different sources of information gathered and the results are presented in the table below:

**Table 2: Comparison of data sources**

| Data source                                    | One-off costs   | Ongoing costs               |
|--|---|-----------------------------|
| Consultation responses (199 responses)         | 30 responses – minimal costs, 16 responses – burdensome |                             |
| Global Witness report                          | £10 per company   | £1 per company per year     |
| Non-representative consultation (32 responses) | Range between £0 and £50,000                            |                             |
| PWC report                                     |   | £12.66 per company per year |
| Companies House                                | £6 for familiarisation                                  |                             |

150. Given the limited, but wide-ranging estimates available on the costs, we felt there was not sufficient information to make an assessment of the costs and benefits of the proposal. Thus BIS commissioned an independent representative survey of companies, undertaken by IFF Research (see **Annex A** for information on the methodology used). The sample reflected companies which were small/micro and ones which were medium/large and also the complexity of their ownership structure.
151. The questions covered were: the familiarisation costs of the proposals; the initial costs of identifying and collecting the details of the beneficial owner; the collation and storage of the data; sending returns to Companies House; and, if they own another company, the cost of responding to a request for information about their beneficial ownership.
152. The total costs figures were calculated based on estimates for the **number of hours** it would take particular employees to comply with the proposals multiplied by the **hourly wage rates**, uprated for non-wage costs, taken from the Annual Survey of Hours and Earnings (as set out in **Annex A**). Estimates of additional costs, such as the cost of external advice, were also provided.
153. Survey responses were collated by size of companies and by complexity of the ownership structure (that is; small simple; large simple; small reasonably complex; large reasonably complex; small complex; large complex).
154. In-depth analysis of the survey data revealed a number of issues with the methodology (more detail is provided at **Annex A**). In particular a number of respondents estimated very high costs in each of the cells, sometimes in contrast to the majority who estimated zero costs. In the light of the range of responses and methodological issues, we undertook further evidence gathering. We held two additional focus groups and commissioned further in-depth interviews with a number of the respondents to the survey. In the former case the intention was to validate or otherwise the cost estimates presented in the consultation IA: in the latter it was to understand better what underpinned the cost estimates. The numbers below used to calculate the costs are based on the results of the first survey uprated to 2014 prices and adjusted in the light of the focus groups and the second survey (**Annex A** includes the details of the new survey and the processing made to the results of the first survey).

155. In summary we made two statistical changes to the data from the first survey:
- we removed extreme values for each of the questions; and
  - we re-coded responses with zero costs.
156. The aim of these changes was to apply standard statistical techniques to adjust for extreme values/outliers and to remove/adjust results which appeared implausible based on our consultations with stakeholders. That is, we adjusted both extreme values and zero costs for all relevant questions. Similarly to the consultation IA, we used a truncated mean in the final IA (and therefore this IA) for each survey question. For the zero costs, an assumption is made that the proposal will have a cost to all companies (e.g. understanding what the new regulations mean for them).
157. The survey also provided estimates of the additional costs companies said that they would incur when accessing professional (external) advice, e.g. from lawyers and accountants. We did not adjust the zero values received as the results of the follow-up survey showed that where companies had said there was no cost in the first survey they confirmed their view in the second. However, two adjustments were made to the raw data. The first adjustment here was that the extreme high values/outliers were removed, as above. Secondly whilst we included the one-off additional costs we did not include the additional costs for ongoing activities. This was done for a number of reasons:
- A priori it was expected that legal/accountancy advice would be used for:
    - **Familiarisation** – for companies to ensure that they knew what they needed to do to meet their legal obligations (both in relation to the primary and secondary legislation)
    - **Identifying** the beneficial owners – to ensure that the communication would enable them to meet the requirements
    - **Collation and storage** – to ensure that the sensitive/personal data was stored correctly and potentially alongside accounting/other ‘check and confirm’ information
    - **Responding** to a request for information – again to make sure that the request was valid and that the response would ensure that the company was complying with the legal requirement
  - However we considered that ongoing advice was less likely to be required when:
    - **Updating** information – as the system would already be set up and it then is a matter of just data inputting
    - **Reporting** to Companies House – again this is a part of a standard process unlikely to require both in-house resources and external advice. However, it should be noted that some companies have an ongoing relationship with a Trust and Company Service Provider (TCSP) (including Company Registration Agents, accountants and legal firms) to provide services such as completing Annual Returns. In these cases a company might use one of these organisations to undertake the work for them, but again it would not be in addition to in-house resources (this is considered in the sensitivity analysis in **Annex C**).
158. As part of the follow-up survey we asked companies to review their answers to the questions about additional costs. Generally, the second survey indicated there were differences in interpretation of the questions on additional costs across respondents. Some companies indicated their estimates were a worst case, others they would actually not incur any costs and still others noted there was some double counting between wage costs and additional costs.

159. On the question of one-off additional costs for beneficial ownership, IFF Research indicate that the results showed that “on the whole” companies said the costs provided in the initial survey sounded about right.
160. On the question of ongoing costs, some companies felt the (low) costs reported in the first survey were about right. However at the higher end of the costs IFF Research indicate that “*they felt that they would not need to incur legal fees*”. Companies from the research commented:
- *“I think that the most likely outcome is that the cost will be negligible... we are only talking about internal time.”*
  - *“Hopefully I would not consider external advice as we now know where the data is and how to access it.”*
  - *“I wouldn’t normally get legal advice unless I felt that it was something I didn’t really understand.”*
161. Furthermore our view was that the policy design – of the reporting being included as part of the new ‘check and confirm’ process<sup>83</sup>, the simple updating of existing records/forms and guidance being provided – would mean ongoing additional advice would not usually be required in addition to ongoing in-house wage costs. In the follow-up survey IFF Research reported that, while half of the companies felt that familiarisation cost would still be the same in the light of the new information on policy implementation, a quarter thought that the costs would go down and a further quarter felt that the cost would be higher: for complying with the requirements, respondents either felt that costs would stay the same or fall. There is also the consideration that, if it were required, it could rapidly decay (and hence the annual cost would not be incurred throughout the 10 year appraisal period at the same level). The issue of additional costs is revisited in the sensitivity analysis (**Annex C**).
162. In conclusion, we have included additional one-off costs only in the base case and we have taken the charge/fee as the opportunity cost to the economy of the external advice.
163. The subsequent focus groups that we set up for the Final IA reconsidered the costs presented in the consultation IA. These were largely validated by the groups and, although the attendees found it difficult to place an accurate figure on how much it would cost them to follow a certain procedure, in general they thought our estimates seemed to be reasonable for small simple companies (around 94% of the population) but costs could be considerably higher for larger and more complex companies. Given that the figure was already weighted by the size and complexity of the company, we considered it to be consistent with the types of comments the groups made. The figures presented in the final IA and this IA resulting from the revised statistical adjustment broadly accord with those presented in the consultation IA.
164. These approaches aim to ensure any data considered is as robust as it can be. **Annex A** provides further information on each of the adjustments and **Annex C** provides the sensitivity analysis on key assumptions. The results of this process are given below.

**Table 3: Breakdown of costs to businesses – wage costs and additional costs associated with obtaining external advice<sup>84</sup>**

|  |                        |                        |
|--|------------------------|------------------------|
|  | <b>Best estimate -</b> | <b>Best estimate -</b> |
|--|------------------------|------------------------|

<sup>83</sup> See Government response to the Company Filing Requirements consultation. The ‘check and confirm’ process will replace the Annual Return.

<sup>84</sup> Updated to 2014 prices

|   | Adjusted mean wage costs per company £ | Adjusted mean additional costs per company £* |
|---|--|---|
| <b>One-off costs</b>                    |  |   |
| Familiarisation costs                   | 57.1                                   | 36.4  |
| Identification and collection**         | 4.4                                    | 9.3   |
| Collation, processing and storage       | 13.4                                   | 11.9  |
| <b>Sub – total average one-off cost</b> | <b>75</b>                              | <b>57.6</b>                                   |
| Responding to request (only for RLEs)   | 10.9                                   | 19.8  |
| <b>Ongoing costs</b>                    |  |   |
| Annually update own records***          | 11.2                                   |   |
| Report to Companies House annually****  | 13.7                                   |   |

\*Additional cost are only included for one-off costs. It is assumed that there will not be any ongoing additional costs (see above for explanation).

\*\*The results for this cost is halved (and is a best estimate) as there will be a shared obligation for these actions falling on both companies and beneficial owners (we have not been able to monetise the costs for the individual beneficial owners as we do not know what costs they will be incurring as they will not be replicating the actions of the companies<sup>85</sup> Also see text below for further explanation).

\*\*\*The policy will require companies to update their own records as they are made aware of changes by the beneficial owner or where they know or have cause to believe that a change has occurred. The changes, due to their nature, are assumed to take place less than once a year (see below for further explanation).

\*\*\*\*It is not clear whether respondents costed this in the context of the existing Annual Return process or as a new, separate process. The latter may be expected to have a higher cost than the former and this may therefore have impacted the responses provided. As the information will form part of the new 'check and confirm' process, the costs estimated here might be overestimates.

165. The table above gives the average cost per company of the various actions they will be required to take as a result of the policy. The 'sub-total' row gives the total average one-off cost that will be imposed on all companies. The 'responding to requests' row is a cost that will only apply to a limited number of companies (see below).

#### One-off costs

166. Based on the information above, the one-off costs to companies for **familiarisation, identification of beneficial owners, collection of data and collation and storage of sensitive/personal data**, i.e. the initial set up costs, have a best cost estimate of **£454.9m** for all companies.

This best estimate is derived as follows: (£75 + £57.6) \*3.43m, where 3.43m is taken as the total number of UK companies in scope.

167. The RPC asked for more informed sensitivity analysis on the central estimates. Sensitivity around this figure to provide high and low estimates is based on the statistical treatment of the survey results based on the coefficient of variation and its use in the degree of truncation to arrive at a mean. These in turn are informed by the second survey and focus groups results (see **Annex A**). Here the range for one-off costs is between £335.8m to £765.7m.

<sup>85</sup> The company, when trying to identify its beneficial owners, will need to produce an explanatory letter, and potentially approach a number of companies/individuals across a number of layers of ownership and chase up non-respondents. The individual having to provide information proactively, apart from familiarisation, is likely to incur just the cost of producing an email. The two types of activity are not synonymous and hence the costs incurred will be different.

168. The cost to companies of identifying and collating data on beneficial owners has been reduced from the initial survey results given that a legal disclosure obligation will also be placed on the beneficial owner to inform the company of their interest in the company in some cases (the survey questions explicitly assumed the obligation would be solely on the company). The company itself will only be required to take reasonable steps to obtain beneficial ownership information. We judge that the costs to companies will be lower as a result, and this is supported by the follow-up company survey. In the light of knowing some beneficial owners would provide information proactively, companies said:

- *“Those times and costs would go down considerably. Down by 90%, because all the work’s done for you. They’re just saying “we’re here, hi.”*
- *“Go down by 25% [...] because we would only have to do it for one shareholder and not three.”*

169. Lacking any further evidence, we have used a best estimate of 50% and sensitivity analysis is carried out on this assumption (see **Annex C**).

170. In addition to these costs there is also the cost of processing and collecting the data. Companies which are RLEs (because they keep their own PSC register or are exempt from the requirements) may also need to respond to requests for information from the companies they own. In other cases the company may already have the required information on the RLE or be able to obtain it from Companies House without contacting the company. We do not have data on how many companies will receive requests from other companies for information.

171. Whilst we cannot specifically say how many firms will need to respond to a request, the FAME database indicates that there are around 130,000 UK companies that have 322,000 subsidiaries<sup>86</sup>, i.e. 130,000 ‘parent companies’. Where those subsidiaries are UK companies required to keep a register, these parent companies might need to be approached by their subsidiaries in the process of determining beneficial ownership and thus we use this as a proxy. The adjusted mean from the survey of the costs of responding to requests for information is £30.8 (£10.9 +19.8) per company, including one-off additional costs of external advice. We have assumed the parent will only incur these costs once, rather than for every subsidiary. This is on the basis that: not every subsidiary will approach their parent (as the subsidiary will have the parent’s information on their own share registry); once the information has been gathered once by the parent, the costs of resending the information would be minimal; and we expect the additional cost (for external legal advice) to be incurred only for the first request. Thus the best estimate cost of this element of the proposal is **£4m** (i.e. £30.8 \* 130,000)<sup>87</sup>. Again the range around this number is provided by the statistical adjustment of the mean and is £3m-£9.6m (see **Annex A**).

172. The separate IA on the protection regime considers the costs to a company wanting information on its beneficial owners to be withheld from the public record (e.g. animal testing companies and domestic violence refuges).

173. **The overall monetised one-off costs are therefore estimated to be £458.9m, within a range of £338.8m to £775.3m.**

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<sup>86</sup> With shareholdings of more 25% in a company.

<sup>87</sup> For ongoing changes to beneficial owners’ information, it is expected that the beneficial owners themselves will tell the companies direct, rather than simply telling the parent company who then tells the subsidiaries.

## Ongoing costs

174. Costs on an ongoing basis are also incurred. This analysis is conducted on the basis that companies will be required to check and confirm beneficial ownership information held by Companies House once in every 12 month period (under the new 'check and confirm' system<sup>88</sup>). Companies would be required to update information held in their register of beneficial owners if they know or have reasonable cause to believe (e.g. because a 30% shareholding has been sold) that a change has occurred. Beneficial owners will be required to inform the company of changes as they occur unless they know that the company already has this information (with the company then updating the records they hold as that information is received).
175. We would not expect the names of the beneficial owners to change while they hold the interest in the company (apart from occasionally: potentially on marriage – less than 1% of women per year<sup>89</sup>; and changes by Deed Poll – approximately 40,000 pa). Neither do we expect the date of birth to change or nationality to change frequently. Thus, the updates companies are likely to receive on an ongoing basis are expected to relate only to changes of address (though not country of residence) or transfers of ownership.
176. The number of beneficial owners is currently unknown. Companies House indicate that 1.9m companies have one shareholder and 3.2m have fewer than four shareholders. We estimate that on average companies will have 1.3 shareholders. The calculation is set out below. If we assume that the number of shareholders is a proxy<sup>90</sup> for the number of beneficial owners then on average companies might have 1.3 beneficial owners. However, some companies will not have any beneficial owners and others might have more than three, e.g. where the beneficial owners are acting jointly to own or control the company. Furthermore some individuals will be beneficial owners of more than one company. On this basis it is not possible to estimate reliably the number of beneficial owners, however, to provide an estimate for the cost to business we assume here that there are 1.3 per company. **Annex C** contains sensitivity analysis on this point.

| (a)  | (b)   | (d)           |
|--|---|---------------|
| Number of shareholders in a company                    | % of companies in each category of shareholders' number | BEST ESTIMATE |
| 1  | 56.0%   | 1.0           |
| 2  | 30.3%   | 1.78          |
| 3  | 6.0%  | 1.84          |
| 4  | 3.4%  | 1.61          |
| 5  | 1.3%  | 1.61          |
| 6 - 10   | 1.8%  | 1.63          |
| 11 - 100   | 1.3%  | 1.97          |
| More than 100  | 0.1%  | 1.59          |
| <b>Weighted average number of PSCs in UK companies</b> |   | <b>1.3</b>    |

177. Source: Companies House, FAME and own calculations

<sup>88</sup> Note that this does not mean that the company has to verify the data, merely confirm it accords with its own records.

<sup>89</sup> ONS (2011): *Marriages in England and Wales (provisional)*, The Guardian, 7<sup>th</sup> March 2013

<sup>90</sup> The number of legal shareholders is not synonymous with beneficial owners, however, robust data on the latter is not available.

178. On average the ONS's publication *Social Trends* indicates that people move about every 10 years (probability of 1/10). We assume that this will be the case for a service address also. Pitchbook and Grant Thornton's *Private Equity Exits* reports indicate that on average non-trade equities (in the US) are held for 4.8 years (i.e. would change twice in 10 years – probability of 2/10). Assuming that the UK holding periods are similar to those in the US, a company with 1.3 beneficial owners might have to change the details they hold on **average 0.52 times a year** (i.e. the probability of moving either address (1/10 plus 1/10) + the probability of changing non-trade equities (2/10) for each beneficial owner \* 1.3 owners). In fact 84% of the survey respondents indicated that the details would never change in a year: on this basis the above calculation of 0.52 times a year might be an overestimate. **Annex C** reviews these assumptions in the sensitivity analysis.

179. From the above Table 3, the companies' **annual update of beneficial ownership data and the annual return to Companies House** are estimated to cost **£67m** ( $3.43m * (£13.7 + (0.52 * £11.2))$ ) reflecting the adjusted mean, with a range of **£45m to £123.5m** reflecting high and low estimates based on the statistical treatment of the survey results based on the coefficient of variation and its use in the degree of truncation to arrive at a mean. These in turn are informed by the second survey and focus groups results (see **Annex A**).

180. **The overall Net Present Value of costs expected to be incurred by companies equals £968.8m over a 10 year period<sup>91</sup>. The EANCB is estimated to be £85.9m pa.**

181. The table below sets out the unit costs, the total cost and the EANCB:

|  | Total best cost per company | Total cost   | EANCB         |
|--|-----------------------------|--------------|---------------|
| <b>One-off costs</b>                       |                             |              |               |
| Familiarisation costs                      | £93.5                       | £320.7m      | £28.4m        |
| Identification and collection              | £13.7                       | £47m         | £4.2m         |
| Collation, processing and storage          | £25.4                       | £87.3m       | £7.7m         |
| <b>Sub – total average one-off cost</b>    | <b>£132.6</b>               | <b>£455m</b> | <b>£40.3m</b> |
| Responding to request (only for some RLEs) | £30.8                       | £4m          | £0.4m         |
| <b>Ongoing costs</b>                       |                             |              |               |
| Annually update own records                | £11.2                       | £20.1m pa    | £13.6m        |
| Report to Companies House annually         | £13.7                       | £47m pa      | £31.7m        |
| <b>Sub-total – average ongoing cost</b>    | <b>£24.9</b>                | <b>£67m</b>  | <b>£45.3m</b> |

*Caveats with the survey results*

182. As mentioned above, concerns have been raised around the accuracy and robustness of the original survey results where both one-off and ongoing costs derived were significantly above what was expected at the beginning of the policy development process, and above some previous cost estimates<sup>92</sup> - in particular familiarisation costs.

183. **Annex A** provides detail on these concerns and how results have been adjusted for the purpose of this final IA. The above estimates have taken the analysis in Annex A and updated it to 2014 prices.

<sup>91</sup> 10 years is the expected life of the policy and the NPV uses standard Green Book compliant inflation and discount rates.

<sup>92</sup> For example, the analysis conducted by John Howell & Co. Ltd. (April 2013): *Costs of Beneficial Ownership Declarations*.

### **C3. Individuals**

184. As outlined above, there is currently no information on beneficial owners. Thus it is not possible to estimate the cost to individuals with a high degree of certainty because we do not know how many beneficial owners of UK companies there are; nor do we know how much it might cost them to become familiar with their obligations, to respond to a request for data, or to provide the data proactively.
185. There are broadly in effect two types of beneficial owner – (i) those with a direct interest of more than 25% of shares/voting rights and (ii) those who otherwise exercise control over the company or have a cumulative and/or indirect interest in more than 25% of shares/voting rights (including by acting jointly with others). The former will be required to read and respond to the request for information from the company and update the company with relevant changes to their circumstances. It is likely that the latter will need to inform the company proactively that they are the beneficial owner and update the company when their relevant circumstances change.
186. For beneficial owners who are also directors of the company the familiarisation would be unnecessary (as they are likely to have done this anyway in their role in the company – costed out above in the business section). Also the company will have/will receive (almost all of) the required personal information anyway (apart from information as to how the individual exercises their control over the company) as the director is required to provide it already. Furthermore, for small companies with simple structures the person obligated to gather the data is likely to be the same person obligated to respond and provide updated information, thus the additional individual's costs will be negligible.
187. Where the beneficial owner is not a director some costs are likely to be incurred. There might be familiarisation costs for those that will need to provide their information proactively. These might also require legal advice. For those that receive a request for information there will be costs around understanding what is being asked and why. Some individuals will be beneficial owners of more than one company and thus will not require this for every company. It is possible that, in terms of actually providing the information in the first place and updating it with change of address etc, an email is likely to be a typical low cost action<sup>93</sup>.
188. Where the beneficial owner is also a shareholder, some of the information will already be required to be provided to the company and updated, though not all will (e.g. date of birth and nationality).
189. Some individuals may also incur costs resulting from their loss of anonymity - e.g. those investing in companies which others deem unacceptable – and from applying to Companies House for their information to be protected from public disclosure. These costs are considered in the separate IA on the protection regime.
190. On the basis of the above there is not sufficient information on the likely costs to individuals to present a robust estimate. However, the one-off and ongoing cost of providing information is likely to be low (e.g. an email). The one-off familiarisation cost for those beneficial owners operating jointly to own or control the company and the one-off costs around 'understanding the request' may be more significant.

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<sup>93</sup> The company, when trying to identify its beneficial owners, will need to produce an explanatory letter, and potentially approach a number of companies/individuals across a number of layers of ownership and chase up non-respondents. For the individual having to provide information proactively, apart from the familiarisation, is likely to incur just the cost of producing an email. The two types of activity are not synonymous and hence the costs incurred will be different.

## **Option 2 - Government-led campaign to encourage enhanced transparency of company ownership: Non-regulatory option**

### **Benefits**

191. The benefits of Option 2 are expected to be primarily associated with increased economic activity arising from increased transparency rather than crime reduction, though in the light of the RPC comments, we consider the possible reduction in crime below.

### **B1. Benefits to government, individuals and business of a reduction in illicit activities**

192. Unlike under Option 1, we would not expect to see significant benefits associated with a reduction in illicit activity as the information provided would be merely voluntary.

193. There are non-regulatory techniques for crime prevention and reduction, as outlined in the Home Office's *Serious and Organised Crime Strategy*<sup>94</sup>. For example, education and communications strategies raise awareness of the impacts of serious and organised crime.

194. However, a key element of that strategy relates to: "*prosecuting and disrupting serious and organised crime*". This necessitates a regulatory approach – regulatory requirements to make it more difficult for criminals to operate and regulatory sanctions to allow prosecution and disrupt criminal activity (e.g. by imprisoning offenders, thereby preventing further criminal activity). In the context of corporate transparency, law enforcement agencies have endorsed the importance of a regulatory approach - highlighting the potential to deter and disrupt criminal activity.

195. We therefore anticipate that a non-regulatory approach would not significantly contribute to reduced levels of crime as companies engaged in criminal activity would simply opt not to disclose this information. Although law enforcement agencies would continue to use existing mechanisms to obtain beneficial ownership information in such cases, Option 2 would not assist them in so doing. And even if enforcement agencies were provided with additional resource to carry out such investigations, this does not address the underlying problem of corporate opacity. A necessary corollary of a non-regulatory approach might therefore be a continued need for increased levels of public sector spending. But this still might not ultimately deliver any more successful outcomes in terms of the identification and prosecution of the individuals really responsible for the crime.

196. It is possible that enhanced transparency – albeit voluntary - may ultimately deter some individuals who would otherwise have chosen to conduct illicit activity through incorporating a company in the UK. However, it is not possible to estimate this impact – particularly as it would likely be contingent, at least in part, on the action other jurisdictions take in this sphere (i.e. whether they do more or less than the UK). Of greater likely impact would be the increased awareness/vigilance of the misuse of companies as this might lead to some reduction in crime.

197. If other jurisdictions do perceive that UK action taken is weak, they may be less willing to collaborate with the UK in terms of cross-border investigations. It is not possible to quantify the reduction in potential benefits to the UK under Option 2 compared to Option 1 as a result of this. However, we might anticipate that it would reduce the benefits to be derived from a collective and collaborative international approach to addressing the misuse of companies – meaning that UK

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<sup>94</sup> Home Office (2013): *Serious and Organised Crime Strategy*

citizens and enforcement agencies would continue to be impacted by crime conducted by overseas companies in the UK.

## **B2. Benefits to companies and individuals from corporate transparency supporting the business environment**

198. As outlined under Option 1, greater transparency of company beneficial ownership will make it easier for external parties to determine the individuals who own and control the company and for shareholders to hold the company to account. This could be expected to contribute to enhanced trust in the business environment and potentially facilitating economic growth.
199. A non-regulatory approach may contribute towards this objective. There is, for example, evidence as to the positive impact that non-regulatory measures, based on behavioural science, can have on instances of fraud, error and debt<sup>95</sup>. We might expect that companies would be incentivised to comply based on their competitors adopting a more transparent approach; and that ultimately, those companies that do not comply might be those that are more likely to have something to hide. In such cases, external parties might become less likely to engage with the company – putting those companies at a competitive disadvantage and making it increasingly difficult for them to do business.
200. However, under this voluntary approach, we would expect the benefits of enhanced transparency to be generally less widespread than under a mandatory approach (i.e. Option 1). This is because, as addressed in the ‘rationale for intervention’ section, even though information about the commercial advantages of corporate transparency exists, companies may be unaware of this or under-estimate the benefits (relative to their assessment of the costs involved). Just a voluntary campaign seems unlikely to be the most effective way to ensure that the benefits of enhanced corporate transparency are universally realised.
201. Finally, under a non-regulatory approach the UK will not meet its G8 commitments and will likely not be compliant with FATF standards. This may impact the UK’s reputation as a clean and trusted place to do business and invest, which could have an adverse impact on economic activity.

## **Costs**

### **Corporate entities in scope**

202. The entities in scope of Option 2 could potentially be wider than under Option 1 as companies that we would exempt under a mandatory approach might choose to provide information under a voluntary approach. However, for the purpose of this analysis we assume that the number of entities in scope is the same.

### **C1. Public sector costs**

203. Under a voluntary disclosure approach, Companies House would incur much the same IT costs as under Option 1 because they do not currently capture any of this data. They would therefore need to amend their existing systems to capture the voluntarily provided beneficial ownership information and make it available. Companies might have a choice whether to provide this information, for example, as part of the ‘check and confirm’ process or by a separate notice.

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<sup>95</sup> Cabinet Office (February 2012): *Applying behavioural insights to reduce fraud, error and debt*: [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/60539/BIT\\_FraudErrorDebt\\_accessible.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/60539/BIT_FraudErrorDebt_accessible.pdf)

It is assumed that there would be no ongoing costs as there would not be 'at risk' beneficial owners identified; and therefore no closed beneficial ownership register to administer. Thus the one-off costs would be **£92.4k** (with a range of £72k to £112k).

204. Companies House operates as a trading fund and would need to recover the costs of these services. For statutory activities they do this by charging fees. Companies House have noted that, based on the current level of information, they do not anticipate higher fees to companies as a result of this proposal.

205. There would be further costs to the public sector associated with promoting the voluntary approach, for example, communications campaigns and business engagement. It is difficult to estimate the cost here given the range of possible campaigns; however, Companies House undertook a campaign to publicise the new Companies Act 2006 and its introduction in 2009, which cost Companies House £800,000. The 2009 changes were broader in scope than the current package, including accounts and audit for instance, though they related to a smaller number of companies than are on the register at present<sup>96</sup>. We have assumed a similar cost might be incurred in this policy proposal (i.e. £894,000 uprated to 2014 costs).

## **C2. Private business and individual costs**

206. Option 2 would provide no new regulatory costs to business or individuals. Companies and individuals deciding to disclose the information would incur some costs, but this would happen on a voluntary basis and therefore it is expected that this will only happen when the benefits to the company or individual outweigh the costs.

## **G. Rationale and evidence that justify the level of analysis used in the Impact Assessment (proportionality approach)**

207. We believe that the analytical approach taken in this IA is proportionate. The table below sets out the data we would have required in order to have obtained a full monetised analysis; and why we were not able to include this.

208. The *Transparency and Trust* package was started with initially very limited evidence, primarily because the criminal nature of the problem we are targeting makes data collection challenging. Moreover, the breadth of the areas addressed in the package has not been studied in detail before.

209. Prior to the launch of the *Transparency and Trust* paper, and both during and after the G8 process, we carried out a number of discussions with industry, NGOs and regulated bodies. During the consultation on the *Transparency and Trust* paper, which fed into the evidence base underlying this IA, we:

- consulted with the Economic and Social Research Council;
- consulted with Companies House;
- undertook a full literature review;
- opened an online survey accessible by the general public;
- consulted with business, regulated entities and law enforcement agencies in a series of focus groups and one-to-ones; and
- commissioned a representative company survey through IFF Research (see **Annex A**).

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96 Based on the Companies House Annual Report of 2012/13:  
[http://www.companieshouse.gov.uk/about/pdf/companiesRegActivities2012\\_2013.pdf](http://www.companieshouse.gov.uk/about/pdf/companiesRegActivities2012_2013.pdf)

210. After the publication of the *Transparency and Trust* discussion paper, we undertook a further series of focus groups and consultation as well as a follow-up survey which revisited some of the respondents to the first survey to understand better the initial responses we received. The evidence gathered from stakeholders has continued to play a key role in our ability to determine which policy options will have the desired effect, without unintended consequences or imposing unnecessary burdens on business.

211. For the purposes of the final and this Enactment IA, in particular we built on the existing evidence base with the following:

- an extension to the company survey, consisting of largely qualitative questions;
- a series of focus groups consisting of businesses and trade associations; and
- further discussions with law enforcement agencies and tax authorities.

For the enactment IA we also:

- updated the cost estimates to 2014;
- used 2014 data on the number of companies in scope;
- refined the estimate of the number of PSCs and
- delayed the start of the ongoing costs until 2016 following policy proposal changes.

The company survey was used to inform the way we treated the data collected in the original survey through a series of in-depth interviews with respondents (the methodology and its implications are explained fully in **Annex A**). The focus groups were used largely to validate the estimates we produced in the consultation IA. Discussions with enforcement authorities provided further evidence on the scale of the problem and the potential benefits of reform.

212. In terms of examining the benefits of corporate transparency for the business environment and those operating within it, Companies House and FAME data first enabled us to identify the population of companies in scope. Once we had conducted a detailed literature review, which made good use of the expert knowledge within the Economic and Social Research Council, we were then able to identify the associated benefits of the *Transparency and Trust* package, including evidence of the important relationship between trust and economic growth. In general, however, the relevant economic literature is in its infancy, which made it unfeasible to monetise the benefits of corporate transparency on the business environment.

213. As explained above, the benefits arising from the potential reduction in crime could not be fully monetised because of the way in which law enforcement agencies collect their data. Given the huge scale of any corporate investigation and the myriad of evidence, there is no systematic distillation of crime data such that we can interrogate the impact of a single factor, such as corporate opacity or specifically opaque beneficial ownership arrangements. We have offered an indication of the scale of the potential benefits but without estimates of the deterrent effect on crime or the increased efficiency and efficacy of investigations and prosecutions resulting from *Transparency and Trust* measures, we could go no further to monetise them.

214. The evidence we have gathered to inform cost estimates in this IA is drawn in large part from a company survey we commissioned through IFF Research. The study was the first of its kind, analysing in detail the costs associated with enhancing corporate transparency. Despite the lengths we went to in order to gather evidence there was still a need for processing of the data to obtain estimates for use in this IA. However, to gain a better grasp of how to treat these data we

undertook a follow-up survey, which helped us identify where it was reasonable to truncate the data and it largely validated the estimates and approach we used in the consultation IA (see **Annex A**).

215. We also held a number of business focus groups, which discussed the likely costs of the proposed reforms related to beneficial ownership, corporate directors and front directors<sup>97</sup>. Largely the companies present agreed with our cost estimates, particularly for small companies (though some said that for small companies the costs might be lower). However, many companies did comment that compliance could cost considerably more for large and more complex companies if legal and accountancy costs were required. Nonetheless, given that our estimates were weighted by the population, which is 98% small companies, this would bring the estimated costs down so the focus groups broadly validated the figures we presented to them.

216. We are satisfied that the evidence presented here represents the most comprehensive and robust assessment available for an Enactment IA within the constraints of proportionality with respect to both cost and time.

**Table 4: Impact Assessment proportionality analysis**

| Cost / Benefit   | Evidence / Data Gap   | Use of evidence or why this evidence has not been included in the IA  |
|--|---|---|
| <b>Benefits</b>  |   |   |
| Benefits from reduction in crime                             | (i) Reduction in crime rate<br><br>(ii) Unit cost of money laundering | <ul style="list-style-type: none"> <li>• Lack of evidence in the academic literature.</li> <li>• During the consultation, none of the respondents were able to provide quantified evidence in this area. This was often due to data not being recorded in such a form which is easily accessible or usable for economic appraisal purposes.</li> <li>• Paucity of evidence on money laundering is common for all financial crime. As noted by FATF: <i>“it is absolutely impossible to produce a reliable estimate of the amount of money laundered”</i><sup>98</sup>.</li> <li>• Evidence from the Home Office does not fully disaggregate by type of fraud and only gives a high level aggregate figure.</li> </ul> |
| Reduced costs for Law Enforcement and Tax Authorities (LEAs) | (i) Monetised cost impact   | <ul style="list-style-type: none"> <li>• During the consultation, none of the LEA respondents were able to provide quantified evidence on the total reduction in crime or indeed the cost impact. This was often due to data not being recorded in such a form which is easily accessible or usable for economic appraisal purposes.</li> </ul>   |
| Corporate transparency and accountability                    | (i) Measureable growth impact   | <ul style="list-style-type: none"> <li>• Lack of evidence in the literature. There is a clear link between growth and trust but the literature is not yet developed enough to attribute changes in corporate governance to trust and ultimately growth.</li> </ul>  |
| <b>Costs</b>   |   |   |
| Familiarisation and set up costs                             | (i) Number of staff and time taken to familiarise                     | <ul style="list-style-type: none"> <li>• Adjusted means from the company survey with IFF Research included.</li> </ul>  |

<sup>97</sup> Please see Annex B for the attendance list.

<sup>98</sup> Financial Action Task Force: [Money Laundering FAQ](#)

|                           |   |  |
|---------------------------|---|--|
|                           | with the proposal<br><br>(ii) Companies House and IT development and staff costs  | • Estimate from Companies House included.  |
| Compliance costs          | (i) Separate cost estimates for each of the steps involved in identifying, collating and reporting beneficial ownership data<br><br>(ii) Compliance costs to individuals  | • Adjusted means from company survey with IFF Research included.<br><br>• Unknown number of beneficial owners or costs they are likely to incur.   |
| Net impact to the economy | (i) Legitimate investment being diverted from the UK due to the increased exposure that investors might face<br><br>(ii) Reduced information asymmetry between principals and agents leading to more optimal investment and mutually beneficial trades taking place and an increase in the UK's integrity | • Very difficult to predict the level of investment diverted or increased due to mutually beneficial business taking place and to associate this investment with the disclosure of beneficial ownership. |

## H. Risks and assumptions

217. As noted above, we have not been able to gather evidence on the number of beneficial owners and as such have made an assumption about this in relation to the costs to companies in updating their information. In addition to this lack of evidence on the number of beneficial owners, we have not been able to calculate the cost to potential individuals affected. **Annex C** sets out some possible ranges but these are merely indicative. There is a risk that a large number of individuals might be affected, however a priori, the cost per individual is likely to be low (with some spending time on one-off familiarisation/understanding of the requirements and more sending (emailing) necessary information).

218. Following standard IA methodology, we have assumed 100% compliance. There is, however, a risk of non-compliance resulting in an impact on the criminal justice system, and potential costs to companies and individuals as a result of the imposition of restrictions on shares and rights. The potential impact on the criminal justice system is set out in the Justice Impact Test, as detailed below.

219. Related to the previous point, there is a risk that benefits from a reduction in criminal activity will not be significant, or that individuals willing to undertake criminal activity might find other ways to hide their interest or involvement in a company. This is not anticipated in this IA, but it might have an impact on the level of benefits achieved by the proposals. This risk is likely

to be mitigated by robust action being taken across the *Transparency and Trust* package, as envisaged by the suite of proposals. Moreover, crime estimates were only available for England and Wales so we scaled them up to cover the whole of the UK. This enabled us to calculate the volume of crime committed and the associated costs across the whole of the UK.

220. We are continuing to work closely with law enforcement and tax authorities as we implement the registry to ensure that the information contained supports timely and effective investigations; and that robust enforcement procedures are in place to tackle instances of non-compliance. As an example of this, we have set up a Law Enforcement User Group, jointly chaired by Companies House and the NCA.

221. There may be a risk in terms of individuals opting to use non-UK companies (rather than UK companies) to facilitate crime, which may still have an impact in the UK. However, this risk is being mitigated by ongoing UK action in the G7, G20, FATF and in Europe to encourage other jurisdictions to take similar action.

222. Some respondents to the discussion paper raised concerns around the burden on business and impacts on the attractiveness of the UK as a place to invest; the ability of Government to enforce effectively the new requirements; whether information obtained would be verified for accuracy and how proposals would impact on individuals' privacy rights. We have sought to address these concerns through policy development where appropriate and continued engagement with stakeholders. For example, the development of an exemptions framework from public disclosure for individuals at risk should mitigate concerns around privacy and well-being impacts.

223. The theory and evidence suggests that the *Transparency and Trust* package could as a whole have benefits with respect to growth because of its impact on trust. However, our ability to disaggregate to the level of individual component parts of the package, specifically here opacity of company beneficial ownership, is limited. On the assumption that the *Transparency and Trust* package will have an impact on trust, the evidence suggests that the package as a whole will have a non-negligible impact on economic growth. We have also made assumptions in adopting the approach of Beugelsdijk (2006) to the relationship between trust and growth. The mechanism through which increasing transparency is considered to affect growth is the enhancement of trust in the business environment. However, the majority of the academic literature related to trust and growth looks generally at societal level trust. Beugelsdijk (2006) considers 'trust' a good proxy for trust in the business environment because trust according to the World Values Survey measure is highly correlated with the effectiveness of institutions.

224. In relation to the cost estimates we have used, there are a series of underlying assumptions:

- we have assumed that the same number of companies will be in scope of non-regulatory approaches under Option 2 as under Option 1;
- the weighted and adjusted mean from the IFF research has been applied to 3.43m UK active and dormant companies<sup>99</sup>; and
- our costs estimates are largely based on figures derived from an externally contracted representative survey of almost 600 companies, undertaken by IFF research, and enhanced by a follow-up survey and focus group (see **Annex A**).

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<sup>99</sup> Company population estimates were extracted from the FAME database (Bureau van Dijk Electronic Publishing, 2013)

225. We have also made a number of assumptions in relation to the policy, as will be set out in secondary legislation. We will refine these assumptions and costs, if required, as the secondary legislation is finalised:

- we assume we will be able to exempt companies listed on prescribed markets from the requirement to maintain a PSC register<sup>100</sup>;
- we assume we will only exempt companies listed on EEA regulated markets from keeping a PSC register; and that only companies that keep a PSC register or are listed on EEA regulated markets will be considered as RLEs;
- we assume that costs to corporations soles, governments and certain other public bodies that are treated like individuals for the purpose of the PSC register will be the same as for individuals; and
- we assume that where a company has been unable to identify its PSCs, or has no PSCs, the costs it incurs in annotating and updating its PSC register will be broadly the same as costs incurred by companies who do have information on individuals to record.

226. During the consultation the issue arose of legitimate investment being diverted from the UK due to the increased exposure that investors might face. There is a risk that we have not accurately accounted for this potential impact on overseas investment in the UK and UK competitiveness arising from the package and its perception, particularly since the UK will likely be a 'first-mover.'

227. The OECD has noted as a general principle that: *“excessive compliance costs, shortening the disclosure period and information overload problems, discourage (foreign) investments in listed companies and negatively affect shareholder engagement<sup>101</sup>”*. They also note that: *“costs of a disproportionate and stringent disclosure regime makes it more difficult for emerging growth companies to attract public investors, these companies will be induced to rethink their stock market aspirations, thereby hampering economic growth and job creation<sup>102</sup>.”* These issues might well be relevant for non-listed companies also.

228. Overall, the risk of accounting for this effect with respect to the *Transparency and Trust* package must be contextualised with respect to the significant influence of many other factors on the UK's ability to attract investment. The UK is the 9<sup>th</sup> most competitive economy in the world (World Economic Forum (WEF) 2014/2015). The WEF highlights the UK's strengths in technology, labour market efficiency, infrastructure, business sophistication and market size, which will by no means be eroded by greater corporate transparency.

229. The main drivers of Foreign Direct Investment would not be likely to be adversely affected by the *Transparency and Trust* package, and indeed could be positively affected. Generally, strong economic fundamentals are thought to be the most important determinants (OECD 2002). In most cases, these include comparative advantage, political and macroeconomic stability, market size, real income levels, the skills base and the quality of the infrastructure (with anonymity of ownership not explicitly referenced as an attractive factor).

230. Moreover, in considering these issues, we should weigh any potential deterrent of investment arising from transparency against the reduced information asymmetry between

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<sup>100</sup> This assumption is subject to the outcome on the EU's Fourth Money Laundering Directive, which may require companies listed on prescribed markets to report beneficial ownership information to a central register.

<sup>101</sup> Vermeulen, E. (2013), *Beneficial Ownership and Control: A Comparative Study - Disclosure, Information and Enforcement*, OECD Corporate Governance Working Papers, No. 7.

<sup>102</sup> Kamar, E., P. Karaca-Mandic and E .L. Talley (2008), *Going-Private Decisions and the Sarbanes-Oxley Act of 2002: A Cross-Country Analysis*, USC Center in Law, Economics & Organization Research Paper No. C06-5, USC Law Legal Studies Paper No. 06-10; UC Berkeley Public Law Research Paper No. 901769

principals and agents leading to more optimal investment and increasing mutually beneficial business, and a potential increase in the UK's integrity and international reputation as a place to do business and invest. It is not possible, however, to place a monetary value on either any lost investment or any possible increase. We do note, however, that companies with foreign ownership did not, in the surveyed sample, appear to cite higher costs than other companies for familiarisation or compliance with proposals in the *Transparency and Trust* package.

231. In policy terms, we will mitigate the risk of an adverse impact on UK investment by promoting this measure as one of many positive features of the business environment in the UK and continuing to encourage action from other jurisdictions. This will include an active approach in the G7, G20, FATF, and in Europe, and wider promotion of the importance of corporate transparency (e.g. through international best practice guidance and standards). This package of policies places the UK at the very forefront of the international transparency agenda. This has already resulted – and will continue to be a key factor – in the UK shaping the international debate and driving international change.

## **I. Direct costs and benefits to business calculations (following OITO methodology)**

232. The measures in this IA implement international commitments the UK made at the 2013 G8 Summit.

233. We understand that the Better Regulation Framework Manual at time of writing sets out that measures to implement international commitments and obligations are out of scope of One In Two Out (OITO) but, where there is a clearly prescribed minimum requirement or standard and the UK is implementing in a way that goes beyond this, that the additional burden over and above the minimum, would be treated as in scope.

234. The G7 is an international forum that brings together seven global leaders (Canada, France, Germany, Italy, Japan, UK and USA, alongside the EU) to address international issues and tackle the most pressing global challenges. The UK held the 2013 Presidency, and the Prime Minister hosted the annual Summit at Lough Erne in June of that year, where the agreements and commitments made by leaders were set out in a formal Communiqué and documentation.

235. At the 2013 Summit the then G8 members agreed a set of Action Plan Principles to prevent the misuse of companies and legal arrangements, and to publish Action Plans setting out the concrete action they would take to implement those Principles. All G7 members have published an Action Plan and are moving ahead with implementation.

236. The *Transparency and Trust* measures are drawn from the UK's Action Plan commitments drawn from the Action Plan Principles. Strong action to deliver reform that fully meets these commitments is now the minimum the UK must deliver to meet its international obligations.

237. The 2013 G8 obligations are binding in that the Government has made a public commitment to implement them; they are politically binding but not legally (or otherwise) binding. The UK and our G7 partners were held to account through G20 Leaders' commitments on beneficial ownership transparency at the November 2014 Brisbane Summit, including:

- Setting out in writing next steps to implement the G20 High Level Principles on beneficial ownership. This commitment reflects the 2013 G20 St Petersburg commitment to lead by

example in implementing the Financial Action Task Force (FATF) standards on beneficial ownership transparency.

- Updating on progress under the 2015-16 G20 Anti-Corruption Action Plan, including an annual progress report to Leaders.

238. The G20 Anti-Corruption Working Group will take forward these commitments over the next two years. On 4-5 March 2015, G20 members agreed to submit written implementation plans before the June Working Group meeting, for consideration by G20 Sherpas in September, and submission to Leaders in November.

239. Failure to deliver against the 2013 commitments would have significant impact on the UK's international standing within the G7 and more broadly, and would create substantial political embarrassment for the Government. However, the forum of the G7 does not set any minimum legal or other standard for implementation, so we judge these measures to be out of scope for OITO.

240. The UK must now act to deliver against its commitments, consistent with and directly relating to the commitments made in the 2013 G8 documentation. As mentioned, every G7 country has committed to an Action Plan, which sets out how they individually plan to take forward a set of Action Plan Principles agreed by all the G7 Leaders, and indeed reflecting the Communiqué.

241. We consider that the measures the UK will take forward are consistent with and directly in response to the commitments the UK has made. The 2013 G8 Action Plan Principles are set out below (though only the relevant provisions have been included). Alongside this the UK has set out a UK Action Plan (also below) to deliver the G8 Action Plan Principles. The UK's delivery of the G8 commitments will be judged against both of these plans.

242. The UK intends to:

- create and maintain a publicly accessible central registry of company beneficial ownership information; introduce sanctions to individuals and companies that fail to comply; and ensure that this information is readily available to national and international enforcement authorities. This is required to deliver points 1, 2, 7 & 8 of the G8 Action Plan Principles and points 2, 3 & 9 of the UK Action Plan;
- remove the right to issue bearer shares and implement transitional arrangements to remove bearer shares from circulation. This is required to deliver point 5 and support the full implementation of point 1 of the G8 Action Plan Principles and points 2 & 7 of the UK Action Plan; and
- restrict the use of opaque arrangements involving company directors. This is required to deliver point 5 and support the full implementation of point 1 of the G8 Action Plan Principles and point 7 of the UK Action Plan.

243. The UK is leading the developments in this area in order to persuade international adoption of these principles and methods. This is required to deliver point 8 of the G8 Action Plan Principles and point 8 & 9 of the UK Action Plan.

244. Points 3, 4 & 6 of the G8 Action Plan Principles and points 1, 4, 5 & 6 of the UK Action Plan are not directly related to corporate transparency and trust and are therefore being taken forward by other parts of Government, most notably HMT.

245. We consider the measures set out here are the minimum measures necessary to comply with the commitments set out in the G8 Action Plan Principles and UK Action Plan. These measures as a package are required to deliver all the G8 and UK Action Plan requirements on corporate transparency and trust.

246. The measures will be implemented in a way to minimise the additional costs to business. Extensive consultation with business and other interested parties has been conducted to ensure that the measures are implemented in the most effective way, without placing unnecessary additional costs on business.

247. We have carefully considered better regulation principles in developing these measures to implement the UK's international commitments, in accordance with good practice and the Better Regulation Framework Manual. This has included consideration of alternatives to regulation and attempts to minimise the costs to business while ensuring the efficacy of the policy interventions. The evidence underpinning these attempts to evaluate and minimise the costs to business is covered elsewhere in this IA.

248. Although, we consider that these measures are not within the scope of OITO, we have, in the interests of good practice, calculated that the preferred option for the beneficial ownership proposal has a net direct cost to business per year of £85.9m.

#### **A. G8 Action Plan Principles to prevent the misuse of companies and legal arrangements**

*Subject to our different constitutional circumstances, and understanding that a one-size-fits all approach may not be the most effective, the G8 endorses the following core principles that are fundamental to the transparency of ownership and control of companies and legal arrangements. These core principles, consistent with the FATF standards, are essential to ensure the integrity of beneficial ownership and basic company information, the timely access to such information by law enforcement for investigative purposes, as well as, where appropriate, the legitimate commercial interests of the private sector.*

*The G8 also commits to publish national Action Plans based on these principles that set out the concrete action each of us will take to counter money laundering and tax evasion. To ensure G8 members are held to account for their commitments, the G8 agrees to a process of self reporting through a public update on the progress made against individual action plans and to inform the Financial Action Task Force.*

*1. Companies should know who owns and controls them and their beneficial ownership and basic information should be adequate, accurate, and current. As such, companies should be required to obtain and hold their beneficial ownership and basic information, and ensure documentation of this information is accurate.*

*2. Beneficial ownership information on companies should be accessible onshore to law enforcement, tax administrations and other relevant authorities including, as appropriate, financial intelligence units. This could be achieved through central registries of company beneficial ownership and basic information at national or state level. Countries should consider measures to facilitate access to company beneficial ownership information by financial institutions and other regulated businesses. Some basic company information should be publicly accessible.*

*[...]*

*5. The misuse of financial instruments and of certain shareholding structures which may obstruct transparency, such as bearer shares and nominee shareholders and directors, should be prevented.*

[...]

7. *Effective, proportionate and dissuasive sanctions should be available for companies, financial institutions and other regulated businesses that do not comply with their respective obligations, including those regarding customer due diligence. These sanctions should be robustly enforced.*

8. *National authorities should cooperate effectively domestically and across borders to combat the abuse of companies and legal arrangements for illicit activity. Countries should ensure that their relevant authorities can rapidly, constructively, and effectively provide basic company and beneficial ownership information upon request from foreign counterparts.*

## **B. UK Action Plan to prevent the misuse of companies and legal arrangements**

*The UK is committed to fully implementing the revised Financial Action Task Force standards in order to improve the transparency of the ownership and control of companies and legal arrangements. This is a matter of good corporate governance as well as a means to tackle a wide range of illicit activity. The UK is committed to taking the following actions to do this.*

[...]

2. *Ensure the Companies Act 2006 and UK Money Laundering Regulations oblige companies to know who owns and controls them, by requiring that companies obtain and hold adequate, accurate and current information on their beneficial ownership.*

3. *Amend the Companies Act 2006 to require that this information is accurate and readily available to the authorities through a central registry of information on companies' beneficial ownership, maintained by Companies House. Consult on whether information in the registry should be publicly accessible.*

[...]

7. *Review of corporate transparency, including bearer shares and nominee directors, by the Department for Business, Innovation and Skills. This will start with the publication of a pre-consultation paper before September 2013.*

8. *Support the Overseas Territories and Crown Dependencies to publish Action Plans setting out the concrete steps, where needed, to fully implement the Financial Action Task Force Standards.*

9. *Improve international cooperation including the timely and effective exchange of basic and beneficial ownership information.*

10. *Implementation of the measures will be through, and at the same time as, transposition of the 4th EU Money Laundering Directive and UK Money Laundering Regulations, changes to the Companies Act 2006, as well as through other relevant bilateral and multilateral agreements<sup>103</sup>*

## **J. Wider impacts**

### **Statutory equality duties**

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<sup>103</sup> On the basis that company law is devolved in Northern Ireland, we will work together with the Northern Ireland Executive to take this forward.

249. This policy will primarily impact UK companies (understood here as the individuals responsible for ensuring a company's compliance with the new requirements) and the beneficial owners of those companies. A wider population may derive benefits from the policy as a result of reduced crime or an improved business environment.

250. We have considered whether any of the following groups might be adversely or positively impacted by this policy in different ways:

- Race Equality;
- Gender;
- Disability;
- Age;
- Marriage and civil partnership;
- Religion and Belief;
- Sexual Orientation;
- Gender Reassignment; and
- Pregnancy and Maternity.

251. We do not anticipate that this would be the case and therefore do not anticipate any equalities impact. We have also conducted and published a separate Equalities Impact Screening Exercise which indicated that the conduct of a full Equalities Impact Assessment was not required<sup>104</sup>.

### Economic impacts

#### *Competition impact test*

252. We have considered the potential competition impact of the proposed reforms but given the substantial coverage of companies this did not identify any particular issues with this policy change.

253. With regard to the impact on smaller entrants relative to large existing companies, the estimated mean costs will not disproportionately fall on small companies.

#### *Small and micro business assessment*

254. The annual turnover and balance sheet thresholds, which along with number of employees determine whether a company is small for accounting purposes, are in the process of increasing. A company is currently classed as small if it satisfies two out of three criteria respectively covering turnover, balance sheet total and number of employees. The maximum turnover figure is increasing from £6.5m to £10.2m. The total balance sheet threshold is increasing from £3.26m to £5.1m. Note, however, that the threshold for the number of employees (of less than or equal to 50 employees) will not change (this is the key criterion for the SaMBA). The thresholds change occasionally over time. This IA uses the earlier thresholds to estimate the impact on the number of small and micro companies to maintain consistency with the Transparency and Trust Final IA and because the new thresholds are not yet fully in force; the employee threshold stays the same; and the turnover, asset and employee numbers available relate to 2014 or earlier. Due to the old data, we cannot accurately determine the impact of the new thresholds on the number of small and micro companies but we estimate a percentage increase in the number of small companies of only 0.03% due to the small number of current medium sized companies that are likely to be reclassified. In this respect the total

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<sup>104</sup> BIS (April 2014): *Transparency and Trust: enhancing the transparency of UK company ownership and increasing trust in UK business: equality impact assessments* <https://www.gov.uk/government/publications/company-ownership-transparency-and-trust-impact-assessments>

estimates for costs in this IA - which cover small, medium and large companies - could be slight overestimates.

255. As set out above, the two main objectives of the *Transparency and Trust* package are to reduce crime, and improve the business environment so as to facilitate economic growth. The assessment is that excluding small and micro businesses from the policy package could risk a significant impact on the ability of the package to reduce crime, and exclude small and micro businesses from the benefits that can be derived from increased transparency.
256. This policy will apply to UK incorporated companies and LLPs, and will require these entities to disclose beneficial ownership information to a central registry. There is a default assumption that small and micro businesses<sup>105</sup> should be exempted from new regulatory measures. However, assessment reveals that such an exemption is not viable in this policy context, and not compatible with achieving a large part of the intended benefits of this measure.
257. It has been widely identified that 'shell' companies are often the vehicle of choice for money-laundering and other crimes<sup>106</sup>. A 2012 study defines a shell company thus: "*In contrast to operating or trading companies that have employees who make a product or provide a service [...] shell companies are little more than this legal identity, and hence the "shell" moniker*"<sup>107</sup>. By this very definition, we believe that the majority of shell companies would be classified as small or micro businesses. Law enforcement have strongly confirmed to us that this is the case, and that excluding small and micro businesses from scope would be a significant risk and ultimately counterproductive. Internationally, the US G8 Action Plan considers targeting small and micro business for selective **inclusion** in scope of company beneficial ownership transparency, and considering larger businesses for exemption where they meet "*certain employee or revenue requirements.*"
258. Allowing any exemptions targeted at small and micro business could therefore have a negative impact on the primary derived benefit from this policy, in terms of a failure to tackle or deter any illicit activity undertaken through companies currently on the register. Exempting small and micro businesses from the requirement would create a significant loophole for those seeking to exploit the company structure for illicit activity in future. In turn, this could damage the reputation of UK small and micro businesses relative to their larger and/or international competitors.
259. Moreover, any exemption for small companies would limit the positive impact on the wider building of trust in the business environment - and therefore economic growth. Were they to be exempted from these transparency requirements, information asymmetries could persist and law-abiding businesses might find themselves, for instance, less able to attract private investment or debt finance.
260. We have undertaken analysis of the costs for small companies using the data obtained in the IFF Research company survey, weighted by the same methodology as for the overall figures. These estimates only use the 'best' estimate for the preferred option and for each cost estimate we have truncated the distribution at the same point as for the estimates for all companies. The methodology is described in full in **Annex A**.

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105 For the purposes of this assessment, the parameter used to define small businesses is up to 49 full-time employees, and for micro businesses up to 10 employees.

106 Findley, Nielson and Sharman (2012): *Global Shell Games: Testing Money Launderers' and Terrorist Financiers' Access to Shell Companies* <http://www.griffith.edu.au/business-government/centre-governance-public-policy/research-publications/?a=454625>

107 *ibid*

261. The survey data suggest that the average costs for the 3.38m small companies will be substantially lower than for large companies, as set out in the table below.

**Table 5: Average costs for small companies<sup>108</sup>**

| Costs*                       | Small company mean | Large company mean |
|------------------------------|--------------------|--------------------|
| Transition costs per company | £94                | £3,127             |
| Ongoing costs per company    | £61                | £1,195             |

262. Small firms, despite their predominance in the population at over 98%, account for only 64% of the one-off costs and 80% of the ongoing costs.

263. Nevertheless, from the outset we have considered measures to minimise burdens to small and micro businesses, including allowing sufficient time for companies to familiarise themselves with these changes and providing sufficient guidance on the policy. We will take steps to identify and fulfil any particular guidance requirements of small and micro businesses in order to support them, in particular, in understanding the new requirements. We have not identified any other potential unintended effects to these businesses, and assuming 100% compliance, the impact will not disproportionately impact small and micro businesses.

264. With these points in mind, our assessment against the advised considerations is as follows:

| Factor  | Consideration  |
|---|--|
| <i>Full exemption</i>                           | We do not believe a full exemption is compatible with achieving crime reduction benefits; and would reduce benefits derived from a more open and trusted business environment.   |
| <i>Partial exemption</i>                        | We have not identified any specific requirements within the proposals from which we would be able to exempt small and micro businesses. We do not believe any exemption is compatible with achieving a large part of the intended benefits.  |
| <i>Extended transition period</i>               | We do not believe a separate transition period for small and micro companies is compatible with achieving a large part of the intended benefits. We will ensure that a sufficient transition period is in place for <u>all</u> companies and that there is sufficient time for a well-supported process of familiarisation and transition.                         |
| <i>Temporary exemption</i>                      | We do not believe a temporary exemption for small and micro companies is compatible with achieving crime reduction benefits, not least because anonymous shell companies are the specific focus of our proposals. Exempting them could therefore provide a means for illicit activity to continue unnecessarily.   |
| <i>Varying requirements by type and/or size</i> | We have not identified a specific type of business that is more or less likely to engage in illicit activity; indeed many of the companies in question will not conduct any business activity. As small, anonymous shell companies are in part the focus of our proposals it would not be appropriate to vary the requirements for small and micro companies. This |

<sup>108</sup> Annex A analysis updated to 2014 prices

|   |   |
|---|---|
| <i>of business</i>  | would not be compatible with achieving a large part of our intended benefits. Where possible, we have sought to use existing precedents which apply to all UK companies.  |
| <i>Direct financial aid for smaller businesses</i>  | We do not believe that the costs of complying with this policy change per company will warrant direct financial aid.  |
| <i>Opt-in and voluntary solutions</i>   | We have considered and discounted non-regulatory approaches in our IA, given the nature of the criminal activity we seek to address. For the same reasons as set out under Option 2 generally, we do not believe that small and micro companies' engaging voluntarily would be a viable solution or compatible with achieving a large part of our intended benefits.  |
| <i>Specific information campaigns or user guides, training and dedicated support for smaller businesses</i> | <p>There might well be a case for tailored information campaigns and user guides, though training is not likely to be required. We will work on meeting the needs of the small and micro business user as we develop overall guidance to support the introduction of the package, and as part of the Government's wider communications campaign.</p> <p>We will implement proposals with a view to our statutory review within three years of the requirement to file information at Companies House coming into force. We considered the value of sun-setting clauses but ultimately viewed the policy proposals as making longstanding improvements to the UK legal framework. While review and optimisation should continue following implementation, the changes we make must be seen to be enduring in order to deliver the benefits from a reduction in crime and from improvements to the business environment, and particularly in order to meet the UK's international obligations to deliver change in these areas.</p> |

Wider environmental and social impacts

| Factor                         | Consideration  |
|--------------------------------|--|
| Environmental impacts          | Our analysis suggests that this policy will not have any adverse impact on the environment – the changes relate purely to gathering, collating and centralising data, and we anticipate this will be done digitally in the majority of cases.  |
| <i>Rural proofing</i>          | Our analysis suggests that this policy will not have any adverse impact on rural areas – the changes relate purely to gathering, collating and centralising data, and we anticipate this will be done digitally in the majority of cases.  |
| <i>Sustainable development</i> | Our analysis suggests that this policy will not have any adverse impact on sustainable development – the changes relate purely to gathering, collating and centralising data, and we anticipate this will be done digitally in the majority of cases.  |
| <i>Health and well-being:</i>  | This policy should prevent or deter crime which will have a positive impact on individuals' well-being. We have sought to mitigate any potential adverse impact on health or well-being as a result of enhanced transparency (e.g. to individuals investing in companies carrying out controversial activities) by intending to provide an exemptions framework for individuals that might otherwise be at risk of harm (see separate Impact Assessment on the protection regime). Beneficial ownership information in these cases will not be placed in the public domain and only specified enforcement authorities will |

|  |              |
|--|--------------|
|  | have access. |
|--|--------------|

### Human rights

265. We do not believe that our proposal to implement a central registry of company beneficial ownership information contravenes our commitments to the European Convention of Human Rights (ECHR).

266. Article eight, section one of the ECHR states that:

*“Everyone has the right to respect for his private and family life, his home and his correspondence. There shall be no interference by a public authority with the exercise of this right except such as is in accordance with the law and is necessary in a democratic society in the interests of [...] the prevention of disorder or crime [...]”.*

267. Implementation of a publicly accessible central registry of company beneficial ownership information means that we are exposing personal data on individuals with a significant beneficial interest in a UK company to anyone who chooses to search for it. However, it is important to note that:

- similar information is already being held on the public record - for example, on company shareholders and directors; and some of the required beneficial ownership information will already be in the public domain (e.g. where the company director is the company’s beneficial owner);
- only information on individuals with a significant beneficial interest in a UK company will be held (i.e. individuals with an interest in more than 25% of the company’s shares or voting rights; or who otherwise control the way the company is run); and
- we intend that there will be a framework of exemptions from public disclosure for individuals at risk.

268. In addition, one of the policy objectives is to reduce crime through tackling the potential for misuse of companies; and there is international agreement (for example, at G8 and through the FATF standards) around the importance of enhanced corporate transparency. This further justifies our analysis that our proposal does not contravene our ECHR commitments.

269. The *Memorandum addressing issues arising under the ECHR in relation to the Small Business, Enterprise and Employment Bill* states the Government’s view that the measures in the SBEE Act – which include the central registry - are compatible with the Convention rights. In relation to the PSC register, we have also conducted and published a full Privacy Impact Assessment: <https://www.gov.uk/government/publications/company-ownership-transparency-and-trust-impact-assessments>

### Justice System

270. Following standard IA methodology this IA assumes 100% compliance with the policy. A Justice Impact Assessment Test has also been completed and has been by the Ministry of Justice.

271. We have extended the application of existing company law offences or used existing company law offences to create similar offences to deal with instances where companies or individuals fail to provide beneficial ownership information; or deliberately provide false information.

272. We anticipate however that most instances of non-compliance will be dealt with by Companies House through their usual compliance procedures. For example, Companies House estimate that in 85-90% of cases they write to the company in the first instance, before referring the matter to BIS or other enforcement agencies, or taking action themselves.

Devolved Administrations

273. We do not anticipate any difference in impact on UK companies as a result of their registered office location. The requirements will apply in the same manner to all companies. Similarly, the requirements will apply in the same manner to all beneficial owners, irrespective of their country of residence.

**K. Summary and preferred option with description of implementation plan**

*Summary*

274. The preferred option is Option 1, implementation of a central registry of company beneficial ownership information.

**Table 6: Summary of options**

| Cost / Benefit  | Option 1 (Central Registry)  | Option 2 (Non-regulatory option)  | Which Option performs better?   |
|-----------------|--|---|---|
| <b>Benefits</b> |  |   |   |
|                 | There is little quantified data about the benefits from this policy proposal. Benefits will be associated with: (1) reduction in crime including increased efficiency by law enforcement agencies; reduced due diligence costs for regulated entities; reduced criminal activity and, from this, efficiency and welfare gains to the economy (reduction in fraud crimes which are estimated at <b>£523m</b> pa (not including the transfer costs related to the impacts on the victims of crime)); and (2) increased transparency which could potentially have an impact on economic growth. | Few benefits from reduced crime are expected under this option, given that a voluntary approach would not fully help to deter, disrupt and sanction criminal activity. There might be some deterrent benefits if criminals opt not to use UK companies, and increased awareness/vigilance from the publication of information on the misuse of companies might have some impact on crime. There might be some increase in transactions from the greater transparency. These impacts are, however, expected to be limited. Overall this option is not likely to achieve the desired objective of the policy. | Option 1 performs better than Option 2 in terms of achieving the desired benefits. This is because the regulatory approach is more likely to deal with the crime element of the proposal. |

| Costs |   |  |   |
|-------|---|--|---|
|       | <p>Costs to Government are estimated to be <b>£72k-112k</b> for the IT development of the registry and communication and <b>£225k</b> pa on-going for the maintenance. Cost to businesses are estimated to be <b>£458.9m</b> set up cost (familiarisation, identification, collection, collation and storage of data) and <b>£67m</b> pa on going costs from updating information and providing returns to Companies House.</p> | <p>There are likely to be costs to the public sector associated with promoting the voluntary approach. For example, communications campaigns and business engagement and costs of IT development for Companies House. These costs depend on the scale of the campaign but are estimated at around <b>£0.99m</b>.</p> | <p>In terms of costs to Government Options 1 and 2 would perform at the same level, given that in both cases Companies House will need to set up systems to capture and store the data. However, costs to Companies House might be lower under Option 2 as there would be no 'at risk' beneficial owners identified and hence no need to support a closed register. In terms of costs to the private sector, clearly Option 2 will impose fewer costs than Option 1 and these costs would be voluntary. However, costs should not be considered on their own but in the context of the benefits stated above. On balance, considering costs and benefits of each option it is thought that Option 1 would perform better.</p> |

### *Implementation plan*

275. We intend to require companies to start keeping their registers from January 2016. They will be required to start filing this information at Companies House from April 2016. This provides companies with a period of at least three months to obtain the required information. Compliance and enforcement action will commence from January 2016. Statutory and non-statutory guidance will be published in advance of January 2016 to enable companies to start familiarising themselves with the new requirements.

276. The UK is expected to undergo its next FATF peer review around 2017. The legislation will be statutorily reviewed within three years of the requirement to file beneficial ownership information at Companies House coming into force.

**A. Background**

1. For the purposes of the final IA (and therefore this Enactment IA), we built on the existing evidence base with the following:

- an extension to our original company survey, consisting of largely qualitative questions;
- a series of focus groups consisting of businesses and trade associations; and
- further discussions with law enforcement and tax authorities.

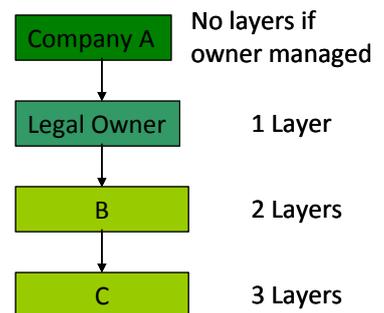
The company survey was used to inform the way we treated the data collected in the original survey, whilst the focus groups were used largely to validate the estimates we produced in the consultation IA. Further discussion with law enforcers provided us with additional data on the scale of the problem and potential benefits as a result of enhanced transparency.

2. For the original company survey, which was first used to inform the consultation IAs, IFF Research conducted a representative survey of UK companies on behalf of BIS, starting in August 2013. BIS worked with IFF to develop a mix of qualitative questions and quantitative cost estimates of 574 companies. The survey was intended to examine the impact of the proposed reforms on all UK companies. Respondents were asked questions to explore the likely cost impact of establishing a central registry of company beneficial ownership information, transparency around ‘front’ directors, the prohibition of corporate directors and the disqualification of certain directors.

**Sampling**

3. To identify the population of interest, we conducted a sample from the FAME<sup>110</sup> database, which is based on Companies House data. Companies were split into a 3x2 grid of quota cells based on corporate structure:

- simple with 0-1 layers in the ownership chain;
- reasonably complex with 2-3 layers of ownership (UK-owned, no trusts in the ownership chain); and
- complex with over 4 layers and/or foreign ownership



As well as company size:

- micro and small (fulfilling 2 of 3 from the following criteria: (i) Turnover < £6.5m; (ii) Balance sheet < £3.26m; (iii) Employees < 50); and
- medium and large (fulfilling 2 of 3 from the following criteria: (i) Turnover > £6.5m; (ii) Balance sheet > £3.26m; (iii) Employees > 50).

4. This sampling framework enabled our analysis to identify rigorously how costs would vary by company size and complexity. Ultimately, this shaped the proposed policy so as to minimise the burden on UK companies, whilst maximising the resulting crime reduction and economic growth enhancement.

**Data Output**

5. The total cost figures were calculated based on estimates for the number of hours it would take particular employees to comply with the proposals. Once IFF Research compiled these data, they

<sup>109</sup> The estimates in the main body of this IA take the adjusted survey results reported here and updates them to 2014 prices  
<sup>110</sup> FAME database. 2013. Bureau Van Dijk Electronic Publishing.

were multiplied by the hourly wage rates taken from the Annual Survey of Hours and Earnings (ONS, 2012)<sup>111</sup>. The wages used were:

|                      | ASHE wage data  | Micro and small companies | Medium and large companies |
|----------------------|---|---------------------------|----------------------------|
| Senior Management    | Chief executives & senior officials   | £48.20                    | £57.18                     |
| Middle Management    | Corporate managers and directors (excluding chief execs & senior officials) | £18.33                    | £23.89                     |
| Administrative Staff | Administrative & Secretarial Occupations                                    | £10.78                    | £11.59                     |

Table 1: Wage rates used in the company survey

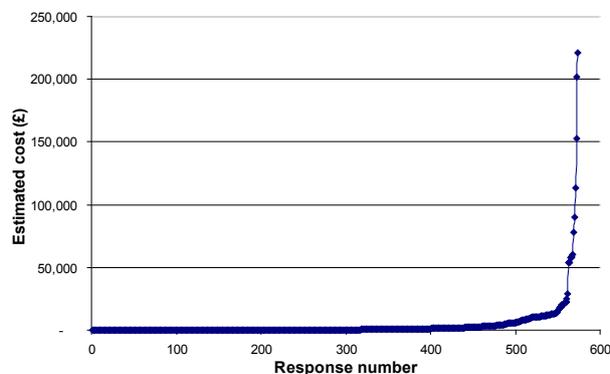
6. The estimated mean was weighted according to the original FAME sample below, such that more weight was given to cells with a greater number of companies. More specifically, the raw sample data were weighted according to their size and structure (as per the share of all companies in each of the 6 cells in the 3x2 grid) and according to the number of observations of each of the 6 company types in the sample. As a result, the overall mean is largely driven by the estimates from ‘small, simple’ companies.

| Weighting grid | Simple | Reasonably complex | Complex      | Total            |
|----------------|--------|--------------------|--------------|------------------|
| Small / Micro  | 93.5%  | 2.9%               | 1.9%         | 98.3%            |
| Medium/ Large  | 0.92%  | 0.28%              | 0.55%        | 1.74%            |
|                |        |                    | <b>TOTAL</b> | <b>3,187,112</b> |

Table 2: Fame data split by company size and complexity

## B. Issues with the original survey

7. In-depth analysis of the survey methodology and responses highlighted several issues. When the survey questionnaire was designed (August 2013), policy was in the early stages of development and was subject to consultation. In fact, IFF Research explained to BIS that some respondents struggled to answer the questions and some had varying interpretations of the questions.
8. We identified a number of striking distributions across all survey questions. The data we received showed a number of respondents who estimated costs which were extremely high, in contrast to a ‘long tail’ of respondents who estimated zero costs. For instance, the question relating to familiarisation costs for the creation of a register of beneficial ownership information, yielded the following distribution of responses:



111 The statistics taken from ASHE are based on the median rather than the mean. This is the preferred measure of earnings as it is less affected by a relatively small number of very high earners and the skewed distribution of earnings. It therefore gives a better indication of typical pay than the mean. The survey takes a sample of employee jobs drawn from HMRC records of gross pay before tax, National Insurance or other deductions. These data were then uplifted by 17.8% to reflect non-wage costs (i.e. National Insurance, pension contributions, other payroll taxes and other non-statutory employee services such as transport and canteen provision). This is in accordance with Eurostat data and forms a standard assumption.

Figure 1: Distribution of responses on familiarisation costs related to beneficial ownership.

| Staff Cost (£) |        | Additional costs (£) |        | Total costs (£) |        |
|----------------|--------|----------------------|--------|-----------------|--------|
| Mean           | Median | Mean                 | Median | Mean            | Median |
| 1,087          | 145    | 1,124                | 0      | 2,211           | 196    |

Table 3: Familiarisation costs related to beneficial ownership

9. Close interrogation of this ‘tail’ of high responses has not indicated any discernible pattern; that is to say, the companies which gave high responses did not consistently adhere to any identifiable characteristics. We might have expected higher costs for larger and more complex companies, but analysis of these respondents showed no relationship between cost<sup>112</sup> and size (based on turnover, employees and assets) and complexity (based on the number of layers of share ownership).
10. If we compare the cost estimates produced by the present survey to other comparable cost estimates, they are substantially higher:

| Source   | Cost                                | Cost estimate per company      | Company Survey Raw Mean                                  |
|--|-------------------------------------|--------------------------------|--|
| Companies House <sup>113</sup> - Filing Requirements | Familiarisation                     | 20 minutes = £6 <sup>114</sup> | £1087 (Beneficial Ownership Familiarisation)             |
| PWC – Admin Burdens Exercise <sup>115</sup>          | Returning a form to Companies House | £12.39 <sup>116</sup>          | £160 (Annually providing information to Companies House) |

Table 4: Cost estimate comparisons

### C. The updated evidence base for the final Impact Assessment

11. IFF Research conducted a follow-up survey with 43 of the 574 respondents to interrogate their original answers and to identify whether their answers would change in the light of new policy detail. Although the follow-up survey used a relatively small sample, IFF Research was able to conduct in depth interviews with the respondents from the original survey.
12. We specifically targeted interviews at the respondents who gave either zero, low (under £5) or high (top 10%) quantitative estimates in the original survey. In total, we received 31 responses to the beneficial ownership questions and 12 responses to the corporate directors questions. Across all the questions we aimed for roughly a 50:50 split between ‘high’ and ‘low’ respondents.
13. Ultimately, the research findings guided us in developing the methodology for this final IA and determined the way in which we treated both the *low* and *high* respondents.
14. For the reasons set out below, the new survey indicated the original survey questions lacked the specificity required to elicit fully informed answers consistently. **We believe these issues have had an effect on the robustness of the responses and therefore on their overall suitability**

112 Although there was a slight tendency for those giving high responses to be ‘large’ – around 60% were.

113 Detail in the cost benefit analysis within consultation on Companies House Filing Requirements.

114 The wage cost used was £19 – the mid point between the median wage and the wage of a company director

115 This study excluded policy costs, which are typically ten times the admin costs

116 Upated from 2007 prices to 2013 prices

for **unqualified** use in our analysis of the costs. The issues we identified with the survey are detailed below for both the beneficial ownership policy and the corporate directors policy. We faced the same issues in the survey with both policies so it is worthwhile discussing them jointly.

### **Reasons companies gave high wage cost estimates**

- Misinterpretation of the questions (e.g. provision of annual cost estimates rather than for a single procedure. This gave estimates which were many times larger than they should have been).
  - Companies provided initial upper estimates, which they expected to fall over time.
  - Double counting (e.g. companies including compliance costs in their familiarisation cost estimate as well as reporting it separately).
  - Reporting the total number of hours for all staff rather than a break down by staff level. This raised cost estimates substantially if the staff hours were recorded as senior staff time with their considerably higher wage relative to admin staff time for instance.
15. In addition to the four types of mistakes we commonly encountered from respondents in the original survey, respondents often revised down their original estimates when they were given new policy information:
- 54% (of the 24 companies which were asked how their estimates would change) revised down their estimates on beneficial ownership from an originally 'high' estimate.
  - 29% (of the 17 companies which were asked how their estimates would change) revised down their estimates on corporate directors, whilst 65% stood by their original 'high' estimate.
16. This finding reinforces our use of the four types of mistakes to inform our treatment of the data to remove a number of the extreme values. If all companies had revised down their estimates, we might have considered removing more of the outliers but we have adopted a more moderate approach here.
17. We by no means considered all the 'high' responses received in the first company survey invalid. However, in the light of the above we targeted the removal of high estimates primarily from 'small simple' companies, as described below - table 6 shows the highest estimates we used were still in most cases several thousand pounds for 'large complex' companies. Although the second company survey did not entirely determine how we treated the data, it did indicate to us that some proportion of cost estimates was implausible.

### Quotes from 'high cost' respondents:

In terms of familiarisation with the beneficial ownership proposals, once companies were given new policy detail they revised down their estimates considerably. One respondent, who previously estimated it would take one senior manager five hours and £10,000 in additional (legal) costs said:

- *“That would obviously take less if it could all be done by this [13 pages of guidance for familiarisation] and less digging had to be done and to make the explanation up front. Should reduce it by at least 25% if I have to give a number.”*  
[micro/small, simple structure]

Similarly, a representative from a small complex company revised compliance cost estimates down substantially after new policy information made the respondent realise compliance would be less onerous than originally expected:

- *“Those times and costs would go down considerably. Down by 90% because all the work’s done for you. They’re just saying “we’re here, hi!””*  
[micro/small, complex structure]

### **Reasons companies gave low wage cost estimates**

- Companies misunderstood and thought the reforms were not relevant to their company (particularly for beneficial ownership) so incorrectly assumed they would not undergo any cost for familiarisation or compliance.
  - Difficulty in answering the hypothetical questions (e.g. most companies answering the corporate directors questions did not have a corporate director, so chose to give low responses.)
18. In the light of new policy information, 79% (of the 19 companies which were asked how their estimates would change) did not revise their estimates on beneficial ownership, whilst the remaining 21% revised up their original 'low' estimate.

#### **Quotes from 'low cost' respondents:**

In the case of companies familiarising themselves with the beneficial ownership proposals, a typical response from a respondent who already knew their company's beneficial owner and understood the associated principles was:

- *"We have 2 shareholders with 50% share each, they're both directors of the company, they both live together and one of them is me. So we are both well aware of the changes and we don't really need to do much else."*  
[micro/small, reasonably complex structure]

Another comment related to a small simple company responding to a request was:

- *"We're only a small private owned company with a couple of shareholders so beneficial ownership is not really much of an issue. It would be one person (i.e. me) writing a letter I suppose, or responding to an email - no systems or infrastructures envisaged."*  
[micro/small, simple structure]

### **Business Focus Groups**

19. Alongside the follow-up company survey we also held a number of focus groups with around 30 companies and 6 business representative organisations (listed in **Annex B**), which together represent at least 240,000 companies and many hundreds of thousand employees. These groups were orientated around validating or disproving the estimates we provided in the consultation IAs.
20. In the case of the beneficial ownership, of the six distinct types of cost, five of them were largely validated by the groups. Collation, processing and storage costs were only partially validated because some companies thought if paper records were required costs could be higher. Although the attendees found it difficult to place an accurate figure on how much it would cost them to follow a certain procedure, in general they thought our estimates seemed to be reasonable for small simple companies (around 94% of the population) but costs could be considerably higher for larger and more complex companies. Given that the figure was already weighted by the size and complexity of the company (as detailed below), we considered it to be consistent with the types of comments the groups made.

### **D. Methodology for the Final Impact Assessment**

21. Despite its flaws, the original representative survey provides the most comprehensive dataset available, and we believe there is value in processing it to produce realistic and duly qualified cost estimates. The results from the original company survey, particularly at the upper end of the distribution, were surprising. Firstly, they didn't fully accord with the discussions we had with stakeholders and secondly it was not clear why the estimates were so high.

22. For the consultation IAs we also adopted a truncated mean approach (i.e. using only feasible values in the mean calculation) to adjust for extreme values. The RPC commented that some further analysis around how the estimates differ, if the data were processed differently, would be informative so we have refined our approach.
23. For this final IA, we were able to gather more evidence from an additional survey and business focus groups to build on the evidence we already had. Indeed, the analysis and evidence gathering for this IA have been in development since July 2013 and we have pursued every relevant evidence source fully. The new evidence enabled us to truncate the data on the basis of this new information. For instance, the second company survey suggested that the extreme 'high' cost estimates commonly suffered from double counting and misinterpretation. Put simply, these extreme estimates were found to be unfeasibly high and not appropriate to include in the dataset. This validated our approach of processing the data to arrive at realistic estimates.
24. Therefore, we have truncated the mean (i.e. used only feasible values in the mean) to adjust for extreme values. Truncation is a statistical technique which is commonly applied to survey data. On this occasion, we utilised a more robust technique to identify where to truncate and we truncated a lower proportion of the data than in the consultation IA.

#### Treatment of High Wage Cost Estimates

25. It is necessary to exclude implausible or unverifiable estimates at the high end of the distribution. Similarly to the consultation IAs we used a truncated mean for each survey question relating to costs. However, on the basis of the new evidence we gathered for this IA, we have revised our truncation method as follows:
- i) we trimmed the weighted values (rather than the unweighted values, as per the consultation IA) to target more effectively the implausibly high estimates, which were biasing our estimate of the mean upwards. This also enabled us to trim a lower share of the data relative to our previous approach in the consultation IA; and
  - ii) we used a robust statistical technique (based on analysing the coefficient of variation\*) to identify the specific point at which to truncate the mean.

\* The coefficient of variation is a measure of sampling error, which takes account of the size of the estimate, giving a relative measure of precision. It is calculated as the standard error divided by the mean. Lower figures imply a more precise estimate of the mean. Standard errors have been calculated taking proper account of the fact that we are using a weighted and truncated mean, such that the highest observations still contribute to the standard error.

26. To explain (i) further, as detailed above, each observation in the sample was weighted according to how commonly its company type (based on the 3 x 2 grid in table 2) was seen in the population. As a result, an estimate given by a small simple company was given a much greater weight than one given by a large complex company. Once these weighted values are totalled and divided by the number of observations, this ultimately produces a mean that is representative of the whole population.
27. By trimming weighted values, we are able to remove most efficiently the observations which are distorting the mean upwards. For instance, if a small simple company were to offer a cost estimate of £1,000, because that type of company is given a large weighting, this single response would drag up the mean substantially. On the basis of our second company survey, the relatively high responses were called into question for the reasons detailed above. It would therefore be sensible to remove the

responses, which were incorrectly raising the mean beyond a feasible value. Moreover, adopting this approach helps to minimise the number of observations that are removed from the dataset.

28. With regard to (ii), for each quantitative question we plotted the coefficient of variation for each potential trim, as shown below for the cost of removing and replacing a corporate director. Adopting this approach rather than simply eyeballing the distributions to identify where to trim, gives us a robust objective rule which is founded upon minimising the sampling error. Trimming on a purely statistical basis, we should trim up to the lowest coefficient of variation (i.e. the global minimum). However, the estimated means produced on this basis produced results which were inconsistent with the costs we would expect based on our latest focus groups and company survey.

29. For this reason, we have adopted a second trimming approach, which trims after the next substantive fall in the coefficient of variation (i.e. the next lowest local minimum). This allows us to arrive at an estimate, which is more consistent with the figures which were validated by industry in our focus groups and company surveys. In the chart below, the vertical red line on the left is the suggested trim based on the first method (1%) and the vertical red line on the right is the suggested trim based on the second method (8%).



Figure 2: Coefficient of variation chart for the cost of removing and replacing a corporate director

30. To provide some sensitivity analysis around these estimated means, we used the following estimates:

- **Low:** Mean from the second trimming approach (local minimum)
- **High:** Midpoint between the two trimming approaches
- **Best:** Mean from: (Percentage of remaining data after second trim x Second trimming approach mean) + (Percentage of data trimmed under second approach x Mean from first trimming approach)

For instance, the best estimate in the case of removing and replacing a corporate director was calculated as follows:  $(93\% \times £58) + (7\% \times £191) = £67$ . This essentially assumes that for 93% of companies, £58 would be a reasonable estimate whilst £191 would be appropriate for the remaining 7%. The low estimate would be £58 (i.e. the second trim) and the high estimate would be £125, calculated as a mid-point between the first and second trims.

31. To explain our thinking further, based on the results of the second company survey and the focus groups, we felt we had to trim the data to arrive at reasonable cost estimates. Of the two trimming approaches we used, the estimates derived from the first trim were not reasonable based on the wider evidence we gathered. For this reason we applied the above sensitivity analysis, which uses both trims, to arrive at a range of estimates that fitted closely with the discussions we had with business.
32. The table below displays where the coefficient of variation led us to trim under the two chosen methods. We also provide the cost estimates for these two methods in addition to the low, best and high wage cost estimates, used in the calculations for this impact assessment. These estimates are in line with the BIS evaluation of the Companies Act 2006<sup>117</sup> in which 33% of the companies surveyed spent under 10 hours in total complying with the whole Companies Act over the course of three years (at the very most around £480 in wage costs).

| Cost  | First trimming approach |      | Second trimming approach |      | Wage cost estimates |      |      |
|---|-------------------------|------|--------------------------|------|---------------------|------|------|
|   | Trim                    | Cost | Trim                     | Cost | Low                 | Best | High |
| Familiarisation with the beneficial ownership reforms                     | 6%                      | £111 | 13%                      | £48  | £48                 | £56  | £80  |
| Identifying and collecting information about the beneficial owner         | 1%                      | £45  | 8%                       | £5   | £5                  | £9   | £25  |
| Responding to a request about your beneficial ownership                   | 4%                      | £35  | 13%                      | £7   | £7                  | £11  | £21  |
| Collation, process and storage of beneficial owners' data                 | 1%                      | £53  | 9%                       | £9   | £9                  | £13  | £31  |
| Updating beneficial ownership information annually                        | 4%                      | £42  | 14%                      | £9   | £9                  | £14  | £26  |
| Providing beneficial ownership information to a central registry annually | 3%                      | £40  | 14%                      | £9   | £9                  | £13  | £24  |

*Table 5: Wage cost estimates and trimming positions*

33. However, as noted above, we trimmed on the basis of weighted cost estimates. Since around 94% of companies were 'small, simple', any estimate from a company of this type would be weighted relatively heavily. As a result, if a 'small, simple' company gave a relatively high cost estimate, combined with their large weighting, their estimate would be more likely to appear at the top of the distribution. It would therefore make it more likely to be trimmed from the dataset as an extreme value.
34. Our a priori knowledge of the likely costs as well as our evidence base (second company survey, business focus groups and consultation) suggested that, particularly for 'small, simple' companies, costs should be relatively low compared with larger more complex companies. This was largely because compliance would be far more straightforward. For this reason, it was deemed plausible that any 'small, simple' estimates at the upper end of the distribution were less reliable and hence correctly caught by the trimming methodology. By contrast, where possible, we avoided removing estimates from larger, more complex companies because compliance could be considerably more time consuming.

<sup>117</sup> <http://www.bis.gov.uk/assets/biscore/business-law/docs/e/10-1360-evaluation-companies-act-2006-volume-1.pdf>

35. The table below compares the maximum cost estimates provided by 'small, simple' and 'large, complex' companies, when the data are untrimmed and at the first and second trimming points<sup>118</sup>. To explain further, iteratively trimming one percent of the data at a time will gradually remove the highest weighted values. As more data points are removed this reduces the threshold level for the maximum estimate, which feeds into the mean. However, the impact will differ by company type because generally the companies with the largest weighting (i.e. 'small, simple') will have their highest cost estimates trimmed first.
36. It is clear to see that at the second trim, the maximum allowed estimate for 'small simple' is substantially reduced. For instance for beneficial ownership familiarisation, the maximum untrimmed estimate for a 'small simple' company was £48,200 but after trimming, the maximum allowed estimate was £59. The maximum estimate for a 'large complex' company falls substantially but remains almost 100 times as large as the 'small simple' estimate. More specifically, it falls from £88,244 to £5,718.
37. This demonstrates that under our trimming method, we are primarily targeting the removal of the 'high' estimates from 'small simple' companies. However, we are not removing proportionately as many of the estimates from 'large complex' companies, for which costs might be substantially higher. This is in line with the evidence we gathered from the business focus groups and the follow-up company survey.

| Cost   | Untrimmed             |                 | First Trim           |                 | Second Trim          |                 |
|--|-----------------------|-----------------|----------------------|-----------------|----------------------|-----------------|
|  | Max recorded estimate |                 | Max allowed estimate |                 | Max allowed estimate |                 |
|  | 'Small simple'        | 'Large complex' | 'Small simple'       | 'Large complex' | 'Small simple'       | 'Large complex' |
| <b>Familiarisation with the proposed beneficial ownership reforms</b>            | £48,200               | £88,244         | £236                 | £13,447         | £59                  | £5,718          |
| <b>Identifying and collecting information about the beneficial owner</b>         | £1,475                | £6,407          | £386                 | £6,407          | £22                  | £2,287          |
| <b>Responding to a request about your beneficial ownership</b>                   | £5,398                | £4,864          | £96                  | £4,864          | £12                  | £1,372          |
| <b>Collation, process and storage of beneficial owners' data</b>                 | £8,819                | £34,678         | £3,889               | £34,678         | £138                 | £18,230         |
| <b>Updating beneficial ownership information annually</b>                        | £2,699                | £4,735          | £96                  | £4,735          | £14                  | £1,372          |
| <b>Providing beneficial ownership information to a central registry annually</b> | £12,050               | £5,248          | £96                  | £5,248          | £12                  | £1,946          |

*Table 6: Maximum allowed estimates under trimming method*

38. To demonstrate the impact of trimming on the means for different company type, for illustrative purposes, table 7 provides the means for 'small simple' and 'large complex' companies. Naturally, by trimming, the means for both company types fall. However, the mean for 'small simple' companies falls substantially more than for 'large complex' companies. For instance, the mean familiarisation costs related to beneficial ownership fall from £1,098 to £46 for 'small simple' companies. By contrast, for 'large complex' companies, the mean falls from £1,858 to £946. This demonstrates the types of mean we arrive at under the trimming approach compared to the means we would arrive at without trimming.

<sup>118</sup> We provide only the data for the second trim for illustrative purposes because this shows the largest change from the untrimmed data.

| Cost  | Untrimmed      |                 | First Trim     |                 | Second Trim    |                 |
|---|----------------|-----------------|----------------|-----------------|----------------|-----------------|
|   | Mean           |                 | Mean           |                 | Mean           |                 |
|   | 'Small simple' | 'Large complex' | 'Small simple' | 'Large complex' | 'Small simple' | 'Large complex' |
| Familiarisation with the proposed beneficial ownership reforms            | £1,098         | £1,858          | £133           | £1,102          | £46            | £946            |
| Identifying and collecting information about the beneficial owner         | £70            | £296            | £41            | £296            | £5             | £228            |
| Responding to a request about your beneficial ownership                   | £181           | £204            | £39            | £204            | £7             | £156            |
| Collation, process and storage of beneficial owners' data                 | £88            | £350            | £55            | £350            | £11            | £230            |
| Updating beneficial ownership information annually                        | £144           | £205            | £45            | £205            | £10            | £171            |
| Providing beneficial ownership information to a central registry annually | £214           | £205            | £43            | £205            | £10            | £172            |

Table 7: Estimated means under second trimming method and untrimmed

### Treatment of Zero Wage Cost Estimates

39. It is also necessary to consider how to treat zero values. A large number of survey respondents answered that there would be zero costs arising, for example, from the proposed policy changes, as detailed in section C. This seems counter-intuitive, because all companies would need to spend at least some time understanding a form, even if just to determine that no or limited action is necessary. For this reason, we re-coded these observations such that they were set to the minimum recorded positive estimate. For instance, if the minimum cost estimate any company in the sample gave was £5, all zero responses would be re-coded to £5. This is a reasonable approach, which reflects the assumption that all companies would have to undergo some cost. It also minimises the bias to the dataset, which we would otherwise have been introduced by re-coding the values to a higher value which is not supported by any evidence. This will raise the estimate mean cost relative to simply including zero cost values in the calculation of the mean.
40. The main benefit of not removing the zero values from the sample as we did in the consultation IA is that we are not losing such a substantial number of observations. Since we need to trim at the top end of the distribution, also removing the zero responses from the bottom end would dramatically reduce the sample size. The table below shows that there was considerable variation in the number of zero responses for each question but on average some 30% of observations were zero.

|   | Number of zero observations | Zero observations as % of all observations |
|---|-----------------------------|--|
| Cost of company familiarisation with the beneficial ownership reforms             | 67                          | 12%  |
| Cost of identifying and collecting information about the beneficial owner         | 387                         | 67%  |
| Cost of responding to a request about your beneficial ownership                   | 185                         | 32%  |
| Cost of collation, process and storage of beneficial owners' data                 | 162                         | 28%  |
| Cost of updating beneficial ownership information annually                        | 119                         | 21%  |
| Cost of providing beneficial ownership information to a central register annually | 76                          | 13%  |

Table 8: Zeros observations in the sample

## Treatment of Additional Cost Estimates

41. The next issue relates to whether the responses to questions around additional costs should be included. As set out above, the responses to the non staff costs were implausibly high when compared with other evidence sources. The question was open-ended and did not define the sorts of costs that should be included, and IFF Research reported that there were very significant differences in interpretation of these questions across respondents, with some highly unusual interpretations. They were clear that the lack of question specificity was a particularly acute issue with these questions.

42. In the follow up study, IFF Research further interrogated the additional costs. Companies generally considered these costs to arise from legal and accountancy advice for the beneficial ownership questions. In the light of new evidence, the majority of companies stood by their original estimate but similarly to the wage cost estimates, a number of companies gave comments that cast some doubt over the validity of the highest estimates. The main issues we noticed were:

- some companies commented that their additional cost estimates were very much a ‘worst case scenario’;
- some companies mentioned that they might not in fact incur additional costs; and
- a few companies noted that on reflection they may have included some staff time in their additional cost estimates – meaning there was some double counting.

43. For instance, one ‘high cost’ additional cost response, came from a company which previously estimated additional costs of £5,000. In the second survey they revised their answer, no longer feeling that it would cost their company anywhere near this, and would be more likely to cost them around £100. This was because, on further discussion, they felt that they would not need to incur legal fees for this particular task.

*“I think the most likely outcome is that the cost will be negligible by which I mean less than £100 and it would be an awful lot to take it £5,000 to be honest on the basis that there’s no cost in terms of fees, so we’re only talking about internal time.”*

[medium/large, simple structure]

44. On this basis, it seemed sensible to truncate the dataset using the same method that we applied to wage costs. The only difference in method for our treatment of additional costs was the inclusion of zero values. In this case, we consider it an entirely valid response for a company to state that it would not undergo optional additional costs because it could comply with the proposals using in-house resources.

45. The table below details where we chose to trim and the resulting estimated mean. These estimates are in line with the BIS evaluation of the Companies Act 2006<sup>119</sup> in which 64% of the companies surveyed spent under £500 in total on additional costs to comply with the whole Companies Act over the course of three years.

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119 <http://www.bis.gov.uk/assets/biscore/business-law/docs/e/10-1360-evaluation-companies-act-2006-volume-1.pdf>

| Cost  | First trimming approach |      | Second trimming approach |      | Additional cost estimates |      |      |
|---|-------------------------|------|--------------------------|------|---------------------------|------|------|
|   | Trim                    | Cost | Trim                     | Cost | Low                       | Best | High |
| Company familiarisation with the proposed reforms                         | 4%                      | £111 | 12%                      | £25  | £25                       | £36  | £68  |
| Identifying and collecting information about the beneficial owner         | 1%                      | £65  | 6%                       | £15  | £15                       | £18  | £40  |
| Responding to a request about your beneficial ownership                   | 1%                      | £87  | 6%                       | £15  | £15                       | £19  | £51  |
| Collation, process and storage of beneficial owners' data                 | 1%                      | £37  | 4%                       | £11  | £11                       | £12  | £24  |
| Updating beneficial ownership information annually                        | 1%                      | £113 | 4%                       | £27  | £27                       | £30  | £70  |
| Providing beneficial ownership information to a central registry annually | 1%                      | £63  | 4%                       | £21  | £21                       | £22  | £42  |

*Table 9: Additional cost estimates and trimming positions*

## Annex B – Focus Groups Attendance List

### Companies in attendance

Abell Morliss International  
Armess  
Assoc of Company Registration Agents  
Bank of America Merrill Lynch  
Broadhead Accountants  
Capita Asset Services  
Centrica PLC  
Charles Russell LLP  
Chettleburgh's Ltd  
Company Registrations Online  
Creditsafe  
Dun and Bradstreet and BIPA

Entone Group  
Experian  
Jordans Trust Company Ltd  
LegalinX-7Side  
MSP Secretaries  
Naylor Wintersgill  
Penfold & Redstone Ltd  
PWC Tax  
RBJ Tax & Accountancy Services  
Slaughter and May  
Stanley Davis & Co.  
The London Law Agency Ltd  
Thomson Reuters  
Thrings Solicitors  
Ward Williams  
Wilder & Coe Ltd

### Business representative organisations in attendance

ICSA - Compliance  
BCC  
ICAEW  
Law Society  
ICSA - Software International  
ICSA - Customer Services

(We have separately discussed these policy proposals and analysis with a range of other business representative organisations including the CBI and IoD.

In total, these business representative organisations represented at least 240,000 companies and the views of hundreds of thousands of employees.)

## Annex C: Sensitivity Analysis

The assessment of the base case presented above relies upon a number of assumptions. The key ones of these are:

1. The number of firms affected
2. The treatment of only one-off additional costs being included in the costs. This includes the use or otherwise of Trust and Company Service Providers (TCSP) which help companies incorporate and may have an ongoing relationship with the company thereafter to undertake certain regulatory obligations (e.g. filing company returns). These include Company Registration Agents, some lawyers and some accountants.
3. The use of the IFF Research data exclusively in the costings but informed by alternative sources of data
4. The sharing of costs between the company and the beneficial owners
5. Number of changes in a year
6. The number of beneficial owners
7. Other assumptions

The statistical treatment of the data to arrive at high, best and low estimates of the costs is set out in **Annex A** and will not be repeated here.

### **1. Number of firms**

Clearly if we were to reduce the number of firms covered there would be a significant change to the EANCB as it is a key number which is used throughout the calculations – halving the number of firms (keeping the proportion of large/small and ownership complexities the same) would halve the costs and negatively affect the benefits.

The number of firms affected is taken from the FAME database. This uses Companies House and other organisations' data. It is judged to be the best available data for this purpose as it breaks down companies by size and complexity of ownership and fully accords with Companies House official filings numbers. Also the policy has explicitly set out the need to close loopholes, and it does this by minimising the number of exemptions to where there is ownership information already in the public domain.

### **2a. Additional costs**

The base case includes only the one-off additional costs that companies might incur (i.e. purchasing of external accountancy or legal advice). This is because the second survey indicated that there were very significant differences in interpretation of these questions across respondents in the first survey and significant uncertainty about what was meant. Some companies indicated that their estimates were a worst case, others that they would actually not incur any costs and still others noted that there was some double counting between wage costs and additional costs. Furthermore our view was that the policy design – of the reporting being added to the 'check and confirm' process and the simple updating of existing records and guidance being provided – would mean that ongoing additional advice would not usually be required. There is also the consideration that, if it were required, the need could rapidly decay and thus the annual costs would decrease over the appraisal period.

However, if the ongoing additional costs (of £30.7pa for updating the companies own records and £22.5pa for sending the information to Companies House annually) are also included in the cost calculation, (ie an extra  $(£30.7pa * 0.52 + £22.5pa) * 3.43m$ ) the EANCB rises to £174.9m. However for the reasons noted in the main body of the text we do not think that this is likely to reflect the true position, especially over time.

If the additional costs were excluded entirely the EANCB would fall to £68.2m (i.e. less (£57.6\*3.43m) + (£19.8\*130,000)). However again we do not think that this would reflect the true costs as we expect that, given the possible novelty of the concept of beneficial ownership for some companies and the new legal requirement coupled with the link to Companies House, the use of accountants and lawyers as a source of advice is entirely plausible.

## **2b. Use of TCSPs**

Companies House data indicate that 73% of new companies use TCSPs to help them incorporate<sup>120</sup>. Furthermore, research commissioned by Companies House estimates that 41% of companies use accountants or agents to file their Annual Return.

Assuming that TCSPs would undertake the familiarisation on behalf of the company with which they have an ongoing relationship (i.e. 41% of companies) the one-off costs could fall to £378.6m from the base case of £458.9m (ie the familiarisation costs would be only £57.1\*59%\* 3.43m<sup>121</sup>): giving an EANCB of £78.8m (compared to £85.9m on the base case).

## **3. Data sources**

The base case uses IFF Research data from the initial representative company survey, adjusted statistically and broadly validated by the focus groups and follow-up survey. We considered that this was the best available information.

However, if we take the Global Witness report<sup>122</sup>, the costs are considerably lower than our base case at £24m one-off costs and £2.3m ongoing costs – this gives an EANCB of £3.9m. As noted above however this research is not based on direct engagement with companies but solely on expert opinion to set the assumptions. It does not cover all the likely costs (e.g. familiarisation and identification).

The PWC estimate of the cost of filing of £12.39 per company is only marginally lower than the £13.7 per company used as the base case: in this case the EANCB falls to £83.6m.

Companies House has estimated the cost of familiarisation of £6 per company rather than the £57.1 wage costs in the base case. Using this estimate the EANCB falls to £70.4m.

## **4. Sharing of costs between the company and the beneficial owner**

The base case has the costs of identifying the beneficial owner split 50:50 between the company and the beneficial owner. This is because both are obligated under this proposal and where the costs fall will depend on the nature of the shareholding/control (e.g. where an individual has a direct interest in more than 25% of the company's shares or voting rights, a company taking reasonable steps will likely identify that person. In other cases, the beneficial owner will more likely need to self-disclose their interest). As we do not know how many beneficial owners there are we have not been able to quantify the costs to the individual.

If we assume all the costs were to fall on the company, the EANCB rises to £90.1m. If the percentage borne by the company falls to 25% of the costs the EANCB falls to £83.8m. The small size of the changes in the EANCB from these costs is due to them being only 5% of the total one-off costs.

## **5. In-year changes to information**

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<sup>120</sup> Companies House, February 2014

<sup>121</sup> i.e. it is assumed that the TCSPs are already included in the 59% who familiarise themselves. They themselves might incur a higher familiarisation cost if more of their staff need to know about the requirements than that assumed by the survey respondents. However we have no further data on this.

<sup>122</sup> John Howell & Co Ltd for Global Witness (2013): *Costs and Beneficial Ownership Declarations*

In the base case, we assume that the in-year changes to information will occur on average 0.52 times a year, based on the number of times a person moves residence, the number of time non-traded shares are bought and sold and an estimate of the number of beneficial owners per company providing information (using legal shareholders as a proxy for beneficial owners).

If we take the response to the IFF company survey, that only 16% of companies expect their PSC information to change within a year, then the number of changes to be made to their own records is 285,000 pa ( $1.3m * 16% * 0.4$ ). In this case the EANCB falls to £74.5m.

The EANCB is broadly resilient to changes in these assumptions about in-year changes, however there is a lack of evidence around the number of beneficial owners providing additional information.

## 6. **Beneficial owners**

Linked to section 5 above, we have no robust evidence as to the number of beneficial owners likely to incur a cost, nor what that cost might be. Thus we have provided no estimate of the costs of these proposals to individuals in the base case. The main body of the text sets out why this is the case. It also sets out the actions we would expect a beneficial owner to undertake. Whilst communication with the company is likely to be low cost (e.g. via email), familiarisation and understanding the requirements are likely to be higher. For illustrative purposes alone, the table below takes the £57.1 one-off company familiarisation costs and applies it to a range of beneficial owner numbers: it also gives an annual average discounted cost (starting in 2015).

| Number of beneficial owners incurring one-off costs for familiarisation/ understanding | One-off cost at £57.1 per beneficial owner | Annual average discounted cost |
|--|--|--------------------------------|
| 500,000  | £28.6m                                     | £2.5m                          |
| 1,000,000  | £57.1m                                     | £5.1m                          |
| 2,000,000  | £114.2m                                    | £10.1m                         |
| 3,000,000  | £171.3m                                    | £15.2m                         |
| 4,000,000  | £228.4m                                    | £20.2m                         |
| 5,000,000  | £285.5m                                    | £25.3m                         |

## 7. **Other assumptions**

Other aspects of the cost calculation are:

- In-year changes to beneficial ownership information will be provided by the beneficial owner themselves (except where the company should be expected to know of the change – e.g. significant share transactions) so for companies updating information will be mainly an administrative task which can be incorporated into their existing processes. In these circumstances we might therefore expect the ongoing costs of updating information to be lower than in the base case.
- The company will need to inform the beneficial owner that their information will appear on the register. However this can be done as part of the initial identification process and, for some companies, the person asking the question will themselves be the beneficial owner. In some cases a further email/letter will need to be sent from the company to the beneficial owner, however we do not know how many this will be, nor the cost.
- For some companies they will only need to gather information from their parent companies rather than request information from their entire ownership chain. This will decrease the costs estimated in the base case for these companies.

- In the base case we assumed that the cost to parents of responding to requests for information from their subsidiaries would in effect be equivalent to the cost of replying just once (i.e. 130,000 actions). Where a parent incurs the cost of responding to every subsidiary (i.e. 322,000), the cost of this element of the proposal rises from £4m to £9.9m: the best estimate EANCB then becomes £86.4m.
- Following standard methodology this IA assumes 100% compliance. We have no evidence to indicate the potential level of non-compliance, however where non-compliance occurs clearly the benefits would be lower, as would the costs. However, as noted in the main body of the IA we anticipate that most instances of non-compliance would be dealt with by Companies House through their usual compliance procedures. For example, Companies House estimate that in 85-90% of cases they write to the company in the first instance, before referring the matter to BIS or other enforcement agencies, or taking action themselves. Where the matter is referred we would anticipate costs to the court service and potentially also the prison service. There might also be some costs incurred to companies and others where a person fails to respond to a request for information and the company imposes restrictions on the shares or rights as a result.

### **Conclusion**

Overall, the assumptions used to construct the base case using the revised IFF Research results, broadly validated by the follow-up survey and focus groups, are robust against changes in assumptions where we have other data to use. The exception to this is around the inclusion of all of the ongoing costs for external accountancy/legal advice. This more than doubles the EANCB. In the base case we have included the estimates of the costs which we think are most valid (i.e. the one-off costs), given the uncertainty around these numbers in the survey. There is also a lack of evidence around the number of beneficial owners and their costs which makes any calculation of the impacts on individuals unreliable.

## Annex D: Additional information

1. This Annex provides additional information on the problem under consideration; the policy variables discounted as part of our development of the preferred option; further detail on potential benefits to law enforcement and tax authorities; and a more detailed explanation of the theoretical and empirical framework linking trust, transparency and growth.

### (i) The problem under consideration: case studies from law enforcement and tax authorities

2. UK law enforcement and tax authorities have provided a number of examples which give an indication of the scope and scale of the misuse of companies:

- Companies are used in **Missing Trader Intra Community (MTIC) VAT fraud**<sup>123</sup>. HMRC's 2011/12 estimate of the MTIC element of the VAT tax gap is between £0.5bn and £1bn. They note that MTIC fraud reduces the amount of money available to fund essential public services and has a negative impact on the economic health of genuine businesses through unfair competition. MTIC fraud may be run by Organised Criminal Groups, many of whom have links to other serious crime such as murder or extortion.
- Further criminality may be involved through **money laundering of the proceeds of the fraud**. As an example, HMRC has one case in which a PAYE assessment of around £800k and a MTIC assessment of £3m is in place. They note that the legal owners of companies involved in such frauds (i.e. the persons named on the company's register of members) are rarely the real beneficial owners.
- The City of London Police has indicated that much of the corporate crime they investigate – such as **boiler room fraud and scams**<sup>124</sup> – involve UK companies. The Financial Services Authority (now Financial Conduct Authority (FCA)) note that victims lose an average of £20k to these scams, with as much as £200m being lost in the UK each year. They note that the biggest individual loss recorded by the police is £6m<sup>125</sup>.
- Within one month of the G8 Summit in 2013, eight people were found guilty following an investigation by North Yorkshire Police's Major Fraud Investigation Team and Her Majesty's Revenue and Customs (HMRC) which showed the use of a series of companies to launder the proceeds of a £1.28m theft from the Department for Environment, Food and Rural Affairs and attempt a £250k VAT fraud<sup>126</sup>.
- Earlier in 2013, two people were found guilty, following an investigation by the Serious Fraud Office (SFO), of using deception and forgery including the use of company structures to perpetrate a fraud worth millions of pounds<sup>127</sup>.

### (ii) Description of options considered: discounted policy variables from our preferred option

#### (1) The definition of beneficial ownership

3. Some respondents to the BIS discussion paper recommended decreasing the 25% threshold to 10%, or removing it entirely. We have opted to retain the more than 25% threshold because:

- More than 25% is the point at which an individual could have a blocking minority in certain company decision-making processes. Individuals with a lower level of interest in shares or voting rights are unlikely to have any real control over the running of the company – and if they do have effective control, they will be required to disclose their interest in line with the 'control' element of the definition;

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<sup>123</sup> MTIC VAT fraud is an organised criminal attack on the EU VAT system in which fraudulent traders acquire goods VAT free from EU Member States; charge VAT on their onward sale and go "missing" to avoid paying the VAT charged to the relevant tax authorities.

<sup>124</sup> Boiler room frauds involve the cold-calling of investors offering them worthless, overpriced or even non-existent shares, promising high returns. See the Financial Conduct Authority website, March 2013: [http://www.fsa.gov.uk/consumerinformation/scamsandswindles/investment\\_scams/boiler\\_room](http://www.fsa.gov.uk/consumerinformation/scamsandswindles/investment_scams/boiler_room)

<sup>125</sup> See Financial Conduct Authority website, March 2013: [http://www.fsa.gov.uk/consumerinformation/scamsandswindles/investment\\_scams/boiler\\_room](http://www.fsa.gov.uk/consumerinformation/scamsandswindles/investment_scams/boiler_room)

<sup>126</sup> July 2013: <http://www.northyorkshire.police.uk/11613>

<sup>127</sup> January 2013: <http://www.sfo.gov.uk/press-room/latest-press-releases/press-releases-2013/achilleas-kallakis-and-alexander-williams-jailed.aspx>

- Lowering or removing the threshold would increase the number of individuals required to be disclosed to the registry. This would increase the overall regulatory cost and burden; and
- Industry should already be familiar with the AML definition (for example, because this information is already requested by regulated entities such as banks). This should reduce familiarisation costs.

## (2) The scope of the registry

4. Some respondents to the discussion paper recommended placing all UK companies in scope, with no exemptions, on the basis that information disclosed to the market under the FCA Disclosure and Transparency Rules does not necessarily equate to beneficial ownership information. There might be a particular concern around companies listed on non-regulated markets, as they are not subject to the additional regulatory requirements that accompany listing on a regulated market.
5. However, we want to avoid duplicative requirements and minimise additional regulatory burdens and costs. As public, trading companies these companies are subject to generally higher levels of regulation and public scrutiny and we therefore judge that the risk of illicit activity is lower. Furthermore, these types of companies might be expected to have more complex and changing ownership structures, so the cost per company of obtaining beneficial ownership information might be higher; contributing to a higher overall policy cost.
6. Some respondents recommended placing all UK formed corporate and legal entities in scope. Whilst this might have the potential to enhance the overall benefits derived from the policy, these entities do not have any existing relationship with Companies House, and in many cases (e.g. credit unions, charities and building societies) are regulated by another Government agency. We do not therefore consider that these entities should come within the scope of this policy, but note that EU measures on beneficial ownership will require them to take similar action to that proposed in this IA. A separate Impact Assessment will be prepared as required.
7. On balance we think that our proposed approach is proportionate, and will not have an adverse impact on our objective to reduce crime facilitated by company misuse.
8. A few respondents to the discussion paper questioned whether small and micro companies should be exempt. The City of London Police stated that such companies are at high risk of misuse, for example, that they are the prime vehicles for boiler room fraud<sup>128</sup>. Furthermore, it has been widely identified that 'shell' companies are often the vehicle of choice for money-laundering and other crimes<sup>129</sup>, which this policy has as a stated objective to reduce. A 2012 study defines a shell company as: "*In contrast to operating or trading companies that have employees who make a product or provide a service [...] shell companies are little more than this legal identity, and hence the "shell" moniker*"<sup>130</sup>. By this very definition, we believe that the majority of shell companies would be classified as small and micro businesses.
9. Compared to public listed companies, private companies, including small and micro private companies, are also subject to fewer regulatory disclosure requirements. Exempting such companies would therefore undermine one of the core policy objectives, which is to target the misuse of companies and support law enforcement and tax authorities in their investigations. We therefore consider it imperative that small and micro companies are in scope.

## (3) How beneficial ownership information is obtained

10. Some respondents suggested that additional or alternate disclosure obligations should be placed on the legal owners of the company. In some cases this might have increased the efficacy of the policy

<sup>128</sup> A description of boiler room fraud is provided by the Financial Conduct Authority (FCA) (2013): "*Share scams are often run from 'boiler rooms' where fraudsters cold-call investors offering them worthless, overpriced or even non-existent shares. While they promise high returns, those who invest usually end up losing their money.*" <http://www.fca.org.uk/consumers/scams/investment-scams/share-fraud-and-boiler-room-scams>

<sup>129</sup> Findley, Nielson and Sharman (2012) *Global Shell Games: Testing Money Launderers' and Terrorist Financiers' Access to Shell Companies*

<sup>130</sup> *ibid*

(for example, where the company or an enforcement agency could identify the legal owner even if not the unknown beneficial owner). However, it also had a clear potential to increase cost and complexity in terms of (duplicative) disclosures being made by multiple parties. Where a company seeks information from the legal owner about a beneficial owner, the legal owner will be statutorily bound to reply. On that basis, we do not think that the potential benefit of such an approach would outweigh the costs and do not intend to pursue this approach.

#### (4) Providing and updating information in the central registry

11. The *Transparency and Trust* discussion paper sought views on replicating the information and disclosure regime which currently applies in respect of company legal owners (i.e. shareholders). This would mean that the company would maintain a register of the names, addresses and details of the beneficial owners' interest in the company. This information would be held at its registered office or other specified location and would be made publicly available on request (provided the request was made for a proper purpose). The company would then be required to provide the names and details of the interests in the company to the central registry on an annual basis, address would also be given on incorporation. This model was supported by many respondents in the business community.
12. However, other respondents were in favour of requiring more information to be collected, as outlined above. This view was shared by law enforcement agencies. Whilst the cost of collating and storing this additional information may lead to higher overall costs (both for the company and Companies House), it is considered that these will be outweighed by the potential increased benefits. This is because collating more information will reduce the occurrence of 'false positives' (i.e. where two individuals appear to be the same because, for example, they have the same name) and therefore enhance the investigative ability of enforcement agencies. The wider community may derive similar benefit from more accurately being able to identify who really owns or controls the company in question through using the public register alone. Overseas agencies may need to make fewer information requests to UK enforcement agencies because they can obtain information by searching the public record. This would also have a cost and time saving for UK authorities.
13. Some respondents to the discussion paper argued that information held by Companies House should be updated within a few days or weeks of a change occurring. This was echoed by Parliamentarians during the passage of the SBEE Act and is consistent with EU requirements on beneficial ownership. As a result, we have announced our intention to increase the frequency with which beneficial ownership information is provided to Companies House after the central registry has been in operation for around 12 months (i.e. 2017). A separate Impact Assessment looking at the costs and benefits of this change will be prepared in due course.

#### **(iii) Monetised and non-monetised costs and benefits of each option (including administrative burden): additional information on the potential benefits to law enforcement and tax authorities**

14. The SFO has indicated that: *"For criminal and confiscation investigations, Companies House data is routinely gathered during a case but especially at the outset [...] clarity of beneficial ownership of UK companies would therefore be of assistance in all, or almost all, SFO cases. In confiscation cases where UK companies feature, it would be an especially useful development as it would force defendants to either declare their interest on the record or else put up "a front man" as an undeclared nominee. If the latter options were used, and other evidence could be adduced to prove the true state of affairs, that would be powerful evidence to bring before a court and provide a deterrent effect to criminals."*
15. They add that: *"Current methods [to identify beneficial owners] include: seeking a production order for banking documents or client identification documents from professional advisers; conducting interviews and taking statements from witnesses; and seeking information from abroad under the Mutual Legal Assistance process. All of these processes can be very time consuming (especially the latter) and may need to be repeated several times if there is a long chain of ownership."*
16. The Met noted that the role of the regulated entities (e.g. banks, accountants and insurance companies) in undertaking their due diligence under the AML laws to identify beneficial owners, whilst helpful, might not always provide up to date information.

17. For example, in 2011 the Financial Services Authority (now Financial Conduct Authority) published a report<sup>131</sup> on banks management of high risk money-laundering situations. They found that: *“A third of banks in our sample failed to take adequate measures to understand and verify their customers’ ownership and control structure. And when the structure appeared complex, banks rarely questioned the rationale for the complexity and few were able to provide convincing reasons for them when challenged. At least a fifth of banks visited also failed to identify indirect beneficial owners who exercised considerable control over the customer. As a result, these banks often did not appear to know who their customer’s ultimate beneficial owner really was.”*
18. The Met therefore noted that, a priori, the proposals would not only help the investigation but would also aid the prosecution and create a deterrent effect. In particular, criminals who have provided false information can then be sanctioned accordingly, even if other offences are initially more difficult to prove.
19. HMRC has indicated that having a central source of information has the potential to help them identify individuals who have been involved in previous suspect companies and design a managed intervention programme around them to allow more focus on the highest risk – allowing them to get ahead of the risk curve rather than trying to recover losses after the event. They have also noted that identifying company beneficial ownership would allow early identification of sectors they are trying to break into with the development of appropriate risk based responses. Finally, it would facilitate the identification and restraint of assets; the identification and management of connections and associations; the identification of Phoenix traders who pose a risk to the revenue which can be mitigated by imposing securities; and the identification of disqualified directors who are acting as beneficial owners.
20. The problem of opaque corporate ownership structures is not limited to UK companies; enforcement agencies and private sector fraud investigators have indicated that cases involving the misuse of companies are often multi-jurisdictional. There might be benefits to be gained – including to the UK – from strong, coordinated, cross-border action. Law enforcement agencies have highlighted the benefit of strong UK action which might encourage other jurisdictions to take similar steps, which would have a beneficial impact on their ability to investigate UK cases involving non-UK incorporated companies. For example, HMRC has indicated that if overseas jurisdictions were to implement a central registry of company beneficial ownership information, they could potentially identify tax evasion committed by UK citizens, thereby increasing the total tax take of the UK. Although HMRC cannot quantify this amount, they anticipate it to be significant. This highlights the potential cross-jurisdictional benefits to be derived from this policy. Nevertheless, given the intangible and indirect nature of this benefit, we have not included this in our assessment.
21. The OECD reported<sup>132</sup> that: *“Almost every economic crime involves the misuse of corporate entities – money launderers exploit cash-based businesses and other legal vehicles to disguise the source of their illicit gains, bribe-givers and recipients conduct their illicit transactions through bank accounts opened under the names of corporations and foundations, and individuals hide or shield their wealth from tax authorities and other creditors through trusts and partnerships.”*
22. They also note that: *“It is extremely difficult to quantify with any precision the extent of misuse of corporate vehicles for illicit purposes. Nonetheless, a number of reports and surveys have concluded that corporate vehicles are used extensively in criminal activities [...] Tax authorities in OECD Member countries have also expressed concern that individuals using corporate entities to hide their assets and activities in order to escape taxes legally due will likely grow. In addition, the United Nations has noted that: “the principal forms of abuse of secrecy have shifted from individual bank accounts to corporate bank accounts and then to [...] other corporate forms that can be purchased readily without even the modest initial and ongoing due diligence that is exercised in the banking sector” [...] a critical factor in misusing corporate vehicles is the potential for anonymity.”*

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<sup>131</sup> FSA (2011): *Banks’ management of high money-laundering risk situations*

<sup>132</sup> OECD (2001): *Behind the Corporate Veil: Using Corporate entities for Illicit Purposes*

23. The EU has noted that: “*The absence of public information about the beneficial owner is seen by some stakeholders as hindering the practical implementation of the requirements. [...] The European Commission’s Internal Security Strategy has also highlighted this issue and suggested, in the light of discussions with its international partners in the Financial Action Task Force, revising the EU Anti-Money Laundering legislation to enhance the transparency of legal persons [...]*”<sup>133</sup>.

24. The FATF recommendations 2012 refer to: “[a] *lack of transparency about the ownership and control of legal persons [...] makes those instruments vulnerable to misuse by criminals and terrorists. The FATF has strengthened transparency requirements in these areas. This means requiring that there is reliable information available about the beneficial ownership and control of companies [...] Measures to improve transparency, implemented on a global basis, will make it harder for criminals and terrorists to conceal their activities.*”

**(iv) Benefits: the theoretical and empirical framework linking trust, transparency and growth**

25. A theoretical framework connecting transaction costs with trust was set out by Bromiley and Cummings (1995) who described a typical agency problem, between a shareholder (principal) who depends on the actions of the company board (agent). They explained, drawing on earlier findings, how a lack of trust can feed into higher transaction costs<sup>134</sup>. This agency problem and the associated complexity related to trust can impact on transaction costs in other settings. Empirically this has received support from Dyer and Chu (2003)<sup>135</sup> who investigated the relationship between 344 buyers and suppliers in the automotive industry of the US, Japan and Korea. Dyer and Cho concluded that transaction costs<sup>136</sup> were five times higher for the least trusted supplier.

26. There is also a known link between overall economic growth and trust<sup>137</sup>, with the literature commonly identifying a significant positive relationship between the two. This emerges because trust motivates investment, innovation and more broadly entrepreneurship<sup>138</sup>. To test the hypothesis that trust reduces transaction costs and therefore enhances growth at a national level, the empirical literature commonly analyses cross-country samples to assess how far countries with higher levels of trust have a higher rate of economic growth. Knack and Keefer (1996)<sup>139</sup> initiated this strand of the literature, finding that a 10 percentage point increase in trust, as measured by the World Values Survey (WVS), is associated with a 0.8 percentage point increase in growth. Zak and Knack (2001)<sup>140</sup> later extended this analysis by adding 12 countries to the dataset - again the relationship between trust and economic growth was significant and positive and a 10 percentage point increase in trust was associated with a 0.7 percentage point increase in growth.

27. The literature has built upon the two seminal papers by Knack and Keefer (1996) and Zak and Knack (2001) by testing their robustness and re-analysing the data. Beugelsdijk et al (2004)<sup>141</sup> find that the Zak and Knack (2001) study had highly robust trust coefficients in terms of significance and magnitude. However, they argued that the relative importance of trust in the study is somewhat affected by which countries are included in the sample and the factors that the regression controls

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<sup>133</sup> REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL on the application of Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, 2012

<sup>134</sup> Bromiley, P. & Cummings, L.L. (1995): *Transactions costs in organizations with trust*. Research on Negotiations in Organizations, Vol. 5: 219–47, set up the theoretical framework, which connected transaction costs with trust. This was based on the findings of Williamson O.E. (1985): *The Economic Institutions of Capitalism* which formally founded the New Institutional school of economics. However, the literature is somewhat ambiguous as to the strength of the link between trust and transaction costs.

<sup>135</sup> Dyer J.H. and Chu W. (2003): *The role of trustworthiness in reducing transaction costs and improving performance*. Organisation Science, vol. 14 no 1, pp57-68

<sup>136</sup> North, D.C. (1990): *Institutions, institutional change and economic performance*, defines transaction costs as ‘*the cost of measuring the valuable attributes of what is being exchanged and the costs of protecting rights and policing and enforcing agreements.*’ Transaction costs come in the form of searching for a contract and relevant information; bargaining and decision making relating to that contract; and policing and enforcing the contract.

<sup>137</sup> The literature commonly considers trust in a general sense rather than specifically looking at trust in the business environment. A frequently used source is the World Values Survey (WVS). This is a cross-country social survey of beliefs and values, which asks ‘*do you think people can generally be trusted?*’. Although the WVS is not directly related to the level of trust in the business environment, as noted by Beugelsdijk (2006) it is strongly correlated with the effectiveness of institutions, which includes industry/business as an institution. We can therefore expect trust to be a good proxy more specifically for trust in the business environment.

<sup>138</sup> However, the literature must carefully control for reverse causality, i.e. how far high growth countries are generally more trusting.

<sup>139</sup> Knack, Stephen and Philip Keefer, (1996): *Does social capital have an economic payoff?: A cross-country investigation*, The Quarterly Journal of Economics, 112(4), pp. 1251

<sup>140</sup> Zak, P.J. and Knack, S. (2001): *Trust and growth*, Economic Journal, 111, 295–321.

<sup>141</sup> Beugelsdijk, S., de Groot, H.L.F. & van Schaik, A. (2002): *Trust and Economic Growth: A robustness analysis*, Oxford Economic Papers 56 (2004), 118–134

- for. More recently Horváth (2013)<sup>142</sup>, however, found interpersonal trust to be a “*robust determinant of long-term economic development*” in a study of 50 countries. Indeed, Horváth disagreed with the findings of Beugelsdijk et al (2004) that the link between trust and growth is sensitive to the factors included in the model.
28. Analysis of US States by Dincer and Uslaner (2010)<sup>143</sup> found a similar (though slightly weaker) relationship between trust and growth – a 10 percentage point increase in trust being associated with a 0.5 percentage point increase in the growth rate. This highlights that the relationship still exists in developed countries or jurisdictions where the rule of law is well established (where one might otherwise have expected it to be restricted to jurisdictions with weaker institutional infrastructure and greater reliance on knowing and trusting business partners).
  29. The relationship between growth and trust is therefore a developing strand in the literature and there are some continuing points of debate around the data used. The empirical studies are often reliant on the World Values Survey (WVS), which asks the general question: “*do you think people can be trusted?*” Comparing responses over time, as Beugelsdijk (2006)<sup>144</sup> comments, might indicate more of a change in a population’s honesty, attitudes or information rather than their behaviour. However, there are few alternative international measures for trust, which in itself is challenging to measure.
  30. The literature does not generally analyse the mechanisms through which trust affects growth. As noted by Dincer and Uslaner (2010), one might expect trust to affect growth via the main growth drivers. To elaborate, one can envisage that individuals in countries with low levels of trust might be more hesitant in engaging in entrepreneurial activity, for fear of protecting their contractual rights, and a lack of innovation and/or investment will certainly impede growth.
  31. Two notable exceptions are Bjørnskov (2012)<sup>145</sup> and Botazzi et al (2010)<sup>146</sup>, which both examine mechanisms through which trust influences growth. Using cross-country data, Bjørnskov (2012) shows that a lack of trust limits the level of schooling, which in turn limits the investment rate and ultimately economic growth. Botazzi et al (2010) identify the strength of the relationship between trust and investment decisions in European venture capital markets. The theoretical mechanism identified by Botazzi is also similar to that found by Guiso et al (2008)<sup>147</sup>, who look at stock market participation. Essentially, trust has an impact on an investor’s perception of brokers and intermediaries, and a lack of trust thereby raises transaction costs and reduces the investment rate.
  32. Indeed, during discussions with business at a series of focus groups, they largely validated this view: “*If a company knew who was behind the company they were making a deal with, it could save them from making bad decisions*”.
  33. Moreover, one business commented that *Transparency and Trust* might encourage Foreign Direct Investment, if the package makes it easier for overseas companies to see with whom they are dealing.
  34. In and of itself, trust is not likely to drive growth, but it certainly feeds into stability and certain economic systems which are key to economic activity. In terms of its relative importance as a factor underpinning growth, Whiteley (2000)<sup>148</sup> found evidence suggesting that social capital, defined as the extent to which people are prepared to co-operate based on interpersonal trust, has a significant impact on growth, at least as strong as education or human capital.

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142 Horváth, R. (2013): *Does trust promote growth?*, Journal of Comparative Economics, Elsevier, vol. 41(3), pages 777-788

143 Dincer and Uslaner (2010): *Trust and Growth* Public Choice (2010) 142: 59–67

144 Beugelsdijk, S. (2006): *A note on the theory and measurement of trust in explaining differences in economic growth*. Cambridge Journal of Economics, 30, 371–387

145 Bjørnskov (2012): *How Does Social Trust Affect Economic Growth?* Southern Economic Journal, Working Paper 06-2

146 Botazzi, L., Da Rin, M. and Hellman, T. (2010): *The importance of trust for investment* NBER Working Papers 16923

147 Guiso, L., Sapienza, P. and Zingales, L. (2008): *Trusting the Stock Market*. The Journal of Finance, Vol 63, Issue 6, pp2557-2600

148 Whiteley, P. (2000): *Economic Growth and Social Capital*, Political Studies 48, 443-466