



HM Treasury

Transposition of the Fifth Money Laundering Directive: consultation

April 2019

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Chapter 1

Introduction

Summary

- 1.1 This chapter sets out the context in which this consultation takes place. It provides relevant background on money laundering and terrorist financing (ML/TF), including their significance from the perspectives of the UK, the European Union (EU) and the Financial Action Task Force (FATF). It also covers the government's approach and plans for transposition of the Fifth Money Laundering Directive (5MLD).

The subject of this consultation

- 1.2 This consultation invites views and evidence on the steps that the government proposes to take to meet the UK's obligation to transpose the directive (EU) 2018/843 (5MLD) into national law. It also seeks views and evidence on the potential costs and benefits of the changes considered. Where EU Member States are given the discretion to make decisions on certain aspects of 5MLD, this consultation seeks your views on the government's proposals and issues to be addressed.
- 1.3 A full list of acronyms used throughout this consultation can be found at Annex A and a list of consultation questions can be found at Annex B.

Background on money laundering and terrorist financing regulation

- 1.4 Money laundering includes how criminals change money and other assets into clean money or assets that have no obvious link to their criminal origins. Money laundering can undermine the integrity and stability of our financial markets and institutions. It is a global problem, and represents a significant threat to the UK's national security. Money laundering is a key enabler of serious and organised crime, which costs the UK at least £37 billion every year.
- 1.5 Terrorist financing involves dealing with money or property that you know or have reasonable cause to suspect may be used for terrorism. There is an overlap between money laundering and terrorist financing, as both criminals and terrorists use similar methods to store and move funds, but the motive for generating and moving funds differs. The UK has a comprehensive anti-money laundering and counter-terrorist financing (AML/CTF) regime, and the government is committed to ensuring that the UK's financial system is effectively able to combat ML/TF.

- 1.6 The international AML/CTF standards are set by the FATF, an inter-governmental body which promotes effective implementation of measures for combating ML/TF along with other threats to the integrity of the international financial system. The Treasury leads the UK delegation to FATF. International standards ensure that there are controls and procedures in place to combat the risk of ML/TF across several sectors. These sectors are currently covered by EU measures through the Fourth Money Laundering Directive, the Funds Transfer regulation and the Fifth Money Laundering Directive.

The national risk assessment

- 1.7 The Treasury and Home Office jointly published the second comprehensive assessment of the money laundering and terrorist financing risks faced by the UK on 26 October 2017.¹ The 2017 National Risk Assessment (NRA) sets out the key money laundering and terrorist financing risks for the UK, how these changed since the UK's first NRA was published in 2015, and the actions taken since 2015 to address these risks.
- 1.8 The findings in the NRA are helping to shape the government's response to money laundering and terrorist financing, ensuring that the UK's AML/CTF regime remains robust, proportionate and responsive to emerging threats.

The Fifth Money Laundering Directive (5MLD)

- 1.9 The Fourth Money Laundering Directive² (4MLD) was published in the EU Official Journal on 5 June 2015, and gave effect to the updated FATF standards³ after they were significantly updated in 2012. 4MLD was predominantly transposed into UK law through the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) regulations 2017⁴ (MLRs or 'the Regulations'), for which the Treasury is responsible, and the Proceeds of Crime Act 2002⁵ (POCA) for which the Home Office is responsible. The MLRs set out an efficient and comprehensive legal framework for addressing and mitigating the risks related to money laundering and terrorist financing.
- 1.10 Following the European Commission's release, in February 2016, of an Action Plan⁶ for strengthening the fight against terrorist financing, EU Member States agreed to revisit some areas of 4MLD to further strengthen transparency and counter-terrorist provisions. This resulted in the publication of the Directive (EU) 2018/843 (5MLD) amending Directive (EU) 2015/849 (4MLD) on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU. 5MLD⁷ was published in the EU Official

¹ <https://www.gov.uk/government/publications/national-risk-assessment-of-money-laundering-and-terrorist-financing-2017>

² https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:JOL_2015_141_R_0003&from=EN

³ http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf

⁴ http://www.legislation.gov.uk/ukSJ/2017/692/pdfs/ukSJ_20170692_en.pdf

⁵ http://www.legislation.gov.uk/ukpga/2002/29/pdfs/ukpga_20020029_en.pdf

⁶ http://europa.eu/rapid/press-release_IP-16-202_en.htm

⁷ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018L0843>

Journal on 19 June 2018 and entered into force on 10 July 2018. 5MLD contains amendments to 4MLD which will improve transparency and the existing preventative framework to more effectively counter ML/TF across the EU.

UK approach to implementation of 5MLD

- 1.11 In March 2018, the UK government and the European Commission agreed the terms of an implementation period. This was included in the Withdrawal Agreement, which will need to be approved by UK parliament and the European Parliament in order to take effect. In implementing 5MLD, the government is catering for the scenario where an implementation period is in place after the UK leaves the EU. During this implementation period common rules will remain in place, meaning that EU law will continue to have effect in the UK in the same way as now until the end of an agreed implementation period. This would require the UK to implement 5MLD by January 2020. The UK played a significant role in the negotiation of 5MLD and shares the objectives which it seeks to achieve on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.
- 1.12 This consultation will play a key role in deciding how best to transpose 5MLD into UK law in a way that appropriately balances the need for a proportionate approach which manages the burden on business, with the need for regulated businesses ('obliged entities') to actively discourage ML/TF activity. (Note that where this consultation uses the terms 'obliged entities' or 'relevant persons', stakeholders should take this to mean those individuals or businesses that are supervised by a UK supervisory authority for compliance with obligations established by 4MLD or 5MLD.) The objective of transposition is to ensure that the UK's AML/CTF regime is kept up to date, effective and proportionate.
- 1.13 The consultation will provide an opportunity for comments, evidence and views from stakeholders. Responses to this consultation will then be used to inform final government decisions on transposition. The Treasury will explain why it has reached these policy decisions in the government response to this consultation. The government will only 'gold-plate' (go further than) the provisions in 5MLD where there is good evidence that a material ML/TF risk exists that must be addressed. The government intends that the new provisions will come into force in national law by 10 January 2020, in line with Article 4 of 5MLD.

Responding to the consultation

- 1.14 The government welcomes your views in response to the questions posed, and how the proposed changes would impact the AML/CTF regime in the UK. The government encourages stakeholders to provide as much evidence as possible to help inform the government's response to the transposition of 5MLD. This will help ensure evidence-based policy decisions.
- 1.15 The government will be running a series of events during the consultation period where stakeholders will be given the opportunity to take part in

interactive discussions about the proposals and issues in this consultation document.

- 1.16 Email responses should be sent to:

Anti-MoneyLaunderingBranch@hmtreasury.gov.uk

- 1.17 Questions or enquiries in relation to this consultation should also be sent to the above email address. Please include the words 'Consultation Views' or 'Consultation Enquiry' (as appropriate) in your email subject.

- 1.18 Written responses should be sent to:

Consultation on the Transposition of 5MLD
Sanctions and Illicit Finance Team (2/27)
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
London

Timetable

- 1.19 The closing date for comments to be submitted is 10 June 2019.
- 1.20 The requirements of 5MLD must come into effect through national law by 10 January 2020 in line with Article 4 of the 5MLD.

HM Treasury consultations – processing of personal data

This notice sets out how HM Treasury will use your personal data for the purposes of the Consultation on the Transposition of the Fifth Money Laundering Directive and explains your rights under the General Data Protection regulation (GDPR) and the Data Protection Act 2018 (DPA).

Your data (data subject categories)

- 1.21 The personal information relates to you as either a member of the public, parliamentarian, or representative of an organisation or company.

The data we collect (data categories)

- 1.22 Information may include your name, address, email address, job title, and employer, as well as your opinions. It is possible that you will volunteer additional identifying information about yourself or third parties.

Legal basis of processing

- 1.23 The processing is necessary for the performance of a task carried out in the public interest or in the exercise of official authority vested in HM Treasury. For the purpose of this consultation the task is consulting on departmental policies or proposals or obtaining opinion data in order to develop effective government policies.

Special categories data

- 1.24 Any of the categories of special category data may be processed if such data is volunteered by the respondent.

Legal basis for processing special category data

- 1.25 Where special category data is volunteered by you (the data subject), the legal basis relied upon for processing it is: the processing is necessary for reasons of substantial public interest for the exercise of a function of the Crown, a Minister of the Crown, or a government department.
- 1.26 This function is consulting on departmental policies or proposals, or obtaining opinion data, to develop effective policies.

Purpose

- 1.27 The personal information is processed for the purpose of obtaining the opinions of members of the public and representatives of organisations and companies, about departmental policies, proposals, or generally to obtain public opinion data on an issue of public interest.

Who we share your responses with

- 1.28 Information provided in response to a consultation may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 2018 (DPA) and the Environmental Information regulations 2004 (EIR).
- 1.29 If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence.
- 1.30 In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury.
- 1.31 Where someone submits special category personal data or personal data about third parties, we will endeavour to delete that data before publication takes place.
- 1.32 Where information about respondents is not published, it may be shared with officials within other public bodies involved in this consultation process to assist us in developing the policies to which it relates. Examples of these public bodies appear at: <https://www.gov.uk/government/organisations>.
- 1.33 As the personal information is stored on our IT infrastructure, it will be accessible to our IT contractor, NTT. NTT will only process this data for our purposes and in fulfilment with the contractual obligations they have with us.

How long we will hold your data (retention)

- 1.34 Personal information in responses to consultations will generally be published and therefore retained indefinitely as a historic record under the Public Records Act 1958.
- 1.35 Personal information in responses that is not published will be retained for three calendar years after the consultation has concluded.

Your rights

- You have the right to request information about how your personal data are processed and to request a copy of that personal data.
- You have the right to request that any inaccuracies in your personal data are rectified without delay.
- You have the right to request that your personal data are erased if there is no longer a justification for them to be processed.
- You have the right, in certain circumstances (for example, where accuracy is contested), to request that the processing of your personal data is restricted.
- You have the right to object to the processing of your personal data where it is processed for direct marketing purposes.
- You have the right to data portability, which allows your data to be copied or transferred from one IT environment to another.

How to submit a Data Subject Access Request (DSAR)

- 1.36 To request access to personal data that HM Treasury holds about you, contact:

HM Treasury Data Protection Unit
G11 Orange
1 Horse Guards Road
London
SW1A 2HQ
dsar@hmtreasury.gov.uk

Complaints

- 1.37 If you have any concerns about the use of your personal data, please contact us via this mailbox: privacy@hmtreasury.gov.uk.
- 1.38 If we are unable to address your concerns to your satisfaction, you can make a complaint to the Information Commissioner, the UK's independent regulator for data protection. The Information Commissioner can be contacted at:

Information Commissioner's Office
Wycliffe House
Water Lane
Wilmslow

Cheshire
SK9 5AF
0303 123 1113

casework@ico.org.uk

- 1.39 Any complaint to the Information Commissioner is without prejudice to your right to seek redress through the courts.

Contact details

- 1.40 The data controller for any personal data collected as part of this consultation is HM Treasury, the contact details for which are:

HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
London
020 7270 5000
public.enquiries@hmtreasury.gov.uk

- 1.41 The contact details for HM Treasury's Data Protection Officer (DPO) are:

The Data Protection Officer
Corporate Governance and Risk Assurance Team
Area 2/15
1 Horse Guards Road
London
SW1A 2HQ
London
privacy@hmtreasury.gov.uk

Chapter 2

New obliged entities

Expanding the scope in relation to tax matters

Summary

- 2.1 Auditors, accountants and tax advisers are already in scope of the MLRs, which includes bookkeepers, payroll service providers, repayment agents and some customs practitioners and virtual assistants under the definition of an accountant, provided in HMRC guidance.¹ 5MLD expands the scope of obliged entities in relation to tax matters.

What changes does 5MLD introduce?

- 2.2 Article 2 of 4MLD as amended expands the scope of obliged entities to include any other person that undertakes to provide, directly or by means of other persons to which that other person is related, material aid, assistance or advice on tax matters as principal business or professional activity. Therefore, the government will expand the definition of “tax advisor” in the MLRs to include firms and sole practitioners who by way of business provide, directly or by way of arrangement with other persons, material aid, assistance or advice about the tax affairs of other persons.

Box 2.A: Expanding the definition of ‘tax advisor’

- 1 What additional activities should be caught within this amendment?
- 2 In your view, what will be the impact of expanding the definition of tax advisor? Please justify your answer and specify, where possible, the costs and benefits of this change.

Letting agents

Summary

- 2.3 Estate agents are already in scope of the MLRs, which means a firm or sole practitioner who, or whose employees, carry out estate agency work when such work is being carried out. Estate agency work should be read in accordance with section 1 of the Estate Agents Act 1979 (as modified by the regulations).

¹ <https://www.gov.uk/guidance/money-laundering-regulations-accountancy-service-provider-registration>

- 2.4 The main categories of estate agency services captured by this definition, and so covered by the MLRs, are residential and commercial estate agency services, property or land auctioneering services, and relocation agency or property finder services. The services covered by the regulations include disposing of or acquiring an estate or interest in land outside the UK where that estate or interest is capable of being owned or held as a separate interest. Estate agents based in the UK who deal with overseas property are covered, as well as estate agents based abroad if they are doing UK based estate agency activity. The MLRs apply to those carrying out a number of services which come under the estate agency business, for example, in the purchase or sale of property as well as the sale or purchase of an interest in land i.e. as a property owner and leaseholder. The MLRs apply in relation to both the buyer and the seller of property.
- 2.5 In the UK, lettings agents are only within scope of the MLRs where they carry out estate agency activity. In these circumstances, letting agency activities of such firms are not within the scope of the MLRs. However, 5MLD expands the scope of obliged entities within the property sector to include the letting agency sector for high value transactions with a monthly rent of EUR 10,000 or more. As part of this, the government will need to decide who should be within scope of the regulations, at what point customer due diligence is completed, as well as who should supervise letting agents. This chapter seeks your views on the above changes and what they could mean in practice.

What changes does 5MLD introduce?

- 2.6 Article 2 of 4MLD as amended states that “estate agents, including when acting as intermediaries in the letting of immovable property, but only in relation to transactions for which the monthly rent amounts to EUR 10 000 or more” are included as obliged entities.

Potential options

Who should be included within the scope of the term ‘letting agents’

- 2.7 We propose to define a letting agent as a firm or sole practitioner who, or whose employees, carry out letting agency work. There are several activities that lettings agencies carry out. For example, introductory services, lets only, rent collection, social housing, commercial lettings, full property management, block management etc. The government would welcome views on the definition, what other types of lettings activity exist and whether all of these activities should be viewed as coming within the meaning of letting agency work, or whether there should be exemptions. For example, we would consider exempting legal professionals when conducting legal activity on behalf of a client, provided they are not also instructed in relation to other letting agency work by that client. Further, online letting agents would be within scope of the definition.
- 2.8 It has previously been noted that the private landlord sector would not be covered by proposals and that this would leave a significant gap in coverage, as there would be no oversight of an agentless business relationship and no

requirement to have policies or procedures in place to mitigate the risk of money laundering and terrorist financing in that relationship. The government invites views and evidence on the risks attached to landlord-tenant relationships in comparison to agent-landlord-tenant relationships.

On whom is CDD done and at what point

- 2.9 The government invites views on how customer due diligence (CDD) should be carried out for letting agents. Letting agents will be required to conduct CDD on their customers. Therefore, it is important to be clear who the customer is. Landlords will likely be the main customers for most lettings agents, though in some circumstances agents have landlords and tenants as their customers, such as when the letting agent acts as an intermediary. The government invites views on the impact for letting agents of carrying out CDD measures on both parties to the rental agreement (i.e. on landlords and tenants) in a transaction where the agents act as intermediaries.
- 2.10 The government would also welcome views on when CDD would need to be carried out by a letting agent (whether in relation to the landlord, the tenant, or both). CDD must be completed before a business relationship is established, which the government expects will be – at the latest – before the first deposit or rent payment is made above the relevant threshold. In practice, therefore, CDD would need to occur before the final rental or letting agreement is concluded. However, where an agreement is signed with, or fees paid to, an agent beforehand, it is likely that this earlier stage will be the point at which a business relationship is established. The government would welcome views on how the CDD duty can most practically be complied with if the agent enters a business relationship before the amount of rent has been agreed. For example, agents might need to conduct CDD in all cases where there is a realistic possibility that the final rent will be above the threshold.
- 2.11 As an alternative to applying CDD measures before the establishment of a business relationship, the regulations could specify that letting agents must apply CDD measures if the agent acts in relation to a transaction for which the monthly rent amounts to EUR 10,000 or more. This would be similar to the way in which the MLRs apply to high value dealers, although the agent may often not be carrying out the transaction itself. The agent would need to carry out CDD before the transaction takes place. The government would welcome views on how we should consider at what point the “transaction” takes place, and what the relevant transaction is – payment of a deposit, first rent payment etc. There may be fewer formalities in lettings, compared to sales of land, and it will be necessary to identify the most practical and well-suited trigger for completing CDD. Therefore, the government welcomes views on how letting agents will be brought into scope of the CDD requirements in the MLRs.

Evidence and scope of the change – EUR 10,000 threshold

- 2.12 Letting agents may be an attractive target for criminals seeking to disguise or hide the proceeds of crime, particularly as it can be a cash-intensive business where agents are more likely to handle rents and deposits and may not always meet landlords face-to-face. Risks around letting agencies being

wholly owned or controlled by a criminal group have also been identified. In the 4MLD consultation, respondents stated that capital transactions are riskier than lettings as they allow integration of large sums of criminal money into the financial system, while respondents also noted that lettings are not a quick or effective method of laundering money, given the time it would take to launder significant sums and because there is an extensive audit trail. Lettings are considered by some as not a lasting store of value and so are an ineffective method of laundering money.

- 2.13 There is a view among some stakeholders that the EUR 10,000 threshold is too high and that it would only cover a small percentage of the rental market. The government would welcome views on the current material risks within the sector and what this might mean for potentially lowering the EUR 10,000 threshold. The government is additionally aware that lowering the threshold would potentially enable a greater number of letting agents to take advantage of the simplified customer due diligence requirements available for pooled client accounts, which are bank accounts where a business holds money on behalf of its clients. Issues regarding pooled client accounts are detailed in Chapter 13.

Supervision of letting agents

- 2.14 The UK AML regime has 25 supervisors, a mixture of self-regulatory bodies and statutory supervisors. They are a highly diverse group including large global professional bodies, smaller professional and representative bodies, as well as public sector organisations. The Treasury is responsible for the appointment and removal of supervisors – by amending the MLRs.
- 2.15 The government would welcome views on who should supervise lettings agents now within scope of 5MLD. The Treasury considers HMRC as a supervisor suited to the role of regulating letting agents, given HMRC is the primary supervisor for this sector. The Treasury will, however, consider appointing self-regulatory body supervisors of letting agents, similar to estate agents. Professional bodies can apply to the Office for Professional Body Anti-Money Laundering Supervision (OPBAS) to become supervisors. If implemented in practice, this would mean that those businesses that were members of eligible estate agency or letting agency professional bodies could be supervised by those bodies for AML/CTF purposes, rather than by HMRC who is the current supervisor of letting agents that carry out estate agency business. HMRC would remain the supervisor of relevant letting agency businesses that were not members of those bodies, or were not otherwise supervised by a UK AML supervisor. This would mean adding another supervisory body to an already crowded landscape which may create challenges in engagement for law enforcement. The government welcomes views on professional bodies in the sector who would be appropriate supervisors and maintaining the status quo through appointing HMRC as the main supervisor, in line with its current supervision of estate agents.
- 2.16 Under regulation 26 of the MLRs, supervisors must approve beneficial owners, officers or managers of estate agency firms, and estate agents who are sole practitioners. This is to prevent criminals, or their associates, with relevant unspent convictions from holding a management function in, or

being the beneficial owners of estate agents. The government asks for views on whether this should be extended to include letting agents, and if so, whether it should be extended to all letting agents or only those to whom the CDD obligations apply (as above).

Box 2.B: Letting agents

- 3 What are your views on the ML/TF risks within the letting agents sector? What are your views on the risks in the private landlord sector, especially comparing landlord-tenant to agent-landlord-tenant relationships? Please explain your reasons and provide evidence where possible.
- 4 What other types of lettings activity exist? What activities do you think should be included or excluded in the definition of letting agency activity? Please explain your reasons and provide evidence where possible.
- 5 Should the government choose a monthly rent threshold lower than EUR 10,000 for letting agents? What would the impact be, including costs and benefits, of a lower threshold? Should the threshold be set in euros or sterling? Please explain your reasoning.
- 6 Do letting agents carry out CDD checks on both contracting parties (tenants and landlords) when acting as estate agents in a transaction?
- 7 The government would welcome views on whom CDD should be carried out and by what point? Should CDD be carried out before a relevant transaction takes place (if so, what transaction) or before a business relationship has been established? Please explain your reasoning.
- 8 The default supervisor of relevant letting agents will be HMRC, but professional bodies can apply to OPBAS to be a professional body supervisor. Are you a member of a professional body, and would this body be an appropriate supervisor? If this body would be an appropriate supervisor, please state which professional body you are referring to.
- 9 What do you see as the main monetary and non-monetary costs to your business of complying with the MLRs (e.g. carrying out CDD, training staff etc.)? Please provide figures (even if estimates) if possible.
- 10 Should the government extend approval checks under regulation 26 of the MLRs to letting agents? Should there be a “transition period” to give the supervisor and businesses time to complete approval checks of the appropriate existing persons (beneficial owners, managers and officers)?

11 Is there anything else that government should consider in relation to including letting agents under the MLRs?

Cryptoassets

Summary

- 2.17 Cryptoassets have the potential to offer benefits to firms and consumers, but they also have qualities which make them appealing for abuse, namely their pseudo-anonymous nature, their accessibility online and their global reach. These features make it possible to obfuscate the source and purpose of funds, making them more attractive for criminals, and may enable the use of cryptoassets for money laundering and terrorist financing purposes. They can also act as a method for payments between criminals, be used for the purchase of illicit tools and services online, and be exploited for other criminal activity such as fraud and cyber-theft. 5MLD introduces requirements for cryptoasset exchanges and custodian wallet providers for the first time. Further, updates to the Financial Action Task Force's (FATF) standards now oblige its members to regulate cryptoassets and cryptoasset service providers. These obligations go further than the 5MLD requirements, and will inform the UK's approach to consulting on regulation in this space.
- 2.18 The UK will not tolerate the use of cryptoassets in illicit activity, and the government is keen to fully address money laundering and terrorist financing risks they pose through regulation. The government has worked closely with the FCA and Bank of England through the Cryptoassets Taskforce to develop a comprehensive policy and regulatory approach to cryptoassets and distributed ledger technology. The Taskforce's final report² highlighted evidence of growing risks from the use of cryptoassets for illicit activity, in addition to risks to consumers and markets. It concluded that the most immediate priority for the government and financial regulators is to mitigate these risks.
- 2.19 This chapter explains what controls cryptoasset exchanges and custodian wallet providers will have to put in place when they are covered by the MLRs, and seeks evidence from interested stakeholders on our proposed approach to transposing 5MLD in light of the increasing ML/TF risks associated with cryptoassets. This chapter also seeks further evidence on areas on which the UK may wish to go further than 5MLD to protect consumers and markets from illicit activity. It will also gather views from interested stakeholders on the costs businesses will face as a result of this regulation.

Definitions of cryptoassets

- 2.20 5MLD defines virtual currencies as "a digital representation of value that is not issued or guaranteed by a central bank or a public authority, is not

²https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/752070/cryptoassets_taskforce_final_report_final_web.pdf

necessarily attached to a legally established currency and does not possess a legal status of currency or money, but is accepted by natural or legal persons as a means of exchange and which can be transferred, stored and traded electronically”.

- 2.21 The Cryptoasset Taskforce defined a cryptoasset as “a cryptographically secured digital representation of value or contractual rights that uses some type of distributed ledger technology and can be transferred, stored or traded electronically”. We will use the term “cryptoassets” throughout this chapter to refer to assets that are otherwise known as virtual currencies in 5MLD, or as virtual assets by FATF, or as any other variant elsewhere (e.g. cryptocurrency, digital currency, digital asset, etc.).
- 2.22 The Cryptoassets Taskforce established a framework of three broad types of cryptoassets: exchange tokens, security tokens, and utility tokens.
- exchange tokens – which are often referred to as ‘cryptocurrencies’ such as Bitcoin, Litecoin and equivalents. They utilise a DLT platform and are not issued or backed by a central bank or other central body. They do not provide the types of rights or access provided by security or utility tokens, but are used as a means of exchange or for investment.
 - security tokens – which amount to a ‘specified investment’ as set out in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO). These may provide rights such as ownership, repayment of a specific sum of money, or entitlement to a share in future profits. They may also be transferable securities or financial instruments under the EU’s Markets in Financial Instruments Directive II (MiFID II).
 - utility tokens – which can be redeemed for access to a specific product or service that is typically provided using a DLT platform.
- 2.23 The government considers that all relevant activity involving all three types of cryptoassets should be captured in AML/CTF regulation, and seeks views on this approach. The government seeks views on whether the 5MLD definition of “virtual currencies” encompasses all three types of cryptoassets identified by the Taskforce, or whether this definition may need to be amended in order to capture these three types. Additionally, the government seeks views on whether there are assets likely to be considered a virtual currency or cryptoasset which falls within the 5MLD definition but not within the Taskforce’s framework.
- 2.24 5MLD defines cryptoasset exchanges as “providers engaged in exchange services between cryptoassets and fiat currencies”. However, we seek to consult on also regulating providers engaged in alternative exchange services, in addition to purely fiat-to-crypto exchange.
- 2.25 5MLD defines a custodian wallet provider as “an entity that provides services to safeguard private cryptographic keys on behalf of its customers, to hold, store and transfer virtual currencies”.

Mitigating AML risks in cryptoassets

- 2.26 The risk profile of cryptoassets is rapidly changing, which reflects the fast-moving nature of the sector itself. The 2015 and 2017 National Risk

Assessments of Money Laundering and Terrorist Financing (NRAs) both assessed the risks associated with cryptoassets to be relatively low for both money laundering and terrorist financing. This is because there was little evidence of them being used to launder large amounts at high volume; nonetheless, the 2017 report noted this would likely increase. Since the 2017 NRA, UK law enforcement authorities have increasingly identified cases of cryptoassets being used to launder illicit proceeds of non-cyber crime.

- 2.27 Like conventional assets, cryptoassets are vulnerable to being exploited for money laundering and terrorist financing purposes. Certain features specific to cryptoassets make them particularly attractive to criminals, and the risks of cryptoassets being used in money laundering (and other criminal activities such as fraud, scams and cyber-theft) are expected to grow as cryptoassets become increasingly accessible and easy to use. Features that make cryptoassets attractive for criminal activity include their accessibility online, their cross-border reach and their pseudo-anonymous nature.
- 2.28 Currently, cryptoassets pose the greatest threat from an illicit finance perspective at the point of exchange; it is at this point where the value can be realised, and can be used to further obfuscate their true source. This is why, much like fiat-to-cryptoasset exchange, the functionality of cryptoasset ATMs, the privacy features of some coins, peer-to-peer exchange facilities, and crypto-to-crypto exchange facilities also fuel the risk of illicit activity associated with cryptoassets. Government intelligence reports suggest these services are being exploited for illicit activity. Cryptoasset exchanges and wallet providers are not currently required within regulations (subject to their business model) to identify their customers, monitor transactions or report suspicious activity, making anonymous transactions possible. In addition, the early stage of development of the market results in varying systems and controls across firms to mitigate these risks.

The government's response & international response

- 2.29 As part of its overall approach to cryptoassets and the transposition of 5MLD, the government is developing a comprehensive and robust response to illicit activity risks. This follows the work of the HM Treasury-Financial Conduct Authority-Bank of England Cryptoassets Taskforce, which assessed the potential risks and benefits of cryptoassets and the underlying distributed ledger technology, and set out the UK's policy and regulatory approach. Although the Taskforce's report recognised the potential benefits that may be delivered by cryptoassets and the underlying technology in the future, it also highlighted growing evidence of risks to consumers and markets, and from the use of cryptoassets for illicit activity.
- 2.30 The government and financial regulators have committed to a series of actions to protect consumers and markets, prevent the use of cryptoassets for illicit activity, allow innovation to thrive. These actions will maintain the UK's reputation as a transparent and safe place to do business in financial services with high regulatory standards.
- 2.31 At an international level, FATF have agreed on the need to regulate "virtual assets and virtual asset service providers", and the UK continues to engage on both the form this regulation should take and how the FATF

recommendations should apply to its members later this year. In anticipating the broad scope of these revised recommendations, and in keeping up-to-date with evolving global standards, the UK is consulting widely on regulating the sector. The overlap of both international FATF standards and EU transposition timelines means our comprehensive approach aligns with emerging global standards on this issue.

What changes does 5MLD introduce?

- 2.32 Article 2 of 4MLD as amended now also applies to “providers engaged in exchange services between cryptoassets and fiat currencies”, and “custodian wallet providers”. This means that firms offering cryptoasset exchange services (between fiat currency and cryptoasset) and custodian wallet services will be required to fulfil customer due diligence (CDD) obligations, assess the money laundering and terrorist financing risks they face, and report any suspicious activity they detect. They will also be required to register with the relevant UK supervisor. The introduction of CDD obligations will ensure that firms verify the identity of their customers, and that law enforcement agencies will be able to use this information to identify the perpetrators of illicit activity.
- 2.33 The MLRs require regulated firms to apply CDD measures before the point at which a business relationship is established (or before carrying out occasional transactions worth over EUR 10,000, or when there is a suspicion of money laundering or terrorist financing). These measures are set out in full in regulation 28 of the MLRs.

Potential options

- 2.34 5MLD is a minimum harmonising piece of legislation (its thresholds are laid out in section 1.17-1.19). The risks associated with entities and activities not captured by 5MLD and the anticipated scope of FATF’s revised recommendations on regulating cryptoassets mean that the government is inclined to go beyond 5MLD’s thresholds, to ensure the UK continues to meet evolving global standards and fully addresses risks. In doing so, it is important that the government makes evidence-based decisions on which, if any, additional cryptoasset service providers are brought within scope of the regulations and the justification for doing so. The government is considering two options: transposing 5MLD provision only; or, transposing the minimum requirements alongside additional provisions. The government is also considering whether and how the cross-border risks posed by cryptoassets could be addressed.

Transpose 5MLD provisions only

- 2.35 Article 2 of 4MLD as amended now also applies to “providers engaged in exchange services between virtual currencies and fiat currencies”, and “custodian wallet providers”. As above, when 5MLD is transposed, firms offering cryptoasset exchange services (between fiat currencies and cryptoassets) and custodian wallet services will be required to fulfil CDD obligations.
- 2.36 In transposing these changes, the government will have to select a supervisory body to ensure firms have appropriate systems and controls.

International standards agreed at FATF call for supervision by competent authorities, as opposed to professional body supervision. The FCA's involvement in the Cryptoassets Taskforce, as well as its recent perimeter guidance, qualifies it for consideration for this responsibility. Further, the FCA's experience in regulating asset-based service providers made them a natural choice for supervisory authority.

2.37 In light of this, the government has asked the Financial Conduct Authority (FCA) to consider taking on the role of supervision of cryptoasset exchanges and custodian wallet providers in fulfilling their AML/CTF obligations. This will also mean the FCA is likely to be the registering authority for cryptoasset firms. The government seeks views on this decision before confirming the identity of the supervisor.

Include additional regulatory provisions when transposing 5MLD

2.38 As highlighted above, government intelligence reports suggest that illicit activity is being carried out at various points of cryptoasset exchange, not just through fiat-crypto exchange services, and we are keen to address these risks by regulating the providers of such services through AML/CTF regulation. The government seeks your views on the ML/TF risks that exist in relation to the activities outlined below. It also seeks views on what the government's approach should be in relation to bringing some, none, or all of the providers of these activities within scope of the regulations (in addition to 5MLD provisions above):

- crypto-to-crypto exchange service providers (firms engaged in exchange services between one cryptoasset and another, or services allowing value transactions within one cryptoasset)
- peer-to-peer exchange service providers (firms that facilitate the exchange of fiat currencies and cryptoassets (both fiat-to-crypto and crypto-to-crypto) between prospective "buyers" and "sellers")
- Cryptoasset Automated Teller Machines (physical kiosks that allow users to exchange cryptoassets and fiat currencies)
- issuance of new cryptoassets, for example through Initial Coin Offerings (ICOs)
- the publication of open-source software (which includes, but is not limited to, non-custodian wallet software and other types of cryptoasset-related software)

Provisions on cross-border risks

2.39 The government seeks views on the cross-border risks (and potential regulatory solutions to these risks) posed by cryptoassets and associated service providers. Firms based outside the UK would theoretically avoid UK regulatory standards and would not be compelled to conduct CDD checks. This also means being based outside the UK has potential benefits for firms (such as avoiding regulatory requirements), which is at odds with the UK's ambition to maintain its reputation as a transparent and safe place with high regulatory standards for financial services. We recognise the challenges

both in terms of practicalities and effectiveness of any approach seeking to address these cross-border risks, and we welcome views on these issues.

Further work

- 2.40 The cryptoasset sector is a rapidly developing market with risks and potential benefits that may arise in the future. The UK will continue to actively engage internationally in FATF to ensure there is a global response that mitigates the risks posed by cryptoassets for illicit activity.
- 2.41 In addition to the approach to the illicit activity risks posed by cryptoassets set out in this chapter, the government and financial regulators are taking steps to further consider other elements of the UK's response to cryptoassets.
- 2.42 The government will consult in 2019 to consider the regulatory perimeter in relation to security and utility tokens, and the further explore whether and how exchange tokens and related firms could be regulated beyond the AML/CTF purposes outlined in this chapter.

Box 2.C: Cryptoassets

12 5MLD defines virtual currencies as “a digital representation of value that is not issued or guaranteed by a central bank or a public authority, is not necessarily attached to a legally established currency and does not possess a legal status of currency or money, but is accepted by natural or legal persons as a means of exchange and which can be transferred, stored and traded electronically”. The Government considers that all relevant activity involving exchange, security and utility tokens should be captured for the purposes of AML/CTF regulation, and seeks views on this approach. Is the 5MLD definition appropriate or does it need to be amended in order to capture these three types of cryptoassets (as set out in the Cryptoassets Taskforce's framework)? Further, are there assets likely to be considered a virtual currency or cryptoasset which falls within the 5MLD definition, but not within the Taskforce's framework?

13 5MLD defines a custodian wallet provider as “an entity that provides services to safeguard private cryptographic keys on behalf of its customers, to hold, store and transfer virtual currencies”. The Government considers that all relevant activity involving exchange, security and utility tokens should be captured for the purposes of AML/CTF regulation, and seeks views on this approach. Is the 5MLD definition appropriate or does it need to be amended in order to capture these three types of cryptoassets (as set out in the Cryptoassets Taskforce's framework)? Further, are there wallet services or service providers likely to be considered as such which fall outside the 5MLD definition, but should come within the UK's regime?

- 14 Should the FCA be assigned the role of supervisor of cryptoasset exchanges and custodian wallet providers? If not, then which organisation should be assigned this role?
- 15 The government would welcome views on the scale and extent of illicit activity risks around cryptoassets. Are there any additional sources of risks, or types of illicit activity, that this consultation has not identified?
- 16 The government would welcome views on whether cryptoasset ATMs should be required to fulfil AML/CTF obligations on their customers, as set out in the regulations. If so, at what point should they be required to do this? For example, before an 'occasional transaction' is carried out? Should there be a value threshold for conducting CDD checks? If so, what should this threshold be?
- 17 The government would welcome views on whether firms offering exchange services between cryptoassets (including value transactions, such as Bitcoin-to-Bitcoin exchange), in addition to those offering exchange services between cryptoassets and fiat currencies, should be required to fulfil AML/CTF obligations on their customers.
- 18 The government would welcome views on whether firms facilitating peer-to-peer exchange services should be required to fulfil AML/CTF obligations on their users, as set out in the regulations. If so, which kinds of peer-to-peer exchange services should be required to do so?
- 19 The government would welcome views on whether the publication of open-source software should be subject to CDD requirements. If so, under which circumstances should these activities be subject to these requirements? If so, in what circumstances should the legislation deem software users be deemed a customer, or to be entering into a business relationship, with the publisher?
- 20 The government would welcome views on whether firms involved in the issuance of new cryptoassets through Initial Coin Offerings or other distribution mechanisms should be required to fulfil AML/CTF obligations on their customers (i.e. token purchasers), as set out in the regulations.
- 21 How much would it cost for cryptoasset service providers to implement these requirements (including carrying out CDD checks, training costs for staff, and risk assessment costs)? Would this differ for different sorts of providers?
- 22 To what extent are firms expected to be covered by the regulations already conducting due diligence in line with the new requirements that will apply to them? Where applicable, how are firms conducting these due diligence checks, ongoing monitoring processes, and conducting suspicious activity reporting?

23 How many firms providing cryptoasset exchange or custody services are based in the UK? How many firms provide a combination of some of these services?

24 The global, borderless nature of cryptoassets (and the associated services outlined above) raise various cross-border concerns regarding their illicit abuse, including around regulatory arbitrage itself. How concerned should the government be about these risks, and how could the government effectively address these risks?

25 What approach, if any, should the government take to addressing the risks posed by “privacy coins”? What is the scale and extent of the risks posed by privacy coins? Are they a high-risk factor in all cases? How should CDD obligations apply when a privacy coin is involved?

Art intermediaries

Summary

- 2.43 In 2016, the UK art market consisted of over 7,580 galleries, dealers and auction houses, directly providing an estimated 41,700 jobs.³ During the same year, this led to the UK being the second largest market globally, with a share of 21% of world sales by value.
- 2.44 Art intermediaries are already regulated for AML/CTF purposes if they are classified as a high value dealer under the MLRs. A high value dealer is a firm, or sole trader, who by way of business trades in goods (including an auctioneer dealing in goods), when the trader makes or receives a payment in cash of at least EUR 10,000 in total from a single or series of linked transactions. This relatively narrow definition means, however, that many art intermediaries are currently not regulated for AML/CTF purposes.
- 2.45 5MLD expands the scope of obliged entities to include art intermediaries for transactions exceeding EUR 10,000, including art galleries, auction houses and free ports. This expansion of scope goes beyond the requirements applied to high-value dealers (which are only regulated in respect of cash transactions of or exceeding EUR 10,000), and extends to payments at or above that threshold regardless of whether they are made in cash. As part of implementing this change, the government will need to make a decision as to which businesses should be within scope of the regulations, how the regulations should apply to the UK art market and who should supervise the new obliged entities. This chapter seeks your views on the above changes and what they could mean in practice.

What changes does 5MLD introduce?

- 2.46 Article 2 of 4MLD as amended states that “persons trading or acting as intermediaries in the trade of works of art, including when this is carried out by art galleries and auction houses, where the value of the transaction or a

³ <http://tbamf.org.uk/wp-content/uploads/2014/08/British-Art-Market-2014.pdf>

series of linked transactions amounts to EUR 10 000 or more” and “persons storing, trading or acting as intermediaries in the trade of works of art when this is carried out by free ports, where the value of the transaction or a series of linked transactions amounts to EUR 10 000 or more,” are included as obliged entities.

Potential options

Who should be included within the scope of the term ‘art intermediaries’

- 2.47 There can be a variety of businesses involved in the sale, conservation, display, transport and storage of art. Generally, an art intermediary is a person or company that buys and sells works of art by way of business. They can be a gallery owner, private dealer, or act as a broker or auctioneer between private sellers and buyers. Most dealers will specialise in one period or style of artwork, and will be able to give legal, storage, conservation and cataloguing advice to owners or potential owners of artwork. Art curators, consultants and appraisers are also active within the market. Specialists in art storage and shipment – and providers of other ancillary services - could also be within scope. Therefore, the government would welcome views on the scope of the term ‘art intermediary’, including the possibility that the intermediary is not making or receiving the payment. We would also welcome views on what other types of activity exist and whether these activities should be viewed as coming within the meaning of acting as an art intermediary, or acting in the trade of works of art.
- 2.48 In order to identify which businesses are in scope of the regulations, we will also need to define ‘works of art’. We welcome views on a specific definition that is appropriate for AML/CTF purposes, such as using the definition in s.21 of the VAT Act 1994,⁴ as amended. This definition outlines that works of art can be executed entirely by hand by the artist, and include pictures, collages and similar decorative plaques; paintings and drawings; original engravings, prints and lithographs; original sculptures and statuary; tapestries and wall textiles from original designs; individual pieces of ceramics; enamels on copper; and photographs taken or printed by the artist. However, the VAT Act distinguishes works of art from antiques and collectors’ items. There is also a definition of ‘artistic work’ under the Copyright, Designs and Patents Act 1998.⁵ Therefore, the government would invite views on a workable definition on which industry can rely, and how this should be defined for AML/CTF purposes.

Free ports

- 2.49 Free ports, also referred to as free zones, are areas designated as special zones for customs purposes. There are currently no free ports in the UK. There are customs warehouses, but these are generally not used for art transactions in the same way as free ports in other non-EU jurisdictions.

⁴ <http://www.legislation.gov.uk/ukpga/1994/23/section/21>

⁵ <https://www.legislation.gov.uk/ukpga/1988/48/section/4>

- 2.50 Although the government is open to ideas that deliver economic advantages for the UK, free ports raise complex issues, and existing customs facilitations deliver many of the same customs advantages. The government welcomes views on whether free ports should be defined within the MLRs as none currently exist within the UK and – if so - what it should include. We also welcome views on the risks attached in a UK context and how the risks of illicit activity could be managed within a free port.

On whom is CDD done and at what point

- 2.51 The government invites views on how art intermediaries will be brought into scope of CDD requirements in the MLRs, the practicalities of carrying out CDD measures on both parties in a transaction if traders are acting as intermediaries, and how CDD requirements can be fulfilled in the case of auctions.
- 2.52 It is proposed that the regulations will specify that art intermediaries must apply CDD measures if acting in relation to a transaction for which the value amounts to EUR 10,000 or more, or the relevant transaction threshold. This would be similar to the way in which the MLRs apply to high value dealers, although the art intermediary may not be carrying out the transaction itself, as there is the possibility that they are not the one making or receiving the payment, unlike high value dealers. In that case, the intermediary would need to carry out CDD before the transaction takes place, but compliance issues could arise if the parties go ahead with the transaction without the intermediary knowing or before the intermediary can carry out CDD. Guidance could make clear expectations in this scenario. The government welcomes views on the likelihood of this scenario, and how it could be resolved to ensure CDD is completed before the transaction takes place. Moreover, in this scenario where the art intermediary is not carrying out the transaction itself, do you agree that both the buyer and the seller of the art work would be considered the customer on whom CDD is carried out by the intermediary? If not, how do you determine which is the customer?
- 2.53 Auctions create further complexity around CDD requirements, and we welcome views and evidence on the difficulties this could create for CDD and AML/CTF purposes. For example, buyers may not be known until after the sale is concluded and the final sale price will not be known. Art intermediaries might need to conduct CDD in all cases where there is a realistic possibility that the final price will be above the relevant transaction threshold. Moreover, we welcome views on the point at which CDD would need to be carried out by art intermediaries in auctions, would CDD be carried out for all potential buyers and sellers in an auction?

Evidence and scope of the change – EUR 10,000 threshold

- 2.54 The art market is susceptible to money laundering risks, similar to those within the high value dealer sector, including the risk of purchasing an item with criminal proceeds to clean 'dirty money' and where the art is the criminal proceed itself e.g. it is stolen. However, there are potential money laundering risks that are more unique to the art trade; for example, paintings and drawings can be attractive to money launderers as they can be easier to store and transport. The value of artworks can increase rapidly,

meaning that profit can be gained through the act of short term money laundering actions. There is also an element of opacity, or lack of transparency, that is often cited as an issue in relation to art transactions as well as problems in ascertaining the provenance of goods.

- 2.55 An issue that has been identified around auctions is that the eventual price which an artwork will achieve can be difficult to predict and similar works can sell for different sums. This makes it challenging to determine in advance whether the value of a transaction will meet the EUR 10,000 threshold. Another issue is in relation to determining what constitutes a ‘transaction’ or a series of linked transactions i.e. does it include the total value of multiple items being bought or sold in a given time period? The issue of linked transactions has been clarified in guidance⁶ for high value dealers, and we welcome views on whether a similar approach should be adopted for art intermediaries. The government welcomes views on these issues, how they can be dealt with practically and what is already in place to mitigate the risks.
- 2.56 The government would welcome views on the current material risks within the sector, what this might mean for potentially lowering the EUR 10,000 threshold, and what impact this might have on smaller businesses.

Supervision

- 2.57 The UK AML regime has 25 supervisors, consisting of a mixture of self-regulatory bodies and statutory supervisors. The Treasury is responsible for the appointment and removal of supervisors by amending the MLRs.
- 2.58 The Treasury considers HMRC as a supervisor suited to the role of regulating art intermediaries, given their current supervision of high value dealers.
- 2.59 Separately, under regulation 26 of the MLRs, supervisors must approve beneficial owners, officers or managers of high value dealers. This is to prevent criminals, or their associates, with relevant unspent convictions from holding a management function in, or being the beneficial owners of high value dealers. The government asks for views on whether this should be extended to include art intermediaries and if so, whether it should be extended to all art intermediaries or only those to whom the CDD obligations apply (as above).

Box 2.D: Art intermediaries

26 What are your views on the current risks within the sector in relation to art intermediaries and free ports? Please explain your reasons and provide evidence where possible.

27 Who should be included within the scope of the term ‘art intermediaries’?

⁶ <https://www.gov.uk/government/publications/anti-money-laundering-guidance-for-high-value-dealers>

- 28 How should a 'work of art' be legally defined, do you have views on whether the above definitions of 'works of art' would be appropriate for AML/CTF? Please provide your reasoning.
- 29 How should art intermediaries be brought into scope of the MLRs? On whom should CDD be done and at what point?
- 30 Given that in an auction, a contract for sale is generally considered to be created at the fall of the gavel, what are your views on how CDD can be carried out to ensure that it takes place before a sale is finalised? How should the government tackle the issue around timing of CDD given the unpredictability of the sale value, and linked transactions which result in the EUR 10,000 threshold being exceeded?
- 31 Should the government set a threshold lower than EUR 10,000 for including art intermediaries as obliged entities under the MLRs? Should the threshold be set in euros or sterling? Please explain your reasoning.
- 32 What constitutes 'a transaction or a series of linked transactions'? Please provide your reasoning.
- 33 What do you see as the main monetary and non-monetary costs to your business of complying with the MLRs (e.g. carrying out CDD, providing information to a supervisor, training staff etc.)? Please provide statistics (even if estimates) where possible.
- 34 What do you see as the main benefits for the sector and your business resulting from art intermediaries being regulated for the purposes of AML/CTF?
- 35 Should the government extend approval checks, under regulation 26, to art intermediaries? Should there be a "transition period" to give the supervisor and businesses time to complete relevant approval checks on the appropriate existing persons (beneficial owners, managers and officers)?
- 36 Is there anything else that government should consider in relation to including art intermediaries under the MLRs e.g. how reliance could be used when dealing with agents representing a buyer or seller.

Chapter 3

Electronic money

Summary

- 3.1 Electronic money, or e-money, is an electronic store of monetary value on a device (such as a prepaid card) that may be widely used for making payments and value transfers, which does not necessarily involve bank account transactions. These instruments pose ML/TF risks, but certain low risk e-money products are exempted from certain CDD measures by the regulations. 5MLD reduces the thresholds above which CDD must be applied, meaning e-money firms will have to conduct CDD measures on a greater proportion of transactions. These changes will help to mitigate some of the risks associated with e-money, which the 2017 National Risk Assessment assessed to be medium risk for both money laundering and terrorist financing.
- 3.2 This chapter outlines the changes to exemptions in relation to e-money, and which products can be made exempt from CDD under Article 12 of 4MLD as amended.

What changes does 5MLD introduce?

- 3.3 Article 12 of 4MLD allows Member States to exempt some low risk e-money products from certain CDD measures, for example the identification and verification of the customer and of the beneficial owner, and the assessment of the purpose and intended nature of the relationship (but not from the monitoring of transactions or of business relationships). These exemptions currently apply where all of the following conditions are met: the maximum amount that can be stored electronically is EUR 250 (or, if the amount stored can only be used in the UK, 500 euros); the payment instrument is not reloadable or is subject to a maximum limit on monthly payments of EUR 250 which can only be used in the UK; the payment instrument is used exclusively to purchase goods and services; anonymous e-money is not used to fund the payment instrument; and any redemption in cash, or cash withdrawal, does not exceed EUR 100.
- 3.4 5MLD limits the conditions in which Member States may apply this exemption. All of the following conditions must be met: the maximum amount that can be stored electronically is EUR 150; the payment instrument is not reloadable or has a maximum limit on monthly payments of EUR 150 which can only be used in that Member State; the payment instrument is used exclusively to purchase goods and services; anonymous e-money is not used to fund the payment instrument; and any redemptions in

cash, or remote payment transactions, do not exceed EUR 50 per transaction.

- 3.5 5MLD specifies that financial and credit institutions acting as acquirers operating in Member States can only accept payments carried out with anonymous prepaid cards issued in non-EU countries where these countries impose requirements equivalent to those set out in 5MLD in relation to e-money. This means anonymous card issuers located in non-EU equivalent states must be deemed by UK firms to be subject to requirements in their national legislation which have an equivalent effect to the MLRs.
- 3.6 Finally, 5MLD permits Member States to not allow payments carried out using anonymous prepaid cards.

Evidence

- 3.7 The 2017 National Risk Assessment¹ identifies both the money laundering and the terrorist financing risks associated with e-money products as medium. It highlights that the nature of services and products that the sector provides can make it attractive to criminals seeking to convert criminal proceeds into other payment methods, conceal the origins of funds, remit funds overseas or transfer value between individuals.
- 3.8 Similarly, the European Commission's Supranational Risk Assessment² also found that e-money poses ML/TF risks because of the anonymity they offer, though it noted that their abuse requires more sophisticated planning, offers lower volumes of transactions and may be subject to a certain level of monitoring.
- 3.9 Further, the FATF issued guidance³ in 2013 noting that the risks around anonymity and prepaid cards exist at the points of purchase, registration, loading and reloading with funds, and at the point of use.
- 3.10 However, e-money firms currently face strict CDD thresholds, and the threshold and usage changes that 5MLD will introduce may significantly increase e-money firms' compliance costs without effectively reducing the risks in the sector.
- 3.11 Considering this available evidence base and existing mitigations, the government is minded to transpose 5MLD as is, maintaining where possible the capacity to provide exemptions, pending evidence garnered through this consultation (as set out above). The government welcomes further evidence on the risks of money laundering and terrorist financing from e-money products.

¹ <https://www.gov.uk/government/publications/national-risk-assessment-of-money-laundering-and-terrorist-financing-2017>

² http://ec.europa.eu/newsroom/just/item-detail.cfm?item_id=81272

³ <http://www.fatf-gafi.org/media/fatf/documents/recommendations/Guidance-RBA-NPPS.pdf>

Box 3.A: Electronic money

- 37 Should the government apply the CDD exemptions in 5MLD for electronic money (e-money)?
- 38 Should e-money products which do not meet the criteria for the CDD exemptions in Article 12 4MLD as amended be considered for SDD under Article 15?
- 39 Should the government exclude any e-money products from both the CDD exemptions in Article 12, and from eligibility for SDD in Article 15?
- 40 Please provide credible, cogent and open-source evidence of the risk posed by electronic money products, the efficacy of current monitoring systems to deal with risk and any other evidence demonstrating either high or low risk.
- 41 What kind of changes, if any, will financial institutions and credit institutions have to implement in order to detect whether anonymous card issuers located in non-EU equivalent states are subject to requirements in their national legislation which have an equivalent effect to the MLRs?
- 42 Should the government allow payments to be carried out in the UK using anonymous prepaid cards? If not, how should anonymous prepaid cards be defined?
- 43 The government welcomes views on the likely costs that may arise for the e-money sector in order to comply with 5MLD.

Chapter 4

Customer due diligence

Electronic identification processes

Summary

- 4.1 5MLD sets out the circumstances under which secure, remote or electronic identification processes may be taken into account in undertaking customer due diligence. These electronic identification processes include those set out in regulation (EU) No 910/2014, in particular with regard to notified electronic identification schemes. The government welcomes views on the need for additional clarification in the regulations as to what constitutes 'secure' electronic identification processes, or whether details of this should be set out in guidance.
- 4.2 Nothing in the existing UK regulations precludes the use of electronic means of identification, but the addition of this explicit mention of electronic identification may provide greater clarity for firms. The requirement for electronic identification processes to be "regulated, recognised, approved or accepted at national level by the national competent authority" in order to be taken into account does not require formal recognition by regulators for a particular identification scheme – approval from the competent national authority can be implicit. The government welcomes views on whether standards on an electronic identification process set out in Treasury-approved guidance (such as that published by the Joint Money Laundering Steering Group) would constitute implicit recognition.

Box 4.A: Electronic identification processes

44 Is there a need for additional clarification in the regulations as to what constitutes "secure" electronic identification processes, or can additional details be set out in guidance?

45 Do you agree that standards on an electronic identification process set out in Treasury-approved guidance would constitute implicit recognition, approval or acceptance by a national competent authority?

46 Is this change likely to encourage firms to make more use of electronic means of identification? If so, is this likely to lead to savings for financial institutions when compared to traditional customer onboarding? Are there any additional measures

government could introduce to further encourage the use of electronic means of identification?

Changes to regulation 28

CDD requirement based on FATF recommendation to identify and verify names of senior management of a body corporate

- 4.3 In December 2018, the FATF released its mutual evaluation report (MER) of the UK's AML/CTF regime. The government is committed to the implementation of the FATF standards. Our position is therefore to fill any gaps in the MLRs that were identified in the UK's MER. Therefore, we are proposing certain changes to regulation 28, and welcome views on the extent to which these changes are clarificatory and codifying existing practice, or are more substantial, and whether they will be of genuine value in reducing ML/TF.
- 4.4 Regulation 28(3)(b) states that relevant persons must, where a customer is a body corporate, take 'reasonable measures' to determine and verify the law to which a body corporate is subject, its constitution and the full names of the board of directors and the senior persons responsible for the operations of the body corporate. The FATF standards (Recommendation 10.9) go further than this, recommending relevant persons be *required* to determine and verify this information. We propose to amend regulation 28 (3) to bring it in line with the FATF recommendations and mandate the determination and verification of this information. The government welcomes views on the potential impact of this proposed amendment.

CDD Requirement to verify the identity of senior managing officials when the beneficial owner of the body corporate cannot be identified

- 4.5 5MLD extends customer due diligence requirements for obliged entities to verify the identity of the senior managing official, when the customer is a body corporate and the beneficial owner cannot be identified.
- 4.6 Article 13(1)(b) of 4MLD as amended states that: "Where the beneficial owner identified is the senior managing official as referred to in Article 3(6) (a) (ii), obliged entities shall take the necessary reasonable measures to verify the identity of the natural person who holds the position of senior managing official and shall keep records of the actions taken as well as any difficulties encountered during the verification process."
- 4.7 Under the MLRs, if the customer of an obliged entity is a body corporate, then the obliged entity may treat the senior person in that body corporate responsible for managing it as its beneficial owner. Currently, if the obliged entity has exhausted all possible means of identifying the beneficial owner of the body corporate and hasn't succeeded, then the obliged entity must keep written records of actions taken to identify the beneficial owner. 5MLD will require the obliged entity to take further measures to verify the identity of the senior person in that body corporate and keep written records of these

actions. The government proposes to amend regulation 28(8) of the MLRs to add this requirement.

CDD requirement based on FATF recommendation to understand the ownership and control structure of customers

- 4.8 The proposal follows on from the above FATF recommendation also highlighted in the UK's MER. FATF Recommendations¹ state that relevant persons should be "required to understand the nature of their customer's business and its ownership and control structure". This recommendation is partly addressed by regulation 28(4)(c) of the MLRs, which requires relevant persons to take 'reasonable measures' to understand the ownership and control structure of a legal person that is beneficially owned by another person. It may also be implicit in some other requirements in the MLRs, such as regulation 33(6)(a)(vi) requiring relevant persons to take account of the customer's corporate structure when assessing the risk of a situation for EDD purposes. However, the general obligation to understand the nature of your customer's business and its ownership and control structure is not explicitly laid out in the MLRs. We therefore propose to amend regulation 28 by adding an explicit requirement for relevant persons to understand this information as part of their CDD obligations, and welcome views on the extent to which obliged entities already undertake this activity.

Box 4.B: Changes to regulation 28

- 47 To what extent would removing 'reasonable measures' from regulation 28(3)(b) and (4)(c) be a substantial change? If so, would it create any risks or have significant unintended consequences?
- 48 Do you have any views on extending CDD requirements to verify the identity of senior managing officials when the customer is a body corporate and the beneficial owner cannot be identified? What would be the impact of this additional requirement?
- 49 Do related ML/TF risks justify introducing an explicit CDD requirement for relevant persons to understand the ownership and control structure of customers? To what extent do you already gather this information as part of CDD obligations?

Changes to regulation 31

- 4.9 The government is also consulting on a change to regulation 31, based on feedback on the MLRs from supervisors and obliged entities. Regulation 31 mandates that reporters cease transactions and consider filing a Suspicious Activity Report (SAR) where they cannot apply CDD under regulation 28. Regulation 31 does not however explicitly apply to situations where a reporter cannot apply the additional CDD measures for credit institutions and financial institutions set out in regulation 29 or the EDD measures set out in regulations 33-35. We would welcome views on whether we should clarify that the requirements of regulation 31 extend to when the additional

¹ Recommendation 10.8 for Financial Institutions and Recommendation 22.1 for DNFBPs

CDD measures in regulation 29 and the EDD measures in regulations 33-35 cannot be applied.

- 4.10 The EDD measures in the regulations are more subjective than CDD measures and therefore a relevant person could find it more difficult to establish whether it can or cannot apply such measures. How do respondents believe this could be reflected in any changes to the regulations?
- 4.11 We do not propose for the requirements of regulation 31 to be extended to the EDD measures which already have their own 'in-built' follow up actions. For example, a relevant person must obtain senior management approval to establish a relationship with a politically exposed person. If a person cannot fulfill this requirement, they cannot establish the relationship and there is consequently no need to also mandate that they cease the transaction under regulation 31.

Box 4.C: Changes to regulation 31

50 Do respondents agree we should clarify that the requirements of regulation 31 extend to when the additional CDD measures in regulation 29 and the EDD measures in regulations 33-35 cannot be applied?

51 How do respondents believe extending regulation 31 to include when EDD measures cannot be applied could be reflected in the regulations?

52 Do respondents agree the requirements of regulation 31 should not be extended to the EDD measures which already have their own 'in-built' follow up actions?

Chapter 5

Obligated entities: beneficial ownership requirements

Summary

- 5.1 Article 14 of 4MLD requires obliged entities to verify the identities of their customers and beneficial owners before establishing a business relationship or carrying out a transaction.
- 5.2 Additionally, Article 14 requires that obliged entities apply CDD measures to existing customers on a risk-sensitive basis, including when the relevant circumstances of a customer change.
- 5.3 5MLD introduces further changes to the requirements for obliged entities on verifying the identities of customers or beneficial owners.

What changes does 5MLD introduce?

Checking registers when entering into new business relationships

- 5.4 5MLD requires that whenever an obliged entity enters into a new business relationship with a company or trust that is subject to beneficial ownership registration requirements (as set out in chapters 8 and 9), they must collect either:
 - proof of registration on this register
 - an excerpt of the register
- 5.5 Regulation 30 (2) of the MLRs currently requires obliged entities to verify the identity of the customer before establishing a business relationship:
- 5.6 Regulation 30 (2) Subject to paragraph (3) or (4), a relevant person must comply with the requirement to verify the identity of the customer, any person purporting to act on behalf of the customer and any beneficial owner of the customer before the establishment of a business relationship or the carrying out of the transaction.
- 5.7 The government envisages amending regulation 30 (2) to include a requirement that the obliged entity must also collect proof of registration or an excerpt of the register from the company or the trust, but this would only be required to happen before a **new** business relationship is established. The effect of this would be to ensure that obliged entities are not required to collect proof of registration or an excerpt from the register in relation to business relationships existing prior to the regulations transposing 5MLD enter into force.

- 5.8 The government proposes to put the onus on the trust or company to provide proof of registration to an obliged entity, upon the obliged entity's request (presumed to occur at the point a business relationship is being contemplated between the two parties). The proposal for trustees is explained in Chapter 9. For companies, the Companies House register is public, so the obliged entity can obtain the information direct if it wishes rather than through the company.

Box 5.A: Checking registers when entering into a new business relationship

53 Do respondents agree with the envisaged approach for obliged entities checking registers, as set out in this chapter (for companies) and chapter 9 (for trusts)?

Requirement for ongoing CDD where there is a duty to review beneficial ownership information

- 5.9 5MLD also requires obliged entities to apply CDD when they have any legal duty in a calendar year to contact the customer for reviewing their relevant beneficial ownership information, or where the obliged entity has this duty under the EU Directive on Administrative Cooperation in the Field of Taxation (DAC2), which was transposed into UK law via the International Tax Compliance regulations, placing a common reporting standard (CRS) reporting obligation on UK financial institutions.
- 5.10 The government envisages therefore placing a requirement under regulation 27(8) of the MLRs for obliged entities to apply CDD where:
- The obliged entity has any legal duty in a calendar year to contact the customer for the purposes of reviewing that customer's beneficial ownership information
 - Where the obliged entity has a duty under the International Tax Compliance regulations for identifying new and pre-existing reportable offshore financial accounts for annual reporting, along with the details of the account holder (including jurisdiction of tax residence)
- 5.11 Further, the government envisages leaving it to the relevant person to determine what is 'relevant information' related to the beneficial owner. This would be in relation to the relevant person's risk assessment for that customer.
- 5.12 We also consider 'beneficial owner(s)' to refer to the beneficial owner of the customer – that is, only where the customer is not an individual.
- 5.13 We consider the scope of legal duty in this instance to be where UK law requires obliged entities to contact customers for the purpose of reviewing any information which (i) is relevant to the risk assessment for that customer for CDD purposes and which (ii) relates to the beneficial ownership information of that customer.

5.14 This consultation seeks feedback on the government's envisaged approach, and on our interpretation of the scope of 'legal duty'.

Box 5.B: Requirement for ongoing CDD where there is a duty to review beneficial ownership information

54 Do you have any views on the government's interpretation of the scope of 'legal duty'?

55 Do you have any comments regarding the envisaged approach on requiring ongoing CDD?

Chapter 6

Enhanced due diligence

Summary

- 6.1 The application of mandatory enhanced due diligence (EDD) measures in relation to designated high-risk third countries is currently determined at a national level. In order to harmonise EDD in relation to high-risk third countries (as identified through the EU listing process), 5MLD sets out a series of requirements for Member States and their obliged entities.
- 6.2 The MLRs already require mandatory EDD measures to be taken to mitigate the risks arising from business relationships and transactions with persons established in designated high-risk third countries. However, 5MLD includes some requirements that are not yet included as part of the MLRs.
- 6.3 The EU list of designated high-risk third countries will continue to have legal effect in the UK during the implementation period, during which time the government will remain committed to any legal obligations that relate to the list. Following the implementation period, the Sanctions and Anti-Money Laundering Act 2018 will provide the UK with the necessary legal powers to maintain a list of high-risk third countries, in connection with which EDD measures must be applied.

What changes does 5MLD introduce?

- 6.4 Article 18a(1) of 4MLD as amended expands the scope of persons on whom obliged entities must conduct EDD from 'natural persons or legal entities established in the third countries' to 'business relationships or transactions involving high-risk third countries.'
- 6.5 Article 18a(1) requires obliged entities to apply a newly defined set of EDD measures with respect to business relationships and transactions involving high-risk third countries. As such, obliged entities are required to obtain additional information on:
 - the customer and beneficial owner(s)
 - the intended nature of the business relationship
 - the source of funds and wealth of the customer and beneficial owner(s)
 - the reasons for the intended or performed transactions
- 6.6 While the MLRs require obliged entities to examine the background and purpose of business relationships and transactions with customers

established in high-risk third countries, obtaining the specific information set out in Article 18a(1) is currently not required.

- 6.7 5MLD also requires obliged entities to carry out enhanced monitoring of any business relationship or transaction involving a high-risk third country. The MLRs currently include a similar requirement, but this is specifically for any business relationship with a person 'established in' a high-risk third country. The wording used in 5MLD is instead 'involving' a high-risk third country.
- 6.8 Obligated entities will also be required to obtain the approval of senior management for establishing or continuing a relationship involving a high-risk third country. Similarly, the requirement set out in the MLRs relates to institutions 'from a third country' rather than the wording used in 5MLD of 'involving' a high-risk third country. The MLRs also currently only require this for credit and financial institutions that are establishing a new correspondent relationship.
- 6.9 Article 18a(1) also provides the UK with the option to impose an additional requirement. This would require obliged entities to ensure that whenever a customer makes their first payment involving a designated high-risk third country, that payment is carried out through an account in the customer's name with a credit institution subject to the Directive's customer due diligence standards. The government will not transpose this optional requirement.
- 6.10 Under Article 18a(2), obliged entities are required to apply, where applicable, at least one of the following additional measures to those carrying out transactions involving designated high-risk third countries:
- applying additional elements of enhanced due diligence
 - introducing an enhanced reporting mechanism or systematic reporting for financial transactions
 - limiting business relationships or transactions with natural persons or legal entities from the designated high-risk third country
- 6.11 In turn, the UK government and supervisory authorities are also required to take certain mitigating measures. Where applicable, they must apply at least one of the following measures with regard to designated high-risk third countries:
- refusing the establishment of obliged entities from the country concerned, or otherwise accounting for the fact that the country does not have an adequate AML/CTF regime
 - prohibiting obliged entities from establishing branches or representative offices in the country, or otherwise accounting for the fact that the obliged entity is establishing itself in a country that does not have adequate AML/CTF regimes
 - requiring increased supervisory examination or increased external audit requirements for branches and subsidiaries of obliged entities located in the country

- requiring increased external audit requirements for financial groups with respect to any of their branches and subsidiaries located in the country concerned
 - requiring credit and financial institutions to review and amend, or if necessary, terminate, correspondent relationships with respondent institutions in the designated high-risk third country
- 6.12 The additional mitigating measures listed under Articles 18a(2) and (3) are only required where applicable. When they are applicable, there is flexibility in deciding which of the measures should be taken. The government will therefore require obliged entities and supervisory authorities to determine which requirements are necessary based on their assessment of risk.

Potential options

What constitutes a business relationship or transaction involving a designated high-risk third country?

- 6.13 Article 18a of 4MLD as amended requires obliged entities to apply enhanced due diligence with respect to business relationships or transactions “involving” high-risk third countries. However, the Directive does not set out directly what “involving” should mean in this context.
- 6.14 While the government recognises the benefits of providing a broad definition to reduce the risk of money laundering, several issues arise if the definition is set too broadly. For example, the government intends to narrow the definition so as to be clear that UK citizens who are also nationals of countries identified as high-risk third countries should not be subject to enhanced due diligence purely as a result of having such a connection. These citizens, if included, may be unjustly denied certain financial services.
- 6.15 The government is seeking evidence from interested stakeholders whether a broad definition of ‘involving’ would have any other unintended impacts, and to what extent these could be mitigated by effective guidance. This should help to identify which issues the government should consider when it defines what constitutes involvement by high-risk third countries.
- 6.16 The government is seeking views on how the listed Enhanced Due Diligence measures can be transposed in a manner that is proportionate and effective in combatting money laundering and terrorist financing.

FATF recommendation to include ‘beneficiary of a life insurance policy’ as a relevant risk factor when determining whether to apply EDD measures (changes to regulation 33)¹

- 6.17 FATF Recommendation 10.13 states financial institutions should be required to include the beneficiary of a life insurance policy as a relevant risk factor in determining whether EDD measures should be taken in relation to a customer. While there is a general requirement for financial institutions to take into account customer risk factors in deciding whether to apply EDD

¹ For the purposes of this section, FIs (financial institutions) includes credit institutions

(regulation 33(6)), there is no specific requirement in the MLRs for financial institutions to include the beneficiary of a life insurance policy as a relevant risk factor. We seek views on adding 'beneficiary of a life insurance policy' as a relevant risk factor explicitly in regulation 33(6), and the extent to which firms already factor this into their account of customer risk factors in deciding whether to apply EDD.

- 6.18 Recommendation 10.13 further states that where a beneficiary, who is a legal person or a legal arrangement, is determined by the financial institution as high risk; as part of its EDD measures that financial institutions should take reasonable measures to "identify and verify the identity of the beneficial owner of the beneficiary, at the time of pay-out". At present, the MLRs (regulation 29) only require financial institutions to verify the identity of the beneficiary as part of their CDD measures and do not require the financial institution to identify the ultimate beneficial owner of the beneficiary, if it is a legal person or legal arrangement.

Box 6.A: Enhanced due diligence

- 56 Are there any key issues that the government should consider when defining what constitutes a business relationship or transaction involving a high-risk third country?
- 57 Are there any other views that the government should consider when transposing these Enhanced Due Diligence measures to ensure that they are proportionate and effective in combatting money laundering and terrorist financing?
- 58 Do related ML/TF risks justify introducing 'beneficiary of a life insurance policy' as a relevant risk factor in regulation 33(6)? To what extent is greater clarity on relevant risk factors for applying EDD beneficial?

Chapter 7

Politically exposed persons: prominent public functions

Summary

- 7.1 5MLD does not make any changes to the requirements contained in the existing regulations relating to the risk-based approach that firms must use to identify and conduct due diligence on Politically Exposed Persons (PEPs), their family members, and their close associates.
- 7.2 The government previously set out, in [responding to its consultation on the transposition of the Fourth Money Laundering Directive](#), its view that PEPs entrusted with prominent public functions by the UK should generally be treated as lower-risk and that firms should apply enhanced due diligence (EDD) accordingly. The FCA and other supervisory authorities have also published guidance on how firms should identify and apply EDD to PEPs.
- 7.3 The FCA's guidance¹ is clear that a case by case approach is required to identifying and applying EDD to PEPs, and that UK PEPs should be treated as low risk unless a firm has assessed that other risk factors not linked to their position as a PEP means they pose a higher risk. The guidance also sets out the FCA's view as to which UK functions are prominent public functions and so mean that a person holding such a function is a PEP. This provides further detail on the open-ended definition of prominent public functions contained in regulation 35(14) of the MLRs.

Identifying PEPs

- 7.4 Regulation 35(14) of the MLRs set out that individuals entrusted with prominent public functions include:
- heads of state, heads of government, ministers and deputy or assistant ministers
 - members of parliament or of similar legislative bodies
 - members of the governing bodies of political parties
 - members of supreme courts; of constitutional courts or of any judicial body the decisions of which are not subject to further appeal except in exceptional circumstances
 - members of courts of auditors or of the boards of central banks

¹ <https://www.fca.org.uk/publications/finalised-guidance/fg17-6-treatment-politically-exposed-persons-peps-money-laundering>

- ambassadors, charges d'affaires and high-ranking officers in the armed forces
- members of the administrative, management or supervisory bodies of State-owned enterprises
- directors, deputy directors and members of the board or equivalent function of an international organisation

This regulation directly transposes Article 3(9) of 4MLD, which is not modified by 5MLD.

7.5 Article 20a(1) of 4MLD as amended requires the UK to issue and keep up to date a list indicating the exact functions which qualify as prominent public functions for the purposes of Article 3(9) of 4MLD. The purpose of this list is to assist firms with identifying UK PEPs.

7.6 The FCA's guidance on how firms should identify and apply EDD to PEPs was published in July 2017, following consultation earlier that year.

7.7 So as to minimise disruption for firms, the government intends to adopt the approach already taken by the FCA in identifying prominent public functions and would welcome comments on this proposed approach. For the avoidance of doubt, this approach would mean that the following UK functions should be treated as prominent public functions:

- members of the UK government, and members of the devolved administrations in Scotland, Wales and Northern Ireland
- members of the UK Parliament, and members of the Scottish Parliament, Welsh Assembly and Northern Irish Assembly
- members of the national governing bodies of political parties represented in any of the UK Parliament, Scottish Parliament, Welsh Assembly and Northern Irish Assembly. Such members should only be treated as exercising a prominent public function where they exercise significant exercise power (e.g. over the selection of candidates or distribution of significant party funds)
- justices of the UK Supreme Court
- members of the Court of the Bank of England
- ambassadors, Permanent Secretaries/Deputy Permanent Secretaries (in the UK, it will not normally be necessary to treat public servants below Permanent or Deputy Permanent Secretary as having a prominent public function), and officers holding the equivalent military rank (Lieutenant General, Air Marshal, Vice Admiral or more senior).
- board members of for-profit enterprises in which the state has an ownership interest of 50% or more, or where reasonably available information points to the state having control over the activities of the enterprise
- directors, Deputy Directors and board members of international public organisations headquartered in the UK

- 7.8 This list would constitute an exhaustive list of which UK functions are considered by the government to constitute prominent public functions. Firms will remain under their existing obligations to identify whether their customers (or beneficial owners of their customers) are PEPs, and to apply EDD accordingly.
- 7.9 So as to take advantage of the flexibility permitted by 5MLD, the responsibility to apply EDD is discharged by the FCA's July 2017 guidance on PEPs, which provides clarity on how firms should take into account a list of functions in determining whether an individual is a PEP for the purposes of the MLRs.
- 7.10 Article 20a(1) of 4MLD as amended further specifies that "Member States shall request each international organisation accredited on their territories to issue and keep up to date a list of prominent public functions at that international organisation for the purposes of point (9) of Article 3".
- 7.11 For these purposes, the government is minded to conclude, in accordance with FCA guidance on PEPs, that an "international organisation" is one which is intergovernmental (such as the UN or NATO) rather than – for example – an international sporting federation or a non-governmental organisation in receipt of public funds.

Box 7.A: Politically exposed persons: prominent public functions

59 Do you agree that the UK functions identified in the FCA's existing guidance on PEPs, and restated above, are the UK functions that should be treated as prominent public functions?

60 Do you agree with the government's envisaged approach to requesting UK-headquartered intergovernmental organisations to issue and keep up to date a list of prominent public functions within their organisation?

Chapter 8

Mechanisms to report discrepancies in beneficial ownership information

Summary

- 8.1 Article 30 of 4MLD introduced a requirement on Member States to ensure that corporate and other legal entities incorporated within their territory obtain and hold information on their beneficial owners. It requires that the information be accessible in a timely manner by competent authorities and FIUs, and requires that the information be held on a central register in the Member State. This information is required to be adequate, accurate and current. Both before and after the transposition of 4MLD, the UK met this requirement for most legal entities through the publicly accessible Register of People with Significant Control (PSC), held at Companies House.
- 8.2 5MLD makes several changes to Article 30 of 4MLD. As a global leader on corporate transparency, the UK's existing PSC regime already meets most of the new requirements. The main new elements for the UK under 5MLD are the new requirements on obliged entities to report any discrepancies they find between the beneficial ownership information available in the central registers and the beneficial ownership information available to them.

What changes does 5MLD introduce?

- 8.3 5MLD makes several changes to Article 30 of 4MLD as amended. The most significant of these is to require Member States to ensure that information on the beneficial ownership of corporate and other legal entities is accessible by members of the general public. As noted above, the UK's regime is already publicly accessible and therefore meets the new requirement.
- 8.4 The UK regime also already meets most of the other changes to Article 30. Our regime contains effective, proportionate and dissuasive sanctions. Our regime contains obligations on any beneficial owner to provide the required information to a legal entity seeking to comply with its obligations under the Directive. These are now required under changes to Article 30(1) of 4MLD as amended.
- 8.5 Our regime already allows for access to beneficial ownership information to be restricted in exceptional cases and includes a right of appeal. This is now required under changes to Article on 30(9).

- 8.6 The principal amendment with which the UK does not currently comply is under Article 30(4). Under 4MLD Member States were required to have adequate, accurate and current information on their central register of company beneficial ownership. Amendments to Article 30(4) of 4MLD now require that “mechanisms” are put in place to ensure that the information held on the central register is adequate, accurate, and current. Mechanisms are not specified, but must include a requirement that obliged entities and, where appropriate, competent authorities (such as relevant law enforcement agencies) report any discrepancies they find between the beneficial ownership information available to them and the beneficial ownership information available in the central registers.
- 8.7 In the case of reported discrepancies, Member States are required to take appropriate actions to resolve the discrepancies in a timely manner and, if appropriate, include a specific mention in the central register in the meantime.

Potential options

Requiring obliged entities to report discrepancies

- 8.8 As part of their customer due diligence requirements, obliged entities are required to identify and take reasonable steps to verify the identity of the beneficial owner(s) of their customers so that the relevant person is satisfied that it knows who the beneficial owner is. They may utilise the Companies House Registers, including the Register of People with Significant Control (PSC Register), as part of this process but cannot rely solely on this information.
- 8.9 Where an obliged entity notices a discrepancy between the information it holds and that on the publicly accessible PSC register, it could be required to report this to Companies House through a bespoke reporting mechanism. This report could include detail on the name of the reporting individual and obliged entity; and the nature of the discrepancy. 5MLD does not specify a body to which the information must be reported, but the government considers that Companies House is best placed to take on this function, investigate and, as required, take further action to resolve the discrepancies.
- 8.10 The aims of such a process will be to allow simple but effective reporting by the obliged entities, to allow easy triaging of data by Companies House, and to contain sufficient data to allow useful reporting to relevant law enforcement agencies as appropriate.
- 8.11 In accordance with their procedures, Companies House would investigate the reported discrepancy. For most queries, Companies House would likely contact the company to bring the issue to their attention and ask the company to amend the data on the register or reconfirm that it is accurate.

Requiring competent authorities to report discrepancies

- 8.12 Competent authorities have access to a range of information and sources, both in the undertaking of their usual statutory functions and in the course of investigations.

- 8.13 In the event that there are discrepancies between the beneficial ownership information available to them and that held on the PSC register, they could report this directly to Companies House. Any notification to Companies House should not interfere unnecessarily with their functions, and should not jeopardise or otherwise impact on ongoing investigations or prosecutions.

Box 8.A: Mechanisms to report discrepancies in beneficial ownership information

61 Do you have any views on the proposal to require obliged entities to directly inform Companies House of any discrepancies between the beneficial ownership information they hold, and information held on the public register at Companies House?

62 Do you have any views on the proposal to require competent authorities to directly inform Companies House of any discrepancies between the beneficial ownership information they hold, and information held on the public register at Companies House?

63 How should discrepancies in beneficial ownership information be handled and resolved, and would a public warning on the register be appropriate? Could this create tipping off issues?

Chapter 9

Trust registration service

Summary

- 9.1 4MLD placed a requirement on the UK to create a register for all express trusts that incur a UK tax consequence. As a result, HMRC set up the Trust Registration Service (TRS), which went live in 2017.
- 9.2 5MLD expands the scope of this register by requiring trustees or agents of all UK and some non-EU resident express trusts to register those trusts with the TRS, whether or not the trust has incurred a UK tax consequence. It also requires the government to share data from the register with a range of persons under certain circumstances.
- 9.3 This chapter sets out the principal issues in relation to the expansion of the TRS, covering:
- the scope of the non-taxpaying express trusts that are required to register
 - the type of data that should be collected
 - how the government will deal with data sharing requests from relevant entities
- 9.4 A more detailed technical consultation run by HMRC will be published later this year. This will include additional information on the proposals for data collection, data sharing and penalties, taking into account responses to this consultation.
- 9.5 A trust is created when a natural or legal person (known as ‘the settlor’) places certain assets into a trust. Any trustees that are appointed have a legal obligation to hold and manage these assets for the benefit of a specified person, or class of persons (known as ‘the beneficiaries’).
- 9.6 Trusts are an intrinsic part of the UK’s legal system and have been in use for centuries. The government wishes to ensure that the many UK individuals and companies using trusts continue to benefit from the various legitimate advantages that they provide, while also taking steps in line with the requirements of 5MLD to ensure that trust structures do not facilitate money laundering or terrorist financing. To this end, the government recognises that the NRA concludes that UK trusts present a low risk of money laundering and terrorist financing, and is keen to ensure that the registration process – and any associated penalty regime – is applied proportionately.

What changes does 5MLD introduce?

- 9.7 The legislation currently requires the trustee of any express trust that is liable to pay one or more of six specified taxes to register that trust on TRS. 5MLD expands the scope of the register, and the following trusts will have to be registered:
- all UK resident ‘express trusts’ – as opposed to only those express trusts with UK tax liabilities as at present. (UK resident for this purpose is where (a) all trustees are UK resident or (b) where there is a mixture of UK and non-UK trustees and the settlor is a UK resident)
 - non-EU resident express trusts that acquire UK land or property either on or after 10 March 2020
 - non-EU resident express trusts that enter into a **new** business relationship with an obliged entity on or after 10 March 2020
- 9.8 Under 5MLD, the government will be required to disclose specific data about a trust and the ‘beneficial owners’ of it held on the register to law enforcement agencies in line with existing requirements under 4MLD. In addition, data on specific trusts will be shared under three circumstances:
- with obliged entities that enter a business relationship with a trust
 - with persons who can demonstrate a ‘legitimate interest’ in access to information on the beneficial ownership of a specified trust
 - with persons who want to know about trusts with a controlling interest in a non-EEA company
- 9.9 The above terms, and the parameters for these data sharing obligations will be set out in this chapter. The government does not envisage changing any of the existing registration requirements on trusts which incur UK tax consequences – the additional requirements set out in this chapter will apply to trusts which are not already subject to a registration obligation.

Potential issues

Who is required to register

UK resident express trusts

- 9.10 5MLD requires the UK to register all UK resident ‘express trusts’ and does not provide scope for carve outs, exemptions, or de minimis thresholds. The term ‘express trust’ is generally defined as a trust that was expressly (i.e. deliberately) created by a settlor, as opposed to being created in other ways – for example, through a court order or through statute. It arises through the settlor’s declaration of an intention to enter into a transaction and can be created, for example, by a written trust deed or under a will.
- 9.11 For an express trust to be effective, valid and enforceable, certain requirements must be satisfied. There must be certainty of:
- words and intention – the words, writing or deed must clearly indicate that the settlor wishes the property to be held on trust, and that a trust is intended

- subject matter – the assets which are to be held under the terms of the trust must be clearly identified
- objects (beneficiaries) – the settlor must identify the persons or classes of persons who the trustees are to regard as the beneficiaries. In some trusts this means that persons who are not born at the time the trust was created can thereafter benefit from the trust property

9.12 The government does not expect to specify a full list of types of express trust within the legislation transposing 5MLD, given the very wide range of ways in which trusts are used. Rather, the onus will be on trustees and their agents to determine whether their trust is an express trust or not, on the basis of the above description (and in due course, through more detailed guidance). However, we have set out below examples of the categories of UK trusts that are likely to fall within the definition of an express trust and therefore will have to register:

- discretionary trusts
- interest in possession trusts
- many types of bare trusts
- charitable trusts
- employee ownership trusts

9.13 Trusts are used for a variety of purposes across the constituent parts of the UK. The government's approach, and future guidance on TRS, will take this into account. The government does not consider that the envisaged approach to trust registration raises specific challenges under the legal framework existing within any of the constituent parts of the UK.

9.14 The government notes that while trusts and other legal arrangements are used across the EU, their use is more widespread in the UK due to our traditional reliance on common law. This means that many arrangements that are essentially contractual in jurisdictions with a civil law tradition would be categorised as trusts under English law. Consequently, and to ensure consistent application of 5MLD, the government will explore the possibility of having regard to the way in which such trusts would be dealt with in other EU Member States when clarifying registration requirements.

9.15 The government is also considering whether there are other registration services already in existence for particular trust types that could fulfil the 5MLD registration requirement, to avoid duplicate registration wherever possible.

9.16 Trusts within the EU are only required by 5MLD to register once. Therefore, EU resident express trusts that have an entry on a register in another Member State do not need to register on the UK's Trust Register. Trustees of trusts in this position should be prepared to provide written proof of registration in the relevant EU Member State if requested.

Non-EU express trusts acquiring UK land or property

9.17 The government envisages that the obligation to register an acquisition of UK land or property with TRS should mirror the existing registration criteria set by each of the UK's constituent parts. For example, in England the Land Registry requires freehold estates or estates with a leasehold estate of over 7 years to register so TRS would follow this format.

Non-EEA express trusts entering a business relationship with a UK obliged entity

9.18 'Business relationship' is already defined in Article 3(13) of 4MLD and is not changed by 5MLD: "A business relationship means a business, professional or commercial relationship that is connected with the professional activities of an obliged entity and which is expected, at the time when the contact is established, to have an element of duration"

9.19 The government's view is that this means a non-EU resident express trust receiving services such as banking, accountancy or legal advice on an ongoing basis from an obliged entity based in the UK will be required to register on the TRS. In this context only, the government envisages this will apply to non-EU resident express trusts that are deemed to be administered in the UK by virtue of having one UK trustee, even if there is a non-UK settlor and there is no other connection with the UK. The government proposes to define 'an element of duration' to encompass working interactions of 12 months or more.

Overseas and non-express Trusts that are liable for UK tax

9.20 For the avoidance of doubt, the government confirms that all trusts that incur a UK tax consequence will still be required to register on TRS, even if they are not express trusts or are non-EU resident express trusts that do not have UK trustees. However, non-express trusts with a UK tax consequence will not be liable to the data-sharing provisions detailed later in this chapter.

Box 9.A: Definition of express trust

64 Do respondents have views on the UK's proposed approach to the definition of express trusts? If so, please explain your view, with reference to specific trust type. Please illustrate your answer with evidence, named examples and propose your preferred alternative approach if relevant.

65 Is the UK's proposed approach proportionate across the constituent parts of the UK? If not, please explain your view, with reference to specific trust types and their function in particular countries.

66 Do you have any comments on the government's proposed view that any obligation to register an acquisition of UK land or property should mirror existing registration criteria set by each of the UK's constituent parts?

67 Do you have views on the government's suggested definition of what constitutes a business relationship between a non-EU trust and a UK obliged entity?

68 Do you have any comments on the government's proposed view of an 'element of duration' within the definition of 'business relationship'?

Data collection

- 9.21 Article 31 of 4MLD says that for every trust which a Member State is required to register, information should be collected on the 'beneficial owners' of the trust. This includes information on:
- the settlor
 - the trustee
 - the protector(s) (if any)
 - the beneficiaries or class of beneficiaries
 - any other natural person exercising effective control of the trust
- 9.22 5MLD requires the UK to share, and therefore first collect, certain information on each person listed in the above paragraph:
- 9.23 in relation to an individual
- the individual's full name
 - the individual's date of birth
 - the individual's nationality
 - the individual's country of residence
 - the nature of the individual's role in relation to the trust
- 9.24 in relation to a corporate entity:
- the legal entity's corporate or firm name
 - the registered or principal office of the legal entity
 - the nature of the entity's role in relation to the trust
- 9.25 The government may choose to collect some additional information with which to establish the legal identity of individuals; for example, National Insurance or passport numbers. Similarly, the government may collect some additional information in respect of non-EU trusts required to register to determine whether or not a trust is subject to some of the data sharing provisions set out in 5MLD. The government will confirm its approach on these points later in 2019 through the technical consultation.
- 9.26 The government expects to continue to collect more information on trusts which generate tax consequences than on trusts that do not generate such

consequences, in line with HMRC's tax collection responsibilities. Even in relation to trusts with tax consequences, however, the government is not currently minded, to continue to collect the full range of information currently required within the existing version of TRS. The government appreciates that some of information required has been found to be onerous for customers, and we will take this opportunity to review and ideally reduce information collected.

Box 9.B: Data collection

69 Is there any other information that you consider the government should collect above the minimum required by 5MLD? If so, please detail that information and give your rationale.

70 What is the impact of this requirement for trusts newly required to register? Will there be additional costs, for example paying agents to assist in the registration process, or will trustees experience other types of burdens? If so, please describe what these are and how the burden might affect you.

71 What are the implications of requiring registration of additional information to confirm the legal identity of individuals, such as National Insurance or passport numbers?

Registration deadlines

Existing trusts

- 9.27 The current TRS registration deadline of 31 January was based on the link to submitting a tax return. Given that this link is broken by 5MLD, the government no longer considers this deadline to be appropriate. We have therefore considered alternative options for existing and new trusts.
- 9.28 For those unregistered trusts already in existence on 10 March 2020, the government proposes a deadline of 31 March 2021 for them to register on TRS. This gives a long lead in time given the greater number of trusts that will need to be registered.

New trusts

- 9.29 For trusts created on or after 1 April 2020, the government proposes that the trust should be registered within 30 days of its creation. The government envisages that this approach would be the most straightforward, as registration can occur as part of the set-up process, when the required details should be readily available to trustees/agents.
- 9.30 The proposal for registration within 30 days for new trusts means there is no single deadline each year and it seems sensible to register the trust at the same time it is created.
- 9.31 It is also intended that this 30 day deadline will be used for any amendments to be made to the TRS data in due course: that is, when any of the required information changes, such as the name or contact details of a trustee or

beneficiary, trustees/agents will be required to update TRS within 30 days of becoming aware of the change, once the facility to do so is available.

Late registration

- 9.32 For late registration on TRS there are currently set penalties based on the self-assessment penalty regime due to the link between registration and taxable activity. However, as 5MLD extends registration to non-taxpaying trusts, this link is no longer appropriate. Therefore, the government considers that the self-assessment penalty regime is not a suitable basis for any future TRS penalty framework.
- 9.33 The government will consult on a suitable replacement penalty framework within the later technical consultation. In the interim, we would be interested in views on the format such a framework might take.

Box 9.C: Registration deadlines

72 Does the proposed deadline for existing unregistered trusts of 31 March 2021 cause any unintended consequences for trustees or their agents? If so, please describe these, and suggest an alternative approach and reasons for it.

73 Does the proposed 30 day deadline for trusts created on or after 1 April 2020 cause any unintended consequences for trustees or their agents? If so, please describe these, and suggest an alternative approach and reasons for it.

74 Given the link with tax-based penalties is broken, do you agree a bespoke penalty regime is more appropriate? Do you have views on what a replacement penalty regime should look like?

Data sharing

General

- 9.34 HMRC currently shares TRS data with law enforcement agencies when requested to do so, as specified in the MLRs. The government does not propose to change the type of information shared with law enforcement, nor the process by which it is shared.
- 9.35 5MLD introduces new data sharing requirements, in relation to obliged entities, those persons with a legitimate interest in specified information on trust beneficial ownership and those requesting information on trusts that hold a controlling interest in a non-EEA company.

Obliged entities

- 9.36 Article 14 of 4MLD as amended requires that, when undertaking a new business relationship with a trust, obliged entities have to collect proof of that trust's registration on TRS in order to complete their due diligence obligation. Chapter 5 of this document sets out the government's view that

the onus should be on the trustee to provide the information to the obliged entity.

- 9.37 The alternative to this would be the obliged entity itself requesting information directly from the trust register. This option would put an obligation on the government to verify the identity of an obliged entity, and whether it has the right to the relevant information. This may be subject to a delay whilst the government verified the identity and credentials of the obliged entity. Therefore, the government proposes that the obliged entity who wishes to enter into a business relationship will be best placed to verify that the relevant trustee has registered the trust on TRS, through obtaining proof of registration.
- 9.38 The type of information required to be given by the trustee to the obliged entity to satisfy this requirement will be included in the scope of HMRC's technical consultation later this year. The government envisages, however, that this information will be more than simply the trust registration number and will probably include information on the trustees including their names and contact details. This will assist obliged entities in complying with their CDD obligations.
- 9.39 The method by which the government will enable trustees to access proof of their trust's registration on TRS is still to be determined, but is likely to involve the facility for trustees to print out an extract of their trust's registration details in order to share that extract with any obliged entity of their choice. More detail on this requirement will be included in HMRC's technical consultation.

Box 9.D: Data sharing with obliged entities

75 Do you have any views on the best way for trustees to share the information with obliged entities? If you consider there are alternative options, please state what these are and the reasoning behind it.

Legitimate interest

- 9.40 The government must consider any request to share information about a trust (or a beneficial owner of a trust) registered on TRS with anyone who claims to have a 'legitimate interest' in accessing that information.
- 9.41 'Legitimate interest' is not defined further within 5MLD, which is clear that "Member States should define legitimate interest, both as a general concept and as a criterion for accessing beneficial ownership information in their national law." It is therefore for the government to determine an appropriate definition for use within the UK.
- 9.42 5MLD allows data sharing in the specified circumstances to combat money laundering and terrorist financing. It is aligned with other high priority initiatives and enhancements to these regimes. It is with this context in mind that the government believes that a definition of legitimate interest which is closely linked to this work makes the most sense.

- 9.43 Trusts are widely used across the UK for many ordinary purposes, including for charitable purposes; to protect assets for children and vulnerable adults; ring-fencing funds for consumer protection purposes; commercial purposes (such as providing security for contracts); or when structuring pension schemes. The government recognises the potential risks associated with sharing individuals' and trusts' data without due cause and considers it important that any definition of legitimate interest protects those persons whose data is held on TRS from purely speculative queries, and from requests made for any inappropriate reason.
- 9.44 Tying the definition to the original purpose of 5MLD in combatting money laundering and terrorist financing sets a suitable bar for requestors to meet, ensuring that trust users who are complying with the law and using trusts for legitimate purposes can have confidence that their privacy will be respected.
- 9.45 In this context, the government considers someone who has a legitimate interest in this data will:
- have active involvement in anti-money laundering or counter-terrorist financing activity
 - have reason to believe that the trust or person that is the subject of the legitimate interest enquiry is involved with money laundering or terrorist financing: in other words, speculative enquiries into all or multiple trusts on TRS will not be deemed legitimate
 - have evidence underpinning that belief
- 9.46 It will be for the government to consider whether or not requests for data meet the definition of legitimate interest. We will set up a clear and robust system to ensure that data is only released when we are confident that a request meets the definition in full and that disclosure does not impede progress of ongoing law enforcement investigations. This process will be set out fully in due course, but is likely to include a requirement to see identification documents for the requestor, and evidence linking the trust or person about whom the request is being made to money laundering or financing terrorism. This will ensure that persons with legitimate investigative roles into money laundering or terrorism financing will be able to access information about trusts registered on TRS that are credibly associated with such activity.
- 9.47 5MLD allows the government to make a charge for the provision of TRS information for legitimate interest requests. The government expects to apply fees proportionate to the costs involved in checking and compiling the information. Furthermore, we believe a detailed internal assessment process, and potentially a right of appeal, may be appropriate. This will be covered in more detail in the technical consultation.
- 9.48 In addition to the evidence and processes used to determine whether or not a request for data constitutes a 'legitimate interest', the government will ensure that personal data on vulnerable individuals associated with any trust that is the subject of such a request will receive special consideration, in line with the provision in Article 30(7) of 4MLD as amended. In particular, we

anticipate withholding information on any minors associated with a trust, even under circumstances where other data relating to that trust had been deemed subject to release.

Box 9.E: Data sharing for legitimate interest requests

76 Do you have any comments on the proposed definition of legitimate interest? Are there any further tests that should be applied to determine whether information can be shared?

Information on non-EEA companies

- 9.49 5MLD provides the right for any legal person to access data on any express trust that “holds or owns a controlling interest in any corporate or other legal entity” that is not registered on any EEA Member State’s corporate beneficial ownership register. In practice, this means any trust that owns or controls a corporate structure based outside the EEA.
- 9.50 The definition of ‘controlling interest’ should address issues of transparency and disguised ownership. The government proposes to use a definition in line with Article 3(6) of 4MLD as amended and with the 2016 regulations and 2017 guidance for the register of Persons with Significant Control (PSC). The government considers these existing regulations are sufficient for the purposes of 5MLD, and there is no merit in developing alternative definitions. Unlike the PSC register, the 5MLD includes public listed companies (PLCs) in scope of ‘corporate entity’. The government therefore plans to include PLCs in this requirement.
- 9.51 This means a trust will be deemed to hold a controlling interest in any corporate or other legal entity:
- when the trust has 25% or more of either voting shares or some sort of equivalent voting rights in respect of that entity
 - where the trust has any of the other means of control over that entity as defined in the 2017 PSC statutory guidance on the meaning of ‘significant influence or control’
- 9.52 Utilising the 2017 statutory guidance, the definition of a trust having control via other means will include examples such as the trust being able to:
- adopt or amend the company’s business plan
 - change the nature of the company’s business
 - make additional borrowing from lenders
 - appoint or remove the CEO
 - establish or amend any profit sharing, bonus or other incentive scheme of any nature for directors or employees
 - grant options under a share option or other share-based incentive scheme

- 9.53 The government considers that ‘corporate entity’ includes a body corporate incorporated under the law of a country or territory outside the EEA, but does not include a corporation sole, or a partnership that, whether or not a legal person, is not regarded as a body corporate under the law by which it is governed.
- 9.54 For the purposes of TRS, the government considers that ‘other legal entity’ would typically include charities, unincorporated associations and non-governmental organisations (NGOs); collective investment schemes; trusts and their equivalents from other legal systems. However, the government would welcome views on whether the concept of ‘other legal entity’ needs to be specifically defined, and if so, in what way.
- 9.55 The government is considering different options for identifying trusts which fall within the definition in 9.48 above. Firstly, the government could require a simple self-declaration by the trustee as to whether or not the trust meets the definition above. Or alternatively, the government could ask trustees to provide detailed evidence demonstrating they hold or own a controlling interest in any corporate or other legal entity, as well as what that interest itself constitutes.
- 9.56 The government’s preferred approach is the option of a self-declaration by the trustee during the registration process, as we consider this to be the most efficient and least resource-intensive approach. Where a trust does have such an interest, the trustee will then be asked for some basic details regarding the corporate or other legal entity in question, still to be determined. Given that we expect trusts with this characteristic to be a relatively small subset of trusts as a whole, this approach will ensure that only trustees of trusts that do fall within this category are then asked to answer additional questions, rather than applying such questions to all registrants.
- 9.57 It is important to note that data held within TRS about these trusts can be requested by anyone. Requests are purpose blind: there is no requirement for an anti-money laundering or counter terrorist financing aspect to the request. The government is therefore interested in views on how this data is best shared.

Box 9.F: Data sharing on trusts owning non-EEA companies

77 Do the definitions of ‘ownership or control’ and ‘corporate and other legal entity’ cover all circumstances in which a trust can indirectly own assets through some kind of entity? If not, please set out the additional circumstances which you believe should be included, with rationale and evidence.

78 Do you have any views on possible definitions of ‘other legal entity’? Should this be defined in legislation?

79 Does the proposed use of the PSC test for ‘corporate and other legal entity’, which are designed for corporate entities, present any difficulties when applied to non-corporate entities?

80 Do you see any risks or opportunities in the proposal that each trust makes a self-declaration of its status? If you prefer an alternative way of identifying such trusts, please say what this is and why.

81 The government is interested in your views on the proposal for sharing data. If you think there is a best way to share data, please state what this is and how it would work in practice.

Chapter 10

National register of bank account ownership

Summary

- 10.1 5MLD requires the UK to establish a centralised automated mechanism – such as a central registry or electronic data retrieval mechanism – which allows identification of natural and legal persons which hold or control bank accounts; payment accounts; or safe-deposit held by credit institutions within the UK.
- 10.2 The European Commission’s Action Plan for combatting terrorist financing of February 2016 sets out the policy rationale for this requirement, noting that “The existence of centralised registers at national level, which provide all national bank accounts listed to one person...is often cited by law enforcement authorities as facilitating financial investigations, including of possible terrorism financing”. The Directive itself is clear that “in order to respect privacy and personal data, the minimum data necessary for the carrying out of AML/CFT investigations should be held in central automated mechanisms for bank and payment accounts”.

What changes does 5MLD introduce?

- 10.3 Article 32a of 4MLD as amended requires the establishment of national mechanisms for retrieving ownership information on bank and payment accounts, and that information held on such *mechanisms* is “directly accessible in an immediate and unfiltered manner to national FIUs”, as well as national competent authorities for fulfilling their obligations under 5MLD.
- 10.4 5MLD further requires that information accessible and searchable through such mechanisms must include:
- the name of the customer account-holder, and any person purporting to act on behalf of the customer, along with a unique identification number or other information required for the purposes of CDD
 - the names of any beneficial owners of the customer account-holder (where relevant), along with a unique identification number or other information required for the purposes of CDD
 - the IBAN numbers of the bank or payment account, along with the dates on which the account was opened and closed
 - the names of the lessees of any safe deposit boxes, along with a unique identification number or other information required for the purposes of CDD, and the duration of the lease period

Potential options

Scope of application

10.5 Article 32a(1) of 4MLD as amended requires that centralised automated mechanisms allow identification “of any natural or legal persons holding or controlling payment accounts and bank accounts identified by IBAN, as defined by regulation (EU) No. 260/2012 of the European Parliament and of the Council, and safe-deposit boxes held by a credit institution within their territory”. So as to comply with this requirement, the government’s view is that the minimum information accessible through the register would need to be submitted by:

- UK-incorporated credit and payment institutions, and UK branches of non-UK credit institutions, providing ownership information of bank and payment accounts identified by IBAN
- UK-incorporated credit institutions, and UK branches of non-UK credit institutions, providing ownership information of safe-deposit boxes held within the UK. This would not extend to safe-deposit boxes held by non-UK branches of UK-incorporated credit institutions

10.6 Above and beyond these minimum requirements, the government is additionally considering requiring each of:

- UK-incorporated credit and payment institutions which issue credit cards
- e-money issuers which issue prepaid cards
- credit unions and building societies which issue accounts not identified by IBAN

to submit ownership information to the register. In the case of credit cards and prepaid cards, any such requirements would be based upon the potential for such cards to be misused for the purposes of money laundering and/or terrorist financing, as identified in relevant sectoral guidance. In the case of case of credit unions and building societies which issue accounts not identified by IBAN, any such requirements would be based upon a potential risk that excluding information on such accounts from the scope of the register may incentivise misuse of these accounts. The benefits of including information on such cards and accounts within the scope of the register will need to be considered against the administrative and financial costs of doing so.

10.7 The government would welcome evidence on the benefits to law enforcement agencies of this information being accessible through the register, and of the additional costs to businesses of providing such information, above and beyond the minimum requirements of the Directive.

Scope of information included on the register

10.8 Article 32a(3) of 4MLD as amended is not clear as to the precise nature of the identifying information to be included on the register in relation to bank and payment account holders. The government is therefore seeking views on the following approach:

- that information held on natural persons holding bank accounts, payment accounts, or safe-deposit boxes should consist of the person's name; information held by the submitting institution on the person's address and date of birth; and a unique identifying number provided by the submitting institution. Where a natural person is acting as a trustee or on behalf of an unincorporated association (or other arrangement without legal personality), the absence of legal personality would require the account-holder's individual details to be included on the register. The government is particularly seeking views on the implications of requiring registration of specific types of unique identifier (such as passport numbers; and/or national insurance numbers) for natural persons, both in relation to whether this would be beneficial for law enforcement authorities, and on any potential implications for access to banking services
- that information held on legal persons holding bank accounts, payment accounts or safe-deposit boxes should consist of the registered name of the legal person; its registered company number (or, for non-UK legal persons, an equivalent identifying number); the names of the ultimate beneficial owners of the legal person (as identified by the submitting institution based on information already held); and unique identifying numbers provided by the submitting institution for the beneficial owners. As set out above, the government is particularly seeking views on the implications of requiring registration of specific types of unique identifier (such as passport numbers; and/or national insurance numbers) for the beneficial owners of legal persons, including on the administrative and financial costs of submitting this information to the register relative to such information being accessed through the public register of UK company beneficial ownership maintained at Companies House
- that information held on bank and payment accounts contained on the register should consist of the IBAN numbers of such accounts, and the day, month and year on which they were opened/closed. The Directive is clear that the date of account closure must be registered, but silent as to whether bank/payment accounts that have been closed prior to the date of the transposition of the Directive must be registered. The government is therefore proposing that only bank/payment accounts which are open on the date on which the Directive is transposed into UK law, and those that are opened subsequently, be registered
- that information held on safe-deposit boxes, aside from that set out above, should consist of the duration of the lease period
- that, if ownership information on: (a) credit cards; and/or (b) prepaid cards; and/or (c) accounts issued by credit unions or building societies that are not identified by IBAN are to be included on the register, that this should consist of the information set out above in relation to natural and legal persons holding bank accounts, payment accounts or safe-deposit boxes

Access to information included on the register

- 10.9 Article 32a(2) of 4MLD as amended requires that that information held on the register be “directly accessible in an immediate and unfiltered manner to national FIUs”, and be “accessible to national competent authorities for fulfilling their obligations under this Directive”.
- 10.10 As is set out above, the stated policy rationale for requiring the establishment of national registers of this type was to facilitate financial investigations, including in relation to terrorist financing. Given this, and so as to safeguard the data contained on the register, the government is therefore seeking views on the following approach:
- that information included on the register be available to the Financial Conduct Authority; National Crime Agency; Serious Fraud Office; the 43 territorial police forces in England and Wales; HMRC; Companies House and the Police Services of Scotland and Northern Ireland
 - that information included on the register be accessible for the purposes of criminal investigations; civil recovery investigations; asset recovery investigations; and strategic intelligence collection
 - that, within organisations to whom information on the register is accessible, records and audit trails should be maintained of persons with access to the register, and that such access should be limited only to accredited financial investigators and financial intelligence officers so as to preserve the security of information held on the register. Where searches are conducted for information held on the register, the person conducting the search should be required to declare the grounds on which they are accessing the information, and why doing so is proportionate in the circumstances

Submission of information

- 10.11 The government envisages that updates to information contained on the register will be submitted by relevant firms on a weekly basis, with there being no obligation to re-submit data which has not changed since the previous date of submission.
- 10.12 An alternative approach – which has been implemented in other jurisdictions which have implemented registers of this type – would be to institute a mechanism by which the organisation holding the register would be able to obtain information on bank/payment account ownership directly from systems of institutions submitting information to the register.
- 10.13 The government would welcome views on the advantages and disadvantages of both approaches, including the potential implications on smaller firms; the costs associated with both options; and any data security/privacy implications associated with both options.

Box 10.A: National register of bank account ownership

- 82 Do you agree with, or have any comments upon, the envisaged minimum scope of application of the national register of bank account ownership?
- 83 Can you provide any evidence of the benefits to law enforcement authorities, or of the additional costs to firms, that would follow from credit cards and/or prepaid cards issued by e-money firms; and/or accounts issued by credit unions and building societies that are not identifiable by IBAN, being in scope of the national register of bank account ownership?
- 84 Do you agree with, or have any comments upon, the envisaged scope of information to be included on the national register of bank account ownership, across different categories of account/product?
- 85 Do you agree with, or have any comments upon, the envisaged approach to access to information included on the national register of bank account ownership?
- 86 Do you have any additional comments on the envisaged approach to establishing the national register of bank account ownership, including particularly on the likely costs of submitting information to the register, or of its benefits to law enforcement authorities?
- 87 Do you agree with, or have any comments upon, the envisaged frequency with which firms will be required to update information contained on the register? Do you have any comments on the advantages/disadvantages of the register being established via a 'submission' mechanism, rather than as a 'retrieval' mechanism?

Chapter 11

Requirement to publish an annual report

Summary

- 11.1 Under the MLRs all AML supervisors are required to report annually to the Treasury, through use of a data return, detailing their AML/CTF supervisory activity. This information informs an annual supervision report published by the Treasury, which provides a summary of the UK's supervisors' activity.

What changes does 5MLD introduce?

- 11.2 Article 34(3) of 4MLD as amended states that all self-regulatory bodies shall publish an annual report containing information on their supervisory activity, such as number of supervisory visits and enforcement actions undertaken in the preceding year. This information is already collected and submitted to the Treasury in the annual data return.
- 11.3 Notwithstanding the new requirements within 5MLD, the government is minded to continue publishing an annual supervision report. This will enable the drawing together of supervisory data into a single location, and the setting out of government priorities for additional improvements to the AML/CTF supervisory regime.

Box 11.A: Requirement to publish an annual report

88 Do you think it would still be useful for the Treasury to continue to publish its annual overarching report of the supervisory regime as required by regulation 51 (3)?

Chapter 12

Other changes required by 5MLD

Summary

- 12.1 Article 32b of 4MLD as amended requires that FIUs and competent authorities have access to information which allows for the timely identification of anyone owning real estate.
- 12.2 Article 38 of 4MLD as amended requires that certain protections be put in place for whistle-blowers within obliged entities.
- 12.3 The government does not envisage making any legislative changes to transpose these requirements, as we consider these to already be addressed within UK law.

Access to information on people who own real estate

- 12.4 Article 32b of 4MLD as amended states that FIUs and competent authorities should have access to information that allows them to identify the owners of real estate in a timely manner, including through registers or electronic data retrieval systems where these registers or systems are available.

Existing approach through which these requirements are met

- 12.5 The UK provides FIUs and competent authorities with timely access to information on owners of real estate through several mechanisms:
 - the Land Registry provides information on the owners of most real estate within the UK
 - the Proceeds of Crime Act 2002 (POCA) and Police and Criminal Evidence Act 1984 (PACE) provide law enforcement with the investigative powers to apply for production orders. These could, for example, get the title deeds from the bank that provides a mortgage, or ask an estate agent or conveyancing solicitor to provide details of beneficial owners or customers involved in a transaction
 - this is in addition to cross-referencing government held databases (for example, within HMRC), revealing information on e.g. a self-assessment return listing the sale of property
- 12.6 Alongside this, the government published a draft Bill in summer 2018 to establish a register of beneficial owners of overseas entities that own or buy property in the UK in 2021. This register will be the first of its type in the world, increasing transparency and trust in the UK property market.

Whistle-blowing protections

- 12.7 Article 38 of 4MLD as amended notes that whistle-blowers within obliged entities should be legally protected from retaliatory or hostile action, in particular from adverse employment actions. Those who face discriminatory actions for reporting suspicions of money laundering or terrorist financing – either internally or to the FIU – are entitled to safely make a complaint to the relevant competent authority.

Existing approach through which these requirements are met

- 12.8 These protections already largely exist under the Employment Rights Act 1996.
- 12.9 Further, the Public Interest Disclosure Order 2014 extends the protections under the Employment Rights Act to employees who disclose to the NCA matters relating to corruption and bribery, and compliance with the Terrorism Act 2000, the Proceeds of Crime Act 2002, or the MLRs.

Box 12.A: Other changes required by 5MLD

89 Are you content that the existing powers for FIUs and competent authorities to access information on owners of real estate satisfies the requirements in Article 32b of 4MLD as amended?

90 Are you content that the government's existing approach to protecting whistle-blowers satisfies the requirements in Article 38 of 4MLD as amended?

Chapter 13

Pooled client accounts

Summary

- 13.1 The MLRs require banks to conduct CDD on their customers. This includes businesses which seek to open a 'pooled client account' (PCA). A PCA is a specific type of bank account in which a business holds money on behalf of its clients. Businesses in several different industries use PCAs, including legal and accountancy professionals, letting and estate agents and organisations who hold money on behalf of vulnerable persons. An important point of distinction of PCAs from regular bank accounts is that the money in a business's PCA belongs to the client, not to the business.
- 13.2 PCAs present ML/TF risks. In PCAs, funds from multiple different sources can be co-mingled and rapidly move through the account. This can present significant challenges in identifying the true owners of the funds in the PCA, particularly from the perspective of the bank holding the account. As the 2017 NRA notes in relation to legal professionals specifically, client accounts have been exploited by criminals to transfer funds to third parties and effectively breaking the audit trail to launder funds. Criminals have entered apparently legitimate relationships with legal service providers, securing access to a client account, then changed their arrangements unexpectedly and with little explanation in order to pass funds to a third party. Most evidence of misuse of PCAs involving legal practitioners relates to property transactions.

PCA requirements

- 13.3 To address these ML/TF risks, specific requirements are placed on PCAs. The European Supervisory Authorities (ESA) Risk Factors Guidelines set out that banks should conduct CDD on both the customer holding the PCA (e.g. the law firm) and the customer's underlying clients (e.g. the person selling their house).¹ This is because the bank should treat the customer's clients as beneficial owners of the funds in the PCA.
- 13.4 The ESA guidelines however recognise that this prescriptive approach may not be necessary where the relationship between the bank and the customer holding the PCA poses a low level of ML/TF risk. The guidelines allow the application of simplified CDD (PCA SDD) where:
- the customer is subject to AML/CTF obligations

¹ Paragraph 110, <https://eba.europa.eu/documents/10180/1890686/Final+Guidelines+on+Risk+Factors+%28JC+2017+37%29.pdf>

- the ML/TF risk associated with the business relationship is low
- the bank is satisfied the customer applied CDD measures to its clients, and
- the bank is satisfied that the customer will provide CDD information if requested

13.5 The PCA SDD measures the bank may implement include:

- identifying and verifying the identity of the customer, including the customer’s beneficial owners
- assessing the purpose and intended nature of the business relationship; and
- conducting ongoing monitoring of the business relationship

13.6 Importantly, the bank does not have to conduct CDD on the customer’s underlying clients. The above requirements are implemented into UK law by the MLRs regulation 37(5)-(8). Similar to the ESA guidelines, the PCA SDD is available where the business relationship presents a low ML/TF risk. These relationships are set out in **Figures 1 and 2**.

Figure 1 – ‘Standard’ PCA CDD relationships

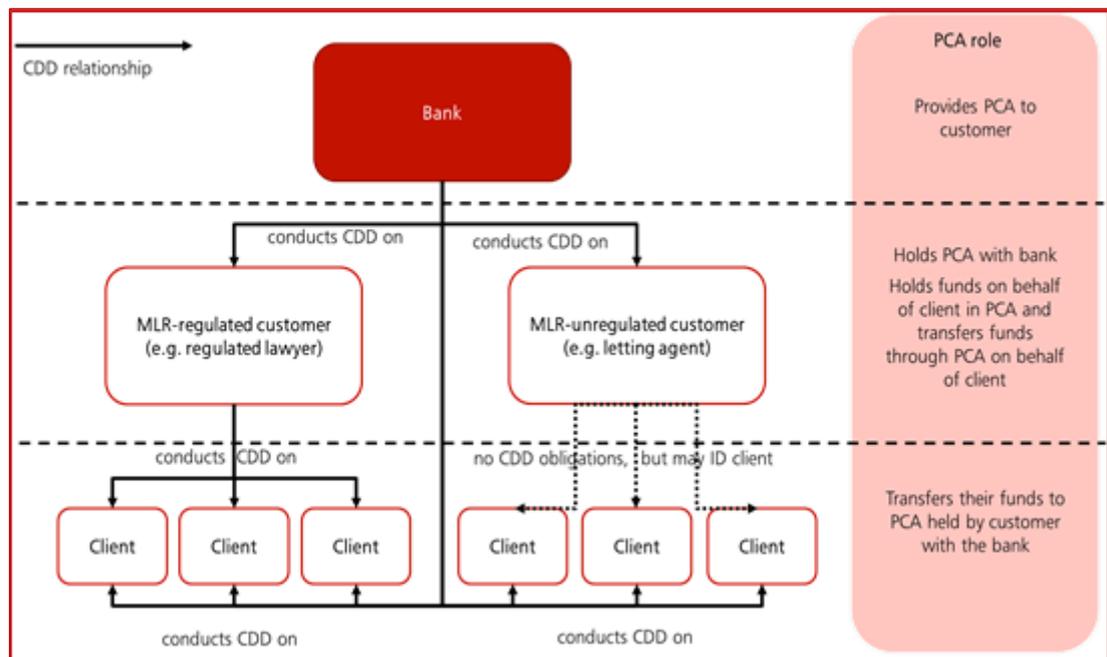
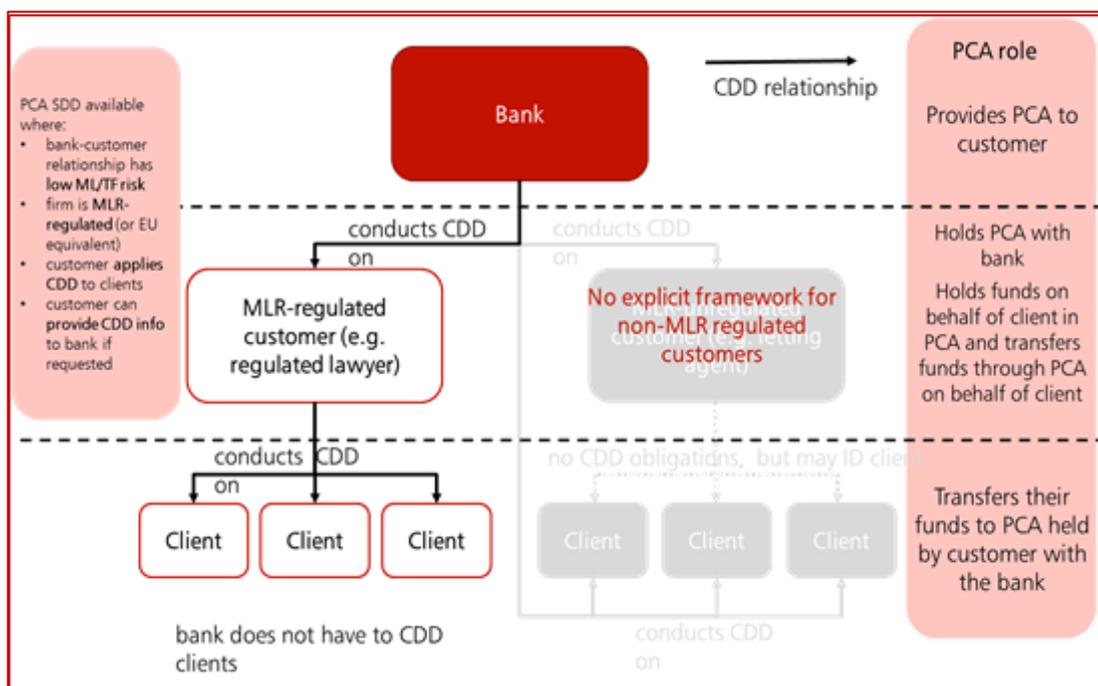


Figure 2 – ‘Low risk’ PCA SDD relationships



13.7 The PCA SDD can only be applied to customers who are regulated under the MLRs (or their EEA equivalent). This includes businesses such as legal practitioners, accountants and estate agents who carry out regulated business. There are however a range of other businesses who are not regulated under the MLRs that use PCAs. This includes:

- letting agents²
- legal practitioners involved in activities that are not regulated under the MLRs³
- organisations involved in the care of vulnerable persons

13.8 The MLRs do not explicitly state what CDD banks should undertake in relation to the non-MLR regulated businesses (see Figure 2). The ESA guidelines are explicit that the default position is that the bank should conduct CDD on both the business and its underlying clients.⁴ This places non-MLR regulated businesses in a difficult position. These businesses do not have MLR obligations as the government has considered that these businesses present a too low ML/TF risk to warrant regulation under the MLRs. However, the current framework implies that the PCAs of these businesses are too high ML/TF risk to access the PCA SDD. Conducting CDD on, for example, every letting agent's underlying client may be impracticable and impose a disproportionate resource burden on banks, their customers and their underlying clients to the risks posed by these PCAs. The lack of

² See Chapter 2 for discussion of the regulation of letting agents under the MLRs.

³ Legal practitioners are only regulated under the MLRs where they carry out certain activities. Some activities which involve the transmission of funds through pooled client accounts are exempt, such as the payment of funds relating to class action lawsuits.

⁴ MLR37(7) states that banks must take the ESA guidelines into account in determining what CDD measures to apply.

clarity around the framework has posed particular difficulties for letting agents in particular, as new client protection obligations in Scotland and England place requirements on agents to have a PCA.

- 13.9 In addition to the issues outlined above, the government is aware that the requirement for a demonstrated low ML/TF risk to access the PCA SDD has presented difficulties in banks in practice.

Potential options

- 13.10 HMT has been working in partnership with representatives from the banking, legal and letting industries to ensure that an appropriate framework for PCAs is maintained that addresses the ML/TF risks posed by the PCAs without imposing disproportionate costs to businesses, while also meeting the UK's international and EU obligations. The government wishes to use this consultation to gather further information from stakeholders on the issues they have faced in implementing the PCA framework under the MLRs. In particular, the government is interested in views on the ML/TF risks posed by PCAs, especially those held by non-MLR regulated business, and any evidence of how often these accounts are misused for ML/TF. The government is also interested in gathering more evidence on the practical barriers industry face in implementing the current framework and how the framework could be enhanced.
- 13.11 This information will assist in the ongoing consideration of the framework surrounding PCAs and how non-MLR regulated businesses should be treated. If the current framework was extended to cover non-MLR regulated businesses, we are interested in views on what CDD obligations should be placed on the banks. These could be similar to those imposed by the current framework, but would need to recognise that non-MLR regulated businesses do not have CDD obligations to the same extent as regulated businesses. Accordingly, banks may need to take steps to understand what systems and control the business has in place to identify clients, whether under other legislation, professional obligations or commercial requirements, as well as the types of clients the customer is likely to transact through its PCA.

Box 13.A: Pooled client accounts

- 91 Are there differences in the ML/TF risks posed by pooled client accounts held by different types of businesses?
- 92 What are the practical difficulties banks and their customers face in implementing the current framework for pooled client accounts? Which obligations pose the most difficulties?
- 93 If the framework for pooled client accounts was extended to non-MLR regulated businesses, what CDD obligations should be undertaken by the bank?

Chapter 14

Additional technical amendments to the MLRs

Enforcement powers

- 14.1 Regulations 25(6) and 60 do not provide the FCA or HMRC with the express power to publish a written notice related to AML failings in cases regarding directions on group undertakings where the FCA or HMRC cannot apply equivalent AML requirements in branches/subsidiaries, and in cases regarding the decision to either reject an application for registration from an Annex I financial institution, or cancel their existing application. We propose amending these regulations to allow the FCA and HMRC to be able (subject to certain exemptions):
- to publish information about any direction which they issue under 25(2), directing a ‘qualifying parent undertaking’ (as defined by section 192B of the Financial Services and Markets Act 2000) to take specified action in relation to third country
 - to publish information about any decision they make to remove or cancel a person’s registration under regulation 60. We propose amending these regulations to allow the FCA and HMRC to publish these written notices
- 14.2 Publishing written notices regarding directions on group undertakings is important both as a deterrent and for publicising the restrictions under which a particular firm is operating. For written notices relating to rejected applications or cancelled registrations, it’s important that the public is able to understand the reasoning behind the FCA’s decisions in these instances.
- 14.3 The MLRs currently also limit the powers of designated supervisory authorities to take action for breaches under regulation 76, 78 and 92 to only include ‘officers’ within relevant firms. The MLRs omit reference to a “manager” within this definition. This arguably has the effect of limiting the individuals against whom supervisors can take action, to those controlling or directing companies (or the equivalents in partnerships), rather than each person who has control, authority or responsibility for managing the business of a firm. We therefore propose to amend the definition of “officer” to include “manager”.

Box 14.A: Enforcement powers

94 Do you agree with our proposed changes to enforcement powers under regulations 25 & 60?

95 Do you agree with our proposed amendment to the definition of “officer”?

Information sharing

- 14.4 Regulation 51 (Regulatory information) and regulation 52 (Disclosure by supervisory authorities), currently lack specific text to facilitate information sharing between the Treasury and the Office for Professional Body AML Supervision (OPBAS). We propose amending the relevant legislation to make these information-sharing powers more explicit.

Box 14.B: OPBAS information-sharing powers

96 Do you agree with our proposed changes to information-sharing powers of regulations 51,52?

Requirement to cooperate

- 14.5 To reinforce OPBAS’ ability to carry out its statutory duties as effectively as possible, we propose introducing a requirement (along with appropriate sanctions) for professional body supervisors to deal with OPBAS in an open and cooperative way, and to disclose to OPBAS anything relating to the professional body supervisor of which OPBAS would reasonably expect notice. This would be similar to the Principle 11 requirement on FCA-regulated firms, which states that: “A firm must deal with its regulators in an open and cooperative way, and must disclose to the FCA appropriately anything relating to the firm of which that regulator would reasonably expect notice.”

Box 14.C: Requirement to cooperate

97 Do you have any views on this proposed new requirement to cooperate?

Changes to the requirement to be registered

- 14.6 Under regulation 56 (Requirement to be registered), High Value Dealers (HVD) and Accountancy Service Providers (ASP) that have applied to register to trade can do so legally until their application has been determined. regulation 56 allows Money Service Businesses (MSB) and Trust and Company Service Providers (TCSP) that have applied to register to trade legally until their application has been determined, because the Fit & Proper check at regulation 58 does not limit them in the same way as regulation 26. We propose amending regulation 56 to close this “grace period”.

Box 14.D: Registration

98 Do you agree with our proposed changes to regulations 56?

Complex network structures

- 14.7 In 2017 the MLRs introduced new requirements on obliged entities with agents who deliver their services. The MLRs require that the relevant person's agents and (where the agent is not a sole proprietor) the beneficial owners, officers, and managers of these agents (i.e. the people who own and control those agents) are 'fit and proper'. However, obliged entities may have more complex arrangements than simply using a single layer of agents, such as multi-layer arrangements with a "super" or "master" agent who have separate arrangements with sub-agents who deal with frontline customers. The MLRs intended that the entity who delivers the obliged entity's business is 'fit and proper', and the employees delivering the obliged entity's business are in scope of the training requirements to counter ML/TF.
- 14.8 For example, this can be the case with a principal Money Service Business (MSB) with a complex network arrangement consisting of a "super-agent" where the super-agent has separate arrangements with sub-agents who deliver the services of the principal MSB. The intention behind the MLRs was that the principal MSB must look at the fitness and propriety of the owners, officers and managers of the super-agent and the agents who deliver that MSB's services to customers. However, there is an argument that the principal only needs to satisfy himself or herself about the fitness of the owners, officers and managers of his or her directly contracted agents. Therefore, the government is considering changes to the MLRs which would extend those requirements to any agent or sub-agent, who delivers the principal MSB's business.
- 14.9 Multi-layer arrangements with sub-agents who deal with frontline customers, can also result in those employees delivering the service to customers not receiving the relevant training. Therefore, the government is considering changes to the MLRs to extend requirements on obliged entities to take measures to ensure training for employees of agents and sub-agents. For example, in the case of a principal MSB operating a network of agents, the MSB would be required to take measures to ensure training for its employees, the employees of the MSB's agents, and of the agents used by those agents. These changes to training requirements would apply to all obliged entities, because the intention behind the MLRs was that the employees of the entity who delivers the business have the relevant training.
- 14.10 The government would welcome views on the extent of complex network arrangements across regulated sectors, and if the above clarifications of intention would affect sectors other than MSBs.

Box 14.E: Complex network structures

99 Does your sector have networks of principals, agents and sub-agents?

- 100 Do complex network structures result in those who deliver the business to customers not being subject to the training requirements under the MLRs?
- 101 Do complex network structures result in the principal only satisfying himself or herself about the fitness and propriety of the owners, officers and managers of his or her directly contracted agents, and not extending this to sub-agents delivering the business?
- 102 If you operate a network of agents, do you already provide the relevant training to employees? Do you ensure the agents who deliver the service of your regulated business are 'fit and proper'?

Criminality checks

- 14.11 Regulation 26 seeks to prevent criminals convicted of relevant offences from holding a function as a beneficial owner, officer, manager or sole practitioner in certain sectors. The government is seeking to amend regulation 26 to require that any application made to a professional body supervisor under that regulation must include sufficient information to enable the supervisor to determine whether the person concerned has been convicted of a criminal offence on criminality and the regulations would also place a duty on supervisors to take necessary measures for ensuring compliance with that requirement, whether or not the applicant is a "relevant person" under the regulations.
- 14.12 The aim of this amendment is to make clear that self-declaration on relevant criminal convictions by those holding a management function or who are beneficial owners in the relevant sectors is not sufficient to comply with the regulations. This amendment will ensure that the integrity of the UK's anti-money laundering regime is not jeopardised by criminals acting in key roles within regulated firms.

Box 14.F: Criminality checks

- 103 Do the proposed requirements sufficiently mitigate the risk of criminals acting in regulated roles?

New technologies (changes to regulation 19)

- 14.13 In December 2018, the FATF released its mutual evaluation report (MER) of the UK's AML/CTF regime. The government is committed to the FATF standards and implementing them as far as possible. Our position is therefore to fill any gaps in the MLRs that are raised in the UK's MER. We welcome views on the extent to which these changes are clarificatory and codifying existing practice, or more substantial and will be of genuine value in reducing ML/TF.
- 14.14 FATF Recommendation 15.2 states that financial institutions should be required to undertake risk assessments prior to the launch or use of new

products, new business practices and delivery mechanisms. The MLRs (regulation 19(4)(c)) currently require financial institutions to take appropriate measures to assess and mitigate any ML/TF risks arising from the adoption of new technology, but this does not extend to explicitly include all new products, business practices and delivery mechanisms. Currently, this is clarified by the Joint Money Laundering Steering Group (JMLSG) guidance, which states that relevant persons should assess ML/TF risks prior to the launch of any new products, business practices or the use of new or developing technologies. We propose amending regulation 19(4)(c) to explicitly include new products, business practices and delivery mechanisms, and we welcome views on the benefits of specifying this in the regulations.

Box 14.G: New technologies

104 Should regulation 19(4)(c) be amended to explicitly require financial institutions to undertake risk assessments prior to the launch or use of new products, new business practices and delivery mechanisms? Would this change impose any additional burdens?

Group policies (changes to regulation 20)

14.15 FATF Recommendation 18.2(b) states that financial groups should be required to implement group-wide programmes against ML/TF, including, when necessary for AML/CTF purposes, the provision of customer, account and transaction information from branches and subsidiaries. The MLRs (regulation 20(1)(b)) require relevant persons to establish and maintain policies, controls and procedures throughout its group for data protection and information sharing for AML/CTF purposes with other members of the group. However, they do not explicitly require relevant persons to have policies, controls and procedures relating to the provision of customer, account and transaction information from branches and subsidiaries. Therefore, we propose changing regulation 20(1)(b) to specifically require relevant persons to have policies relating to the provision of customer, account and transaction information, and welcome views on the impact of this proposed change.

Box 14.H: Group policies

105 Should regulation 20(1)(b) be amended to specifically require relevant persons to have policies relating to the provision of customer, account and transaction information from branches and subsidiaries of financial groups? What additional benefits or costs would this entail?

Annex A

List of acronyms

List of the acronyms used in this consultation:

4MLD – The Fourth Money Laundering Directive

5MLD – The Fifth Money Laundering Directive

AML – anti-money laundering

AML/CTF – anti-money laundering and counter terrorist financing

CDD – customer due diligence

EDD – enhanced due diligence

EU – European Union

EUR – Euros (currency)

ESA – European Supervisory Authority

FATF – Financial Action Task Force

FIU – Financial Intelligence Unit

HMRC – Her Majesty's Revenue and Customs

JMLSG – Joint Money Laundering Steering Group

ML – money laundering

ML/TF - money laundering and terrorist financing

MLRs/the regulations – Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017

MSB – money service business

OPBAS – Office for Professional Body AML Supervision

NCA – National Crime Agency

NRA – National Risk Assessment

PCA – pooled client account

PEP – politically exposed person

PSC – Persons with Significant Control regime

SAR – suspicious activity report

SDD – simplified due diligence

Annex B

List of consultation questions

Expanding the scope in relation to tax matters

- 1 What additional activities should be caught within this amendment?
- 2 In your view, what will be the impact of expanding the definition of tax advisor? Please justify your answer and specify, where possible, the costs and benefits of this change.

Letting agents

- 3 What are your views on the ML/TF risks within the letting agents sector? What are your views on the risks in the private landlord sector, especially comparing landlord-tenant to agent-landlord-tenant relationships? Please explain your reasons and provide evidence where possible.
- 4 What other types of lettings activity exist? What activities do you think should be included or excluded in the definition of letting agency activity? Please explain your reasons and provide evidence where possible.
- 5 Should the government choose a monthly rent threshold lower than EUR 10,000 for letting agents? What would the impact be, including costs and benefits, of a lower threshold? Should the threshold be set in euros or sterling? Please explain your reasoning.
- 6 Do letting agents carry out CDD checks on both contracting parties (tenants and landlords) when acting as estate agents in a transaction?
- 7 The government would welcome views on whom CDD should be carried out and by what point? Should CDD be carried out before a relevant transaction takes place (if so, what transaction) or before a business relationship has been established? Please explain your reasoning.
- 8 The default supervisor of relevant letting agents will be HMRC, but professional bodies can apply to OPBAS to be a professional body supervisor. Are you a member of a professional body, and would this body be an appropriate supervisor? If this body would be an appropriate supervisor, please state which professional body you are referring to.
- 9 What do you see as the main monetary and non-monetary costs to your business of complying with the MLRs (e.g. carrying out CDD, training staff etc.)? Please provide figures (even if estimates) if possible.
- 10 Should the government extend approval checks under regulation 26 of the MLRs to letting agents? Should there be a "transition period" to give the

supervisor and businesses time to complete approval checks of the appropriate existing persons (beneficial owners, managers and officers)?

- 11 Is there anything else that government should consider in relation to including letting agents under the MLRs?

Cryptoassets

- 12 5MLD defines virtual currencies as “a digital representation of value that is not issued or guaranteed by a central bank or a public authority, is not necessarily attached to a legally established currency and does not possess a legal status of currency or money, but is accepted by natural or legal persons as a means of exchange and which can be transferred, stored and traded electronically”. The Government considers that all relevant activity involving exchange, security and utility tokens should be captured for the purposes of AML/CTF regulation, and seeks views on this approach. Is the 5MLD definition appropriate or does it need to be amended in order to capture these three types of cryptoassets (as set out in the Cryptoassets Taskforce’s framework)? Further, are there assets likely to be considered a virtual currency or cryptoasset which falls within the 5MLD definition, but not within the Taskforce’s framework?
- 13 5MLD defines a custodian wallet provider as “an entity that provides services to safeguard private cryptographic keys on behalf of its customers, to hold, store and transfer virtual currencies”. The Government considers that all relevant activity involving exchange, security and utility tokens should be captured for the purposes of AML/CTF regulation, and seeks views on this approach. Is the EU Directive definition appropriate or does it need to be amended in order to capture these three types of cryptoassets (as set out in the Cryptoassets Taskforce’s framework)? Further, are there wallet services or service providers likely to be considered as such which fall outside this Directive definition, but should come within the UK’s regime?
- 14 Should the FCA be assigned the role of supervisor of cryptoasset exchanges and custodian wallet providers? If not, then which organisation should be assigned this role?
- 15 The government would welcome views on the scale and extent of illicit activity risks around cryptoassets. Are there any additional sources of risks, or types of illicit activity, that this consultation has not identified?
- 16 The government would welcome views on whether cryptoasset ATMs should be required to fulfil AML/CTF obligations on their customers, as set out in the regulations. If so, at what point should they be required to do this? For example, before an ‘occasional transaction’ is carried out? Should there be a value threshold for conducting CDD checks? If so, what should this threshold be?
- 17 The government would welcome views on whether firms offering exchange services between cryptoassets (including value transactions, such as Bitcoin-to-Bitcoin exchange), in addition to those offering exchange services between cryptoassets and fiat currencies, should be required to fulfil AML/CTF obligations on their customers.

- 18 The government would welcome views on whether firms facilitating peer-to-peer exchange services should be required to fulfil AML/CTF obligations on their users, as set out in the regulations. If so, which kinds of peer-to-peer exchange services should be required to do so?
- 19 The government would welcome views on whether the publication of open-source software should be subject to CDD requirements. If so, under which circumstances should these activities be subject to these requirements? If so, in what circumstances should the legislation deem software users be deemed a customer, or to be entering into a business relationship, with the publisher?
- 20 The government would welcome views on whether firms involved in the issuance of new cryptoassets through Initial Coin Offerings or other distribution mechanisms should be required to fulfil AML/CTF obligations on their customers (i.e. token purchasers), as set out in the regulations.
- 21 How much would it cost for cryptoasset service providers to implement these requirements (including carrying out CDD checks, training costs for staff, and risk assessment costs)? Would this differ for different sorts of providers?
- 22 To what extent are firms expected to be covered by the regulations already conducting due diligence in line with the new requirements that will apply to them? Where applicable, how are firms conducting these due diligence checks, ongoing monitoring processes, and conducting suspicious activity reporting?
- 23 How many firms providing cryptoasset exchange or custody services are based in the UK? How many firms provide a combination of some of these services?
- 24 The global, borderless nature of cryptoassets (and the associated services outlined above) raise various cross-border concerns regarding their illicit abuse, including around regulatory arbitrage itself. How concerned should the government be about these risks, and how could the government effectively address these risks?
- 25 What approach, if any, should the government take to addressing the risks posed by “privacy coins”? What is the scale and extent of the risks posed by privacy coins? Are they a high-risk factor in all cases? How should CDD obligations apply when a privacy coin is involved?

Art intermediaries

- 26 What are your views on the current risks within the sector in relation to art intermediaries and free ports? Please explain your reasons and provide evidence where possible.
- 27 Who should be included within the scope of the term ‘art intermediaries’?
- 28 How should a ‘work of art’ be legally defined, do you have views on whether the above definitions of ‘works of art’ would be appropriate for AML/CTF? Please provide your reasoning.

- 29 How should art intermediaries be brought into scope of the MLRs? On whom should CDD be done and at what point?
- 30 Given that in an auction, a contract for sale is generally considered to be created at the fall of the gavel, what are your views on how CDD can be carried out to ensure that it takes place before a sale is finalised? How should the government tackle the issue around timing of CDD given the unpredictability of the sale value, and linked transactions which result in the EUR 10,000 threshold being exceeded?
- 31 Should the government set a threshold lower than EUR 10,000 for including art intermediaries as obliged entities under the MLRs? Should the threshold be set in euros or sterling? Please explain your reasoning.
- 32 What constitutes 'a transaction or a series of linked transactions'? Please provide your reasoning.
- 33 What do you see as the main monetary and non-monetary costs to your business of complying with the MLRs (e.g. carrying out CDD, providing information to a supervisor, training staff etc.)? Please provide statistics (even if estimates) where possible.
- 34 What do you see as the main benefits for the sector and your business resulting from art intermediaries being regulated for the purposes of AML/CTF?
- 35 Should the government extend approval checks, under regulation 26, to art intermediaries? Should there be a "transition period" to give the supervisor and businesses time to complete relevant approval checks on the appropriate existing persons (beneficial owners, managers and officers)?
- 36 Is there anything else that government should consider in relation to including art intermediaries under the MLRs e.g. how reliance could be used when dealing with agents representing a buyer or seller.

Electronic money

- 37 Should the government apply the CDD exemptions in 5MLD for electronic money (e-money)?
- 38 Should e-money products which do not meet the criteria for the CDD exemptions in Article 12 4MLD as amended be considered for SDD under Article 15?
- 39 Should the government exclude any e-money products from both the CDD exemptions in Article 12, and from eligibility for SDD in Article 15?
- 40 Please provide credible, cogent and open-source evidence of the risk posed by electronic money products, the efficacy of current monitoring systems to deal with risk and any other evidence demonstrating either high or low risk.
- 41 What kind of changes, if any, will financial institutions and credit institutions have to implement in order to detect whether anonymous card issuers located in non-EU equivalent states are subject to requirements in their national legislation which have an equivalent effect to the MLRs?

- 42 Should the government allow payments to be carried out in the UK using anonymous prepaid cards? If not, how should anonymous prepaid cards be defined?
- 43 The government welcomes views on the likely costs that may arise for the e-money sector in order to comply with 5MLD.

Customer due diligence

- 44 Is there a need for additional clarification in the regulations as to what constitutes "secure" electronic identification processes, or can additional details be set out in guidance?
- 45 Do you agree that standards on an electronic identification process set out in Treasury-approved guidance would constitute implicit recognition, approval or acceptance by a national competent authority?
- 46 Is this change likely to encourage firms to make more use of electronic means of identification? If so, is this likely to lead to savings for financial institutions when compared to traditional customer onboarding? Are there any additional measures government could introduce to further encourage the use of electronic means of identification?
- 47 To what extent would removing 'reasonable measures' from regulation 28(3)(b) and (4)(c) be a substantial change? If so, would it create any risks or have significant unintended consequences?
- 48 Do you have any views on extending CDD requirements to verify the identity of senior managing officials when the customer is a body corporate and the beneficial owner cannot be identified? What would be the impact of this additional requirement?
- 49 Do related ML/TF risks justify introducing an explicit CDD requirement for relevant persons to understand the ownership and control structure of customers? To what extent do you already gather this information as part of CDD obligations?
- 50 Do respondents agree we should clarify that the requirements of regulation 31 extend to when the additional CDD measures in regulation 29 and the EDD measures in regulations 33-35 cannot be applied?
- 51 How do respondents believe extending regulation 31 to include when EDD measures cannot be applied could be reflected in the regulations?
- 52 Do respondents agree the requirements of regulation 31 should not be extended to the EDD measures which already have their own 'in-built' follow up actions?

Obligated entities: beneficial ownership requirements

- 53 Do respondents agree with the envisaged approach for obligated entities checking registers, as set out in this chapter (for companies) and chapter 9 (for trusts)?
- 54 Do you have any views on the government's interpretation of the scope of 'legal duty'?

- 55 Do you have any comments regarding the envisaged approach on requiring ongoing CDD?

Enhanced due diligence

- 56 Are there any key issues that the government should consider when defining what constitutes a business relationship or transaction involving a high-risk third country?
- 57 Are there any other views that the government should consider when transposing these Enhanced Due Diligence measures to ensure that they are proportionate and effective in combatting money laundering and terrorist financing?
- 58 Do related ML/TF risks justify introducing 'beneficiary of a life insurance policy' as a relevant risk factor in regulation 33(6)? To what extent is greater clarity on relevant risk factors for applying EDD beneficial?

Politically exposed persons: prominent public functions

- 59 Do you agree that the UK functions identified in the FCA's existing guidance on PEPs, and restated above, are the UK functions that should be treated as prominent public functions?
- 60 Do you agree with the government's envisaged approach to requesting UK-headquartered intergovernmental organisations to issue and keep up to date a list of prominent public functions within their organisation?

Mechanisms to report discrepancies in beneficial ownership information

- 61 Do you have any views on the proposal to require obliged entities to directly inform Companies House of any discrepancies between the beneficial ownership information they hold, and information held on the public register at Companies House?
- 62 Do you have any views on the proposal to require competent authorities to directly inform Companies House of any discrepancies between the beneficial ownership information they hold, and information held on the public register at Companies House?
- 63 How should discrepancies in beneficial ownership information be handled and resolved, and would a public warning on the register be appropriate? Could this create tipping off issues?

Trust registration service

- 64 Do respondents have views on the UK's proposed approach to the definition of express trusts? If so, please explain your view, with reference to specific trust type. Please illustrate your answer with evidence, named examples and propose your preferred alternative approach if relevant.
- 65 Is the UK's proposed approach proportionate across the constituent parts of the UK? If not, please explain your view, with reference to specific trust types and their function in particular countries.

- 66 Do you have any comments on the government's proposed view that any obligation to register an acquisition of UK land or property should mirror existing registration criteria set by each of the UK's constituent parts?
- 67 Do you have views on the government's suggested definition of what constitutes a business relationship between a non-EU trust and a UK obliged entity?
- 68 Do you have any comments on the government's proposed view of an 'element of duration' within the definition of 'business relationship'?
- 69 Is there any other information that you consider the government should collect above the minimum required by 5MLD? If so, please detail that information and give your rationale.
- 70 What is the impact of this requirement for trusts newly required to register? Will there be additional costs, for example paying agents to assist in the registration process, or will trustees experience other types of burdens? If so, please describe what these are and how the burden might affect you.
- 71 What are the implications of requiring registration of additional information to confirm the legal identity of individuals, such as National Insurance or passport numbers?
- 72 Does the proposed deadline for existing unregistered trusts of 31 March 2021 cause any unintended consequences for trustees or their agents? If so, please describe these, and suggest an alternative approach and reasons for it.
- 73 Does the proposed 30 day deadline for trusts created on or after 1 April 2020 cause any unintended consequences for trustees or their agents? If so, please describe these, and suggest an alternative approach and reasons for it.
- 74 Given the link with tax-based penalties is broken, do you agree a bespoke penalty regime is more appropriate? Do you have views on what a replacement penalty regime should look like?
- 75 Do you have any views on the best way for trustees to share the information with obliged entities? If you consider there are alternative options, please state what these are and the reasoning behind it.
- 76 Do you have any comments on the proposed definition of legitimate interest? Are there any further tests that should be applied to determine whether information can be shared?
- 77 Do the definitions of 'ownership or control' and 'corporate and other legal entity' cover all circumstances in which a trust can indirectly own assets through some kind of entity? If not, please set out the additional circumstances which you believe should be included, with rationale and evidence.
- 78 Do you have any views on possible definitions of 'other legal entity'? Should this be defined in legislation?

- 79 Does the proposed use of the PSC test for 'corporate and other legal entity', which are designed for corporate entities, present any difficulties when applied to non-corporate entities?
- 80 Do you see any risks or opportunities in the proposal that each trust makes a self-declaration of its status? If you prefer an alternative way of identifying such trusts, please say what this is and why.
- 81 The government is interested in your views on the proposal for sharing data. If you think there is a best way to share data, please state what this is and how it would work in practice.

National register of bank account ownership

- 82 Do you agree with, or have any comments upon, the envisaged minimum scope of application of the national register of bank account ownership?
- 83 Can you provide any evidence of the benefits to law enforcement authorities, or of the additional costs to firms, that would follow from credit cards and/or prepaid cards issued by e-money firms; and/or accounts issued by credit unions and building societies that are not identifiable by IBAN, being in scope of the national register of bank account ownership?
- 84 Do you agree with, or have any comments upon, the envisaged scope of information to be included on the national register of bank account ownership, across different categories of account/product?
- 85 Do you agree with, or have any comments upon, the envisaged approach to access to information included on the national register of bank account ownership?
- 86 Do you have any additional comments on the envisaged approach to establishing the national register of bank account ownership, including particularly on the likely costs of submitting information to the register, or of its benefits to law enforcement authorities?
- 87 Do you agree with, or have any comments upon, the envisaged frequency with which firms will be required to update information contained on the register? Do you have any comments on the advantages/disadvantages of the register being established via a 'submission' mechanism, rather than as a 'retrieval' mechanism?

Requirement to publish an annual report

- 88 Do you think it would still be useful for the Treasury to continue to publish its annual overarching report of the supervisory regime as required by regulation 51 (3)?

Other changes required by 5MLD

- 89 Are you content that the existing powers for FIUs and competent authorities to access information on owners of real estate satisfies the requirements in Article 32b of 4MLD as amended?
- 90 Are you content that the government's existing approach to protecting whistle-blowers satisfies the requirements in Article 38 of 4MLD as amended?

Pooled client accounts

- 91 Are there differences in the ML/TF risks posed by pooled client accounts held by different types of businesses?
- 92 What are the practical difficulties banks and their customers face in implementing the current framework for pooled client accounts? Which obligations pose the most difficulties?
- 93 If the framework for pooled client accounts was extended to non-MLR regulated businesses, what CDD obligations should be undertaken by the bank?

Additional technical amendments to the MLRs

- 94 Do you agree with our proposed changes to enforcement powers under regulations 25 & 60?
- 95 Do you agree with our proposed amendment to the definition of "officer"?
- 96 Do you agree with our proposed changes to information-sharing powers of regulations 51,52?
- 97 Do you have any views on this proposed new requirement to cooperate?
- 98 Do you agree with our proposed changes to regulations 56?
- 99 Does your sector have networks of principals, agents and sub-agents?
- 100 Do complex network structures result in those who deliver the business to customers not being subject to the training requirements under the MLRs?
- 101 Do complex network structures result in the principal only satisfying himself or herself about the fitness and propriety of the owners, officers and managers of his or her directly contracted agents, and not extending this to sub-agents delivering the business?
- 102 If you operate a network of agents, do you already provide the relevant training to employees? Do you ensure the agents who deliver the service of your regulated business are 'fit and proper'?
- 103 What would be the costs and benefits to your business of the regulations clarifying intention to extend requirements to layers of agents and sub-agents?
- 104 Do the proposed requirements sufficiently mitigate the risk of criminals acting in regulated roles?
- 105 Should regulation 19(4)(c) be amended to explicitly require financial institutions to undertake risk assessments prior to the launch or use of new products, new business practices and delivery mechanisms? Would this change impose any additional burdens?
- 106 Should regulation 20(1)(b) be amended to specifically require relevant persons to have policies relating to the provision of customer, account and transaction information from branches and subsidiaries of financial groups? What additional benefits or costs would this entail?

HM Treasury contacts

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