

Article 30 of the fourth directive to address money laundering

Department for Business, Energy and Industrial Strategy

RPC rating: fit for purpose

Description of proposal

In 2015, the European Union (EU) adopted the fourth directive to address money laundering. By 26 June 2017, member states are required to implement it in domestic law. A consultation stage impact assessment (IA), from HM Treasury, on the whole directive received a ‘fit for purpose’ opinion from the RPC.¹ This present, final stage, IA covers only the implementation of article 30, for which the Department for Business, Energy and Industrial Strategy is the lead government department.

Article 30 requires member states to ensure that adequate, accurate, and current information on the beneficial ownership of “*corporate and other legal entities*”, incorporated within their territory, is held on a central register. An obligation on companies to maintain a register of people with significant control (PSC), and to provide this to the UK registrar of companies (Companies House), was put in place through the Small Business, Enterprise and Employment (SBEE) Act 2015 and subsequent regulations in March 2016. Following consultation specifically on article 30, it has, however, been established that some changes to the UK’s PSC regime are needed for the UK to meet fully the requirements of the directive. There are two main areas where the requirements of article 30 go beyond existing UK requirements.

1. Scope of entities covered

The UK’s existing domestic requirements apply to most companies and limited liability partnerships, covering over 3.5 million organisations. The Department has identified the following organisations that would additionally be brought into scope:

- European Co-operative Society (SCE) organisations, open-ended investment companies, and investment companies with variable capital.
- Scottish limited partnerships and Scottish partnerships, each of whose members is a limited company.

¹ RPC-HMT-3244(1) ‘*Transposition of the Directive on the prevention of the use of the financial system for money laundering or terrorist financing*’, 16 February 2016.

- Unregistered companies subject to the Unregistered Companies Regulations 2009.
- Companies listed on a UK prescribed market, such as AIM or ISDX.

These organisations are estimated to number 74,653. They will be required to investigate and report to a central register the details of their beneficial ownership. Where they do not have a beneficial owner, such entities will still need to report that finding.

In addition, there is a second group of legal entities structured in a way that makes it possible for them to have a beneficial owner – but they are, in practice, very unlikely to have one. These are charitable incorporated organisations (CIOs) and are estimated to number 11,864. They will be required to place information on the PSC register only where they identify themselves as having a beneficial owner.

An estimated total of 86,517 additional organisations are, therefore, expected to be brought into scope.

2. Ensuring information on the PSC is “current”

UK law currently requires entities to update PSC information on their own register as soon as practicable, and to confirm, via an annual confirmation statement, to Companies House. To meet the requirement of article 30 that information on the register is “current”, entities will be required to update their own PSC records within 14 days of a change (referred as an “event trigger”) and update the central register, held by Companies House, within a further 14 days.

Impacts of proposal

Data sources

The primary source for the present IA is evidence gathered to produce estimates in the Trust & Transparency (T&T) IA, written in 2014; that IA covered the introduction of the UK’s PSC regime. The IA utilised, in particular, a telephone survey of 575 companies, carried out by IFF Research, to gather cost estimates. To supplement the T&T estimates, the Department also contacted Companies House and surveyed a number of “presenters”, representing both entities currently in scope and those who will be brought in scope, and CIOs. (“Presenters” are companies which file documents, such as confirmation statements and annual accounts, with Companies House on behalf of their clients).

The IA's cost estimates, using Companies House's own internal projections, allow for the likelihood that the number of in-scope entities on the PSC register will grow over time.

One-off costs

Familiarisation costs

The Department estimates that the familiarisation cost for each entity newly brought into scope would be around £96 (equivalent to 3.6 hours of a manager's time). For those entities already in scope, familiarisation costs would be much lower: the Department assumes it would be a fifth of this amount. The combination of these assumptions results in an estimate of £76.4 million for familiarisation costs.

Entities finding out if they have a beneficial owner

Existing entities coming into scope of the PSC regime for the first time may not know whether they have a beneficial owner or owners. Even if they do, they will need to collect information or confirm that the information they have is accurate. The Department estimates that the cost of identifying, collecting, processing and storing beneficial ownership information will be £40.18 per organisation. Applied to the 86,517 organisations newly brought into scope, this gives a further one-off cost of £3.5 million.

Ongoing costs

Event-based filing and the annual confirmation

For organisations already in scope of the current regime, the only additional cost will be 'event-triggered' filings, estimated to cost £25.66. On pages 30-31 of the IA, the Department sets out its method for estimating the likely number of PSC changes; this leads to an estimate of half the number of companies on the register having to report a PSC change during the year. Using Companies House data, the Department, however, estimates that three quarters of these instances would involve a change to a director's details, which entities are, in any case, already required to provide. In these instances, the only additional action necessary is to 'copy and paste' the new details provided for the director into the text fields for the PSC information. It is assumed that this cost will be negligible. The number of additional event filings is, therefore, calculated as 3.64 million (the total number of entities on the register) x 0.5 x 0.25 = 0.45 million; this is multiplied by £25.66 to give an annual cost of £11.6 million in the first year.

For organisations newly brought into scope, the annual confirmation also represents a new cost, estimated at £14.06. Based upon the Department's new survey of CIOs, it is estimated that 80 per cent (9,491) of the 11,864 CIOs do not have a beneficial owner and will, therefore, not be required to take any action. The overall cost of additional annual confirmations is, therefore, estimated to be $77,026 \times £14.06 = £1.08$ million in the first year.

Familiarisation costs relating to new entrants

The IA also considers those who wish to set up new businesses of the type being brought into scope by the proposal; these will be required to be familiar with the beneficial ownership regime. The Department calculates the ratio of the number of new incorporations to the number of businesses on the Companies House register and applies this to its projections of the number of in-scope entities. It, then, applies the familiarisation costs described above, to arrive at an annual cost of around £13.6 million in the first year.

Overall costs

Allowing for forecast growth in the number of entities over time, the overall cost, in the first year, is estimated to be £109.1 million. In present value terms, ongoing costs average around £28 million each year. The equivalent annual net direct cost to business (EANDCB) is estimated at £39.0 million.

Quality of submission

The Department's approach of using evidence gathered for the T&T IA, supplemented by surveys of presenters and CIOs, appears to be proportionate given that the additional impact of the directive is much smaller from the introduction of the domestic PSC regime. The evidence presented is sufficient for the RPC to validate the EANDCB figure. As described below, there are some particularly good features of this IA and a number of areas where it could be significantly improved.

Areas of particularly good practice

These include:

- Over the appraisal period, the IA's baseline builds in an expected increase in the number of companies subject to the PSC regime using Companies House projections.
- The explicit capture of additional familiarisation costs to new entrants.

- A comprehensive sensitivity analysis (pages 41-43), which identifies the impact on the EANDCB of each assumption and clearly highlights the key assumptions for the EANDCB.
- A sensible, if explicitly limited, monitoring and evaluation plan.
- A clear presentation, in the table, of different types of costs and benefits.

Areas for improvement

Familiarisation costs. Although covered by the sensitivity analysis, the IA would benefit from providing clearer evidence to support the assumption, in the central case, that familiarisation costs for those already in scope would be 80 per cent lower than for those newly brought into scope.

Benefits to business. The IA states that a proportion of the costs to business will come from obtaining outside advice from service providers, such as accountants. The revenue to these providers is correctly excluded from the EANDCB. It is, however, incorrectly included in the societal NPV which, as a consequence, is reduced by 24 per cent in absolute terms. This inclusion results from it being incorrectly classified as an indirect benefit to business; this impact, instead, falls into the category 'resource used in complying with regulation', as set out in RPC case histories.² It should, therefore, not be included in the societal NPV (or, if it was, it would be cancelled out by the foregone benefit from putting these resources to alternative uses.)

Benefits of the proposal. The Department is unable to monetise the benefits of the proposal, but undertakes a break-even analysis. In this case, where the scope of existing arrangements is being extended slightly, a break-even analysis is not particularly informative. The IA would benefit from focusing on the likely balance of costs and benefits of the additional EU requirements, given the UK's decision not to include these requirements when it introduced the PSC regime in 2014.

Impacts on the public sector and individuals. The Department specifically excludes these impacts (page 38), but the IA would benefit from an assessment of these impacts.

Presentation. The IA would be improved by explaining that the overall figures in table 7 (page 38) do not exactly match those earlier in the IA - because they allow for a projected increase in the number of entities covered. The total cost figures (in

² <http://regulatorypolicycommittee.weebly.com/case-histories>.

paragraph 128 and box on page 33) appear to be incorrect and should, before publication, be amended. (The correct figure is in table 7, from which the EANDCB is calculated.) More generally, the IA would benefit strongly from clearer referencing of the various studies on which it draws.

Further impact assessments

Costs to industry-funded regulators, which the IA recognises will be a direct cost to business, have not, in this IA, been monetised. The Department explains that, at this stage, this is due to a lack of information about the potential costs of introducing these changes. The IA states that, in 2017, BEIS will submit a revised impact assessment, covering these costs, to the RPC.

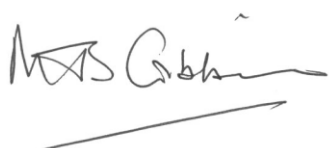
The RPC will also expect to see an IA, presumably from HM Treasury, covering the remainder of the directive.

Departmental assessment

Classification	Non-qualifying regulatory provision (EU)
Equivalent annual net direct cost to business (EANDCB)	£39.0 million
Business net present value	-£364.7 million
Societal net present value	-£276.2 million

RPC assessment

Classification	Non-qualifying regulatory provision (EU)
EANDCB – RPC validated	£39.0 million
Small and micro business assessment	Not required



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