



Financial
Intelligence Centre

Trust Service Providers- Why It Matters

20 September 2018

Presentation Points

- **The Global Consensus: Why Trusts Matter**
- **International Standards For Trust Service Providers**
- **Vulnerabilities of the Trust Service Provider Industry**
- **An Abuse of Trust**
- **The Test – An Effective AML/CFT Regime**
- **The Domestic Compliance Picture**
- **Changing the Terrain – Amending Item 2 to Schedule 1**
- **Who is / are the Beneficial Owner/s of the Trust?**
- **The Benefits To Better Regulating Trust Service Providers**
- **Selected Recommended Reading**

The Global Consensus: Why Trusts Matter

“Trusts provide an unparalleled degree of secrecy, making them an ideal getaway vehicle for money launderers”

Global Witness - Don't Take It On Trust, 23 Feb 2017

“Trusts often constitute the final layer of anonymity for those seeking to conceal their identity”

OECD – Behind the Corporate Veil, 2011

“While trust and company service providers (TCSPs) appear to be less likely to be the masterminds of schemes designed to obscure beneficial ownership, the services provided by TCSPs are vulnerable to exploitation by criminals and other professional intermediaries involved in these schemes.”

FATF & Egmont Group – Concealment of Beneficial Ownership, July 2018

The Global Consensus: Why Trusts Matter

The G20 High-Level Principles on Beneficial Ownership Transparency, Sydney 2014

- “The G20 considers financial transparency, in particular the transparency of beneficial ownership of legal persons and arrangements, is a high priority.”
- “The G20 Leaders’ Declaration from St Petersburg states, ‘We encourage all countries to tackle the risks raised by the opacity of legal persons and legal arrangements’.”
- “Improving the transparency of legal persons and arrangements is important to protect the integrity and transparency of the global financial system.”
- “Preventing the misuse of these entities for illicit purposes such as corruption, tax evasion and money laundering supports the G20 objectives of increasing growth through private sector investment.”

The Global Consensus: Why Trusts Matter

Caught Between Hammer (AML/CFT) and Anvil (Tax Collection)

The drive globally for greater transparency of corporate vehicles (including trusts)
is squeezing

- The Opaque Centre –

between the Combatting Tax Evasion Activities and Anti Money Laundering/Combating Financing
Terrorism measures both of which are tackling illicit financial flows to offshore havens

The Tax View – The OECD – Work on Taxation 2018

Tax is at the heart of our societies...Tax evasion is a significant component of illicit financial flows (IFFs)...Tax transparency and exchange of information is the best universal weapon to fight IFFs, shedding light on the legal and beneficial ownership of companies and other legal entities and arrangements located offshore, which are most often used to carry out illegal activities that result in IFFs.

The Global Consensus: Why Trusts Matter

Caught Between Hammer (AML/CFT) and Anvil (Tax Collection)

FATF & Egmont Group View, Concealment of Beneficial Ownership, 2018 - para 231

“The use of specialists and professional intermediaries is a key feature of schemes designed to conceal beneficial ownership.

The majority of case studies analysed involved professional intermediaries.

While it was not always explicitly stated in the case studies,

approximately **half of all cases** were assessed as involving a **complicit professional intermediary** (gatekeepers were determined to be complicit if, on the basis of the case summary provided, **they appeared to have had a role in designing the scheme, knew of the scheme’s illegal nature, or were charged with a crime**).

This demonstrates that although complicity may be a factor, it is not strictly necessary when facilitating a scheme designed to obscure beneficial ownership, and that some professionals are unwitting or negligent in their involvement.”

International Standards For Trust Service Providers

FATF has established standards on transparency, so as to deter and prevent the misuse of corporate vehicles.

“Despite the essential and legitimate role that corporate vehicles play in the global economy, under certain conditions, they have been misused for illicit purposes, including money laundering (ML), bribery and corruption, insider dealings, tax fraud, terrorist financing (TF), and other illegal activities.”

“This is because, for criminals trying to circumvent anti-money laundering (AML) and counter-terrorist financing (CFT) measures, corporate vehicles are an attractive way to disguise and convert the proceeds of crime before introducing them into the financial system.”

“The misuse of corporate vehicles could be significantly reduced if information regarding both the legal owner and the beneficial owner, the source of the corporate vehicle’s assets, and its activities were readily available to the authorities.”

FATF Guidance – Transparency and Beneficial Ownership, October 2014

International Standards For Trust Service Providers

FATF Recommendation 22 on designated non-financial businesses and professions” (DNFBPs)

- Includes lawyers, accountants, **trust and company service providers**, real estate agents and dealers in precious metals & stones
- The trust service providers required by the FATF to be covered by domestic AML/CFT legislation

Importance reflected in FATF Immediate Outcome 5:

- Legal persons and arrangements are prevented from misuse for money laundering or terrorist financing, and information on their beneficial ownership is available to competent authorities without impediments.

G20 Core Principle 5: the transparency of beneficial ownership of legal persons and arrangements

- Countries should ensure that **trustees of express trusts maintain adequate, accurate and current beneficial ownership information**, including information of settlors, the protector (if any), trustees and beneficiaries. These measures should also apply to other legal arrangements with a structure or function similar to express trusts.

Vulnerabilities of the Trust And Company Service Providers industry

- Trust and company service providers' industry is exposed to potential exploitation by those looking for ways to launder criminal proceeds or raise funds for terrorist activity
- This industry generally includes **All** those persons and entities that, on a professional basis, participate in the creation, administration and management of trusts and corporate vehicles (such as companies)
- Trust and company service providers and other similar professions (such as accountants) are acknowledged as gatekeepers to the financial system
- “Gatekeepers” can be described as those who provide gateways to the financial system through which potential users of the system, including launderers, can pass in order to do business with financial institutions

International Case Studies: An Abuse of Trust

The Trusted Presidential Palace

- The owner and beneficiary of a multi-million dollar presidential palace in Ukraine was hidden by a trust linked to former President Victor Yanukovich. While Yanukovich lived there, the estate was privatised in a “murky chain of operations” to a series of holding companies ultimately owned by a Lichtenstein trust. Soon after, opulent renovations began with nearly \$9.5 million spent on fittings in just 18 months, including a \$100,000 chandelier. Once this work was completed the estate included a five-story palace, golf course, yacht club and helicopter pad. Yet the owner and beneficiary of the palace, and its vast renovations, remains hidden by the Lichtenstein trust – the only information disclosed is that it is run by an Austrian lawyer.

An Abuse of Trust 2

Brunei Prince's "Jersey"

- A Brunei royal prince who stole billions from his country may have prevented an exclusive London property from being rightfully returned to Brunei using a Jersey trust. While Prince Jefri Bolkiah was the Finance Minister of Brunei and the chair of its sovereign wealth fund, the Brunei Investment Agency (BIA), he siphoned \$14.8 billion out of the fund into his personal bank accounts, funding a prolific international spending spree: 500 properties, antique paintings, 1000s of cars, 5 boats, private Boeing 747.
- While the BIA was attempting to recover these stolen assets, Prince Jefri bought most expensive house in UK, an exclusive property in the heart of London's Mayfair using an offshore company, owned by a Jersey trust.
- Beneficiaries were the Prince, his wife, the issue of the Prince, the issue of the parents of the Prince – including the Sultan.
- By using the trust to hide his ownership he may have been able to hide the property from the BIA to prevent it from being returned to the Brunei government.

An Abuse of Trust 3

Trusted Maltese PEPs Exposed

- Two Maltese politicians set up trust structures capable of keeping their business interests secret. The politicians, the Minister of Health and Energy Mizzi, and the Chief of Staff in the Prime Minister's office, Schrembri, both set up New Zealand trusts in 2015 run by Orion Trust, as trustees, the New Zealand arm of Mossack Fonseca, the notorious law firm at the heart of the Panama Papers leaks.
- Rotanuda Trust set up by Mizzi is a revocable trust, with his wife and children as beneficiaries – trust assets was not fully divested by the settlor into the trust.
- Haast Trust established by Schrembri, is a 'self-settled' trust with Schrembri both the settlor and beneficiary, undermining the intended separation between the settlor and beneficiaries of the trust.
- Panama Papers suggest that they intended to use the trusts to hide their prospective interests in other businesses. Maltese PEPS were openly permitted to hold shareholdings in other businesses.
- They could not explain the secrecy and need to disguise their interests through trusts. In response the politicians have said that the trusts were intended for family assets, properly declared and never exploited commercially.”

An Abuse of Trust 4

The Tolstoy Connection

- The October 2017 Judgment of Mr Justice Birss of UK High Court Chancery Division [HC-2014-000262] in Sergei Viktorovich Pugachev matter
- About 5 New Zealand discretionary Trusts set up by wealthy Russian oligarch and founder of Mehzprom Bank in 2011 and 2013 (4 trusts) for benefit of his mistress, Tolstoy's grand-niece, and their issue
- Sued by insolvent Mehzprom Bank and liquidator Deposit Insurance Agency for RUR 76.6bn
- Finding – At all times Pugachev regarded all assets in trusts as belonging to him and intended to retain ultimate control – all assets beneficially his before transfer to trusts
- The point of the trusts were not to cede control of his assets to someone else – it was to hide his control of them – a pretense to mislead other people – by creating the appearance the trust property did not belong to him when it really did
- The role of protector was the means by which control was exercised – none of protector's powers were fiduciary of nature – “were purely personal powers which may be exercised selfishly”

International Case Studies: An Abuse of Trust

The Tolstoy Connection

- Provisions in trust deed conferring an absolute or uncontrolled discretionary on the trustee, certain powers and discretions vested in trustee only exercisable by prior written consent of the protector
- The position of son Victor as potential Protector was part of the pretence – Victor was acting on his fathers instructions
- Named beneficiaries would benefit from the use of assets of the trusts but that would only be on Pugachev's say so – it would be just the same as a situation in which settlor was in control and that control was not hidden
- With Pugachev as protector the true effect of all trust deeds leaves Pugachev in control of the trust assets – Pugachev is the beneficial owner – they amount to a bare trust for Pugachev
- True effect of trust deeds – Pugachev's intention by setting up trusts was to retain control of all trust assets
- If this interpretation is wrong, such that Pugachev was divested of beneficial ownership of the trust assets, then the trusts are shams and should not be given effect to!

The Test - An Effective AML/CFT Regime

An effective system can and should demonstrate the following:

- Basic information is available publicly, and beneficial ownership information is available to competent authorities.
- Persons who breach these measures are subject to effective, proportionate and dissuasive sanctions.
- This results in legal persons and arrangements being unattractive for criminals to misuse for ML and TF
- The FATF Recommendations require countries to ensure that adequate, accurate and timely information on the beneficial ownership of corporate vehicles (including trust arrangement) is available and can be accessed by the competent authorities in a timely fashion.

Characteristics of an effective system: Measures are in place to:

- prevent legal persons and arrangements from being used for criminal purposes;
- make legal persons and arrangements sufficiently transparent; and
- ensure that accurate and up-to-date basic and beneficial ownership information is available on a timely basis

Making The FIC Act Effective

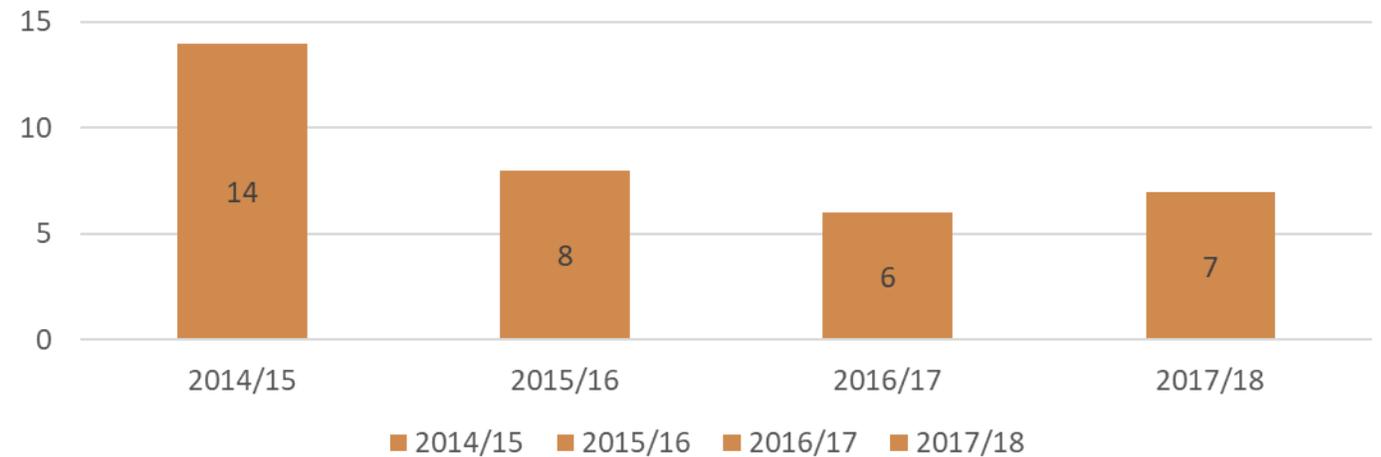
- Central to implementing the AML/CFT regime, is the FIC Act's intent of:
 - making the financial system transparent
 - requiring affected institutions to apply risk based customer due diligence measures
 - to better know its customer, their financial transactions and source of funds used
- Institutions achieve customer due diligence measures by adequately capturing required customer information in their records
- Institution report transactions to FIC for analysis of ML and TF activities, where necessary
- The FIC uses the regulatory information submitted by affected institutions, businesses and persons as well as additional information to develop its financial intelligence reports
- FIC makes referrals to or responds to requests for assistance from mandated agencies

Trust Companies Registered & Inspected

	Trust Companies registered	Trust Companies inspected
2018/2019*	177	
2017/2018	173	7
2016/2017	154	6
2015/2016	140	8
2014/2015	128	14
2013/2014	110	
2012/2013	88	
2011/2012	130	

*Figures for 2018/2019 is for the period 1 April 2018 to 31 August 2018.

Inspections conducted on Trust Companies the last 4 years



FIC Reporting Statistics - Trust Companies

Trust Companies	CTR		CTRA		Total S28 CTR/CTRA	STR	SAR	Total S29 STR/SAR	Total S28A TPR
	Number of Batches reported	Number of Transaction Reports	Number of Transaction Reports	Number of underlying Transactions	Number of Transaction Reports	Number of Reports	Number of Reports	Number of Reports	Number of Reports
2018/2019*	14	16	192	3,639	208	3	1	4	-
2017/2018	29	29	315	4,369	344	6	1	7	-
2016/2017	50	58	349	2,301	407	22	-	22	-
2015/2016	82	-	-	-	82	10	-	10	-
2014/2015	64	-	-	-	64	10	-	10	-
2013/2014	59	-	-	-	59	14	-	14	-
2012/2013	95	-	-	-	95	8	-	8	-
2011/2012	101	-	-	-	101	-	-	-	-
2010/2011	18	-	-	-	18	-	-	-	-

*Figures for 2018/2019 is for the period 1 April 2018 to 31 August 2018.

Domestic Compliance Picture under FIC Act

New 7 Pillars of Compliance, Reporting and Inspections



FIC Amendment Act – Key Changes

Requirement	FIC Act	FIC Amendment Act
1 - Customer Due Diligence (CDD)	Rules-based, obtain information referred to in Regulations based on client type	Risk rate clients and apply CDD in accordance with client risk, understand business and source of funds, beneficial ownership, foreign and domestic prominent persons, ongoing due diligence.
2 - Record Keeping	Record of business relationship and transactions to be kept for 5 years	Records of business relationship, transaction and reports filed to be kept for 5 years – also in electronic format if preferred
3 - Reporting	STR, CTR and TPR reports to be submitted when required	Property associated with UN Security Sanctions to be reported and reports to be made available for inspection purposes
4 - Document Risk Processes and Procedures	Internal rules on CDD, record keeping and reporting as required under Regulations 25, 26 and 27	Develop, document, maintain and implement a Risk Management and Compliance Programme (RMCP) describing the identification, mitigation and managing of AML/CFT risks explained in section 42

FIC Amendment Act – Key Changes (continued)

Requirement	FIC Act	FIC Amendment Act
5 - Compliance Officer	Compliance Officer to be appointed to ensure compliance with FIC Act by AI and its employees	Responsibility for FIC Act compliance by highest authority and appointment of competent person(s) to assist with compliance
6 – Training	Training to be provided to employees to comply with the FIC Act and internal rules	Ongoing training to be provided to comply with FIC Act and RMCP
7 - Registration with FIC	All AIs and RIs to register under the appropriate Schedule item	All AIs and RIs to register under the appropriate Schedule item
3A - Targeted Financial Sanctions		Freeze property, service or support relating to persons and entities identified by UN Security Council Targeted Financial Sanctions and report to FIC

Changing the Terrain: Amending Item 2 to Schedule 1

South Africa's capability to combat ML and TF is being enhanced, as follows:

- The FIC Amendment Act 2017 (Act No. 1 of 2017) finally aligned regime to the 2012 FATF Standard;
- The Amendment of FIC Act Schedules 1, 2 and 3 will include new sectors required to be covered by the FATF Standard
- An Amendment of Schedule 1 in relation to Trust Service Providers must better align the scope of activity to FATF requirements and assist in fulfilling Recommendation 25: Transparency and Beneficial Ownership of Legal Arrangements
- The Consultation must answer whether Item 2 of Schedule 1 of the FIC Act, which now reads:
“A board of executors or a trust company or any other person that invests, keeps in safe custody, controls or administers trust property within the meaning of the Trust Property Control Act, 1988 (Act 57 of 1988).”

adequately and clearly covers the require activities contained in FATF Recommendation 25?

Changing the Terrain: What Activities Are Covered

The FATF Standard requires Trust and Company Service Providers to be covered under the scope of the FIC Act when they prepare for or carry out transactions for a client concerning the following activities:

- Acting as a formation agent of legal persons and arrangements;
- Acting as (or arranging for another person to act as) a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons and arrangements;
- Providing a registered office; business address or accommodation, correspondence or administrative address for a company, a partnership or any other legal person or arrangement;
- Acting as (or arranging for another person to act as) a trustee of an express trust or performing the equivalent function for another form of legal arrangement;
- Acting as (or arranging for another person to act as) a nominee shareholder for another person.

Changing the Terrain: What To Know

What to Know

As in general, the lack of adequate, accurate and timely beneficial ownership information facilitates ML/TF by disguising:

- the identity of known or suspected criminals,
- the true purpose of an account or property held by a corporate vehicle, and/or
- the source or use of funds or property associated with a corporate vehicle.

The Trust Practitioner needs to know:

- ❖ the identity of known actors: the settlor/s, trustee/s, protector (if any), beneficiaries / class of identifiable or ascertainable beneficiaries;
- ❖ the true purpose of an account or property held by a corporate vehicle; and/or
- ❖ the source or use of funds or property associated with a corporate vehicle; AND
- ❖ The Beneficial Owner/s of the Trust

Who is / are the Beneficial Owner/s of the Trust?

- ❖ Mindful of the Separation of Legal Ownership v Beneficial / Economic / Equitable Ownership
 - Settlor – to identify the origins of the trust assets
 - Trustee – to identify who currently controls and manages the trust assets
 - Beneficiary or class of beneficiaries – to identify who is or will ultimately benefit from the assets held by the trust,
 - Protector (if any) – or other **natural person** exercising control
- ❖ The view of international compliance officers

Extent of Coverage – Which Professionals??

- **All Professionals** involved in the creation, administration or management of an express trust in South Africa or of a similar structure outside the Republic, except for a trust established by virtue of a testamentary writing or court order

FATF Defines Beneficial Owner & Beneficiary

“**Beneficial owner** refers to the natural person(s) who ultimately **owns or controls** a customer **and/or** the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.”

“**Beneficiary** - In trust law, a beneficiary is the person or persons who are entitled to the benefit of any trust arrangement. A beneficiary can be a natural or legal person or arrangement...”

FATF Interpretative Note to Recommendation 10 – C.5.b.(ii).i.

Identify the beneficial owners of legal arrangements:

“For Trusts - the identity of the settlor, the trustee(s), the protector (if any), the beneficiaries or class of beneficiaries, and any other legal person exercising ultimate effective control over the trust (including through a chain of control/ownership);”

No cascade applied - because all the related parties have to be identified from the beginning

Benefits to Better Regulating Trust Service Providers

- Better AML/CFT regulation of trust service providers would require understanding and awareness of ML/TF risks and tighten the sector against criminal exploitation;
- Better understand the identity of the client (whether settlor, trustee, or beneficiary), the source of funds used by a client for a transaction and the nature of the intended business relationship with the client;
- Better Transparency of useful legitimate trust vehicle that may be misuse for illicit and illegal purposes;
- Spreading the regulatory coverage (and burden) to all sectors vulnerable to ML/TF abuse;
- Closing regulatory, financial intelligence, investigative and prosecution gaps to facilitate “the following of the money”;
- Ultimately enhancing the reputation of the South African trust industry and financial system, as one having integrity.

Selected Recommended Reading

- FATF, Concealment of Beneficial Ownership, July 2018.
- G20 High-Level Principles on Beneficial Ownership Transparency, Sydney 2014
- FATF Guidance on Transparency and Beneficial Ownership, October 2014
- World Bank, The Puppet Masters: How the Corrupt Use legal structures to hide stolen assets and what to do about it, 2011.
- FATF Typology Report, Laundering the Proceeds of Corruption; July 2011.
- Judgment of Mr Justice Birss of UK High Court Chancery Division [HC-2014-000262] in Sergei Viktorovich Pugachev matter, October 2017.
- OECD, Behind the Corporate Veil, 2011
- Global Witness, Don't Take It On Trust, 23 Feb 2017

Summation & Questions

