

The Trust Property Control Act Amendment



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Financial Action Task Force (FATF)

- ✧ Intergovernmental policymaking body combatting all forms of money laundering and terrorism financing
- ✧ Paris-based
- ✧ Over 200 members
- ✧ Sets global anti-money laundering (AML) and counter financing terrorism (CFT) standards to prevent the illicit exchange of finances and activities that harm society
- ✧ Ensuring the implementation of FATF standards and also holds the nation accountable for compliance failures

Money Laundering

- ✧ Criminal act of legitimizing the money acquired through illegal or unethical means by disguising the origin of the crime
- ✧ Usually involves the creation of assets to conceal the relationship between the funds and their dirty sources
- ✧ People do laundering by often exploiting the vulnerabilities of legal or financial systems
- ✧ 3 stages of money laundering:



Placement



Layering



Integration

What is a FATF greylisting?

- ✧ To be greylisted by the FATF means a country's shortcomings threaten the international financial system
- ✧ Serious blow to a country's reputation
- ✧ Subjected to increased monitoring and has to deal with adverse economic consequences for trade and transactions with other countries
- ✧ Regulators in the US, the UK and the EU may also restrict their banks from transacting with greylisted countries' banks
- ✧ The list essentially warns of the significant danger of money laundering and terrorism financing that a particular nation holds in global dealings
- ✧ Mutual evaluation considers compliance standards from two angles:
 - ✧ technical compliance (whether South Africa has the necessary infrastructure and legislation in place to be comply with the FATF standard)
 - ✧ effectiveness of the legislation

Which countries got the badge?

Greylisted (increased monitoring):

- ✧ Albania
- ✧ Barbados
- ✧ Burkina Faso
- ✧ Cambodia
- ✧ Cayman Islands
- ✧ Democratic Republic of Congo
- ✧ Gibraltar
- ✧ Haiti
- ✧ Jamaica
- ✧ Jordan
- ✧ Mali
- ✧ Morocco
- ✧ Mozambique
- ✧ Panama
- ✧ Philippines
- ✧ Senegal
- ✧ South Sudan
- ✧ Syria
- ✧ Tanzania
- ✧ Turkey (first G20 country - is SA second?)
- ✧ Uganda
- ✧ United Arab Emirates (FATF has worryingly raised more serious concerns about SA than it did about the UAE)
- ✧ Yemen

Blacklisted (non-cooperative in the global fight against money laundering and terrorist financing):

- ✧ North Korea
- ✧ Iran
- ✧ Myanmar

What could the impact be? Mixed results

Studies:

- ✧ Recent IMF study - capital inflows typically decline by 7.6% of GDP at the time of a greylisting (with a typical range of 4.5% to 10.5%)
 - ✧ Two empirical studies found that blacklisting had no significant and enduring impact on banking flows and tax havens
 - ✧ Latin American study - small (0.3% - 0.4% of GDP) impact on foreign direct investment (FDI) but no consistent impact on other flows
 - ✧ Two further studies - 10% and 15% decline in cross-border receipts and growth in bank inflows, respectively
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- Difficulty in accurately estimating the economic impact of the FATF's greylisting and/or blacklisting
 - Investors would typically react to these fundamentals independently and not only to the listing status itself
 - Already priced in the risk of transacting with and within the SA financial system.
 - Mirrors the same dynamic as that of a sovereign credit rating downgrade

However...

Safe to assume that landing on the grey list will be detrimental to the integrity of the SA banking system and jeopardise the country's relationships with overseas banks

- ✧ Regulators from some of SA's main trading partners, such as the US, the UK, China and Japan, may restrict their banks from transacting with SA banks
- ✧ Of those able to transact, the associated costs will be raised significantly. May have a material adverse impact on capital flows and subsequent growth, as well as on the currency and bond markets.
- ✧ Will become increasingly difficult to invest offshore, even for the wealthiest investors

Mauritius a good example

- ✧ Was able to get off the greylist in under 2 years, much to its longer-term economic benefit
- ✧ Initially greylisted in February 2020 for several reasons:
 - ✧ Lack of effective risk-based supervision
 - ✧ Limited access to beneficial ownership information
 - ✧ Insufficient oversight of non-profit organisations that may be subject to terrorist financing
 - ✧ General ineffectiveness in conducting money laundering investigations
- ✧ After quickly and proactively implementing the necessary reforms, the country's financial sector is beginning to stand out for all the right reasons - attracting significant international growth and development opportunities

Mauritius a good example (cont.)

- ✧ Now fully compliant with 39 of the 40 FATF recommendations
- ✧ FATF-approved objectives set out across core strategies such as:
 - ✧ Strengthening AML/CFT legal and regulatory frameworks to meet international standards, effectively mitigating risks
 - ✧ Implementing a comprehensive, risk-based supervision framework to monitor financial institutions and designated non-financial businesses, such as real estate brokers, banking and securities, and jewellery stores
 - ✧ Improving the process of detecting fraud threats, prosecuting criminals, and confiscating illegal proceeds
 - ✧ Enhancing the transparency of legal persons and enlisted national coordination, as well as regional and international cooperation
 - ✧ Increasing training and capacity and raising awareness to ensure all stakeholders are working in accordance with AML/CFT obligations
 - ✧ Implementing an AML/CFT data collection system to continuously improve risk detection

Pakistan - comparable to SA?

- ✧ Pakistan's economy is a similar size to that of South Africa
- ✧ On FATF's grey list since June 2018!
- ✧ Pakistan's exit from the grey list recently has brought little cheer to the country's economy, according to media reports, "even as estimates suggest that the cumulative real GDP losses for the country due to the blacklisting had soared to US\$38 billion" (R675 billion)

SA findings by FATF

- ✧ The review did not go well
- ✧ SA has “a solid legal framework to fight money laundering and terrorist financing” but has “significant shortcomings implementing an effective system, including a failure to pursue serious cases”
- ✧ The FATF final report, published in October 2021, showed full compliance in only three of 40 technical areas
- ✧ Out of 40 ratings on legislation adequacy, half of SA’s ratings scored as partially compliant or non-compliant
- ✧ Out of 11 ratings on the efficiency of implementing the legislation, SA was scored critically weak on all ratings

SA findings by FATF (cont.)

SA's three most-critical weaknesses are:

1. customer due diligence;
2. terrorist financing offences; and
3. targeted financial sanctions for terrorism and terrorist financing

- ✧ SA principally struggles to detect and prosecute terrorist-financing offences (Based on scorecard on the work of the Directorate for Priority Crime Investigation (DPCI or Hawks), police, intelligence agencies and the National Prosecuting Authority (NPA))
- ✧ Authorities' understanding of terrorist-financing risks is "underdeveloped and uneven"
- ✧ Law enforcement "lacks the skills and resources to proactively investigate money laundering and terror financing." (Mutual evaluation report)

Timeline for SA

- ❖ Period in 2019 - SA was evaluated for a on its anti-money laundering and combatting the finance of terrorism systems through a peer review process facilitated by the FATF
- ❖ October 2021 - published an evaluation of SA's anti-money laundering measures. It is a two-fold assessment of the adequacy of SA's legal framework and the efficiency with which legislation is implemented
- ❖ 29 August 2022 - National Treasury published the General Laws (Anti-Money Laundering) Bill.
- ❖ 4 October 2022 to 10 October 2022 - Period for public comment - 6 days!
- ❖ 25 October 2022 - date until public comment re-opened
- ❖ SA had until October 2022 to show FATF that it has made sufficient progress in remedying the identified deficiencies
- ❖ 11 October 2022 - A public hearing by SCOF
- ❖ 22 December 2022 - Signed into law General Laws (Anti-Money Laundering) Act
- ❖ 23 December 2022 - Signed inot law Protection of Constitutional Democracy Against Terrorism and Related Activities Amendment Act
- ❖ SA authorities attended a face-to-face meeting with the FATF Joint Group in Rabat, Morocco on 13 January 2023
- ❖ International Co-operation Review Group make final recommendation to the FATF Plenary
- ❖ FATF is due to make its final decision on the composition of the formal greylist 22 - 24 February 2023

The scramble...

- ✧ Significant progress had to be made in a very short period to avoid such an adverse outcome of the FATF process currently underway
- ✧ FATF assessments lend substantial weight to any demonstrable effort by policymakers (such as interventions by the SARB and Treasury) to address SA's shortcomings
- ✧ FATF assessments embody inherent subjectivity, which clouds estimating any probability that SA can make enough progress timeously to avoid being greylisted
- ✧ “High” probability of such an outcome appear pertinent

The plan for SA

- ✧ Cabinet approved a raft of new amendment bills in late August 2022
- ✧ The omnibus of bills amends the Financial Intelligence Centre Act, the Non-profit Organisations Act, Trust Property Control Act, the Companies Act and the Financial Sector Regulations Act. Aim to respond to the deficiencies identified during the peer review of the country conducted by the FATF; address around 14 of the 20 areas in which the FATF found SA deficient.
- ✧ The Protection of Constitutional Democracy against Terrorist and Related Activities Amendment Act addresses 2 other deficiencies
- ✧ Remaining technical deficiencies - addressed through various non-statutory initiatives
- ✧ Completed a second round of assessments of money laundering and terrorist financing risks and developed a national strategy to address these
- ✧ Other aspects of the FATF review will require a broader political response to correct. Authorities will need to restore confidence in SA's capacity to deliver accountability for state capture crimes and its ability to recoup the funds looted from state institutions by those implicated in high-level state capture offences

Could kick-start and accelerate much-needed reforms to counter fraud, corruption, and terrorism financing in SA

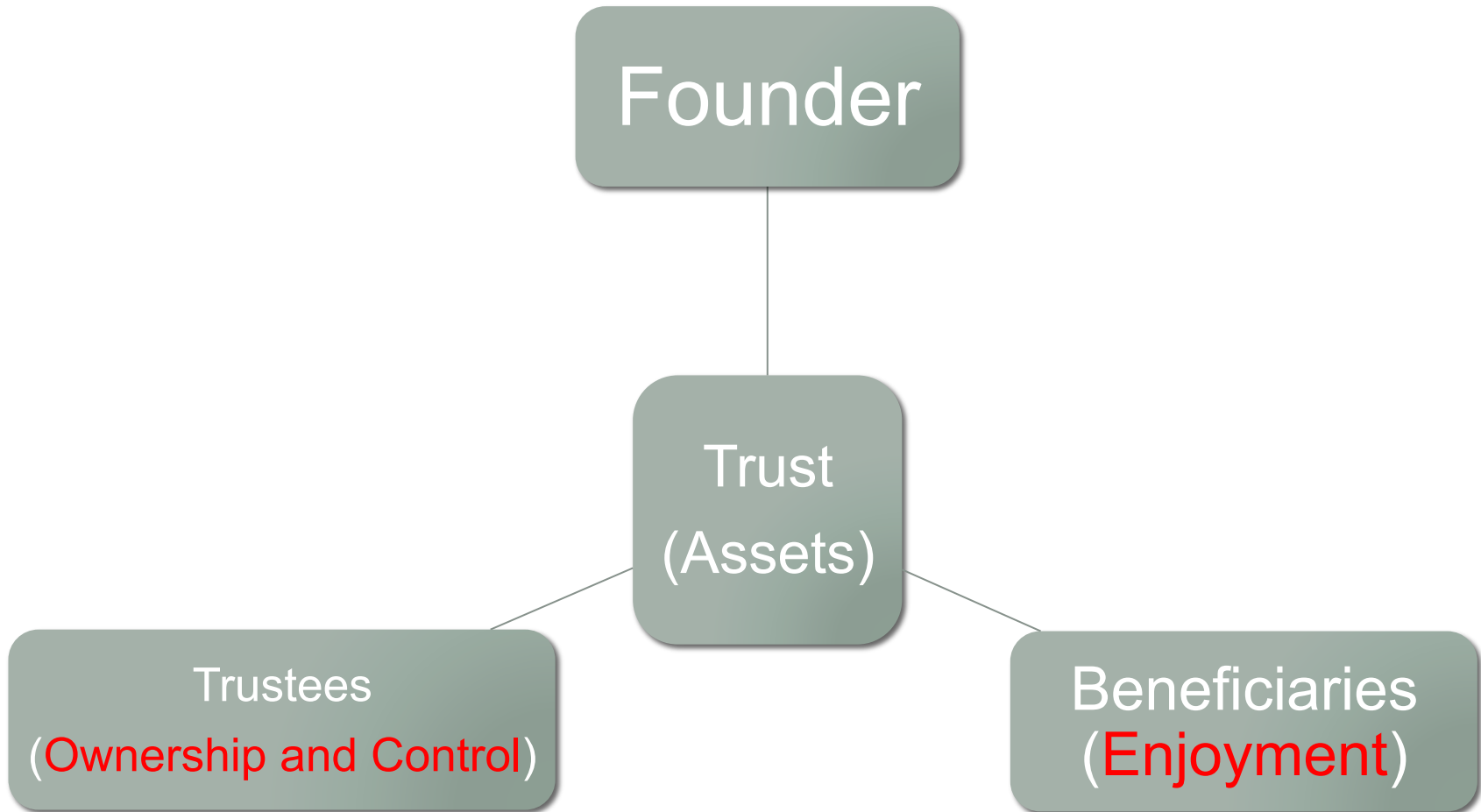
The TPCA targeted

- ✧ Currently, the Master's Office only has records of the identity of trustees, founders and the beneficiaries specifically named in the trust instrument
- ✧ No requirement to disclose the ultimate ownership or control of these persons
- ✧ The requirement for trustees to record and disclose this information would make the control and use of trust structures significantly less uncertain

The TPCA targeted (cont.)

- ✧ The Trust Property Control Act, 1988 (TPCA) was last amended in 1997. Mainly deals on a high level with trust operations and the office of the Master of the High Court as the trust regulator
- ✧ The General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act, however, proposes significant changes to the TPCA. The intention of the amendments is to prevent the misuse of trusts and ensure that there is adequate, accurate, and timely information on the control of trusts available to the authorities.
- ✧ Amendments will set vague, complex, and unrealistic limitations on the trustees of trusts and may cause convicts of ordinary citizens who are only attempting to do their duty

Why is a trust unique?



Beneficial owner?

- ✧ Include new definition of a “beneficial owner” of a trust - align with the definition of “beneficial owner” in the Financial Intelligence Centre Act. The definition covers “*anyone who directly or indirectly ultimately owns the relevant trust property or exercises effective control of the administration of the trust*”. However, the definition in the latter Act is clearly confined to “a legal (or juristic) person”, which a trust is not. This specifically includes:
 - ✧ trustees, including the controllers of a corporate trustee (i.e. a trustee which is a legal person or representative of a partnership and not a natural person)
 - ✧ the trust’s founders, and if a founder is a legal person or partnership, its ultimate controllers
 - ✧ any beneficiary referred to by name in the trust instrument, and if a beneficiary is a legal person or representative of a partnership, its ultimate controllers
 - ✧ any person who can control the votes of, or appoint, trustees or beneficiaries

Beneficial owner?

- ✧ English law notion of a ‘divided’ ownership - recognises divided title in that a trustee holds “legal ownership” and the beneficiary holds “equitable ownership” in the same trust property. In SA law a trust beneficiary under an ownership trust does not hold a real right to the trust property, but only a personal right against the trustee to enforce the provisions of the trust deed. The use of the term “beneficial owner / ownership” to describe the legal position of the SA trust beneficiary - inaccurate
- ✧ The SA concept of trust differs substantially from the Anglo-American legal systems’ concept of trust, from which the amendments seem to originate
- ✧ Blanket inclusion of “*each beneficiary referred to by name in the trust deed or other founding instrument in terms of which the trust is created*” as a “beneficial owner” - not in line with our law. No distinction between ownership trust and bewind trust.

Beneficial owner?

- ✧ Definition of beneficial owner, recognised by FATF, focuses on:
 - ✧ natural (not legal) persons who own and take advantage of capital or assets of the legal person
 - ✧ those who really exert effective control over it

- ✧ Inclusion of trustees in the definition of “beneficial owner” of a trust was in conflict with the role of a trustee as envisaged by the existing definition of a “trust” in the Trust Property Control Act
 - ✧ Act does not amend the definition of a “trust”. A trustee, in South African law, does not hold trust property for his or her own benefit but for the benefit of another person. Therefore, a trustee can never be the “beneficial owner” of the trust property.
 - ✧ Including a trustee under the definition of “beneficial owner” is incompatible with the fiduciary duty required of a trustee as envisaged by Section 9 of the TPCA

More changes to TPCA

- ✧ Definitions of ‘accountable institution’ and ‘beneficial owner’ into Section 1 of the TPCA. Amend Section 10 of the TPCA to require a trustee to disclose their position as trustee to any accountable institution with which the trustee engages in that capacity, and to make it known to that accountable institution
- ✧ Section 6 - to specify matters that would disqualify a person from acting as a trustee, for example failing the ‘fit and proper’ test
- ✧ Disclosure details in Section 11(1) of the Act will be prescribed by way of regulation
- ✧ New Section 11A - information that must be kept by trustees in relation to beneficial ownership:
 - ✧ trustees must keep up-to-date records of the beneficial ownership of the trust and lodge a register of the prescribed information on the beneficial owners (as defined) with the Master;
 - ✧ the Master must keep a register in the prescribed form containing the prescribed information about the beneficial ownership of trusts; and
 - ✧ trustees and the Master must make the information contained in the register available to any person as prescribed after consultation with the Minister of Finance and the Financial Intelligence Centre
- ✧ The definition of “beneficial owner” in clause 1 of the Bill, together with the proposed insertion of section 11A into the Act, contains provisions which may open the door to premature acquisition of certain rights by beneficiaries of the trust. This will encroach on the discretion afforded to trustees and severely limit existing rights of trustees and the founder of a trust.
- ✧ New independent trustee - to get info regarding founder - may be impossible - amendment of section 19 of the Act

Complaints

- ✧ Lack of consultation
- ✧ A trust not a legal person - definition of “beneficial owner” refers to someone who “control[s] the votes of the trustees”
- ✧ Trusts are not corporate structures as trusts do not have legal personality, but are, according to the Supreme Court of Appeals, accumulations of assets and liabilities
- ✧ A trustee in South African law cannot legally be “controlled” by another person. Any attempt at such “control” is null and void and, where such *de iure* control is written into a trust instrument, will result in a void trust
- ✧ Any “*person who, through the ability to control the votes of the trustees or to appoint the trustees, or to appoint or change the beneficiaries of the trust, exercises effective control of the trust*”
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- ✧ De facto control, not *de iure* control - abuse of trust form
- ✧ Control written into trust instrument - *de iure* control - sham trust, trustees do not have sufficient independence, substance over form

Complaints (cont.)

- ✧ If a beneficiary learns from the disclosure required by the proposed amendments that s/he is a beneficiary, that beneficiary can notify the trustees in writing that the benefit is accepted and can then never be removed as beneficiary without his/her agreement
- ✧ Devastating effect on the cost of proper trust administration, particularly in the case of smaller trusts where vulnerable beneficiaries need benefits intended for them to be protected effectively

Complaints (cont.)

- ✧ No indication as to how far a trustee must go to “establish” the “beneficial ownership” - do whatever it takes?
- ✧ It appears that the information required about “beneficial ownership” is to be regulated by the Minister in consultation with the FIC, without any need to involve industry bodies or Parliament. This is clearly undesirable as it places far too much power in the hands of the Minister and the FIC to dig into the private affairs of individuals.

Alternative solution

- ✧ Trustee is not a beneficial owner of a trust and should not be included in the definition
- ✧ It is important for law enforcement agencies to know who the parties (potential or real) controlling, or deriving benefit from, a trust happen to be. This can be achieved by placing appropriate duties of disclosure on the trustees, with the proviso that these duties should not place unfair and impractical burdens on trustees
- ✧ Trustees to give details of parties to the trust to master in prescribed format
- ✧ Submit changes to the Master
- ✧ Identity and other details of named beneficiaries should not be open to anyone other than the Master and the FIC, to prevent the premature acquisition of rights under the trust by such beneficiaries
- ✧ Powers to FIC to inspect records

Thank you!

Linkedin -

<https://www.linkedin.com/company/trusteeze-pty-ltd>

For a free demo of our platform -

<https://lnkd.in/e4jvz2F3>

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