

**Out of the dark:
Unveiling hidden
risk associated
with ultimate
beneficial
ownership**

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In an era that requires heightened corporate transparency, organizations are increasingly obliged to know the individuals who ultimately own the businesses they plan to or are currently partnering with. This need to understand ownership structures extends beyond financial services into many industries, and being able to identify beneficial owners and the associated risks they pose is a crucial aspect of a business' entity verification and risk mitigation strategies.

Central to the need for identifying beneficial owners and ultimate beneficial ownership (UBO) is understanding where potential money laundering, terrorist financing, and sanctions evasion risks lie concealed within a third-party network. These illicit activities pose compliance issues, potential for reputational damage, and they can threaten global financial stability and security.

This whitepaper delves into the complexities surrounding UBO identification and explores best practices to mitigate hidden risks as part of combating financial crime. By recognizing the significance of UBO disclosure and the potential repercussions of non-compliance, organizations can implement proactive measures to help safeguard their business and its reputation, mitigate risks, and contribute to a more transparent and secure global financial landscape.

INTRODUCTION

The Financial Action Task Force (FATF) sets comprehensive global standards – known as [FATF Recommendations](#) – to combat money laundering and terrorist financing. Recommendations 24 and 25 provide guidance for institutions and countries on implementing FATF's beneficial ownership standards.

To establish a clear threshold for identifying significant beneficial ownership via ownership interest, the FATF recommends that countries set a maximum benchmark of 25%¹. This means that an individual is considered a significant beneficial owner if they have a direct or indirect ownership interest of 25% or more in a business entity.

When considering beneficial ownership through control or other means, financial institutions should consider other factors outside of ownership interest, such as: differential voting rights; control through other legal vehicles, informal means, or debt instruments; and power to appoint the majority of senior management. Seeing as these are factors that could be in place without a 25% ownership, there are cases in which this FATF recommended threshold does not serve as a measure for determining UBO.

25%

FATF's recommended threshold for significant beneficial ownership

Direct ownership

Direct ownership refers to situations where an individual holds shares or other equity interests in an entity directly. This can include:

- Common shares: The most common type of equity, representing ownership in a company.
- Preferred shares: Shares that offer specific rights, such as a guaranteed dividend, but may have limited voting rights.
- Warrants: Options to purchase shares at a specified price within a certain period.

Indirect ownership

Indirect ownership occurs when an individual controls a business entity through intermediaries, such as:

- Trusts: Legal entities that hold assets on behalf of beneficiaries.
- Nominees: Individuals or entities that hold assets or property on behalf of another.
- Holding companies: Companies that own shares in other companies.
- Partnerships: Business structures where two or more individuals or entities share profits and losses.

¹ [Guidance on Beneficial Ownership of Legal Persons](#), FATF, March 2023

To determine indirect ownership, institutions may need to analyze the ownership structure of multiple entities to identify the ultimate beneficial owner. This can involve tracing ownership through various layers of intermediaries and considering factors such as voting rights, control mechanisms, and economic interest.

The FATF 25% threshold has become a widely accepted standard in the financial services industry and more broadly. It is used by financial institutions, corporations, and other organizations as a component of their compliance and risk assessment processes to prevent money laundering, terrorist financing, and other illicit activities.

THE UBO IDENTIFICATION CHALLENGES INSTITUTIONS FACE

Lack of standardized frameworks

A significant challenge facing institutions in UBO identification is the absence of universally adopted reporting frameworks. This lack of standardization leads to several key issues:

- **Inconsistent data formats:** Different jurisdictions may have varying requirements for UBO data formats, making it difficult for institutions to consolidate and compare information from multiple sources.
- **Difficulty in data exchange:** The lack of standardized reporting frameworks can hinder the efficient exchange of UBO information between institutions, regulators, and law enforcement agencies, in turn creating challenges in cross-border investigations.
- **Increased compliance burden:** Institutions may need to comply with multiple sets of reporting requirements, increasing their administrative costs and compliance burden.
- **Limited data interoperability:** The absence of standardized frameworks can make it challenging to integrate UBO data with other relevant data sources, such as financial transaction data or customer due diligence information.

There is a growing need for the development and adoption of international standards for UBO reporting. In 2023, FATF updated its guidance on beneficial ownership of legal persons (Recommendation 24) and legal arrangements (Recommendation 25²) to mitigate some challenges in implementing earlier guidance on transparency of beneficial ownership requirements³. Such standards could help provide a common framework for data collection, exchange, and analysis, thereby improving the effectiveness of UBO identification efforts and enhancing global financial transparency.

Data quality and completeness

The quality and completeness of beneficial ownership data can be hindered by several factors. Firstly, while shareholder registers often provide information on legal ownership, they may not accurately reflect beneficial ownership. This potential discrepancy may arise due to a variety of corporate arrangements, including the use of nominee shareholders, trusts, or complex corporate structures (e.g., shell companies, holding companies, and offshore entities), which can obscure the ultimate beneficiary. These arrangements can make it more difficult to trace ownership chains and accurately identify the individuals who ultimately control a company.

Secondly, institutions may face difficulties in obtaining accurate information from shareholders. This can be attributed to several factors, including:

- **Limited authority or power to request information:** Institutions may lack authority to compel shareholders to provide accurate and up-to-date beneficial ownership information, especially in jurisdictions with weaker corporate governance standards.

² [Guidance on Beneficial Ownership and Transparency of Legal Arrangements](#), FATF, March 2024

³ [Guidance on Transparency and Beneficial Ownership](#), FATF

- **Lack of timely notification:** Shareholders may not be required to notify the company within a specified time period when there are changes in ownership or control, leading to outdated information.
- **Non-disclosure of beneficial owners:** Shareholders may not be required to disclose the names of the individuals on whose behalf shares are held, particularly in jurisdictions with secrecy laws or fewer transparency requirements.
- **Difficulty in verifying information:** Companies may struggle to verify the accuracy and completeness of the information provided by shareholders, especially when dealing with complex corporate structures or when there is a lack of supporting documentation.

Thirdly, law enforcement agencies may encounter difficulties in enforcing beneficial ownership requirements for non-resident subjects who operate in multiple countries, as different jurisdictions implement UBO disclosure rules to varying degrees. This can be particularly challenging when individuals from one jurisdiction are operating in another jurisdiction (often with a different legal framework) or where there is limited cooperation among authorities.

Complexity of corporate structures

The complexity of corporate structures can pose significant challenges to UBO identification. Companies may employ opaque ownership structures, such as anonymous shell companies or trusts, which in turn may obscure the identities of beneficial owners. These complex structures create multiple layers of ownership between the company and the UBO, potentially making it difficult to trace the exact level of ownership and the key individuals involved.

Frequent changes in ownership also make corporate structures highly dynamic. Those within a business or financial institution tasked with maintaining up-to-date UBO information may have challenges responding as swiftly as the changes happen. Moreover, regulated businesses are tasked with continuous monitoring of the ownership structure for purposes of identifying newly sanctioned individuals in the structure and taking subsequent actions to comply with sanctions regimes – obligations that intersect with UBO identification and the potential difficulties in doing so.

Additionally, the emergence of new and innovative ownership vehicles, such as [special purpose acquisition companies \(SPACs\)](#), can further complicate UBO identification. SPACs, often involving complex ownership structures, are primarily focused on acquiring private companies or cryptocurrency-based ownership structures. They can be used to tokenize various assets, including real estate, securities and even intellectual property. Evolving structures may require institutions to adapt their UBO identification processes to address the unique challenges posed by these new ownership models.

AVOIDING DETECTION: INTENTIONALLY OBSCURE OWNERSHIP STRUCTURES

Given the widespread awareness of the 25% threshold, individuals or entities may intentionally use complex ownership structures to maintain ownership – direct or indirect – over companies without being formally identified as UBOs. The common, identifiable patterns used to hide true ownership include:

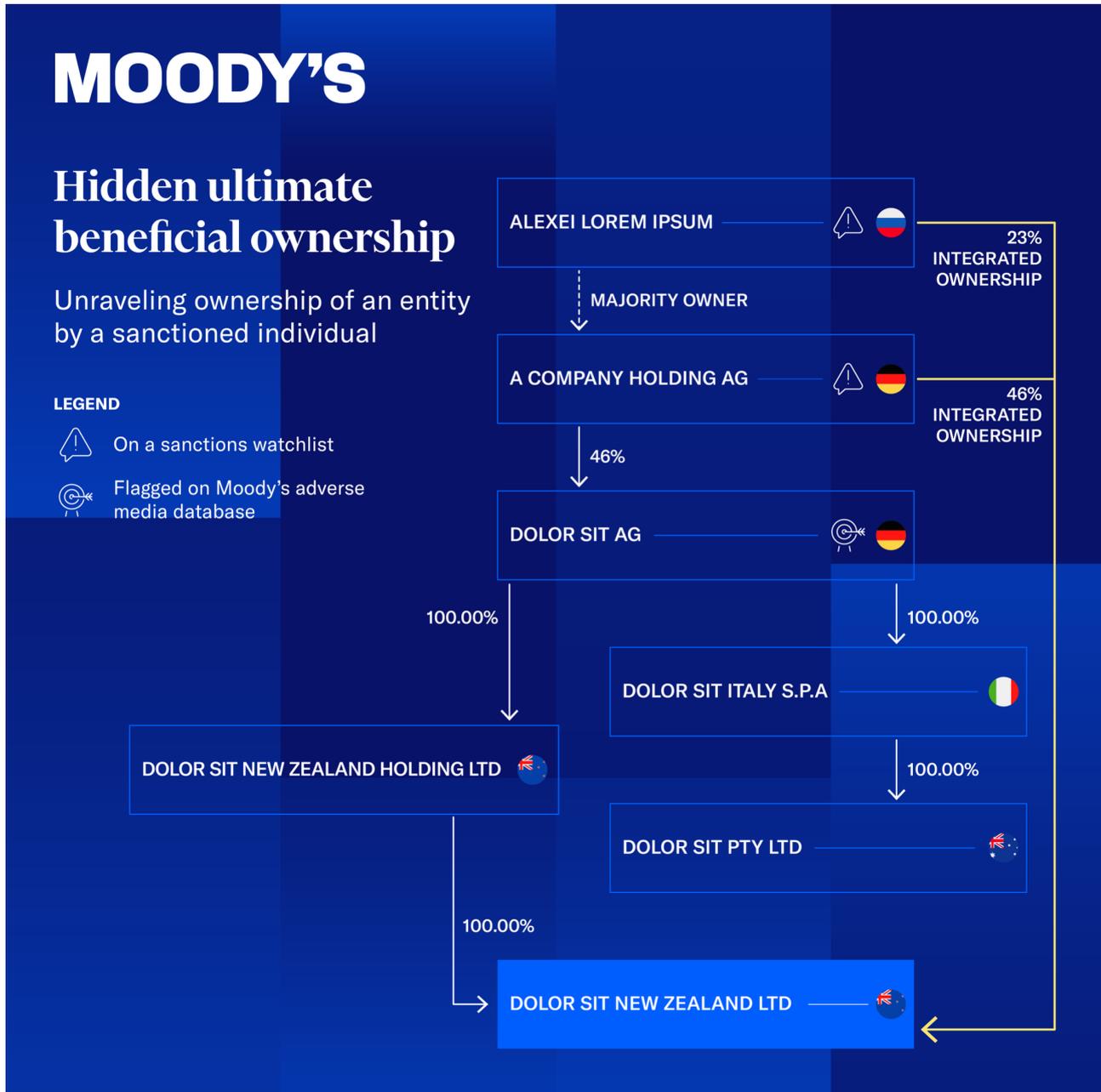
- **Multiple layers of ownership:** Creating a series of subsidiaries or holding companies to obscure the true ownership structure. Each layer is structured to have ownership interests just under the 25% threshold, obscuring the true extent of control.
- **Nominee arrangements:** Using third-party individuals or entities to hold ownership interests on behalf of the beneficial owner.
- **Trusts and foundations:** Establishing trusts or foundations to hold ownership interests, making it difficult to trace the ultimate beneficiary.

→ **Complex voting structures:** Implementing voting structures that give certain shareholders disproportionate control, even if they have relatively small ownership stakes.

By carefully structuring their ownership interests, individuals or entities can maintain control over companies without the same level of scrutiny experienced by other significant beneficial owners.

CASE STUDY: THE COMPLEXITY OF DELIBERATELY HIDDEN ULTIMATE BENEFICIAL OWNERSHIP

FIGURE 1 Complex corporate structure masking the ultimate beneficial owner, a sanctioned Russian individual



Disclaimer: All persons, entities, organizations, and events portrayed in this case study are entirely fictional. Any resemblance to actual persons or entities, living or dead, or actual events is purely coincidental. This case study is intended solely for educational and illustrative purposes and should not be construed as reflecting real-world scenarios or legal advice.

HIDDEN ULTIMATE BENEFICIAL OWNERSHIP

The case study shown in Figure 1 provides a compelling example of the complexities involved in determining beneficial ownership and calculating integrated ownership behind **Dolor Sit New Zealand Ltd**. The company's corporate structure is complicated, involving multiple layers of subsidiaries and holding companies.

Ownership below the threshold

At first glance, **Alexei Lorem Ipsum** – a Russian individual and the ultimate owner – appears to hold an integrated ownership stake of 23% in **Dolor Sit New Zealand Ltd**. This figure falls just short of FATF's recommended 25% threshold, which is the threshold adopted by a number of institutions as part of their onboarding and customer screening process. However, this figure does not take into account any indirect control that **Alexei Lorem Ipsum** holds. The deliberate positioning of ownership interests below the 25% threshold can be a tactic used to obscure beneficial ownership and evade regulatory scrutiny.

The fact that ownership by this sanctioned individual through **A Company Holding AG**, which is also sanctioned, is right below 50%, could also be indicative of potential circumvention of the OFAC 50% Rule⁴ for sanctions.

In this case, Alexei's involvement in **A Company Holding AG** could grant him indirect control over **Dolor Sit New Zealand Ltd**, even though his direct ownership stake is below the threshold. A majority shareholder may have the power to appoint the majority of directors and therefore exert control over the entities further down the ownership chain. From a sanctions perspective, the companies in the whole ownership chain may be considered to have significant sanctions risk as a result.

While the 25% threshold is one way to identify significant beneficial owners – alerting organizations to potential risks in a client's network – this example highlights the limitations of relying solely on this benchmark. When deeper investigation is warranted, access to investigative tools and comprehensive, global datasets can help provide a more thorough analysis of beneficial owners, especially when factoring in other measures of control or influence and the intent behind ownership arrangements.

Integrated ownership

Integrated ownership refers to the total ownership interest held by an individual or entity, both directly and indirectly through other entities. It encompasses not only the shares or equity interests held directly by an individual, but also the ownership interests held through intermediaries.

By considering the ownership structure of a company's parent companies, subsidiaries, and affiliated entities, integrated ownership can offer a more comprehensive picture of ultimate beneficial ownership. This can be particularly important in cases where ownership is spread across multiple entities or where complex corporate structures are used to deliberately obscure a UBO.

The challenge in calculating integrated ownership lies in determining the intricate relationships between entities and the exact percentage of ownership and whether, in aggregate, that reaches the 25% threshold. In the example provided, the ownership structure at first glance does not provide sufficient information to ascertain whether **Alexei Lorem Ipsum** is an ultimate beneficial owner of **A Company Holding AG**.

An additional layer of complexity arises in the designation of **A Company Holding AG** as a sanctioned entity, and the fact that it has an integrated ownership of 46% over **Dolor Sit New Zealand Ltd**. While 46% is below the 50% rule for sanctions (so it technically isn't sanctioned-by-extension through ownership), it is close enough to the threshold such that banks,

⁴ OFAC's 50 Percent Rule states that the property and interests in property of entities directly or indirectly owned 50 percent or more in the aggregate by one or more blocked persons are considered blocked. Similar rules exist in the EU, UK, Australia, Canada, and other jurisdictions.

suppliers, and other relevant parties should be aware of it as it may affect their own sanctions risk exposure. In certain cases, integrated ownership percentages that fall just under the 50% threshold may still result in de-risking by their banks through restrictions on their transactions or through off-boarding.

Thorough due diligence is required to protect organizations – this may involve automated sanctions screening, reviewing adverse media reports, conducting enhanced due diligence checks, shell company risk analysis, and analyzing corporate structures to uncover hidden ownership interests that could pose a risk. By proactively identifying and addressing such risks, institutions can build a more holistic picture of risk and help prevent their involvement with bad actors and illicit activities.

Given sanctions exposure can impact the operations and financial stability of a company or bank found to be directly or indirectly working with a sanctioned entity, it is crucial to detect these connections and mitigate the risks that arise from them.

ENHANCED RISK MANAGEMENT THROUGH UBO TRANSPARENCY

Creating transparency around UBO structures is part of good practice in third-party risk management. By gaining a more comprehensive understanding of the individuals or entities that ultimately own a company, organizations can better evaluate potential risks. These risks can have far-reaching consequences, including potential for reputational damage, financial penalties, and legal liabilities.

Opaque ownership structures, often characterized by complex networks of subsidiaries and holding companies, can be used to deliberately disguise the true sources of funds, making it difficult for authorities to trace the flow of money and identify those involved in criminal activities.

Gaining a clearer picture of the UBOs associated with each third party an organization works with enables them to make risk-based decisions and implement appropriate mitigation measures.

To mitigate risks associated with opaque beneficial ownership, it is imperative to implement measures that enhance transparency and help ensure beneficial ownership can be traced across multiple jurisdictions and layers of ownership. This includes using comprehensive beneficial ownership databases that can identify and unpack complex corporate structures.

BEST PRACTICES

Efforts to enhance UBO transparency continue worldwide, yet institutions face obstacles in a fragmented regulatory landscape and from those deliberately obfuscating their business practices. Technology and data analytics, when used to help organizations map out intricate ownership networks and track UBO information continuously, can play a crucial role in addressing these challenges.

Moody's offers solutions for compliance and third-party risk management that provide extensive data and tools to assist in the identification of UBOs. With the right tools, organizations can more efficiently and effectively pinpoint and confirm UBOs and mitigate the risks linked to dubious ownership.

Maxsight™

Moody's Maxsight™ analyzes thousands of data points to deliver powerful analytics for shared risk intelligence across multiple workflows, all in a single unified risk platform. Identify and verify UBOs for the following use cases:

- **Digital onboarding:** Automate digital onboarding processes tailored to your organization's risk policies and appetite using data from Moody's extensive global entity and risk data estate.
- **Sanctions exposure:** Leverage up-to-date sanctions data – e.g., ownership and control information, sanctions by extension data, and comprehensive sanctions lists and watchlists – to help you identify sanctions risk exposure in your network.
- **Ongoing monitoring:** Conduct ongoing monitoring for sanctions and financial crime risks by integrating Moody's datasets into a workflow. Support risk assessments with automated data checks to surface material changes in ownership or control.
- **Third-party risk management:** The Maxsight™ platform supports you to assess risks associated with each customer and supplier in your network for deeper insights and more holistic risk decisioning.

Entity Verification API

Facilitate know your business (KYB) screening and entity verification by leveraging a real-time network that connects to commercial registers and authoritative sources across the globe, alongside a comprehensive risk database and advanced technologies for risk assessment. Moody's configurable solution is accessible via a single source.

Shell Company Indicator

Shell companies can be used to deliberately conceal beneficial ownership for illicit purposes. It can be helpful for businesses to detect shell company risk in their network.

Moody's Shell Company Indicator provides insight, typology-driven flags during customer and third-party onboarding and investigations to alert businesses to potential shell company risk.

SEVEN KEY INDICATORS OF POTENTIAL SHELL COMPANY ACTIVITY

Outlier directorships

Unusual patterns in current/past directorships and associations with inactive companies

Circular ownership

Instances of circular ownership

Jurisdictional disparity

Differences in nationality/residency of directors or beneficial owners compared to company registration, especially involving high-risk jurisdictions

Mass registration

Patterns indicating mass or bulk company creations within a specific registration period

Outlier age of key individuals

Company owners who are unusually young or old

Financial anomalies

Operating revenues higher than normal relative to the number of employees

Dormancy

Companies inactive for more than five years

THE PATH TOWARDS A BRIGHTER FINANCIAL FUTURE

As regulatory landscapes shift and the demand for corporate transparency intensifies, identifying UBOs becomes a key element of a robust risk management strategy. The task of UBO identification and verification, working with complex ownership structures to varying jurisdictional requirements, highlights the need for strong frameworks and innovative solutions with access to up-to-date data.

Proactively addressing challenges and leveraging the strategic value of comprehensive UBO identification better positions organizations to make decisions about who they work with and to safeguard themselves against financial and reputational risks.

GET IN TOUCH

Moody's works with organizations to implement robust UBO screening and due diligence for effective compliance and third-party risk management – please get in touch for more information or if we can help your business.

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