THE LAW SOCIETY
OF NEW SOUTH WALES

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9 March 2017

Mr Jonathan Smithers
Chief Executive Officer
Law Council of Australia
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By email: Natasha.molt@lawcouncil.asn.au

Dear Mr Smithers,

Treasury Consultation – Beneficial Ownership of Companies

Thank you for your memorandum dated 16 January 2017 requesting input into the Treasury Consultation Paper on *Increasing Transparency of Beneficial Ownership of Companies*. The Law Society's Business Law Committee has contributed to this submission.

Overview

The Law Society welcomes the proposals in the Consultation Paper to increase the transparency of beneficial ownership of companies. This increase in transparency is consistent with international practice and the Australian Government's approach to other areas such as anti-money laundering and counter-terrorism financing ("AML/CTF"). The disclosure of the beneficial owners of companies will assist authorities such as law enforcement and tax authorities to enhance the performance of their functions. It will also allow members of the public to have a greater understanding of the identity of those who control Australian companies. This is becoming more important as global capital, finance and power becomes increasingly concentrated.

Given that the requirement to maintain beneficial ownership records is being introduced to allow the government to meet its AML/CTF commitments and in order to reduce the compliance burden for companies, particularly smaller ones, we propose that:

- The Australian Securities and Investments Commission ("ASIC") should be appointed as the regulator with responsibility for holding a central register of beneficial interests;
- The data sets required for completion should be as close as possible to the existing regulatory framework as set out in the AML/CTF frameworks and the *Corporations Act 2001* (Cth). This may simplify the identification requirements for beneficial owners and/or assist to reduce the verification requirements for a company.

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We also suggest that the existing AML/CTF framework for beneficial ownership verification be extended to larger investors with diverse owners such as retail trusts, superannuation funds custodians and/or nominee trustees.

Australia has committed to implementing the Financial Action Task Force ("FATF") recommendations. The Consultation Paper notes, at page 8, that FATF recommends that countries should ensure that competent authorities can obtain or access, in a timely fashion, adequate, accurate and timely information in relation to express trusts. The Consultation Paper, however, only deals with recommendation 24 in relation to companies. As the questions in the Consultation Paper relate exclusively to companies and do not relate to the use of trusts, our answers to the specific questions, provided below, do not canvass any issues that may arise from the use of trusts.

1. **Should listed companies be exempt from any new requirements to report on its beneficial owners in light of existing obligations on such companies? If so, should an exemption apply to companies listed on all exchanges or only to specific exchanges?**

   The Law Society submits that companies listed on any exchange, including the Australian Securities Exchange ("ASX") should be exempt from the new requirements. There is sufficient information available via the tracing notice provisions. Requiring companies with diverse and dynamic share registries to comply with these obligations would impose an unfair and unnecessary compliance burden on them.

   The Law Society further suggests that for larger investor classes such as retail trusts, custodians and so on that the AML/CTF framework be extended to cover these requirements.

2. **Does the existing ownership information collected for listed companies allow for timely access to adequate and accurate information by relevant authorities?**

   The Law Society considers that the current regime does allow for timely access to adequate and accurate information by relevant authorities.

3. **How should a beneficial owner who has a controlling ownership interest in a company be defined?**

   The Law Society considers that the definition of "beneficial owner" should follow FATF guidance as much as possible, to ensure consistency of Australian law with other jurisdictions. Our members note that when individuals set up companies online, they often have no idea of what is meant by "beneficial ownership" and further guidance would be of assistance.

4. **In light of these examples given by the FATF, the tests adopted by the UK (see Part 3.2 above) and the tests applied under the AML/CTF framework and the Corporations Act, what tests or threshold do you think Australia should adopt to determine which beneficial owners have controlling ownership interest in a company such that information needs to be collected to meet the Government's objective?**

a) Should there be a test based on ownership of, or otherwise having (together with any associates) a 'relevant interest' in a certain percentage of shares? What percentage would be appropriate?

The Law Society agrees that the test for determining whether someone has a "controlling interest" should be based on ownership of, or otherwise having (together with any associates) a 'relevant interest'. We consider that this test is consistent with the tests under the AML/CTF framework and the *Corporations Act 2001* (Cth) for identifying substantial shareholders.

The Law Society suggests that this is most easily determined by a percentage of the voting shares in a company. This percentage should be in line with percentages set in other jurisdictions such as the United Kingdom ("UK").

b) Alternative to the percentage ownership test, or in addition to, should there be tests based on control that is exerted via means other than owning or having interests in shares, or by a position held in the company? If so, how would those types of control be defined?

The Law Society suggests that the five tests adopted by the UK would be an appropriate basis for determining whether a beneficial owner has a controlling interest in a company. As discussed at page 8 of the Consultation Paper, the UK is one country which has established a register of people with relevant beneficial interests in a company as part of its implementation of FATF standards. The UK has developed the concept of People with Significant Control ("PSC") as those beneficial owners who may ultimately have a controlling ownership interest in the company.

A PSC has been defined as individuals who meet one or more of the following five conditions:

1. Directly or indirectly holds more than 25% of shares in the company
2. Directly or indirectly holds more than 25% of voting rights in the company
3. Directly or indirectly holds the right to appoint or remove a majority of the directors of the company
4. Has the right to exercise, or actually exercises, significant influence or control over the company
5. Where a trust or firm would satisfy one of the first four conditions if it were an individual, any individual holding the right to exercise, or actually exercising, significant influence or control over the activities of that trust or firm. This is not limited to the trustee of the trust.

We note that this includes a percentage ownership test.

5. **How would the natural persons exercising indirect control or ownership (that is, not through share ownership or voting rights) be identified (other than through self-reporting) and how could such an obligation be enforced?**

The Law Society suggests that the AML/CTF framework for "know your client" or "know your customer" could be extended to identify natural persons who exercise indirect control or ownership. This framework is one that many Australian companies are familiar with as the *Corporations Act 2001* (Cth) has provisions applicable to 'associated' entities and 'relevant interests', which are based on control tests. As these tests are already established, it would not create a new or unfamiliar compliance regime for Australian companies.

6. **Should the process for identification of beneficial owners operate in such a way that reporting must occur on all entities through to and including the ultimate beneficial owner?**

The Law Society notes that the purpose of the FATF framework is to ensure that the reporting occurs through to and including the ultimate beneficial owner. Therefore, any new process for identification of beneficial owners must operate in such a way that reporting must occur on all entities through to and including the ultimate beneficial owner.

7. **Do there need to be special provisions regarding instances where the relevant information on a beneficial owner is held by an individual who is overseas or in the records of an overseas company and cannot be identified or obtained?**

The Law Society considers that the principles that apply under the AML/CTF framework for identifying individuals or companies in overseas jurisdictions should be applied to information on beneficial owners of companies.

8. **Should there be exemptions from beneficial ownership requirements in some circumstances? What should those circumstances be and why?**

The Law Society suggests that provided that the AML/CTF framework, which recognises identification and verification of certain entities through registration (eg Australian Registered Scheme Number or Registrable Superannuation Entities), or in custody records, is extended to large and public investors such as ASX listed, retail trust and superannuation funds, there should not be exemptions from the beneficial ownership requirements as this defeats the purpose and intent of the policy.

9. **What details should be collected and reported for each natural person identified as a beneficial owner who has a controlling ownership interest in a company?**

The Law Society suggests that the UK model be adopted, for the information collected on each natural person identified as the beneficial owner who has a controlling interest in a company. That is, name; date of birth; nationality; country, state or part of Australia where the beneficial owner usually lives; service address; usual residential address; the date when the individual became a beneficial owner with a controlling interest; and, if a percentage is adopted, the percentage of voting shares held by that individual or; if a combination of tests is

adopted, which tests the individual satisfies to make them a beneficial owner with a controlling interest.

10. What details should be collected and reported for each other legal persons identified as such beneficial owners?

The Law Society suggests such other information as is required to determine the identity of the ultimate beneficial owner.

11. In the case of foreign individuals and bodies corporate, what information is necessary to enable these persons to be appropriately identified by users of the information?

The Law Society submits that the same or similar information be collected as required under the AML/CTF framework.

12. What obligations should there be on a company to make enquiries to ascertain who their beneficial owners are and collect the required information? What obligations should there be on the beneficial owners themselves?

The Law Society recommends that the UK framework for companies and "people with significant control" should apply.

13. Should each company maintain their own register?

The Law Society submits that each company should be required to maintain its own register.

14. How could individual registers being maintained by each company provide relevant authorities with timely access to adequate and accurate information? What would be an appropriate time period in which companies would have to comply with a request from a relevant authority to provide information?

The majority of company registers are now maintained electronically. It should be relatively straight forward for the information, if held electronically, to be extracted and provided to the relevant authorities.

The Law Society considers that the timeframe for a company to comply with a request from a relevant authority should be two (2) business days for listed companies, to align with the tracing notice obligations and within twenty eight (28) days of a request for all unlisted companies.

15. Should a central register of beneficial ownership information also be established?

The Law Society submits that a public register maintained by ASIC, which is publicly searchable, should be maintained.

16. What do you see as the advantages and/or disadvantages of a central register compared with individual registers being maintained by companies?

The Law Society submits that if the policy intention is to identify and to allow the public to know, who are the underlying beneficial owners of a company, then a central public register should be maintained by a regulator.

While holding information in individual registers maintained by companies is necessary for their own corporate governance, it does not meet the public policy test of providing transparency of the ownership of the companies.

17. In particular, what do you see as the relative compliance impact costs of the two options?

The Law Society submits that if the data sets required to be collected are the same and can be collected electronically, there should be a relatively low compliance cost under either option post the transition phase.

18. Who would be best placed to operate and maintain a central register of beneficial ownership? Why?

We suggest ASIC, as it already maintains a public searchable central register of shareholders of Australian companies.

19. What should the scope of the register operator's role be (collect, verify, ensure information is up to date)?

The Law Society considers that primary responsibility for the register should reside with the company secretary. Provided that the rules are sufficiently clear, and provided that the obligation lies on both the company and the beneficial owners themselves to keep the information up to date, this should minimise the burden on the company secretary. The Law Society notes that the ability to perform identity verification via police checks and other reference checks has increased and that there are a number of businesses who specialise in providing information for these purposes.

ASIC's role should be to hold a central register of information identified and verified by companies. ASIC should not be required to verify the information collected.

20. Who should have an obligation to report information to the central register? Should it be the company only or also the persons who meet the test of being a relevant 'beneficial owner'?

The company and the persons who meet the test of being a relevant "beneficial owner", should have an obligation to report information to the central register.

21. Should new companies provide this information to a central registry operator as part of their application to register their company?

Yes.

22. Through what mechanism should existing companies, and/or relevant beneficial owners, report?

For companies, the annual statement lodged with ASIC should be the relevant reporting mechanism. It will be necessary for a separate report to be made where there is a change in shareholder beneficial ownership, before the relevant lodgment date, that takes the control percentage over the recognised level for reporting.

Beneficial owners could report the information on a similar basis directly to the company.

In each case, providing this information electronically should reduce the compliance and data entry burden.

23. Within what time period (how many days) should any changes to previously submitted beneficial ownership information have to be reported to a company (where registers are maintained by each company) or the registry operator (where there is a central register)?

We suggest the reports should be made to the company within 14 days; to the registry operator within 28 days, and to be consistent with other obligations, to report to ASIC (such as change of principal place of business).

There would also be the annual update submitted in the annual statement.

24. If reporting to a central register is required, should this information be included in the annual statement which ASIC sends to companies for confirmation with an obligation to review and update it annually?

Yes.

25. What steps should be undertaken to verify the information provided to a central register by companies or their relevant beneficial owners? Who should have responsibility for undertaking such steps?

The Law Society submits that similar steps to those under the AML/CTF regime should apply to verify the information on beneficial ownership that is disclosed to the central register. Companies should be responsible for verifying the information provided to the central register.

26. Should beneficial ownership information be provided to one relevant domestic authority and then shared with any other relevant domestic authorities? Please explain why you agree or disagree.

If beneficial ownership information is held in a central register by one domestic authority, then it would not be necessary for that authority to share it with others, as other authorities would be able to search the central register.

27. Should beneficial ownership information be automatically exchanged with relevant authorities in other jurisdictions? Please explain why you agree or disagree.

Yes, this is consistent with the approach taken by the Organisation for Economic Co-operation and Development members on tax compliance under the Base Erosion Profit Shifting proposals, such as country-by-country reporting.

28. What sanctions should apply to companies or beneficial owners which fail to comply with any new requirements to disclose and keep up to date beneficial ownership information?

We suggest that the sanctions should mirror those applying under the AML/CTF regime for consistency.

29. How long should existing companies have from when the legislation commences to report on their beneficial owners? What would be an appropriate transition period?

The Law Society submits that a 12–18 month transition period would be appropriate to allow companies to begin reporting at the start of the next reporting period.

30. Do you foresee any practical implementation issues which companies or beneficial owners may face in collecting and reporting additional information?

For companies that do not have electronic registers or keep electronic records of their owners, this may be difficult, although additional compliance costs should be minimal.

31. What types of compliance costs would your business incur in meeting any new requirements for record-keeping and reporting of beneficial ownership information?

We are not able to provide a response to this question.

32. If you are already required to comply with AML/CTF obligations, how do you see any new requirements to collect beneficial ownership interacting with those existing obligations?

We are not able to provide a response to this question.

33. If companies had access to the additional beneficial ownership information collected, could this reduce companies' compliance costs by making it easier for them to comply with other existing reporting obligations such as those under the AML/CTF legal framework?

The Law Society suggests that if companies are able to search the proposed central register for information relating to individuals, that may also assist to reduce those companies' compliance costs when reporting under other existing reporting obligations.

34. Could any changes be made to streamline or merge existing reporting requirements in order to reduce the compliance costs for businesses?

The Law Society submits that the ASIC annual statements would be the most appropriate format for companies to use to report in the first instance. We also recommend that updating of data regarding beneficial ownership should be required to be undertaken online to ASIC using the Corporate Key, in the same way as for information relating to directors and shareholders.

35. Are the current substantial holding disclosure provisions sufficient to identify associates which may have the ability to influence or control the affairs of a company? What changes could be made to improve their operation?

The Law Society submits that the current substantial holding disclosure obligations are not sufficient to identify associates who may have the ability to influence or control the affairs of the company.

We suggest that the tests set out in the AML/CTF framework be extended to identifying associates who may have the ability to influence or control the affairs of a company.

36. Are the current tracing notice obligations sufficient to achieve the aim of providing timely access to adequate and accurate information to relevant authorities about those who control these companies?

The Law Society considers that the tracing notice obligations are not sufficient and that the onus needs to shift on to companies and their beneficial owners to accurately disclose adequate information.

37. In your experience, are there issues or obstacles (specific to obtaining ownership information) which currently arise when using tracing notices? If so, what are those issues or obstacles?

We are not able to provide a response to this question.

38. In order to improve and incentivise compliance with the tracing notice regime should ASIC have the ability to make an order imposing restrictions on shares the subject of a notice until the notice has been complied with?

Yes.

39. What other changes could be made to improve the operation of these provisions?

We suggest that the Court should have the same powers and remedies as are available under section 1325A of the *Corporations Act 2001* (Cth) with regard to the existing notice regime. Consideration could also be given to providing a specific power of inquiry for an administrator or liquidator of a company to obtain this information from not only the company's officers, but also any other person who may hold this information on behalf of the company.

40. Who uses nominee shareholding arrangements, and for what purpose?

Superannuation funds, custodians or other collective investment funds that hold shareholdings in companies for investment/fiduciary purposes are the main user of nominee shareholding arrangements. Private estate planning structures may also utilise nominee shareholding to simplify flexibility of such structures.

41. How often are nominee shareholding arrangements used?

Frequently in Australia for investment purposes through custodians; this is not as common in private arrangements.

42. What do you see as the benefits of nominee shareholding arrangements? Are there any negative aspects of their use?

The benefits are that they provide a basis for disparate and diverse group of investors such as retail or unsophisticated investors to invest in diverse assets. They also provide protection to the custodian or nominee shareholder by limiting those entities liability.

However, nominee shareholding arrangements can also be used for tax minimisation or avoidance purposes or to deliberately hide on the share register who the beneficial owners of an asset are.

43. Should further obligations be introduced in order to increase the transparency of the beneficial owners of shares held by nominee shareholders?

The Law Society submits that the framework under the AML/CTF regime that applies to nominee shareholders be extended to the requirement to disclose beneficial owners in private arrangements. This is not needed for custodian nominee shareholdings as the custody records already show ultimate beneficial ownership details.

44. Are you aware of practical obstacles which would make increased reporting in respect of shares held by nominee shareholders problematic?

As most nominee shareholders shown on share registers are custodians, the custody records can produce reports of ultimate beneficial ownership, although this would incur costs.

45. Who uses bearers share warrants, and for what purpose?

Bearer share warrants are sometimes held as part of an investment portfolio mandate by large investment organisations through custodians as they are an easily transferrable/sellable off market asset with a clear value.

46. How often are bearer share warrants used?

These are not a common investment as they are not commonly issued.

47. What do you see as the benefits of bearer share warrants? Are there any negative aspects of their use?

They are an easily transferrable/sellable off market asset.

48. Should a ban be introduced on bearer share warrants?

Bearer share warrants are no more risky with regard to the identification of a holder than are cheques and should not be banned. As with cheques, obligations could be introduced on the issuer to identify and verify a holder when the warrant is accessed.

Please do not hesitate to contact Liza Booth, Principal Policy Lawyer on 02 99260202 or liza.booth@lawsociety.com.au if you would like to discuss this in more detail.

Yours sincerely,

Pauline Wright
President