

WHITEPAPER

UBO Monitoring

The Challenges and Practicalities

An Ultimate Beneficial Owner (UBO) is defined as 'The natural person(s) who ultimately gains from, owns or controls a legal entity'.

A beneficial owner can either be a direct shareholder of a given company, or have an equity holding in another entity that has ownership of the given company.

Understanding UBOs is a fundamental regulatory requirement in the EU Money Laundering Directive, which forms part of a risk-based approach to Anti-Money Laundering (AML), Know Your Client (KYC) and Client Due Diligence (CDD) efforts. The Money Laundering Directive is backed by G20 initiatives aimed at building transparency and good corporate governance. The ultimate goal is to ensure confidence in companies operating in regulated markets.

Establishing UBOs contributes to protecting the brand reputation of companies. This involves screening for unlawful behavior such as bribery, corruption, sanctions, politically exposed persons (PEPs), ongoing litigation and negative media coverage. Gaining insight into UBOs is quite a challenge, involving multiple lines of research, missing links and conflicting information. And now that regulations require monitoring of information about UBOs, compliance teams must make an extra effort.

In this whitepaper, we explore ways to overcome the challenges of UBO verification and monitoring, including:



Approaches for consistent calculation of ownership and control



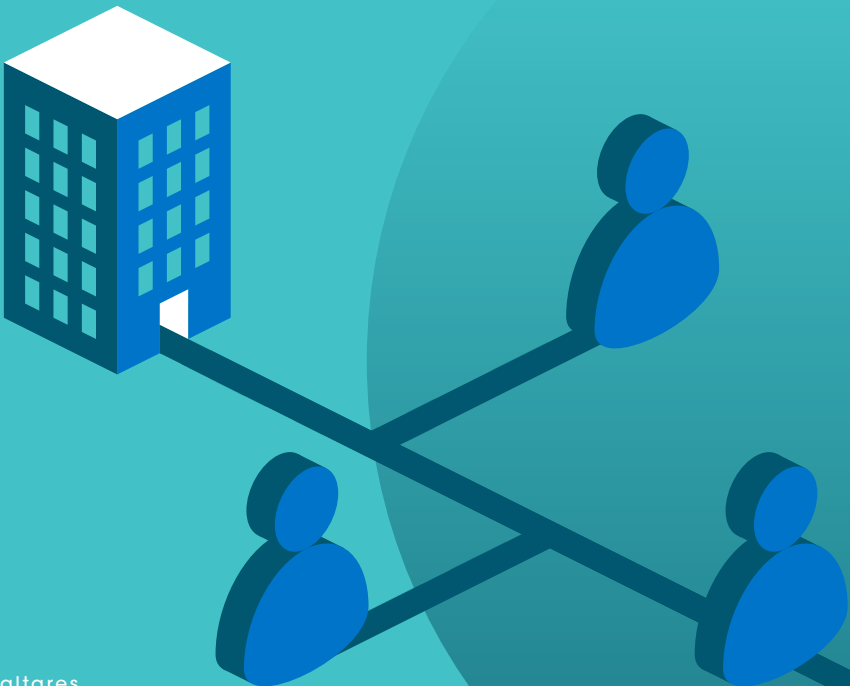
The complexities involved in monitoring



How technology can help organizations embrace UBO monitoring and evaluate the impact of changes in UBOs.

Beneficial ownership: the background

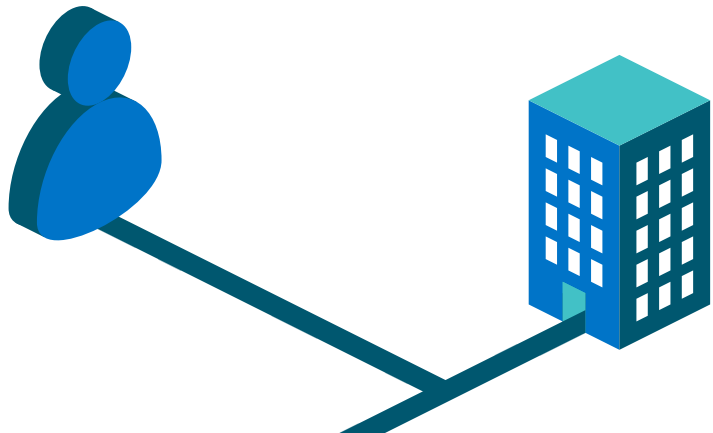
The European Union has been leading the way in the field of regulation for some years now, particularly regarding beneficial ownership of companies.



EU Member States are establishing registers of ultimate beneficial owners (UBOs) of companies and other legal entities, and making part of the data more publicly accessible, thus improving transparency. This goes far beyond meeting the regulatory requirement to demonstrate a legitimate interest in a company.

Identifying and verifying UBOs is nowadays an essential component of both the Know Your Client (KYC) on-boarding process and the monitoring process. In an earlier paper "[Understanding UBO structures](#)" we described the complexity of different possible ownership structures.

Perhaps most relevant for operational managers and compliance teams, the European Commission has been tasked to connect the various UBO registers at EU level by 10 March 2021, to create an EU-wide register. The aim is to ensure a consistent and transparent pool of information on UBOs in all member states.



The theory is that the information provided on the ultimate beneficial owner should include at least the following:



month and year of birth;



country of residence;



nationality;



and the nature and extent of the beneficial interest held.

But as with all other directives, each EU member state will apply them in the way that best suits its unique frameworks and political needs – ultimately adopting different approaches based on broadly the same set of criteria. It remains to be seen whether countries will provide transparency to meet the increasingly widely felt need for insight into the ultimate beneficial ownership and control of companies, both as part of the onboarding process and in existing client relationships.

In view of the lack of consistency in the registration approach across member states, different levels of data availability and the complex regulatory requirements (not to mention the increasingly less transparent hierarchical structures of enterprises), the question is how compliance professionals should deal with determining ultimate beneficial ownership and control. In this paper we will be sharing our knowledge in these areas.

The challenges of establishing ultimate beneficial owners

There is a shift towards a heterogeneous approach to determining ultimate beneficial ownership and control.



This may mean that companies need to follow more than one line of research. For example, there can be one line of research for voting rights, one for traditional ownership and one for influence and control. This can result in multiple people being designated as ultimate beneficial owners.



When ultimate beneficial ownership is discussed, simple examples with full information are often used to illustrate connections and business relationships between companies. However, these examples usually show only a handful of levels to illustrate how dilution of holdings is calculated. Things often look very different in reality. Time to address some of the most common challenges.

In short: the challenges faced when tracking down the UBO



1 OVERSEAS OWNERSHIP

- Opaque jurisdictions
- Tax havens



2 DILUTION OF SHAREHOLDERS

- Undisclosed ownership percentages
- Disclosure obligation for majority shareholdings only



3 CONFLICTING INFORMATION

- Timing of filings
- Differing definitions of ownership/control

1

OVERSEAS OWNERSHIP

This is by far the most common problem. While there is a good level of information transparency in the Netherlands, this is rarely the case in jurisdictions abroad. Moreover, there is a good chance that the entity in question is not incorporated in the Netherlands. For many companies, an international client base poses the most problems. This makes it a lot harder to contact managers and owners. Ultimate beneficial owners can therefore be several levels removed from the legal entity that forms the starting point of the UBO investigation.

2

DILUTION OF SHAREHOLDERS

There are many jurisdictions in which ultimate beneficial ownership can be determined on the basis of available data. However, it is not always possible to calculate an exact ownership percentage. Some links in the ownership structure may be missing, or the register only states that they are majority owned. This can make it difficult to determine the correct diluted ownership percentage for the entire company structure.

3

CONFLICTING INFORMATION

Where ownership structures span the globe, we often see missing or conflicting information. There are various causes for this. For example, the information requirements of some registries (such as the UBO register) may disregard certain levels of ownership, or some jurisdictions may have other requirements.

There are various combinations of processes for requesting or sharing information about the rightful or direct owner and the ultimate beneficial owner. If a natural person in China is seven levels removed from a Dutch company and there are changes in their ownership interests, the question is whether, as a person with significant control, they will actually take their Dutch obligations into consideration.

It is also possible that companies indicate in their annual accounts who their ultimate beneficial owner is. That person may differ from the person with significant control, which in turn may differ from the ultimate beneficial owner stated in the confirmation statement, depending on the time of reporting.

UBO Monitoring

Gaining insight into UBOs and screening them is no easy task, but as we have just seen, there are ways to take control of this process.



Monitoring UBO information for changes within a relevant timeframe is also crucial in terms of minimizing risks and increasing transparency from a regulatory point of view.

However, it is extremely difficult to determine how UBO information should be monitored and updated without compromising efficiency or creating new operational sore points.

UBO monitoring often takes place as part of a risk-based approach. There are periodic assessments, and organizations start each year with a clean slate. Normally, a periodic assessment reveals important information. Sometimes the information is updated as a result of various changes with respect to the client and counterparties in three main areas:

- business-related changes (addresses, names, etc.)
- information about directors
- ownership

Before starting UBO monitoring, it is important systematically to determine the end point of a line of research. The following methods and techniques can help in this:

‘SPIDERING’

This method takes a company as a starting point and follows each individual relationship to the end, and then looks at the entire ownership structure. By splitting the spidering of the network (spidering) and the algorithm for calculating the ownership percentage, it is possible to apply different perspectives and calculations. This can be done quickly for the same returned dataset, because spidering is not conditional.

The technology behind graph databases has matured, so that large volumes of data can be processed and returned in seconds.

ALGORITHMS

A flexible suite of algorithms is available, to support various application scenarios. One example of this is the application of a worst-case scenario algorithm. Other algorithms can in turn be tailored to determine the level of control. This approach usually provides a reasonable level of detail, but for some aspects a specific percentage may not be available, so a full calculation of the ownership percentage cannot be performed. This means that ultimate beneficiaries or owners can be identified, but there is a lack of information on the exact size of their holding. Using a worst-case scenario approach it is possible to give an indication based on the remaining percentages as to whether or not owners should be considered. If all owners and their percentages are added up, the calculated total percentage can sometimes exceed 100%. However, this approach can significantly reduce the number of ultimate beneficial owners that meet a risk threshold. In most cases this is likely to result in a tenfold reduction in the number of links in the chain, even if a worst-case scenario is taken into account.

Why is it important to review the beneficial ownership of third parties?



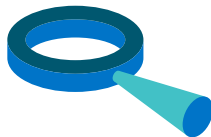
- The Fifth Money Laundering Directive (5AML) requires you to monitor and keep UBO information up to date
- Ownership structures are complex, and changes often occur at multiple levels
- Percentage changes may be above or below the risk threshold set in the organization's policy
- Entities within the structure can relocate to countries deemed a higher risk
- This ensures you have the most current overview of owners of third parties.

Master Data Management style updates have been available for many years, enabling the updating of company data of clients and their directors and/or executives. It is possible to deliver large data volumes quickly and easily, so that the data can be updated instantly, offering the possibility to draw up rules for determining the relevance of changes.

The direction in which things are moving is clear: the onus is increasingly on organizations to automate their processes.

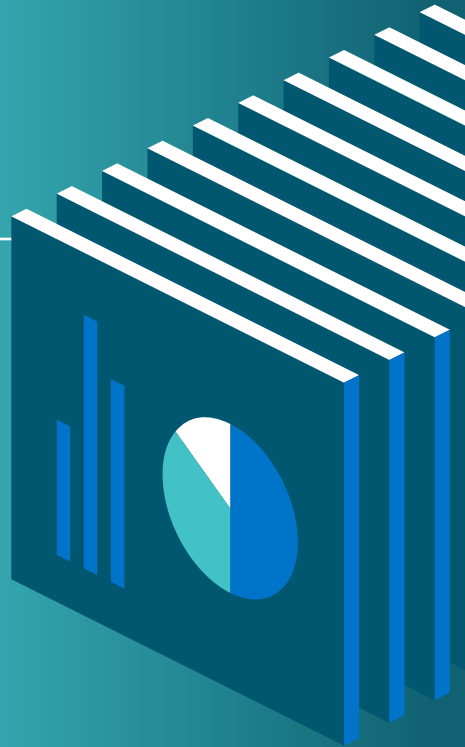
There are several reasons for this:

- More and more information is becoming available.
- Companies need to continuously scale up their assessment processes. However, this is difficult to do without investing in expensive staff and constantly developing their skills.
- An increasing number of requirements is being added to the list for checking and screening UBOs. This makes it increasingly difficult to keep up with developments and to match the level of service to the expectations of both internal and external clients.



Switching to systematic monitoring

Many organizations are now seriously looking at how they can structure the monitoring aspect of due diligence for clients and third parties in a system that makes it possible to move from periodic review to continuous assessment.



There are potential benefits to this, such as time savings and a degree of consistency that is not achievable with manual assessments. The main advantages are automation and the ability to create rules for identifying hidden complexity.

Continuous assessment provides much faster insight into the actual risks for each client or counterparty. Ultimately, this offers the opportunity to tap into a client's additional revenue potential more quickly.

Although automation can bring cost savings, a certain amount of human intervention is still necessary and valuable. Continuous assessment provides much faster insight into the actual risks for each client or counterparty. Ultimately, this offers the opportunity to tap into a client's additional revenue potential more quickly.

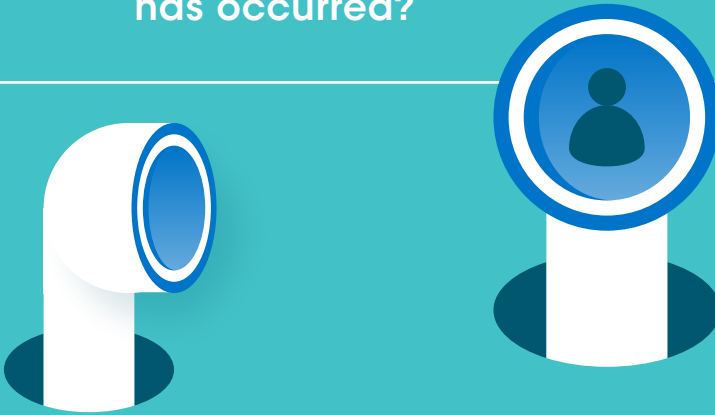
However, monitoring and continuous assessment of the legal or ultimate beneficial ownership/control has turned out to be more difficult in practice.

At Altares Dun & Bradstreet, we believe that ownership of a legal entity should be approached in the same way as every other assessment criterion. In this context, three simple questions need to be answered:

- How can we determine whether any change has occurred?
- How do we determine what exactly has changed?
- Does the change affect the compliance process, the client, the internal policy or the organization?

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How can we determine whether any change has occurred?

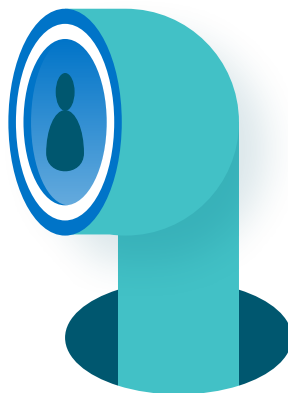


Without a baseline or end point, it is difficult to gain insight into actual changes. If an end point is determined, a new calculation of the ownership percentage can be performed daily or monthly to see if the outcome remains the same. And while there may be certain aspects that seem cut and dried when viewed by human eyes, software can identify small details that could indicate problems.

Suppose, for example, that a new entity is added to a holding structure while the ultimate shareholders remain the same. If shareholders are recorded in a different way, this could result in a change that is actually 'noise'. In other words: strictly speaking a change has taken place, but it is not one that is relevant to the ultimate ownership.

Depending on regulatory requirements, industry differences and organizations' risk appetite, it can also be useful for compliance teams to consider what to do in a situation in which there is a shift from legal ownership to ultimate beneficial ownership, while the ultimate owners remain unchanged. It is crucial to standardize, compare apples with apples and identify 'real' changes.

Compliance teams would also do well to filter out all parties that are not ultimate beneficial owners, as far as their risk appetite allows. To determine ultimate beneficial ownership, organizations need to think about how they want to represent UBOs and decide whether a change to the line of research without a change of individuals is relevant to their organization.



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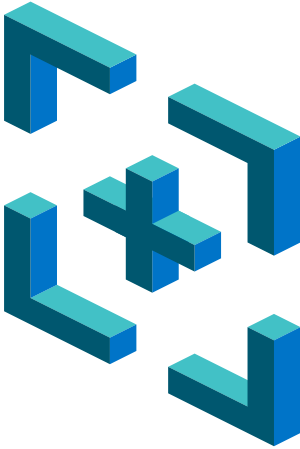
How do we determine what exactly has changed?



Most systems used to detect change apply a unique ID for each record. They then check each related attribute in chronological order (old to new). In effect, these systems assess a subset of data that is brought together in a single row. Each time a change is detected, they compare that row in the same way.

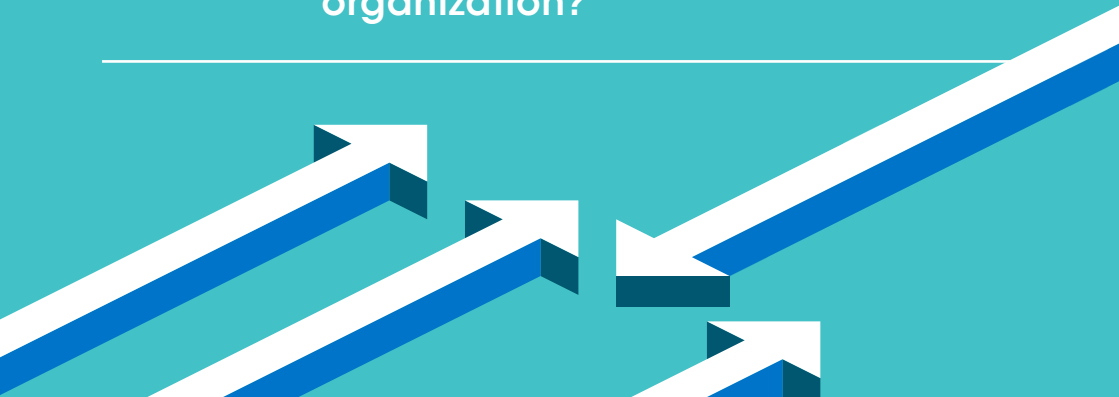
However, determining beneficial ownership requires a different approach that assesses attributes that are not part of a standard data row, but are connected through relationships. These attributes and relationships must also be checked. For example, a change to a person's name or date of birth is highly unlikely, but it is quite possible that their percentage holding in a company will change. In such cases, the beneficial owner has not changed, but the attributes have. In practice, the most likely scenario is that an ultimate beneficial owner has been added or removed.

Ownership has an inherently elastic data structure. Changes to one link in the chain can have a knock-on effect. Whatever control mechanism the organization uses to detect changes, it needs to be able to compare the old and new situations, in order to accommodate potentially important changes caused by an event further down the chain.



3

Does the change affect the compliance process, the client, the internal policy or the organization?



One change within an ownership structure can have a range of consequences, depending on the enterprise that is the starting point of the assessment. Determining the actual change therefore requires contextual information.

A change at the highlighted link will have various consequences for the other links in the chain. Implementing the change within the entire chain and assessing and calculating its consequences therefore demands powerful technological solutions.

Compliance teams need to set some rules in order to be able to process these changes and make sense of them. The most obvious is the threshold check, which monitors for situations in which there have not been any changes to or removal of owners, but rather a change to the ownership percentage attribute.



If new beneficial owners have been identified, compliance teams need to be able to see whether these exceed a risk threshold. If that is the case, they must proceed to the next step: screening. In some cases, a large number of ultimate beneficial owners may be identified, even if a worst-case scenario is used. This is possible if there is a large client or supplier base. Organizations may choose to apply a company-specific set of rules to assess the impact of changes.

For example, a financial service company may wish to screen all new owners. An industrial company could choose to average out unknown ownership. However, if there are hundreds of beneficiaries, it could also decide that is unlikely that one of them will have full control.

Professionals with experience in screening for sanctions, politically exposed persons and negative media coverage know how difficult it is to filter out false positives. It is therefore important to be meticulous so that less work is needed at a later stage. Applying thresholds and rules and deciding on a risk appetite determine what happens in the next stage.

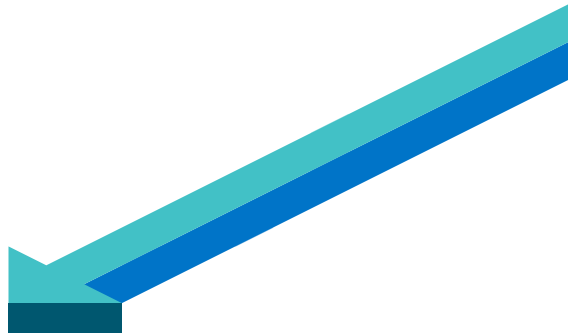
If a screening does not yield any hits, the assessment of a UBO change could be fully automated. If there are hits, and all necessary manual reviews of false positives have been completed, a realistic picture of the consequences of the changes emerges. Of course, the converse should take place if owners have been removed. It is quite possible that this would have a positive effect on the risk threshold if the screening process yielded hits for these persons.

An increase in the number of data points means that more aspects need to be weighed up regarding the rules applied. For example, with a risk-based approach, it may be decided not to carry out a further investigation if a company is listed on a recognized stock exchange. Some organizations may give extra significance to state-owned enterprises, while others may want to consider other factors, such as the company's score on Transparency International's Corruption Perceptions Index in the jurisdiction in question. Various other attributes can be attached to links in the chain to determine whether entities are relevant, what level of risk they represent and whether or not they need to be screened.

Finally, compliance teams can evaluate whether the outcome of all these combined rules actually results in a change to the risk profile for the entity in question.

So far we have focused mainly on the ultimate beneficial ownership. However, there is an increasing focus on other assessments and factors, such as who has influence on, or control over, the company.

In addition to calculating ownership percentages, compliance teams must also consider what the future may bring, such as new perspectives on ownership and control. It is therefore advisable to store all types of attributes and data so that they can be included in the monitoring process in the future.



Conclusion



1

Try to future proof your monitoring approach and systems, so that you can meet future monitoring requirements and support new ownership structures.



2

Take a systematic and consistent approach to calculating ownership and control.



3

Gain insight into the complexity of monitoring and the elastic nature of the data and changes.



4

Embrace emerging technologies for automating processes and assessing the impact of changes.

How Altares Dun & Bradstreet can help you

The data and solutions of Altares Dun & Bradstreet enable you to monitor your entire network in real-time.

With our global data, you will be able to uncover an organization's entire ownership structure, regardless of its geographic location. Receive automatic alerts as soon as changes occur in the UBO structure of your clients, suppliers and other parties. Take control and proactively manage changes.

- ▶ Monitoring information is updated daily
- ▶ A change history for the past 12 months gives you insight into the current and previous situation for all ultimate beneficial owners.
- ▶ Receive information about direct and indirect changes in ownership and control structure and changes in data (such as percentage changes)
- ▶ Identify additions of UBOs to the structure or their removal
- ▶ Use an API to add notifications to your existing workflow

OUR VISION

Smart insights to shape your future

WE believe data
is only valuable
when it has a
purpose



WE guide you
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expanding data
universe



YOU create a
company culture
where data is
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If you are interested to find out more about our compliance solutions, please contact our consultants.

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