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CORPORATE INVESTIGATIONS SECTOR ALERT

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Compliance Bulletin: Everything you need to know about Ultimate Beneficial Ownership

In this series, CDH's Corporate Investigations experts will provide key insights into proposed amendments to the Companies Act 71 of 2008 aimed at enhancing transparency around ultimate beneficial ownership on the heels of FATF's Mutual Evaluation Report of South Africa.

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Compliance Bulletin: Everything you need to know about Ultimate Beneficial Ownership

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On 1 October 2021, the Minister of Trade, Industry and Competition published the Companies Amendment Bill (Bill) for public comment. The Bill, which proposes certain changes to the Companies Amendment Act, 2008 (Companies Act), was first published for public comment on 21 September 2018. Thereafter, it was significantly revised following extensive public engagement and has been published a second time (in an amended form) to enable further public comment.

The Bill recognises the current inadequacies of the Companies Act around establishing the identity of true owners of companies and that transparency in respect of beneficial ownership reporting is becoming a matter of global concern. These inadequacies were echoed in the Financial Action Task Force (FATF) Mutual Evaluation Report of South Africa, released on 26 October 2021, which identified moderate deficiencies in South Africa's efforts to achieve transparency around beneficial ownership of legal persons.

Bribery risks

It is widely accepted that opaque ownership structures create the perfect setting to disguise the proceeds of unlawful activity and may easily be used for illicit purposes, particularly in financial crimes such as money laundering. The Bill also recognises that establishing and disclosing the true ownership of companies will increase transparency around public procurement and government procurement spending, both of which rank highly on the South African anti-bribery agenda.

International legislative framework

From an international legislative framework perspective, the Group of Twenty's (G20) Global Framework for Tracing Beneficial Ownership, to which South Africa is affiliated, requires member countries to encourage beneficial owner disclosure in all their legislation governing business and investment institutions. The South African Government, accordingly, adopted the G20 High-Level Principles on Beneficial Ownership Transparency in October 2015 to prevent misuse of juristic persons and legal arrangements of ownership for illicit purposes; however, subsequent reviews by anti-corruption and anti-money laundering watchdogs have revealed that South Africa displayed a poor level of compliance with the G20 principles.

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FATF's Mutual Evaluation Report identified that, in South Africa, Beneficial Owner information is not always timely available to competent authorities and there is still limited access to such information.

The FATF, to which South Africa is also affiliated, is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction. The FATF Recommendations are recognised as the global anti-money laundering and counter-terrorist financing standard.

FATF Recommendations 24 and 25, relating to transparency and beneficial ownership of legal persons and of legal arrangements respectively, state that countries should take measures to prevent their misuse for money laundering and terrorist financing.

Common challenges

According to the FATF, the common challenges identified in implementing measures to identify beneficial ownership are:

- 1) Inadequate risk assessments concerning the possible misuse of legal persons for money laundering and/or terrorist financing.
- 2) Inadequate mechanisms such as a database to ensure that competent authorities have access to beneficial ownership information.
- 3) Insufficient risk mitigating measures to address the money laundering and terrorist financing risk posed by bearer share and nominee shareholder arrangements.
- 4) Lack of effective sanctions on companies which fail to comply with requirements aimed at identifying ultimate beneficial ownership.

- 5) Inadequate mechanisms for monitoring collaboration with other countries.

FATF's Mutual Evaluation Report identified that, in South Africa, Beneficial Owner information is not always timely available to competent authorities and there is still limited access to such information.

Measures to improve transparency

According to the FATF's Best Practices on Beneficial Ownership for Legal Persons, published in October 2019, the following multi-pronged approach was recommended to identify the beneficial owners behind legal persons, such as companies and foundations:

- The Existing Information Approach, in which beneficial ownership is gathered from existing sources of information including competent authorities, company, land and other types of registries.
- The Company Approach, in which companies are required to obtain and hold up-to-date information on shareholders or members.
- The Company Registry Approach, which requires registries that will obtain and hold up-to-date information of beneficial ownership.

In June 2021, the FATF held a plenary meeting, in which South Africa participated. During that meeting, following investigations, it was concluded that countries are still not doing enough to ensure that beneficial ownership information is available and up to date.

The measures proposed by the Bill, outlined below, appear to be hybrid of the Company Approach and the Company Registry Approach.

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The Companies Amendment Bill introduces several new measures that companies will have to implement to establish and report their true ownership.

New measures proposed by the Bill

To address these challenges and the current inadequacies of the Companies Act, the Bill introduces several new measures that companies will have to implement to establish and report their true ownership. This is part of the broader objective of identifying the holders of beneficial interests in the company.

In terms of the Companies Act, unless a public company knows the identity of all the persons who hold a beneficial interest in its shares, the company must request registered holders of shares to disclose the identity of holders for whose benefit the shares are held. The proposed amendments to Section 56, in an endeavour to identify the true owner more effectively, are aimed at:

- placing an obligation on companies to require details from the registered shareholder of the identity of persons who hold beneficial interests;
- strengthening provisions requiring companies to establish and maintain a register of owners of beneficial interests in their shares;
- requiring companies to publish in their audited financial statements, details of all persons who alone or in the aggregate hold beneficial interests amounting to 5% or more of the total number of shares of that class; and
- strengthening the provisions for registered shareholders to disclose to companies who hold beneficial interests in their shares.

In terms of the Companies Act, a company may request holders of shares to disclose the identity of the ultimate beneficial-interest holders, that is the juristic persons or nominees for whose benefit the shares are held. According to the Bill, it seeks to ensure transparency not only around this first tier of beneficial

holders (or all nominee arrangements in the security register) but also to require that companies reveal the ultimate beneficial owners.

In addition, the Companies Act does not compel companies to request holders of their shares to disclose the identity of the holders of the beneficial interests, and if a company suspects that shares are held for the beneficial interest of others, it "may" require the registered or suspected beneficial owners to declare the true state of affairs. Clause 13 of the Bill intends to amend this by changing the "may" to "must", thereby placing an obligation on companies to procure this information.

The Bill requires that all beneficial ownership information be requested by and disclosed to the company concerned, but that the company in turn be required to publish shareholding information only in instances where persons in the aggregate, alone or together with other persons, own 5% or more of the beneficial interests of the shares in a class. The Bill requires that companies must request this information from registered shareholders once every quarter.

However, there are different interpretations proposed as to when the requirement on companies to request true ownership should apply. Two options were identified:

- First, that companies should only have to request information relating to true ownership from those shareholders with 5% or more shareholding of a company. This option will avoid placing an undue burden on shareholders and firms by only requiring significant levels of shareholdings to be subject to disclosure of beneficial ownership and interests in those shares.
- Second, to make such provision applicable to all shareholdings.

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The proposed amendments to the Companies Act in relation to the enhancement of transparency around ultimate beneficial ownership will, amongst other things, assist counterparties in mitigating their money laundering, financial crime and reputational risk by having full disclosure in relation to company ownership.

The motivation given is to avoid shareholders fragmenting their economic interest through multiple smaller shareholdings held through nominee companies in an effort to disguise their ownership.

Conclusion

The proposed amendments to the Companies Act in relation to transparency around ultimate beneficial ownership will, amongst other things, assist counterparties in mitigating their money laundering, financial crime and reputational risk by having full disclosure in relation to company ownership.

In our view, the proposed amendments to the Companies Act will not occur in isolation. It is likely that further amendments to, amongst others, the

Financial Intelligence Centre Act 38 of 2001, South Africa's primary piece of anti-money laundering legislation, can also be expected.

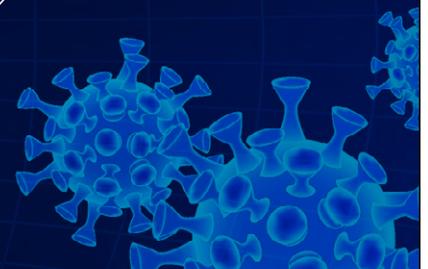
This, in part, will be aimed at ensuring greater compliance with FATF's Recommendations 24 and 25, following FATF's Mutual Evaluation Report, in which South Africa was found to be only partially compliant.

Krevaria Pillay, Associate in our Corporate Investigations Sector, will be unpacking the recent changes in South Africa's anti money laundering framework, in particular in relation to ultimate beneficial ownership, at the South African Anti-Money Laundering Integrated Taskforce Conference on 2 December 2021.

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