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LISTED COMPANY SERIOUS LOOPHOLE

this issue

The listed entity loophole results in no reporting on account holder, nor on beneficial owners.



Issue highlights

CRS evaders are listing their single owned private investment company on a small stock exchange. Due to FATF due diligence recommendations, the FI does not determine the beneficial owner of a listed entity. The evader will not self-certify that he is a controlling person. Hence there is no CRS reporting, despite the original owner retaining 100% of the entity shares.

How to address loophole: Self-certification verifiable with stock exchange transparency

FATF recommendation 10 and CRS state that FIs do not need to determine beneficial ownership of a company listed on a stock exchange if exchange subject to "disclosure requirements, either by stock exchange rules or through law or enforceable means."

This transparency by stock exchange does not result in CRS reporting unless FI obliges the listed entity to self-certify controlling persons who own more than 25% of listed company, which is verifiable through the requisite transparency of the stock exchange.



Listed companies are a major CRS loophole. More than one entity is listed per week in Curacao / Malta / Cyprus to avoid the CRS (i) Beneficial owners are not identified by the FI according to FATF due diligence recommendations (ii) in any event, FIs incorrectly categorize a listed company as a non-reportable person, despite it not being regularly traded, or (iii) categorise as an Active NFE even if not regularly traded.

Lawyers have cottoned onto the listed entity CRS loophole. CRS diligently follows FATF recommendations that beneficial ownership of listed entities need not be identified.

Why it works

According to the CRS, the Financial Institution is **not required to determine the beneficial ownership** of the account maintained of a listed entity. The CRS clearly states, "it is accepted that a Reporting Financial Institution will not be able to determine the Controlling Persons for CRS purposes". This is reinforced in the OECD implementation handbook.



How it works

A CRS evader lists their offshore investment company on a small stock exchange such as in Curaçao or Malta. Despite being listed, there is no regular trading of the entity shares on the market with original owner retains 100% shares.



a) No report on Controlling Person:

The bank maintaining the entity's account does not report the account because they do not have to determine any controlling person according to the FATF AML. Thus, cannot determine if the controlling persons is a reportable person.

b) No report on entity as account holder:

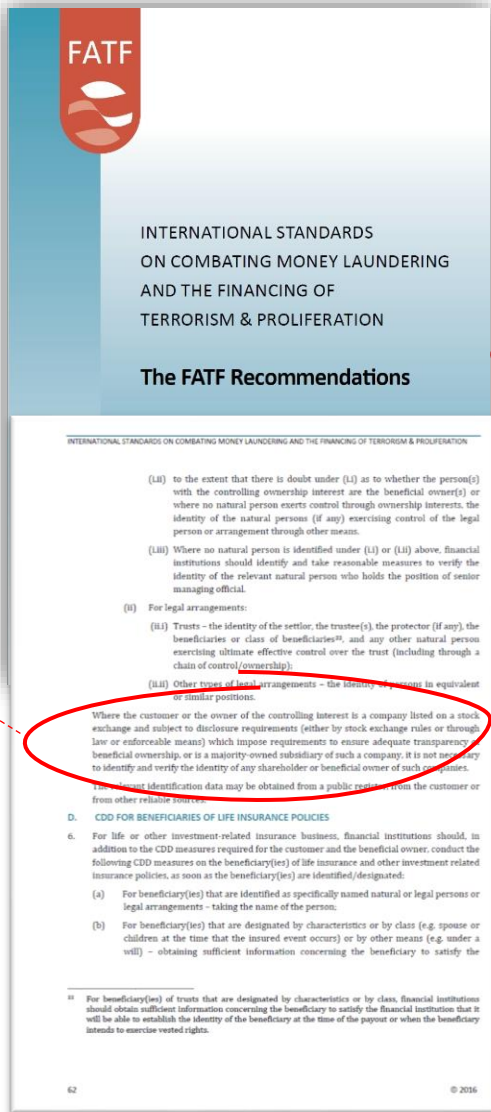
As an extra barrier to avoid CRS reporting, FIs incorrectly categorises the listed entity as a non-reportable person, despite it not being a regularly traded entity.

The OECD implementation guideline unambiguously states "it is accepted that a Reporting Financial Institution will not be able to determine the Controlling Persons for CRS purposes."



(i) The root cause of the loophole is Financial Action Task Force recommending identification of beneficial owners of listed companies are not required. FATF Interpretive Note to Recommendation 10 (Customer Due Diligence) Pg. 62.

Where the customer or the owner of the controlling interest is a company listed on a stock exchange and subject to disclosure requirements (either by stock exchange rules or through law or enforceable means) which impose requirements to ensure adequate transparency of beneficial ownership, or is a majority-owned subsidiary of such a company, it is not necessary to identify and verify the identity of any shareholder or beneficial owner of such companies.



UBO of listed entities are not identified by FIs. This is reaffirmed in the OECD CRS implementation handbook



CRS Implementation Handbook Pg. 69 par (144) The term Controlling Persons corresponds to the term “beneficial owner” as described in the Financial Action Task Force Recommendations , in Recommendation 10 and the corresponding Interpretive Guidance.

CRS Pg. 39 par(2)(b) For the purposes of determining the Controlling Persons of an Account Holder, a Reporting Financial Institution may rely on information collected and maintained pursuant to AML/KYC Procedures.

CRS Implementation Handbook Pg. 70 par (148) FATF recommendations do not require the determination of beneficial ownership if an Entity **is listed on a stock exchange** and is subject to market regulation and to disclosure requirements (either by stock exchange rules or through law or enforceable means) to ensure adequate transparency of beneficial ownership. **Thus, in such cases, it is accepted that a Reporting Financial Institution will not be able to determine the Controlling Persons for CRS purposes.**

Hold your horses

CRS page 70 However, the savings grace to close this loophole is for new entity accounts Determining whether the Account Holder is a Passive NFE, which it will likely be unless regularly traded. A requirement to determine Controlling Person by means of “a self-certification from the Account Holder. And this can be confirmed from stock exchange for that anyone owns more than 5% as stock exchange is transparent on ownership.

(ii) FIs incorrectly categorise all listed companies as non-reportable “regularly trade” person. Bear in mind, a listing on a stock exchange does not automatically mean regularly traded

CRS Pg. 57 par (D)(2) The term “Reportable Person” means a Reportable Jurisdiction Person other than:

- (i) a corporation the **stock of which is regularly traded** on one or more established securities markets or a corporation that is a Related Entity of a regularly traded corporation
- (ii) a Governmental Entity
- (iii) an International Organisation
- (iv) a Central Bank; or
- (v) a Financial Institution

Many FIs wrongly assume a listed entity is a non-reportable person because they incorrectly assume listed means regularly traded. It is very likely a CRS evader listing their company, is not regularly traded.

So, this misapplication of the CRS rules results no reporting on the account holder to where it is tax resident.

Practical demonstration on how listed entity loophole is utilised

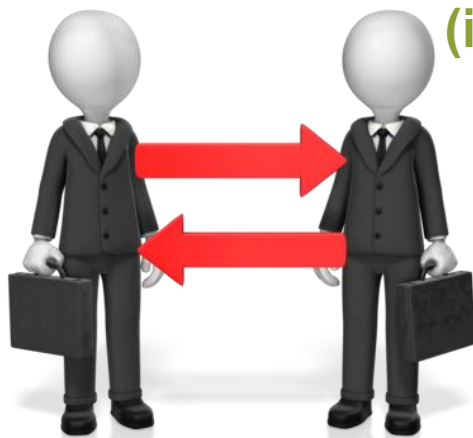
Future Assets

Chinese resident has company bank account with Taiwan bank.

Taiwan has announced it will join CRS in 2019 / 2020. Chinese resident lists his company on Curacao stock exchange but there is no trading of shares. When Taiwan joins CRS, the bank will not identify the beneficial owner according to FATF. Furthermore, the bank may incorrectly categorise the entity as an Active NFE.

Current Assets

Client has company holding OTC derivatives. Currently most Australian FIs mistakenly believe OTCs are not reportable financial assets. However, aware that there may soon be clarification that this will be reportable, the owner lists his company on a small stock exchange. The bank will then not determine or report on the Controlling Persons.



(iii) FIs incorrectly assume a listed entity is automatically an Active NFE Type[B] even if it is not regularly traded

Definition of regularly traded Active NFE

A class of stock would generally be treated as meeting the “regularly traded” requirement for a calendar year if the stock is traded during such year **on an established securities market** and is **regularly quoted by dealers making a market in the stock**. A dealer makes a market in a stock only if the dealer regularly and actively offers to, and in fact does, purchase the stock from, and sell the stock to, customers who are not related persons with respect to the dealer in the ordinary course of a business.

Regularly traded CRS Commentary page 193 par (113)

has a meaningful volume of trading on an on-going basis” if:

- (i) trades in each such class are effected, other than in de minimis quantities, on one or more established securities markets on at least 60 business days during the prior calendar year; and
- (ii) the aggregate number of shares in each such class that are traded on such market or markets during the prior year are at least 10% of the average number of shares outstanding in that class during the prior calendar year.

An exchange has a “meaningful annual value of shares traded on the exchange” if it has an annual value of shares traded on

the exchange (or a predecessor exchange) exceeding USD billion during each of the three calendar years immediately preceding the calendar year in which the determination is being made. If an exchange has more than one tier of market level on which stock may be separately listed or traded, each such tier must be treated as a separate exchange.



How OECD can easily address the listed entity loophole



The FI must obtain from a listed entity account holder the self-certification of controlling persons, which can be confirmed with information held by the stock exchange.

Believe it or not, the way to address the listed entity loophole non-reporting of significant owners is already described in the CRS.

1. CRS beneficial owner need not be same as FATF recommendations, e.g. debt interest of investment entities or protectors of trusts. The FI obtains self-certification on controlling persons, which may be confirmed on disclosure transparency rules of the stock exchange.
2. Redact from CRS Pg. 70 par (148) this sentence "Thus, in such cases, it is accepted that a Reporting Financial Institution will not be able to determine the Controlling Persons for CRS purposes.
3. Prevent incorrect categorization of listed entity as an Active NFE without checking if it meets the 4 conditions of regularly traded.

Self-certification of listed entity for controlling persons

The FI should determine beneficial owners who own more than 25% of a listed company. This information is kept with the stock exchange. The FI should mandate the entity to reveal owners holding more than 25% shares of the listed entity and prove it with data held by the stock exchange. Note that FATF / CRS says FI need not identify beneficial owners if

Subject to disclosure requirements (either by stock exchange rules or through law or enforceable means) which impose requirements to ensure adequate transparency of beneficial ownership

CRS does not slavishly follow FATF to determine beneficial owner e.g. Although FATF recommends the beneficial owner of listed entities need not be determined

How to prevent incorrect categorization of listed entity as Active NFE

1. Remind FIs that a listed company is only an Active NFE if it is **regularly traded**, i.e. 4. Conditions regularly traded entity unless it meets the four conditions prescribed in the CRS.
2. Amend CRS FAQ that non-reportable person is a regularly traded entity. A listed entity is not a



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