

SBO – Navigating Through The Framework to Reveal The True Owners

Recently, it was observed by the Corporates and the professional community that MCA Central scrutiny Centre (CSC) has been sending advisory to all foreign subsidiaries to comply with the Significant Beneficial Ownership rules. Even though the rules have been effective from 2018, many Companies are still fumbling to understand and determine the applicability of the rules. Companies and their foreign holdings are often seen complaining about sharing extensive data about their shareholding patterns and ultimate beneficiary individuals citing restrictions implied on them by the virtue of confidentiality clauses in their shareholders agreements which could be breached by sharing sensitive information with external jurisdictions.



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INTRODUCTION

Recently, it was observed by the Corporates and the professional community that MCA Central scrutiny centre (CSC) has been sending advisory to all foreign subsidiaries to comply with the Significant beneficial Ownership rules. Even though the rules have been effective from 2018, many Companies are still fumbling to understand and determine the applicability of the rules. Companies and their foreign holdings are often seen complaining about sharing extensive data about their shareholding patterns and ultimate beneficiary individuals citing restrictions implied on them by the virtue of confidentiality clauses in their shareholders agreements which could be breached by sharing sensitive information with external jurisdictions. In order to counter such arguments, it is very important to understand the genesis of these requirements and also that it is not only Indian government which is asking for such data but all jurisdictions who are member states of the Financial Action Task Force (FATF) are required to collect and scrutinize such data from companies where ownership is not clearly visible through documentation available with the regulators. Member Countries are required to abide by the FATF recommendations in this respect and are peer reviewed for the processes

followed by each country so that they are not tagged as a jurisdiction requiring monitoring or high-risk jurisdictions by the FATF which will affect the reputation of the country and in turn the financial inflow in the country.

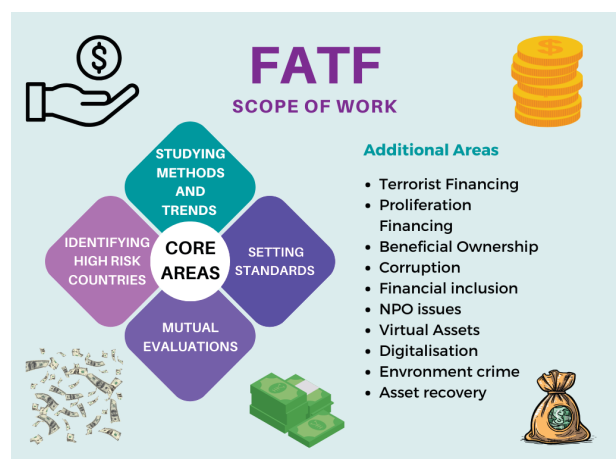
FIRST LET'S UNDERSTAND WHAT FINANCIAL ACTION TASK FORCE - FATF IS?

i) FATF and its Role

The Financial Action Task Force (FATF) is the global money laundering and terrorist financing watchdog.

FATF is an inter-governmental body whose main focus is to sets international standards to prevent illegal activities that can cause harm to the society at large. It brings together almost 200 major countries who have committed to abide by the recommendations made by FATF and cause a crackdown on the organised crime network including terrorism, corruption, drug trafficking, money laundering, arms trade, cybercrime etc. in their jurisdiction.

The FATF was established in 1989 and is based in Paris. Mr. T. Raja Kumar of Singapore is the President of the FATF from 1 July 2022 to 30 June





2024. Mr. Kumar succeeded Dr. Marcus Pleyer of Germany.

FATF conducts various researches to identify the mechanism used by crime syndicates and terrorists to launder money and raise, use and move funds for criminal activities. It develops standards to mitigate risk and also comments on the practices followed by member countries and assesses whether it is sufficient.¹

ii) FATF Recommendations

After undertaking various researches and seeking public consultation on best practices to combat the abuse of the existing financial systems by criminals and terrorists, FATF released its recommendations to tackle the menace of financial crimes and money laundering and updates it from time to time.

FATF has released its recommendations 'International standards on combating Money Laundering and the financing of Terrorism and Proliferation' which was adopted by the FATF plenary in February 2012. The most recent update in it was made in Feb 2023. The FATF Recommendations are recognized as the global Anti-Money Laundering (AML) and Counter-Terrorist Financing (CFT) standard.

Part E – para 24 and 25 of the Standards which are reproduced below deal with the requirement of transparency and beneficial ownership of legal persons and arrangements.

*24. Transparency and beneficial ownership of legal persons * Countries should assess the risks of misuse of legal persons for money laundering or terrorist financing, and take measures to prevent their misuse. Countries should ensure that there is adequate, accurate and up-to-date information on the beneficial ownership and control of legal persons that can*

be obtained or accessed rapidly and efficiently by competent authorities, through either a register of beneficial ownership or an alternative mechanism. Countries should not permit legal persons to issue new bearer shares or bearer share warrants and take measures to prevent the misuse of existing bearer shares and bearer share warrants. Countries should take effective measures to ensure that nominee shareholders and directors are not misused for money laundering or terrorist financing. Countries should consider facilitating access to beneficial ownership and control information by financial institutions and DNFBPs undertaking the requirements set out in Recommendations 10 and 22.

*25. Transparency and beneficial ownership of legal arrangements * Countries should assess the risks of the misuse of legal arrangements for money laundering or terrorist financing and take measures to prevent their misuse. In particular, countries should ensure that there is adequate, accurate and up-to-date information on express trusts and other similar legal arrangements including information on the settlor(s), trustee(s) and beneficiary(ies), that can be obtained or accessed efficiently and in a timely manner by competent authorities. Countries should consider facilitating access to beneficial ownership and control information by financial institutions and DNFBPs undertaking the requirements set out in Recommendations 10 and 22.²*

This requirement is the genesis of the rules and regulations framed and adopted by most countries including India to understand the 'Single Beneficial Owners' controlling the entities registered in its jurisdiction and the probable illicit use of its financial system by any beneficiary masked under layers of shell companies in various jurisdictions. So it's imperative to understand the importance of this data for curbing supply to the channels that probably fuel the nefarious aspirations of organized crime syndicates.

iii) Identification of ‘jurisdictions which require increased monitoring’ and ‘high risk jurisdictions’.

One of the key responsibilities of FATF is to identify and flag from time to time and publish the names of jurisdictions which need increased monitoring, in June 2023 it has published such a list and named countries like Albania, Barbados, Burkina Faso, Cayman Island, Cameroon, Democratic Republic Of Congo, Croatia, Gibraltar, Haiti, Jamaica, Jordan, Mali, Mozambique, Nigeria, Panama, Philippines, South Africa, Sudan, Syria, Tanzania, Turkey, Uganda, UAE, Vietnam, Yemen a countries which need increased monitoring.³

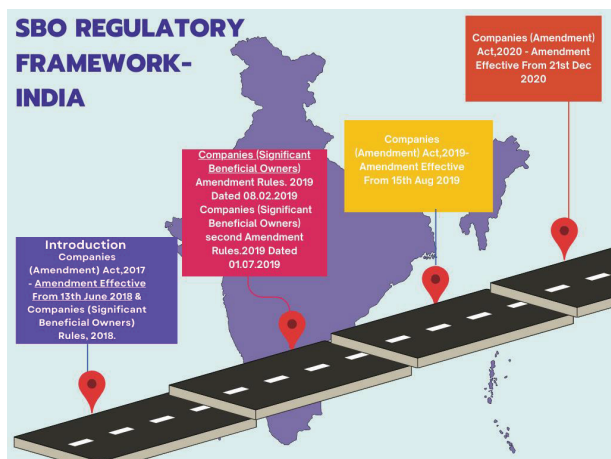
FATF also identifies and releases a list of high-risk jurisdictions based on the weak measures adopted to combat money laundering and terrorist financing (AML/CFT) and in the latest list released in June 2023. it has listed names of countries like North Korea, Iran and Myanmar⁴.

SBO REGULATORY FRAMEWORK IN INDIA

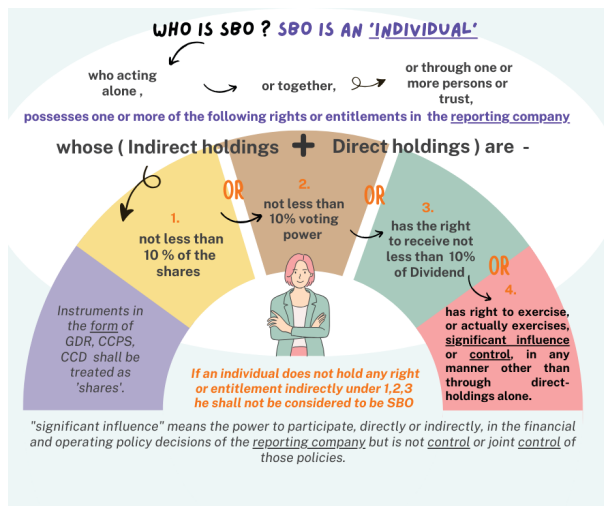
India is a member state of the FATF. In accordance with its commitment to crackdown on the money laundering and terrorism financing network, it had introduced the SBO compliance framework in 2017, however after ironing out many issues and removing interpretation difficulties of stakeholders on various aspects, the reporting could not be started until years later.

Finally, after many amendments, clarifications and consultations with commerce bodies, India has a preliminary framework to address the issue and support the world in the fight against financial crime. FATF is continuously conducting research and updating its recommended policies from time to time and expects its members to respond quickly with the updates, therefore we will see many changes in the coming days and India Inc will have to gear up for it.

i) Timelines of SBO rules notification in India

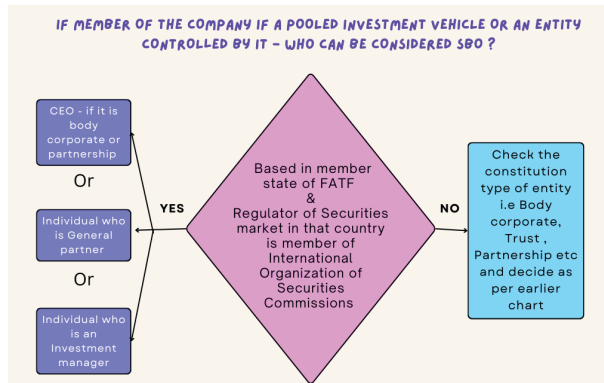
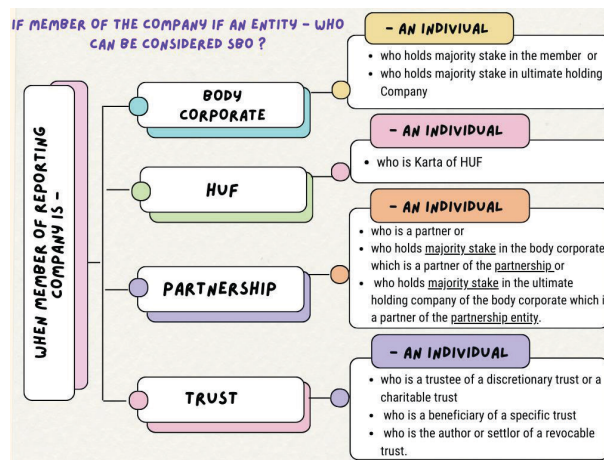


ii) So, Who is an SBO as per the rules ?

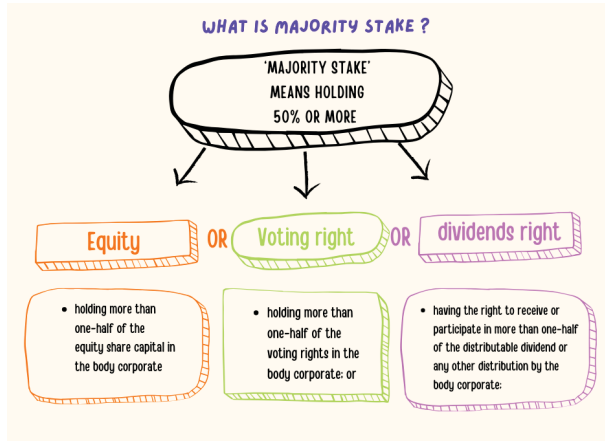


The expression ‘acting together’ has been clarified in the rules to include individuals acting through any person or trust, with a common intent or purpose of exercising any right or entitlement or exercising control or significant influence over a reporting company pursuant to an agreement or understanding, formal or informal.

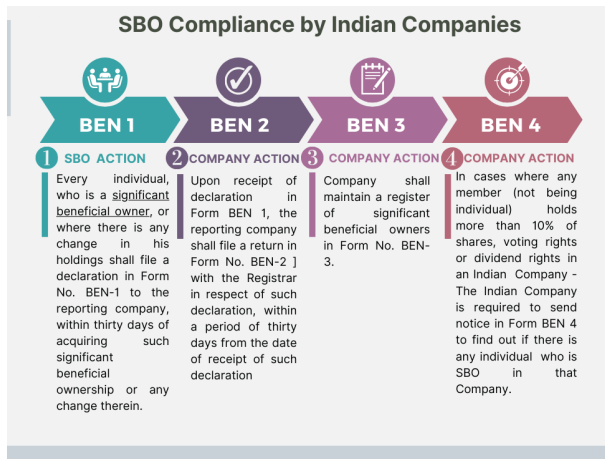
iii) What if Member of the reporting Company is an entity? How to identify SBO in such cases?



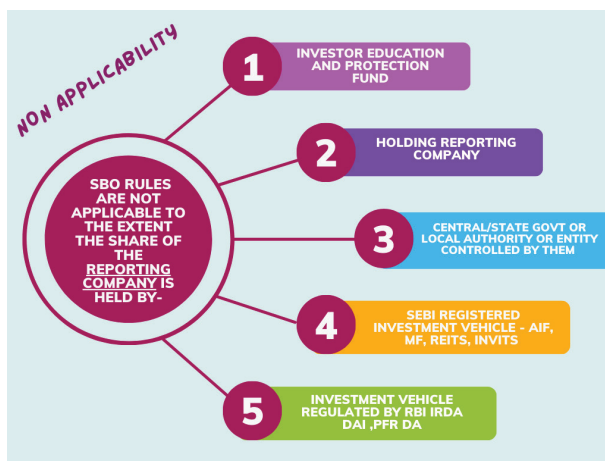
Who is a majority stake holder?



What compliances are required to be undertaken by Indian Companies ?



Non Applicability of SBO rules



CONSEQUENCES OF NOT DECLARING AN SBO OR DECLARING INCORRECT DATA

If any person fails to make any such declaration as required under the rules, he/she shall be

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liable to Fifty thousand Rupees and in case of continuous failure one thousand rupees for each such day of failure subject to a maximum of 2 lakhs Rupees.

If any person/entity, wilfully furnishes any false, incorrect information or suppresses any material information of which is aware in the declaration made by it under the SBO provisions then the provision of Section 447 – Punishment for Fraud is invoked and becomes applicable on the person. Therefore, it is advisable to thoroughly understand the provisions and then make the required declarations under these rules.⁵

CONCLUSION

While the intent of the law is noble, there are many interpretational challenges and unaddressed situations where deciding who is an SBO becomes difficult. It is said that change is the only thing that is constant and on the same principle we will be seeing many changes in the rules before the rules can effectively start doing the job for which they were implemented. But being a step in the right direction and with the support of the professional community surely the nuances of modern crimes, shady transactions, money laundering etc will be tackled sooner or later.

REFERENCES:

- <https://www.fatf-gafi.org/>
- The Fatf Recommendations International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation*
- FATF Publication - Jurisdictions under Increased Monitoring - 23 June 2023*
- FATF Publication - High-Risk Jurisdictions subject to a Call for Action - June 2023*
- Section 90 (10) & (12) of the Companies Act 2013.*