



Consultation on the Transposition of 5MLD
Sanctions and Illicit Finance Team (2/27)
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
London
By email: Anti-MoneyLaunderingBranch@hmtreasury.gov.uk

10 June 2019

Dear Sir/Madam

Re: BVCA response to HMT consultation on the transposition of the Fifth Money Laundering Directive (the “Consultation”)

We are writing on behalf of the British Private Equity and Venture Capital Association (“BVCA”), which is the industry body and public policy advocate for the private equity and venture capital industry in the UK. With a membership of over 770 firms, the BVCA represents the vast majority of all UK based private equity and venture capital firms, as well as their professional investors and advisers. Over a period of five years (2013-2017), BVCA members have invested over £32bn into nearly 2,500 UK companies. Our members currently back around 3,380 companies, employing close to 1.4 million people on a full-time equivalent basis (“FTEs”) across the world. Of these, around 692,000 FTEs are employed in the UK. Of the UK companies invested in during 2017, around 83% were SMEs. Between 2013 and 2017, BVCA members rescued 91 companies experiencing trading difficulties, helping safeguard over 37,000 jobs.

The BVCA is delighted to have the opportunity to respond to the Consultation. We have responded only to those questions with particular relevance to our member firms.

Customer due diligence

47. To what extent would removing ‘reasonable measures’ from regulation 28(3)(b) and (4)(c) be a substantial change? If so, would it create any risks or have significant unintended consequences?

As a general proposition, where the underlying CDD obligation necessarily involves a degree of subjectivity or judgement, we believe the concept of taking 'reasonable measures' should be retained. Otherwise, it is very difficult for firms to determine whether or not they have fulfilled their obligations, which is likely to result in firms taking a disproportionately conservative approach to CDD.

In relation to regulation 28(3)(b), we consider that this change would have a very limited impact. Regulation 28(3)(b) requires firms to determine and verify a finite set of objectively verifiable information. There is relatively little practical difference between a "reasonable endeavours" obligation and a requirement here; in either case, the practical result is that firms will need to obtain and verify the relevant details. We think it would be unusual in the private equity sector for a firm to find itself unable – despite its reasonable endeavours – to determine and verify the information



required by regulation 28(3)(b) in relation to a particular customer, but still to be comfortable proceeding with the transaction or relationship. While we do not think the proposed change to this regulation would materially improve the quality of CDD, we also do not think there would be material downsides or unintended consequences.

In practice, regulation 28(4)(c) as currently drafted is of relatively limited application for our member firms; in the vast majority of situations, the beneficial owner will be an individual and regulation 28(4)(c) will not apply. We therefore think the practical impact of this change would be limited for our sector. However, as a matter of principle, we consider the points made in our response to Q49 below to be equally relevant here.

48. *Do you have any views on extending CDD requirements to verify the identity of senior managing officials when the customer is a body corporate and the beneficial owner cannot be identified? What would be the impact of this additional requirement?*

We think the impact of this additional requirement would be very limited and see no reason not to extend this CDD requirement as proposed. In the private equity industry, we believe that regulations 28(6) and (7) are rarely relied on. In practice, if a firm has tried, but is unable, to identify the beneficial owner of a customer who is a body corporate, in most situations the firm would conclude that it has been unable to apply CDD to the customer in a satisfactory manner and so would not proceed with the transaction or the relationship, rather than proceeding instead to treat the senior manager as the beneficial owner.

49. *Do related ML/TF risks justify introducing an explicit CDD requirement for relevant persons to understand the ownership and control structure of customers? To what extent do you already gather this information as part of CDD obligations?*

Our member firms typically already gather this information as part of CDD in any case (see, for example, paragraphs 5.3.30 and 5.3.147 of Part I of the JMLSG Guidance, which indicate that this is expected). If an explicit requirement is included, this must be a "reasonable endeavours" (or "reasonable steps") obligation rather than an absolute requirement to avoid creating a disproportionate burden for firms. Many smaller firms in particular will face strong resistance from customers to obtaining details which can be highly commercially sensitive and will often add little value to the assessment of money laundering risk where a firm has been able to confirm the identity of beneficial owners. From the firm's perspective, being comfortable that you understand the ownership and control structure of the customer is clearly important, but this necessarily includes a degree of subjectivity and judgement. It is important that firms, and the individuals within firms who are responsible for CDD processes, are able to make a good faith assessment that they have made reasonable enquiries and are reasonably satisfied as to the information provided and their understanding of it. A "reasonable endeavours" (or "reasonable steps") obligation therefore seems appropriate here and would be consistent with the current JMLSG guidance.

In our experience, firms consider that the requirement to apply "reasonable endeavours" sets a high bar. We doubt that any additional AML/CFT benefit would, in practice, be achieved by imposing an absolute requirement on firms to understand the ownership and control structure of



customers. It would, however, make it significantly harder for firms to be confident that they have satisfied their CDD obligations, with a consequent risk that the process becomes materially more protracted and burdensome for both firms and customers. If an absolute requirement is imposed, we do not believe this will result in firms obtaining better quality CDD information than at present, but it would make it significantly harder for compliance teams to be confident that the firm's CDD obligations have been satisfied. We anticipate this would result in a more protracted and bureaucratic process that would be contrary to the overall risk based approach that underpins the CDD regime.

Mechanisms to report discrepancies in beneficial ownership information

61. *Do you have any views on the proposal to require obliged entities to directly inform Companies House of any discrepancies between the beneficial ownership information they hold, and information held on the public register at Companies House?*

We understand that this proposal relates only to UK obliged entities in situations where they are conducting CDD on customers that are subject to UK beneficial ownership registration requirements (i.e. the Companies House PSC register or, where relevant, the TRS). It would be helpful for this to be stated explicitly in the implementing legislation.

Whilst we recognise that HMT is required under 5MLD to create a requirement for obliged firms to report discrepancies between CDD information they hold and information on the public register, we have significant concerns about this proposal. Private equity is a global industry, and private equity structures often include overseas entities, limited partnership structures and other vehicles. The voting and share rights in some of these vehicles are determined by their constitutional documents, and may vary significantly between entities that are ostensibly similar. It is not at all straightforward for an external party to assess whether the information contained in the beneficial ownership register for a UK company with such a holding structure is correct, even if they are in possession of full CDD information. Indeed, it is likely to have taken the private equity firm itself a significant amount of time, with advice from external counsel, to determine its registration position.

It is essential that this new requirement does not effectively require a counterparty to rerun its customer's beneficial ownership analysis, or to monitor for changes on an ongoing basis. The requirement should be narrowly drawn, so that only fundamental discrepancies that are self-evident from the CDD information provided are reportable. It could perhaps be framed in terms that an obliged entity is required to report discrepancies if it has reasonable grounds to suspect that the information recorded on the public register in relation to the customer is false and that it has been registered with an intention to mislead.

It is also important that the requirement is relatively narrowly drawn so that the quality and volume of information received is such that Companies House can readily identify those situations requiring investigation. If the reporting requirement is too broad, we consider there to be a material risk of over-reporting, resulting in a high volume of poor quality information being received.



We would be happy to discuss the contents of this letter with you; please contact Tim Lewis at tim.lewis@traverssmith.com and Tom Taylor (ttaylor@bvca.co.uk).

Yours faithfully,

A handwritten signature in blue ink, appearing to be 'Tim Lewis', with a long horizontal flourish extending to the right.

Tim Lewis
Chair, BVCA Regulatory Committee