

insights

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New FinCEN beneficial ownership requirements for legal entity customers to become effective in May 2018

Effective May 11, 2018, new Financial Crimes Enforcement Network (FinCEN) regulations (codified at 31 C.F.R. §§ 1010.230 and 1020.210(b)(5)) (the "New Regulations") require that covered financial institutions, including banks:

- Enhance their due diligence practices when opening new accounts for legal entity customers by obtaining and maintaining information identifying the beneficial owners of those legal entity customers, and
- Amend their anti-money laundering (AML) program requirements related to collecting, monitoring, and maintaining this information.

Purpose of the New Regulations

By requiring identification of the individuals who own legal entity customers as well as individuals who control such legal entity customers, the New Regulations are aimed at preventing financial crimes conducted through accounts created and operated anonymously through a "straw man" or nominee. The information collected under the New Regulations will assist financial institutions in assessing risks in opening new accounts, as well as facilitate investigation of compliance with tax and other targeted FinCEN regulations.

Who must comply with the New Regulations?

All "covered financial institutions" must comply with the New Regulations. A "covered financial institution" (CFI) for purposes of the New Regulations refers to the following: banks, federally insured credit unions, savings associations, corporations organized for international or foreign banking or financial operations, trust banks or trust companies that are federally regulated and subject to an anti-money laundering program requirement, mutual funds, brokers or dealers in securities, futures commission merchants, and introducing brokers in commodities.

What is a legal entity customer?

For purposes of the New Regulations, a "legal entity customer" is defined as a corporation, limited liability company, general partnership, and any other entity created by filing a public document with the secretary of state or similar office, such as a business or statutory trust, as well as a similar business entity formed in a foreign country. Legal entity customers do not include, for example, sole proprietorships, unincorporated associations, estate-planning trusts, or natural persons opening accounts on their own behalf.

Identifying the beneficial owners of legal entity customers

The New Regulations require that CFIs enact due diligence procedures to identify the beneficial owners of legal entity customers and verify the identity of each beneficial owner identified to the CFI. The beneficial owners identified for each legal entity customer must include:

1. **Ownership:** Each individual^[1] (if any) who *directly or indirectly* owns 25% or more of the equity interests of a legal entity customer. Depending on the facts, up to four individuals may need to be identified; and
2. **Control:** At least one^[2] individual with "significant responsibility to control, manage, or direct a legal entity customer" (including an individual acting in an executive office or senior management position, such as a Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, or Treasurer).

Obtaining and verifying the information

Information identifying beneficial owners may be obtained either from an individual seeking to open a new account on behalf of a legal entity customer (whether or not that individual is a beneficial owner within the above definitions), or from another CFI that has collected the information, so long as the reliance is reasonable, the other CFI is also subject to compliance with the New Regulations and regulated by a federal functional regulator, and the CFIs have entered into a contract setting forth certain required terms. For example, in a syndicated credit agreement, an individual lender can obtain its information directly from the borrower or from another lender or the agent bank, assuming it, too is a CFI.

- **Certification Form:** FinCEN has provided a standard “[Certification Form](#).” CFIs may, but are not required to, use this form to comply with the New Regulations. This Certification Form includes spaces to collect the name, date of birth, address, and social security number (or, for foreign individuals, passport number) of each applicable beneficial owner.

Further, the New Regulations do not require the CFI to conduct independent due diligence or research to verify the ownership of an entity, and no additional documentary verification or reporting requirements are being implemented with regard to identifying beneficial owners, provided that the CFI has no knowledge of facts that would reasonably call into question the reliability of such information. CFIs are still responsible, however, for understanding the nature and purpose of the customer relationship, maintaining ongoing monitoring procedures, reporting suspicious transactions, and updating beneficial owner information as determined by the CFI based on risk.

AML program amendments

In addition to the beneficial ownership information components discussed above, the New Regulations also amend the AML program requirements for CFIs to explicitly require them to implement and maintain appropriate risk-based procedures for conducting ongoing customer due diligence for such CFIs.

Anticipated issues for financial institutions

Ahead of the New Regulations going into effect, CFIs can prepare for implementation by assessing business lines that will be impacted by the New Regulations and revising due diligence requirements for those affected areas accordingly. CFIs should decide how to collect, verify, and maintain the required beneficial ownership information moving forward, whether choosing to use FinCEN's standard Certification Form for recordkeeping or creating standard forms of their own (which may involve merely updating already-existing Customer Identification Program documentation). Further, CFIs should consider amending customer documents to include covenants for legal entity customer compliance under the New Regulations.

Some beneficial owners may be wary of providing the required personal information. CFIs can encourage transparency by providing clear-cut information about the requirements and underlying purpose of the New Regulations, hopefully ensuring cooperation of legal entity customer owners and management.

If you have further questions concerning the regulation and its impact on your due diligence requirements, please contact us.

[1] If a trust directly or indirectly owns 25% or more of the equity interests of a legal entity customer, the beneficial owner shall mean the trustee.

[2] The New Regulations and FinCEN's corresponding guidance only specify that a minimum of one individual is required to be identified. A CFI may identify additional individuals if it deems appropriate based on risk.

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