

The Association of Investment Companies

MONEY LAUNDERING REGULATIONS 2007

Executive Summary

- Non-executive directors of all companies (including investment companies) potentially have to register with HM Revenue & Customs (HMRC) under the Money Laundering Regulations 2007 (the MLRs) as Trust or Company Service Providers (see paras 2 & 3) and comply with the other obligations of the MLRs (see para 4).
- However, in practice, as a result of guidance issued by HMRC ('the HMRC Guidance'), the vast majority of directors of investment companies are unlikely to have to register as a result of their investment company directorships, though directors may need to keep their status under review. Directors may, however, need to register as a result of their other directorships.
- In particular, directors will not need to register under the MLRs if:
 1. They are not acting in the course of business carried on by them in the UK (paras 6 & 7). This may be particularly relevant for offshore resident directors of offshore domiciled investment companies.
 2. The investment company(ies) that they are a director of are not carrying out business in a 'high risk jurisdiction' or 'high risk sector' (paras 8, 11, & 12).
- Subject to certain conditions, directors whose services are made available via a Personal Service Company (PSC) will not need to register their PSC if they would not have had to register under the MLRs as an individual (para 15).

In view of the deadline for registration of 30 September 2008, and the potential penalties involved for failing to register, it is advised that all directors consider this guidance as soon as possible to establish whether they need to register under the MLRs or not.

Disclaimer

This paper is not exhaustive and is intended to be general guidance only. It is not intended to be a substitute for reading the HMRC Guidance. It is intended for use solely by the AIC's members and their directors, who should consider taking professional advice before relying on anything contained in this paper.

The AIC accepts no responsibility for any errors or omissions in this paper or for any loss occasioned to any person acting or refraining from action as a result of any material contained in this publication.

The Association of Investment Companies

MONEY LAUNDERING REGULATIONS 2007

Guidance on whether directors of investment companies, or their personal service companies, need to register

1 Introduction

- 1.1 Following discussions between HM Treasury, HMRC and the AIC, this paper considers whether directors of investment companies fall within scope of the regulations and need to register with HMRC under the Money Laundering Regulations 2007 (the MLRs) solely by virtue of their directorships of investment companies.
- 1.2 It also considers the position where the services of a director are made available via a Personal Service Company (PSC). The paper considers the position of both onshore and offshore investment companies, as well as onshore and offshore resident individuals acting as directors of these companies.
- 1.3 This paper does not consider any other money laundering, or similar obligations that may arise under other legislation. It also does not consider the question of whether individuals may need to register by virtue of their directorships of other types of companies. However, it should be noted that the HMRC Guidance does not specifically address the position of directors of investment companies and that the HMRC Guidance is applicable to directors generally. Therefore, directors of investment companies may need to register by virtue of their other directorships.

2 Background

- 2.1 The MLRs, which implement the EU 3rd Money Laundering Directive, make it clear that firms or individuals providing the service of acting as a company director by way of business to other persons fall within the scope of the regulations.
- 2.2 However, HMRC has now published updated guidance covering this to reflect feedback from businesses in their discussions with HM Treasury. The HMRC Guidance is available from <http://www.hmrc.gov.uk/mlr/mlr9.pdf>.
- 2.3 Individuals providing their services as company director will fall within scope only when they act for firms carrying out business in high risk areas and only if those businesses are not already supervised for compliance with the MLRs.
- 2.4 This advice is provisional, because HM Treasury is continuing to reflect on whether investment companies need to be regulated and supervised as

The Association of Investment Companies

relevant persons under the MLRs. Any decision on this matter will affect whether individuals acting as directors of these companies fall within scope of the regulations and may be required to register with HMRC. **However, HMRC has indicated that, until the position has been clarified, directors of investment companies which are within the scope of the MLRs (leaving aside the question of whether investment companies will be supervised), will need to register by the appropriate deadline.**

3 Do directors of investment companies potentially have to register with HMRC under the MLRs?

3.1 Yes. A director may fall within the scope of the MLRs as a Trust or Company Service Provider (TCSP) which is defined in regulation 3(10) as follows:

(10) “Trust or company service provider” means a firm or sole practitioner who by way of business provides any of the following services to other persons—

(a) forming companies or other legal persons;

(b) acting, or arranging for another person to act—

(i) as a director or secretary of a company;

(ii) as a partner of a partnership; or

(iii) in a similar position in relation to other legal persons;

(c) providing a registered office, business address, correspondence or administrative address or other related services for a company, partnership or any other legal person or arrangement;

(d) acting, or arranging for another person to act, as—

(i) a trustee of an express trust or similar legal arrangement; or

(ii) a nominee shareholder for a person other than a company whose securities are listed on a regulated market, when providing such services.

Therefore a director of an investment company may be within the scope of the MLRs. However, this is subject to a number of exceptions, which are likely to mean that many directors will not fall within the scope of the regulations.

3.2 The regulations do not apply to an individual who is only a director of a company that is his/her employer. This is because he/she will not be acting as a director “by way of business”. Therefore, executive directors of self-managed investment companies should not be within the scope of the MLRs.

3.3 Directors falling within the scope of the regulations as TCSPs that are not already supervised for the purpose of the MLRs by the FSA or a designated professional body specified in schedule 3 of the regulations will be required to register with HMRC. In most cases, therefore, directors of investment companies who fall within the scope of the regulations would need to register with HMRC. (See para 8 onwards for the issues

The Association of Investment Companies

that directors will need to consider to determine if they fall within scope of the MLRs.)

4 What are the implications of being within the scope of the MLRs?

4.1 In addition to registering, all businesses falling within the scope of the regulations must put in place anti-money laundering policies and procedures in order to identify and report where they have reasonable grounds for knowledge or suspicion of money laundering or terrorist funding. Further guidance on this issue can be found at <http://www.hmrc.gov.uk/mlr/mlr8.pdf>.

4.2 If a director determines that he/she, or his/her PSC, needs to register, then details on how to do so can be found on <http://www.hmrc.gov.uk/mlr/register.htm>.

5 When would a director or PSC need to register by?

5.1 If a business (including that of a director acting as a TCSP) is required to register with HMRC the relevant dates are:

- existing businesses must apply to register by **30 September 2008** so that they are on the register by 1 January 2009
- new businesses must be on the register before they act as director.

5.2 However, because of delays in processing registration applications and clarifying the scope of the regulations, HMRC has indicated that they will be sympathetic if new businesses have delayed applying to register during the period May to July 2008, but they must now apply without delay and make sure that they put in place anti-money laundering systems and processes.

6 Do directors of offshore investment companies potentially fall within the scope of the MLRs?

6.1 Yes. The focus of the regulations is on where the director carries on business and the regulations envisage that customers may be outside the UK. The MLRs state that the regulations apply to:

“persons acting in the course of business carried on by them in the United Kingdom”

Regulation 3(1) MLR 2007

The Association of Investment Companies

- 6.2 It is where the director carries on his business rather than where the company of which he/she is a director is incorporated or located, or where board meetings are carried out, or where he/she is resident, that will determine whether an individual carries out the business of acting as a director in the UK. This is a question of fact that will in most cases be quite clear to the individual, but must always be decided on a case-by-case basis.
- 6.3 For example, offshore resident directors of offshore domiciled investment companies, who do not carry out any of their duties in the UK, or have any business presence in the UK, may be able to establish quite easily that they are not within the scope of the MLRs on the basis that they are not acting in the course of business carried on by them in the UK.
- 6.4 However, if someone resident in Germany were to provide services through a UK registered PSC to a non-UK company, he could still be carrying on business as a TCSP in the UK, although he would not be resident in the UK or attending board meetings in the UK. Similarly, if someone lives in London but carries out all his TCSP activity in Ireland and has no business presence in the UK, the fact that he is resident in the UK is irrelevant.
- 6.5 In view of the penalties associated with failure to comply with the regulations, including putting in place anti-money laundering systems and processes, directors in any doubt over this issue are likely to want to consider whether they fall within the scope of the regulations and need to register with HMRC, or whether they fall outside the scope of the regulations for other reasons (as set out below).

7 Do non-UK resident directors of UK domiciled investment companies potentially fall within the scope of the MLRs?

- 7.1 Yes. A non-UK resident director of a UK incorporated investment company will fall within the scope of the regulations if they carry on the business of acting as a director in the UK.
- 7.2 It is where the director carries on his/her business rather than where the company of which he/she is a director is incorporated or located, or where board meetings are carried out, or where he/she is resident, which will determine whether an individual carries out the business of acting as a director in the UK. This is a question of fact that must be decided on a case-by-case basis.
- 7.3 For example, if someone resident in Ireland provides his services through a UK registered PSC to a UK company, he could still be carrying on business as a TCSP in the UK, although he would not be resident in the UK.

The Association of Investment Companies

8 Will individuals acting as directors of investment companies therefore need to register with HMRC and apply the money laundering obligations?

- 8.1 This will depend on the businesses for which they are acting as director. The HMRC Guidance provides that only individuals acting as director for businesses operating in certain high risk areas will need to comply with the requirements of the MLRs and register with HMRC.
- 8.2 The guidance states that the following individuals acting as directors would need to comply with the MLRs:

Any individual providing their service

- o *as nominee director or nominee company secretary or*
- o *as company director, company secretary or partner to a firm carrying out business in the following high risk areas;*

*within a high risk jurisdiction
within a high risk sector*

unless the firm is

- o *already supervised under the MLRs or*
- o *a public authority or*
- o *a firm authorised by a public authority to act on their behalf where the only customers are also public authorities*

MLR Guidance 6.1

9 Are investment companies supervised under the MLRs?

- 9.1 Investment companies are not currently supervised for the purposes of the MLRs. HM Treasury and the FSA are reviewing how investment companies are dealt with under the MLRs, and whether they should be supervised. Until the review is concluded, if directors fall within the scope of the MLRs, they should register with HMRC unless they fall outside the scope of the MLRs for other reasons.
- 9.2 Therefore, where an individual is carrying on business in the UK as a director of an investment company, the director would need to register if the company is 'carrying out business' either 'within a high risk jurisdiction' or 'within a high risk sector'.

The Association of Investment Companies

10 What does the term 'carrying out business' mean in the context of an investment company?

10.1 The HMRC Guidance refers to 'carrying out business' rather than 'carrying out its business'. As a result, the AIC considers that the term is not limited to where the company carries out its business of portfolio management, but rather relates to where it carries out any business transaction.

10.2 The term is therefore potentially very wide, and would mean that the director would need to consider the status, amongst other things, of the following:

- Where the investment company is incorporated
- Where the fund management takes place
- Where it transacts its investment dealings
- The countries it invests in

11 What is a high risk jurisdiction?

11.1 The HMRC Guidance (6.1.13) states that this will include a jurisdiction noted by the Financial Action Task Force as having weak anti-money laundering systems. It also states that guidance on high risk jurisdictions can be found on the financial crime pages of HM Treasury website at:

http://www.hm-treasury.gov.uk/documents/financial_services/money/fin_crime_policy.cfm

11.2 The most recent pronouncement identified the following countries as high risk:

- Uzbekistan
- Iran
- Pakistan
- Turkmenistan
- São Tomé and Príncipe
- the northern part of Cyprus.

11.3 As a result, at present, the AIC would envisage that most of its Members are not carrying out business within a high risk jurisdiction. However, even if this is the case, the position could change in the future and so directors of investment companies which are not supervised in the UK would need to monitor the position on a regular basis.

The Association of Investment Companies

12 What is a high risk sector?

12.1 The HMRC Guidance (6.1.14) states that a high risk sector is:

- A firm carrying out frequent cash transactions of €15,000 or more
- A company operating within the UK but incorporated outside the UK in a non-equivalent jurisdiction
- A company with a holding interest in their capital held in the form of unregistered bearer shares

12.2 Most, if not all, investment companies will not carry out frequent cash transactions, or issue unregistered bearer shares. However, this is a question of fact that must be determined on a case-by-case basis.

13 What does 'operating within the UK' mean in the context of an offshore investment company?

13.1 No guidance is given on what the term 'operating in the UK' means. However, this term might cover investment companies which:

- Invest in UK companies
- Whose fund manager is based in the UK
- Carries out transactions on UK exchanges

13.2 Many investment companies may, therefore, be considered to be operating in the UK.

14 What is an equivalent jurisdiction?

14.1 The HMRC Guidance states (6.1.15) that this is a country with anti-money laundering systems/countering terrorist finance regimes of similar quality to those of the EU. It also refers to the Treasury's financial crime page which contains a list of countries considered to have equivalent anti-money laundering and countering terrorist financing regimes.

http://www.hm-treasury.gov.uk/documents/financial_services/money/fin_crime_policy.cfm

14.2 As the MLRs derive from EU legislation, all EU countries would be automatically considered to be equivalent without the need to refer to the Treasury's list.

14.3 The Crown Dependencies are currently considered to be equivalent. Bermuda and the Cayman Islands are currently not. However, in cases where the company is domiciled in a non-equivalent jurisdiction, it will only be considered high risk if it is also operating in the UK.

The Association of Investment Companies

14.4 As a result, with the exception of a handful of Members, the vast majority of the AIC's Members are incorporated in equivalent jurisdictions.

15 What if the director's services are provided by a Personal Service Company (PSC)?

15.1 The above analysis only applies to directors acting as individuals. The AIC is aware that a substantial number of directors make their services available via a PSC.

15.2 The HMRC Guidance (6.1.6) states that a PSC supplying the services of an individual will only fall within scope of MLRs to the extent that the individual they represent falls within scope and providing that the PSC:

- only supplies the services of that individual; and
- that individual owns or controls at least 50% of the business and the sole business purpose of the company is to provide the services of that individual.

15.3 In many, if not all, cases the PSCs of directors of investment companies will meet the last two conditions.

15.4 If this is the case, then directors whose services are provided by PSCs should consider whether they would have needed to register under the MLRs as individuals if the PSC did not exist (as per the above analysis). If this is not the case, then the directors do not need to register the PSC.

16 Conclusion

16.1 As a result, although directors of investment companies are potentially within the scope of the MLRs, the AIC believes that most will not actually be within scope for the reasons given above, though this position may need to be monitored on an ongoing basis. However, directors may, of course, need to register by virtue of their other (non-investment company) directorships.

16.2 In due course, if UK investment companies become supervised under the MLRs, then it will become easier for directors of these companies to demonstrate that they do not need to register.