Trust and Anti-Money Laundering Regulation in Italy

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Summary:

1) Introduction
2) Trust and anti-money laundering law
3) The beneficial owner and the Directive 2005/60/CE
4) The “client” according to the anti-money laundering regulation
5) The “beneficial owner” according to the III EU Directive and the IV EU Directive
6) The Register of information on beneficial owners
7) Due diligence obligations
8) Disclosure obligations and confidentiality of client information

1. Introduction

Despite some hurdles mostly related to the fact that, as is commonly known, Italy does not have a proper trust regulation, the interest for this instrument is growing also in our Country for quite a few
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years now. This is shown also by the increasingly settlement of trusts which has characterized our jurisdiction during the last years.

Indeed, the institute of trust has been recognized in Italy through the ratification of the Hague Convention of July 1st 1985. The Convention pursued the aim of harmonizing the Private International rules, related to trusts, in order to allow civil law countries to borrow the trust instrument from foreign jurisdictions whose legislation regulates the trust instrument properly.

As a result of that process, nowadays trusts are fairly used in Italy, even if for many years, also after the Hague Convention, there was no reference to the trust matter in the Italian legislation.

The Italian Parliament is working on that subject, preparing for what has been announced as one of the most important legislative innovations to be achieved in the near future: the reform of the trust institution.

Indeed, rather than a proper “reform”, it shall be only the first sign of the introduction of an organic regulation of an institute that, born and consolidated in the common law legal experience, has entered our juridical system more than twenty years ago, seeking timidly to affirm even in the strictest logic of the civil law tradition.

Up to now, in fact, despite various legal drafts (presented in the past, but resolved in a nutshell) and a tight and fragmented tax discipline, our juridical system still lacks a civil discipline of trust.

It is worth reminding that as set forth in article 6 of the Hague Convention "trust shall be governed by the law chosen by the taxpayer" and, as provided by the following article 7 "Where no applicable law has been chosen, a trust shall be governed by the law with which it is most closely connected.". The possibility, provided by the Convention itself, to adopt Jersey law rather than the Isle of Man Law or the United Kingdom one,
however, is probably the most weakness of the institute. In fact, it continues to be perceived with doubt, almost inevitably subverting any abusive or evasive behavior.

2. Trust and anti-money laundering law

The money laundering topic is particularly sensitive if related to the institute of trust.

As a matter of fact, dealing with the multifaceted trust instrument, an apparently straightforward procedure such as the so called “thorough verification” turns into an activity that requires legal knowledge other than domestic and comparative law awareness. Most of the time the concept of “client” is related to the trust and not to the trustee, such as the concept of “beneficial owner” that is related mostly to the trustee or the protector and rarely to the beneficiaries.

Considering that the results of a proper verification are relevant to any subsequent investigation of that operation, it is deemed crucial to carry out all the due diligence obligations, such as identification, collection of information and documents and, under certain circumstances, monitoring activities.

It comes clear how the atypicality of this instrument and therefore its use for different purposes, in addition to the natural effect of the dissociation between formal ownership and substantial ownership, encourages the use of the trust instrument not only for legitimate purposes but also for illegal purposes.

To worsen the situation our law system as well as the most commonly used foreign jurisdictions, no mandatory public disclosure of the Trust Deed is required in order to make it valid.

Moreover, another critical circumstance is that the trustee, often based in geographic areas which do not have public registers, is bent to keep the secrecy about the relationship between the subjects involved into the trust.
Therefore, it is worth looking into the trust instrument with a keen eye for the anti-money laundering legislation.

3. The beneficial owner and the Directive 2005/60/CE

The Legislative Decree no. 231/2007 (hereinafter “Anti-Money Laundering Regulation”) has transposed in Italy the provisions of the European Directive 2005/60/CE (so called “III Directive”), which introduced specific rules for the identification of the beneficial owner, specially with reference to the trust.

The difficulty in the identification is even worse for Italian entities, since, in the lack of an Italian regulation, it is necessary resort to foreign legislations not requiring any obligation as those provided by the Directive 200/60/CE (e.g. Jersey, Guernsey, Man and San Marino). Therefore, it is easy to understand that Italian professionals need often to face problems related to the anti-money laundering obligations as well as those related to the identification of the beneficial owner of the trust.

In relation to the abovementioned countries is not possible to benefit of simplified obligations whether the trustee – or the entities which provide to make the thorough verifications - are resident there, for the same reasons already explained.

4. The “client” according to the anti-money laundering regulation

According to article 18 of the Anti-Money Laundering Regulation, the required obligations for the client verification consist of the following activities: a) identify the clients and verify their identity on the basis of specified documents, data or information obtained from a reliable and independent source; b) identify the beneficial owner and verify his/her identity; c) collect information on the intended purpose.
and nature of the professional performance; d) supervise the activities in relation to the professional performance.

On the basis of the above, the first step is to properly identify the client.

According to article 1, II comma, letter e) of AML Regulation, it is deemed to be “client” the individual or the entity who has a continuing relationship or carry out operations with the recipients of articles 11 (financial intermediaries) and 14 (other related subjects) or, alternatively, the subjects whom the recipients of article 12 (professionals) and 13 (auditors) perform a professional assignment, due to a specific mandate.

Apparently, the “client” seems to be the trustee of the trust. However, the AML Regulation clarifies that the client is the trust, even though it does not have a proper legal personality.

Indeed, article 19, paragraph I, lett. b) of the abovementioned regulation provides that trusts are deemed to have legal personality, specifying that "identification and verification of identity of the current beneficial owner is carried out simultaneously with the identification of the client and imposes, for the legal entities, trust and similar legal entities, the adoption of specific measures and commensurate with the situation of risk to understand the property and control structure by the client".

As mentioned, article 19 of the Anti-Money Laundering Regulation requires the identification of the beneficial owner of the trust. This circumstance confirms that the "client" shall be identified in the trust.

As a matter of fact, the beneficial owner must be identified with reference to the "client": in accordance with article 1, paragraph II, lett. u), it is considered as "beneficial owner" “the natural person who, ultimately, possess or exercise control over the client”. If it is necessary to investigate who are the
beneficial owners of the trust and these are the persons who "own and control the client" (trust), it comes clear that the trust is to be considered as a "client".

5. The “beneficial owner” according to III EU Directive and the IV EU Directive

According to the Directive 2005/60/EC of the European Parliament of 26th October 2005, the beneficial owner is the natural person on whose behalf an operation or activity is performed, or, in the case of a legal entity, the person or natural persons who ultimately possess or control this entity or become beneficiaries, according to the criteria described in the technical annex to Legislative Decree 231/2007.

In particular, in the case of a trust, the beneficial owner is within the meaning of Directive 2005/60/EC, article 3 “in the case of legal entities, such as foundations, and legal arrangements, such as trusts, which administer and distribute funds: (i) where the future beneficiaries have already been determined, the natural person(s) who is the beneficiary of 25% or more of the property of a legal arrangement or entity; (ii) where the individuals that benefit from the legal arrangement or entity have yet to be determined, the class of persons in whose main interest the legal arrangement or entity is set up or operates; (iii) the natural person(s) who exercises control over 25% or more of the property of a legal arrangement or entity”.

The definition provided by the IV Directive aimed at redefining the notion of beneficial owner specified by the III Directive, provides otherwise “in the case of trusts: (i) the settlor; (ii) the trustee(s); (ii) the protector, if any; (iii) the beneficiaries, or where the individuals benefiting from the legal arrangement or entity have yet to be determined, the class of persons in whose main interest the legal arrangement or entity is set up or operates; (iv) any other natural person exercising ultimate control over the trust by means of direct or indirect ownership or by other means”.

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Which are the main differences between the III and IV Directive and how the concept of beneficial owner is finally changed?

Firstly, the IV Directive, transposed in Italy through the Law Decree no. 90 of May 5th 2017, extends the notion of beneficial owner for anti-money laundering purposes also to the settlor, the protector or the trustee; whereas the Directive 2005/60/EC did not include those subjects, unless they exercised control over the trust asset.

Secondly, the relevant threshold, for anti-money laundering purposes, for the beneficial owner of a trust disappears. Indeed, the concept of beneficial owner provided by the Directive 2005/60/EC requires the beneficiary to be entitled to 25% of the asset of the Trust, while this limit does not appear in the notion of beneficial owner provided for by the IV Directive.

Finally, while the Directive 2005/60/EC mentions clearly different alternative categories of beneficial owners (e.g. who are entitled to more than 25% of the capital of the trust and, in the lack of any of them, beneficial owners are deemed to be the class of persons in whose main interests the Trust is set up or operates), with the IV Directive the concept of beneficial owner could be extended to one or more persons: e.g. the settlor and/or the trustee and/or a beneficiary.

On the basis of the above, according to the recent amendments to the anti-money laundering regulation, also the Italian tax monitoring obligations have been changed.

Indeed, article 4 of the Law Decree no. 167 of June 28th 1990, converted by the Law no. 227 of August 4th 1990 and concerning the Italian tax monitoring obligations, provides that individuals, companies and non-commercial entities who hold foreign investments or foreign financial assets must complete the RW Form on their Italian tax return, declaring the value of the asset held abroad.
As already well-known, following the Law no. 97 of August 6th 2013 (so called 2013 European Law) the obligation to indicate financial assets held abroad has been extended also to the actual beneficial owner.

For that purpose, in order to identify the beneficial owner, the Italian tax law refers directly to the notion provided by the anti-money laundering regulation.

With specific reference to trusts, in fact, the Italian Revenue clarifies that the actual beneficial owner, in accordance with the anti-money laundering rules, shall be: (I) if the future beneficiaries have already been determined (vested), the natural person or natural persons receiving 25% or more of the trust’s fund; (II) if the beneficiaries have not been determined yet, the category of people in whose principal interest the trust is set up or operates (although, as specified in Circular no. 38/E of 2013, for trust purposes such rule shall not be applied); or (III) the natural person or natural persons exercising control over 25% or more of the trust’s fund.

Therefore, since the Italian monitoring obligation rules (as stated by the abovementioned article 4 of the Law no. 167/1990) refer to the notion of beneficial owner provided by the anti-money laundering regulation, all the changes made by the IV European Directive are relevant in Italy also for tax purposes and tax monitoring obligations. Consequently, for instance, whether the settlor of a trust qualifies as an Italian tax resident, he/she has to report in his Italian tax return also the trust’s assets.

6. The Register of information on beneficial owners

One of the most important novelties introduced by the IV Directive regarding the anti-money laundering regulation is the introduction of a new mandatory Register containing all the information on the actual ownership of corporations and legal entities, such as for example trusts and foundations.
More precisely, a special section of the Italian Companies’ Register will be the instrument for collecting and storing the information related the beneficial owners of the legal entities or trusts.

The omission of the beneficial owner disclosure is punishable by a fine which goes from a minimum of 103 euro up to 1,032 euro.

The introduction of the Register shall be related to the request of transparency on the beneficial owners of the legal entities or corporate vehicles. Indeed, since October 2016, the Financial Action Task Force (GAFI) published a report addressed to the Finance Ministers and Central Bankers of the G20 countries, summarizing the ongoing work to improve the implementation of international standards in transparency, including the availability and exchanging of information about the beneficial owners.

GAFI's activity began in 2003 aimed at increasing the transparency for anti-money laundering purposes and anti-terrorism financing, but the work carried out has shown some weaknesses in the implementation standards.

In 2012, GAFI strengthened the rules in order to limit the use of corporate vehicles for tax advantages or for money laundering purposes. In fact, the "International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation" provide in paragraph E.24 ("Transparency and Beneficial Ownership of Legal Persons") that Countries shall:

- prevent the misuse of "legal persons" by encouraging money laundering or terrorist financing;
- ensure appropriate, accurate and timely information on the beneficial owners and ownership of "legal persons", in order to ensure timely access to the competent authorities;
• if provided, entities that are able to issue bearer shares or bearer share warrants, or which members or directors may issue, adopt specific anti-money laundering or terrorist financing measures;

• introduce measures to facilitate access to the data of beneficial owners and control by financial institutions.

In addition, paragraph E.25 ("Transparency and Beneficial Ownership of Legal Arrangements") provided that countries shall introduce measures to prevent the misuse of regulatory requirements for money laundering or the financing of terrorism. In particular, they should ensure that there is an appropriate, accurate and timely information on express trusts, including information on the settlor, the trustee and the beneficiaries, allowing timely access to the competent authority.

The most recent report, however, analyzed the abuse of some legal instruments, companies, trusts and corporate vehicles, which help to hide the actual beneficial owner of assets and focuses on the low efficacy of measures introduced by each country for the implementation of international standards.

At this regard, in order to reach the objectives aimed to the transparency and sharing of information, GAFI suggested more cooperation between itself and the Global Forum on Transparency and Exchange of Information for Tax Purposes.

Therefore, the Italian Legislator, transposing the IV Directive and according to GAFI's recommendations, introduced the new Register of the beneficial owners, aiming to share more information with anyone who needs them.
Thus, the "centralized" information in that Register must be available to: (a) the competent authorities, such as Revenue Agency, Financial Police, etc.; (b) the Financial Information Units, the so-called UIF; (c) anyone who is obliged to make due diligence on the clients.

All the other persons or legal entity should, in order to have access to the Register, demonstrate to have a legitimate interest with reference to money laundering, terrorist financing and linked presumed crimes (in which case the information that may be acquired will be limited to the date of birth, citizenship, country of residence of the actual owner as well as the nature and extent of the beneficiary interest held).

It is worth noting that, according to the new regulation, if someone is obliged to verify the beneficial owner of an entity, the information provided by the new Register does not relief the individual from the regular due diligence for anti-money laundering purposes and for the risk of terrorist financing. In these cases, he should apply all the preventive measures related to the high risk noticed.

More precisely, article 21 of the Legislative Decree no. 90 of May 25th 2017, which transposed the IV EU Directive, provides that whether trusts are considered relevant for tax purposes in Italy, they must be registered with the new Register of beneficial owner. The provision seems, thus, to exclude any obligation of registration for trusts that are non deemed to be tax relevant (so called “tax interposed”), according to the Italian tax law. It is the case of trusts whose assets are still in the hands of the settlor or are already available to the beneficiaries.

With such a strict interpretation, the relevance of the Register would be devaluated, since the Italian Tax Authority could, in any moment, challenge the trust interposition.
Moreover, whether the trust is deemed to be relevant for tax purposes also because there are tax monitoring obligations - mandatory for Italian tax residents - related to the assets held by the trust, only the trusts whose beneficial owners are tax resident in Italy should be subject to registration.

However, this matter in Italy is not straightforward, since it is necessary to verify, case by case, if the conditions required by the law in order to be considered tax resident are met: it is quite impossible to think that the person obliged to make an ordinary due diligence should verify every time all those circumstances.

Finally, more clarifications about the modalities of registration are still awaiting from the Ministry of Economic and Finance (MEF) by a Law Decree providing all the missing information.

7. *Due diligence obligations*

Article 23 of the abovementioned Legislative Decree no.90 of May 25th 2017 clarifies that, given the low risk of money laundering, which has been actually measured by the application of the ordinary procedures and risk’s preventions, all the obliged parties must identify in any cases the client, monitoring of the ongoing relationship or the professional performance provided to him/her.

According to the IV Anti-Money Laundering Directive, it has been provided also a non-exhaustive list of clues and circumstances related to the type of client, which characterizes a low risk profile.

The provision finally states that the suspect of terrorism financing or money laundering excludes the application of simplified measures of client’s due diligence.

Furthermore, article 24 provides a non-exhaustive list of clues and circumstances, related to the type of client, describing an high risk profile.

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In order to apply the enforced due diligence of a client, the obliged parties take into account at least the following factors:

- clients’s risk factors such as:
  - continuous relationships or professional services established or executed under abnormal circumstances;
  - client domiciled in high-risk geographic areas in accordance with the criteria referred below;
  - companies or any structure qualifying as tax interposed or fiscal vehicles;
  - economic activities characterized by high use of cash;
  - complex structures or type or company if compared to the nature of the business carried out;

- risk factors relating to products, services, operations or distribution channels such as:
  - services with a high degree of customization, offered to client with valuable asset;
  - products or transactions that could favor anonymity;
  - payments received by third parties without a clear relationship with the client or with his business;
  - next-generation commercial products and practices, including innovative distribution mechanisms and use of innovative and emerging technologies for new or pre-existing products;

- geographical risk factors such as those at:
  - third countries which, on the basis of independent sources such as mutual evaluations or detailed public assessment reports, are considered to lack effective prevention measures for terrorist financing and money laundering;

1 This is a non-exhaustive list
- third countries that are considered to be characterized by a high level of corruption or by other criminal activities;

- countries subject to penalties, embargo or similar measures issued by competent national and international bodies;

- Countries that are used to finance terrorism or in which terrorist organizations operate.

Another important novelty of the new regulation is the elimination of the possibility (which is provided in the former decree) that, if the client is different from a natural person, the beneficial owner does not exist at all.

More specifically, in case of a trust, as already anticipated in paragraph no. 5, the IV Directive provided that the beneficial owner should be identified with the settlor, the trustee, the protector, the beneficiaries or any other natural person exercising ultimate control over the trust (it should be noted that the beneficial owner could be different depending on the legal structure of the trust: in certain cases he/she is identified with the trustee, in other cases with the protector or the settlor). Therefore, according to the above, the Italian Legislator, through the Legislative Decree no. 231/2007, provides that the obliged parties must identify "cumulatively" as beneficial owners all settlors, trustees, fiduciaries and all beneficiaries, regardless to the control they actually have on the assets held by the trust.

It is really important, however, that – with respect of the type of beneficiary position and the rights referred to it - some interpretative adjustments will be carried out by the Legislator.

For instance, let us think about the case of a client (trust) whose economic beneficiaries are only potentially identified (the grandchildren of the settlor, not born yet) or do not know they actually are.
Or, moreover, in the case of a so called “guarantee trust”, set up with the purpose of satisfying the settlor’s creditors (which, of course, may change over the time).

It is evident that, given those assumptions, the obliged subject (professional, financial intermediary and similar entities) will be unable to make the ordinary due diligence and proper verification. But it is equally evident that he will be not responsible for the omission at all.

8. Disclosure obligations and confidentiality of the client information

It is worth underlining that one of the most relevant issue is the equilibrium between the confidentiality of the information provided by the client and the obligations imposed by the anti-money laundering legislation.

Indeed, according to the principle of the risk-based approach, it is up to the obliged subjects or individuals to identify the most appropriate procedure and solutions to balance the requirements of information with those of confidentiality.

However, it should be paid more attention to the structures and vehicles which are extremely suitable to shield the actual ownership, such as trusts or fiduciaries, or particularly complex corporate structures, especially if located in high risk countries or black list countries.