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The 5th Money Laundering Directive and its implications for the “transparency register” in Germany

must be transposed into national law by the Member States by 10 January 2020

Although the provisions of the “Fourth Money Laundering Directive” had not yet been transposed into national law in all Member States by the deadline for transposition on 26 June 2017, the “5th Money Laundering Directive” (EU Directive 2018/843), which amends and tightens up the earlier directive (EU Directive 2015/849), nonetheless came into force on 9 July 2018. This must be transposed into national law by the Member States by 10 January 2020. This will, in particular, involve tightening up the regulations relating to national transparency registers.

further tightening up of the law

In Germany, the transparency register for the identification of the beneficial owners of corporations, in particular legal persons but also of trusts and foundations, has been implemented in national law in sections 18 et seq. of the Money Laundering Act (GwG) on the basis of the “Fourth Money Laundering Directive” (EU 2015/849). The “5th Money Laundering Directive (MLD 5), which is a consequence of the Panama Papers and the terrorist attacks in Paris and Brussels, will lead to a further tightening up of the law, particularly with regard to the transparency register.

“beneficial owners” = natural person

Under the Directive, the “beneficial owners” of companies who must be identified and information about whom must be held in the central register are all natural persons who ultimately own or control a legal entity through direct or indirect ownership of a sufficient percentage of the shares or voting rights or through control via other means; a shareholding or ownership interest of more than 25% is deemed to be an (irrefutable) indication of beneficial ownership.

EU-wide network of existing national transparency registers

Article 30 X/Article 31 IX of MLD 5 prescribes an EU-wide network of existing national transparency registers. This network will take the form of the European Transparency Register which is legally established in EU Directive 2017/1132.

to inspect the transparency register will in the future be possible for all members of the public

MLD 5 will significantly extend the rights to inspect the transparency register. Where it was previously necessary to state a legitimate interest in inspecting the transparency register in Germany, and only certain public authorities such as tax and criminal prosecution authorities were able to inspect the transparency register, it will in the future be possible for all members of the public to inspect the transparency register; lawmakers hope that, in the light of publications relating to the Panama Papers, this will provide for greater public control through the press and organisations such as NGOs.

Identification and/or reporting obligation

Obliged entities which are required to fulfil identification and/or reporting duties as part of their general due diligence requirements at the outset of any new business relationship are now required under Article 14 of MLD 5 to inspect the transparency register to identify beneficial owners if they are not able to identify them from other sources, such as the commercial register.

Scope of the additional reporting obligation not yet clarified

Where discrepancies are found between the information provided to the obliged entity by, say, the subject and the information in the transparency register, the entity which is obliged to inspect will be required to report this to the transparency register in the future. However, the extent of this additional reporting duty is not yet clear, and in particular whether reports only have to be made to the national transparency register in the obliged entity’s own country or whether such reports must also be made to the transparency registers in other EU Member States.

NEW: Reporting obligation for trusts

The reporting duties of trusts will also be tightened up in the future, regardless of the national laws and regulations on which such legal arrangements are based, as certain kinds of trusts had not been recorded and controlled anywhere in the EU in the past. Under Article 31 IIIa of MLD 5, the reporting duties must in the future be fulfilled in the country in which the administrator or beneficiary of the trust is domiciled.

Further significant tightening

MLD 5 not only impacts the transparency register, it also tightens up the law substantially in other areas as well. It will also be possible in the future to retrieve bank accounts and their holders centrally. Anonymous safety deposit boxes will be prohibited.

The group of PEPs (politically exposed persons), to whom tough identification duties apply, will be expanded considerably. The same applies to identification duties in connection with third countries subject to an especially high risk of money laundering and terrorist activities, to mention just a few of the changes which MLD 5 will introduce in the future.

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New legal framework for prospectuses

As a key element in the "capital market union" some parts of the new EU Prospectus Regulation came into force in July 2017; the remaining elements will only become legally binding during the course of this year.

Prospectuses for financial securities must be drawn up both as part of the process of making public offerings and for the admission of securities to a regulated market. As well as providing equivalent investor protection the aim is to reduce the administrative burden and costs involved in producing prospectuses for small and medium-sized enterprises (SMEs) in particular as well as for issuers of secondary issuances and frequent issuers.

Exemption thresholds for prospectuses

The exemptions in Articles 1 and 3 of the Prospectus Regulation were expanded and fully transposed into German law with effect from July 2018.
Public offerings with a price totalling less than EUR 100,000 or less than EUR 500,000,000 for public offerings by CRR credit institutions and issuers whose shares are already admitted to trading on an organised market remain exempt from the obligation to publish a prospectus.

A further threshold applies to public offerings for which the total consideration exceeds EUR 1,000,000 but is less than EUR 8,000,000. Offerings such as these may only be made to non-qualified investors by way of investment advice or investment brokerage by an undertaking providing investment services. The undertaking providing investment services must check certain thresholds for single investments for non-qualified investors (non-qualified investors up to EUR 1,000 or up to EUR 10,000, if the investor holds a bank balance or financial instruments of at least EUR 100,000 or if the amount invested does not exceed twice the person's average monthly net income).

In addition, there is no obligation to issue a prospectus for public offerings of up to EUR 8,000,000 if the issuer has obtained approval of a capital investments information sheet (WpIB) from the Federal Financial Supervisory Authority (BaFin).
The public offering may only be made in a Member State which has transposed the thresholds into national law. The European Passport, which allows cross-border offers to be made on the basis of an approved prospectus, is to this extent not valid.
The exemption for the issue of shares of the same class has also been increased from 10% to 20%. It is important to note in this respect that the subscription right under the German Stock Corporation Act may, under certain circumstances, only be excluded for capital increases of up to 10%.

The applicable thresholds can be summarised as follows:

EUR 100,000	Maximum limit for offers of securities to the public without obligation to issue a prospectus and without WpIB
EUR 1,000,000	Maximum limit for offers of securities to the public without obligation to issue a prospectus but with WpIB and without obligation to perform subject to thresholds for single investments for non-qualified investors
EUR 5,000,000	Maximum limit for offers of securities to the public without obligation to issue a prospectus and without WpIB for CRR credit institutions and issuers whose shares are already admitted to trading on an organised market
EUR 8,000,000	Maximum limit for offers to the public without obligation to issue a prospectus and with WpIB

Streamlined summary

The form and content of the prospectus summary should be much briefer and more clearly communicated in the future.

The summary contents are based on the key information document (KID) in compliance with the key PRIIP Regulation (Packaged Retail and Insurance-based Investment Products Regulation) which came into force on 1 January 2018. The maximum number of pages in the summary has been reduced from its current 15 to 7 DIN A4 pages, which will present quite a challenge in practice. At the same time, the Prospectus regulation provides for various simplifications which may make the summary longer in some cases (if for example guarantors need to be described or the key information document is used). The risk factors relating to the issuer, the securities and any guarantors which must be included in the summary must be limited to a maximum of 15 of the more substantial risk factors. Sub-sections should be given a heading in question form.

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Weighted categorisation oft he risk factors

Existing practice with to some extent excessively long catalogues of risk factors should be streamlined in the future. Issuers use this to reduce the liability risks as far as possible, which ultimately results in highly abstract risks being described as well. In the future, prospectuses must not be overloaded with risk factors which may effectively conceal the specific risk factors which really are relevant for the investor.
Under the Prospectus Regulation, only those risk factors should be included in the future which are specific to the issuer and/or to the securities and which are material for taking an informed investment decision. The inclusion of general industry or sector risks which are not specifically related to the issuer's ordinary activities should therefore be superfluous in the future. The risk factors must be subdivided into a limited number of categories within which the most material risks are presented based on the probability of their occurrence and the expected magnitude of the negative impact. Every risk must be adequately described with an explanation of how it may affect the issuer or securities being offered. Each risk can be categorised using a qualitative scale of low, medium or high.

Tap issues

After obtaining approval of an optional "universal registration document" an issuer may receive the status of a frequent issuer and then benefit from a faster approval process. The registration document describes the issuer's organisation, business, financial position, earnings and prospects, governance and shareholding structure. The approval periods for registration documents are reduced from 10 to just 5 working days. The issuer must submit the universal registration document to the competent supervisory authority every year for approval. After two consecutive years, the issuer only needs to file the universal registration document with the supervisory authority from the third year on and no longer needs to obtain approval. The original condition comes back into force, however if a universal registration document is not filed in one financial year.

Secondary issuances

Companies whose securities have been admitted to trading on an organised market or SME growth market within the last 18 months may benefit when making secondary issuances from simplified admission and/or public-offer prospectus requirements. An SME growth market is a multilateral trading facility (MTF) which is registered with the home competent authority in compliance with Article 33 of Directive 2014/65/EU (MiFID II) as an SME growth market.
The scope of application includes the issuance of securities which can be traded with previously admitted securities as well as the issuance of non-equity securities by issuers whose equity securities (and shares in particular) have already been admitted. The simplified prospectus consists of a summary, a specific registration document and a specific securities note.

In contrast to previous practice in which a comprehensive disclosure of the assets and liabilities, profits and losses, financial position and prospects of the issuer was made, it will be sufficient for future secondary issues to describe the prospects of the issuer and the significant changes in the business and the financial position since the end of the last financial year. The period of historical financial information is limited to the annual and half-yearly financial information published over the twelve (12) months prior to the approval of the prospectus. In the future, the information for secondary issues will be abridged to such an extent that prospectuses may be much shorter.

EU growth prospectus for SMEs

The newly introduced format for the EU growth prospectus makes life easier for SMEs. The EU growth prospectus should be much shorter and consist of a special summary of issuers and description of securities. The EU growth prospectus is relevant for the following group of companies:

a. Companies which have an average market capitalisation of less than EUR 200,000,000 within the meaning of Article 4(1) 13 of Directive 2014/65/EU (MiFID II).
b. SMEs within the meaning of the Prospectus Regulation, i.e. companies, which, according to their last annual or consolidated accounts, meet at least two of the following three criteria: An average number of employees during the financial year of less than 250, a total balance sheet not exceeding EUR 43,000,000 and an annual net turnover not exceeding EUR 50,000,000.
c. Companies which have an average market capitalisation of not more than EUR 500,000,000, which are not SMEs and whose securities are or are intended to be traded on an EU growth market.

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Security issuances of a total volume of less than EUR 20,000,000 can also benefit from the simplifications if the issuer's securities are traded on an MTF and if fewer than 500 employees were employed in the previous financial year.

Conclusion

The new Prospectus Regulation provides clarity and simplifications for issuers. This enhances trust in the capital market as prospectuses will be easier for consumers to understand in the future and will also relieve issuers of excessive costs.
The increase in exemptions from the obligation to issue a prospectus as well as the simplifications for the drawing up of prospectuses for secondary and tap issues by security issuers are also welcome. It remains to be seen whether regional stock exchanges and over-the-counter markets will make use of the opportunities which SME growth markets offer.
Whether these simplifications are retained or are restricted again by lawmakers for the purpose of protecting investors is not as yet apparent. On 18 February 2019, the German government submitted draft legislation on the further development of the EU Prospectus Regulation and the amendment of financial market laws. This will involve a major amendment to the Securities Prospectus Act. The rules on prospectus liability and liability for capital investments information sheets will be largely retained. The exceptions from the obligation to provide a prospectus introduced on 21 July 2018 will remain in place. The aim is to achieve consistency in the thresholds for offers for which prospectuses do not have to be produced.

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