13: Private Equity

Note: This sectoral guidance is incomplete on its own. It must be read in conjunction with the main guidance set out in Part I of the Guidance.

Overview of the sector

13.1 Private equity firms in the UK are subject to the ML Regulations as they are generally "financial institutions" within the meaning of the ML Regulations.

13.2 For the purposes of this guidance, private equity means a form of equity investment into companies and encompasses areas of fundraising and transactional activity:

- **Fundraising**: Marketing and raising private equity funds. Capital is raised from a variety of investors (see paragraph 13.7) who can commit large sums of money for long periods of time.

- **Transactions**: Entering into private equity transactions. This involves:

  - Investing the capital raised in private equity funds and/or proprietary capital, by providing long term finance to a range of businesses, from early stage companies to large established corporate groups. Capital is usually invested in private companies but may be used to buy out (take private) public companies whose equity is subsequently delisted;

  - Syndicating equity to co-investors;

  - Managing portfolios of investments (often involving participation on company boards as non-executive directors) and exercising negotiated shareholder rights;

  - Acquiring or selling debt instruments or derivatives;

  - Transactions by a portfolio company which will result in a realisation or return for, or a further investment being provided by, a private equity fund; and

  - Realising the investment by way of a full or partial private sale or an IPO of the portfolio company.

The rest of this sectoral guidance addresses each of the money laundering issues for both of these two distinct areas.

13.3 Investors typically invest in a private equity fund vehicle as limited partners in a limited partnership and the private equity fund is represented by a general partner. The general partner usually appoints a private equity firm either to manage (in lieu of the general partner) or advise the private equity fund. Whilst the private equity fund will enter into transactions and have rights and obligations as regards portfolio companies, the AML responsibilities may reside with either the general partner of the private equity fund or with the private equity firm. The role and authority of the private equity firm is dependent on structure of the private equity fund. References throughout this sectoral guidance to "private equity firm" should be taken to include or make reference to a private equity fund as represented by its general partner (or other similar administrator), where the AML responsibilities reside with the private equity fund.

13.4 This sectoral guidance refers to "portfolio company" throughout. This may include a corporate group as a whole, a single entity or a company at the top of a corporate group. It may also include a company or group of companies which are the target of an intended investment, but which do not yet form part of the portfolio of a private equity fund. References to "portfolio company" should be interpreted according to the circumstances.

What are the money laundering risks in private equity?

Fundraising

Product risk

13.5 Investors invest in a private equity fund for the long term and the timing of any return of capital is unpredictable. Minimum commitment sizes are usually very substantial and commitments are drawn down as required over the investment period of a fund at relatively short notice. This form of investment is also very illiquid with limited ready market. Redemptions, withdrawals and transfers of interests in a partnership can take place, but usually only after the parties have conducted detailed due diligence and usually only with the specific approval of the fund's general partner or manager (and in some funds only after a minimum initial investment period). Payments/repayments would also only tend to be made to the fund investor itself (any payment to a third party would usually only be made with the express consent of the general partner or manager of the fund and the registered investor).

13.6 For the reasons stated in paragraph 13.5 above, an investment into a private equity fund would normally be considered to be a low risk product.

Customer risk

13.7 Investors in a private equity fund are mostly institutional, such as insurance companies, pension funds of large corporates or state organisations, Sovereign Wealth Funds, other financial services companies, charitable organisations and funds of funds. Investors may also include high net worth individuals typically investing through a 'family office'.

13.8 The acceptance of investors into a private equity fund is a relatively long process with significant levels of due diligence performed by the private equity firm and a prospective investor and the final negotiation of key contracts that govern the relationship between the private equity fund and the investor. Key representatives of the prospective investor will normally meet face to face with senior executives of the private equity firm as part of this due diligence process. Investors will need to meet strict eligibility criteria to invest in private equity funds. The private equity firm has full discretion in admitting an investor to a fund and can decline a potential investor for any reason (including AML concerns).

13.9 It is not uncommon for a high proportion of investors to commit over a number of years to consecutive funds of the private equity firm; thus many investor relationships develop and continue over many years, often decades.

13.10 For the reasons set out in paragraphs 13.8 and 13.9, fund investors would generally be considered to be low risk, although certain investors may require extra consideration in any risk evaluation.

13.11 Private equity firms seeking to raise funds for the first time, or from a significantly larger or less institutional investor base, may be considering accepting funds from potentially higher risk investors, and the extent of the due diligence should be adapted accordingly.

Transactions

Product risk

13.12 The product is considered to be the provision of finance by a private equity fund that is operated, managed or advised by a private equity firm to predominantly unquoted companies. The funding can take place in a variety of ways and is usually provided for the long term after the portfolio company and its management have been subject to detailed due diligence. The private equity firm has an ongoing obligation to its investors to monitor its fund portfolio companies and will typically receive regular financial and operational information. The private equity fund will typically request the right to representation on the board of the portfolio company (this will usually be one or more of the executives from the private equity firm that manages or advises the fund but may be an external candidate chosen by the private equity firm for their relevant industry experience). The private equity fund will also typically have the right to attend portfolio company board meetings as an observer either instead of or in addition to the right to appoint a director.

13.13 The private equity fund's shareholding in a portfolio company is often highly visible and any failings on the part of the portfolio company are closely aligned to the reputation of the private equity firm.

13.14 If many of these factors are present it is considered unlikely that the provision of funding will be used for illegal purposes and therefore the product is low risk. The absence of certain of these factors, such as the absence of detailed due diligence work and/or the absence of customary investor protections, may require the private equity firm to conduct more detailed verification to satisfy itself that the financing being provided by the private equity fund is for legitimate purposes.

Customer risk

13.15 The range of portfolio companies invested in is determined by the specific parameters of the private equity fund as agreed with the fund investors. The level of regulation and standard of controls governing each portfolio company can vary considerably. The private equity firm's due diligence process should identify the risk profile of a prospective portfolio company and the private equity firm should consider its AML/CTF approach to that portfolio company accordingly.

13.16 Private equity investment is frequently provided to corporate groups whose operations span a number of different jurisdictions. The jurisdiction(s) in which a portfolio group operates may increase the money laundering risk profile, even if the parent is incorporated or registered in a well-regulated jurisdiction. A private equity firm would need to adapt its AML/CTF approach accordingly.

13.17 Likewise, the business sector(s) in which a portfolio company is engaged should be assessed from the perspective of money laundering risk. Certain sectors/businesses are more likely to be a target for money launderers than others, and the approach to due diligence should be adapted accordingly.

13.18 There will always be an obligation for a private equity firm to carry out such investigative work as it feels necessary where any circumstances exist which may lead it to suspect money laundering or terrorist financing is a risk, and the following guidance should be read in that context.

Who is the customer for AML purposes?

13.19 For AML purposes, the "customer" is considered to be a party with whom a private equity fund is transacting on an occasional basis or a party with whom a private equity fund establishes a business relationship. Although these parties are referred to as "customers" for AML purposes, they are not parties that a private equity firm would typically consider to be "customers" from a regulatory perspective. In a private equity context there are two distinct groups of AML "customers":

- **Fundraising**: Investors in private equity fund vehicles operated, managed or advised by private equity firms.
- **Transactions**: Persons transacting with a private equity fund operated, managed or advised by the private equity firm when making, managing and exiting from investments (e.g. portfolio companies, purchasers and sellers of portfolio companies and co-investors).

Customer due diligence

Fundraising

Identification of customer

13.20 In relation to each fund investor, a private equity firm should refer to the guidance for that type of investor in Part I, Chapter 5.

Identifying the beneficial owner

13.21 Where the investor is a natural person or a wholly-owned investment vehicle of a natural person, the firm should be able to identify the beneficial owner (i.e. a natural person who ultimately owns or controls an interest exceeding 25%).

13.22 Where the investor is a family office, the money will usually be provided by one or more trusts. The private equity firm should look through the investment structure to identify the relevant trusts, and verify the trusts' identities in accordance with Part I, paragraphs 5.3.246 – 5.3.269. A private equity firm may have to take a decision as to whether it can rely on a representation from the administrator of the family office (or equivalent), or the trustees, as applicable, concerning the beneficial owners, or in appropriate cases confirmation from a reputable professional services firm. The amount and type of documentation collected will vary depending upon the firm's risk-based approach.

13.23 Where the investor is a pension fund or endowment, the private equity firm must first understand the structure of the pension fund or endowment in order to determine its approach to identification. The private equity firm should identify both the source of the funding, for example the sponsoring employer, and the person who controls the investment decision, for example the trustee or an investment committee, although the exercise of investment discretion may have been delegated to a regulated firm acting as agent. In identifying the beneficial owner, there is likely to be an identified class of beneficiaries, in which case it is unlikely that any one individual will have an entitlement to more than 25% of the property.

13.24 The guidance in paragraphs 13.47 to 13.52 is relevant for customer due diligence relating to investing corporates.

13.25 It may be more complicated to identify a beneficial owner where the investor is itself a fund vehicle, for example a private equity fund of funds. The guidance in paragraphs 13.53 to 13.64 is relevant for customer due diligence relating to investing funds.

Timing of customer due diligence

13.26 Identification checks in respect of investors in a fund should be completed and the private equity firm satisfied as to the source of funds before any unconditional contractual commitment to accept the investor into the fund is made. Where there is any assignment of an interest in a fund, any identification checks should be completed before the assignment is approved and executed.

Transactions

13.27 There are a number of parties involved in a private equity transaction, and the level of identification required in respect of each will vary, depending on the type of transaction, the nature of the party and their role in the transaction and how well they may already be known to the private equity firm.

New investments

13.28 On a new investment a private equity firm should consider applying customer due diligence measures, adopting a risk-based approach, to the following counterparties (each of which is explained in further detail below):

- the portfolio company;
- directors of the portfolio company (see paragraph 13.34);
- potentially, any new company formed for the purposes of making the investment;
- any party who is selling shares to either the private equity fund or a new company formed for making the investment; and
- potentially, a party making a co-investment alongside the private equity fund.

- *Portfolio companies*

13.29 Where the investment is provided directly to a company, customer due diligence in accordance with Part I, Section 5.3.131 onwards should be applied to that portfolio company.

13.30 Beneficial owners of the portfolio company must be identified and the private equity firm must take risk-based measures to verify their identity. These are often the same parties identified as part of the customer due diligence undertaken on the sellers where the private equity investment is being used to fund an exit by existing shareholders.

13.31 One or more new special purpose vehicles (“newcos”) may be used for the purposes of the transaction. This means that the private equity firm or its funds may only enter into a direct transaction with a newco and not the portfolio company. Nevertheless, the investment funds will ultimately be flowing down to the portfolio company in linked transactions so there must be a clear understanding of the underlying beneficial ownership or recipient of the funds and the flow of financing. For this reason, customer due diligence should be conducted on the portfolio company to be acquired by a newco. See paragraphs 13.35 and 13.36 for guidance on the customer due diligence requirements in relation to newcos.

13.32 Where the investment is provided to a corporate group (whether directly or indirectly through one or more newcos), customer due diligence should be applied to the top entity within the corporate group that is being acquired or that is receiving the private equity investment, as it existed prior to imposition of any newcos. Where the corporate group receiving the investment is being ‘carved out’ from a larger corporate group, customer due diligence should be applied to the top company of the grouping being carved out, prior to the imposition of any newcos.

13.33 A private equity firm must consider and understand the ownership and control structure of the portfolio group as a whole.

- *Directors*

13.34 The private equity firm will identify all board directors of the portfolio company by obtaining the standard evidence for a corporate in accordance with Part I, paragraph 5.3.138. The private equity firm should consider whether to verify the identity of one or more directors in accordance with Part I, paragraph 5.3.155.

- *Newcos*

13.35 One or more newcos may be used for the purposes of the transaction, either to acquire the target portfolio group or for the purposes of efficient tax structuring. Newcos are typically formed by the private equity firm or professional advisers representing any of the private equity firm, a lead co-investor or investing management. The initial directors and shareholders of such newcos will usually be connected to the private equity firm or the professional adviser and will be changed before or at signing. Assuming this to be the case, where any newco has not previously traded and was formed in anticipation of a transaction, there should be no reason to carry out formal customer due diligence on any newco. The jurisdiction of the newco may carry a higher risk profile, but provided that the newco has been properly established and that the reason for the selection of jurisdiction is understood and appropriate, that of itself should not give rise to the need to obtain additional verification. Where any newco does not meet these criteria, customer due diligence measures may be appropriate according to a private equity firm’s assessment of the risks.

13.36 Where the transaction introduces a chain of newcos, it should only be necessary to consider customer due diligence (if any, as per paragraph 13.35 above) with respect to the top newco in the proposed corporate structure, into which the private equity firm or its funds is investing, assuming that the newcos below will all be wholly-owned by the top newco and that all directors are representatives of the private equity firm or co-investors or are known from within the portfolio group or will be changed before or at signing to such directors.

- *Sellers*

13.37 The decision to invest by the private equity firm may be used to fund an exit by existing shareholders, resulting in one or more individuals or entities benefiting financially.

13.38 Sellers of a portfolio company will be customers of the private equity fund for AML purposes where they are transacting directly with the private equity fund. A private equity firm should identify all sellers and adopt a risk-based approach to verifying the identity of sellers (and any beneficial owners), according to the firm’s assessment of the money laundering risk presented by each seller. Even if the placement of newcos in the structure means that there is no direct transaction between the private equity fund and any sellers, the private equity firm should conduct customer due diligence on the sellers given that all or part of the benefit of the private equity investment is flowing to them. The nature of the due diligence work performed is such that the origins of the business will have been the subject of extensive review and investigation.

13.39 The guidance in paragraphs 13.47 to 13.52 is relevant for customer due diligence relating to selling corporates.

13.40 The guidance in paragraphs 13.53 to 13.64 is relevant for customer due diligence relating to selling funds.

- *Co-investors*

13.41 Private equity transactions can involve a variety of co-investors. These might include other private equity funds, institutional investors (who may also be invested in the private equity fund alongside which they are co-investing), incoming directors or managers, or existing founders / managers / employees of a business who are continuing (or 'rolling over') their investment in a portfolio company or being provided with a new opportunity to co-invest. Depending on the circumstances, a private equity firm should consider whether to identify co-investors, particularly in the following circumstances:

- Where the private equity fund acts as lead investor in the round of financing where it has arranged a co-investor's involvement in the deal, and where the co-investor is formally relying on the private equity fund, as can be the case in venture financing rounds or club deals; or

- Where a co-investor is taking a significant stake (more than 25%) of the portfolio investment, alongside the private equity fund; or

- When a co-investor is an individual and is or will be a board director of the portfolio company.

13.42 A private equity firm should adopt a risk-based approach to verifying a co-investor's identity according to the firm's assessment of the money laundering risk presented by a co-investor. The guidance in paragraphs 13.53 to 13.64 is relevant for customer due diligence relating to co-investing funds.

Further investments

13.43 On a further or follow-on investment in a portfolio company, a private equity firm should consider whether its ongoing monitoring of the portfolio company (see paragraph 13.73 onwards) has been sufficient for AML purposes or whether it would be appropriate to update its customer due diligence on the portfolio company. It should not be necessary to re-verify or obtain current documentation unless the identification data held is not adequate for the risk of the business relationship or there are doubts about the veracity of the information already held. The same considerations apply to any co-investors also making a further investment or new commitment.

Timing

13.44 Customer due diligence checks should generally be completed when it is reasonably certain that the new or further investment will go ahead, and in all cases before the private equity fund becomes unconditionally legally obliged to complete the investment.

Realisations

13.45 When realising an investment in a portfolio company (either fully or partially) the private equity firm should consider applying customer due diligence measures, adopting a risk-based approach and depending on the nature of the exit as follows:

- On a private sale, the purchaser of the portfolio company;
- On an IPO, the lead underwriters in the underwriting agreement;
- On a buy back, either on the purchasing managers or the portfolio company itself depending on who is buying back the shares.

- *Purchasers*

13.46 The pressures of achieving a timely and successful exit may heighten the risk of limiting the amount of due diligence performed on any potential purchaser on exit. In these circumstances the private equity firm needs to ensure that its controls for proper verification of identity and establishing source of funding remain robust.

- *Transacting with corporates*

13.47 Where the purchaser is a corporate entity the private equity firm should apply customer due diligence measures in accordance with Part I, Section 5.3.131 onwards.

13.48 Where a purchaser establishes a newco to make the acquisition, customer due diligence should identify those directors and beneficial owners who will ultimately own and control newco when the transaction completes, rather those who formed newco. If ownership of newco will change between signing and closing, a private equity firm may need to identify those in place at signing as well as closing.

13.49 In a corporate structure, beneficial ownership may be exercised through a direct holding or through several intermediate investment vehicles. A private equity firm must understand the ownership and control of the corporate structure to which the purchaser belongs and identify the names of all individual beneficial owners, even where these interests are held indirectly, whether through one or multiple vehicles. Enquiries should continue up the chain of ownership until either a natural person who owns or controls in excess of 25% of the purchaser is encountered or it is established that no such individual exists (for example, as may be the case with a company whose ultimate parent is listed on a regulated market).

13.50 Beneficial ownership should be considered on a look-through basis. If one individual appears in several different places within a corporate structure, that individual may have effective beneficial ownership or control of more than 25% of the purchaser as a consequence of the aggregated holdings. Conversely, an individual owning or controlling more than 25% of a company at the top of a corporate structure is not necessarily a beneficial owner of the transacting purchaser if he does not have effective control or ownership of more than 25% of the transacting purchaser because of the dilutive effect of intermediate companies which are not wholly-owned e.g. Individual A who owns/controls 30% of Company B (which in turn owns/controls 40% of Company C) is not necessarily a beneficial owner of Company C as Individual A's effective ownership/control of Company C is diluted to 12% (i.e. 30% of 40%).

13.51 If there is no natural individual owning or controlling more than 25% of a corporate structure, the private equity firm should consider whether an individual owning or controlling a lower percentage exercises effective control (either alone or acting together with other connected individuals).

13.52 Where there is a series of corporates in the ownership chain, which ultimately ends with a beneficial owner, the private equity firm must take risk-based and adequate measures to verify the identity of any such beneficial owner. There is no need to verify the identity of all entities in the intermediate ownership layers, although the private equity firm should retain suitable evidence of all intermediate ownership layers and relevant ownership percentages.

- *Transacting with funds*

13.53 It is reasonably common to encounter private equity (or similar) funds as counterparties in private equity transactions.

13.54 In the UK, fund vehicles are typically formed as limited partnerships. Limited partnerships are registered at Companies House and have a registration number and a registered address. In other jurisdictions, funds may be in the form of partnerships or corporate vehicles. Funds will normally have a general partner or a manager who exercises discretion over the assets of the fund. In these paragraphs "Fund Manager" refers to this entity/person, regardless of form or title.

13.55 A private equity firm must conduct customer due diligence on a fund, as set out in Part I, Chapter 5 according to the form of the fund vehicle. This may be achieved, subject to the considerations outlined below, by way of reliance on representations from its Fund Manager (see paragraphs 13.58 to 13.64).

13.56 Customer due diligence, whether by way of reliance on representations or directly obtaining standard evidence, must identify the names of all purchasing funds and their beneficial owners. Part of identifying beneficial owners will be to establish the name of the Fund Manager given its ability to control the fund assets. A private equity firm will also need to identify and take risk-based measures to verify any natural person who owns or controls an interest in excess of 25% of the fund.

13.57 If a private equity firm conducts customer due diligence directly (either instead of or to supplement a Fund Manager's representations) it may obtain other items of standard evidence, for example basic constitutional or incorporation documents in relation to the fund vehicle and its Fund Manager and evidence of the Fund Manager's regulated status (if relevant).

13.58 A private equity firm may accept representations from the Fund Manager (whether or not the Fund Manager is regulated or supervised, but see paragraphs 13.59 – 13.61 below) to fulfil its customer due diligence requirements as regards the identity of the funds, its Fund Manager and the Fund Manager's regulated status and to establish whether or not there are any investors in the fund that are beneficial owners. Funds are often widely held and it may be the case that no investor is a beneficial owner i.e. a natural person who owns or controls an interest in excess of 25% of the fund.

13.59 Where a fund does have beneficial owners who must be identified and whose identity should be verified, there will often be legitimate confidentiality concerns on the part of the Fund Manager with respect to investors in the fund. A private equity firm must take a risk-based approach to verifying identity. A private equity firm may consider it appropriate, depending on its knowledge and assessment of the Fund Manager, to rely on a representation from the Fund Manager that it has verified a beneficial owner's identity and will retain documentary evidence and provide it on request.

13.60 Where the Fund Manager is regulated and subject to supervision in the UK, the EU or an equivalent jurisdiction, it will be subject to the requirements of the ML Regulations or equivalent in the respective jurisdiction and a private equity firm is entitled to rely on such a Fund Manager's representation relating to verification of identity of beneficial owners. This representation may take the form of a letter or similar from the Fund Manager as outlined below.

13.61 Where the Fund Manager is not in the UK, the EU or an equivalent jurisdiction (even though it may be regulated), or where the Fund Manager operates in an equivalent jurisdiction but is unregulated, the private equity firm needs to exercise its judgement as to the likely risk presented by investors in the fund. Factors to take into consideration include:

- the profile of the Fund Manager in the market place;
- its track record in the private equity industry; and
- its willingness to explain its identification procedures and provide confirmation that all underlying investors in the fund have been identified and are known to the Fund Manager.

The private equity firm should ask what customer due diligence enquiries have been undertaken on fund investors and be satisfied that it has been conducted to a standard compatible with the ML Regulations, taking into account the ability to use different sources of verification and jurisdictional specific factors.

13.62 Notwithstanding a private equity firm's acceptance of Fund Manager representations, the private equity firm will remain liable for non-compliance and it may not always be appropriate to rely on another Fund Manager to undertake its customer due diligence checks.

13.63 Representations from a Fund Manager should confirm the name and jurisdiction of the fund, that the Fund Manager acts as the manager for the fund, whether or not the Fund Manager is regulated, the nature of the due diligence the Fund Manager has carried out on the fund investors and whether there is any natural person owning or controlling an interest in excess of 25% of the fund.

13.64 Possible examples of the representations referred to in paragraph 13.63 are set out below.

Example of representation provided by a Fund Manager

"We [*name of firm*] [regulated by [*name of regulator and firm reference number if any*]] confirm the following in respect of [*name of fund vehicle(s)*] (the "Fund(s)"), established in [*fund jurisdiction(s)*] for whom we act as manager/general partner.

1. [In accordance with the laws of our jurisdiction, and the procedures under which we operate, designed to combat money laundering] we confirm that:

   - we have identified the underlying beneficial owners in respect of the Fund(s) and carried out customer due diligence on all of the investors in the Fund(s);
   - we confirm that to our actual knowledge [(having made reasonable enquiries)] there are no undisclosed or anonymous principals; and
   - we are not aware of any activities on the part of those investors which lead us to suspect that the investor is or has been involved in money laundering or other criminal conduct.

2. To our actual knowledge [(having made reasonable enquiries)] there is no natural person who owns or controls an interest exceeding 25% of any of the Fund(s).

3. We will retain, until further notice, all documentation required to identify the underlying beneficial investors in the Fund(s) [and which we have obtained for the purposes of our due diligence]. We will provide such documentation to you/to your Compliance Officer/direct to any regulatory authority on request/where you are required to disclose it to such regulatory authority."

- *Buy backs*

13.65 If the sale is to a member of existing management on whom customer due diligence was conducted at the outset or during the life of the investment and who has been known to the private equity firm in the context of the investment concerned (or of another investment), the private equity firm should consider the relevance of carrying out further customer due diligence given its existing relationship with, and knowledge of, the member of management concerned.

13.66 If the portfolio company is funding the buyback, the company is the purchaser and the private equity firm should consider its existing relationship with the company and whether it has up to date knowledge of the portfolio company through its existing monitoring processes, in deciding whether it is necessary to refresh its customer due diligence.

- *IPOs*

13.67 On an IPO, where the private equity fund is able to sell some of its shares in the portfolio company, the private equity fund will typically be transacting with one or more lead underwriters. The private equity firm need not be concerned with sub-underwriters unless the contractual arrangements provide for the private equity fund to sell directly to them. The private equity firm should undertake customer due diligence on any lead underwriter. Since it will be a regulated firm, the private equity firm will be able to apply simplified due diligence where it is in the UK, the EU or an equivalent jurisdiction. Whether acting as agent or principal for the private equity fund in selling the shares, the lead underwriter will be subject to AML rules and will either sell the shares on a regulated market or through another broker, so the private equity firm need not concern itself with identifying the ultimate purchasers of the shares. The private equity firm would expect to see some acknowledgement of the lead underwriter's compliance with relevant AML rules in the underwriting agreement.

13.68 Where a private equity fund does not sell at the time of the IPO, there is no transaction or customer for AML purposes. Any later sale will trigger customer due diligence requirements although this will frequently be transacted through a regulated broker, where similar considerations to those in paragraph 13.67 will be relevant.

Timing

13.69 Identification checks should generally be completed on the relevant parties as soon as practicable when a deal looks reasonably likely to proceed and in all cases before the private equity fund becomes unconditionally legally obliged to complete the sale.

Other issues

Representations issued by private equity firms to third parties

13.70 A private equity firm should be prepared to confirm whether in their actual knowledge there is any natural person who owns or controls an interest exceeding 25% of a private equity fund for which they have AML responsibilities. When disclosing information about investors in accordance with relevant confidentiality provisions, private equity firms should consider agreeing to disclose the information to a certain department within the third party, such as the Compliance Officer, only. Such confirmations might be required by another party transacting with the private equity fund or, more commonly, by a bank funding a portfolio company that is conducting or refreshing its own customer due diligence on the portfolio company's beneficial owners.

Use of verification carried out by others

13.71 Private equity firms make extensive use of professional advisers, especially where the required knowledge does not exist in the private equity firm itself. A portfolio company and any co-investors will usually appoint professional advisers to ensure that their own interests are represented in any negotiation. In some cases, these advisers are themselves under an obligation under the ML Regulations, or under similar legislation in the EU or in an equivalent jurisdiction, to carry out customer due diligence on their clients. Depending on the circumstances, and the private equity firm's knowledge of/relationship with the portfolio company, the private equity firm may consider it appropriate to take account of information or written assurances provided to the private equity firm by these third parties, as part of the overall risk-based approach.

13.72 The requirement to appear before a notary in certain jurisdictions when signing documents such as the sale and purchase agreement or shareholders' agreement can provide adequate verification. However the notary's certificate should only be considered as adequate if it states the full names and identity card numbers (or equivalent) of the individuals appearing before the notary, plus details of the evidence provided for their authority to act as representatives of the parties involved.

Monitoring

13.73 A private equity firm must conduct ongoing monitoring of "customers" (for AML purposes) with whom it establishes business relationships. Although a private equity firm may carry out customer due diligence on a wide variety of parties in the course of transactions, many of these are as a result of occasional transactions rather than any intention to establish a business relationship for AML purposes. In an AML context, private equity firms usually establish business relationships with fund investors and portfolio companies. Although private equity firms may make multiple investments alongside the same co-investors, the contractual nature of the arrangements between co-investors are bespoke for each investment and the relationship is not one for which a private equity firm is generally expected to conduct ongoing monitoring.

13.74 The extent of the ongoing monitoring must be determined on a risk sensitive basis but a private equity firm should bear in mind that as the business relationship develops, the risk of money laundering may change. It should not be necessary to re-verify or obtain current documentation unless the identification data held is not adequate for the risk of the business relationship or there are doubts about the veracity of the information already held, for example, where there is a material change in the risk profile of the customer.

Fundraising

13.75 Investors in private equity funds tend to have long established relationships with the private equity firm, normally resulting in a well-known investor base.

13.76 Private equity firms will have regular one-on-one meetings with representatives of their fund investors or may organise investor conferences to update them on the performance of their funds. The private equity firm will typically provide regular written reports to fund investors on the performance of a fund and its portfolio.

13.77 Fund investors regularly submit questionnaires to private equity funds asking them to confirm compliance with the fund's organisational documents and various aspects of the fund management policies and procedures and their house investment approach.

13.78 These activities are indicative of continuing dialogue and communication and should be considered sufficient ongoing monitoring of the relationship for AML purposes.

Transactions

13.79 Prior to making any investment in a business, the private equity firm will conduct extensive due diligence on the business and its owners, identifying areas of risk, including money laundering considerations. Once invested, ongoing monitoring of the investment through board participation and regular involvement allows the private equity firm to assess whether the portfolio company's activities are consistent with its financial performance, and also enables the private equity firm to observe the conduct of the key managers of the business at first hand. In connection with portfolio companies, this will satisfy a private equity firm's obligation to conduct ongoing monitoring of the business relationship for AML purposes.