

Ownership transparency's implications on sustainable development goals

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Abstract

This paper explores possible implications the implementation of beneficial ownership transparency requirements could have on the achievement of specific sustainable development goals, among others through their role in corporate disclosure and tax transparency.

Slovenia is one of the first EU members to transpose and implement the 4th Anti-Money Laundering Directive to national legislation. National legislation even exceeds the requirements of the transposed directive. Slovenia is thus one of the few EU member states that established a public register of beneficial owners for all companies and trusts, which are registered or tax liable in the member state. Author presents the Slovenian register of beneficial owners and related legislation as well as the role the register can play in striving to improve corporate tax responsibility and wider corporate social responsibility.

The paper further presents the findings of interview-based survey of different stakeholders' viewpoints on the application value of the register of beneficial owners in Slovenia. The issues raised by accountants and representatives from business, public administration and civil society give an insight into the value of the current register. Although the vast majority of affected legal entities have entered their data, a nominee director is named instead of a beneficial owner in many cases. What are the reasons and implications?

Lastly, the author of the paper discusses what needs to be done to raise public awareness and scrutiny on topics related to beneficial ownership in the framework of sustainable development.

Keywords: Ownership Transparency, Beneficial Owners, Sustainable Development Goals, Corporate Social Responsibility, Illicit financial flows, Hub for Tax Justice, Anti-Money Laundering Directive



1 Introduction

The register of beneficial owners (BO)¹ obligates the owners of legal entities to register. Experts that are subjected to due diligence by customer (DDC) use the information about BO (found in documents, registers, contracts). If the information is used for planned purposes and if the disclosures are fair, the society should benefit, as there would be less corruption, less profit from criminal offences and more tax paid in countries, where companies carry out their actual economic activity. The register of BO is one of 'ABCs' instruments to battle illicit financial flows (IFF), together with country by country reporting (CBCR) and automatic exchange of data. For persons subjected to register, the compliance costs are very small, yet the effects for the society could be enormous. However, due to loss of anonymity, banks, financial and other intermediaries might lose some of their clients to other countries to facilitate for their future IFF.

2. Role of public register of beneficial owners

2.1 Slovenia transposed the EU directive into national legislation and established a public register of beneficial owners

The fourth European Anti-money directive's (AMLD4) aim is to harmonize definitions, actions and sanctions of money laundering offences and to strengthen national disclosure requirements for BO and to establish shared registers of BO that shall be accessible to obliged entities for purposes of DDC. This should be done according to the directive, by law firms, banks and others when formatting company or entering a business relation with a company. This DDC includes actions of indentifying customer identity, identifying beneficial owner and verifying his/her identity, including legal persons, trusts, companies, and action of controlling the nature of business and transactions. Not applying this, should be sanctioned at least twice the amount of benefit. (Vail, 2018)

2

2.1.1 Slovenia leading in transposing the BO register from AMLD4

Slovenia is one of the first EU countries to establish a public register of beneficial owners. The access is free (no admission costs for users) and without restrictions (person interested in information does not have to prove that it has legitimate interest, but not all data are public). It is not in open data format. The personal data are not available (e.g. citizenship, address). The register includes all foreign trusts doing business or tax liable in Slovenia (but not applicable for domestic trusts) and legal arrangements. Slovenia uses the option that executive managers may be listed as beneficial owners². If no owner has 25%+1 share or voting rights or other control, there is no beneficial owner. When compared to other EU members, Slovenia is an example of best practice in implementation of AMLD4 in the field of BO. In other EU members, registers do not include all companies and trusts that are in any way related to country and that threaten the AMLD4 goals. The problem is that data about BO are published in different forms in different jurisdictions and it is hard to make investigation in other EU member states.

¹ Beneficial owner by FATF definition is "natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes these persons who exercise ultimate effective control over a legal person or arrangement."

² Nevertheless, it is disclosed that function of BO is senior manager.



Financial and legal professionals in Slovenia do not perfectly comply with AMLD4 requirements on DDC obligations or do not report suspicious activities (in 2015: lawyers reported only 3 suspicious activities, accountants and auditors none). Other non-financial professionals do not appear to be aware about risks of money laundering when lending money, investing or operating with non-publicly disclosed owner. People interviewed reported insufficient awareness of money laundering risks that should be addressed with identification of beneficial owners. They are not trained by governmental or public organisation for BO identification. Public authorities do not control the fulfilment of AML obligations (in 2015: 10 sanctions and other remedial actions were applied by them). And schools do not offer systematic education about prevention of money laundering (Brillaud, 2017).

Panama Papers identified 58 Slovenians, public sector employees, businesspersons and public figures using OFC to obscure their identity due to tax evasion. After the revealing, the state secretary of Ministry of Finance publicly stated that the damage of money laundering is excessive, and implementation of AMLD4 was high on agenda.³

2.1.2 The information from registration agency and business public

The experts committed to performing DDC, use data from public registers, contracts or documents, one of them is the Register of BO hosted by Agency of the Republic of Slovenia for Public Legal Records and Related Services (AJPES). If the business partner is operating only on local market and it has only obligations to local financiers and owners, the risks are lower and DDC performed is superficial (Bezljaj, 2018).

The obligation of entering the BOs in AJPES register was fulfilled in last minute. One week before the deadline all communication lines at AJPES were occupied. Most questions were about digital certificate that was needed to enter the data and about single member limited liability companies and associations⁴. Most of people interested in registers were not managers of enterprises, but their deputies. (Lubarič, 2018).

2.1.3 Owners and foreign citizenship

The main risk in the field of money laundering is doing business with persons without clear business relations in Slovenia, said the regulator, Banka Slovenije. The company for registration of enterprises DATA d.o.o. was facilitating the establishment of companies of BOs (according to the address of residency), that were operating with post address and puppet directors. DATA d.o.o. did not perform detailed DDC. However, journalists in commercial register of enterprises GVIN found 2268 companies that have at least one owner residing in Italy. Next common feature is having the same business address and Slovenian resident for a manager without business skills and qualifications. Companies made no incomes. The DATA d.o.o made superficial DDC as it trusted their clients. They were shell companies used only

³ The effect on taxation was proven in UK: Cost-benefit analysis shows that free access to public register of beneficial owners implies lower costs and higher benefits. For one UK pound invested in register the UK Treasury receive two UK pounds of additional collect taxes and other incomes.

⁴ In business register, there are also recorded business subjects that do not have equity (association (društvo), there are more then 24.000 associations, institutions or trade unions and more than 47.000 single member limited liability companies.



for IFF. The Council of Europe warned Slovenia not to give up control. Banks⁵, under public and media scrutiny, started to react and end their business relationship with these Italian companies (Kos, 2018).

The register should contain BO of business subjects that control these subjects or influence in other way on activities of these subjects. BO enters data about country of origin of BO, but this information is not public.

Table: Business subjects by citizenship of BO

Citizenship	Number of beneficial owners (BO)	Proportion of BO6
Slovenia	73.934	89,16%
Italy	1.396	1,68%
Russia	1.088	1,31%
Austria	829	1,00%
Croatia	759	0,92%
Serbia	647	0,78%
Bosnia and Herzegovina	613	0,74%
Germany	483	0,58%
Ukraine	417	0,50%
Kosovo	382	0,46%
Macedonia	292	0,35%

Source: AJPES (data from 3.8.2018)

The structure of nationality entered in BO register shows East and South east Europe's BOs. They have the following characteristics: they are non-EU citizens, they are from countries that are "reservoirs" for workers that are posted from Slovenia to Germany⁷. In the interview, an accountant that provides services to enterprises with non-EU owners assured that she implemented the legislation: to enter client as BO in register. To prove to AJPES that client has no criminal record in Slovenia and in country of his origin. To prove that her client will have the foreseen incomes on his bank account⁸.

The index of financial secrecy is composed of different components, including one related to BO transparency indicators. The financial transparency is when relevant information is publicly recorded or reported to government authorities or exchanged internationally.

⁵ 66% of Slovenians do not trust banks; the weak reputation was earned also due to IFF of foreigners.

⁶ In August 2018, about 20% of subjects did not yet enter the data in BO register. Source: Interview with employee at AJPES.

⁷ In 2015, there were around 2 million work postings in the EU. The main destination among EU countries was Germany (28% of all posted workers). In relative terms Luxembourg (24.7%) and Slovenia (14.2%) have the highest share of sent posted workers as a share of domestic employment. In 2014, 49% of posted workers from Slovenia went to Germany. On 31. 12. 2014, the top 10 nationalities of posted workers from Slovenia were: 1. BIH, 2. Slovenia, 3. Serbia, 4. Croatia, 5. Bulgaria, 6. Kosovo, 6. Hungary, 7. Macedonia, 8. Romania, 9. Slovakia, 10. Italy (Rogelja 2016). They worked mostly in construction business.

⁸ Source: An interview with a manager and BO of established middle sized accounting service on 3. 9. 2018.



OFC provide secrecy to residents of other territories. These non-residents chose OFC due to secrecy that has the effect on the exclusion of financial cash flows from supreme authority of original jurisdiction⁹. 82 countries were assessed on 15 key financial secrecy indicators¹⁰. Top ten offshore countries include USA, Luxemburg, Switzerland, Germany and Jersey. Non-residents establish shell companies, trusts, special purpose vehicles and mutual funds in these countries. (Cobham, 2015).

The shell companies from OFC can transfer large sums of money without public scrutiny. The owners create them with or without disclosing identity, using other persons as directors. These companies can often be used for tax evasion (trade mis-invoicing is specific for developing countries) or tax avoidance. In some countries, firms that facilitate the formation of shell companies are not penalized or controlled sufficiently when not properly screening potential clients. The time for establishing a shell company is very short (in Delaware, USA, one hour).

Slovenia should have good marks when appraised by criteria of disclosure of BO. However, this article can lead to conclusion that many enterprises that entered BO in AJPES register, are operating in Germany. From them Germany receives workers that are inexpensive in comparison with workers from Germany (as Slovenian social contributions are lower) and that are in deficit in labor market in Germany. The company that is established in Slovenia pays taxes and social contributions to Slovenia. There is also no secrecy (the owner is recorded in Slovenian BO register), but there is effect on the exclusion of financial cash flows from supreme authority of original jurisdiction (as social security contributions and taxes are paid in Slovenia and not in Germany). This legal situation shows that the secrecy is not needed when legislation does not prevent IFF and has characteristics of OFC.

2.2 Global effect of battle against offshore centers. How can it be measured?

Target 16.4 of UN SDG is to reduce globally IFF. They are indicated by dollar value of IFF. A part of them are capital financial flows due to tax evasion, avoidance and regulatory abuse (for example antimonopoly), the other part are from criminal activity. The indicators of financial secrecy measure exposure to risk of county. If cash flow is illicit, it is not necessarily illegal, but it is at least not custom and is not morally accepted (like profit shifting of multinationals). These immoral cash flows (commercial tax dodging using transfer prices and accounting changes in tax base) are in first place of IFF, illegal money laundering on second place. Illegal evasion and legal avoidance are part of profit shifting that is part of a broader profit misalignment (if employment, sales and investment in property, plant and equipment is not in the same country as profits are reported).

The actors who committed these IFF can come from private sector, public sector and criminal groups. IFF can be found in all these sectors – they use the same secrecy and inventiveness to legitimize their behavior. The subjects of transaction are funds (capital) – owned by legally proved (but not publicly known) owners or criminals. The change of ownership or form of

⁹ From the point of view of OFC, their strength is the quantity of financial services provided to non-residents as proportion of global financial services for non-residents that is sum of all world exports of financial services.

¹⁰ Disclosure of BO is measured with 3 indicators. Other three key financial secrecy indicators are grouped in corporate transparency efficiency of tax authority and government and international cooperation of governments in fight against IFF. There are 15 key financial secrecy indicators within four broader groups. In group 1, disclosure of BO has 3 indicators.



funds (capital) is motivated with bribery, money laundering, or only avoiding taxation in country of origin. Anonymity is used in these flows: inwards investments (to hide market dominance or political involvement – abuse of power), outward investment (to hide political involvement), to sell public asset without control, to make public contract (to avoid the control of market dominance and control of political involvement), to transfer ownership to OFC (to make corrupt payments from there). Criminal IFF are from these types of behaviour: tax evasions, bribery, theft, fraud, bankruptcy, drug trafficking, etc. Unlawful IFF are from market and regulatory abuse and unlawful tax avoidance. Legal IFF is from Tax compliance and (lawful) tax avoidance.

The indicators of IFF in existing methodologies use the estimations on the base of the capital account, trade (including import over-invoicing or export under-invoicing between unrelated parties, and trade with related parties, that lower the tax base of multinational companies at least for 10%), and offshore wealth. According to one estimate people from South America, Asia and Africa have 1.850 billion euros of wealth in OFCs, causing countries to lose 52 billion euros of tax income annually). There is around 10% of European wealth hidden in OFCs (Eurodad, 2015)).

Corporate tax avoidance estimates are made based on multinationals' balance sheets, surveys and other data. They include losses to profit shifting that is legal (differences in tax rates in countries) and the difference due to lower tax base of multinational companies.

The Tax Justice Network (TJN) relates the indicators of IFF with consequences that should be removed with these “ABC goals”: the countries automatically (A) exchange tax information between jurisdictions; beneficial (B) ownership is transparent in public registers for companies, trusts and foundations and country by country reporting (CBCR); (C) disclosures about multinational profit shifting are public. This could be used to measure the SDG 16.4.1. The indicator is a sum of results that are calculated as proportions of all of multinationals economic activity in each jurisdiction multiplied with global gross profits of all multinationals that is deducted with share of profit of all the multinational companies declared in each of jurisdiction. (Cobham, 2017)

3 Conclusions and suggestions for further research

Slovenia can by implementing EU directive and engaging all stakeholders, promoting use of BO register in private sector improve her national budget incomes and the global effect of financial transparency on achievement of SDG 16.4, which aims to “significantly reduce IFF and arms flows, strengthen recovery and return of stolen assets, and combat all forms of organized crime”.

The effect of these should be measured on the global and on the national levels. With quantifying the goals, there will be objective criteria for assessing governments' activity. In Slovenia, the public trust in businesses and institutions is low, as banks are seen as tools for money laundering. To re-gain the public trust, there should be rigid rules that are executed daily. This can also be measured.

Experts, for example accountant in interview noticed the ambiguous role of Slovenia. The level of regulation is high, but as OFC for non-EU companies posting workers to Germany Slovenia is loosening the regulation.



Slovenia started influencing the improvement of global indicators of transparency with use of public BO register. The fifth EU AMLD arrangement of register of BO is identical with Slovenian legislation (except for thrusts). In future, there should be more efforts put in policy coherence in Slovenia, as many of them influence global combat against IFF.

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