Recent progress on shell companies, trusts, beneficial ownership and CbCR

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Beneficial ownership registries

The **European Union** has played a leading role on beneficial ownership registries by adopting (in 2015) the Anti Money Laundering Directive (known as Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.) All Member States are supposed to implement this Directive within two years. While this is a great advance towards transparency compared to what is happening elsewhere, the politics were frustrating. This got close to being a real breakthrough until the UK opposed the proposed wide scope of registration of trusts; and countries led by Germany resisted the public nature of the registry (e.g. see here and here). EU countries may still decide to offer public registries for legal persons, but for now they the Directive only requires them to grant access to those with a "legitimate interest".

Shell companies and other legal entities

Article 30.1 of the same Directive requires that all legal entities (such as companies, etc.) incorporated within EU member states have to register their beneficial ownership in a central registry, and this information will be accessible at least by anyone with a "legitimate interest" (and in some cases – as in the UK – which have already adopted the Directive into their national legislation, by the public at large).

Trusts: obstruction and slippery language

Provisions on trusts (these are usually regarded as legal *arrangements*, as opposed to legal *entities* or legal *persons*) are filled with so many holes that progress is virtually absent.

In the same EU money laundering Directive (see above: *shell companies and other legal entities*) requiring beneficial ownership information of shell companies and other entities to be registered, the UK has successfully lobbied for trusts to be excluded. The clear and direct language on companies and other entities in Article 30 stands in stark contrast to the language on trusts, one article down (Article 31), which is far more restricted, ambiguous and squirrelly.

First, it is not made clear[1] which trusts the Directive applies to.

1. Does it apply only to *trustees* subject to EU law (and thus, not to trustees outside the EU), regardless of the law governing the trust; or
2. Does it apply to trusts governed by the laws of any EU Member State, regardless of who or where the trustee is (although enforcement for non-EU trustees would be unlikely), or
3. Does it apply only to trustees where the trust is governed by the *same* law as the trustee (for example, a UK trustee of a trust governed by UK law); or
4. Something else?

Second, beneficial ownership information on these (uncertain) trusts will only be held in a central registry if the trust "generates tax consequences." This is super-slippery language. Many trusts are created with the very purpose of ensuring that there will be 'no tax consequences.' And one might ask further questions. For instance, where do these 'tax consequences' need to fall for this to apply? What do they even mean by 'tax consequences?' Who knows: this language, which has never been publicly explained, seems likely to exclude the most common offshore trusts.

Third, there is no mention of access by the public or at least anyone with a 'legitimate interest' in knowing who owns the assets.

Trusts must and will become a new arena in the battle for global financial transparency. Otherwise we may end up seeing a boom in trust creation, especially for those tax dodgers and money launderers trying to escape the increasingly more transparent shell companies and other legal entities.

Country-by-country reporting (CbCR)

In the area of CbCR it is again **Europe** that has been taking a lead on. The world's first CbCR regulations (for banks) have been implemented; and another Directive for extractive industries will kick in soon. To be more precise:

i) Article 89 of the EU Directive 2013/36/EU (Capital Requirements Directive IV, or CRD IV) requires Country-by-country reporting for financial institutions. The rules include annual disclosure of turnover, number of employees, profit or loss before tax, tax on profit or loss, and public subsidies received, in each country of operation.

ii) Article 42 of the EU Directive 2013/34/EU says Member States "shall require large undertakings and all public-interest entities active in the extractive industry or the logging of primary forests to prepare and make public a report on payments made to governments on an annual

[1] Article 31 reads: "Member States shall require that trustees of any express trust governed under their law obtain and hold adequate, accurate and up-to-date information on beneficial ownership regarding the trust (…)"

basis." Article 53 says reporting should begin for financial years commencing on or after January 1, 2016.

The **OECD**, by contrast, has made little progress on CbCR transparency.

Its "BEPS" project proposals published in October 2015 to curb corporate tax cheating do establish a template for CbCR, which represents progress. Yet the reports will not be made public; and multinationals will only have to file this information with their home tax authority (so other jurisdictions where a multinational is active will then have to beg the multinational's possibly recalcitrant home country to get the information they need to assess the multinational's tax liability.) These restrictions will also deny journalists, civil society actors, investors, other countries's tax authorities – and many others with a legitimate interest in disclosure – of the information they need. In terms of transparency, this a failure.

The **United States**' Dodd-Frank Act (Section 1504) is supposed to require CbCR for extractive industries. But despite this promise, the process has met heavy political opposition. Implementing regulations are expected to be issued for extractive industries in 2016, but earlier drafts on CbCR have already been challenged via court proceedings, and this raises doubts over the whole agenda. (For a summary of the legal development regarding of Dodd-Frank Act see this April 2015 report by the U.S. Congressional Research Service.)