

## CHAPTER 13

# Beneficial Ownership: Filling the Gap in Transparency and Accountability in the Extractive Industries and Improving Governance

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**Abstract:** Transparency through disclosure of beneficial ownership and the resulting accountability have the potential to transform governance structures in the extractive industries, particularly in natural resource rich developing countries. Benefits from the disclosure of beneficial ownership accrue to the public sector, since increased transparency allows the state to reduce various points of natural resource revenue leakages, and thereby retain more precious financial resources required to invest in education, healthcare, and infrastructure, as well as other public priorities. The private corporate sector too benefits from such disclosures, as this helps minimize legal and reputational risks that might arise through association with business partners or suppliers having opaque ownership structures. In addition the ensuing transparency helps foster competition, reduce corruption and promote fair business practices.

**Keywords:** transparency, beneficial ownership, disclosure, natural resources, accountability, natural resources management, governance, fair business practices, anti-corruption, competition

Citation: Radon, J., Achuthan, M., & Ravichandran, N. (2019). Beneficial Ownership: Filling the Gap in Transparency and Accountability in the Extractive Industries and Improving Governance. In R. Krøvel & M. Thowsen (Eds.), *Making Transparency Possible. An Interdisciplinary Dialogue* (pp. 159–179). Oslo: Cappelen Damm Akademisk. <https://doi.org/10.23865/noasp.64.ch13>

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## Introduction

Legal practitioners often encounter the repercussions of ignoring or failing to procure beneficial ownership information on companies involved in oil, gas and mining industries in resource rich countries. Beneficial ownership information entails the disclosure of real or ultimate owners of a company, namely the natural persons who own or control such a company, no matter how many intervening layers of other companies and/or legal entities may exist in between such a company and its natural person owners.

As such, when beneficial ownership of oil, gas or mining companies is opaque, transfer of both information and profits to companies registered in so-called “tax havens” such as the British Virgin Islands and Mauritius,<sup>1</sup> which do not yet require ownership registration or beneficial ownership disclosure, likely leads to loss of natural resource revenue for resource rich countries (“host countries”), located mainly in the developing world. Often host countries are offered relatively small amounts of taxes and other compensation for the operation of an oil, gas or mining project, with further profits invariably distributed to unknown or hidden persons, many of whom are highly placed public officials or other politically compromised or exposed persons in their own government, through companies with opaque ownership structures. How extensive this problem is has been exposed through the now infamous Panama Papers and Paradise Papers leaks,<sup>2</sup> although the actual amounts of the huge sums involved are at best educated guesses.<sup>3</sup>

Disclosure of beneficial ownership is a necessary and integral part of the efforts to promote and institutionalize transparency in the extractive

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1 Over, Marco Chown. British Virgin Islands growing rich as a global tax haven, *The STAR*, (2016, April 4); Doward, Jamie. Deloitte promotes Mauritius as tax haven to avoid big payouts to poor African nations, *The Guardian*, (2013, November 3). Accessed on August 20, 2018, and at <https://www.theguardian.com/business/2013/nov/03/deloittes-tax-savings-investments-in-poor-countries>.

2 International Consortium of Investigative Journalists, Leaders (ICIJ), Criminal celebrities. Retrieved from <https://www.icij.org/investigations/panama-papers/> ICIJ, ICIJ releases Paradise Papers data from Appleby, (2017, November 17) at <https://www.icij.org/investigations/paradise-papers/icij-releases-paradise-papers-data-appleby/>.

3 Henry, James. S. The price of offshore revisited: New estimates for missing global private wealth, income inequality and lost taxes, (2012, July) at [http://taxjustice.net/cms/upload/pdf/Price\\_of\\_Offshore\\_Revisited\\_120722.pdf](http://taxjustice.net/cms/upload/pdf/Price_of_Offshore_Revisited_120722.pdf).

industries, and also to enable a more equitable amount of the sums earned in natural resource rich countries to actually be retained by them. Transparency as such is the sine qua non for governance reform in the extractive industry not only promoting accountability, but also fostering linkages to wider governance reforms in the industry, thus providing for a more equitable distribution or sharing of the profits of natural resource exploitation. From the perspective of private sector companies, minimizing the risk of association with undesirable business partners or questionable suppliers and dodgy entities or individuals posing political risk, is imperative in order to avoid any violation of laws regulating corruption and financial crimes, including money laundering and financing of terrorism.<sup>4</sup> Transparent beneficial ownership disclosures would presumably lead to the exposure of organizations linked with or owned by individuals posing a high political and legal risk to companies.

From the public sector perspective, natural resources such as oil, gas and minerals are by law held in trust by the government of a country, for the benefit of the people of that country. Public policy would thus dictate that the people should have accurate and complete knowledge of the management of their natural wealth. Transparency in the extractive industry fosters public trust and informs and engages the public on crucial matters relevant to the governance and use of their natural resources, thus also benefiting the private sector as it engenders the process of obtaining and maintaining the social license to operate from the communities. Some advocates<sup>5</sup> of maintaining the status quo of not disclosing

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4 Kelly, E. John, McBride, Thaddeus R., Richardson, Eli J. & Palmeri, Cheryl A. Proposed legislation would combat terrorist financing, money laundering. Accessed on June 8, 2017, available at <https://www.lexology.com/library/detail.aspx?g=790a6c30-f647-46e0-a653-c792d9317309>. See also Woods, Martin. Is beneficial ownership really so difficult? *Thomson Reuters*, (2015, January 19).

5 Kenney, Martin. Open company UBO registers are not the panacea to financial crime, *The FCPA Blog*, (2018, May 7). Accessed on August 20, 2018, available at <http://www.fcpcbog.com/blog/2018/5/7/martin-kenney-open-company-ubo-registers-are-not-the-panacea.html>. [Martin states, "Why should a businessperson conducting perfectly legitimate business be denied the right to privacy in order to do so? The argument that 'if it's legitimate then why try and keep it confidential?' doesn't fly. We are all entitled to the protection of private data unless we are doing something wrong. Privacy is closely aligned to human dignity. The legitimate right to privacy is analogous to the privacy of a bank account and other financial data (expected, but not unqualified) and medical records."].

identities of beneficial owners, point out issues of privacy (including protection from kidnapping and extortion if it becomes known that a person has considerable assets); protection of legitimate business interests,<sup>6</sup> such as the decision to acquire or merge companies; protection of intellectual property; or the quiet pursuit of a new creative venture. Recently, some of these advocates have started to realize that tax authorities and other public regulators should have the right to examine, for specific purposes, officially maintained registers in which the identities of beneficial owners are disclosed. While, as briefly noted above, there can be valid business and personal reasons for the confidentiality of beneficial ownership information, it is questionable whether any of these reasons should, or do, apply to the natural resources sector in host countries of the developing world. Here, because of public ownership of such resources, states issue licenses or enter into agreements with operating companies to develop the resources. In such instances, the state is usually a partner in the project, and as such has a commercial interest in knowing with whom it is entering into a partnership, particularly when politically exposed or compromised individuals from its own government enrich themselves through opaque ownerships<sup>7</sup> in the very companies partnering with the state.

Transparency, accountability and trust are important features of a robust governance framework for the extractive industry, ranging from the allocation of licenses to the collection and management of revenues. Revenues from the extractive industry are an essential source of income for many developing countries, without which they cannot help fund their most critical institutions, their schools and their infrastructure. On the other hand, transparency helps foster competition, reduces cronyism and corruption, promotes fair business practices, and reduces reputational risks for the private sector. This results in an improved, reliable and friendly business/investment environment for private sector investors, and encourages them to enter emerging markets. The benefits of

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6 See Stiglitz, Joseph & Pieth, Mark. Overcoming the shadow economy, *Friedrich-Ebert-Stiftung*, (2016, November 11), page 6, for discussion on potential, legitimate reasons for the use of tax havens.

7 ICJ, How family that runs Azerbaijan built an empire of hidden wealth. Retrieved from <https://www.icij.org/investigations/panama-papers/20160404-azerbaijan-hidden-wealth/>, April 4, 2016.

transparency in the extractive industry are numerous and accrue to a diverse set of stakeholders, including the state/government, citizens, the private sector, and civil society. Ironically, it appears from the authors' experience as advisors to governments and state-owned entities in emerging nations, that the advantages of transparency are still not fully understood by the extractive industry, probably due in part to a failure to appreciate the risks of non-transparency and the repercussions these companies can suffer from the failure of beneficial ownership disclosure. In fact, governments do not fully appreciate that transparency has the benefit of creating a more secure and reliable investment climate and facilitating better governance,<sup>8</sup> which, from the authors' experience, can become a virtuous circle. As such one of the goals of the recommendations made herein, is to help further the discourse on the benefits of disclosing ownership, including advancing the creation of such a circle in emerging nations rich in natural resources.

## **Disclosure of beneficial ownership eliminates opaque ownership structures**

The obvious benefit of disclosure of beneficial ownership for host countries and their people relates to the elimination of opaque ownership structures, which allow companies to hide improper relationships with politically exposed or compromised individuals – in short it is a powerful tool in minimizing corruption, which has spawned civil unrest and decades-long conflicts around the globe. There have been repeated cases of countries (specifically emerging economies) losing millions on account of sham companies or politically connected companies. For instance, the Democratic Republic of Congo (DRC) lost approximately \$1.36 billion in mining revenues, about twice the amount of the annual budget for health and education, between 2012 and 2013, because of the sale of undervalued mining assets to offshore companies with questionable ownership

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8 Johnston, Michael. Good governance: Rule of law, transparency, and accountability, at <http://unpan1.un.org/intradoc/groups/public/documents/un/unpano10193.pdf>.

structures.<sup>9</sup> Loss of valuable natural resource revenues impacts both the public and the private sector. As countries and governments lose potential revenue from the exploration and exploitation of natural resources, they lose the capacity to develop and improve their economy sustainably. Subsequently investors, particularly foreign investors, are hesitant to invest in the extractive industries since the country is unable to invest in infrastructure and other non-resource sector industries, which may attract direct foreign investment in potential projects, attractive to prospective investors. For instance poor or absent infrastructure hinders development,<sup>10</sup> and oil, gas or mining investors might be hesitant if access to assets and the facilitation of project operations require the investor to develop basic infrastructure like roads, which ideally should have already been in place. Further, loss of revenue fosters a cycle of corruption in developing nations, diluting all efforts made by the international community, and the developing nations themselves, to make the extractive industry as transparent as possible.<sup>11</sup>

Information on who ultimately owns and benefits from the activities of a corporation will eliminate the phenomenon of hidden owners and beneficiaries, revealing politically exposed or compromised individuals, who often use shell companies and/or tax haven jurisdictions to hide their ownership in oil, gas or mining assets, thus evading payment of taxes on the income derived from such assets, and avoiding the liability<sup>12</sup> associated with the operation and use of such assets.<sup>13</sup> Benefits from

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9 Africa Progress Report 2013: Equity in extractives Africa: Stewarding Africa's natural resources, *Africa Progress Report*, p. 56.

10 DW, Poor infrastructure is key obstacle to development in Africa, (2011, July 26).

11 Votava, Cari. Extractives sector corruption: What we have learned, *Extractive Industry Transparency Initiative (EITI)*, (2018, January 18).

12 If the ultimate owners of a company are not known, it is difficult to hold them liable for the simple reason that their identity is unknown. If the identity of ultimate owners is made transparent to government authorities, there are still legal hurdles to overcome, particularly because shareholders/stockholders of a company are by law not liable for the obligations of a company, although, in some jurisdictions, liability for environmental damage is now being extended to controlling shareholders. Knowledge of beneficial owners of a company provides the opportunity to issue an operating license with the condition that all significant shareholders of that company must execute a guarantee for the obligations and liabilities incurred by the company, especially for any liability for environmental damages.

13 Panama Papers reveal wide use of shell companies by African officials, (2016, July 25). *New York Times*.

the transparency of ownership structures are not only restricted to host countries. Profit shifting through innovative corporate structures can also result in tax evasion or avoidance in the countries in which the oil, gas and mining companies are incorporated (home countries). In fact, the Extractive Industries Transparency Initiative (EITI), the “global standard to promote the open and accountable management of oil, gas and mineral resources,”<sup>14</sup> is supported by some home countries,<sup>15</sup> and global international oil companies such as Chevron, BP, Exxon Mobil and Hess.<sup>16</sup>

The EITI has, as of 2016, included the disclosure of beneficial ownership within the EITI Standards reporting requirements, calling upon members states to keep a “publicly available register of the beneficial owners of the corporate entity(ies) that bid for, operate or invest in extractive assets, including the identity(ies) of their beneficial owner(s), the level of ownership and details about how ownership or control is exerted”. In addition where possible, information on beneficial ownership should be incorporated in “existing filings by companies to corporate regulators, stock exchanges or agencies regulating extractive industry licensing.”<sup>17</sup> Furthermore by 2020, all member states “have to ensure that all oil, gas and mining companies that bid for, operate or invest in extractive projects in their countries disclose their real owners,” identifying the name, nationality and country of residence of the owners.<sup>18</sup> The European Union too issued a directive in June of 2015, the 4th Anti-Money Laundering Directive (EU) No. 2015/849 (4th AMLD), requiring all member states to enact national laws on disclosure requirements for “beneficial ownership information for corporate and legal entities.”<sup>19</sup> Such information, as per the directive, requires “adequate, accurate and current information on beneficial owners” of companies, including the “name, date of birth, place

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14 EITI, About us. Accessed August 12, 2018, available at <https://eiti.org/about/who-we-are>.

15 EITI, Supporting countries. Accessed August 12, 2018, available at <https://eiti.org/supporters/countries>.

16 EITI, Companies. Accessed August 12, 2018, available at <https://eiti.org/supporters/companies>.

17 EITI, EITI Standards 2016. Accessed on July 16, 2018, available at <https://eiti.org/node/4922#r2-5>.

18 EITI, EITI beneficial ownership requirements. Accessed on July 16, 2018, available at <https://eiti.org/beneficial-ownership>.

19 Association of Certified Anti-Money Laundering Specialists (ACAMS), Ultimate beneficial ownership, (2017, December). Retrieved from <https://www.acamstoday.org/ultimate-beneficial-ownership/>.

of residence, and nature and extent of such beneficial ownership,” which are eventually to be placed on national registries accessible to regulators, entities that might need to undertake customer due diligence, and individuals who can prove a “legitimate interest” in requiring access to such information.<sup>20</sup> Recent amendments to the directive further cover the disclosure of beneficial ownership of trusts<sup>21</sup> in a private register available to tax regulators, law enforcement authorities and businesses subject to anti-money laundering rules.<sup>22</sup>

The directive covers natural person(s) who ultimately own or control the company through “direct or indirect ownership of more than 25 percent”<sup>23</sup> of the shares or voting rights or ownership interest, or through “control via other means”; or hold(s) the position of “senior managing official,” in the event that no other natural person is “identified (having exhausted all possible means and provided there are no grounds for suspicion) or if there is any doubt that the person so identified is the beneficial owner.”<sup>24</sup>

In the United States, in 2016 the Financial Crimes Enforcement Network (FinCEN), created the “fifth pillar” of the Anti-Money Laundering/Bank Secrecy Act compliance, for customer due diligence programs, which incorporates new features requiring “covered financial institutions,” such as banks, credit unions, brokers or dealers in securities, mutual funds, futures, commission merchants and commodities brokers<sup>25</sup> to collect and maintain data on beneficial owners, commencing in May 2018. Beneficial owner(s) are defined as “[e]ach individual, if

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20 Mardle, David & Cloake, Debbie. (2017, June 30) Navigating the new European regime for disclosure of beneficial ownership. Retrieved from <https://www.lexology.com/library/detail.aspx?g=ef7a3a89-91c6-48c6-bf27-880dcd8f1016>.

21 Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU (Text with EEA relevance).

22 Lochner, Eric. Public registers expand EU third-party compliance risks, *FCPA blog*, (2018, April 4).

23 The 25% standard will most likely not be effective in disclosing ownership by politically compromised individuals or those attempting to evade taxes for the simple reason that 25% can still obviously hide significant ownership positions.

24 FCPA Blog.

25 Federal Register / Vol. 82, No. 187, September 28, 2017, available at [https://www.fincen.gov/sites/default/files/federal\\_register\\_notices/2017-09-29/CDD\\_Technical\\_Amendment\\_17-20777.pdf](https://www.fincen.gov/sites/default/files/federal_register_notices/2017-09-29/CDD_Technical_Amendment_17-20777.pdf).



any, who owns, directly or indirectly, 25 percent or more of the equity interests of the legal entity customer (e.g., each natural person owning 25 percent<sup>26</sup> or more of the shares of a corporation); and “[a]n individual with significant responsibility for managing the legal entity customer (e.g., a Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, or Treasurer).”<sup>27</sup>

Additionally, the United States Senate held hearings in February 2018 for a bill on beneficial ownership disclosures, which would direct states that receive funding under the Edward Byrne Memorial Justice Assistance Grant program to enact laws requiring entities that form corporations or limited liability companies to disclose their beneficial owners, the definition of which includes all natural persons who “directly or indirectly exercise substantial control over a corporation or LLC (limited liability company), through ownership interests, voting rights or agreements,” or “have substantial interest in or receive substantial economic benefits from assets” of such a corporation or limited liability company.<sup>28</sup>

## The case for disclosure

### Information on beneficial ownership results in an efficient and optimum allocation of licenses/concessions

Disclosure of beneficial ownership will help governments ascertain the financial capacity and technical expertise of oil, gas or mining companies prior to granting licenses/concessions, and will require parent companies of such companies to guarantee the financial and technical obligations

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26 The 25% standard will most likely not be effective in disclosing ownership by politically compromised individuals or those attempting to evade taxes.

27 Federal Register, September 2017. See also FinCen’s long-awaited final rule on collection of beneficial ownership information and customer due diligence, *Provititi*. Accessed on June 24, 2016, available at <https://www.provititi.com/US-en/insights/fincen-final-rule-collection-beneficial-ownership-information-and-customer-due-diligence>.

28 <https://www.congress.gov/bill/115th-congress/senate-bill/1454/text>.

of oil, gas or mining companies under such licenses/concessions. The need to ensure adequate technical expertise and financial capacity cannot be stressed enough, especially where the applicant company, in many cases, is a subsidiary or affiliate company with no independent financial and technical wherewithal. For instance, license allocation on the basis of inadequate information to an extractive company with insufficient funds or technical knowledge can lead to situations where communities and the environment are significantly compromised, particularly when the license holder does not have the financial resources or the technical capacity to avoid and/or mitigate adverse impacts on the environment, and undertake rehabilitation measures and compensate communities for such adverse impacts.<sup>29</sup> As such, beneficial ownership disclosure can inform the government about the financial and technical capabilities of the applicant for a license and its beneficial owners, and given this information, the government can require the beneficial owner to guarantee the technical and financial abilities of the applicant for the life of the project, and during and after closure, as appropriate, especially in respect to environmental damage.<sup>30</sup>

## Information on beneficial ownership can ensure accountability

Often developing countries in the nascent stages of establishing their natural resource industries and the regulations governing such

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29 Time, Gray. (2017, July 14). Who cleans up the mess when oil and mining companies go bankrupt? *The Globe and Mail*.

30 In the absence of a guarantee, the applicant company could easily become a shell company, namely a company without any assets, other than the right to exploit or develop a natural resource, as the profits of that company are regularly and normally distributed as dividends to the shareholders registered on the books of the company, with the consequence that that company does not have adequate or sufficient financial resources to meet its obligations. This is particularly and often the case at the end of the life of a project, at which time the resource is almost depleted and the accumulated profits have all been distributed (and spent). Consequently, it is prudent for a state to require a guarantee from the owners of a company for such liabilities, especially for covering the cost of restoration of the exploited area to its original condition and ensuring that there are no lingering environmental costs.

industries, are handicapped by weak institutions.<sup>31</sup> Due to lack of proper training, civil servants often lack the requisite skills, tools and experience, to protect the country and its people from natural resource revenue leakages. An asymmetry of information<sup>32</sup> emerges, where companies with access to resources can equip themselves with an abundance of valuable information in order to negotiate complicated energy deals, while governments, and particularly government officials, are unable to effectively counter-negotiate due to lack of access to such information.

In addition, as mentioned earlier, extractive industries are associated with negative externalities, such as costs and damages arising from adverse impacts to the environment and surrounding communities, etc. Moreover, abandonment of extractive assets and/or inadequate implementation of mine closure activities by the license holder are not uncommon,<sup>33</sup> with the consequence that the state bears the costs of cleanup and rehabilitation.<sup>34</sup> For example, submissions made by a civil society group to the relevant government ministry in Ontario, Canada noted that the taxpayers of Ontario bore the burden of clean-up costs of many active and abandoned mines, for which the financial assurances were inadequate.<sup>35</sup> In other instances, governments have undertaken mitigation and/or rehabilitation measures, spending taxpayers' money on clean-up activities, due to the absence of specific obligations on the extractive companies, as in the case of the government of South Africa, which had to

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31 Totaro, Paola. (2017, June 28). Few resource-rich countries properly manage their natural resources: report. *Reuters*.

32 Stiglitz, Joseph. E. (2000). The contributions of the economics of information to twentieth century economics, *The Quarterly Journal of Economics*, 115(4).

33 Ashton, S., Bausch, K., Bulman, A.M., Cunha, I.P., Liu, D., Pathmanathan, J., Pham, L., Ravichandran, N., Srikrishnan, M., Tecson, C., Ueda, K., & Yi, R. (2015). Supervised by Radon, J. Mining in Peru: Benefiting from natural resources and preventing the resource curse, Capstone Workshop, Columbia University.

34 Superfunds in the United States were created pursuant to legislation in 1980 that allows the United States Environmental Protection Agency (EPA) to use public funds to clean up contaminated sites, such as abandoned or unmanaged mining sites. See EPA, "What is a superfund?" Accessed on August 11, 2018, available at <https://www.epa.gov/superfund/what-superfund>.

35 See Ontarians for a Just Accountable Mineral Strategy (OJAMS), Submission to the Ontario Ministry of Northern Development and Mines, May 2015, <http://www.ojams.ca/wp-content/uploads/2015/10/ojams-may2015-submission.pdf>.

spend at least \$6.6 billion on mine closures and associated clean-up activities for abandoned mines.<sup>36</sup>

Knowledge of beneficial ownership better equips government officials with the tools needed to leverage their position in negotiating agreements governing natural resources. Carefully and well drafted contractual frameworks can require license holders to provide security, financial guarantees or fully bonded rehabilitation programs to cover environmental costs. However, license holders are invariably a subsidiary or an affiliate company of another company, and as such have a limited financial and technical capacity to perform such contractual obligations, if such obligations are in fact negotiated. In these circumstances, knowledge of beneficial ownership of oil, gas and mining companies can give governments the opportunity to protect themselves and the public, by requiring that the beneficial owners provide guarantees to cover the costs of adverse impacts on the environment and communities, mine closure, decommissioning and abandonment, rehabilitation and/or clean-up costs of extractive industry sites.

## Disclosure of beneficial ownership informs communities and facilitates the social license to operate

In addition to acquiring the legal license to operate, extractive companies are finding it increasingly difficult to sustain their investments and their projects without obtaining a social license to operate – i.e., the ongoing responsibility of a business or company to “ensure its activities respect the rights of all those in any community” in which it operates.<sup>37</sup> Obtaining the social license to operate in the impacted/affected communities and communal buy-ins for an extractive project is crucial in order to operate the project sustainably. Ernst & Young, a global professional services firm, in 2015 identified the failure to secure a social license to operate as

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36 Vecchiato, Paul (2015, August 19). South Africa cost for cleaning up old mines almost \$6.6 billion, *Bloomberg*.

37 Morrison, John, (2014, September 29). Business and society: Defining the ‘social licence’, *The Guardian*.

the third most prevailing business risk faced by mining companies today, moving it up from fourth place in its previous assessment for the year 2013–2014.<sup>38</sup>

Increasingly in this regard, stakeholders, including communities, lenders, governments, civil society, and activist shareholders alike expect companies to adhere to the highest transparency standards, thus fostering trust between the communities, governments and the company. Disclosure of beneficial ownership would therefore inform the local communities and other stakeholders of the real owners of the extractive company, and facilitate the process of acquiring and maintaining the social license to operate.

## Disclosure of beneficial ownership also serves the interests of other constituencies

Beneficial ownership information not only serves the interests of a government or the public, but also companies, as such information can help identify questionable business partners and entities on the supply and value chain. Multinational companies understand the benefits of beneficial ownership disclosures in terms of: reducing pressure points for corruption and unsound business relationships with domestic companies, and goods and service suppliers that create risk; upholding the principles of competition by creating a fair and transparent process of granting project licenses; and creating transparency in terms of complete and accurate market information.<sup>39</sup> Furthermore, private sector actors are increasingly aware and concerned about their association and partnership with questionable entities and politically exposed individuals, in relation to both legal and reputational risk. As such, beneficial ownership disclosure can only improve their due diligence efforts to reduce the risk of partnering with such entities and individuals.

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38 Ernst & Young. Business risks facing mining and metals 2014–2015. Available at [http://www.ey.com/Publication/vwLUAssets/EY-Business-risks-facing-mining-and-metals-2014%E2%80%932015/\\$FILE/EY-Business-risks-facing-mining-and-metals-2014%E2%80%932015.pdf](http://www.ey.com/Publication/vwLUAssets/EY-Business-risks-facing-mining-and-metals-2014%E2%80%932015/$FILE/EY-Business-risks-facing-mining-and-metals-2014%E2%80%932015.pdf).

39 The B Team. (2015, January 15). Ending anonymous companies: Tackling corruption and promoting stability through beneficial ownership transparency – the business case.

## Recommendations

The issues discussed above are only some of the concerns that can be addressed and resolved by beneficial ownership disclosures. The benefits can also be noticed in other circumstances, such as fund structures where knowledge of sponsors/beneficial owners can help alleviate the concerns of limited fund life, etc. At its core, disclosure of beneficial ownership provides information and permits better assessment of potential partners.

Mismanagement and corruption resulting from a lack of transparency have many manifestations, and can result in dire consequences for governments and citizens of resource rich countries.<sup>40</sup> Transparency through disclosure of beneficial ownership and the resulting accountability have the potential to transform governance structures in the extractive industries. As discussed above, countries can significantly benefit from disclosure of beneficial ownership, as increased transparency can help plug natural resource revenue leakages, and retain precious resources needed to invest in education, healthcare and infrastructure. A shift in focus away from the issues relating to disclosure of beneficial ownership will, therefore, have particularly far-reaching impact on these countries.

The outrage over the circumstances arising from lack of information on beneficial ownership has been growing, strengthening the demand for a viable solution to the problem, from various sectors.<sup>41</sup> In the United States, for instance, the Secretary of State of Delaware has publicly given his support to the end of anonymous shell company formation in his state,<sup>42</sup> pursuant to the Counter Terrorism and Illicit Finance Act which has been introduced in the United States Congress. Even the Treasury Secretary of the United States, recently announced that legislative initiatives need to be made to “deter money laundering and financing of

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<sup>40</sup> Reuters (2017).

<sup>41</sup> Fuller, Clay. (2018, July 30). It's long past time for Congress and the Treasury to step up their global anti-corruption efforts, *American Enterprise Institute*.

<sup>42</sup> Secretary of State of Delaware. June 8, 2018, available at <https://thefactcoalition.org/wp-content/uploads/2018/06/DE-June-2018-Letter-to-HFSC-on-BOT.pdf>; Rubenfeld, Samuel (2018, June 25). Delaware backs overhaul of shell company rules, *Wall Street Journal*.

terrorism through the use of shell companies” by finding an “efficient and prudent way” to access beneficial ownership information”.<sup>43</sup>

## The case for less ambiguous definitions of beneficial ownership disclosures

Beneficial ownership definitions should broadly consist of the following:

- All natural persons who, directly or indirectly, ultimately own or control the license holder/extractive company.
- Details on name, nationality, location/address, personal identification number, and other identifying markers and information for the abovementioned beneficial owners.
- Currently different formulations of what constitutes “beneficial ownership” exist with the shareholding thresholds set at 25 percent and above, which is worrying as a 25 percent shareholding threshold allows companies attempting to hide questionable owners to circumvent the disclosure requirement by simply adopting structures that would keep the shareholding below this threshold. While the urge to simplify the definition for ease of compliance cannot be denied, it is important to ensure that we do not succumb to the trap of oversimplification. The definition of ‘beneficial ownership’ should achieve its ultimate aim at all times: procuring information on all natural person(s) who ultimately own or control the extractive company.
- Different standards should be applicable to private and publicly listed companies:
  - o **With respect to private companies:** All natural persons that own or control (either directly or indirectly) any share or equity interest in the extractive company should be disclosed as beneficial owners. Given that a private company by nature will have

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43 Rubenfeld, Samuel. (2018, July 12). Mnuchin seeks shell company changes within six months, *Wall Street Journal*.

limited shareholders, disclosing information on all its shareholders is not an onerous requirement.

- o **With respect to publicly listed companies whose shares are listed on recognized international stock exchanges, and domestic companies that are listed on domestic stock exchanges (that are not internationally recognized):** All natural persons that own or control, either directly or indirectly, 5 percent<sup>44</sup> or more of the shares or equity interest in the extractive company should be disclosed as beneficial owners.
  - Ownership can be through shares or equity interest or in any other number of diverse manners, including contractual rights, voting arrangements, convertible stock, proxies, etc.
  - Ownership and control can be exercised individually or together with any corporate or other legal entity(ies) and/or natural person(s) who act in consort.
  - “Control” triggers for disclosure include:
    - o The right (directly or indirectly) to:
      - Appoint a majority of the directors of any of the companies in the entire corporate chain that have a relationship to the license holder, and/or
      - Control the management or policy decisions of any of the companies in the entire corporate chain that have a relationship to the license holder.
        - o De facto and de jure control.

## The case for public registries

Efforts are being made to develop and institute national beneficial ownership registries. According to a publication by the Law Library of the United States Congress, information on corporate registration and

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44 In the United States, when “a person or group of persons acquires beneficial ownership of more than 5% of a voting class of a company’s equity securities, registered under Section 12 of the Securities Exchange Act of 1934,” such person or group of persons are required to file a Schedule 13D with the SEC. See U.S. Securities and Exchange Commission, Fast Answers, accessed August 14, 2018, available at <https://www.sec.gov/fast-answers/answerssched13htm.html>.



beneficial owners is collected by business registrars in countries such as Afghanistan, Argentina, India, Sweden, and the United Kingdom;<sup>45</sup> national tax authorities in Brazil; securities regulators in Australia and Pakistan; securities exchanges such as in South Africa; central banks as in Armenia and Costa Rica;<sup>46</sup> or as required by the new amendment to the EU directive, a designated publicly available central registry in EU member states.<sup>47</sup> Moreover, recently there has been discussion of a worldwide registry<sup>48</sup> to facilitate efficient and swift access to information on beneficial owners, specifically in regard to criminal investigations by tax and enforcement agencies in different jurisdictions. In fact the private sector and its advisors are currently trying to address the issue of collecting necessary information to identify beneficial owners. For instance, financial institutions face the challenge of not having the knowledge and know-how to investigate layered and complicated shareholding structures across various jurisdictions, to identify questionable legal entities and exposed political individuals.<sup>49</sup> Worldwide registries would help both private sector actors and governments alike to access information that could help the former comply with beneficial ownership disclosure requirements, and the latter with investigating potential financial crimes such as money laundering, corruption and tax evasion.

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45 As of May 1, 2018, the parliament of the United Kingdom “voted to accept an amendment to the sanctions and anti-money laundering bill” that requires the United Kingdom’s overseas territories, which include Anguilla, Bermuda, British Virgin Islands, Cayman Islands, Falkland Islands, Gibraltar, Montserrat and the Turks and Caicos Islands, “to publish public registers of company ownership by the end of 2020.” See EITI, UK’s overseas territories to have beneficial ownership registers. Accessed on August 14, 2018, available at <https://eiti.org/news/uks-overseas-territories-to-have-beneficial-ownership-registers>.

46 The Law Library of Congress, *Global Legal Research Center*, Disclosure of beneficial ownership in selected countries, (2017, July).

47 Lochner, Eric (2018, April 4). Public registers expand EU third-party compliance risks, *FCPA blog*.

48 Stiglitz & Pieth. (2016).

49 Chrusciel, Grzegorz (2016). Identifying the ultimate beneficial owner (UBO): The challenge of finding the needle in the haystack, *Thomson Reuters*.

## The case for reformed policy on service providers

The disclosures of 214,000 shell companies through the infamous Panama Papers illuminated the growing concern over the role of service providers in creating shell companies as part of complex ownership structures, to help many questionable beneficial owners hold assets without much regulatory tax oversight.<sup>50</sup> Service providers, such as the law firm of Mossack Fonseca, were exposed as the facilitators of lost natural resource revenues, bringing to light their decades long offshore financial services business in the off-shore center of Panama, for example the “externalization of billions of dollars”<sup>51</sup> of mining revenue from the DRC. As such, regulations overseeing all service providers to the extractive industries should require that such providers are independent, and certify the correctness of the identification of all the true owners and the absence of all conflicts of interest. Further, such service providers should submit to the jurisdiction in which their services to their client have an impact. For instance, if non-U.S. service providers provide services that have an impact in the United States, resulting in tax evasion or money laundering, which can be a conduit for the financing of terrorism, then these service providers must subject themselves to the jurisdiction of the United States. Such jurisdiction can be established through bilateral agreements, such as double taxation treaties and investment agreements that countries enter into.<sup>52</sup>

## The case for creating an environment of transparency and fair business practices

Governments, particularly those of developing countries rich in natural resources, must realize that transparency and accountability is a two-way

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50 Koren, Marina (2016, April 3). What are the Panama Papers? *The Atlantic*. Retrieved from <http://www.theatlantic.com/international/archive/2016/04/what-are-the-panama-papers/476658/>. See also Stiglitz, Joseph E. & Pieth, Mark (2016, September 29). The real scandal behind the Panama Papers, *Vanity Fair*. Retrieved from <http://www.vanityfair.com/news/2016/09/the-real-scandal-behind-the-panama-papers>.

51 Panama Papers unravel DRC mining concession deals, *ANCIR*. Retrieved from <https://panama-papers.investigativecenters.org/drc-copper-mining>.

52 This article focuses on ownership structures of companies, but trusts, by the nature of their legal characteristics, can create opportunities for politically exposed and compromised individuals, and as such the beneficial ownership disclosure of trusts needs to be handled separately and distinctly.

street. If governments wish to curb the loss of natural resource revenues by requiring and using beneficial ownership disclosures to vet dubious applicant companies, then they must also inspire confidence amongst private sector companies and their lenders that governments are committed to transparency and fair business practices. Companies and foreign investors too are concerned about their reputation and their relationship with dubious and politically connected companies, locally in host countries where they operate. Often companies will enter joint ventures with local companies or enter contracts with local service providers (such as contractors and sub-contractors) due to cost efficiency, convenience or local content/service procurement requirements in host country regulations or contractual obligations. As such while investing companies are responsible for conducting due diligence on local partners, third-party vendors or service providers, it is equally imperative that governments of developing countries rich in natural resources take all steps possible to curb the formation of sham companies with dubious ownership structures operating within their jurisdictions. This requires host governments not only to prosecute politically connected individuals from within their ranks, who hide their ownership of sham companies with the intent to evade or avoid taxes, launder money or finance terrorism, but also to provide certification of the true ownership of local companies that investors in the oil, gas and mining industries might partner or enter into contracts with. Showing a strong commitment to allowing only the incorporation of legitimate companies, creates a better environment for business and attracts investors, since they will have greater confidence that their reputational and even legal risks decrease once they invest in the country.

## Conclusion

Transparency through disclosure of beneficial ownership and the resulting accountability have the potential to transform governance structures in the extractive industries. As discussed above, countries can significantly benefit from disclosure of beneficial ownership, as increased transparency can help plug natural resource revenue leakages, and retain

precious resources required to invest in education, healthcare and infrastructure. Mismanagement and corruption resulting from lack of transparency have many consequences, most costly of which are loss of natural resource revenue, and damage to the environment and communities. Beneficial ownership disclosure is one of the easiest and most efficient ways of preventing loss of natural resource revenue, as companies can easily ascertain and disclose their owners, and allow governments and government officials to accurately map the potential money trail of natural resource revenue.

Admittedly, dedicated government officials of emerging nations are often reluctant to impose conditions on natural resource companies, and which industry considers burdensome, non-competitive or adverse to their interests. This leads to officials fearing that industry will simply not invest, especially if other nations do not have similar requirements. At the same time, government officials are also hesitant to impose beneficial ownership disclosure rules because of the fear of highly placed corrupt officials, who stand to enrich themselves personally through opaque ownership structures in companies involved in the natural resource sector, leading to natural resource revenue loss for their own country.

The natural resource industry functions like the real estate industry, where location carries a premium and is the prime factor in corporate decision making. Natural resource development follows the simple rule of real estate development, which is location, location, location. If a state has an exploitable and profitable quantity of natural resources, especially if there are low security risks in that state, companies will come. As such a state can require disclosure of beneficial ownership information, since the existence of the natural resource will remain the magnet that attracts the industry.<sup>53</sup> On the other hand, the private sector should not fear disclosure as it also benefits industry. Transparency promotes fair business practices, and alerts companies to dubious business parties that might want to partner with them. Additionally, financial institutions needing to comply with regulations on beneficial ownership of account holders, can

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53 Radon, Jenik & Ravichandran, Nandini. The 'business' of extractives: My resources, my rules, *Namibian*. Retrieved July 8, 2015 at <https://www.namibian.com.na/index.php?id=139106&page=archive-read>.

be further assisted by the increasing effort of the international community to set up platforms for disclosing information in publicly available registries. Furthermore, lenders who are concerned about the types of companies they provide with project financing or project loans, will also benefit from beneficial ownership disclosure.

Given that both the public and the private sector benefit from the transparency that ensues through beneficial ownership disclosure, it is prudent that it gains the much-needed traction necessary to make it a common feature of natural resource projects, instead of merely a voluntary exercise in disclosure. Disclosure of beneficial ownership promises to be a win-win for all.