Leveraging Beneficial Ownership Information in the Extractive Sector

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Regulatory and public pressure to increase transparency about the real people who own, control, or gain substantial economic benefits from companies—also known as beneficial owners—is growing globally. The demand for such disclosures is linked to increasing awareness that hiding beneficial ownership can facilitate corruption and financial misconduct.[1] Innovations around beneficial ownership disclosure in extractive sector licensing highlight a new opportunity for coordination on legal frameworks and data platforms that cut across commercial sectors, agency mandates, and national jurisdictions to combat illicit financial flows (IFFs) yet still maintain flexibility for customization to meet challenges and risks in specific administrative and sectoral contexts.

INNOVATIONS IN THE EXTRACTIVE SECTOR

Nearly one billion people live in poverty in countries that are rich in oil, gas, and minerals but manage these resources poorly.[2] In these countries, conflicts can arise between local actors who enjoy few direct benefits from or face increased harms as a result of extraction and those who are seen to profit from the sector, either legally (e.g., through local employment, revenue sharing, and community development) or illegally (e.g., through corruption and self-dealing). Legal frameworks and regulatory systems in resource-rich countries often lack integrity mechanisms, transparency, and accountability, which can make corruption more difficult to detect, prevent, and prosecute. Natural resource transactions are also often opaque, complex, and transnational. And citizens need to have information regarding extractive sector deals, given that natural resources belong to the state and state authorities are supposed to manage these assets for public benefit. Collectively, these factors have contributed to demands for beneficial ownership transparency in the extractive sector.

Global trends around beneficial ownership transparency are still rapidly evolving. One emerging picture is that sector-specific beneficial ownership disclosure requirements have primarily been aimed at local or national levels (e.g., in luxury real estate acquisitions), while regional and international efforts have been broader and non-sector-specific (e.g., financial due diligence and corporate registration requirements covering all types of commercial endeavors). Innovations in extractive sector licensing transparency could represent a hybrid approach, with sector-specific beneficial ownership disclosure requirements emerging from an international multistakeholder body.

In 2016, the public disclosure of beneficial ownership information became a requirement in the Extractive Industries Transparency Initiative (EITI), an international standard for extractive sector

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transparency developed jointly by governments, civil society, and companies, and implemented by national multistakeholder groups in more than fifty countries. By 2020, EITI countries must request, and companies that apply for or hold extractive licenses or contracts in such countries must disclose, beneficial ownership information. The EITI Standard also requires that these disclosures identify any beneficial owners who are government officials or their close associates—referred to as politically exposed persons (PEPs).[3] In meeting these core requirements, implementing countries have flexibility in determining how they institutionally, legally, and procedurally pursue such disclosures.

Part of what motivated this EITI requirement were scenarios in which improper conduct related to beneficial ownership was linked to corruption and IFFs. A study of one hundred cases of corruption in extractive sector licensing gives a sense of the scale of the problem: over half of the cases involved a PEP as a hidden beneficial owner.[4] Foreign or domestic firms sometimes seek out a PEP to whom they can give a beneficial ownership stake in an exploration and production company (or in a subcontractor enterprise) in exchange for preferential treatment in attaining an extractive license or in the terms of a contract. A PEP sometimes sets up an entity to conceal his or her beneficial ownership stake in a company and uses his or her influence to ensure that the company obtains an extractive license or other preferential treatment. To comply with the host country's local content requirements, a foreign firm sometimes enters into a joint venture agreement with a domestic company or enlists domestic subcontractors, and a PEP may hold a beneficial ownership stake in these local entities.

Scenarios like these can violate host country laws that prohibit PEP ownership and self-dealing in government transactions. A recent Natural Resources Governance Institute (NRGI) review of more than fifty mining and oil laws found that about half of them contained prohibitions on PEPs holding interests in companies applying for extractive licenses. Such scenarios could also entail violations of both international and host country anti-bribery legislation, particularly if a firm did business with a PEP's company as a quid pro quo for receiving a license.

If one or more cross-border transactions is involved, the transfer of funds used to acquire or financial returns stemming from an illegally obtained extractive license could constitute IFFs. Such flows could include bribery payments to obtain the license, proceeds from selling a license, profits from licensed exploration or production, or subcontractor takings. Beyond the initial license allocation, maintaining an interest in an extractive project can give a PEP a mechanism for diverting funds on a sustained basis.

PART OF BROADER MOMENTUM

Collecting beneficial ownership information has been part of regional and international policy frameworks to reduce IFFs for some time. The Financial Action Task Force (FATF) includes ascertaining and verifying the identity of beneficial owners in certain risk-based recommendations on due diligence that financial institutions should conduct before establishing business relationships, conducting transactions, and opening accounts. In 2014, the Group of Twenty (G20) adopted high-level principles on beneficial ownership transparency.[5] And between late 2017 and early 2018, the European Union passed the fourth and fifth Anti–Money Laundering Directives, which require companies registered in member states to disclose beneficial ownership information on national registers that will be interconnected to enable the exchange of information among countries, and to put in place verification mechanisms regarding beneficial ownership information.[6]

A consortium of transparency-focused nongovernmental organizations launched OpenOwnership in 2017 to build a public global beneficial ownership register and develop a universal open data standard for beneficial ownership information.[7] A number of national beneficial ownership registers are already active. In 2016, for example, the United Kingdom launched a public beneficial ownership register, referred to as the people with significant control (PSC) register. In May, the country's parliament adopted legislation requiring the beneficial owners of companies registered in UK overseas territories to be disclosed on public registries by the end of 2020.

What these policies and platforms have in common is their breadth: they apply to anyone opening a bank account or any company pursuing registration. This broad scope is critical, as governance challenges related to beneficial ownership cut across jurisdictional and sectoral lines. However, certain sectors in which particular corruption and IFF risks are especially acute warrant more targeted approaches.

The extractive sector represents such a high-risk circumstance. Another high-risk sector is luxury real estate. After the *New York Times* reported that international buyers, some of whom were under investigation in various international jurisdictions, were using shell companies to purchase expensive Manhattan apartments, the U.S. Department of the Treasury began requiring title insurance companies to collect beneficial ownership information about buyers making all-cash purchases of high-value residential real estate in certain cities and counties.[8] The department has indicated that cases involving foreign corrupt officials informed the establishment of this policy and the focus on certain sought-after locations, including New York City and counties in California, Florida, Hawaii, and Texas.[9] Following similar news coverage about hidden ownership of real estate in London, the United Kingdom recently announced that foreign entities that own UK real estate will need to publicly disclose beneficial owners on the PSC register by 2021.

TRANSPARENCY ONLY A STARTING POINT

The push to raise global awareness about the risks of hidden beneficial ownership has gained ground largely due to compelling cases emerging at critical moments, as with the Panama Papers leak and Global Witness' coverage of the OPL 245 case, combined with the clarity of messaging on the need to increase transparency.[10]

The disclosure of beneficial ownership information is certainly an essential starting point in the fight against IFFs. Basic building blocks—such as a comprehensive legal definition of "beneficial owner" and timely mechanisms to systematically collect, update, and preserve information on changes in beneficial ownership—need to be put in place for an effective transparency regime. However, as with any transparency measure, beneficial ownership disclosures will be most useful if they advance efforts to deter, detect, and penalize illegal conduct. Thus, mechanisms that require companies to disclose their beneficial owners will likely do more to curb corruption and IFFs if they are complemented by

- government and company policies that define and prohibit certain inappropriate beneficial ownership interests (e.g., stakes that create conflicts of interest);
- active screening of beneficial ownership information for risk factors indicating potential corruption;
- workable systems for verifying the accuracy of disclosed information; and

- reliable enforcement of sanctions when illegal activities are identified.

Verification and due diligence are already part of many beneficial ownership norms and policies, especially with respect to financial institutions. However, more broadly, the screening and verification of beneficial ownership information remain insufficient. Transparency International recently found that no G20 country requires authorities to verify the beneficial ownership information collected in company registers.[11]

Verifying beneficial ownership information can be challenging. In the award of extractive licenses, administrators may be unable to locate conclusive evidence that a PEP is or is not a hidden beneficial owner of a company when seeking to verify information that companies have provided. Given these challenges and in light of limited resources within government agencies tasked with reviewing beneficial ownership information, a targeted and risk-based approach should be considered for certain sector-specific applications.

Utilizing such an approach in the extractive sector could mean that in-depth verification measures are triggered when preliminary screening indicates manifest deficiencies in submitted beneficial ownership information (e.g., a company claims it has no beneficial owner or that its beneficial owner cannot be identified, or a company identifies another company as the ultimate beneficial owner) or if other risk factors indicate suspicious activity (e.g., a company fails to meet technical or financial criteria but is still shortlisted or awarded government contracts). The World Bank has recently launched a manual that outlines good practices utilizing a risk-based approach to improve integrity due diligence in extractive licensing processes, including regarding beneficial ownership.[12]

CROSS-SECTORAL, INTERAGENCY, AND CROSS-JURISDICTIONAL COORDINATION NEEDED

Implementing effective deterrence, screening, verification, and enforcement measures will require legal frameworks and data platforms that cut across commercial sectors, agency mandates, and national jurisdictions, yet still leave flexibility for customization to meet particular challenges and risks in specific administrative and sectoral contexts. A case involving corruption and IFFs often includes registering a company, opening a bank account, obtaining a government license or contracts, and purchasing real estate, all as part of a single corrupt endeavor taking place across several countries. Awareness that problematic beneficial ownership relationships can be concealed at each of these stages in a transaction offers an opportunity to build linkages among the incorporation, banking, extractive sector, and real estate spheres.

Commercially, a unified front across these spheres could increase global pressure on legal, financial, and other service providers to develop stronger professional codes of ethics, better customer due diligence frameworks, and improved risk assessment mechanisms to reduce the extent to which these intermediaries enable inappropriate or illegal beneficial ownership linkages. Coordinated efforts could demand more proactive industry leadership from publicly listed companies, which generally do not make stand-alone beneficial ownership disclosures in light of their distributed ownership but which often partner with privately held companies and could exert commercial pressure for improved transparency. Such coordination would also be critical to fulfilling the potential and managing the risks that frontier tools, such as blockchain and other distributed ledger technologies, could eventually bring to tracking beneficial ownership information.

At the country level, interagency coordination and information-sharing could also help spread some administrative burdens and financial costs associated with screening and verification, although additional specialized review and evaluation would likely still be required to meet certain agency-specific screening needs and timelines. Such coordination could also help distribute the political will needed to tackle challenges related to problematic beneficial ownership linkages, especially given that power differentials can vary widely among the relevant agencies, including the registrar general, financial intelligence unit, banking regulator, mining and oil ministries, anticorruption agency, and law enforcement.

In the area of sanctions, establishing legal prohibitions on self-dealing, conflicts of interest, and bribery are foundational for beneficial ownership information to help curb corruption and IFFs. If a country's laws allow a company to give an official a beneficial ownership stake in exchange for an oil license or if a mining minister can lawfully award a mining license to a close family member's company, then disclosures of such companies' beneficial owners could raise questions among citizens or journalists about the appropriateness of such behavior but fail to offer concrete mechanisms to prevent such self-dealing.

Thus far, sanction efforts have relied on anti-bribery legislation in the home countries of extractive companies, notably the Foreign Corrupt Practices Act in the United States. Enforcement of such home-country legislation remains critical. But given that many resource-rich countries are undertaking legal reforms to embed beneficial ownership transparency in their extractive sectors, a real opportunity exists to address underlying anticorruption policy gaps in these host countries at the same time. This would mean establishing clear prohibitions on certain PEPs holding extractive company interests that present conflict-of-interest risks and on companies seeking linkages with PEPs that raise corruption concerns. NRGI, for instance, has developed model legal provisions that can help countries incorporate such anticorruption provisions into extractive licensing guidelines, along with template provisions on collecting and publishing beneficial ownership information as part of license applications, screening beneficial ownership information in applications for manifest accuracy and corruption problems, and scrutinizing corruption risks in selected awardees.[13]

Transnationally, broader coordination across these spheres would be valuable around standard-setting and information-sharing and could help alleviate some of the mixed messaging regarding best practice noted below. Stronger anticorruption legal frameworks that span both home country and host country legislative frameworks would not only provide clearer guidance to well-intentioned officials and companies about what constitutes inappropriate beneficial ownership linkages but also lay the groundwork for better enforcement against officials and companies that cross the line. On the data front, the global beneficial ownership register and data standard are good examples of platforms and standards that facilitate broad international coordination. More broadly, increased coordination on beneficial ownership regimes is also warranted among international organizations focused on tax evasion and those with a corruption focus.

PRIORITIZATION AND PHASED APPROACHES NEEDED

At the same time, broad efforts on beneficial ownership transparency and scrutiny need to be tempered with a recognition of sector- and country-level differences and needs. One pragmatic reason for this is the difficulty of getting many countries and sectors to agree on what constitutes best practice. This is already an issue for beneficial ownership transparency.

In some contexts, for instance, transparency standards mandate proactive public disclosure of beneficial ownership information, while in others sharing such information only among relevant authorities or upon request is considered sufficiently transparent. These differences can exist even among similar mechanisms: beneficial ownership disclosures related to luxury real estate in the United States are only shared with relevant authorities, while the United Kingdom plans to make such information public. Similarly, the United Kingdom has built a national register of beneficial owners that is public, but the beneficial ownership register being considered in the United States under the draft Counter Terrorism and Illicit Finance Act entails access only for relevant authorities. Similar differences exist among broader regional and international norms, as beneficial ownership standards promoted by FATF and the G20 focus on accessibility for relevant authorities, while EU and EITI standards require public disclosure.

Defining a single approach to best practice can be difficult because beneficial ownership information plays a role in tackling different governance challenges, in different institutional contexts, and on different timelines. How a registrar general would seek to collect and use beneficial ownership information when reviewing a company's application to register a company differs from how a bank would seek to gather and analyze such information when conducting due diligence for an account applicant, which in turn differs from how a mining ministry would obtain and consider such information when seeking to reduce conflict of interest risks during mining license allocations. Greater assessment is needed about what these varied approaches to using beneficial ownership information have in common and how harmonized legal policies and centralized data platforms can support coordination on these shared aspects, as well as increased understanding of how sectoral needs differ and what sorts of flexibility and customization will be essential.

Adding to this complexity, many of the countries trying to roll out new beneficial ownership norms face major political, technical, and financial constraints that make it difficult to implement multifaceted beneficial ownership plans that seek to tackle multiple policy objectives. Given such limitations and facing a bombardment of mixed messages about how best to collect and use beneficial ownership information, a real risk exists of countries implementing a grab bag of half measures that expend considerable resources but are too diffuse to have any real effect on reducing corruption.

For example, resource-rich countries are already grappling with how to allocate resources to meet FATF requirements on beneficial ownership information-sharing among relevant authorities while also meeting public beneficial ownership disclosure requirements under EITI. The momentum and buzz around registers in the United Kingdom and European Union have resulted in some EITI countries pursuing national beneficial ownership registers that cover all sectors. While such ambitious plans should be supported, starting with a targeted effort to collect and publish beneficial ownership information regarding extractive license-holders and applicants could prove to be more risk-responsive and rapid in terms of legal reforms and practical implementation.

To mitigate the current mixed messaging about best practice, international standard-setting bodies that promote beneficial ownership disclosure should coordinate more on global messaging and country-level planning. Such coordination would need to occur regarding legal policies, as well as data standards and platforms. On the policy front, clarity of global messaging would be greatly enhanced if international bodies that focus on beneficial ownership information-sharing among relevant authorities proactively indicated support for countries that choose to establish public disclosures, even if such bodies do not focus on public disclosure in their own efforts.

In countries with limited financial and human resources, planning around beneficial ownership transparency should include consideration of the following coordination and prioritization options:

- convening an interagency coordination committee that includes agencies that work on incorporation, banking, and the extractive sector, as well as relevant anticorruption and law enforcement agencies;
- prioritizing public beneficial ownership disclosure in the sectors that present the most pressing potential corruption risks and economic losses, and ensuring that the ultimate use of such disclosures to tackle these governance challenges is what shapes the planning process;
- maximizing harmonization and interoperability across core components of beneficial ownership legal frameworks and data platforms (e.g., beneficial owner definitions and company identifiers) while enabling flexibility for sector-specific customization or additions to meet particular agency needs and contexts; and
- developing a phased approach to broadening beneficial ownership transparency coverage as resources and capacity increase.

ENDNOTES

1. There is also considerable interest in the role that hidden beneficial ownership can play in tax avoidance and tax evasion in the extractive sector and more broadly. While this angle is worth continued exploration, especially with respect to transparency about full corporate affiliation hierarchies, it is not the focus of this paper.
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