

CORPORATE TRANSPARENCY AND REGISTER REFORM CONSULTATION

Submission from Transparency International UK to the Department for Business, Energy & Industrial Strategy's (BEIS) consultation on corporate transparency and register reform

Transparency International UK (TI-UK) welcomes this consultation as an opportunity for the Government to address weaknesses that allow criminals to access UK companies and abuse them with impunity.

There is now a wealth of evidence showing how UK companies have been used to facilitate corruption and launder illicit wealth.¹ Their ease of incorporation and the lack of checks on information submitted to Companies House continue to render these legal entities vulnerable to abuse despite improvements to the UK's corporate transparency regime. The 2018 Financial Action Taskforce (FATF) mutual evaluation review of the UK identified the lack of verification of company information as a key weakness in Britain's response to money laundering.² This loophole should be closed as part of wide-ranging reforms to UK corporate transparency and Companies House.

KEY RECOMMENDATIONS

Providing accurate, public company data is critical to deterring criminals from using UK legal entities for financial crime and would help secure Britain's position as a world leader in corporate transparency. Achieving this requires three key areas of reform:

1. **Protecting against the abuse of UK legal entities through verifying company data:** It is imperative that checks are introduced both on the identities of those seeking to run UK companies as well as the veracity of the information they submit.
2. **Detecting and pursuing potential false reporting through an empowered Companies House:** Using analysis of UK company data as well as the information it receives from other sources, Companies House should be empowered to investigate breaches of the transparency rules with appropriate sanctioning powers to provide a credible deterrent against non-compliance.
3. **Reducing the avenues for criminal activity by closing loopholes and increasing transparency:** The use of opaque corporate partners and nominees should be curbed with greater levels of public information on where companies hold bank accounts.

As the UK seeks to renegotiate its relationship with the EU and takes a new place in the world, the Government should act quickly to implement these changes to protect the Britain's reputation as a safe business environment and a global leader of corporate good governance.

¹ Transparency International UK, *Offshore in the UK: Analysing the use of Scottish Limited Partnerships in Corruption and Money Laundering*, (June 2017) <https://www.transparency.org.uk/publications/offshore-in-the-uk/>; Transparency International UK, *Hiding in Plain Sight: How UK Companies are used to launder Corrupt Wealth* (November 2017) <https://www.transparency.org.uk/publications/hiding-in-plain-sight/>; Global Witness, *The Companies We Keep: What the UK's open data register tells us about company ownership* <https://www.globalwitness.org/en/campaigns/corruption-and-money-laundering/anonymous-company-owners/companies-we-keep/#chapter-0/section-1>

² FATF, *Mutual Evaluation Report of the United Kingdom* (2018) <https://www.fatf-gafi.org/publications/mutualevaluations/documents/mer-united-kingdom-2018.html>

1. Protecting against the abuse of UK legal entities through verifying company data

TI-UK welcomes the ambition for Companies House to verify the identity of those involved in owning and running UK companies. This would represent an important step in preventing criminals accessing UK legal entities. Verifying information submitted to Companies House should help increase the accuracy and reliability of the register by:

Reducing the potential for the fraudulent use of identities: requiring supporting documentation to register information at Companies House should make it more difficult criminals to steal the identities of innocent individuals and companies to facilitate financial crime.

Protecting against the incorporation of companies for criminal purposes: requiring supporting documentation from those incorporating and controlling UK legal entities, either directly or through regulated Trust and Company Service Provider (TCSPs), should help identify those suspected or known to be involved in financial crime.

Pursuing deliberate false reporting: documentation gathered from this exercise can help identify, investigate and pursue deliberate false reporting.

Whose identification should be verified

Supporting documentation should be required from directors, shareholders and people with significant control (PSC) to help authenticate their identities. This should apply to both natural persons and legal entities.

Companies House should use this data to create unique identification numbers for those acting as directors, shareholders and PSCs of UK companies, allowing the public and law enforcement agencies a holistic view of their UK corporate footprint. This would allow the identification of suspicious activity, for example, individuals who are directors and/or PSCs of thousands of companies. Currently, this analysis is impossible because the lack of controls on information accepted by Companies House, and shareholder data being unavailable.

Directors should not be recorded on the register or have any legal rights or responsibilities in relation to a company until their identity is verified. We recognise that the exact same approach cannot be taken for PSCs who are not also directors or shareholders because their information is not included on incorporation. Those PSCs who have not undergone this verification process should be required to submit the relevant documentation with or prior to the first confirmation statement after they have become a PSC. Those that have not been verified in the period leading up to their confirmation statement should be flagged on the public Companies House register to make data users aware of the uncertainty surrounding the PSC's identity. PSCs who have failed to submit relevant documentation for verification by the time their company's confirmation statement is due should face sanctions as a deterrent against wilful non-compliance, for example, having their company frozen or being subjected to civil monetary penalties.

We also recognise that requiring the verification of shareholders from companies owned by a large number of small investors could provide an administrative burden that is disproportionate to the risk of financial crime.³ Provision could be made to allow for optional verification in these circumstances, with a flagging system to identify those who have and have not had their identities supported by official documentation. We think this is a more

³ The exact threshold for exemption could be determined through secondary legislation.

targeted approach to addressing the challenges identified in the consultation document.⁴ However, given that the overwhelming number of UK legal entities have a small number of shareholders,⁵ it would not seem disproportionately burdensome to require the vast majority of companies to have their shareholders verified on a compulsory basis (where they have not already been verified as a PSC).

How identification should be verified

The proposals below recognise there are currently two avenues for incorporating legal entities in the UK: direct incorporation via Companies House and indirect incorporation via regulated TCSPs. In both avenues, there should be verification of the identities for both natural persons and companies involved in the management and ownership of UK legal entities. Individuals should be required to provide official documentation, such as their passport or driving licence, for verification purposes. Legal entities should be required to provide official records demonstrating their incorporation and active status, including their jurisdiction of incorporation and company registration number.

We acknowledge that this consultation is soliciting views on the use of technological solutions to help authenticate the identity of individuals, which could be particularly beneficial where a potential director or shareholder does not hold any other form of official documentation. However, it is not clear whether under the current proposals Companies House will also be able to use data within the wider public sector to help undertake this task, or whether they would just use the same methods as regulated TCSPs. We think it should have access to this data for verifying individuals' identity however note that this could create a difference in the quality of checks undertaken depending on the avenue for incorporation.

We agree with the Government's proposed approach that companies should not be incorporated if any of their director's details have not been verified and appointments being conditional on the verification of director's identities.

Direct Incorporation via Companies House

UK legal entities that are incorporated directly without the involvement of a third party should have the information of directors and shareholders verified by Companies House. This should include cross referencing supporting documentation against a number of datasets including the Driver and Vehicle Licensing Agency (DVLA) database, National Insurance data and credit reference databases, to authenticate their identity.

To identify potential red flags for money laundering, Companies House should make use of available resources, for example risk intelligence databases, open source research and reported discrepancies from the private sector. As is required of TCSPs working for clients, this Know Your Customer exercise should include looking out for companies being incorporated on behalf of Politically Exposed Persons (PEPs), or for individuals or organisations on international sanctions lists. This would necessitate a change to the powers and functions of Companies House, which we have elaborated on below.

Indirect incorporation via regulated TCSPs

TCSPs should share with Companies House the underlying data from verification checks they have carried out. This will help give confidence in the authenticity of the identities they

⁴ Department for Business, Energy & Industrial Strategy (BEIS), *Corporate transparency and register reform* (May 2019) Paragraph 114 p.37

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/819994/Corporate_transparency_and_register_reform.pdf

⁵ Companies register activities: statistical release 2018 to 2019 <https://www.gov.uk/government/statistics/companies-register-activities-statistical-release-2018-to-2019>

report to Companies House and enable it to create a unique identification number for these individuals and entities for the public register.

Only TCSPs regulated in the UK or in jurisdictions with at least equivalent regulatory standards should be able incorporate and maintain UK legal entities. This should introduce higher levels of accountability for information submitted to Companies House and mitigate against severe money laundering risks from jurisdictions with woefully inadequate anti-money laundering (AML) laws and implementation.

TCSPs incorporating UK legal entities would need to provide proof of their AML registration on any documents they submit to Companies House, for example, proof of registration with an AML supervisor. For UK supervised firms, this could be validated against a pre-populated list of registration details obtained from AML supervisors, so only those officially signed-up with a UK AML supervisor are allowed to incorporate via Companies House.

Information on those individuals responsible for managing companies within TCSPs could also be collected and published to provide greater assurance in who specifically was responsible for the incorporation process.⁶

2. Detecting and pursuing potential false reporting through an empowered Companies House

Companies House must be empowered to ensure the accuracy of the data it holds, which will require an increase in its mandate and functions. Its current statutory powers under Part 35 of the Companies Act 2006 ('Companies Act') require it to accept documents and not to scrutinise their accuracy. In reality, the expectation and necessity is that Companies House has a similar remit and set of powers and sanctions akin to other statutory regulators managing official registers, such as the Charities Commission⁷ and the Electoral Commission,⁸ in order to ensure the information it maintains is trustworthy.

To enable it to provide greater confidence in the integrity of the register, Companies House should be given the statutory responsibility for monitoring and ensuring compliance with company law, which would include:

- Administering the register to provide an accurate and current view of companies incorporated and operating in the UK.
- Providing advice and guidance to those incorporating or maintaining UK legal entities in order to help ensure high levels of compliance amongst those willing to abide by the law.
- Monitoring compliance with the rules, including an intelligence function to proactively identify intentional non-compliance and cooperate with law enforcement agencies if there is evidence of a criminal offence, and a risk assurance function to help direct resources effectively to where they are likely to have the biggest impact.
- Enforcing the rules and creating a credible deterrent against non-compliance through enhanced powers to investigate potential non-compliance and the transparent and proportionate use of effective sanctions, which should include the power to strike-off companies and impose civil monetary penalties.

Some of this is already undertaken by Companies House however there are some notable areas where reform is needed.

⁶ Including the name and address of the TCSP and the individual responsible for submitting documents to Companies House.

⁷ Section 15, Charities Act 2011 <https://www.legislation.gov.uk/ukpga/2011/25/section/15>

⁸ Section 145, Political Parties, Elections and Referendums Act 2000 (PPERA) <https://www.legislation.gov.uk/ukpga/2000/41/section/145>

Monitoring compliance

The use of UK companies in corruption and associated money laundering mean that Companies House is a major partner in the fight against financial crime. Therefore, its activities should go beyond reviewing the timeliness of the information it receives to helping those who are responsible for policing the UK's money laundering regulations and more serious breaches of substantive money laundering offences. We recognise that it has made positive steps to make better use of the information it holds to identify potential breaches of corporate transparency requirements, and encourage this to become a core aspect of its role in monitoring compliance with the law.

We support the creation of proportionate legal gateways to facilitate the exchange of information gathered through this monitoring process with relevant law enforcement and supervisory agencies. For example, this could include analysis to support the Joint Financial Analysis Centre (JFAC), which is hosted at the National Crime Agency (NCA). We have provided some suggestions below how analysis by Companies House can help it fulfil this new statutory function and support the work of law enforcement agencies in tackling financial crime.

Identifying suspicious networks of companies and rogue TCSPs

There is a wealth of information in the public domain that can be combined with data collected by Companies House⁹ to identify networks of suspicious legal entities and rogue TCSPs facilitating criminal activity. For example, there are known individuals and companies who have repeatedly helped to incorporate and manage UK legal entities that have been involved in high-level corruption and money laundering. Combining this knowledge with data collected on TCSPs and analysis of common red flags – for example, large numbers of companies registered to the same address with opaque corporate structures – should help direct law enforcement agencies and AML supervisors towards potential regulatory and criminal non-compliance.

Assessing the veracity of PSC statements

Company shareholder data could be utilised to a greater degree to cross-check the veracity of PSC statements. Currently, this data is not held in a standardised format and would require legislation to change how shareholder data is currently submitted and held. To enable this form of automated check, shareholder data would need to be submitted in a way to allow it to be published in a machine readable format on at least an annual basis. These disclosures could be submitted in conjunction with the company confirmation statement.

Companies House could also cross reference this shareholder data with that on the UK's Trusts Register held by HM Revenue and Customs (HMRC). Anomalies could be identified in UK companies which featured in both datasets, for example, legal entities listed as settlors, trustees or beneficiaries of trusts, or HMRC registered trusts that are PSCs of UK entities.

As more countries introduce public beneficial ownership registers, Companies House will be able to analyse overlaps between the UK and overseas registers, for example, overseas companies that hold shares in UK companies. This provides another source to help check the validity of PSC statements.

Identifying discrepancies

Government has committed to implementing the EU's Fifth Money Laundering Directive (5MLD), meaning it must introduce the necessary legislation to transpose it into UK law

⁹ We envisage this will include information Companies House collects as part of its new due diligence checks on those incorporating legal entities directly.

before January 2020.¹⁰ 5MLD includes provisions requiring regulated entities, such as banks and TCSPs, to report anomalies between PSC data available to them and that on the company register. Governments are also required under 5MLD to take ‘appropriate actions’ to resolve anomalies in a timely manner, potentially flagging the anomaly in the register in the interim.¹¹

We welcome the introduction of these requirements as an additional check on data accuracy; however, how this will be implemented in practice is yet to be confirmed. Getting this right is key to improving the quality of information that is submitted and maintained on the register. We have already provided some proposals to HM Treasury as part of its consultation on 5MLD implementation on how this could work in practice.¹²

Identifying ‘nominee’ PSCs and shareholders through the use of unique identifiers

By assigning every officer, shareholder and PSC with a unique identifier, it will be much easier to identify individuals and companies who control an unusually high number of UK legal entities and, therefore, are probably a nominee. At the moment, this can only be checked through manual or semi-manual data matching exercises where the names of officers and PSCs across numerous companies are similar, which is time-consuming and not always accurate.

Identifying false Relevant Legal Entities (RLEs)

UK companies listed as corporate PSCs should be validated against the company numbers they supply to ensure they are actually registered with Companies House. Foreign corporate PSCs should provide their company numbers which could then be checked (for example, through third-party aggregators such as OpenCorporates) and their ticker symbols (an identification code for a stock) if it is listed on a relevant stock exchange to verify if they are Relevant Legal Entities (RLE)s. Where RLEs fail this validation test it should automatically trigger further investigation.

Enforcing the rules

Creating a credible deterrent against submitting false information is key to providing a more accurate and reliable register. Current enforcement levels against filing false or inaccurate data are unlikely to deter individuals seeking to avoid naming a PSC. The first ever prosecution for filing false information came in March 2018 for a formation agent who purposefully set-up companies with incorrect information to highlight how easily this could be done – drawing this to the authorities’ attention in the process.¹³ Since then there has been little public information on further prosecutions despite there being a sizeable number of entities who appear to be purposefully evading the new rules. This indicates an inadequate deterrent against wilful non-compliance, which undermines confidence in the integrity of the register.

We think there are two key deficiencies in the UK’s approach to enforcing the transparency requirements of the Companies Act.

¹⁰ HM Treasury, *Transposition of the Fifth Money Laundering Directive: consultation* (April 2019) https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/795670/20190415_Consultation_on_the_Transposition_of_5MLD_web.pdf

¹¹ European Union Parliament and Council, *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*, Article 30, Paragraph 4 <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32015L0843>

¹² Transparency International UK, *Submission to the HM Treasury consultation on the UK’s implementation of the EU’s Fifth Money Laundering Directive* (June 2019) <https://www.transparency.org.uk/publications/ti-uk-government-5mld-implementation-consultation/>

¹³ <https://www.gov.uk/government/news/uks-first-ever-successful-prosecution-for-false-company-information> [Accessed 30 July 2019]

Firstly, Companies House has no statutory powers to investigate potential non-compliance, with most of its existing powers merely relating to the format in which it receives information from companies or amendments it can make to the register. This reflects its current role as a recipient of information instead of an active guardian of company information. Without the powers to require the disclosure of documents or provide evidence, it will have to rely on the inquiries of others to establish the facts surrounding alleged breaches of the rules.

Secondly, there is an over-reliance on criminal offences as a sanction for non-compliance. As raised by both Professor Richard Macrory over a decade ago¹⁴ and the Law Commission more recently,¹⁵ there are significant questions about relying solely or heavily on criminal offences to achieve effective regulatory outcomes. Doing so inevitably creates an enforcement gap whereby the law is broken, but pursuit of a minor breach through the courts deemed too expensive or disproportionate to the offence being committed, leaving the law unenforced. We agree with the Law Commission's draft proposal that "[criminal offences] should not be used as the primary means of promoting regulatory objectives"¹⁶ and that Companies House requires a new suite of civil sanctions to help it provide proportionate and effective deterrents against more administrative non-compliance.

3. Reducing the avenues for criminal activity by closing loopholes and increasing transparency

We are not opposed to the measures proposed in the consultation document that seek to deter the misuse of UK companies; however, we think three measures in particular should help reduce the avenues for criminal misuse of UK legal entities.

Reforming the use of offshore corporate officers

The use of corporate directors and partners to control UK legal entities represents an ongoing vulnerability to the UK's corporate transparency regime. It remains possible to control Limited Liability Partnerships (LLPs) and Limited Partnerships (LPs) solely through offshore corporate officers registered in secrecy jurisdictions like the Seychelles and Belize, where there is little public information about companies and their beneficiaries. We have seen this opaque structure used on an industrial scale to facilitate illicit financial flows. Similar methods using at least one corporate director have also been used to exploit private limited companies for criminal activity.

As we noted in our 2018 submission to BEIS' consultation on limited partnership reform, the abuse of opaque corporate directors was a primary driver for requiring limited companies to have at least one natural person as an officer.¹⁷ There also are provisions in the Small Business, Enterprise and Employment Act 2015 that would have ended the use of corporate partners for private limited companies.¹⁸ It is clear that corporate officers remain an avenue to abuse UK legal entities, yet the 2015 reforms remain un-commenced and there is no equivalent reform of LPs and LLPs, which have been misused on an industrial scale.

Government should legislate to prohibit the use of corporate partners in most circumstances for UK legal entities.

¹⁴ Professor Richard B. Macrory, *Regulatory Justice: Making Sanctions Effective* (November 2006)

<https://webarchive.nationalarchives.gov.uk/20121205164501/http://www.bis.gov.uk/files/file44593.pdf>

¹⁵ The Law Commission, *Criminal Liability In Regulatory Contexts: A Consultation Paper* (August 2010) https://s3-eu-west-2.amazonaws.com/lawcom-prod-storage-11jxou24uy7g/uploads/2015/06/cp195_Criminal_Liability_consultation.pdf

¹⁶ The Law Commission, *Criminal Liability In Regulatory Contexts* paragraph 8.1 p.147

¹⁷ Transparency International UK, *Consultation Submission: Reform of Limited Partnership Law* (July 2018) p.2

<https://www.transparency.org.uk/publications/beis-limited-partnership-consultation/>

¹⁸ <http://www.legislation.gov.uk/ukpga/2015/26/part/7/crossheading/corporate-directors/enacted>

Introducing a cap on directorships

We strongly support the introduction of a cap on the number of directorships that can be held by any one individual. Our research has shown nominee directors to be a common component of money laundering schemes to obfuscate the true owners of UK limited companies.¹⁹ For example, we have carried out analysis on the officers of more than 560 LLPs involved in money laundering. Some of the natural persons registered as officers for these entities were the directors for hundreds of other companies on the UK register. One particular individual, for example, had been an officer for 568 UK legal entities. A cap of 25 directorships appears to be a reasonable limit that would prevent widespread abuse whilst still allowing innocent individuals to run a large number of legitimate businesses.

Requiring information on the jurisdiction of legal entities' bank accounts

Information on the jurisdiction of a company's bank accounts would be useful for identifying suspicious activity that is indicative of financial crime. In recent years, various exposés by journalists, like the Organised Crime and Corruption Reporting Project (OCCRP),²⁰ Private Eye²¹ and The Herald,²² have shown how LPs and LLPs have been used in conjunction with accounts from Baltic banks with weak AML measures to move large amounts of illicit funds out of the former Soviet Union. Making this information publicly available would have made this systemic abuse of UK corporate entities easier to spot and reduced the attractiveness of them as vehicles for illicit financial flows.

Government should consider bringing in a requirement for UK entities to report certain bank account information to Companies House, some of which could be made public. This could include whether the company has a UK bank account, and the jurisdiction of any overseas bank accounts. This would allow law enforcement, the regulated sector and civil society to identify suspicious activity – for example, tens of thousands of companies being incorporated during a short period by one TCSP with bank accounts in jurisdictions with a poor AML checks – much earlier than is currently the case and subject it to scrutiny.

¹⁹ Transparency International UK, *Hiding in Plain Sight* p.25

²⁰ <https://www.occrp.org/en/laundromat/> [Accessed 31 July 2019]

²¹ <https://www.private-eye.co.uk/special-reports/where-theres-muck> [Accessed 31 July 2019]

²² <https://www.heraldsotland.com/news/16122937.latvia-strikes-blow-against-scotlands-secrecy-firms/> [Accessed 31 July 2019]

ABOUT TRANSPARENCY INTERNATIONAL UK

Transparency International (TI) is the world's leading non-governmental anti-corruption organisation. With more than 100 chapters worldwide, TI has extensive global expertise and understanding of corruption.

Transparency International UK (TI-UK) is the UK chapter of TI. We raise awareness about corruption; advocate legal and regulatory reform at national and international levels; design practical tools for institutions, individuals and companies wishing to combat corruption; and act as a leading centre of anti-corruption expertise in the UK.

We work in the UK and overseas, challenging corruption within politics, public institutions, and the private sector, and campaign to prevent the UK acting as a safe haven for corrupt capital. On behalf of the global Transparency International movement, we work to reduce corruption in the high risk areas of Defence & Security and Pharmaceuticals & Healthcare.

We are independent, non-political, and base our advocacy on robust research.

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