SHELL COMPANIES AND EXPOSING BENEFICIAL OWNERSHIP: TESTING THE BOUNDARIES OF THE INTERNATIONAL COMMITMENT TO FIGHT CORRUPTION

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Corporate vehicles are used by corrupt actors because they obscure the real person, the 'beneficial owner', behind transactions, thereby enabling the evasion of anti-corruption laws and regulations. This paper argues that while the Australian and international communities have addressed the misuse of corporate vehicles and their role in facilitating transnational corrupt activity, they have not done so in a meaningful way. Shell companies, in particular, continue to function as an 'iron curtain', behind which corrupt activity is hidden. This paper nevertheless proposes that this deficiency can be rectified and a culture of compliance at the international level built.

This paper first explores the current international legal response to this particular issue in the transnational corruption space and demonstrates that there is a significant disconnect between states' rhetorical commitment to fight the use of corporate vehicles in corrupt transactions and their practical implementation of anti-corruption measures. This paper uses Australia as a case study to illustrate this argument. It then engages with the possible reasons for the disconnect between rhetoric and practice, proposing that the disconnect largely flows from flaws in the international legal obligations themselves rather than from the actions of states. This paper suggests a way to meaningfully engage with the issue. It advocates for the adoption of a strategy of 'strategic privatisation', a development within the law in the broad area of transnational anti-corruption regulation, and for the application of that strategy to the narrower issue of the exploitation of corporate vehicles.

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I INTRODUCTION

> The corporate veil need not be an iron curtain.[1]

Transnational corruption is an 'aggressive cancer to development'[2] and an international crime with devastating social and economic consequences. It is a 'driving force of civil conflict, poverty and famine',[3] resulting in weakened economic development and growth,[4] an erosion of societal equality,[5] and the destruction of both democratic institutions and the rule of law.[6] It is a complex and widespread phenomenon and it requires multifaceted regulatory responses.

This paper examines only one aspect of that wider picture: the use of corporate vehicles to undertake and facilitate corrupt transactions. Corporate vehicles are used by corrupt actors because they obscure the real person, the 'beneficial owner', behind transactions, thereby enabling the evasion of anti-corruption laws and regulations. This paper argues that this particular issue in the transnational corruption space has not been addressed either by Australia or by the international community in a meaningful way. But it also proposes that this deficiency can be rectified with an understanding that, while corporate vehicles play an essential role in the Australian and global economic systems, '[t]he corporate veil need not be an iron curtain'.[7]

To support this argument, how corporate vehicles are used to facilitate corrupt activity across borders is explained first and an argument for international law as a governing body of law in this space then made. The current international response is then considered. This paper demonstrates that the existence of international legal obligations has resulted in little more than a relatively superficial addressing of the issue. While states have now, by and large, committed

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1 Tom Spencer, 'Finding the Wisdom of Salomon' (2012) 40(2) *Australian Business Law Review* 64, 75. See also *Wallersteiner v Moir* [1974] 1 WLR 991, 1013 (Lord Denning MR).

2 Glenn T Ware and Gregory P Noone, 'The Anatomy of Transnational Corruption' (2005) 14(2) *International Affairs Review* 29, 43.

3 Ilias Bantekas, 'Corruption as an International Crime and Crime against Humanity: An Outline of Supplementary Criminal Justice Policies' (2006) 4(3) *Journal of International Criminal Justice* 466, 484. See also ibid (n 2) 29, quoting UN GAOR, 58th sess, 50th plen mtg, UN Doc A/58/PV.50 (31 October 2003) (Kofi Annan, Secretary-General) 12–13; Kath Hall, 'Strategic Privatisation of Transnational Anti-Corruption Regulation' (2013) 28(1) *Australian Journal of Corporate Law* 60, 61–2.

4 Nikolay A Ouzounov, 'Facing the Challenge: Corruption, State Capture and the Role of Multinational Business' (2004) 37(4) *John Marshall Law Review* 1181, 1182. See also Patrick X Delaney, 'Transnational Corruption: Regulation Across Borders' (2007) 47(2) *Virginia Journal of International Law* 413, 419; Paolo Mauro, 'The Effects of Corruption on Growth, Investment, and Government Expenditure: A Cross-Country Analysis' in Kimberly Ann Elliott (ed), *Corruption and the Global Economy* (Institute for International Economics, 1997) 83, 86; Susan Rose-Ackerman, 'The Political Economy of Corruption' in Kimberly Ann Elliott (ed), *Corruption and the Global Economy* (Institute for International Economics, 1997) 31, 44–5.

5 Delaney (n 4) 419.

6 Duane Windsor and Kathleen A Getz, 'Multilateral Cooperation to Combat Corruption: Normative Regimes Despite Mixed Motives and Diverse Values' (2000) 33(3) *Cornell International Law Journal* 731, 757. See also Brian C Harms, 'Holding Public Officials Accountable in the International Realm: A New Multi-Layered Strategy to Combat Corruption' (2000) 33(1) *Cornell International Law Journal* 159, 166; Delaney (n 4) 420–1; Martin Krygier, 'Ethical Positivism and the Liberalism of Fear' (1999) 24 *Australian Journal of Legal Philosophy* 65, 71.

7 Spencer (n 1) 75.

to stopping the exploitation of corporate vehicles, and significant progress has recently been made, this has not always translated into practice. Australia is used as a case study. This paper then suggests a possible explanation for the disconnect between rhetoric and practice, and an argument is made that it largely comes from flaws in the international legal obligations themselves, as opposed to the actions of states. This paper suggests a potential pathway for meaningful engagement with the issue. It advocates for the adoption of a strategy of 'strategic privatisation', which is a development within the law in the broad area of transnational anti-corruption regulation,[8] and the subsequent application of that strategy to the narrower issue of the exploitation of corporate vehicles.

II A PLACE FOR INTERNATIONAL LAW

It is necessary first to understand exactly how corporate vehicles are used to facilitate corrupt activity across borders. This section explains this and outlines why international law and regulation are the best responsive tools to deal with the issue. The concept of 'corruption' is, of course, complex, but the references to 'corruption' here should be understood very broadly as 'behavior which deviates from the formal duties of a public role because of private-regarding … pecuniary or status gains; or violates rules against the exercise of certain types of private-regarding influence'.[9]

'Transnational corruption' is a narrower term. It excludes those transactions which only take place within state boundaries.[10] It is 'corruption that crosses borders, involves corporate and state actors, and employs sophisticated and grand schemes to siphon the wealth of a developing country from its rightful owners: the people of the country'.[11]

A *Corporate Vehicles, Beneficial Owners and Transnational Corruption*

The most common corporate vehicles are: (i) *shell companies*: non-operational legal entities with 'no independent operations, significant assets, ongoing business activities, or employees';[12] (ii) *trusts*: legal institutions 'which enable a separation of legal ownership and beneficial ownership of assets';[13] (iii) *foundations*: un-owned economic entities, 'in which asset contributors cede rights of ownership, control, and beneficial interest to the foundation';[14] and (iv) *fictions*: 'fictitious entities and unincorporated economic organizations', where the entities 'exist *entirely* as an alternative name under which persons conduct business'.[15]

Corporate vehicles have both legal owners and beneficial owners, and beneficial ownership is the relevant concept here. Definitions of beneficial

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8 See generally Hall (n 3).

9 JS Nye, 'Corruption and Political Development: A Cost–Benefit Analysis' (1967) 61(2) *American Political Science Review* 417, 419.

10 Delaney (n 4) 418.

11 Ware and Noone (n 2) 31.

12 Emile van der Does de Willebois et al, *The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do about It* (Report, 2011) 34 ('*Puppet Masters*').

13 Financial Action Task Force, *Transparency and Beneficial Ownership* (Guidance, October 2014) 6 ('*FATF Guidance*'). See generally *Puppet Masters* (n 12) 44–7.

14 *Puppet Masters* (n 12) 47.

15 Ibid 49 (emphasis in original).

ownership vary, but that of the Financial Action Task Force ('FATF') is generally internationally accepted.[16] A beneficial owner is, under that definition, 'the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted … [including] persons who exercise ultimate effective control over a legal person or arrangement'.[17]

The central idea is therefore one of ultimate control and the focus is on the person who actually derives the benefit, and not on formal legal ownership.[18] Knowledge of a corporate vehicle's formal ownership is still, of course, helpful in tracking down and obtaining information about that vehicle's beneficial ownership.[19]

This paper takes the view that neither corporate vehicles nor the concept of beneficial ownership is inherently pernicious. It recognises that, 'the overwhelming majority of corporate vehicles operate for genuine and legitimate purposes'[20] and shell companies in particular are used for perfectly legitimate transactions, such as 'domestic and cross-border currency and asset transfers, or to facilitate corporate mergers and re-organizations'.[21] Similarly, the definition of 'beneficial ownership' does not, in itself, 'refer to a person who intentionally uses a company or a legal entity to hide his/her identity, assets and activities for criminal purposes', though much international opinion and observation in the area of corruption use the term to mean as such.[22] The concept of beneficial ownership is, rather, viewed here as a basic and historic legal doctrine, derived from trust law and underlying many legitimate legal forms, transactions and purposes.

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16 Michele Riccardi and Ernesto Savona, *The Identification of Beneficial Owners in the Fight against Money Laundering* (Final Report, 2013) 14 ('*Project BOWNET*').

17 Financial Action Task Force, *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations* (Report, June 2019) 113 ('*International Standards*').

18 *FATF Guidance* (n 13) 8. See also Transparency International, *Ending Secrecy to End Impunity: Tracing the Beneficial Owner* (Policy Brief No 2/2014, 2014) 2 <https://images.transparencycdn.org/images/2014_PolicyBrief2_BeneficialOwnership_EN.pdf>, archived at <https://perma.cc/5RC8-CEJ8> ('*Ending Secrecy to End Impunity*'). See also *Puppet Masters* (n 12) 3, 19. See also *Project BOWNET* (n 16) 14; Fianna Jurdant, 'Disclosure of Beneficial Ownership and Control in Indonesia: Legislative and Regulatory Policy Options for Sustainable Capital Markets' (Corporate Governance Working Paper No 9, OECD, 11 July 2013) 33, 41.

19 See *Puppet Masters* (n 12) 3.

20 Joy Geary, 'Beneficial Ownership: Part II' (May 2010) *Anti-Money Laundering Magazine* 17 <https://afma.com.au/afmawr/_assets/main/lib90059/2010_may_aml%20magazine.pdf>, archived at <https://perma.cc/2H8Z-KTRY>.

21 Financial Crimes Enforcement Network, Department of the Treasury (United States), *The Role of Domestic Shell Companies in Financial Crime and Money Laundering: Limited Liability Companies* (Report, November 2006) 4, quoted in Shima Baradaran et al, 'Funding Terror' (2014) 162(3) *University of Pennsylvania Law Review* 477, 492. See also Rohan Bedi, 'KYC for Shell Companies' (Industry Working Paper No 07-01, Saw Centre for Financial Studies, National University of Singapore, February 2007) 5; *Puppet Masters* (n 12) 34–5; Michael G Findley, Daniel L Nielson and JC Sharman, *Global Shell Games: Experiments in Transnational Relations, Crime, and Terrorism* (Cambridge University Press, 2014).

22 *Project BOWNET* (n 16) 15. See, eg, *Puppet Masters* (n 12) 17.

When corporate vehicles are tied into transactions involving corruption, however, as demonstrated by several case studies,[23] any gleam of legitimacy, of course, disappears. At a general level, the following often takes place:

> [T]he recipient of the bribe creates a corporate vehicle to hide the assets and any connection that he may have to them. In cases in which the official is given a concealed stake in the venture or the company offering the bribe, these corporate vehicles become the opaque link between the corrupted party and the wealth acquired.[24]

The corporate vehicle provides a veil which hides the corrupt activity so that an illusion of a legitimate origin for ill-gotten gain is created and anonymity maintained.[25]

Shell companies are both the most common corporate vehicles used for corrupt activities and potentially the most dangerous, and it is for this reason that they are the central focus of this paper. The corrupt beneficial owner of the company, benefiting from the transaction, is obscured and domestic and international commitments are circumvented. Anonymous corporate vehicles shield the real owners from exposure and accountability.[26]

The Grand Corruption Database Project, a component of the World Bank's report, *The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do about It* ('*Puppet Masters*'), found, for example, that corporate vehicles were used in 150 of the 213 grand corruption investigations it examined.[27] Of those 150 cases, companies were the corporate vehicles used to hide the corrupt proceeds in 128 cases,[28] and, in more than half of those 128 cases, shell companies were specifically involved.[29] The *Puppet Masters* report remains, years on, the leading and, in effect, the only thorough investigation into the use of corporate vehicles in cases of grand corruption, money laundering and terrorist financing. It examined how corporate vehicles were misused to conceal proceeds of grand corruption, collecting a database of grand corruption cases from a vast

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23 See Colin Nicholls et al, *Corruption and Misuse of Public Office* (Oxford University Press, 2nd ed, 2011) 285–6; Committee on Homeland Security and Governmental Affairs, United States Senate, *Keeping Foreign Corruption out of the United States: Four Case Histories* (Report, 4 February 2010), archived at <https://perma.cc/G73C-6TUN>; Lynne Walker, Australian Federal Police, 'Corruption in International Banking and Financial Systems' (Conference Paper, Transnational Crime Conference, 9–10 March 2000), especially regarding the case studies presented on the Bank of Credit and Commerce International and the Bank of New York. See generally *Puppet Masters* (n 12) 171–217.

24 *Puppet Masters* (n 12) 39.

25 Transparency International, *Fighting Money Laundering in the EU: From Secret Ownership to Public Registries* (EU Policy Paper No 1/2014, 2014) 1 ('*Fighting Money Laundering in the EU*'). See also JC Sharman, 'Shopping for Anonymous Shell Companies: An Audit Study of Anonymity and Crime in the International Financial System' (2010) 24(4) *Journal of Economic Perspectives* 127, 129.

26 Mike Callaghan et al, Lowy Institute for International Policy, *G20 2014: Reform of the International Organisations, Financial Regulation, Trade, Accountability and Anti-Corruption* (Report No 13, September 2014) 42 <https://www.lowyinstitute.org/sites/default/files/g20-monitor-september-2014_0.pdf>, archived at <https://perma.cc/YV4R-QQHE>.

27 *Puppet Masters* (n 12) 117.

28 Ibid 34.

29 Ibid. See also OECD, *Behind the Corporate Veil: Using Corporate Entities for Illicit Purposes* (2001) 17.

range of jurisdictions, undertaking 'extensive interviews with practitioners' and collecting 'evidence from a solicitation exercise'.[30]

The OECD's 2014 review of over 300 bribery cases similarly found that one in four of those cases involved shell companies facilitating the passing of illicit money.[31] In addition, Cobus de Swardt argues that shell companies are also, at least potentially, the most destructive of all the corporate vehicles because of the very ease with which they are set up and run.[32]

B *International Law and Regulation*

The general process outlined above presents the corrupt transaction as being quite straight forward, but, of course, in reality there are usually several corporate vehicles being used by the beneficial owner across several jurisdictions in ways that are difficult to understand and, importantly, to trace. The FATF explains: '[c]riminals often create, administer, control, own, and financially operate corporate vehicles from different countries, thereby preventing competent authorities in any one jurisdiction from obtaining all relevant information'.[33]

A white paper produced by LexisNexis Business describes this:

> This issue is exacerbated by a myriad of different laws governing company registrations and management in different geographic territories. It is possible for a United States company to be partly owned by an offshore company, which in turn is part-owned by another company which has three shareholders all based in different countries. Depending on the geographical location of each company, there will be different disclosure requirements for each company and individual. This can make it impossible to know for certain who the beneficial owner really is.[34]

This is a global issue and it requires and demands an international legal response and global regulation.

III AN INTERNATIONAL LEGAL RESPONSE

There has been some international response to the issue outlined above (namely, of shell companies being used to facilitate corrupt activities across borders). This part provides an overview of that international response and examines the relevant binding legal obligations and aspirational recommendations

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30 *Puppet Masters* (n 12) 2–3.

31 OECD, *OECD Foreign Bribery Report: An Analysis of the Crime of Bribery of Foreign Public Officials* (Report, 2014) 29. See also LexisNexis, *The Hidden World of Beneficial Ownership: A Due Diligence Challenge for Too Long* (Report, December 2016) 2 ('*The Hidden World of Beneficial Ownership*').

32 See, eg, Cobus de Swardt, 'Put an End to Money Laundering, Bribery, and Corruption', *Global Financial Integrity* (Web Page, 9 July 2014) <http://www.gfintegrity.org/put-end-money-laundering-bribery-corruption/>, archived at <https://perma.cc/8R6F-LRDM>.

33 *FATF Guidance* (n 13) 6. See also *Project BOWNET* (n 16) 10; *Puppet Masters* (n 12) 1, 53–4; David Chaikin, 'Commercial Corruption and Money Laundering: A Preliminary Analysis' (2008) 15(3) *Journal of Financial Crime* 269, 275; AUSTRAC, *Money Laundering in Australia 2011* (Report, 17 July 2019) <https://www.austrac.gov.au/business/how-comply-guidance-and-resources/guidance-resources/money-laundering-australia-2011>, archived at <https://perma.cc/9U3T-QNEQ>. See generally Transcrime, *Cost Benefit Analysis of Transparency Requirements in the Company/Corporate Field and Banking Sector Relevant for the Fight against Money Laundering and Other Financial Crime* (Final Report, 27 February 2007) ('*Cost Benefit Analysis of Transparency Requirements*').

34 *The Hidden World of Beneficial Ownership* (n 31) 3.

and principles. At the outset, it is worth noting, however, that the applicable *hard* and *soft* law obligations are few and far between, do not address the issue completely squarely and that there has been little academic examination or consideration of those obligations. Overall, the international response can be described as fairly minimal.

The focus of that international response, both in its *hard* and *soft* law forms, has been on exposing the beneficial owners of shell companies. The exposure of beneficial owners has, at least prima facie, two rationales. First, there is a prevention rationale: dissuading others from undertaking the corrupt behaviour, given the likelihood of being found out. Secondly, there is a detection rationale: allowing authorities to conduct investigations and find out who is behind the corrupt activity with greater ease. The crux of the matter is, really, 'whether authorities can "look through" the corporate veil to find the individuals pulling the strings (referred to as the "beneficial owner")'[35] and thereby stop and prevent the corrupt practice.

A *The United Nations Convention against Corruption*

There are no legally binding international obligations which directly and openly address the misuse of shell companies. But there are some relevant articles in the *United Nations Convention against Corruption* ('*UNCAC*'),[36] which, at a general level, require parties to criminalise corruption.[37] The following are particularly relevant:

- Article 12(2)(c) calls on states to promote transparency among private entities and take measures, where appropriate, to identify 'legal and natural persons involved in the establishment and management of corporate entities'.[38]
- Article 14(1)(a) calls on states to '[i]nstitute a comprehensive domestic regulatory and supervisory regime for banks and non-bank financial institutions', as well as 'other bodies particularly susceptible to money-laundering'.[39] It recommends beneficial ownership identification requirements as part of this.
- Article 52(1) requires states to take measures to require financial institutions to 'verify the identity of customers' and 'take reasonable steps to determine the identity of beneficial owners of funds deposited into high-value accounts'.[40]

Evidently, the articles do not directly address shell companies. But they at least do touch on beneficial ownership and transparency issues more generally.[41]

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35 Findley, Nielson and Sharman (n 21) 7.

36 *United Nations Convention against Corruption*, opened for signature 9 December 2003, 2349 UNTS 41 (entered into force 14 December 2005) ('*UNCAC*').

37 See ibid arts 15–28. See also Delaney (n 4) 418; *Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*, opened for signature 17 December 1997, 2802 UNTS 225 (entered into force 15 February 1999).

38 *UNCAC* (n 36) art 12(2)(c).

39 Ibid art 14(1)(a).

40 Ibid art 52(1).

41 Christine Clough, UNCAC Coalition, *Public Disclosure of Beneficial Ownership* (Briefing Note, November 2013) 3.

UNCAC at least thereby operates on the issue because, as was outlined above, exposure of beneficial ownership is central to overcoming the misuse of shell companies.

B *Recommendations and Principles*

It is largely in the more 'aspirational' arena of recommendations and principles that the international community has focused its engagement on shell companies and the revealing of beneficial ownership. The idea of these mechanisms is, generally, to 'operate through dialogue and persuasion rather than coercion'.[42] This section looks at only the most important recommendations and principles currently in place, based on the breadth of their acceptance, the authority of the body behind them and their status as the most recent mechanisms in this sphere.

1 *Financial Action Task Force Recommendations*

The FATF is 'an independent inter-governmental body that develops and promotes policies to protect the global financial system' in terms of, in particular, anti-money laundering and counter-terrorism funding.[43] Its recommendations have been taken to be relevant to the transnational corruption context,[44] and the FATF has been recognised as producing the primary international standard on the issue of the misuse of corporate vehicles in facilitating transnational corruption.[45] More than 180 countries have committed to the FATF standards, and the standards have been endorsed by key global institutions such as the United Nations, the G20 and the World Bank.[46]

The FATF recommendations are extensive. Most notably, Recommendations 24 and 25 require countries to 'ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons' (Recommendation 24),[47] and legal arrangements (Recommendation 25).[48] That information should be able to be obtained or accessed by the relevant authorities 'in a timely fashion'.[49]

The FATF recommends that those standards be met by government imposition of due diligence requirements on both financial institutions and other providers to identify the beneficial owner of a legal person or arrangement (Recommendations 10 and 22),[50] and by establishing registries of beneficial ownership information.[51]

The FATF recommendations are, importantly, actively coercive, at least in so far as the FATF publishes reports and makes public statements on its website in

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42 Delaney (n 4) 443.

43 See the text of the front matter in *FATF Guidance* (n 13). See also *Project BOWNET* (n 16) 20.

44 *FATF Guidance* (n 13) 4 [5].

45 *Puppet Masters* (n 12) 5–6.

46 Findley, Nielson and Sharman (n 21) 9. See generally 'Countries', *FATF* (2014) <http://www.fatf-gafi.org/countries/>, archived at <https://perma.cc/3K9F-7NTX>.

47 *International Standards* (n 17) 20. See generally *FATF Guidance* (n 13) 12–28.

48 *International Standards* (n 17) 20. See generally *FATF Guidance* (n 13) 29–35.

49 *Puppet Masters* (n 12) 13. *International Standards* (n 17) 20.

50 *International Standards* (n 17) 12–13, 17–18.

51 Ibid 87. See generally *FATF Guidance* (n 13) 19–22.

relation to non-complying countries.[52] The recommendations very directly target circumstances, such as those in the usual transaction outlined in the first part of this paper, by focusing on governments imposing obligations on financial institutions and providers. The recommendations emphasise the need to collect information in order to expose beneficial ownership at both the state level and the service-provider level. This, as discussed above, is the action most critical to the deterrence and prevention of the misuse of shell companies.[53]

2 *G20 High-Level Principles*

In 2014, the G20 endorsed the FATF standards on beneficial ownership and also released their own set of principles aimed at supporting and facilitating processes that reveal the beneficial owners of shell companies.[54] The G20 High-Level Principles on Beneficial Ownership Transparency ('G20 High-Level Principles'), which were unanimously accepted by the G20 countries,[55] called for states to ensure that 'legal persons maintain beneficial ownership information onshore and that information is adequate, accurate, and current'.[56] The idea was that this could be done through 'central registries of beneficial ownership of legal persons or other appropriate mechanisms'[57] and that, accordingly, the information would be shared between domestic and international enforcement agencies.[58] Transparency International is a global, non-governmental organisation charged with the broad aim of tackling corruption.[59] It is a prominent voice for this issue, with its campaign called 'Unmask the Corrupt'.[60] It supports the G20 High-Level Principles and their promotion of due diligence for financial service providers and, in particular, the idea of implementing public, jurisdiction-based searchable registries of beneficial ownership information.[61] According to Transparency International, such registries can 'break the vicious cycle of impunity that hidden ownership allows' by exposing the ultimate controllers of a company.[62]

Effective global regulation, of course, needs the support of the world's biggest economies. The release of the G20 High-Level Principles and the G20 countries' commitment to improving the transparency of beneficial ownership gave 'new political momentum to longstanding promises to tackle the secrecy behind

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52 See, eg, 'FATF Public Statement', *FATF* (Web Page, 27 February 2015) <http://www.fatf-gafi.org/topics/high-riskandnon-cooperativejurisdictions/documents/public-statement-february-2015.html>, archived at <https://perma.cc/B296-8Q3E>.

53 See above n 35 and accompanying text.

54 'G20 High-Level Principles on Beneficial Ownership Transparency', *Stolen Asset Recovery Initiative* (Web Page, 2014) 1 <https://star.worldbank.org/sites/star/files/g20_high-level_principles_beneficial_ownership_transparency.pdf>, archived at <https://perma.cc/M7TN-VBSG> ('G20 High-Level Principles').

55 Maira Martini and Maggie Murphy, Transparency International, *Just for Show? Reviewing G20 Promises on Beneficial Ownership* (Report, 2015) 7 ('*Just for Show?*').

56 Ibid 2 (Principle 3).

57 Ibid 2 (Principle 4).

58 Ibid 1 (Principle 2), 2 (Principle 8).

59 'FAQs on Transparency International', *Transparency International* (Web Page) <https://transparency.org/whoweare/organisation/faqs_on_transparency_international>, archived at <https://perma.cc/4TWS-GV5A>.

60 *Unmask the Corrupt* (Website) <https://unmaskthecorrupt.org/>.

61 *Ending Secrecy to End Impunity* (n 18) 4.

62 Ibid 1.

corruption'.[63] The G20 High-Level Principles thereby tackle the issue of shell company misuse to facilitate cross-border corrupt activity at a much-needed political level with their pledge for transparency of beneficial ownership.[64]

IV THE DISCONNECT BETWEEN RHETORIC AND PRACTICE

The international response in terms of legal obligations, recommendations and principles set out above undoubtedly demonstrates at least a theoretical, rhetorical engagement with transnational corruption in the emphasis on removing the secrecy associated with the misuse of shell companies. But when attention is turned to the actual 'on the ground' implementation and practice, it is readily apparent that most countries are making in-principle commitments but not following up on those commitments in practice. To demonstrate this, the analysis in this part starts with a brief global survey and then uses Australia as a case study.

A *A Brief Global Overview*

There has, since 2013, been an international consensus forming on the part of both governments and companies about the need for transparency and on the need to put in place measures to expose beneficial ownership in order to combat the misuse of shell companies to facilitate corrupt transactions.[65] Active steps have been taken by significant economies towards meaningful engagement with the issue, and there is constant movement on this front. Key examples include the United Kingdom and the European Union.

In March 2015, for example, the UK enacted legislation requiring companies to keep a register of persons with 'significant control' of companies,[66] a requirement intended to expose beneficial ownership information. In May 2015, the European Parliament adopted the *4th Anti-Money Laundering Directive*.[67] That Directive required EU states to create central registers of beneficial ownership to be available and accessible to authorities.[68] More recently, in April 2018, the European Parliament adopted the *5th Anti-Money Laundering Directive*, amending

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63 Jamie Smyth, George Parker and Vanessa Houlder, 'G20 Leaders Back Drive to Unmask Shell Companies', *Financial Times* (online, 17 November 2014) <https://www.ft.com/content/25ae632e-6d60-11e4-8f96-00144feabdc0>, archived at <https://perma.cc/77QE-CSEM>. See, eg, '2015–16 G20 Anti-Corruption Action Plan', *Stolen Asset Recovery Initiative* (Web Page, 2014) 1 <https://star.worldbank.org/sites/star/files/g20_2015-2016_anti-corruption_action_plan_australia_2014.pdf>, archived at <https://perma.cc/22C6-ALDZ> ('G20 Anti-Corruption Action Plan').

64 See generally 'G20 High-Level Principles' (n 54).

65 See *Puppet Masters* (n 12) 2; Sharman (n 25) 127. See also *B20 Anti-Corruption Working Group Report to the B20 Office and Taskforce Chairs* (Report, July 2014) 5 ('*B20 Report*').

66 See *Small Business, Enterprise and Employment Act 2015* (UK) s 81.

67 See *Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the Prevention of the Use of the Financial System for the Purposes of Money Laundering or Terrorist Financing, Amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and Repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC* [2015] OJ L 141/73 ('*4th Anti-Money Laundering Directive*').

68 Ibid Preamble para 7(14). See also Transparency International UK, *Corruption on Your Doorstep: How Corrupt Capital Is Used to Buy Property in the UK* (Report, March 2015) 20 ('*Corruption on Your Doorstep*').

the *4th Anti-Money Laundering Directive* and requiring registers of beneficial ownership to be publicly accessible by 10 January 2020.[69]

These instances are undoubtedly significant and reflect the serious attention paid to the problem by major global players. But most countries, including the world's most significant economic powers, are still in the promises and plans stage, without strict legislative obligations to expose beneficial owners.

In 2014, Transparency International noted that despite the strengthening of global standards, 'such as those set by the [FATF] and [*UNCAC*]', and in direct contradiction to those standards, still only a 'few jurisdictions [actually] require[d] companies to report information on beneficial ownership to their national authorities'.[70] The organisation's 2015 report, *Just for Show? Reviewing G20 Promises on Beneficial Ownership*, for instance, then looked specifically at progress and implementation in light of the G20 High-Level Principles and found that '[f]ifteen of the 19 countries demonstrated either an average or weak legal framework for implementing the principles'.[71] The organisation's 2018 report, *G20 Leaders or Laggards? Reviewing G20 Promises on Ending Anonymous Companies*, in turn found that 11 countries still had weak or average legal frameworks on beneficial ownership and progress had been slow.[72] The UK was, in 2015, the only country to be given a 'very strong framework' rating for exposure and identification of the beneficial owners of corporate vehicles,[73] and by 2018, only France and Italy joined the UK in having a 'very strong framework'.[74]

Several more studies support Transparency International's findings. The *Puppet Masters* report, for example, found that 159 countries have generally shown low levels of compliance with Recommendations 24 and 25.[75] This was supported by the FATF's producing a guidance in 2014 on Recommendations 24 and 25 in light of the implementation of those recommendations having 'proved challenging'.[76] The *Puppet Masters* report, which carried out country evaluations on more than 159 countries, also found that service providers still failed to 'adequately identify the beneficial owner when establishing a business relationship'.[77] Such a failure is directly in contradiction with FATF

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69 *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* [2018] OJ L 156/43, Preamble paras 7(33), (53) ('*5th Anti-Money Laundering Directive*').

70 *Ending Secrecy to End Impunity* (n 18) 2. See also Concepcion Verdugo Yepes, 'Compliance with the AML/CFT International Standard: Lessons from a Cross-Country Analysis' (IMF Working Paper No 11/177, International Monetary Fund, July 2011) 6. See also Global Agenda Council on Organized Crime, *Organised Crime Enablers* (Report, July 2012) 14.

71 *The Hidden World of Beneficial Ownership* (n 31) 7, citing *Just for Show?* (n 55).

72 Maíra Martini and Maggie Murphy, Transparency International, *G20 Leaders or Laggards? Reviewing G20 Promises on Ending Anonymous Companies* (Report, 2018) 10–11 ('*G20 Leaders or Laggards?*').

73 *Just for Show?* (n 55) 8.

74 *G20 Leaders or Laggards?* (n 72) 10–11.

75 *Puppet Masters* (n 12) 13. See also at app A. The *Puppet Masters* report refers to (now former) Recommendations 33 and 34, as contained in the former 2003 FATF Recommendations. These correspond, respectively, with current Recommendations 24 and 25: see *International Standards* (n 17) 5.

76 *FATF Guidance* (n 13) 4 [6].

77 *Puppet Masters* (n 12) 6. See also Findley, Nielson and Sharman (n 21) 1.

Recommendation 10. The 2014 OECD report supported these conclusions. That report found that, among OECD countries, there was insufficient compliance with the FATF due diligence standards,[78] and 'generally weak' compliance with the FATF beneficial ownership transparency obligations, with some OECD countries not requiring any beneficial ownership information to be collected when a shell company or corporate vehicle is established.[79]

These statistics are concerning, not only because they show limited engagement with the international legal obligations, but because particularly key economies are among those which are not complying. Transparency International rated China and the United States, for instance, as having 'weak' frameworks in place for exposing the beneficial owners of corporate vehicles in 2015[80] and only 'average frameworks' in 2018.[81] In both 2015 and 2018, China was found to still need to implement measures to ensure legal entities record beneficial ownership information, and financial institutions and designated non-financial businesses and professions identify and verify their customers' beneficial ownership information.[82] The US was found in 2015 to not be fully compliant with any G20 High-Level Principles.[83] In 2018, the US was found to still be without a proper definition of beneficial ownership and to be one of four countries to not require 'designated non-financial businesses and professions' to identify and verify beneficial ownership information.[84] The US' framework is particularly weak in light of the fact that, as Transparency International explained in both 2015 and 2018, 'each state has a separate company register and requires different information from legal entities', with a result that, '[i]n some of the registers (for example, Delaware), information on shareholders or directors is not even recorded, making the identification of the beneficial owner more difficult'.[85]

The fact that few countries, including the world's most prominent economic powers, have not properly implemented their international legal obligations is particularly problematic, given that the issue requires global and cross-jurisdictional regulation.[86]

B *Australia*

Australia has acceded to *UNCAC*, endorsed the G20 High-Level Principles and openly committed itself to stopping the exploitation of corporate vehicles in the

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78 OECD, *Illicit Financial Flows from Developing Countries: Measuring OECD Responses* (Report, 2014) 31.

79 Ibid 42.

80 *Just for Show?* (n 55) 8; *G20 Leaders or Laggards?* (n 72) 10.

81 *G20 Leaders or Laggards?* (n 72) 11.

82 *Just for Show?* (n 55) 10; ibid 29.

83 *Just for Show?* (n 55) 10.

84 *G20 Leaders or Laggards?* (n 71) 59. See also ibid 10, 42. 'Designated non-financial businesses and professions' include 'lawyers, accountants, notaries, dealers in precious metals and real estate': *G20 Leaders or Laggards?* (n 71) 25.

85 *G20 Leaders or Laggards?* (n 72) 32; *Just for Show?* (n 55) 28–9.

86 See *The Hidden World of Beneficial Ownership* (n 31) 2.

service of corruption.[87] Legislation has been enacted. The most relevant laws in this area are the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) ('*AML/CTF Act*') and the *Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007* (Cth) ('*AML/CTF Rules*'),[88] which impose obligations on providers of financial, remittance, gambling and bullion-dealing services.[89] Although not directly phrased in terms of corruption, the *AML/CTF Act* and its customer due diligence requirements are linked to Australia's broader fight against corruption, and the FATF recognises that Anti-Money Laundering and Counter-Terrorism measures assist in fighting against corruption.[90] Australia's self-reporting, in the *Accountability Report Questionnaire 2014* ('*Accountability Report*'), found that with such legislation in place, it met its international obligations in terms of collecting beneficial ownership information.[91]

The findings of the Australian Government's 2017 consultation paper entitled *Increasing Transparency of the Beneficial Ownership of Companies* essentially demonstrate that Australia's self-reporting in the *Accountability Report* was not entirely accurate.[92] The *G20 2014 All-Country Summary Report* contradicted Australia's self-reporting and Australia's rhetoric on the issue, finding that Australia did not meet its international obligations in terms of beneficial ownership transparency of companies as set out earlier in this paper.[93] Similarly, Transparency International, in 2015, rated Australia as having a 'weak' legal framework to address the misuse of corporate vehicles. Among its findings, Transparency International found that 'Australia is only fully compliant with one [G20] principle' and 'serious improvements in the current legal framework are needed'.[94] This finding was in turn reflected in the FATF's *Mutual Evaluation*

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87 *UNCAC* (n 36); The Treasury, Australian Government, *Increasing Transparency of the Beneficial Ownership of Companies* (Consultation Paper, The Treasury, February 2017) 1, 7 ('*Treasury Consultation Paper*'). See also 'Global Leadership in Combating Corruption', *Attorney-General's Department* (Web Page) <https://www.ag.gov.au/Integrity/AntiCorruption/Pages/Globalleadershipincombatingcorruption.aspx>, archived at <https://perma.cc/B8HF-LNN9>. See 'G20 Anti-Corruption Action Plan' (n 63).

88 *Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007* (Cth) ('*AML/CTF Rules*').

89 *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) ss 5 (definition of 'designated service'), 6 ('*AML/CTF Act*'). See also *Treasury Consultation Paper* (n 87) 6.

90 Financial Action Task Force, *A Reference Guide and Information Note on the Use of the FATF Recommendations to Support the Fight against Corruption* (Report, 2010) 2. See also Chaikin (n 33) 274.

91 See G20 Anti-Corruption Working Group, *Accountability Report Questionnaire 2014* (Report, 2014) <https://star.worldbank.org/sites/star/files/accountability_report_questionnaire_2014_australia.pdf>, archived at <https://perma.cc/P5E5-XTND>. See also AJ Brown, 'Anti-Corruption Bar Set Higher, but Australia Still Has More to Do', *The Conversation* (online, 21 November 2014) <https://theconversation.com/anti-corruption-bar-set-higher-but-australia-still-has-more-to-do-34494>, archived at <https://perma.cc/YR28-UJCB>.

92 *Treasury Consultation Paper* (n 87) v, 11–18. See also 'Global Leadership in Combating Corruption', *Attorney General's Department* (Web Page) <https://www.ag.gov.au/integrity/anti-corruption/global-leadership-combating-corruption>, archived at <https://perma.cc/UZ2Z-CBW9>; 'G20 Anti-Corruption Action Plan' (n 63).

93 G20, *All Country Summary Report on Accountability* (online, December 2014), archived at <https://perma.cc/8AAZ-HZS3>. See above Part III(B).

94 *Just for Show?* (n 55) 10.

Report in 2015, which found that Australia was only 'partially compliant' with Recommendations 10 and 24 and 'non-compliant' with Recommendation 25.[95] That 2015 report provides the most extensive examination of Australia's compliance and non-compliance with the FATF's recommendations in this space. The 2015 report's findings, which are examined in detail below, and the FATF's more recent 2018 *3rd Enhanced Follow-Up Report and Technical Compliance Re-Rating* on Australia[96] are consolidated in the FATF's continually updated review and assessment of all countries against the FATF recommendations.[97] As FATF is the primary governing body in this space, this paper particularly relies on these reports for its evaluation of Australia's compliance with its international obligations. Notably, this was also the approach taken by the Australian Government to assess compliance.[98]

The FATF's *Mutual Evaluation Report* found that 'there are no direct requirements to identify and verify the identity of the customer in the Act or in the Rules', but that '[r]eporting entities are required to have AML/CTF programmes that include procedures to identify/verify the identity of the customer and enable them "to be reasonably satisfied" that the customer is who/what he claims to be'.[99] But, there are some notable problems. The very definition of 'reporting entity', to which the *AML/CTF Rules* apply, is already only limited to those particular service providers listed above.[100] Only 'reporting entities' are subject to this identification and verification requirement as opposed to third parties that set up corporate vehicles, such as trust and company service providers, lawyers or accountants.[101] In addition, r 4.12.2(1) further modifies that broad requirement. It says that, unless there are 'reasonable grounds to consider otherwise', when the customer is a natural person, the reporting entity may assume that the customer and the beneficial owner are the same person.[102] In addition to this modification and caveat for 'natural persons', there are also many more exceptions to the undertaking of due diligence obligations in the *AML/CTF Rules*, depending on the company type and structure of the customer.[103] For example, companies and trusts verified under the Rules' simplified company/trustee verification procedures, Australian Government entities, and foreign listed public companies subject to disclosure requirements elsewhere are exempted.[104] The breadth of these exceptions means that it is not completely clear to whom due diligence

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95 FATF and APG, *Anti-Money Laundering and Counter-Terrorist Financing Measures: Australia* (Mutual Evaluation Report, April 2015) 20, 24 ('*Mutual Evaluation Report*').

96 FATF, *Anti-Money Laundering and Counter-Terrorist Financing Measures: Australia* (3rd Enhanced Follow-Up Report, November 2018) <http://www.fatf-gafi.org/media/fatf/documents/reports/fur/FUR-Australia-2018.pdf>, archived at <https://perma.cc/Q53L-MLL9>.

97 'Consolidated Assessment Ratings', *FATF* (Web Page, 26 September 2019), archived at <https://perma.cc/XEQ4-CZZF>.

98 See *Treasury Consultation Paper* (n 87).

99 *Mutual Evaluation Report* (n 95) 152. See also at 178; *AML/CTF Rules* (n 88) r 4.12.

100 *AML/CTF Act* (n 89) ss 5 (definition of 'reporting entity'), 6. See also *Treasury Consultation Paper* (n 87) 6.

101 *Mutual Evaluation Report* (n 95) 110.

102 *AML/CTF Rules* (n 88) r 4.12.2(1).

103 Ibid r 4.12.2.

104 Ibid.

requirements apply.[105] Notably, there is also no requirement in Australian law 'to terminate the business relationship when the reporting entity is unable to comply with [customer due diligence] requirements'.[106] Recommendation 10 does not contemplate these 'exemptions and simplified due diligence measures'.[107] Loopholes exist and Australia is only partially compliant.

In Australia, there is also still no clear procedure for the obtaining or recording of companies' beneficial ownership information and there is no requirement for companies 'to obtain and hold up-to-date additional information to determine the ultimate natural person who is the beneficial owner beyond the immediate shareholder'.[108] The *Corporations Act 2001* (Cth) only requires companies to hold very basic information about members, which only relates to legal, not beneficial ownership,[109] and nominee directors and shareholders still do not have to disclose the identity of the beneficial owners on whose behalf they work.[110] The Australian Securities and Investments Commission does have some power to trace the beneficial ownership of shares,[111] but this mechanism 'only deals with public-listed companies'.[112] Accordingly, in many circumstances, beneficial ownership information is only really known if the legal ownership and beneficial owner happen to be identical.[113] In corrupt transactions, as per the very general example transaction set out earlier in this paper,[114] legal and beneficial ownership are rarely likely to be the same. This contradicts Recommendation 24, which requires states to ensure beneficial ownership information is available. Australia is only partially compliant.

Australia does not oblige 'trustees to hold and maintain information on trusts' or to 'keep this information up-to-date and accurate'.[115] There is, accordingly, no real guarantee of transparency in terms of legal arrangements in Australia as required by Recommendation 25, let alone in the 'timely manner' called for by that recommendation.[116] Australia is non-compliant with this FATF recommendation.

Australia has not yet met its international obligations in a meaningful way. Although progress has been made in meeting them and the failure to meet international obligations has been acknowledged by the Australian Government,[117] there has undoubtedly been and remains 'a huge gap between the rhetoric of leaders and the reality of their governments' actions'.[118]

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105 *Mutual Evaluation Report* (n 95) 153.
106 Ibid 20.
107 Ibid.
108 Ibid 178.
109 Ibid 111. See *Corporations Act 2001* (Cth) ('*Corporations Act*') s 169.
110 *G20 Leaders or Laggards?* (n 72) 52–3; *Just for Show?* (n 55) 12.
111 *Corporations Act* (n 109) s 672A; *Mutual Evaluation Report* (n 95) 111–12, 177.
112 *Mutual Evaluation Report* (n 95) 180.
113 Ibid (n 95) 178.
114 See above Part II(A).
115 *Mutual Evaluation Report* (n 95) 181.
116 Ibid 24.
117 See above n 92.
118 Brown (n 91).

V EVALUATING THE DISCONNECT BETWEEN THEORY AND IMPLEMENTATION

Explanations for the failure to effectively implement obligations that have been accepted in principle have generally centred on the hesitation on the part of countries to 'go first'. This part argues a further point, suggesting that the disconnect between the rhetoric and the implementation reality also flows from the failure of the G20 High-Level Principles themselves, with their emphasis on registries, their failure to grapple with shell companies' legitimate economic uses and their failure to directly address other key actors in the transaction in addition to states.

A *The Political Game: 'Going First'*

As outlined in Part III of this paper, some states have indeed 'gone first' and implemented, in some form, their international legal obligations in this space. But some states, especially those with less significant global economies, (understandably) do not want to be in the small minority of states that are currently enforcing those obligations. The Premier of the Cayman Islands, Alden McLaughlin, despite committing to the G20 High-Level Principles in theory in 2014,[119] articulated this reasoning openly:

> [U]nless such registers become the new global standard and are being used by all major players … then neither we nor any other Overseas Territory … intend to go first and have our economies experimented with and potentially damaged. … [W]e see no need for a central registry that would increase cost to business and the country and also create a potential single data source, which motivated and skilled individuals could hack into …[120]

Notably, even those countries that are leaders in this space, demonstrated by the domestic implementation of their international legal obligations, are not fully discharging those obligations. The UK, for example, only received its 'very strong legal framework' assessment in 2015 because the beneficial ownership standards for corporate vehicles incorporated in the British Overseas Territories and Crown Dependencies, such as the Cayman and the British Virgin Islands, were excluded from analysis,[121] and the 2018 Transparency International report found that there remain problems with the beneficial ownership legal frameworks in the British Overseas Territories and Crown Dependencies.[122] Further, while the *4th Anti-Money Laundering Directive* notably required the implementation of beneficial ownership registries, the directive was implemented at slow and differing paces by member countries, particularly by prominent European economies.[123]

Since the obligations depend for their effectiveness on a significant majority of countries undertaking them relatively simultaneously as a global whole, this

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119 See Cayman Islands Government, *Maintenance of Legal and Beneficial Ownership Information* (Consultation Report, 30 December 2014) 11.

120 Cayman Islands, *Official Hansard Report: Electronic Version*, Legislative Assembly, 8 December 2014, 748–9 (Alden M McLaughlin) <http://www.legislativeassembly.ky/portal/pls/portal/docs/1/12278698.PDF>, archived at <https://perma.cc/PKU7-ZQ57>, quoted in *Corruption on Your Doorstep* (n 68) 21. See also ibid 9.

121 *The Hidden World of Beneficial Ownership* (n 31) 8.

122 *G20 Leaders or Laggards?* (n 72) 19, 59.

123 *The Hidden World of Beneficial Ownership* (n 31) 10.

political factor is a powerful and intractable reason for the disconnect between rhetoric and reality in this space.

B *Registries as the Solution*

Corporate registries of beneficial ownership information appropriately have a significant place in the matrix of international obligations, in that they 'constitute a primary source of information for law enforcement and other authorities in their search for information on the persons connected to a particular legal entity'.[124] Registries also make due diligence obligations on financial service providers easier[125] and are a relatively inexpensive way to address the issue.[126] If they are public, as Transparency International advocates that they should be, registries increase the 'accountability of companies and public officials, helping civil society and the media to assess their structures'.[127]

The emphasis on registries in the international obligations[128] is nonetheless problematic. First, registries depend on actually being used both consistently and correctly by financial institutions undertaking due diligence and, as Transparency International notes, '[d]ue diligence procedures are fairly easy to circumvent as financial institutions may be negligent or incapable to perform them to the necessary depth'.[129] It is particularly difficult to check whether due diligence is undertaken correctly and consistently (and particularly easy to circumvent a registry) when it is considered that a corrupt transaction usually involves layers of different corporate vehicles and spans jurisdictions.[130] Registries cannot appreciate this complexity.

Secondly, registries are 'predominantly archival and passive' in nature.[131] Information may not be continually updated, thereby compromising its reliability and accuracy.[132] A registry could, for example, thereby even give the shell company, a false appearance of legitimacy, preventing it from being on the radar of potential investigation at all. The 2017 Global Legal Research Center's report, produced by the Law Library of Congress, surveyed the EU and 29 countries from all continents and major geographic regions and found that, at least at that time, few countries had strict chronological reporting limits and '[a]s a rule, governments do not verify information provided by companies and no data verification mechanisms are foreseen by national legislation'.[133]

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124 *Puppet Masters* (n 12) 102. See also at 4.

125 *Ending Secrecy to End Impunity* (n 18) 4. See also *FATF Guidance* (n 13) 42.

126 Transparency International EU, *Under the Shell: Ending Money Laundering in Europe* (Report, 2017) 29, citing *Cost Benefit Analysis of Transparency Requirements* (n 33).

127 *Ending Secrecy to End Impunity* (n 18) 4.

128 See above Part III(B).

129 *Ending Secrecy to End Impunity* (n 18) 2. See, eg, Financial Services Authority, *Banks' Management of High Money-Laundering Risk Situations: How Banks Deal with High-Risk Customers (Including Politically Exposed Persons), Correspondent Banking Relationships and Wire Transfers* (Report, June 2011) 6 [22]–[24].

130 *FATF Guidance* (n 13) 6–7. See Sharman (n 25) 132–3. See generally *The Hidden World of Beneficial Ownership* (n 31) 3.

131 *Puppet Masters* (n 12) 102. See also at 4; Findley, Nielson and Sharman (n 21) 9.

132 *Puppet Masters* (n 12) 72, 74.

133 Global Legal Research Center, 'Disclosure of Beneficial Ownership in Selected Countries' (Research Paper, The Law Library of Congress, July 2017) 2.

Thirdly, forcing relevant beneficial ownership information to be made public, as per Transparency International's campaign, amounts to a potential imbalance of very general and abstract public interest concerns against privacy interests and principles. Making this information available to regulatory and enforcement agencies, let alone making the information public, would demonstrate a key break in core principles of financial privacy, which value the confidentiality of personal and transactional customer information. Further, the putting of all beneficial ownership information into a public registry also means that customers' financial and personal information is open to data compromise, breach and potential misuse.

A public register of beneficial ownership is not a 'silver bullet' for combatting this issue,[134] and at the very least, registries are not the only instrument that should be used by the international community to address the misuse of shell companies.

C *Shell Companies as a Legitimate Economic Tool*

There has not been, at the level of international concern and response, an adequate appreciation of the need for shell companies and of their usefulness in legal, legitimate transactions and corporate activities (as outlined in Part II of this paper).[135] The international focus on transparency has led to this legitimate use of shell companies and corporate vehicles generally being ignored both in the rhetoric and in the obligations imposed. It is at least arguable, at a policy level, that companies using shell companies for legitimate economic purposes should not be exposed to onerous, potentially confidentiality-breaching obligations, or to obligations, such as those requiring the publication of all information on a public registry, which may compromise perfectly legitimate corporate activity by affecting their 'ability to invest in new projects without distorting market pricing'.[136]

The failure to grapple with this fact means that states, for which a functioning economy is of course critical, are less likely to accept the obligations at all or take them seriously if the obligations could threaten their economic wellbeing. They are, in particular, less likely to incorporate them into their legislative corporate governance structures.

International obligations depend for their effectiveness on governments' legislative implementation and, as Melanie Botho Emmen considers, '[r]egulating the whole for the few does not make good policy', and, is probably ultimately politically unfeasible at a global level.[137] The international instruments which

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134 Alex Marriage, European Network on Debt and Development, 'Secret Structures, Hidden Crimes: Urgent Steps to Address Hidden Ownership, Money Laundering and Tax Evasion from Developing Countries' (Report, 2013) 30; Transparency International, *Fighting Money Laundering in the EU* (n 25) 3. See also *Puppet Masters* (n 12) 8. See generally Ware and Noone (n 2) 42.

135 See Geary (n 20) 20–1.

136 Hugh McDermott, 'Beneficial Ownership: Part III' (May 2010) *Anti-Money Laundering Magazine* 22 <https://afma.com.au/afmawr/_assets/main/lib90059/2010_may_aml%20magazine.pdf>, archived at <https://perma.cc/2H8Z-KTRY>.

137 Melanie Botho Emmen, 'When Transparency Isn't the Answer: Beneficial Ownership in High-End Real Estate', *The Global Anticorruption Blog* (Blog Post, 23 March 2015) <http://globalanticorruptionblog.com/2015/03/23/when-transparency-isnt-the-answer-beneficial-ownership-in-high-end-real-estate/comment-page-1/>, archived at <https://perma.cc/V72K-T7JK>.

address the issue at hand here are undermined and their legitimacy called into question by their failure to appreciate the business and economic rationales for shell companies.

D *Failure to Address Both Sides of the Transaction*

The international obligations here apply to states and largely only require the compliance of states alone. This is, of course, usual for international legal obligations. But in the area of transnational corruption, regulatory models have previously applied to the other, 'corporate', side of the transaction. Most notably, the UN's *Global Compact* focuses on and targets corporations directly as opposed to simply viewing governments and states as the key to enforcement.[138] The *Global Compact* is a voluntary initiative by which transnational corporations pledge to observe principles, with a failure to do so made public.[139] It has been successful, in part, because it has been responsive to the corporate sector's legitimate concerns.[140]

The failure of international obligations to address the corporate side (including financial institutions and intermediaries) in a situation where a corporate vehicle is misused to facilitate corrupt activity isolates those players and, in turn, functions to de-legitimise the international obligations and minimise the likelihood of corporate sector cooperation for their implementation. The corporate side is critical to the transaction and, accordingly, to reducing the misuse of corporate vehicles to facilitate corrupt activity.[141]

The proposal set out in the next part of this paper specifically seeks to address this failure of international legal obligations. It demonstrates how an aspect of the 'corporate' side, namely service providers, can directly be engaged with.

VI A PROPOSAL: STRATEGIC PRIVATISATION AND SYSTEMS-BASED REGULATION

Various proposals have been made to overcome the disconnect between theoretical, in-principle commitments and actual implementation, as analysed above.[142] Detailed consideration of those proposals is beyond the scope of this paper. However, it is broadly accurate to say that no proposal has been successful, and it is this paper's claim that this is because the proposals have, generally speaking, failed to value corporate vehicles as legitimate economic tools or to acknowledge the relevant and not insignificant business and political concerns that public registries pose.

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138 'The Ten Principles of the UN Global Compact', *United Nations Global Compact* (Web Page) <https://www.unglobalcompact.org/what-is-gc/mission/principles>, archived at <https://perma.cc/9NBH-AQ4V>.

139 Ibid. See generally Deloitte and United Nations Global Compact, *UN Global Compact Management Model: Framework for Implementation* (Report, 2010) 8–9. See also Papa Louis Fall and Mohamed Mounir Zahran, Joint Inspection Unit, *United Nations Corporate Partnerships: The Role and Functioning of the Global Compact*, UN Doc JIU/REP/2010/9 (2010) 9; Katarina Weilert, 'Taming the Untamable? Transnational Corporations in United Nations Law and Practice' (2010) 14(1) *Max Planck Yearbook of United Nations Law* 445, 470.

140 Weilert (n 139) 480.

141 See *B20 Report* (n 65) 3.

142 See, eg, Ware and Noone (n 2) 40–1; *Puppet Masters* (n 12) 6. See also *Treasury Consultation Paper* (n 87) 14–17.

It is suggested here that a possible new pathway, which might overcome the deficiencies of the other approaches in those ways just described, could lie in the adoption of a 'responsive regulation' approach. The theory of responsive regulation was developed by Ian Ayres and John Braithwaite in the early 1990s.[143] As Peter Drahos and Martin Krygier explain, Ayres and Braithwaite

> shift[ed] the debate about business regulation away from the frozen positions of those who favoured deterrence-based regulation through the consistent and present application of rules and penalties and those who favoured removing as many of those rules as possible, thereby maximising the role of freedom and rationality in the business world. Responsive regulation advanced the idea that regulators should understand the context and motivations of those whose conduct they were regulating and then choose a response based on that contextual understanding.[144]

The analysis in this paper thus far has laid the groundwork for a near textbook application of responsive regulation. The absence of extensive and comprehensive rules in this space has clearly failed, but so have the few *hard* and *soft* law rules and penalties that function as 'deterrence-based' type regulation.

More specifically, this paper suggests the adoption of a particular development within that broader responsive regulation approach, namely Kath Hall's strategic privatisation concept and her advocacy of a systems-based regulation strategy and the translation of that development into this very specific and narrow aspect of the broader transnational corruption picture.

According to Hall, systems-based regulation is a private, strategic, broad, transnational anti-corruption strategy, requiring 'corporations to implement adequate procedures and internal systems to reduce or remove the risk of corruption … [by] drawing upon the rules, guidelines and standards of global private regulators'.[145] Effective systems-based regulation should involve 'an external body such as a government regulator, industry body or private organisation monitoring corporate compliance with regulation and/or holding a corporation liable in the event of non-compliance'.[146]

In brief, the approach gives corporations a 'flexibility in designing their response to laws, while still holding them accountable for the adequacy and efficacy of the systems they adopt'.[147]

Hall advocates for the application of systems-based regulation in the context of general transnational corruption regulation. It is proposed here that, with one key difference, an extension of that application is possible and desirable and that the systems-based regulation strategy can be also translated into the narrower context of the misuse of shell companies to facilitate corrupt activity. The key difference is as follows: instead of requiring corporations in the transaction to 'implement adequate procedures and internal systems', it is specifically proposed here that that role is performed at the service provider level (such as banks, lawyers, accounting

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143 See generally Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (Oxford University Press, 1992).

144 Peter Drahos and Martin Krygier, 'Regulation, Institutions and Networks' in Peter Drahos (ed), *Regulatory Theory: Foundations and Applications* (ANU Press, 2017) 1, 5.

145 Hall (n 3) 61.

146 Ibid 64–5. See also Christine Parker, *The Open Corporation: Effective Self-Regulation and Democracy* (Cambridge University Press, 2002).

147 Hall (n 3) 65, citing Sharon Gilad, 'It Runs in the Family: Meta-Regulation and Its Siblings' (2010) 4(4) *Regulation and Governance* 485, 485–6.

firms).[148] While regulation at the 'gatekeeper' level has been advocated for and drawn upon in other corporate contexts,[149] the service provider level has not been adequately utilised by the international legal community to address the misuse of corporate vehicles. In turn, as was demonstrated by the Australian case study above, domestic legislators and policy makers have largely ignored the service provider level in this space. The *AML/CTF Rules*, for example, are not imposed on service providers who create and register corporate vehicles and there is minimal regulatory oversight at this level.

The proposed idea here is that service providers would themselves create and implement systems to overcome the misuse of shell companies and effectiveness would require there being a body in place to ensure compliance with those systems. These entities are in a critical position in the usual transaction that was set out at the very beginning of this paper, with their having 'unique insight into the day-to-day operations and the real "financial life" of the corporate vehicle, that is, the financial flows of funds',[150] and their performing key 'administrative procedures necessary for establishing a company or other corporate vehicle'.[151] Service providers may not be as directly connected to the transactions (and, therefore, have fewer incentives toward wrongdoing) as the other players in the transaction, such as corporations and public officials.

Most significantly, the proposed pathway directly addresses the arguable causes for the disconnect between theory and practice set out above. Accordingly, the application of the proposed pathway should, at least in theory, be able to overcome the poor performance in implementation in this space in countries such as Australia. For instance, the proposed pathway addresses the non-public official (corporate) side of the corrupt transaction and provides a potentially effective methodology without, as international legal obligations outlined in this paper traditionally have, undermining the economic benefits that flow from the proper use of shell companies or exposing all users of those companies to public disclosure about personal and transactional information. But perhaps the greatest advantage of this pathway is its potential to build a culture of compliance. Its voluntary nature and ability to be developed by and within service providers themselves (with proper, external oversight) may lead to an effectiveness that has been missing so far. The implementation of this strategy would operate pursuant to a more nuanced understanding of the activities of service providers than laws may provide,[152] and, therefore, would be more likely to be acceptable to them. It has already been shown to be a highly successful pathway in the broader transnational corruption regulation context.[153]

It is acknowledged that, despite the demonstrated success of the 'strategic privatisation' strategy, its reliance on service providers 'doing the right thing' inevitably leaves the concept open to particular criticism and scepticism and to the

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148 Hall (n 3) 61. See generally *Organised Crime Enablers* (n 70) 9–12.

149 See, eg, Stavros Gadinis and Colby Mangels, 'Collaborative Gatekeepers' (2016) 73(2) *Washington and Lee Law Review* 797.

150 *Puppet Masters* (n 12) 5. See also Chaikin (n 33) 275.

151 *Puppet Masters* (n 12) 84.

152 See generally Hall (n 3) 65.

153 Ibid 61, 70–1. See also David Vogel, 'The Private Regulation of Global Corporate Conduct: Achievements and Limitations' (2010) 49(1) *Business and Society* 68.

more general critiques of responsive regulation.[154] It is also worth noting that this paper's purpose is not to explore every intricacy or practical implication involved in adopting the strategic privatisation strategy. Rather, it is hoped that the proposal might provide a new and novel direction for global (and, in particular, Australian) policy makers and legislators to take to address the misuse of corporate vehicles and, more broadly, to address transnational corruption.

But there are counteracting factors that are worth mentioning in support of the proposal. First, putting these arrangements in place is, arguably, actively beneficial to businesses,[155] because it is good business practice for 'banks and other companies to know who they are doing business with and minimize their financial exposure to others' misdeeds'.[156] The imposition of due diligence requirements can also be reputationally beneficial. The provider is of course less likely to be exposed to scandal and subsequent public scrutiny, such as that seen in 2015 with the 'Panama Papers' scandal, if due diligence requirements are followed.[157] As Joy Geary considers, 'the damage that *one* single client relationship can inflict on a financial institution's reputation' is significant.[158] Government and public entities are also intuitively more likely to contract and deal with providers with a reputation of strict due diligence requirements because of that reduced likelihood of scandal and public scrutiny. Secondly, there are indications, both in Australia and globally, that courts are increasingly willing, 'in the context of determining breaches of directors' duties', to look beyond the corporate veil and examine those steps directors actually take to mitigate and reduce the corruption risk.[159] Thirdly, the introduction of a systems-based regulation system and focus on 'strategic privatisation' would supplement, not replace, domestic and international legal obligations. This is of course important from several perspectives, such as the practical, political and legal, to name a few. As Braithwaite has put it, '[t]he most fertile legal systems will be those that enable both strategic privatization of the public and strategic publicization of the private'.[160]

This strategy thereby has the potential to overcome the deficiencies of the obligations outlined above, provides a dynamic and realistic way to overcome the misuse of shell companies and provides incentives on financial institutions' own

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154 See, eg, Jonathan Kolieb, 'When to Punish, When to Persuade and When to Reward: Strengthening Responsive Regulation with the Regulatory Diamond' (2015) 41(1) *Monash University Law Review* 137.

155 See The B Team, *Ending Anonymous Companies: Tackling Corruption and Promoting Stability through Beneficial Ownership Transparency* (Report, January 2015).

156 Mary Beth Goodman, 'Beneficial Ownership Rules Would Drag Criminals into Daylight', *American Banker* (Blog Post, 18 February 2015) <https://americanbanker.com/opinion/beneficial-ownership-rules-would-drag-criminals-into-daylight>, archived at <https://perma.cc/5RJA-B3AZ>.

157 See, eg, Juliette Garside et al, 'Panama Papers: A Special Investigation into the Leaked Documents Created by Panamanian Law Firm Mossack Fonseca', *The Guardian* (online) <https://www.theguardian.com/news/2016/apr/08/mossack-fonseca-law-firm-hide-money-panama-papers>, archived at <https://perma.cc/D4HW-FGJM>.

158 Geary (n 20) 17 (emphasis in original), citing Global Witness, *Undue Diligence: How Banks Do Business with Corrupt Regimes* (Report, March 2009).

159 Hall (n 3) 61. See, eg, *Australian Securities and Investments Commission v Lindberg* (2012) 91 ACSR 640; *Securities and Exchange Commission v Peterson* (ED NY, Civ No CR12-224-JBW, 3 May 2012). See also *Criminal Code Act 1995* (Cth) pt 2.5, discussed in Hall (n 3) 66.

160 John Braithwaite, 'Strategic Socialism, Strategic Privatization and Crisis' (Regnet Research Paper No 2013/11, Australian National University, 2013) 1.

terms. The task of understanding just with whom companies, and financial services organisations in particular, are doing business has been made all the more difficult by complex ownership trails that cross geographical and legal boundaries. This pathway has practical and achievable mechanisms in place, which mean that it is less likely to remain merely aspirational. Most importantly, it has significant potential to build a culture of compliance.

VII CONCLUSION

The Australian and international communities have addressed the misuse of shell companies and their role in facilitating transnational corrupt activity. But they have done so insufficiently. Shell companies continue to function as an 'iron curtain', behind which corrupt activity is hidden.[161] A disconnect remains between states' rhetorical commitment to fight the use of corporate vehicles in corrupt transactions and their practical implementation of anti-corruption measures. This paper engaged with that disconnect and proposed a way to build the culture of compliance required to defeat this particular aspect of the broader transnational corruption crisis.

[161] Spencer (n 1) 75.