

SUBMISSIONS ON THE COMPANIES AMENDMENT BILL [B-2018]

("The Companies Amendment Bill, 2018")

Introduction

1. Corruption Watch ("CW") is a non-profit civil society organisation. It is independent, and it has no political or business alignment. CW intends to ensure that custodians of public resources act responsibly to advance the interests of the public. CW's ultimate objectives include: fighting the rising tide of corruption and abuse of public funds in South Africa; promoting transparency; and accountability to protect the beneficiaries of public goods and services.
2. CW has a vision of a corruption free South Africa, one in which educated and informed citizens are able to: recognise and report corruption without fear; where incidents of corruption and maladministration are addressed without favour or prejudice; and where public and private individuals are held accountable for the abuse of public power and resources.
3. As an accredited Transparency International Chapter in South Africa, core to our mandate is the promotion of transparency and accountability within private sector and state institutions in order to ensure that corruption is addressed and reduced through the promotion and protection of democracy, rule of law and good governance
4. CW therefore welcomes the opportunity to make submissions on the Companies Amendment Bill, 2021 (**the Bill**).
5. We note the series of amendments in the 2021 Bill are aimed at achieving three main policy objectives - improving ease of doing business in respect of certain administrative related provisions of the Companies Act; providing for greater transparency on wage ratios at firm level and addressing true or beneficial ownership of companies aimed at addressing money laundering challenges.
6. Our submission is focused on ***enhancing transparency and accountability within the new provisions related to beneficial ownership in light of the global effort to address corruption,***

anti-money laundering and financing of terrorism as well as on appropriate triggers for disclosure and the content of the disclosure.

7. We note that the Bill proposes the following new provisions on beneficial ownership;
 - 7.1. An explicit obligation on companies to know and disclose the identity of their true shareholders who hold a beneficial interest amounting to 5% or more of the total shares in a company.
 - 7.2. Recognition that ultimate beneficial ownership by an individual may be held either by a single nominee or through multiple nominees holding smaller levels of shares. Importantly however, that nominee shareholders are not beneficial owners.
 - 7.3. A clear distinction is made between on the one hand, the company requesting information from shareholders and the shareholder disclosing such information to the company; and on the other hand, the company reporting or publishing the beneficial ownership information.
 - 7.4. All beneficial ownership be requested by and disclosed to the company concerned, further, that the company in turn be required to report/publish shareholding information only in instances where persons in the aggregate, alone or together with other persons own 5% or more of the beneficial interests of the shares in a class.
8. While we welcome the above mentioned provisions, most critically that the Bill incorporates the international best practice of the 5% threshold for reporting beneficial ownership. Our concern however is that the proposed amendments do not go far enough to enable effective transparency. ***The provisions, if implemented in this form, will not lead to the design and implementation of an effective beneficial ownership reporting regime that would be in line with international best practice and anti-corruption aims.***
9. It is with this in mind that we submit that the Bill fails to make sufficient provisions for the advancement of key parts of its objectives to tackle the vulnerabilities of beneficial ownership opacity as an enabler to grand corruption. We unpack these vulnerabilities under the following headings:
 - 9.1. Ambiguous scope of beneficial owners/ship.
 - 9.2. Uncertainty regarding the Central Register.

9.3. Reporting Regime and Disclosure.

Ambiguous scope of beneficial owners/ship

10. Our primary concern is that the provisions in the entirety of the Bill, and the proposed amendments seem to only apply to shareholders, or that beneficial ownership is defined as a natural person who exercises influence or control over shares. ***We submit that this is an inappropriate scope of beneficial ownership and does not take into consideration other forms of direct and indirect ownership and control or other corporate structures.***
11. We highlight the inclusive, legal definitions of a beneficial owner is imperative to ensuring that regulatory loopholes are not exploited and for policy to create an ease for competent authorities and entities with reporting obligations to understand and apply their legal responsibilities and obligations. Where beneficial ownership is defined by the percentage of shareholding as proposed it will not always correspond with the reality of control and ownership of a legal entity particularly the legal entities that pose high money laundering risks such as partnerships – which the Bill does not cover in the proposed amendments.
12. We note that section 56 recognizes the potential for illegitimate use of trusts to disguise ownership and trustees as beneficial owners. We welcome this provision as our research in the mining space illustrates the concerning growing trend in South Africa of mining right holders use of trusts to hide identities and ownership of assets, especially using trusts as a final step in a complex ownership chain of companies.¹ ***We submit that identifying the beneficial owners of trusts and the BO data of trusts or similar legal arrangements, or/and where they might appear in the ownership structure of a legal entity can help reveal a trust's control and ownership structure, as well as any companies contained within.***
13. Our concern however is that the Bill does not provide the definition or an identifying criterion for the BO of trusts. In practice all the parties to a trust have to be identified from the beginning when establishing the business relationship. Whereas thresholds commonly feature in

¹ <https://www.corruptionwatch.org.za/wp-content/uploads/2021/08/3727-CW-FLOW-OF-BENEFITS-MINE-COMM-REPORT-SPRD-LINKS.pdf> at page 21-23 last accessed 25 October 2021. See also https://transparency.org.au/wp-content/uploads/2020/10/TIA_EITI_Paper.pdf last accessed 26 October 2021.

definitions of BO of legal persons e.g. 5% or more voting rights or shares for companies - because of the nature of trusts and the difficulty in establishing who exercises ultimate control, or who ultimately benefits from the arrangement, no thresholds apply to trusts.

14. ***We submit that in order to ensure no beneficial owners are left undeclared, the Bill follow the FATF recognized approach and consider all parties to a trust as beneficial owners.***² The FATF approach requires that all parties to a trust should be identified and verified from the beginning, regardless of the proof of control.³
15. We do note that the area of BO in trusts is rapidly developing therefore the definition across the various jurisdictions vary which has the potential to cause some uncertainty in their application at a practical level. ***Our submission however, is that the Bill must include disclosure obligations that cater to situations where; trusts appear in the ownership structure of a legal entity; and companies appear in the ownership or control of a trust.***
16. We further note Clause 13 which proposes that a holding company can be a beneficial owner. ***We submit that a holding company cannot be a beneficial owner and guide the committee to best practice definitions which concludes that beneficial owners should be natural persons in the vast majority of competent jurisdictions.*** We submit that in the case of government-owned companies, stock exchange-listed and employee-owned companies, the Bill must include specific reporting requirements as discussed in the section below.

Ambiguous Provisions regarding the Establishment of a Central Register

17. The provisions do not make clear whether there is obligation to set up a central register. ***We submit that beneficial ownership registers or an alternative mechanism with equal efficiency***

² Guidance on Transparency and Beneficial Ownership, FATF, (Paris: FATF), October 2014, 9, <https://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-transparency-beneficial-ownership.pdf> last accessed 23 October 2021.

See also See: FATF Recommendations 2012 (as amended in October 2020), Interpretive Note to Recommendation 10, 60; EU AMLD, Article 31(1).

³ A similar provision has also been incorporated in the OECD, Standard for Automatic Exchange of Financial Information in Tax Matters: Implementation Handbook (2nd edn, Paris: OECD, 2018), para 266, which states that “the definition of [BO for trusts] excludes the need to inquire as to whether any of these persons can exercise practical control over the trust.

are a standard requirement for any form of beneficial ownership transparency and the Bill must explicitly state this position.

18. We submit that this is supported by the Financial Action Task Force (FATF) Recommendation 24 amendments on beneficial ownership and the most recent Interpretive Note⁴ focused on strengthening the global standard on corporate secrecy.⁵
19. We note that the FAFT Recommendations do not require centralised registers and has ‘encouraged’ countries to make the registers public. However, we bring to the attention of the committee that while Recommendation 24 requires countries to ensure that competent authorities have access to adequate, accurate and up-to-date information on the true owners of companies operating in their country, the FATF standard does not prescribe how access to BO information should be guaranteed. Each country decides through which mechanism this objective will be achieved.
20. ***We submit that the numerous investigative reports and scandals⁶ highlight the clear value of company ownership information on companies’ real owners. This is most conveniently achieved through implementation of beneficial ownership registers.⁷*** Our concern is that without regulatory certainty and elevating the minimum standard to address the grand corruption peculiarities within South Africa that enable anonymous companies to fuel corruption, tax evasion, and illicit financial flows more broadly, we submit that this will continue to have devastating consequences to citizens, the rule of law and democracy.
21. ***We further submit that requiring a public central register is considerably advantageous*** to the ability to access information quickly and effectively, enables ease of financial crime and investigations as it manages the tip off risks and does not alert potential suspects, enables scrutiny of the information for suspicious patterns, addresses inaccuracies or discrepancies and; a public register provides a public good that can contribute to lower due diligence and risk management costs for business.

⁴ <https://www.fatf-gafi.org/publications/fatfrecommendations/documents/public-consultation-r24.html> last accessed 26 October 2021.

⁵ Ibid.

⁶ <https://www.icij.org/investigations/pandora-papers/about-pandora-papers-leak-dataset/> last accessed 25 October 2021.

⁷ <https://www.transparency.org/en/news/fatf-consultation-global-standard-company-beneficial-ownership-transparency-key-fixes> last accessed 25 October 2021.

22. We further emphasise that while financial institutions – such as banks – and Designated Non-Financial Business and Professions (DNFBPs) – such as real estate agents, accountants and lawyers – play an important role in anti-money laundering and anti-corruption efforts as the information they collect as part of their compliance and due diligence work on the individuals behind the transactions is crucial for the authorities investigating financial crime. ***We submit that it is equally important to note the significant corruption vulnerability and limited scope for scrutiny to have financial institutions as the only source of beneficial information available to competent authorities.⁸ We submit that financial institutions and banks must be seen as supplementary measures to a centralised beneficial ownership register in order to help ensure that beneficial ownership information is accurate, complete and authorities can access it in a timely manner.***

Reporting Regime and Disclosure

23. We note the proposed amendment to section 56 of the Act places an obligation on companies to require from the registered share holder details of the identity of persons who hold beneficial interests. The provisions suggest two options as an obligation on companies: identify the true ownership of any shareholding in the company >5%; and identify the true ownership of all shareholdings, so as to avoid the vulnerabilities of fragmented holdings.
24. ***We submit that neither option is effective and that companies must be obliged to identify all true owners with an effective interest >5%. We further submit that this submission is most effective if the Act itself creates an obligation to report beneficial ownership.***
25. The DTIC must further enact implementing regulations and issue guidance on how to identify beneficial owners, as the success of this submission is case specific and will depend on the nature of the corporate structure and shareholdings.
26. Clause 8 proposes the companies must include BO information in the annual statement. As noted in the abovementioned section, without the explicit requirement of a central register with specific guidelines of reporting and enabling transparency for public scrutiny, ***we submit***

⁸ <https://www.transparency.org/en/press/reliance-on-information-from-banks-hindering-investigations-of-white-collar> last accessed 26 October 2021.

that this proposal is not an effective disclosure requirement for making BO information public nor is it effective as the only means of disclosing the information to the Companies' Register.

27. We submit that BO information in annual statements can create data gaps and vulnerabilities for verification as the information could be out of date by the time of the disclosure and a company could make changes just before reporting to disguise ownership. Additionally, for listed companies annual reporting will only provide a snapshot at one moment of time which will not be helpful for effective public scrutiny.
28. We note and welcome the requirement for companies to report changes 5 days after end of month and submit that it is a necessary part of the reporting regime. However, we also want to bring it to the committee's attention that this form of reporting will only provide a snapshot for stock-exchange listed companies.
29. We hope our submissions are useful to the committee. Further, kindly note our request to participate in the parliamentary hearings and to make oral submissions before the committee.

Submitted by Corruption Watch on 28 October 2021

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