

Corporate Tax and Company Ownership Transparency

Montenegro 2020 report

Recommendations



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Introduction

A fair tax system is essential for a well-functioning society. The arrival of the Covid-19 pandemic has made it painfully obvious just how valuable tax-funded resources, and their correct allocation, are to the proper functioning of our health systems. “The State of Tax Justice 2020”, [1] by Tax Justice Network showed that Montenegro has a total annual tax loss of \$107,096,593 (of which \$106,190,277 was lost due to corporate tax abuse). This tax loss could have paid the annual salaries of 10,313 nurses, who would have been essential in helping fight the pandemic.

Currently, companies in Montenegro are subject to a 9% corporate tax rate, considered one of the lowest in Europe. This, coupled with the fact that there is high secrecy around corporate taxes and a lack of transparency on company ownership data means that the current system in Montenegro is facilitating fraudulent corporate behaviour, tax secrecy and tax loss. This document will address the systemic issues around lack of transparency of corporate tax and beneficial ownership, offering recommendations.

[1] https://taxjustice.net/wp-content/uploads/2020/11/The_State_of_Tax_Justice_2020_ENGLISH.pdf

Tax Loss and Financial Secrecy in Montenegro

In their report “The State of Tax Justice 2020”, [2] Tax Justice Network offers the below calculations on tax loss in Montenegro:

- Total annual tax loss \$107,096,593;
- Annual tax loss due to corporate tax abuse \$106,190,277;
- Annual tax loss due to offshore tax evasion \$906,315;
- Total tax loss in number of nurses’ annual salaries 10,313 nurses.

The Financial Secrecy Index, which ranks jurisdictions according to their secrecy and the scale of their offshore financial activities, gave Montenegro an overall secrecy score of 60, which is below the global average. [3] Areas in which it was deemed “exceptionally secretive” were:

- Indicator 3 – Recorded Company Ownership;
- Indicator 5 – Limited Partnership Transparency;
- Indicator 6 – Public Company Ownership;
- Indicator 7 – Public Company Accounts;
- Indicator 8 – Country by Country Reporting;
- Indicator 10 – Legal Entity Identifier;
- Indicator 14 – Tax Court Secrecy;
- Indicator 18 – Automatic Information Exchange.

As we can see, it is corporate tax abuse that is causing the most annual tax loss for Montenegro, which is being facilitated by the current tax and corporate secrecy levels in the country.

[2] https://taxjustice.net/wp-content/uploads/2020/11/The_State_of_Tax_Justice_2020_ENGLISH.pdf
[3] <https://fsi.taxjustice.net/PDF/Montenegro.pdf>

Systemic Issues and Recommendations

1. The complete company register in Montenegro is not publically available

All companies in Montenegro must record all owners in the Central Registry of Business Entities,[4] yet only basic information is available online. In addition to this, according to the Financial Secrecy Index, information on complete company ownership isn't always available online, especially when this concerns limited partnerships and limited liability companies. [5]

Companies can often have complicated ownership structures. Without an open and transparent company register it is not possible to see these the full extent of these structures. This can lead to fraudulent shell companies going undetected, achieving public contracts and squandering public funds.

Recommendation: Complete, full and updated information on all owners of all companies in Montenegro should be publically available for free in the Central Registry of Business Entities.

2. Montenegro does not have a beneficial ownership register

Beneficial ownership registers publically identify the natural persons who ultimately own, control or benefit from companies. This information is one of the key tools used to investigate and eventually prosecute those involved in financial crimes. Without transparency of beneficial ownership, an environment is created that allows for the creation of shell companies, which leads to corruption, illicit cash flows and tax evasion, evidently illustrated by the Panama Papers. [6]

Even under normal circumstances, procurement is a high-risk area to corruption. With the arrival of the Covid-19 pandemic, however, this risk was increased exponentially as we saw urgent spending, accelerated procurement and relaxed rules across the globe, creating an environment where corruption could thrive. [7] The lack of data on beneficial ownership meant that governments couldn't be sure who they were trading with, allowing corrupt actors to profit from a lack of oversight. Subsequently, we saw squandering of public money, failure to properly allocate much needed resources, and as a consequence those on the front line ran short of vital equipment needed to save lives.

The fact that there is no beneficial ownership register in Montenegro, means that the system is facilitating corruption and wasting of public funds.

Recommendation: Establish a publically available, free, centralised beneficial ownership registers for all companies in Montenegro.

[4] <http://www.crps.me/>

[5] https://fsi.taxjustice.net/database/dbr_Jurisdiction.php?Juris=ME&Per=20

[6] <https://www.transparency.org/en/news/panama-papers-four-years-on-anonymous-companies-and-global-wealth>

[7] <https://www.transparency.org.uk/covid-19-has-created-conditions-which-corruption-health-procurement-can-flourish-heres-how-open>

3. The Law on Free Access to Information states that public authorities may deny access to information that is a business or tax secret. This exception goes against internationally accepted standards.

According to Article 14(6) on the Law on Free Access to Information a public authority may limit access to information or part of the information, if it is a business or a tax secret in accordance with the law.

Montenegro has signed and ratified the Council of Europe Convention on Access to Official Documents, which came into force on 1 December 2020. This Convention lists a set of internationally accepted exceptions to accessing official documents – the specific limitation of access due to a business or tax secret is not an internationally accepted limitation. Therefore, in using this exception, Montenegro is going against its international obligations under the Convention on Access to Official Documents.

Recommendation: The business or tax secret exception under Article 14(6) of the Law on Free Access to Information should be removed.

4. Corporate taxes are considered tax secrets under The Law on Free Access to Information, they are not published proactively nor are they released in response to freedom of information requests

After the introduction of the exemption on releasing information that is considered a business or a tax secret under Article 14(6) on the Law on Free Access to Information, in practice there has been a severe lack of transparency of corporate taxes in Montenegro, for both state-owned and private companies.

Data on the calculation of tax liabilities of the state-owned companies, as well as information on income taxes have been declared a tax secret by both the Administrative Court [8] and the Supreme Court [9] and are therefore not available to the public.

Data on taxes paid by private companies are not available to the public. After the amendments to the Law on Freedom of Information that introduced tax secret, the Agency for Free Access to Information (the Agency) stated that it was lawful to deny access to this information under the new provision. Such decisions of the Agency were confirmed by both the Administrative and Supreme Court. [10]

[8] U.No.1601/17 of 26.02.2018

[9] Uvp. No.501/18 of 31.05.2018

[10] Uvp. no. 1314/19 of 19 September 2019, judges Dr. Vesna Vučković, Vesna Jočić and Stanka Vučinić

Recently, however, the Administrative Court has been seen to go against the view that private company taxes were to be considered a tax secret, stating:

"For now, the court cannot accept as a well-founded conclusion of the administrative bodies that this is a tax secret, which, given its importance, is an obstacle to the exercise of the prosecutor's right to free access to the requested information. This is bearing in mind the fact that the Tax Administration, in addition to the list of tax debtors, also publishes the White List - a list of the most regular taxpayers." [11]

The Administrative Court should continue with its recent opinion and take steps to implement it in practice, thereby setting a precedent that creating a blanket ban on tax secrets (of both private and state-owned companies) is an obstacle to the right to information. In line with this, public bodies should now start releasing this information, although this has not yet happened.

Not only would disclosing this information in response to freedom of information requests facilitate individuals in the fulfilment of their fundamental right to information, but proactive disclosure of corporate tax information (both state-owned and private companies) would help regulators to police corporate governance and apply political pressure for good tax policy. [12] In addition, disclosing corporate tax information will act as a deterrent to tax evasion or aggressive tax positions, and ultimately increase tax compliance, especially for businesses that rely on a good public image and customer loyalty.

Good examples of tax transparency can be seen in the Nordic countries which release varying forms of taxable income and taxes paid for companies and private individuals.

In terms of corporate tax disclosure, taxable income is released publicly for all Swedish companies, and both taxable income and the tax liability are publicly available in Norway. Finland annually releases tax information on corporations and tax syndicates, this information includes name, address and corporate codes. In addition, the following are public information: 1) taxable income and property; (2) the total amount of taxes imposed; (3) the total amount of withholding tax; (4) the amount to be levied or refunded in the course of tax collection. [13]

In terms on tax disclosures of private individuals, Finland, Sweden, Iceland and Norway have some sort of public disclosure at a personal level. Norway even more exceptional in that it publishes this information online. In order to improve the balance between transparency and privacy, Norway and Sweden taxpayers can see who has viewed their information.

This transparency around taxes makes it hard for people to consider tax evasion, and it helps keep companies in check, both in terms of declaring profits and when it comes to offering competitive salaries, thereby decreasing the gender pay gap. [14]

Recommendation: State-owned and private company tax information should not be considered to be a tax secret. The Government of Montenegro should ensure at least some form of public access to corporate taxes, with information released proactively and reactively in response to freedom of information requests, subject only to acceptable exceptions.

[11] U. no. 7606/18 of 05.05.2020

[12] <http://www5.austlii.edu.au/au/journals/eJITaxR/2015/4.pdf>

[13] Finland's Tax Transparency: EATLP Annual Congress 2018 Tax Transparency Finland Dr Kristiina Äimä

[14] <https://theculturetrip.com/europe/norway/articles/norway-country-public-tax-returns/>

5. Lack of transparency of tax-related court proceedings

In Montenegro, full text of judgements / verdicts issued by both criminal and civil tax courts are not always published online for free. The “Rule of Law Department” of the Organisation for Security and Cooperation in Europe (OSCE) makes a direct connection between the Universal Declaration of Human Rights and public access to court judgements:

“The obligation of states to ‘make public’ the decisions of their courts is found within the provisions on ‘the right to a fair trial’. This right stems from Article 10 of the Universal Declaration of Human Rights (1948) and has been elaborated and set down in binding form in the International Covenant on Civil and Political Rights (ICCPR) and the European Convention on Human Rights and Fundamental Freedoms (ECHR)”. [15]

Preventing public access to tax court judgments shields those who are using the system to avoid paying taxes and may result in important court decisions that have an impact on the public’s revenue, being made without the public’s knowledge.

While all tax proceedings should be public, in order to address data protection concerns, balancing the taxpayer’s right to privacy and the public’s right to transparent judicial proceedings, specific personal data of taxpayers could be redacted from verdicts, to the extent that court verdicts contain such data. Yet, while anonymisation in exceptional circumstances, such as to protect victims’ lives or minors, is acceptable, anonymisation should not be used for all or most decisions as this would hinder public accountability. [16] A good example has been seen by the Canadian Customs and Revenue agency, which publishes court convictions for tax fraud and releases the names of offenders.

Recommendation: Tax proceedings should be made public, with the possibility to redact specific personal information in exceptional circumstances.

6. Tax avoidance and uncertain tax schemes do not have to be reported

Regarding tax avoidance schemes, tax advisers are not required to report on certain tax avoidance schemes they have used/sold/marketed to their clients. Additionally, tax advisers are not required to report on details of uncertain tax positions for which reserves have been created in the annual accounts. Requiring tax avoidance and uncertain tax schemes to be reported, at least annually, would act as a huge deterrent.

[15] Organisation for Security and Co-operation in Europe, ‘Access to Court Decisions: A Legal Analysis of Relevant International and National Provisions’, 2008, 5 https://www.right2info.org/resources/publications/publications/OSCE_AnalysisAccessToCourtDecisions17092008.pdf

[16] <https://fsi.taxjustice.net/PDF/14-Tax-Court-Secrecy.pdf>

In addition to this, those who have been found to commit tax evasion should be publically disclosed. In certain countries, there is public disclosure of information about tax evaders:

In Greece the law states that the presentation of a new budget must be accompanied by the names of tax evaders in the previous year compiled by the finance ministry;

In New Zealand the Commissioner of Inland Revenue regularly releases a document entitled "Tax Evaders Gazette" that lists those taxpayers who have been prosecuted or had penal tax imposed for evading their taxation obligations; as of April 1997 the Commissioner is able to also publish the names of those taxpayers involved with "abusive tax avoidance."

Recommendation: There should be mandatory disclosure rules requiring tax advisors (and other intermediaries e.g. accountants and lawyers) to report on aggressive tax planning schemes they have sold to their clients. These mandatory rules should also require uncertain tax positions to be reported in annual financial accounts. Those found to be evading tax should be publically disclosed.

7. Tax audits are deemed to be tax secrets

The Agency has confirmed the decisions of the Tax Administration that the data on inspection audit are a tax secret, and such decisions are also confirmed by the Administrative Court. The Supreme Court also finds that data on taxpayer control should be hidden from the public, even in cases where there is a suspicion that a criminal offense has been committed. [17]

As with the release of court proceedings concerning tax, the release of audits could be used as a deterrent strategy available to a tax authority, utilised to improve compliance.

Recommendation: Tax audits should be made public, and used as a tool to ensure compliance with tax obligations.

Conclusion

With a Financial Secrecy Index score of 60, and an annual loss of \$106,190,277 due to corporate tax abuse, Montenegro needs to address the above systemic issues surrounding tax and corporate ownership transparency. Public disclosure of corporate taxes and beneficial ownership should be seen as part of an overall strategy to increase taxpayer compliance.