

Institution: City, University of London (City)		
Unit of Assessment: 19 Politics and International Studies		
Title of case study: A new Equity Mapping forensic technique to prevent illicit financial flows, improve corporate regulation, and aid investigative journalism		
Period when the underpinning research was undertaken: January 2010 - ongoing		
Details of staff conducting the underpinning research from the submitting unit:		
Name(s):	Role(s) (e.g. job title):	Period(s) employed by submitting HEI:
Ronen Palan Anastasia Nesvetailova	Professor Professor	September 2007 to present September 2012 to present
Period when the claimed impact occurred: April 2017– Dec 2020		
Is this case study continued from a case study submitted in 2014? No		
1. Summary of the impact		
<p>Using equity mapping, Palan, Nesvetailova and their CORPLINK team have developed an innovative technique for capturing and interpreting the inner architecture of modern firms; their technique empowers regulators by providing concrete evidence of gamesmanship and jurisdictional arbitrage perpetrated by the corporate sector. The OECD, and its program on illicit finance in the energy trading sector, is using the results of CORPLINK's study to map risks in the sector and improve regulations. In addition, based on the team's direct input, the Extractive Industry Transparency Initiative (EITI), the global standard for the good governance of oil, gas and mineral resources, introduced specific changes to its 2020 guidelines, which have already been implemented by companies including Trafigura. Furthermore, journalist Carole Cadwalladr of <i>The Observer</i> reached out to Palan in 2017 to aid her investigation and inform her reporting on the way in which money is funneled into political financing in the UK, resulting in her subsequent groundbreaking exposé on Cambridge Analytica and Facebook.</p>		
2. Underpinning research		
<p>Palan and Nesvetailova's research on offshore havens has centred on the concept of jurisdictional arbitrage. [3.1, 3.2, 3.3] This concept secured a £1.6million advanced European Research Council-funded project, CORPLINK, which investigated the use of modular corporate structures in modern corporate ecology, a technique used by companies to benefit from gaps, loopholes, or omissions in state's laws and regulations. [3.4] Contrary to common perception, multinational enterprises (MNEs) are not single entities but composed of separate legal persons, or subsidiaries. Each subsidiary has its own set of directors, files annual accounts, and engages with other members of the group on an 'arm's length' basis. MNEs typically establish hundreds, if not thousands, of subsidiaries, allocating intangible rights to different arms of the same group, transferring funds directly or indirectly through financial swaps and derivatives, thereby creating a complex, layered corporate structure that is highly opaque. [3.5] Obscurity within the corporate structure and financial transfers are often used to arbitrate rules and regulations, including taxation of states. The result is that sophisticated MNEs can end up paying little or no corporation tax whilst avoiding liability and responsibility for their actions. Regulators have long been concerned that complex MNEs 'game' national and international regulations by using internal transfers between different arms of the same group. [3.4, 3.5, 3.6] In an attempt to address this issue, various policy routes were explored by regulatory agencies, led in particular by the Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting (BEPS) program. Using existing analytical tools, BEPS could identify generic types of arbitrage; yet the BEPS initiative was unable to identify whether or not such techniques were being used by specific corporate entities, and if so, where and how. Lacking information on corporate structures, regulators rely largely on whistleblowers, or on ex-lawyers of corporate organisations to shape regulations. [3.4]</p>		

The CORPLINK team devised a novel technique for mapping corporate structures involving an algorithm that collates information from the Orbis database, ‘cleans’ the data, and presents a visual map (equity map) of the organisation. [3.4 and Fig. 1]

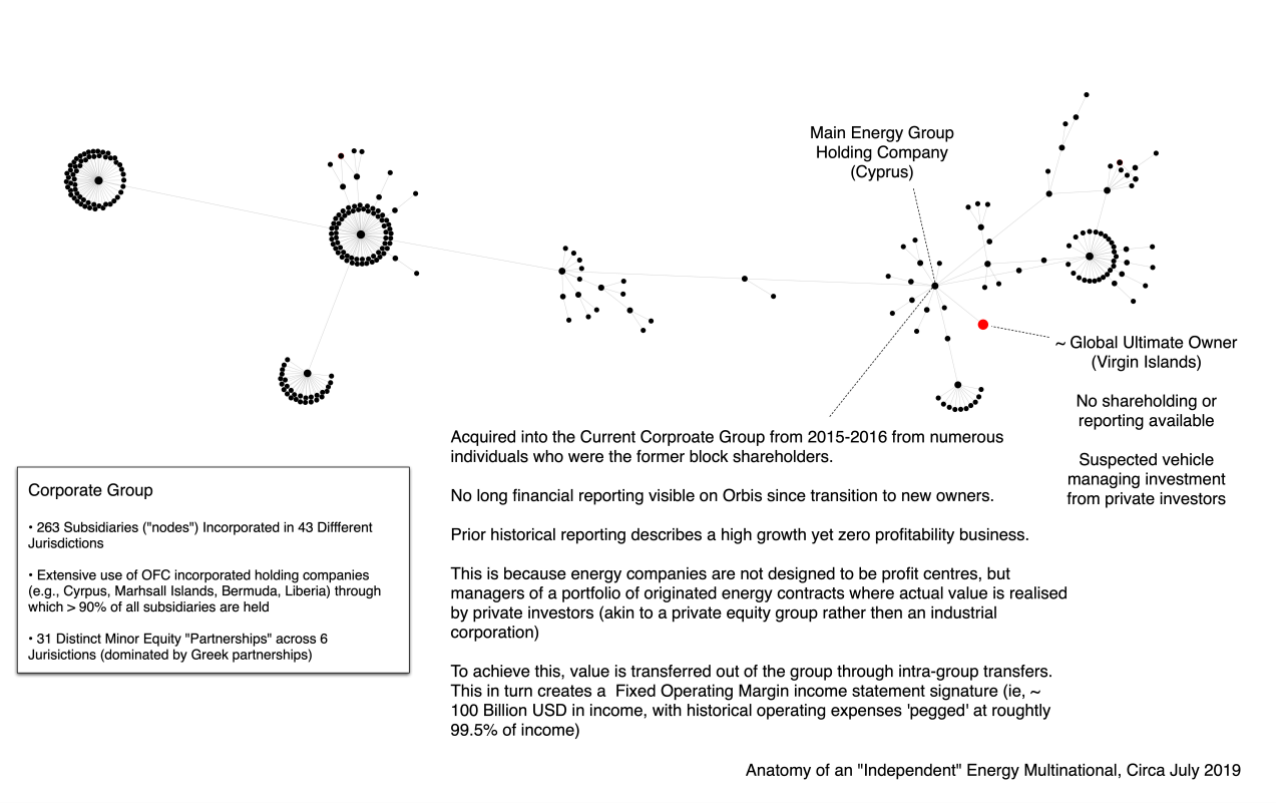


Fig. 1. CORPLINK's equity mapping technique demonstrating corporate subsidiaries of a multinational energy company.

The research team correlated corporate maps with shareholder and accounting data to identify the existence and location of arbitrating structures in the corporate ecology. In doing so, the CORPLINK method created new possibilities for going beyond the generic approach to jurisdictional arbitrage. An area of ‘known unknowns’ could now be mapped in detail that had previously been unavailable; this equity mapping approach identifies with a great degree of confidence the precise location of arbitrating structures and the amount of revenues they control among the 100 largest multinationals in the world. [3.4] The team’s method was further refined in a consultancy project undertaken for the OECD on energy trading and adapted to identify patterns of organization in the energy sector that can pose illicit finance risks. [3.6] The analysis demonstrated that the sector, and in particular the five largest independent energy trading firms with a combined turnover in excess of USD \$800 billion per year, are the most opaque organisations, operating almost exclusively through offshore financial centres.

3. References to the research (maximum of six references)

3.1 Nesvetailova, A., Palan, R. (2014). ‘Elsewhere, ideally nowhere: shadow banking and offshore finance’. *Politik*. 16(4), pp. 26-34. DOI: [10.7146/politik.v16i4.27559](https://doi.org/10.7146/politik.v16i4.27559)

3.2 Palan, R. (2020). ‘An evolutionary approach to international political economy: the case of corporate tax avoidance’. *Review of Evolutionary Political Economy*. 1, pp. 161-182. <https://doi.org/10.1007/s43253-020-00017-0> .

3.3 Palan, R. (2014) ‘Where the struggle against international tax avoidance is heading: multi-jurisdictionality’, *The FSC Report 2014*, pp.11–14.

3.4 Philips, R., Petersen, H., Palan, R. (2020). 'Arbitrating Sovereign Rules: Estimating the Share of Corporate Income and Profits Controlled by OFC-based Subsidiaries'. *Journal of International Business Policy*. <https://link.springer.com/article/10.1057/s42214-020-00069-3>

3.5 Nesvetailova, A., Guter-Sandu, A., Palan, R., Millo, Y. (2018). *Tax Evasion and Avoidance Through Financial Engineering: The State of Play in Europe*, 77.

https://researchcentres.city.ac.uk/data/assets/pdf_file/0010/582787/CITYPERC-WPS-2018-03-Nesvetailova-et-al.pdf

3.6 Nesvetailova, A., Palan, R., Petersen, H. and Phillips, R. (2020). *IFFs and Commodity Trading: Opportunities for Identifying Risks in Energy Trader's Financial Conduct Using Groups' Corporate Filings*. https://researchcentres.city.ac.uk/data/assets/pdf_file/0005/583565/IFFs-AND-COMMODITY-TRADING-final-oct-2020-.pdf

Indicators of quality for underpinning research

Three of the outputs were published in prestigious academic journals which apply a rigorous peer-review process prior to acceptance of papers.

Grant funding

Ronen Palan. Corporate Arbitrage and CPL Maps: Hidden Structures of Controls in the Global Economy (CORPLINK). European Research Council (ERC) Advanced Grant. 1 December 2016 - 30 November 2020. Funding value: £1,617,794. Grant Reference Number: [694943](#).

4. Details of the impact

Understanding illicit financial flows and aiding corporate regulatory policy

In July 2018, the OECD secretariat set up an Anti-Corruption Task Team (ACTT) to investigate the role of energy trading companies in illicit financial flows (IFFs) and invited Nesvetailova to serve as expert advisor and develop a program of work on IFFs and development, with a particular focus on commodity trading. [5.1] The task team concluded that IFFs operate through a global financial infrastructure, including banking and clearing systems, and company networks (subsidiaries, affiliates, holding companies), spanning both onshore markets and offshore financial centres and hybrid spaces. To better understand these global networks, the Team Lead of Governance for Development of the OECD commissioned the CORPLINK team to produce 25 equity maps of selected oil trading companies to profile and classify these energy-trading entities according to their ownership, equity, and financial accounting structures. The aim was to assess the potential risk of IFFs and to shed light on the ways in which corporate identities involved in the oil and gas trade create and maintain conditions (complexity, dynamism, opacity, etc.) that might be conducive to illicit financial flows.

The EM technique is a new, previously unused tool, which has enabled the OECD to take a closer look at the inner structure of corporate organisations. Whereas it was previously known that firms create opacity through their legal structure that allows them a degree of freedom from scrutiny, the CORPLINK study gave the ACCT's programme concrete evidence of the existence of structural weaknesses in the governance systems of the main players in this field, weaknesses that may sustain illicit financial activities. The study allows the program, in addition, to take a deeper dive into 'who exactly are we regulating?' and 'how does regulation work in a world of decentered corporation'? It also empowers regulators to develop measures to counter these weaknesses in the governance structure of the industry, limiting scope for IFF activities. This is something that could not be done by regulators before. In her testimonial the Team Lead writes: "the work produced by City's CORPLINK team is entirely greenfield and brings a crucial dimension to the OECD's Development Co-operation Directorate program of work and to our understanding of illicit financial flows and commodity trading, clarifying the structure and functioning of oil commodity traders, including their exceptionally high use of offshore financial centres...With domestic resource mobilisation at the top of the DAC [the OECD's Development Assistance Committee whose participants include 30 development ministers across the globe for the purpose of promoting development co-operation and reviewing policy issues] agenda, the findings

presented by CORPLINK...will contribute to raising awareness and steering future work at the OECD towards effective strategies for countering trade-based money-laundering and rendering corporate taxation rules more efficient.” [5.2]

In light of the findings from the OECD project, the Policy Director of the Extractive Industry Transparency Initiative (EITI) sought advice from Palan and team on developing new reporting guidelines for companies involved in the purchase of energy, gas and minerals. Published in September 2020, [5.3b] the guidelines implemented Palan’s suggestions to include contextual information about the buying company and specific registration details with a view to increasing company transparency, i.e. in the section on ‘Who is buying the product’ the EITI has added ‘buying entity’ and now requests the full name and country of registration of the buying company. [5.3a, 5.3b] As a result of these changes to EITI’s guidelines, companies such as Trafigura, with a turnover circa USD200 billion a year, have already complied, “exceed[ing] prior disclosures made” according to its CFO, “to build confidence amongst existing and prospective SOEs (State-Owned Enterprises) [...] and to ensure that those same SOEs are able to maintain trust amongst the citizens and wider civil society that they serve” by shining more light on its commercial activities. [5.3c, p. 3] EITI hopes to get more companies on board “with this kind of reporting in the coming year” [5.3a], attributing the contribution to more useful disclosures directly to Palan’s input. [5.3a, 5.3b]

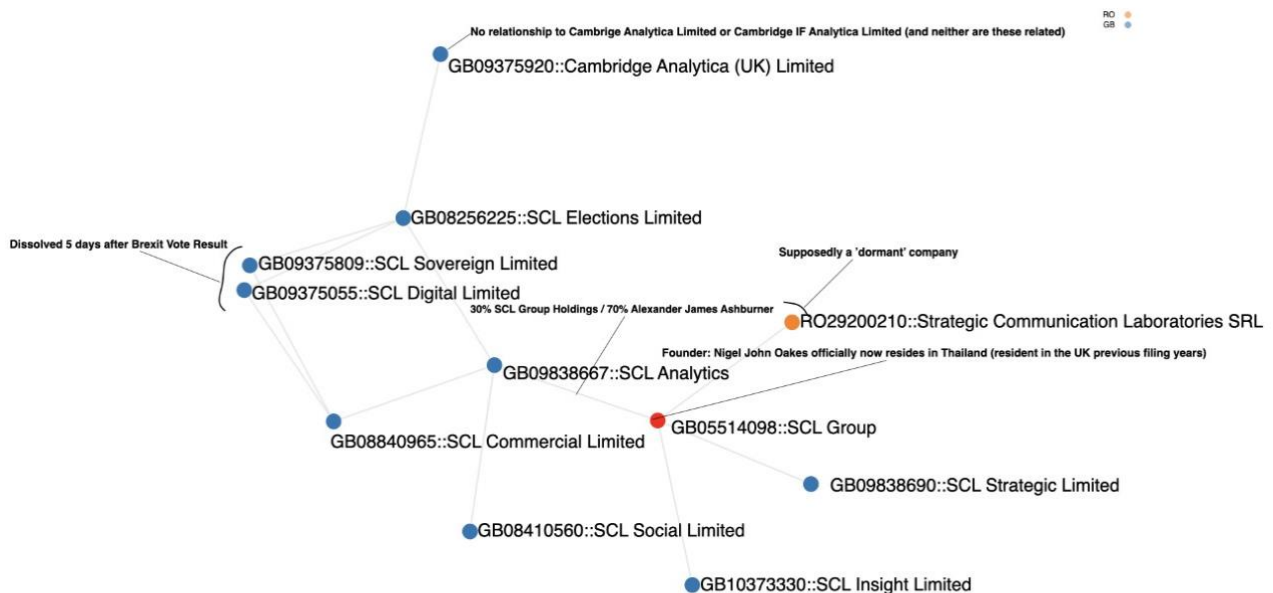


Fig. 2. CORPLINK’s equity map of Cambridge Analytica revealing SRL and SCL Holdings as subsidiaries.

Using CORPLINK’s equity mapping technique to underpin investigative journalism

Observer journalist Carole Cadwalladr was the first investigative journalist to explore the strands linking Cambridge Analytica, Trump and Brexit. Cadwalladr reached out to Palan for information and proof of the “dark undertow connecting us all globally” [5.5, 8:41] of which Cambridge Analytica played a role, initially requesting details on Arron Banks and First Bank Luxembourg. Palan provided Cadwalladr with an equity map drawn using their forensic technique which revealed that most of the work had been conducted not by Cambridge Analytica, but by SCL Group Holdings (Fig.2). The analysis identified previously unknown links among different members of the SCL group and the Leave/Remain campaigns and proved a turning point in the investigation. In the words of Cadwalladr, “I think you have turned up something...I have never heard of SCL Sovereign and SCL Digital.” [5.4] Cadwalladr used the equity map displaying Cambridge Analytica’s offshore companies to fuel her investigation and subsequent groundbreaking exposé on Cambridge Analytica and Facebook and went on to give her TED conference talk in April 2019

(with >4 million views) in front of Silicon Valley's tech giants. [5.5] These revelations had widespread reach and tapped into an investigation by the UK Information Commissioner's Office (launched in 2017) into the use of personal information and political influence. In a letter to Parliament in October 2020, the Information Commissioner disclosed that as investigators were closing in on SCL/Cambridge Analytica, the company had been "drawing up plans to relocate its data offshore to avoid regulatory scrutiny; [The Information Commissioner's Office] followed up their complex company structure with overseas counterparts and concluded that while plans were drawn up, the company was unable to put them into effect before it ceased trading." [5.6] In her public statement, the Commissioner summed up how Cadwalladr, in reporting on this topic, had "transformed the way that people around the world understood the value of their personal data and their relationships with social media giants." [5.7]

5. Sources to corroborate the impact

5.1 Email from the OECD inviting Nesvetailova to join the Anti-Corruption Task Team (ACTT)

5.2 Testimonial from the Team Lead for Effective, Inclusive and Accountable Institutions, OECD, Paris, France

5.3a Email from the Policy Director, Extractive Industry Transparency Initiative in Oslo, Norway

5.3b Extractive Industry Transparency Initiative's *Reporting Guidelines for companies buying oil, gas and minerals from governments* (September 2020), pp. 11-13.

<https://eiti.org/document/reporting-guidelines-for-companies-buying-oil-gas-minerals-from-governments>

5.3c Trafigura's *Payments to governments report* (2020)

<https://www.trafigura.com/media/3004/2020-trafigura-payments-to-governments-report.pdf>

5.4 Email correspondence between Cadwalladr and Palan

5.5 Carole Cadwalladr (April 2019) TED talk, 4,199,334 views

https://www.ted.com/talks/carole_cadwalladr_facebook_s_role_in_brexit_and_the_threat_to_democracy?language=en

5.6 Letter from the UK Information Commissioner to House of Commons' Chair of Digital, Culture, Media and Sport Select Committee, dated 02.10.20 https://ico.org.uk/media/action-weve-taken/2618383/20201002_ico-o-ed-l-rtl-0181_to-julian-knight-mp.pdf (clause 11, p3.)

5.7 *The Observer* (11.10.20) Editorial: The Observer view on the information commissioner's Cambridge Analytica investigation.

<https://www.theguardian.com/commentisfree/2020/oct/11/the-observer-view-on-the-information-commissioners-cambridge-analytica-investigation>