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Slovak experience with the Register of Public Sector Partners and its impact on public procurement

Introduction

Transparency of the ownership structures is more and more recognized as a necessity. In the globalized world complicated ownership structures are often misused for circumvention of national tax regulations and also for money-laundering. This problem was identified on the European level and afterwards it was implemented in the Slovak Republic by the introduction of the Register of Beneficial Owners.

However, the implementation of the European legislation in Slovakia has proved to be ineffective. In order to increase transparency, the Slovak Republic created a new form of identifying true beneficial owners. The outcome is the new Register of Public Sector Partners, which establishes unprecedented examination of the ownership

structures. However, the ambitious legislation faces numerous obstacles. The aim of this paper is to introduce the Slovak law which aims not only to fulfil obligations arising from the European legal standards but it examines the ownership structures even further.

After first years of practice, we will be able to identify which aims of the law seem to be successfully fulfilled and what are the limitations of the Slovak approach. This analysis may also serve as an example for foreign practice.

1. Slovak Register of Public Sector Partners – how is the ownership structure revealed?

1.1. European legislation and the new Slovak register

Basic purpose of the public procurement is not only to achieve more for less, but it is combined with increasing quality requirements. With the existence of complicated cross-border ownership structures, the demand for the higher transparency of this process is arising.¹ The need for transparency is underlined by numerous illegal activities that benefit from unclear ownership structures of legal entities.²

New trends and developments are reflected in numerous legal acts on both European and national levels. At the European level, it is necessary to point to the 4th and 5th anti-money laundering Directive.³

¹ A. Erridge, J. McIlroy, *Public Procurement and Supply Management Strategies*, "Public Policy and Administration" 2002, vol. 17, iss. 1, p. 52.

² Slovak Republic is trying to increase transparency of public procurement with progressive approach to electronic services. Register of Public Sector Partners may be considered a partial outcome of these efforts. Compare: M.M. Svidroňová, T. Mikuš, *E-procurement as the ICT Innovation in the Public Services Management: Case of Slovakia*, "Journal of Public Procurement" 2015, vol. 15, iss. 3, p. 317.

³ 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 and the most recent

Pursuant to the 5th AML Directive, it is important to know the real ownership structure of the beneficial owners so that information on the ownership structure of legal persons will be publicly available.⁴

This European legislation has been transposed into the Slovak legal system by Act No. 297/2008 Coll. on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing. The institution of beneficial owners became part of the Slovak legal system and along with a new Register of Beneficial Owners was also created. Entry in the register has become a condition for participation in public procurement. However, this process proved to be ineffective and inflexible in practice and therefore, it was replaced with a new concept.⁵

From this point, the Slovak regulation deviated from the European concept and introduced a specific approach to the disclosure of information about persons entering into relations with the state, respectively public institutions. A different approach resulted in the creation of the Register of Public Sector Partners introduced by Act No. 315/2016 Coll. on Register of Public Sector Partners (“RPSP Act”)⁶, effective as of February 1, 2017. The aim of the new legal regulation is to cover the full range of public property management, not only public procurement, which represents only 20 percent of it.⁷ The requirement to identify beneficial owners under the AML regulations is

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.

⁴ Explanatory note (30) of the Directive (EU) 2018/843: “Public access to beneficial ownership information allows greater scrutiny of information by civil society, including by the press or civil society organisations, and contributes to preserving trust in the integrity of business transactions and of the financial system.”

⁵ P. Lukáčka, F. Petrek, *Register of Public Sector Partners and Related Obligations of Public Procurement Candidates*, “Acta Facultatis Iuridicae Universitatis Comenianae” 2019, vol. 38, iss. 1, p. 50.

⁶ In Slovakia, this legal regulation is also known as Anti-letterbox Act.

⁷ Former legal regulation based on the Register of Beneficial Owners was focused mainly on the public procurement. See explanatory note to the RPSP Act.

therefore maintained, however the implementation method is specific for the Slovak Republic.

1.2. Enhanced engagement and increased formality

The RPSP Act not only aims to broaden the scope of obliged entities, but it also introduces a new form for revealing the ownership structure of entities identified as Public Sector Partners. Obligated persons do not carry out their verification themselves, hence a simple declaration of honour by beneficial owners is no longer sufficient.⁸ Collecting relevant facts and determination of beneficial owners⁹ are entrusted to a selected group of third entities.

The definition of Public Sector Partner is formulated quite broadly. It consists of both positive and negative definitions.

The positive definition contained in Sec. 1 (1) aims to cover almost all cases of trading with public entities or drawing public funds.¹⁰ In order to reduce the administrative burden for small entities, the legislator also introduced a negative definition, consisting of numerous exceptions.¹¹ The determination whether an entity is or is not a Public Sector Partner is therefore not a trivial act and it requires a specific, formal examination. The formality of the process significantly increases the costs for the liable

⁸ Explanatory note to the RPSP Act states “(author’s translation)”: “Recent legislation does not sufficiently address the identification of beneficial owners as it is based on a solemn declaration of honour; the draft law abandons this concept and introduces a stricter beneficial owner verification regime.” Original Slovak wording: “Súčasná právna úprava nerieši dostatočným spôsobom identifikáciu konečného užívateľa výhod, pretože je založená na čestnom vyhlásení; od tohto konceptu návrh zákona upúšťa a zavádza sprísnený režim verifikácie konečného užívateľa výhod.”

⁹ Only the register of beneficial owners was replaced by the Register of Public Sector Partners. Legal definition of the beneficial owners is still contained in Act No 297/2008 Coll. The RPSP Act refers to this regulation in Sec. (2) d).

¹⁰ The positive definition covers mainly the cases of direct donations from public funds or EU funds and also entering into a contract with public entities; provision of health care covered by health insurance etc.

¹¹ Exceptions are conceived as financial limits or specific groups of non-regulated entities (e.g. public administration entities, public enterprises, persons working mostly in the non-profit sector, third countries and their authorities, etc.).

entity but, on the other hand, it should lead to more comprehensive conclusions comparing to the previous legislation.¹²

The whole process consists of two phases. The main aim of the first phase is to analyse the whole ownership structure of the company and to identify the beneficial owners. This phase is covered by the so-called entitled persons. The second phase consists of registration into the public register and it is entrusted to the District Court in Žilina. This District Court is responsible for registration of subjects for the entire Slovak Republic.

Under the RPSP Act, the most difficult and most responsible part of the process is the first step, i.e. identification of beneficial owners, therefore we will analyse it in the following section. The registration proceedings, held in front of the court, are on the other hand quite straightforward and the whole process is held solely on electronic basis.

The registration procedure was created as a *sui generis* procedure, consisting of: (i) data entry; (ii) modifications of registered data; and (iii) termination of registration. As the verification of the ownership structure was executed prior to the registration proceeding, the court only deals with the fulfilment of formal obligations. The whole responsibility for truthfulness and completeness of provided information is on the entitled person and the public sector partner.

The obligation to register lasts throughout the whole duration of a contract with a public entity. The term “contract duration” is understood as the period during which the Public Sector Partner receives funds or property benefits from the public entity. At this point the question arises whether the registration period should not be extended beyond the expiry of the contract duration. However, the principle of public scrutiny is here confronted with the personal data protection of beneficial owners and their right to be forgotten.¹³ Therefore, interference with the private rights of beneficial owners should not exceed justified reasons.

¹² See: A. Leontiev, M. Anderle, *Register konečných užívateľov výhod – stop pre schránkové firmy vo verejnom obstarávaní?* “Bulletin Slovenskej advokácie” 2017, vol. 23, iss. 1–2, p. 6.

¹³ Compare: Ch. Savia, *Processing Financial Crime Data under the GDPR in the light of the 5th Anti-Money Laundering Directive*, Örebro universitet Juridicum, vol. 1, p. 33.

1.3. Entitled persons and the identification of beneficial owners

The registration application must be submitted to the court by the so-called “entitled person”, which acts on behalf of the public sector partner. An entitled person shall be understood as: (i) attorney-at-law; (ii) notary; (iii) bank; or (iv) tax advisor with their place of business or registered office in the Slovak Republic.¹⁴

Prior to the submission of the application, the entitled person shall verify the registrant. This activity is *sui generis*, therefore it is independent of general activities of the entitled person. The relationship between the entitled and the obliged person is based on a contract governed by provisions under the RPSP Act and additionally by provisions on the control activity contract under the Commercial Code. This leads to an interesting legal construction which uses the status of certain regulated professions, for which the RPSP Act creates a new type of service.¹⁵

The RPSP Act does not contain an explicit manual for the verification of public sector partners. It only determines the criteria that must be fulfilled during execution of the verification. Pursuant to Sec. 11 (5), the entitled person must act: (i) impartially; (ii) with due care; and (iii) procure all available information on the registered subject and to evaluate it. Unlike due care determined under terms of the civil law (which is based on the Roman perception of due diligence), the RPSP Act establishes a new type of due care. Due care under the RPSP Act is characterised as an appropriate care connected with the function of the entitled person, which should be based on impartial professional evaluation of all available information. It is important to notice that the entitled person is obliged to evaluate the information it was provided with, but also information it could have obtained and which may affect its conduct.¹⁶

This definition of due care entails a fundamental interpretation problem. What kind of actions is the entitled person obliged

¹⁴ A foreign person who carries out one of the professions listed as entitled person must have its enterprise or branch located in Slovakia.

¹⁵ P. Lukáčka, F. Petrek, op. cit., p. 63.

¹⁶ See Sec. 11 (5) of the RPSP Act.

to perform in order to fulfil the legal precondition of due care? It is obvious that RPSP Act requires assessment on *ad hoc* basis. In general, revealing of the ownership structure should lead to accurate identification of specific natural persons – beneficial owners.¹⁷ However, it would be unjust to require from the entitled person knowledge of all jurisdictions under the consideration. Affidavits of registered entities are therefore still relatively common, as these may (to some extent) confirm due care of the entitled person.

After successful verification of the registered person, the entitled person submits a proposal to enter all relevant data into the register. As it was already stated, the process takes place in front of the District Court in Žilina and it is solely electronic. As the data examination is entrusted to the entitled person, the court does not examine the veracity of the application. It focuses exclusively on compliance with formal requirements.

Unlike the Commercial Register or similar registers, the Register of Public Sector Partners is built on a system of continuous verifications. In practice it means that successful registration does not end the list of the public sector partner's obligations. The identification of the beneficial owners must be carried out not only when the registered data have changed but also in legally enumerated cases¹⁸ (e.g. conclusion of a new contract or receipt of finances exceeding € 1,000,000 within 30 days) and also by December 31 of each calendar year. The latest amendment of the RPSP Act also introduced voluntary verification of beneficial owners.

1.4. Qualified notification and judicial review

By execution of registration, the court's position in the process does not end. In case of any doubts concerning correctness of entered data, the court can *ex officio* or on the basis of the so-called "qualified

¹⁷ When examining the status of a beneficial owner, the following must be examined pursuant to the definition contained in Act No. 297/2008 Coll.: direct or indirect impact of the person on corporate governance or creation of corporate bodies; share of the person on voting rights, equity or economic benefits, which must exceed 25 per cent.

¹⁸ See Sec. 11 (2) of the RPSP Act.

notification” examine the authenticity and completeness of the registered data. In such a case, the court carries out material research, including proper inquiry.

The qualified notification can be lodged by any private or public entity. This ensures truly a wide range of control opportunities. Effective watchdog activities are in this way available for civil society and NGOs.¹⁹

The purpose of the judicial review is to clarify factual situation and to draw consequences. In this respect the decision of the District Court in Žilina No. 5PExre/5/2018 of October 9, 2018, is significant and it states “(author’s translation)”:

The aim of the proceeding pursuant to Sec. 12 is not to verify the assets of beneficial owners..., or to solve potential crimes perpetrated by involved parties (including the offense of direct or indirect corruption or tax offenses). A strict distinction must be made between the competences of various law enforcement bodies... The importance of the Register of Public Sector Partners can be seen in particular in the creation of a publicly available database regarding entities entering into legal relations with the public sphere, which cannot be subsequently changed by registered entities.²⁰

It follows that the court shall examine solely the circumstances which may be relevant to assess the veracity of registered data. Any other questions should be subject of a separate procedure.

¹⁹ Only 26 out of 91 proceedings were carried out by the district court ex officio; the remaining proceedings were initiated on the basis of a qualified notification. The information is based on the official data of District Court Žilina provided to the author on the basis of Act No. 211/2000 Coll. on Free Access to Information. The data obtained refer to the state in December 2019.

²⁰ Original Slovak wording as follows: “Účelom konania podľa § 12 nie je preverovať majetkové pomery konečných užívateľov výhod..., či riešiť eventuálnu trestnú činnosť zúčastnených (vrátane trestného činu priamej alebo nepriamej korupcie či daňových trestných činov). Treba jasne rozlišovať medzi kompetenciami jednotlivých orgánov ochrany práva... Význam RPVS možno vidieť najmä v tom, že sa vytvorila verejne dostupná databáza údajov o subjektoch vstupujúcich do právnych vzťahov s verejnou sférou, ktoré nie je možné zapísanými subjektmi dodatočne zmeniť.”

Until major amendment of the RPSP Act²¹, it was unclear which factual state shall be relevant for the judicial review. The prevailing opinion was the time of submission of the qualified notification, respectively initiation of ex officio proceedings.²² The amending law confirmed this practice. A significant disadvantage of this approach is factual impunity of possible violation of the law in case the registered person remedied the situation before the commencement of the proceeding. Voluntary examination of registered data makes such impunity even easier than before the amendment.

If the court decides, on the basis of submitted evidence, to erase the entity from the Register of Public Sector Partners, the entity concerned cannot bring any appeal. Regarding the introduction of a two-year registration prohibition (in the event of erasure), the procedure before only single instance appears to be inadequate. From our point of view, this can seem as a legal shortcoming in the future since the revision procedure can be abused by the market competitors and we cannot also exclude possible inadequacies in the court investigation.

1.5. Impact of the new register on public procurement

Since obtaining of public funds is *de iure* excluded without entry in the Register of Public Sector Partners, the registration has a significant impact on the public procurement. The Act No. 343/2015 Coll. on Public Procurement explicitly states that the contracting authority cannot enter into a contract with an entity which is obliged to register in the Register of Public Sector Partners and this obligation has not been fulfilled.²³ This obligation also applies to the subcontractors of the liable entities. There is only one exemption from the aforementioned rule (related to the suppression of unnecessary administrative duties) – it does not apply to framework service agreements concluded between the contracting authority and several natural persons.

²¹ Made under Act 241/2019 Coll.

²² See decision of the District Court Žilina No. 5P Exre/5/2018 of October 9, 2018.

²³ See Sec. 11 of Act No. 343/2015 Coll.

The infringement of the aforementioned obligation linked to the public procurement is accompanied by numerous sanction mechanisms. Penalties are associated both with the omission of registration and also with registration of inaccurate data. Public entities are responsible for entering into a contract with an unregistered entity, i.e. the obligation to examine whether the successful tenderer has fulfilled its registration obligation lies on the contracting authority. Violation of this obligation is an offense punishable by a fine from € 1,000 to € 100,000.

The correctness of the data entered in the Register of Public Sector Partners is the responsibility of both (i) the public sector partner and (ii) the registrar (the so-called authorized person). Incorrect registration can result in a sanction imposed to the registered person or its statutory body; the erasure of the public sector partner from the register; or creation of a withdrawal right from the contract for the public institution. A subject erased from the register is also not entitled to submit new registration application within two years after the court decision.²⁴

2. Enhanced form for revealing the beneficial owners or unnecessary administration?

Probably the biggest disadvantage of the RPSP Act is the expensiveness of verification and registration proceeding. Remuneration for the verification depends on the requirements of the entitled person. The cost range is therefore quite wide. Total estimated costs for external services connected with verification of the beneficial owners clearly exceed 10 million euros per annum.²⁵ Such expenses create

²⁴ This change is introduced by the amending Act No. 241/2019 Coll. as of November 1, 2019. Before this amendment, the public sector partner was entitled to submit a new registration application directly after its erasure.

²⁵ According to the analysis of Transparency International Slovakia, the remuneration for the entitled person mainly varies from 250 up to 600 Euro. When estimating

considerable element for the entrepreneurs and it is often included in the price for services invoiced to the state. Therefore, it is appropriate to raise a question if it would not be better to determine exact price for the verification procedure.

Another problem is connected with the list of entitled persons. With respect to the aforementioned total price for services, it might be helpful if the verification process was carried out by a state authority. Undoubtedly an advantage would be the income for the state and also fixed remuneration for the whole process. On the other hand, currently the process is built on the responsibility for the entitled person and the partner of the public sector. In case the verification process is carried out by a state authority, the aim of the legal regulation would be endangered.

Issues connected with the RPSP Act are not only systemic but also interpretative. For instance, we can point to the basic definition of the “public sector partner” and its exceptions (i.e. part of the negative definition).²⁶ Interpretation problems with “one-off performance”, respectively “repeated performance” arise for instance in case of drawing finances from EU funds exceeding the €100,000 per annum limit. Funds are usually drawn several times a year but their total amount is predetermined. The application practice in this area is still not uniform. In our opinion, the use of EU funds should be probably seen as a one-off performance. Despite several instalments, it is still a claim for one performance. Interpretation problems also occur in some cases when it is necessary to assess if the remuneration is paid in instalments (i.e. it is a one-off performance) or if it is a repeated performance (e.g. payment of the rent).

the total verifications costs, the analysis calculates with 20,000 registered entities. As of March 2020, the number of registered persons exceeded 30,000 registered entities. For more see: <https://transparency.sk/sk/ako-dobrou-hodnotou-za-peniaze-je-protishrankovy-zakon/>

²⁶ Pursuant to Sec. 2 (2) and (3) of the RPSP Act, a public sector partner is not the one: a) who should be given a one-off performance arising from the contract which does not exceed € 100,000; or b) who should be given numerous partial or repeated performances arising from the contract which do not exceed € 250,000.

However, it is necessary to point also to the positive aspects of the RPSP Act. After three years of practice we can see first the results of the judicial decision – making practice. As of December 2019, the District court in Žilina held 91 cases concerning truthfulness and completeness of entered data: 65 cases were closed, of which 40 ended with a halt, 2 companies were erased from the register for breach of their obligations and 23 cases ended in another way. Totally 8 public sector partners were fined in the total amount of 540 thousand Euros.²⁷

Conclusions

By adoption of the RPSP Act, the Slovak Republic made a significant step towards transparency in public procurement. The new Slovak approach is in some aspects pioneering and a longer period of time is needed to evaluate its impact. Accordingly, many practical questions arise which need to be answered by application and practice.

In this article, we tried to describe the verification and registration process under the RPSP Act which can be interesting as an example for foreign practice and also to point out its shortcomings. From our point of view, it was rather a courageous decision to entrust the verification process to a closed list of entitled persons. Some critics oppose that a public entity would be more suitable for this task but from our point of view, the responsibility ties under the RPSP Act work quite sufficiently.

In general, the RPSP Act can be evaluated as an ambitious project with some progressive ideas (e.g. a new form of due diligence). We also positively evaluate the latest amendment that has major impact on some former interpretation issues.

²⁷ The information is based on the official data of District Court Žilina, provided to the author on the basis of Act No. 211/2000 Coll. on Free Access to Information. The data obtained refer to the state as of December 2019.

Słowackie doświadczenia w zakresie Rejestru Partnerów Sektora Publicznego i jego wpływu na zamówienia publiczne

Streszczenie

W artykule przeanalizowano niedawno zmienione ustawodawstwo Republiki Słowackiej, które ma na celu szczegółowe zbadanie istnienia beneficjentów rzeczywistych i które ma zasadniczy wpływ na sektor zamówień publicznych. Autor wskazuje na zalety i słabości Rejestru Partnerów Sektora Publicznego oraz opisuje unikatowe słowackie ustawodawstwo, które może w przyszłości stać się źródłem doświadczeń dla innych krajów Unii Europejskiej.