

Rosamaria Tristano

ESTONIAN E-RESIDENCY: A MODEL FOR EUROPE

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Coordinatore Editoriale: Serenella Quari

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E-mail: submissions@diritticomparati.it

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Rosamaria Tristano

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Avvocato, Università degli Studi di Palermo

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1. Freedom of establishment and its implications

Freedom of establishment, freedom of capital movements and freedom to provide services are widening the horizons of economic development¹, offering new opportunities for European countries and companies².

Today in fact it is easy to establish or transfer a company abroad, and, in some circumstances, it can also be really convenient because in the EU a company is subject to the national tax rules of the country where is resident, even when it is active all over the continent.

For this reason, European countries are in a sort of competition with each other and, particularly after the economic crisis of the last decade, they have tried to attract foreign companies and investments, in order to increase their economy.

Different countries adopted various tools: first of all, the offer of a competitive tax system, as in Malta, but also of technological advancement, as in Estonia.

2 The Maltese experience: a profitable tax system to promote foreign investments

The choice of a competitive tax system may be a useful tool to attract foreign companies wanting to preserve their revenues reducing taxation.

For this reason, some European governments, such as the Irish or some eastern European ones, launched a sort of tax competition, reducing their corporate tax rates, or signing with major contributors, like multinational corporates, tax deals, also called «sweetheart tax deals», that

¹ P. Juillard, *Freedom of Establishment, Freedom of Capital Movements, and Freedom of Investment*, ICSID Review - Foreign Investment Law Journal, 2000, Vol 15, No 2, pp 322–339

² Article 54 of the TFEU provides for freedom of establishment, that enables a company, as well as for people, to carry on an economic activity in a stable and continuous way within the European single market, and to move freely from one member state to another.

determines a fixed and even lower rate. In this way, they have become proper tax heavens, as well as the residency of choice of the largest companies which operate in Europe (Apple, Facebook, Google, and also Netflix, as recently revealed by the British think tank Tax watch³).

Malta takes advantage of a peculiar tax system too. First, in this island, are in force the territorial taxation principles, according to which only the income produced by a company within the Maltese borders is taxed, while the foreign income is exempted.

Therefore, many companies opt to settle or relocate in a country like this, reducing taxation lawfully: in fact, the Maltese tax authority imposes taxes on the income produced in Malta, and these revenues are not taxed in the country of origin of the company, in order to avoid the phenomenon of double taxation.

It is well known in fact that different countries, including Malta, have signed treaties and conventions (generally based on a model provided by the Organization for Economic Cooperation and Development, OECD) to coordinate their tax systems and limit their taxation of international business, in order to augment trade between signatory countries, and to prevent revenues to be taxed both in the country where they are produced and where their owners are resident.

Second, it should be added that Malta, despite of the formally elevated corporate tax rate, has in effect one of the most convenient tax systems in Europe: the official tax rate for companies is 35%, but when a foreign one settles in Malta, and pays dividends to its shareholders, benefits from a 6/7 tax refund of the amount paid for profits from commercial activities, or a 5/7 tax refund of the amount paid for profits generated by interests or royalties. So, the real rate falls considerably for foreign companies, down to 5%.

For example, an Italian company can establish its tax residency in Malta, even if it is managed by just a few Maltese persons and the shareholders are mostly Italian, and when it books its foreign income, the ultimate beneficial owners, in Italy, can claim an 85% refund on the tax levied in Malta on their dividends. The result is an effective tax rate of 5%, instead of the standard 35%.

The same tax system is suitable for trusts too. In Malta are in force the Trust and trustees act (Cap. 331) and the Hague Convention of July 1st 1985 on the Law applicable to trusts and on their recognition; the laws which govern the taxation of trusts in Malta are the Income Tax Act (Cap. 123) and the Income Tax Management Act (Cap. 372).

The competent authority to supervise trusts and trustee's activities is the Malta Financial Service Authority (MFSA).

The *Trust and trustees Act* is applied to trusts formed in Malta or regulated by Maltese law as the chosen applicable one, but it also recognizes and gives effect to trusts regulated by a foreign law or established abroad.

In addition, Maltese Courts have jurisdiction over Maltese trusts, but also over foreign trusts when the trustee is a Maltese resident, or trust property is situated in Malta, or the administration of the trust property is carried on in Malta.

³ The report «No tax and chill: Netflix's offshore millions» has been recently released by the British think tank Taxwatch and is only the latest in a string of such cases. It can be found online at the link: https://www.taxwatchuk.org/netflix_tax/.

According to the Maltese order, it is possible to relocate a trust to Malta, just like for companies, and on the basis of certain conditions, a trust can be led to Maltese taxation, so that its income is taxed in Malta: if the trustee is a Maltese resident and has been authorized by MFSA, he may elect to compute the chargeable income in relation to the revenues attributable to the trust as if it has been produced by a Maltese company, provided that the trust takes place by written form.

The request can be made within 30 days of the formation of the trust or the appointment of the Maltese trustee. Once made, the election is irrevocable, and the trust will be subject to taxation as a company. This means that distributable profits shall be allocated in the same way applicable to Maltese companies, and their distributions to beneficiaries shall be treated as if they were dividends distributed to shareholders. Consequently, the tax refunds foreseen for companies shall be applicable.

That's the reason why Malta has become one of the best places to set up investments or trust funds, and it's not a surprise that Italian shareholders control almost 8,000 Maltese companies and that the numbers of Maltese trade register are continuously growing, at a rate of 4-5% per year, with a total of more than 70 thousand at the end of 2016.

The downside is that companies or trust funds are frequently relocated to Malta for illicit reasons: it's common knowledge that one of the widespread techniques of money laundering or tax evasion is the segregation of capital assets by establishing a trust or set up a company abroad, in a country that ensures a high grade of opacity. In particular, the establishment of a trust may have the illicit aim to create a fictitious screen for the real possession of the assets, in order to circumvent tax authorities or obstruct the identification of their criminal origin.

In fact, when assets and saving of the potential tax avoider are entrusted to a trustee, who manages them, they are unrelated to their owner and untraceable by creditors and tax authorities and, in addition, attack a foreign trust is particularly difficult: one must first obtain a favourable judgment in his country, and then establish a new procedure in the jurisdiction of the country where the trust is established.

In 2017 the EIC (European Investigative Collaboration) carried out an articulated journalistic investigation that culminates with the publishing of the «*Malta files*» spread sheet, the result of an analysis exceptionally conducted on more than 100,000 classified documents, regarding the effective owners of foreign companies with Maltese residency. The authors of this inquiry argue that the generous Maltese system of tax credits is a perfect tool to wash money from criminal organizations, in fact the island «*works as a pirate base for tax avoidance inside the EU, and profiting from the advantages of EU membership, also welcomes large companies and wealthy private clients who try to dodge taxes in their home countries*»⁴.

Indeed, it was found that every year around € 2 billion are taxed in Malta as profits generated outside the island, so that € 200 million in tax receipts are retained in Malta⁵. Even

⁴ See: <https://eic.network/projects/malta-files>. On the EIC website is available the complete work, included all the articles published in the newspapers that cooperated in the investigation.

⁵ See: M. Vella, *Every year Malta wipes out €2 billion in foreign tax by giving shareholders 85% rebates on their tax*, in *Malta today*, 13 September 2016. Available at: https://www.maltatoday.com.mt/news/national/69486/every_year_malta_wipes_out_2_billion_in_foreign_tax_by_giving_shareholders_85_rebates_on_their_tax_#.Xa2Xfy9aaRu

nowadays statistics shows that thanks to the convenient tax system, the Maltese gross domestic product is dramatically growing: from 2017 it has increased from 4% to 8.9% in 2018, according to the provisional data released in March 2019 by the Maltese National Statistic Office, equivalent to more than 1 thousand euros. Nevertheless, investigations for tax evasion, money laundering and corruption are growing too, and they are conducted by tax authorities from all over Europe and beyond.

The «tax system trick» has now been discovered, and the attention of European governments and of the EU itself is constantly growing, together with stricter investigations and new laws, like the EU directive 2018/843, the 5th Anti money laundering directive, which introduces more effective anti-laundering instruments and is being transposed in all member states⁶.

3. The Estonian digital revolution

3.1 e-Estonia

A generous tax policy is not the only tool available for governments wishing to attract investments, and in these days the real breakthrough is technology, which is increasingly advanced and more and more affordable by everyone thanks to the Internet.

Technology, in fact, is an excellent tool to improve economic growth. That is why certain countries, relying on electronic advancements, are offering unique opportunities in order to attract foreign companies and investors.

One of the best and most successful examples is Estonia. When Estonia gained its independence from the Soviet Union, in 1991, had to catch up with the Western world in every way, for this reason, its government began adopting new technologies and optimizing its services to make them easily accessible, in order to become one of the most advanced digital society in the world.

The five cornerstones of the Estonian digital revolution are synergy between public and private sector, decentralization in different systems that dialogue together in a common platform, freedom of access to digital services, interconnectivity, and an open-ended processing. On these grounds, already in 1997 took its first steps «e-Estonia»: a government-sponsored project to move online almost all bureaucratic tasks, from voting to medical prescriptions⁷.

In 2000 were established the e-banking, e-Tax and e-government systems, and was officially introduced the digital signature; since 2001 the Registry is online, and since 2002 also schools operate on a digital platform⁸; in 2003 national databases were all unified and thanks to the «State portal» they interact with each other, and even the police is online, since 2005. In

⁶ See: V. Marria, *The EU's 5th Anti-Money Laundering Directive: What Does It Mean?* in *Forbes*, 13 September 2018. Available at: <https://www.forbes.com/sites/vishalmarria/2018/09/13/eu-5th-anti-money-laundering-directive-what-does-it-mean/#3dece95fa5d3>

⁷ On the Estonian Government's official website can be found constantly updated information and statistics. See: <https://e-estonia.com>

⁸ See: *E-Schoolbag*. Available at <https://e-estonia.com/solutions/education/e-schoolbag/>

2007 and 2011 Estonia used the i-Election system in a general election⁹, and between 2007 and 2008 the business register was moved online and the public healthcare system started working electronically; finally, in 2011 the «Smart Grid» program revolutionized the energy sector, giving consumers the possibility to control their consumption electronically. Add to these, there are also minor initiatives, like free Wi-Fi or apps to buy parking lots or train and bus tickets.

The success of the initiative is confirmed by high numbers: according to the Estonian government website, currently, 99% of services are online, 98% of Estonians have an ID-card, a 99.6% rate of banking transactions and a 96.3% rate of tax returns are made online.

3.2 e-Residency

A key part of this project is the e-residency, launched in 2014: it is an exclusively digital residence, that everyone, from every country, can obtain by an online request, and that allows to be part of the Estonian digital community¹⁰.

Estonian government website describes e-residency as «*a government-issued digital identity and status that provides access to Estonia's transparent digital business environment*» and «*allows digital entrepreneurs to manage business from anywhere, entirely online*»¹¹. e-Residency, in fact, is not an actual residency, neither a visa, nor an entry permit. It is different from citizenship, that is a status that assigns specific rights and duties: it is just a special form of identification, a transnational digital identity, that allows the use of the Estonian digital services and consent to administering a location-independent business online.

Through e-residency, information technology is used to allow a person to engage in society, politics or government, but without taking part in these physically: it has been defined as «*the civil, political and social rights of a citizen in their online activities, their political engagement, and activity through digital means, and their membership of an online community that is a distinct source of identity*»¹².

Thanks to this program, Estonia created a borderless digital society, that works as a complete end-to-end service, without phone calls, office visits or physical paperwork, which is facilitated by distributed databases in communication with each other. It means that e-residency works as a ledger that contains a list of transactions or contacts and is located on a decentralized

⁹ See: *Estonia's I-voting: more secure, more popular*. Available at <https://e-estonia.com/estonias-i-voting-more-popular-more-secure/>

¹⁰ e-Residency immediately intrigued the press. See: M. Paterson, *Embracing the 9 themes of digital citizenship in EdTech*, 2015. Available at <https://edtechmagazine.com/k12/article/2015/09/embracing-9-themes-digital-citizenship>; The Economist, *Estonia Takes the Plunge*, 28 June 2014. Available at: <http://www.economist.com/news/international/21605923-national-identity-scheme-goes-global-estonia-takes-plunge>; A. McLean, *E-Estonia: what is all the fuss about?* in ZDNet, 2018. Available at <https://www.zdnet.com/article/e-estonia-what-is-all-the-fuss-about/>; N. Heller, *Estonia, the digital republic*, *The New Yorker*, 11 December 2017. Available at: <https://www.newyorker.com/magazine/2017/12/18/estonia-the-digital-republic>

¹¹ Using these words, the Estonian official website (<https://e-resident.gov.ee>) describes the program.

¹² L. Reynolds - R. Scott, *Digital citizens: countering extremism online*, London, 2016, p.19.

network, consisting of different people who do not need to be near each other but can be based anywhere. What makes this unique is that there is no need for either an intermediate or centralized body or authority controlling and coordinating the data. Every member of the network has direct access to the ledger, and any changes to the ledger must be unanimously agreed by everyone within the network. This has a range of advantages including making the system tamper-proof, decentralized and secure, as the data added to the ledger are unchangeable, secure and preserved for the life of the ledger, with the agreement of all participants as to the contents¹³.

Apply for the e-residency is as easy as registering to any website, but there are controls too. The request is made by filling in a form online, together with the sending of a copy of personal ID and passport, and other useful information such as CVs, links to social networks, and especially details about crimes eventually committed, or bans and restrictions related to the applicant himself or his business. Then the Estonian police will verify the identity of the applicants through their documents, and only if background checks are exceeded the digital ID can be granted.

After passing checks, is necessary to pick up personally the e-residency kit, within six months from the request, by visiting one of the designated pick-up location, such as police and border guard station in Estonia, or an Estonian embassy: they can be found in 38 different countries, not only in Europe, but also in the United States, in Asia and in some Middle Eastern states. In this occasion the applicants must show up in person and prove their identity again, and also provide their biometric data and fingerprints. Once granted the e-residency, start a new company and run a business in Estonia, and therefore in EU, is quick and easy.

An Estonian e-resident, in fact, can start a company totally online and operate his business remotely, with no need to re-establishing, just using a computer from anywhere in the world: this company will be registered online as an Estonian one, in the digital e-Business Register, and consequently will have access to the EU Single Market and the European payment systems.

This implies relevant consequences, especially for entrepreneurs and freelancers from outside the EU, for example from developing countries. e-Residency, in fact, offer them services that are useful for different reasons. First of all, it allows them to manage a company without moving and with no need to hire a local director in Estonia: that may be not only expensive, but also difficult, because it is not uncommon that these countries serve travel restrictions, complex bureaucracy, or an instable political climate that makes impossible to run a company abroad.

¹³ About e-residency and blockchain technology see: M. Rauchs - A. Glidden - B. Gordon - G. Pieters - M. Recanatini - F. Rostand - K. Vagneur - B. Zheng Zhang, *Distributed ledger technology systems: a conceptual framework*, Cambridge, 2018; A. Deshpande - K. Stewart - L. Lepetit - S. Gunashekar, *Understanding the landscape of distributed ledger technologies/block chain*, Cambridge, 2017; T. Kotka - I. Liiv, *Concept of Estonian Government Cloud and Data Embassies in Electronic Government and the Information Systems Perspective: Proceedings of the 4th International Conference EGOVIS 2015*, Valencia, 2015, pp. 149-162; C. Sullivan - E. Burger, *E-residency and block chain in Computer Law and Security Report*, 2017, 33(4); Z. Zheng - S. Xie - H. Dai - X. Chen - H. Wang, *An Overview of Block chain Technology: Architecture, Consensus and Future Trends*, 2017. Available at: https://www.researchgate.net/publication/318131748_An_Overview_of_Blockchain_Technology_Architecture_Consensus_and_Future_Trends

Second, many of these countries don't provide effective digital services, like an online payment system; finally, e-residents can establish their business and operate in the European economic environment as a trusted EU company, so they have the possibility to reach and gain the trust of Western investors and partners, which would be impossible operating from their country of origin¹⁴.

E-residents who run a company in Estonia will declare and pay corporate taxes online, thanks to the e-Tax program, and they will also be able to open a bank account in Estonia: this is not automatic, but it may be necessary to pay share capital and distribute dividends, so it is in practice required. In addition, e-residents can rely on platforms that provide business services or find a fintech partner which may assist the company management in the Estonian service provider marketplace, that can be easily found on the e-residency program website.

As for the granting of the e-residency, there's a high level of transparency: digital companies are subject to the same control as the resident operating ones, and the data about their activities, ownership and financial formation, will be publicly available.

Furthermore, e-residents are continuously supervised through on-going checks between state institutions, and those who fail to comply with Estonia's business rules will have their digital ID certificates revoked¹⁵.

Statistics supplied by the Estonian government official website shows that there are almost 55,000 e-residents registered in Estonia, who come from 150 different countries and have already established about 6,000 companies, but there is not a shortage of supporters, who doesn't have economics interests in Estonia, but are just intrigued by the program.

Actually, has been observed that there are basically three categories of e-residents: «fans» of the program, as said, entrepreneurs and freelancers, and real visitors¹⁶.

To the first category belong all those who have a personal interest in e-residency program, and in 2015 they were 25% of the whole e-residents. They have not any business to conduct in Estonia, nor economic interests, but their political or ideological opinions just make them believe that e-residency is a full and completed manifestation of freedom of using Internet and an innovative communication tool, that allows them to relate within a real community, inside which they can act in absolute safety, and with total respect for their privacy. This may seem less relevant, regarding to other potentiality of e-residency, but it is enough to think to all those countries where governments repress press freedom, Internet freedom and many political and civil rights, to see the usefulness and precious opportunities offered by e-residency to these people.

¹⁴ See: T. Kotka - C. I. Vargas Alvarez del Castillo - K. Korjus, *Estonian e-Residency: Redefining the Nation-State in the Digital Era*, Oxford: Cyber Studies Program working paper No. 3, Oxford, September 2015. Available at: <https://www.politics.ox.ac.uk/materials/publications/14883/workingpaperno3kotkavargaskorjus.pdf>

¹⁵ V. Lubi, *Here's why money launderers are disappointed with e-Residency*, 2019. Available at: <https://medium.com/e-residency-blog/heres-why-money-launderers-are-disappointed-with-e-residency-40de3a5fe18f>

¹⁶ See: T. Kotka - C. I. Vargas Alvarez del Castillo - K. Korjus, *Estonian e-Residency: Redefining the Nation-State in the Digital Era*, Oxford: Cyber Studies Program working paper No. 3, Oxford, September 2015. Available at: <https://www.politics.ox.ac.uk/materials/publications/14883/workingpaperno3kotkavargaskorjus.pdf>

The second category is made up by all those people who want to expand their business in a digital environment, or who want to start a virtual business, regardless of having already economic interests in Estonia, or not. Thanks to e-residency they can operate flexibly, and conduct their business, and plenty of the related required tasks, effectively and totally online, without moving from their office, or even from home. In addition, base a business in Estonia means not only operate in a technological advanced environment, but also benefit from a transparent and profitable corporate tax system.

Finally, e-residents are all of them who spend part of their time in Estonia and find themselves even temporarily included in a fully digitised nation, where life without a digital identity is obsolete and limiting. A good example is given by academics, diplomats, journalists, business partners of Estonian companies, and all those who work or are often related with Estonia. No coincidence, in fact, that the first e-resident was a British journalist, Edward Lucas, correspondent for a British newspaper, *The Economist*, during the 29th session of the Baltic Assembly.

Finally, many personalities are e-residents too: The Pope, or German Chancellor Angela Merkel and others, in fact, received an honorary e-residency.

e-Residents are a very heterogenous group, and in fact has been said that if it is not possible to choose one's homeland, one might well choose not only where to live physically, but now also a country of digital residence¹⁷.

An interesting point regarding e-residents' origin and grounds, is that the rate of British citizens has increased meaningfully after Brexit. There was a 75 percent spike in UK traffic on the Estonian website after former Prime Minister Theresa May triggered the article 50 EU exit clause in 2017, and the number of applications to e-residency from Britain has grown from three to more than 50 per week¹⁸. When the Brexit route will be completed, Britain will leave the European single market and the customs union, and there would no longer be free movement of goods and services: in this scenario if a British entrepreneur becomes an Estonian e-resident and establishes a company producing goods in Estonia, they will have free access to the EU market, just like European companies¹⁹.

A case in point is the experience of the British start-up «Twipes», told by its founders on the Estonian website blog, which collect the testimonies of various e-residents around the world. The company is based in London, where both its founders live, but since the advent of Brexit they signed up for e-residency to mitigate the risk for their business, and registered the company in Britain and in Estonia, to boost investor confidence and reduce their concerns²⁰.

¹⁷ See: T. Kotka - C. I. Vargas Alvarez del Castillo - K. Korjus, *Estonian e-Residency: Redefining the Nation-State in the Digital Era*, Oxford: Cyber Studies Program working paper No. 3, Oxford, September 2015. Available at: <https://www.politics.ox.ac.uk/materials/publications/14883/workingpaperno3kotkavargaskorjus.pdf>

¹⁸ See: J. Anderson, *One way to get around Brexit: become an e-resident of Estonia*, in Quartz, 19 July 2016. Available at: <https://qz.com/736004/one-way-to-get-around-brex-it-become-an-e-resident-of-estonia/>

¹⁹ See: B. Hammersley, *Concerned about Brexit? Why not become an e-resident of Estonia*, in Wired UK, 27 May 2017. Available at: <http://www.wired.co.uk/magazine/archive/2015/07/features/estonia-e-resident>

²⁰ The story of «Twipes», and many others has been told by its founders on the official blog of the Estonian Government. It is available at: <https://e-resident.gov.ee/meet-the-e-residents/#were-the-mayor-of-londons-entrepreneurs-of-the-year>

The need to remain European citizens, in fact, is strongly felt in Britain, and this is testified also by the high number of requests of Irish citizenship and passports. According to the data released by the Irish Government almost one million of new passports has been requested in 2019, and most of them by British citizens from Northern Ireland, that have dual citizenship, or by other British people eligible to apply for Irish citizenship.

e-Residency, therefore, can be able to meet a real need, and is a great alternative for those who cannot apply for Irish citizenship, furthermore, it offers many benefits that Ireland cannot match, like a tax system equally convenient²¹, but even more transparent²².

3.3 Dangers lurking: money laundering and transparency

In response to controls and the high level of transparency, Estonia is ranked as one of the countries with the lowest risk of money laundering: according to the latest Basel AML Index (an independent ranking and risk rating tool, released every year by the Swiss Basel Institute on Governance, that assesses money laundering and terrorist financing (ML/TF) country risk around the world), issued in August 2019, Estonia is the last in a ranking of 125 countries around the world from highest to lowest level of risk, and his situation improved by 0.05% compared to 2018.

In this Index Estonia is indicated as one of «*the best performing countries*», together with Finland and New Zealand, however the report to the Index highlights that, despite the high ratings, «*this score may worsen when Estonia is re-assessed according to the FATF fourth-round methodology focusing on the effectiveness of AML/CFT measures and not only technical compliance*». Furthermore, it recalls that Estonia has been subject to recent criticism of its effectiveness in preventing money laundering, and concluded with the caveat that «*the data does not reflect the risk of Estonia's geographic proximity to Russia and the issues that may be associated with this*», in fact, the Baltic country, «*has been labelled as one of the first ports of entry for Russian money launderers wishing to gain access to the European financial market*». According to the Basel Index analysis' report, the main issues are related to «*legal entity, such as public company ownership and tax disclosure, as well as recorded company ownership*»²³.

This final annotation draws inspiration from an infamous precedent, that arose between 2017 and 2018, when Estonia took centre stage in one of the largest-ever money laundering scandals. It was found that, already since 2007, the Estonian branch of Danske Bank helped funnel money from Russia and other ex-Soviet states, for an amount of over 200 billion euros.²⁴

²¹ E. Liivamägi, *How do e-residents pay taxes?*, 2017. Available at: <https://medium.com/e-residency-blog/how-do-e-residents-pay-taxes-73b8c96902b6>,

²² See: Edward Lucas on Brexit: *Estonian e-residency has never been more useful*. Available at <https://e-estonia.com/edward-lucas-on-brexit-estonian-e-residency-has-never-been-more-useful/>

²³ <https://www.baselgovernance.org/sites/default/files/201908/Basel%20AML%20Index%202019.pdf>

²⁴ F. Coppola, *The Tiny Bank at The Heart of Europe's Largest Money Laundering Scandal*, Forbes, 26 September 2018. Available at: <https://www.forbes.com/sites/francescoppola/2018/09/26/the-tiny-bank-at-the-heart-of-europes-largest-money-laundering-scandal/#2f21b3b32805>; S. Kroft, *How the Danske Bank money-laundering scheme involving \$230 billion unrevealed* in CBS News, 19 May 2019. Available at: <https://www.cbsnews.com/news/how-the-danske-bank-money-laundering-scheme-involving-230-billion->

The first doubts about the activities of Danske Bank in Estonia were raised in different reports, issued by the Estonians and Danish Financial Supervision Authorities: they claimed that the bank was knowingly dealing with shady funds of uncertain origin, in order to funnel money from Russia and other ex-Soviet states. According to the allegation of a whistleblower, later identified as Howard Wilkinson, former head of trading for Danske Bank in Estonia, Latvia & Lithuania, most of the funds managed by Danske Bank in Estonia came from the family of the Russian President Vladimir Putin and the Russian security service (FSB).

Furthermore, it seems that Danske Bank used its own IT-system, and documents written in Estonian or Russian, without implementing any change that would have made controls easier for the Danish headquarter. The greatest part of the funds managed by Danske Bank, in fact, came from abroad, and transactions were made mostly using shell companies. The highest amount of non-resident accounts was from Russia, and, according to the Danish Financial Supervisory Authority, in 2012 they made up 35% of total profits of the bank. Other significant non-resident portfolios came from Britain, Cyprus and New Zealand, as well as other banks in Latvia and Moldova, and from ex-soviet states, like Azerbaijan.

Later, as assessed by the Estonian Financial Supervisory Authority, came out that in the Estonian branch of Danske Bank were committed «*large-scale, long-lasting systemic violations of anti-money laundering rules*»²⁵.

Denmark, Estonia, and other countries started investigating on the 200 billion euros of suspicious payments made by Danske Bank in Estonia: in December 2018, ten former employees in this branch were arrested by Estonian authorities, and in 2019 the bank was required by the Estonian government to close its Estonian branch. In Denmark the CEO of Danske Bank resigned in 2018 and was charged in 2019 with neglecting his responsibility, together with the bank's former finance director, charged with failing to prevent the suspicious transactions, and Danish Parliament increased penalties for money laundering, making them some of the toughest in Europe.

This affair opened the Pandora's box of the risks of money laundering in Estonia: banks with operations in the Baltic country started to perform more strict checks on clients that were found to be non-resident, and the Estonian Financial Supervision Authority submitted all the banks operating in Estonia to extraordinary anti money laundering inspections. Not infrequently non-residents' accounts appeared suspect and were closed as a result of the checks, in order to avoid risks of money laundering. After the increase of checks, the Estonian Financial Supervision

[unraveled-60-minutes-2019-05-19/](https://www.intellinews.com/money-laundering-crisis-reshapes-estonia-s-relations-with-non-resident-businesses-160452/); S. Kuznetsov, *Money-laundering crisis reshapes Estonia's relations with non-resident businesses* in *Intellinews*, 30 April 2019. Available at: <https://intellinews.com/money-laundering-crisis-reshapes-estonia-s-relations-with-non-resident-businesses-160452/>; ERR News, *Finance ministry and LHV differ on e-residency money laundering risk*, 5 June 2019. Available at: <https://news.err.ee/949260/finance-ministry-and-lhv-differ-on-e-residency-money-laundering-risk>; J. O'Donnell – T. Virki, *Dirty money risks encroach on Estonia's digital utopia* in *Reuters*, 1 February 2019. Available at: <https://www.reuters.com/article/us-estonia-danske-digital-insight/dirty-money-risks-encroach-on-estonias-digital-utopia-idUSKCN1PQ3UU>.

²⁵ See: *Statement by Finantsinspektsioon, an Estonian financial supervision and resolution authority, on information published in the media about the Estonian branch of Danske Bank*, 27 February 2018, Available at: <https://www.fi.ee/en/news/statement-finantsinspektsioon-estonian-financial-supervision-and-resolution-authority-information>

Authority stated that the risks for Estonian banks from serving non-residents has been substantially reduced, as the majority of the banking sector is not at high risk of money laundering and is now focused mainly on serving local or related business and private clients.

Anyway, according to other banks who still operates in Estonia, and as said in a roundtable on cyber security hosted by the Estonia Banking Association, it would be advisable to rather accept fewer foreign nationals, and in ideal case rather the ones who can demonstrate a clear connection with Estonia, in fact one measure of risk is the share of non-resident deposits, especially those from high-risk non-residents who generally have no link to the Estonian economic environment, or who operate in high-risk jurisdictions²⁶.

Actually, statistics confirm this change of course: according to the report issued in September 2019 by the Estonian Banking Association (EBA) the share of non-resident deposits in Estonian banks has been decreasing significantly in recent years and are continuing to do so: at the beginning of 2013 it constituted almost a 20% rate, but by the end of 2018 the share had decreased to 9%. Also, the share of deposits originated by non-resident customers registered in offshore territories has decreased ten times, currently making up less than 1% of the whole deposit portfolio²⁷.

3.4 e-Residency 2.0

Danske Bank scandal made need for action in order to maintain the good reputation not just of Estonia as a digital state, provided with an effective money laundering repression and prevention system, but particularly of the e-residency program as a safe and lawful opportunity for the development of economy on a global scale.

In a roundtable on cybersecurity organized by the Estonian Banking Association of Commercial Banks on June 4th 2019, different representatives from various banks operating in Estonia discussed about future perspectives and needs, in order to reduce the gap formed between the image of e-Estonia, damaged by Danske Bank scandal, and the actual involvement, awareness and efficiency of the Estonians public and private sectors in preventing the risk of money laundering thanks to advanced information technology solutions.

Following this trail, the Estonian government is currently in the process of improving both the convenience and security of e-Residency even further through an initiative called e-Residency 2.0, which involves a wide selection of stakeholders from both the public and private sector. e-Residency 2.0 is not meant to be a revolution, and most features are unchanged: e-residency remain the instrument to engage with foreign people and create a digital community that goes beyond the Estonian borders, and obviously between there will still be investors, attracted by the possibility to manage their business totally paperless, from anywhere in the world, just using their computer.

²⁶ The Baltic Course reports part of the speech of Tiit Hallas, cyber security chief at LHV bank. See: The Baltic Course, *LHV: Estonian e-residency, prevention of money laundering working against each other*, 5 June 2019. Available at: <http://www.baltic-course.com/eng/finances/?doc=149623>

²⁷ See: <https://www.ebf.eu/estonia/>

The guiding values of the e-residency program rest the same: «*empowerment, inclusion, legitimacy, and transparency*»²⁸. In particular, the latter is the most significant in the renewal perspective pursued by Estonia, in fact, the aim of e-residency 2.0 is to offer the possibility to operate in a transparent and safe business environment, allowing e-residents to gain the trust they need to operate their business location-independently.

The enhancement of e-residency aims to bring positive results, useful for all concerned: for foreign investors, but also for the global market, strengthened by the connection between different companies and economic environment and from the easy investments circulation, and also for Estonia, whose economy will be enriched thanks to the growth of more and more digital companies.

Trigger this virtuous circle and cast out the shadow of Danske Bank scandal is the aim of e-residency 2.0. The results of this initiative are summed up in the «e-Residency 2.0 White paper», which contains 49 recommendations to make e-Residency more beneficial to everyone who is part of the Estonian digital nation ²⁹.

According to this paper the most important tools for hedging risks of money laundering are transparency and cooperation with the e-residents' countries of origin, in order to exchange data, collect information about past activities of the applicants and improving checks, both engaging cooperation with anti-laundering organizations and more precisely defining the roles and responsibilities of Estonian Police and other competent authorities³⁰.

4 Conclusions

The examples of Estonia and Malta shows how different can be the results of the pursuit of the same aim, economic development, and how freedom of establishment can be differently interpreted and concretized. The contact point between these situations is not only the purpose, but also the risk of money laundering and tax evasion, which manifest itself in both of them.

These two countries address the issue on the basis of different values and guiding principles, and from that descends the diversity of the results. While Malta served the price of a disproportionate economic growth with investigations and convictions conducted worldwide for corruption, money laundering and tax evasion, Estonia stayed true to the value of transparency, and for this reason is activated to neutralize risks and improve its services and security systems, so as not to appear an offshore country, but a digital, transparent and trusted economy.

Even with new technologies, in fact, there are no new dangers: risks are the same, but they are amplified, and harder to fight. For this reason, it's imperative that also remedies evolve, adapting themselves to the new context. Concurrently, in addition to treatment, prevention is

²⁸ K. Korjus, *E-Residency 2.0: What do Estonians think of the program?*, 2018. Available at: <https://medium.com/e-residency-blog/e-residency-2-0-what-do-estonians-think-of-the-programme-99853274a55b>

²⁹ e-Residency 2.0 white paper are available online at: <https://s3.eu-central1.amazonaws.com/ereswhitepaper/e-Residency+2.0+white+paper+English.pdf>

³⁰ N. Angelovska, *Estonia's E-Residency Contributed €14M To Its Economy 'E-Residency 2.0 Will Be A True Forerunner*, Forbes, 25 April 2019. Available at: <https://www.forbes.com/sites/ninaangelovska/2019/04/25/estonias-e-residency-contributed-e14m-to-its-economy-e-residency-2-0-will-be-a-true-forerunner/#31955cca9da5>

needed: the development of new technologies should consider the existing risks and prepare improvements and new instruments to successfully combat them.

Abstract: This paper aims to examine one of the main implications of freedom of establishment: since it is possible to transfer a company abroad effortlessly, in fact, governments are adopting various strategies to make themselves more attractive. These are based on two main directives: first, a convenient tax system, as in Malta, on the other side technology, as proposed in Estonia. These countries' strategy is radically different: Malta offers an extremely profitable tax system, while Estonia, on the other side, is the only nation in Europe where the optimal use of technology and its potential allows the consolidation and implementation of a totally digital system, whose advantages outweigh those of taxation. Estonian system is compared to the Maltese one and critically discussed, also through the analysis of different sources, including blogs and online newspapers, that have greater relevance in the Estonian digitalized context. This work makes it possible to identify strengths and weaknesses of these systems, especially regarding the risk of money laundering, which is faced differently in the two countries. This paper shows how Maltese and Estonian systems, pursue the same purpose and collide with the same money laundering issues, but they deal with them in opposite ways. The Estonian system appear more dynamic and reactive in order to remove risks of money laundering, and this made of this country a proper model for other nations.

Keywords: Freedom of establishment; Money laundering; Estonia; e-residency; Digital Revolution