Standard Life Investments

Beneficial Ownership Team
Department for Business, Energy & Industry Strategy
1st Floor Victoria
1 Victoria Street
London SW1H 0ET

Email:transparencyandtrust@beis.gov.uk

Standard Life Investments
1 George Street
Edinburgh
EH2 2LL

www.standardlifeinvestments.com

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Dear Sir/Madam

Overseas Entity Register Call for Evidence Response

We refer to the above consultation and submit herewith our response to your call for evidence.

About Standard Life Investments

Standard Life Investments is one of Europe's leading investment houses with assets under management of approximately £277.9 billion, as at 31 December 2016. As at 31 March 2017, our real estate assets under management are currently valued at £22.3 billion.

We are a dynamic, growing real estate business with one clear aim – to deliver premium investment solutions to our clients. Our ambition is backed by the heritage and financial strength of our parent company that was founded in 1825.

We have been active participants in the global real estate market for over 50 years and have garnered both significant experience and scale. We have an aptitude for innovative solutions to meet the changing requirements of our clients and have developed a number of specialist real estate products. Several of our flagship funds have performance track records of over 25 years. This makes them some of the longest established and largest real estate vehicles in the market.

Our passion for real estate investment runs deeply at Standard Life Investments. Drawing on our years of experience and the broader expertise within the business, we have the scale and specialist capabilities required to manage a wide range of real estate investments around the globe.

We always strive to deliver the investment performance and service our clients expect. By understanding their needs and interpreting the ever-changing dynamics in the market, we seek to constantly improve the results we deliver and develop innovative real estate investment solutions.

At the heart of our real estate business lies our team of experienced professionals and the relationships they have developed around the world with our clients, consultants and service providers. Founded on research and paired with the real estate skills with which we execute fund and asset strategies, we adhere to robust processes to ensure results are consistent and compelling.

We are well equipped to realise opportunities and offer investment solutions across the real estate spectrum to the benefit of our investors, whether through direct property assets or listed real estate funds.

We aim to add value from each stage of our disciplined investment process. The dynamic nature and our flexible approach are key features of this process. Each of the key elements are monitored and reviewed regularly to ensure effectiveness in operation, and to assess impact on portfolio returns.

Response

Executive Summary

1. Instead of serving to promote the UK as a transparent place to do business (a principle with which we completely agree, and whilst it will certainly serve this end) the policy, at the present time and in the current environment, is more likely to be viewed as adding an additional layer of bureaucracy to the real estate market and result in a consequent disincentive to do business in the UK at a time when we need it most.

2. We are not convinced that the policy, as proposed, adds in materially to existing KYC/MLR legislation.

3. Our following responses are provided with the above in mind.

Preliminary note on terminology: We believe that the use of the term "real estate" is preferable to "property" as the latter denotes a broader class of assets that includes real estate.

Question 1: Do you agree that all legal forms that can hold properties should be in the scope of the new register's requirements? If not, what legal forms should we consider an exemption for and why?

Response: We agree that all legal forms that can hold real estate should fall within the scope of the new register's requirements.

A distinction should however be drawn between (see response to Q24):

- Regulated vs unregulated entities
- Listed vs unlisted entities

Question 2: Is the suggested definition of leasehold appropriate?

Response: No. We assume that the register is seeking to capture dealings in real estate which are similar to a sale or acquisition of a freehold or heritable interest with an equivalent consideration paid on sale (i.e. long leasehold interests). We do not believe that a term of 21

years is appropriate (for either commercial or residential leases) as this is too low a threshold, would unnecessarily increase the compliance burden and could give rise to unintended consequences of capturing longer term occupational commercial leases which may have a duration in excess of 21 years. A minimum term of 50 years would be more appropriate and should be linked to the unexpired term of the lease rather than the original term. A minimum purchase price threshold should also be considered.

Question 3: Will setting the leasehold definition at leases over 21 years create any unintended consequences?

Response: See response to Q2.

Question 4: Do you agree that the definition of beneficial owner for the new overseas register should be aligned to the definition of PSC in the PSC regime?

Response: In principle, yes. Careful consideration must however be given to the impact of the register requirements on overseas purchasers, real estate transactions and the UK real estate market as a whole.

Question 5: Do you agree that entities that are not similar to UK companies limited by shares should use these adaptations to identify their beneficial owners?

Response: For certainty, it may be preferable to supply a list of the vehicles intended to be caught plus the catch-all adaptions.

Question 6: Do these adaptations provide sufficient flexibility in the beneficial owner conditions to apply to most legal entities? If not, what additional adaptations should there be?

Response: See response to Q5.

Question 7: What methods of raising awareness would be most effective?

Response: Publication/notification as HM Land Registry (or equivalent) and Companies House requirements in addition to raising awareness through industry bodies such as RICS and The Law Societies/SRA. The prospect of a transaction being rendered void *ab initio* is likely to result in the inclusion of transactional warranties (regarding register status) into template agreements of sale/transfer. The commercial consequences of breaching said warranties is likely to focus the minds of contacting parties on the issue before due diligence costs are incurred.

Question 8: Do you have any information that is relevant to our assessment of the cost and benefits of the policy to businesses, society and the economy?

Response: Aside from the additional one-off costs of registering existing overseas entities, the increase in governance obligations will result in an increased cost to businesses, (and particularly to investment managers who manage or own large numbers of such entities) and those who are transacting with them together with real estate lenders. Whilst these costs might be regarded as reasonable in the context of the overall benefit/s, it is imperative that the policy touch-points (i.e. the point at which non-compliance bites) do not increase the risk of commercial loss to either buyer or seller (e.g. wasted due diligence costs).

Furthermore from a practical perspective, an essential element of real estate transactions is the ability to act quickly. Deals are often concluded prior to the real estate-owning entity being established (which often happens at the last minute once due diligence has been completed). It is unclear how long it will take to satisfy the requirements of the register and procure a registration number. This will create uncertainty as to deal execution and will potentially place overseas purchasers at a disadvantage. It will also create the impression that the UK is a complicated and bureaucratic place to do business- with the risk that investors might opt for more competitive jurisdictions.

Question 9: What, if any, impact do you think that the proposed policy will have on the UK property market (residential and commercial)? Please describe the impacts and provide evidence.

Response: Whilst the policy is likely to promote confidence in the UK market as a transparent environment to do business, we expect both short and long-term impact. Large companies, sovereign wealth and private investment entities that for strategic investment and competitive purposes customarily keep their ownership structures confidential are likely to view the UK less favourably as an investment destination.

We expect joint venture and collective investment schemes (where ownership/control exceeds 25%) to be impacted due to the implicit "veto" right created by the policy in favour of majority owners. This will require further consideration in light of the proposed "opt out" mechanism (i.e. if information is withheld or unavailable) and how this is intended to work.

In the short term the policy may give rise to delays in transaction timeframes or even deals aborting. As mentioned above, it is imperative that the policy does not increase the risk of commercial loss to either buyer or seller (e.g. time/delay penalties or wasted due diligence costs) and that its implementation and associated transitional arrangements do not act as a disincentive to bona fide purchasers looking to invest in UK real estate. The point at which non-compliance bites must be sufficiently clear to allow any issues to be addressed by the parties as early as possible in the life of a transaction.

We question the timing of the proposal in that it comes at a time when the UK should be welcoming investment (and simplifying processes and making it easier to do business). As mentioned in the response to Q8, the risk is that the policy might in fact have the opposite effect (perceived or otherwise) to that intended.

Question 10: Do you agree that the duration of the period given to overseas entities to comply with the new requirements should be one year?

Response: One year is too short a period to exit an investment in certain real estate sectors, particularly during periods of economic distress (e.g. in a Brexit environment- as was the experience in the Global Financial Crisis) and may trigger a fire-sale scenario that may impact price, thereby prejudicing bona fide sellers (particularly those who were unaware of the requirements). A period of two years is more reasonable and would also seem more appropriate a period for Companies House to deal with the associated registrations.

Question 11: Is a system of statutory restrictions and putting notes on the register, backed up by criminal offences, a comprehensive way to ensure compliance?

Response: In principle, yes. Care however needs to be taken as to who attracts the penalty. In this regard, please note the comments in our response to Q20.

In addition, it will be necessary to ensure that the sanctions do not give rise to stagnation in the property market with properties unable to be sold due an owner's continued failure to register the details of its beneficial owners. It should be clarified what the ultimate sanction/s will be for non-compliance (e.g. satisfaction of criminal fines through forced sale of the asset with proceeds after satisfaction of debt being held in trust for the owner until such time as it satisfies the requirements to allow payment to a source).

Question 12: Do you agree that we should prevent any beneficial interest in the property passing to an overseas legal entity that does not have a valid registration number at completion or settlement?

Response: It appears that the restriction on acquisitions during the one year grace period applies from the date of commencement of the legislation. There is a need to have a transitional period from commencement to cover transactions that are already in progress to limit the potential costs and delay that would occur from waiting to obtain a registration number. Disposals and acquisitions should be treated in the same way. We suggest a phasing in period for acquisitions (where deals can be completed under the proviso that the requirements of the register must be complied with by the end of the two year grace period).

During the transitional phase title to a real estate asset should be capable of being registered at the Land Registry without the required registration number. If the buyer ceased to obtain a registration number by the end of the transitional phase then it would be unable to undertake any further dealings with the asset and sanctions would apply. Our comments regarding prevention of transfer of beneficial interest of transactions following completion of the transitional phase are set out below. It should also be noted that the concept of "beneficial interest" does not exist under Scots law.

Question 13: Do you agree that the most appropriate way to do this would be to void the transfer document?

Response: The document should be void *ab initio* (as opposed to at a point later on in the transaction) and certainly would have to be before the buyer has paid the purchase price. The reason for this is that parties (particularly purchasers) incur significant due diligence costs from day one. Clarity as to the invalidity of the transaction as early as possible in the process is likely to mitigate this risk.

Question 14: Is there another way that we could achieve this result?

Response: In our view, it is in the interests on all parties to establish their contractual *locus standi* as early as possible in a transaction. The risk to a transaction being rendered void *ab initio* provides such an incentive.

Question 15: Which is your preferred option for procurement and why?

Response: No response provided.

Question 16: Do you agree that the information on the new register for overseas entities should be the same as the information required under the PSC regime?

Response: Yes, this would be necessary to treat all entities (UK and Non-UK) fairly for the exemption to operate.

Question 17: Do you agree that entities unable to give information about beneficial owners should be asked to provide information about their managing officers?

Response: In principle, yes- however, to the extent that this information is identifiable from the entity's home public register, would a link not suffice to avoid duplication?

Question 18: Is there any additional information that we should ask for from entities that are unable to give information about their beneficial owners?

Response: No, we do not believe that further information is necessary- as a balance should be drawn between reasonable and onerous disclosure requirements and the impact of the latter on inbound investment.

As mentioned above (under Q8), real estate transactions are often subject to severe time constraints. Introducing additional requirement/s (and certainly an element of subjectivity- i.e. where Companies House is required to decide on the suitability/acceptability of information provided before issuing a registration number) is likely to impact negatively on transaction timeframes (and the perception of the UK as a place to do business).

Question 19: Is a requirement for an update every two years appropriate?

Response: Three years is perhaps more reasonable. Overseas companies are already obliged (subject to sanction) to update the register in the event that information changes. We believe that this is sufficient incentive to do so. Changes in ownership of companies which would trigger conditions requiring updates are generally irregular occurrences. The administrative burden of updating the register comes at a cost. In our view, the obligation to update the register every two years is excessive when compared with the risk that a party might purchase and dispose of an interest in an entity within this period.

In the event that three years is regarded as too long, we suggest an exemption (of three years) for entities directly or indirectly (i.e. as part of a fund structure) managed by a UK regulated investment manager.

Question 20: Would a criminal offence be an appropriate way of enforcing the requirement to update information?

Response: We are not convinced that criminal sanction will have the desired effect, particularly where the vehicle is intended to be the subject of the sanction. In many cases, these entities might be managed by employees of investment houses or professional directors- who might have no contact with or control over the ultimate beneficial owners.

Question 21: Do our proposals achieve the right balance between ensuring compliance and enabling overseas entities to maintain existing assets?

Response: Care needs to be taken not to duplicate legislative obligations that already exist under KYC, MLR and associated legislation.

Aside from the proposed publication of the register, we are not convinced that the policy adds materially to the verification process for ultimate beneficial ownership already in place under existing legislation. Therefore, and further to our responses in Q.8 and Q9, (and for the purposes

of promoting the UK as an investment destination of choice) it might, at least for the short term, be preferable to rely on (or, if necessary, extend the ambit of) existing KYC/ML legislation.

Question 22: Are these mechanisms enough to deal with situations where bidders provide false beneficial ownership information or do not keep their information up to date?

Response: No response provided.

Question 23: Do you think that this provides the correct balance between protecting individuals from harm and ensuring transparency of how properties are owned?

Response: In our view it is not necessary that the register be made available to the public at large and this should be considered in the context of the Freedom of Information Act. This, in our view creates data protection issues (particularly from an EU GDPR perspective). The purpose of the register is to reduce the risk of money laundering and corrupt activities and making this information available increases the already increasing burden for businesses in mitigating against fraudulent acts through unlawful use of information. This purpose could be achieved (whilst balancing the risk to be averted and the interests of the parties concerned) by limiting access to:

1. Government authorities (e.g. financial intelligence departments);
2. Regulated financial institutions;
3. Third parties who can show a legitimate interest in the information.

A fee should also be payable by the party seeking to view the information.

Question 24: Are there additional situations we should consider where protections should be granted?

Response: As mentioned above, certain commercial transactions or relationships may be market-sensitive and are governed by existing confidentiality provisions. To the extent that it is not possible to amend these existing confidentiality provisions, disclosure of information required for the purposes of the register might expose an entity to a claim for damages. This situation should be carved out (and additional provision should be made for future transactions that might require such confidentiality provisions due to their market-sensitive nature).

The following entities should also be exempt from putting information on the register:

1. Overseas entities managed by a regulated UK investment manager;
2. Overseas entities listed on the London Stock Exchange;
3. Entities registered in Jersey, Guernsey and the Isle of Man to the extent that said entities are managed by a Jersey, Guernsey or Isle of Man investment manager regulated by either the Jersey, Guernsey or Isle of Man regulator.

In the above regard, consideration might be given to providing regulated investment managers (who generally manage multiple real estate asset holding vehicles) with adviser registration numbers. Under this mechanism, investment managers would be entitled to verify/certify UBO details via a form of umbrella authorisation.

Question 25: Are there other situations where exemption from putting information on the register should be permitted for entities participating in procurement?

Response: No response provided.

Question 26: How can we best ensure that only legitimate lenders are able to repossess and dispose of a property with a restriction against it?

Response: Care needs to be taken that this does not have the unintended consequence of limiting the availability of real estate financing from legitimate sources. The Global Financial Crisis (GFC) saw a rise in non-bank lenders who have increased their market share in commercial real estate lending (which has served to mitigate the risks experienced in the crisis relating to lack of liquidity in the market to (re)finance real estate transactions). Accordingly a sufficiently broad definition of "legitimate lender" would need to be agreed that encompasses all stakeholders (based on a commerciality or business purpose test, as opposed to a closed list of lender type). This definition should also include *bona fide* third parties seeking to have recourse to real estate in satisfaction of an obligation (e.g. overage, profit participations, securitisations).

It also important to ensure that lenders remain protected should an owner subsequently fail to comply with its registration requirements and additionally that insolvency practitioners be permitted to satisfy debts due by the sale of real estate where an owner is not in compliance (whether or not a fixed charge is secured against the asset).

Question 27: We are interested in views and evidence of other commercial transactions that could be disrupted by the proposed restrictions regime.

Response: No response provided.

Question 28: Are there additional third party impacts that should also be addressed?

Response: Other third parties requiring protection could include:

1. Any bona fide third party litigant (where an order of execution has been procured against a party who has failed to comply with the requirements of the register);
2. A properly appointed insolvency practitioner (e.g. liquidator or administrator) seeking to dispose of assets for the benefit of creditors.

Yours faithfully

[redacted]

Standard Life Investments Limited