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SHEPHERD+ WEDDERBURN

BY EMAIL
Beneficial Ownership Team
Department for Business, Energy & Industrial Strategy
1st Floor
1 Victoria Street
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Dear Sirs

Response to Call for Evidence
Register of Beneficial Owners of Overseas Companies and Other Legal Entities

We write in response to your call for evidence (the "**Call for Evidence**") on a register showing who owns and controls overseas legal entities that own UK property or participate in UK government procurement.

About our firm

Shepherd and Wedderburn is a leading UK law firm. From offices in Edinburgh, Glasgow, Aberdeen and the City of London, the firm delivers comprehensive multi-jurisdictional legal advice across every business sector as well as offering the full range of private client and wealth management services.

Our response to the Call for Evidence

Our comments below address matters of the law of England and Wales and the law of Scotland, which have a bearing on the proposals currently under consideration in the Call for Evidence and are limited to the questions relevant to our role as legal advisors. We have not considered any matters of the law of Northern Ireland or the law of any other jurisdiction. Whilst we act as legal advisors to owners of UK property and participants in UK government procurement, our comments below are not made on behalf of any clients of our firm. Please treat our comments below as confidential.

We respond to the relevant questions in the Call for Evidence as follows:-

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

> We think the suggested definition of leasehold is appropriate for England and Wales. We query whether this would be the best approach in Scotland however. In our view, the threshold in Scotland should be more closely aligned to whether the lease is registerable (rather than setting the length for Scotland based upon the requirements for registration in Northern Ireland). If the purpose of this definition is to include those entities which have long leases then we think it does not make sense to set a definition which would exclude certain long leases in Scotland. Under Scots law, any long lease

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over 20 years is registerable and setting the definition at leases of over 21 years would create an anomaly for leases having a duration of between 20 and 21 years and would mean there would be long leases which are registerable but to which the definition does not apply. This is potentially confusing and would produce a less coherent land registration system in Scotland. We therefore consider there to be strong policy grounds for favouring a blanket rule in Scotland applying to all registerable leases.

Additionally, we query the premise that long leases of over 21 years are akin to 'freehold'. In Scotland, ultra long leases (i.e. for a term of more than 175 years with still 175 years left to run (for non residential leases) and a nominal rent and which meet certain other conditions) were treated as akin to ownership and the Long Leases (Scotland) Act 2012 converted those qualifying long leases to ownership on 28 November 2015.

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?

Aligning the definition of beneficial owner to the PSC regime may help to produce coherence between the PSC regime and the proposed regime for overseas entities. However, it is important to avoid replicating the difficulties which have arisen under the PSC regime in relation to its application to banks and other lenders who have taken security over the shares in a Scottish company. Due to deficiencies in the drafting of paragraph 23 of Schedule 1A to the Companies Act 2006 (which refers to "rights attached to shares", but does not expressly refer to "shares") a bank or other lender which has taken fixed security over the shares of a Scottish company could become registrable under the PSC regime. It is clear that this was not the intention of those drafting the PSC legislation, but it appears to be the consequence of the wording of that legislation. If a decision is taken to apply the definition under the PSC regime to the proposed regime for overseas entities, we recommend that care is taken to avoid a similar consequence, as a bank or lender should not, in our view, be considered to own or control an overseas entity merely because it has taken security over shares or membership interests in such an entity.

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.

Issues of personal privacy should be taken into consideration. The requirement for privacy, or for reasons of commercial sensitivity and in some cases for cultural reasons, for some overseas investors, the requirement to disclose certain details could constitute a barrier to their decision to invest in the UK. While appreciating the need for transparency, some overseas entities may be concerned that the information is publicly available, and that it may therefore be used for reasons other than business and market transparency or for legitimate anti-corruption and money laundering concerns. This concern might be assuaged somewhat by requiring that a person seeking information must submit a request for that information, giving reasons why the information is required.

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?

No- whilst a one-year transitional period might afford sufficient time for an overseas entity which already owns UK property to take steps to identify and obtain information on its beneficial owners, that period is unlikely to be adequate to allow arrangements under existing and ongoing transactions involving UK property to be reviewed and, if necessary, amended. For example, where UK property owned by an overseas entity has been included as collateral in a structured finance transaction – such as a commercial mortgage-backed securitisation – the legal agreements relating to that transaction may require to be reviewed and amended to ensure that the additional regulatory requirements do not interrupt the agreed arrangements or the structure of the transaction. Such

amendments may require the convening of meetings or the obtaining of consents from investors or other transaction parties and a one-year transitional period is likely to be too short for this purpose.

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?

We query whether a criminal offence for a failure to register is proportionate and we have concerns about introducing more regulatory offences which are of limited efficacy and doubts as to how this would be policed for overseas entities in any event.

The concept of title restrictions is not one which is familiar to the Scottish system of land registration and consideration needs to be given as to how such a concept would be implemented in Scotland. We are also concerned about how it is intended the restriction or note on the title (referenced in paragraph 44 of the Call for Evidence) that an overseas entity has not complied with the registration requirements would be policed. In Scotland, we assume this would have to be dealt with by Registers of Scotland as custodians of the relevant property registers. Our concern here is that Registers of Scotland do not have sufficient resources to do this, which would presumably involve a trawl through the whole of the registers to locate properties held by overseas entities, but who had not registered under the proposed new regime. This would be an enormous and time-consuming task. The resources of the Registers of Scotland are already overstretched and consequently this is not a realistic option.

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?

This question appears to overlook the absence of equitable title in Scotland. In Scottish transactions, to obtain a proprietary right (e.g. ownership) you must register a conveyance (usually a deed called a Disposition) with Registers of Scotland. Prior to that registration, a buyer would have a personal right based on the law of contract, but would not have any legal or beneficial title.

Although the seller would lose their economic interest in the property once completion (i.e. "settlement") has occurred (and payment of the price has been made and the conveyance delivered), ownership does not actually transfer until the purchaser registers their conveyance in the Land Register. Until registration takes place, a purchaser may also be at the risk of the intervening insolvency of the seller.

The closest concept to beneficial interest in Scotland is found in trust law as a beneficiary under a trust has a beneficial interest in the trust fund (but not ownership). It is possible to insert a trust clause in a conveyance stating that the seller holds the property on trust for the purchaser until such time as the purchaser registers their title. However, there is debate regarding the effectiveness of such clauses.

Therefore, ownership in Scotland would not actually pass until registration of the conveyance and, under the proposed new regime, registration of a conveyance in favour of an overseas entity could not occur until the overseas entity had a valid registration number. We do not think that, in Scotland, any further legislation is required in relation to beneficial interest as this aim would already be achieved under Scots law by preventing the overseas entity from acquiring ownership.

Consideration should also be given to the practicalities at completion of a transaction and whether searches in the proposed new register could safely be carried out a number of days ahead of completion (as is the case with land registry searches, where parties may rely upon priority or protected periods under priority searches or advance notices). Requiring parties to a transaction to carry out searches in the proposed new register on the day of completion could give rise to practical problems and make the completion of commercial transactions in the UK more cumbersome.

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

No, insofar as the proposals relate to Scotland – as above, ownership would not pass until registration so preventing registration would be sufficient; there is no need to void any documentation. In any event, we think this interferes too heavily with the contractual rights of the parties.

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

As above, we think preventing registration would be sufficient in Scotland and nothing additional would be required to adequately cover beneficial interest. It may be prudent for wording to be inserted in Scots law contracts for the purchase and sale of property but this would be something for contracting parties and their legal advisers to deal with themselves.

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

It is unclear what policy aim this would achieve and we are doubtful as to the justifications cited in the Call for Evidence for taking a different approach on this point from the approach under the PSC regime. Additionally, we consider that the definition of managing officer in the proposed legislation would necessarily be broad and open in view of the many different legal forms which overseas entities may take and such a definition would give rise to uncertainty as to who falls within the definition. To the extent that the proposed regime includes criminal sanctions for non-compliance, any uncertainty in interpreting the requirements of the proposed regime must be avoided.

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

We query whether a criminal offence for a failure to update information is proportionate and we have concerns about introducing more regulatory offences which are of limited efficacy and doubts as to how this would be policed for overseas entities. Please also see our response to question 17 on the need for certainty in interpreting the requirements of the proposed regime, where criminal sanctions apply for non-compliance.

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?

We would caution against any requirement that a chargee be "an accredited or legitimate lender". Taking security over UK property *per se* is not (nor in our view should it be) subject to regulation. Charges are commonly registered over UK property for reasons which are entirely unrelated to lending, e.g. the fortification of contractual agreements, the protection of option rights, the restructuring of liabilities, etc. We consider that enforcement of the proposed regime should focus on the overseas entity which owns the property and on its beneficial owners, not on security-holders. In practice, we do not regard the loophole mentioned in the Call for Evidence to be of significant concern, because in order to have acquired a registered title to the property and to have granted a charge over the property, the relevant overseas entity would, at the outset, need to have complied with the requirements of the proposed regime and, accordingly, information on its then beneficial owners should be available. Those beneficial owners would, we expect, be under a duty to notify any changes to their details. Enforcement of the proposed regime against the overseas entity itself and its beneficial owners should therefore be sufficient to achieve the aims of the regime without the need to interfere with the rights and responsibilities of security-holders.

The Call for Evidence indicates that new lending secured against a property would not be possible where an overseas entity has not complied with the requirements of the proposed regime. We assume that this concerns the granting by the relevant overseas entity of a new charge over the property, rather than the advancing of a new loan to the overseas entity under the security of an existing charge on the property. Any restriction on the latter could have a significant impact on the ability of financial institutions to offer secured overdrafts and revolving credit facilities to overseas entities owning UK property.

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

Transactions involving co-ownership could be affected, where one of the co-owners is an overseas entity, e.g. home reversion and shared ownership schemes. In Scotland, the court remedy of division and sale is fundamental to such co-ownership arrangements and care should be taken to ensure that any restrictions under the proposed regime upon an overseas entity conveying its interest in a property do not interfere with the powers of a Scottish court to ordain the overseas entity to grant a conveyance pursuant to an action of division and sale.

Yours faithfully

For and on behalf of Shepherd and Wedderburn LLP