Law Society of Scotland

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Written evidence

Draft Registration of Overseas Entities Bill

March 2019

Introduction

The Law Society of Scotland is the professional body for over 11,000 Scottish solicitors. With our overarching objective of leading legal excellence, we strive to excel and to be a world-class professional body, understanding and serving the needs of our members and the public. We set and uphold standards to ensure the provision of excellent legal services and ensure the public can have confidence in Scotland's solicitor profession.

We have a statutory duty to work in the public interest, a duty which we are strongly committed to achieving through our work to promote a strong, varied and effective solicitor profession working in the interests of the public and protecting and promoting the rule of law. We seek to influence the creation of a fairer and more just society through our active engagement with the Scottish and United Kingdom Governments, Parliaments, wider stakeholders and our membership.

Our Banking, Company and Insolvency Law and Property and Land Law Reform sub-committees and Property Law Committee welcome the opportunity to consider and respond to the Joint Bill Committee call for evidence on the Draft Registration of Overseas Entities Bill. Our comments refer to the version of the Bill as published for consultation by the Department for Business, Energy and Industrial Strategy in July 2018.[1] We have the following comments to put forward for consideration.

General remarks

We fully support the aims of the proposal in increasing transparency and in seeking to combat money laundering, corruption and terrorism. Any action that prevents or reduces such activities is strongly to be welcomed.

We do not condone the use of legitimate business structures for criminal intent and purposes and are fully supportive of proportionate, appropriate and targeted measures aimed at preventing this. As the professional body for Scottish solicitors we would take robust disciplinary action against any Scottish solicitor who was involved in facilitating any criminal activity. However, in considering any proposed measures, care should also be taken to avoid introducing measures which may impose a burden on legitimate businesses and commercial activities, but which may not effectively dissuade those businesses or individuals intent on criminal behaviour.

Furthermore, the Scottish legal profession serves clients across the globe. We recognise the benefits which may result from a more transparent economy and welcome measures to encourage investment.

[1] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/727915/Draft_Registration_of_Overseas_Entities.pdf

We note that the Scottish Government has recently consulted on draft *Land Reform (Scotland) Act 2016 (Register of Persons Holding a Controlled Interest in Land) (Scotland) Regulations 2021*[2] and we responded to that consultation,[3] which has some points of overlap with the Draft Registration of Overseas Entities Bill.

Relationship with Scottish registers

Clarification is needed as to how the UK Government's proposed Register of Overseas Entities will operate alongside the Scottish Government's proposed Register of Persons Holding a Controlled Interest in Land. There is obvious overlap and therefore the two government bodies will need to address the potential for both duplication and conflict in operating two separate systems. At this stage, our comments should therefore be considered with this concern in mind.

The Scottish land registers and the legislation the draft Bill proposes to amend (Schedule 4) are devolved matters and therefore sit within the competence of the Scottish Parliament. We note the Department for Business, Energy & Industrial Strategy "will continue to work with the Devolved Administrations as the proposals are refined."[4] Additional information is needed as to how this will operate and further consultation with Scottish stakeholders may be required.

We are concerned that the proposed registration system as presented in the draft Bill would be likely to add to the delays in the registration procedure already being experienced in Scotland. It will be necessary for the Keeper of the Registers of Scotland to be afforded additional resources to discharge her increased responsibilities and safeguard the integrity of the Scottish property registers and the accuracy of the information recorded.

We also note that this system would create an additional expense in any transaction affecting land in Scotland as the Bill would require those acting for the transaction's parties to establish whether any party is, or should be considered, a registered overseas entity even where this is *prima facie* not the case (for example where a relevant party is a Scottish partnership).

We are concerned that the proposed registration system as presented in the draft Bill would be likely to create additional risks for purchasers in the purchase of property from Overseas Entities.

Finally, we note that the proposed register of overseas entities is to be maintained by the registrar of companies for England and Wales (clause 3), even where the entity has an interest in Scottish land. It is likely that this will require Scottish solicitors to inspect the register in London in every case, albeit we expect that electronic access will be available. There is a question as to whether this would be acceptable from the perspective of Scottish stakeholders as there is a separate Scottish register of companies, and therefore Scottish registrar.

[2] https://consult.gov.scot/land-reform-and-tenancy-unit/transparency-in-land-ownership/
[3] https://www.lawscot.org.uk/media/361338/18-11-08-plc-pllr-consultation-delivering-improved-transparency-in-land-ownership-in-scotland-final.pdf
[4] See page 3

Drafting

We consider that some aspects of the Bill require greater clarification in terms of their drafting.

For example, in Schedule 2, paragraph 23(4) and (5), we consider that further clarity is required in relation to the definition of foreign limited partner. It is not clear what "arrangements" means, nor the scope of characteristics which the Secretary of State might provide for in delegated regulations.

We consider that the provisions of the new section 112A (Offence by an overseas entity, found in schedule 4 of the draft Bill) would merit greater clarity. The cross referencing in section 112A(1) to paragraph 2 of the new schedule 1A to the 2012 Act (also found in schedule 4 of the draft Bill) is confusing and we suggest that the requirements of the offence be set out in full in section 112A.

In the new Schedule 1A, it is not clear from the face of the draft Bill as to whether in section 1(1), each of (i) to (iii) qualify both "…a qualifying registrable deed" and "a registrable deed…". We consider that the drafting in this regard could be improved and the relationship between sections 1(1) and 1(2) made clearer.

In addition, we consider there is ambiguity in paragraph 2(1)(a) of the new Schedule 1A. We assume that the qualification "which is a standard security" is intended to apply only to a registrable deed, and that paragraph 2(1) is intended to apply to any qualifying registrable deed, whether or not it is a standard security. However, we consider this is not clear in the current drafting.

We comment on the drafting of paragraph 7(3) of the new Schedule 1A in our answer to question 12.

Dispute resolution

Whether or not an entity has legal personality will be a matter of fact under the law of the relevant jurisdiction. We do note that there is a potential for a dispute to arise if an entity considers it does not meet the requirements for registration and Companies House takes a different view (or even vice versa). We consider that in the first instance it would be appropriate for advice to be sought from an independent expert, competent to advise on the law of the relevant jurisdiction. In the longer term there may be merit in guidance notes or similar being produced by Companies House, including a list of those organisation types which are accepted as being overseas entities and those which are not.

At the same time, we acknowledge that disputes might nevertheless arise and consider that it should be possible to lodge an appeal and go through a dispute resolution process. If the dispute involves determining the application of the Bill in relation to a particular type of entity, we consider it most appropriate that this be resolved by the courts, which would allow Companies House and the relevant party/parties to lead evidence on foreign law as a matter of fact. We note that if no such system was established, the offence mechanisms would apply. We note that there is also a potential for the Keeper of the Land Register to reject an application if there were concerns although there is a question as to the degree to which the Keeper would be under a duty to form a view.

Response to questions

Objectives & scope

1. Will the public register as established by the draft Bill effectively deliver the policy aim of preventing and combatting the use of land in the UK for the purposes of laundering money or investing illicit funds?

As with all legislation of its nature, the answer to this question will depend on the extent to which the Bill is enforced and is practically enforceable.

2. Will the proposed register have a dampening effect on overseas investment into the UK property market? Is this a necessary consequence of increased transparency?

We have no statistical or other research to offer on this point.

However, we anticipate that the proposed register may have a dampening effect if it is seen as unnecessarily cumbersome or complicated to comply with. Certain individuals may be discouraged from investing in the UK property market if they consider that the register would prevent them from maintaining a particular level of privacy. It is important to recognise that a desire to preserve details of individual's economic affairs from public knowledge does not mean that the individual concerned is engaged or attempting to engage in illegal activity.

At the same time, we note there are also costs to the economy generated by crime, terrorism and money laundering activities.

In addition, we note that the costs of compliance with the regime may impact upon overseas investment. We consider that the cost estimates provided by the Government as to the average cost to entities to obtain external advice in relation to the new Bill and costs to identify beneficial owners and collect their information are unrealistically low. For example:

(i) these estimates do not include the cost of registration dues;

(ii) we anticipate that in some circumstances, legal opinions from foreign jurisdictions will be required; and

(iii) the costs appear to refer to the cost of allowing an overseas entity to comply with the legislation. We understand that this does not include costs that may be incurred by purchasers seeking to transact with an overseas organisation in testing whether or not such the overseas organisation should be registered.

If costs of compliance are high, this could impact upon the desire of overseas entities to invest in the UK property market.

3. Are the conditions for "registrable beneficial owners" appropriate? Are they sufficiently clear (i) for overseas entities with different ownership structures to be able to determine which individuals or legal entities are registrable, and (ii) to capture different types of legal entity?

We note that the proposed register will "mirror as far as possible the regime currently in place for UK entities subject to the PSC regime" (that being the requirement to maintain a register of people with significant control over a company under the Companies Act 2006 ss.390C and Schedule 1A).[5] In this regard, there are a number of points, which merit consideration.

Generally, we consider that aligning the definition of beneficial owner to the PSC regime should help to ensure coherence between the PSC regime and the proposed regime for overseas entities.

However, it is important to avoid replicating the issues which have arisen under the PSC regime regarding its application to banks and other lenders who have taken security over shares in Scottish companies. A possible interpretation 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") is that a bank or other lender which has taken fixed security over the shares of a Scottish company could become registrable under the PSC regime. While it is clear that this was not the intention, concerns have been raised that this could nevertheless be a consequence of the wording of that legislation. If the definition under the PSC regime is to be replicated for the proposed regime for overseas entities, it is important that this particular problem is not replicated for the new register. We do not consider that it is appropriate for a bank or other lender to be considered to own or control an overseas entity.

Schedule 2, paragraph 6 of the draft Bill states ('condition 4') that the 'beneficial owner' of an entity includes a person who may exercise 'significant influence or control' over the entity. There is no attempt to define the meaning of this phrase for the purposes of the draft Bill, which is identical to paragraph 5 of Schedule 1A to the Companies Act. Moreover, the draft Bill does not contain provisions equivalent to paragraph 24 of Schedule 1A which requires the Secretary of State to publish "guidance" (which is subject to parliamentary control) about the meaning of "significant interest or control". We do not consider it to be satisfactory that the question of whether a criminal offence has been committed under the draft Bill's proposals should depend on the precise meaning of this undefined phrase. Even if guidance were to be given, this might not be sufficient to give the level of clarity necessary where a person may find themselves guilty of a criminal offence.

[5] Explanatory Notes, paragraph 23

Schedule 2 paragraph 18(3)(d) of the Bill provides that a person has a “majority stake” in an entity if that person exercises “dominant influence or control” over that entity. “Dominant influence or control” is not defined (and this term does not appear in the PSC legislation). For the reasons indicated above, we consider that this phrase should also be given further definition.

(i) and (ii) We are not aware of any specific types of overseas entities that would be within the scope of the regime but would not have a route to comply. However, as commented in our previous response, if a company is not sufficiently similar to UK companies limited by shares, there may be practical difficulties in determining how the relevant company ought to comply.

Furthermore, the Bill only applies to an 'overseas entity' as defined in clause 2, being a 'legal person' governed by the law of a country or territory outside the UK. However, this raises a couple of concerns:

(a) 'Entity' is not defined. However, a statutory definition would be preferable in case there is difficulty particularly with foreign concepts of what exactly constitutes an 'entity' and its 'legal personality'. Practitioners and the registers may have difficulty in applying this to unfamiliar foreign judicial concepts.

(b) No attempt is made to control the use of an individual as, for example, disponee where that person is acting as nominee of an (unregistered) 'overseas entity'. We are concerned that this could leave the system open to abuse. There may be an answer if the relationship between this proposal and the Scottish register noted above is adequately clarified.

Finally, we consider that there may be difficulties faced by those acting for purchasers in assessing whether an overseas entity is a legal person under foreign law. We anticipate that very few Scottish solicitors will be qualified to advise on the foreign law affecting each overseas entity. The example of a partnership as understood in the UK may be instructive here. In Scotland, a partnership has separate legal personality; in England, however, it does not. We anticipate that similar situations will arise in foreign jurisdictions where it will not be clear whether an entity has legal personality. We note that in the event of there being uncertainty, there is the potential for the over-registration of entities, which could lead to further confusion and frustrate the objective of transparency.

4. Should other types of entity (such as trusts) be included in the scope of the draft Bill?

We consider that this is a policy decision.

We note however that where trustees, which would include executors, are not registered owners of the land held by the trust, they will be subject to individual liability and could face criminal penalties if the registration requirements are not adhered to. This might discourage people from acting as executors and could create unnecessary distress at a time when people may be vulnerable. This does not appear to the be the kind of situation at which the register is aimed, and we consider that an exception to the registration rules might be considered in this context. Given the nature of trusts and the ways in which they can be

created or arise, the inclusion of trusts may give rise to additional legal considerations. This is based on an assumption that overseas trusts are analogous to trusts in the UK, however this may not be the case.

5. Are the proposed powers allowing the Secretary of State to exempt, or modify application requirements for, certain types of entities appropriate? Under what circumstances should these powers be exercised?

We have no comment on this question.

Operation of the register

6. Are the information requirements sufficiently comprehensive? Are there other types of information that it would be useful to include? Conversely, do the requirements place an undue burden on entities?

It should be sufficient that the beneficial owner's address be that of a contact address at which they are able to be reached, such as a business address. For privacy reasons, we do not consider they should be required to give their home address although we note the terms of clause 20 in respect of residential addresses.

We consider that there may be some merit in also requiring an email address or contact telephone number to be provided but again there should be no requirement that these are private contacts. If the only contact details are personal ones, or the Government has a particular reason for requiring, for example a home address, we consider it appropriate for these to be held by Companies House but not published on the public register.

We note that the date on which the individual became a registrable beneficial owner is part of the information to be provided. While this is likely to be clear and demonstrable in the case of voting rights or ownership of shares, establishing the date on which an individual "…. actually exercises, significant influence or control…." may be hard to demonstrate if the control is demonstrated by a pattern of behaviour over time.

7. What controls should be in place to verify the information provided to the register?

We note that as a general rule, information submitted to Companies House is not submitted to verification procedures. Registers of companies in relevant jurisdictions may be of assistance in verifying information provided to the register where these have been made public. However, in practical terms it may be difficult

to create processes to verify much of the information without incurring unreasonable costs and potentially delays.

8. Does Companies House have sufficient capacity or resources to administer and monitor the register?

As noted above, Companies House does not currently monitor the information submitted to it for domestic company register purposes etc. Companies House will be best placed to determine the answer to this question in terms of administering the register, however, we anticipate that they would require additional resources of some description unless the expected scale of registrations is very small.

We also consider there will need to be a short time limit for processing of the information submitted to Companies House so that it does not unfairly delay the conveyancing process and those inspecting it know that they can rely on the information recorded. A consistent timescale for making entries or amendments would help to ensure that there is the increased transparency which the creation of the register is intended to achieve. We consider that there should be certainty as to the maximum time for processing any application for registration, or for accepting an annual update (including the shortening of an update period). If it was possible for an application for registration to be held up for any length of time, then there is the potential for a party to a contract involving the transfer of property to be put in breach of their obligations as a result of such delays by Companies House or parties would need to provide for flexibility for the date of settlement. In some cases, where the date of entry is time critical (for example, at the year end, or where settlement is linked to other transactions), the need to provide for flexibility would likely have an adverse impact of parties.

9. Should entities which cannot identify, or provide full details of, their beneficial owners be allowed to register? Is it useful to hold the information of a managing officer in place of a beneficial owner? Is there any additional information that should be required from entities that are unable to give information about their beneficial owners?

In the interests of transparency (and given difficulties that may arise with providing all the information requested, for example see our answer to question 6), it would be preferable to allow such entities to register even where they have not provided full details as the lack of those details would at least be made transparent. It would seem sensible to require entities to provide information about managing officers if all the information on beneficial owners cannot be supplied.

10. Does the draft Bill provide sufficient protections for individuals who could be put at risk by having information about them made publicly accessible?

We refer to our answer to question 6.

In addition, we note the terms of clause 22 of the draft Bill, being an enabling provision for the Secretary of State to make regulations in relation to the protection of information beyond the date of birth and residential address of is registrable beneficial owner or managing officer in relation to an overseas entity. As the provisions are enabling, it is difficult to assess whether the draft Bill provides sufficient protections.

Given the potential nature of the circumstances in which an individual will wish to apply to have information protected, such applications should be given high priority in the registration process.

As it is likely that the decision as to whether or not to accept an application will be at the discretion of the Registrar, it is important that there is clear and thorough guidelines for this process. We suggest that careful consideration be given as to "the information to be included in and documents to accompany an application" - victims of abuse, intimidation, or threats may find it difficult to obtain certain information or documents, particularly if this is required within a short period of time. It is essential that the registration requirements do not cause harm to individuals at risk.

11. Should it be possible to appeal the suppression of information from public disclosure?

Yes, we consider it appropriate for there to be an appeal process in relation to such matters. Any application for an appeal should be considered on a confidential basis.

Compliance & enforcement

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

As we commented in our response to the BEIS consultation, the question of whether or not to introduce a criminal offence for failure to update information is a matter for policymakers. However, we have significant concerns that this is not a practicable or efficient method to ensure compliance.

In our response to the consultation on improving transparency in land ownership in Scotland, we took the view that, on balance, a failure to comply with registration requirements should not constitute a criminal offence. In particular we highlighted potential difficulties in identifying who in fact is "in control" – which relates to overseas companies as it would to domestic companies. We did not think a criminal sanction

would be effective or justified in that context, particularly considering the potential harm involved should there be a failure to comply. The same reasoning applies in the current context.

One possibility might be to introduce a civil penalty if the foreign entity failed to comply with the requirement to update records, which might be a more appropriate response.

There is a further question as to the effectiveness of introducing a criminal offence which applies solely to overseas companies, many of which are likely to be beneficially owned or controlled by individuals over whom the UK cannot easily claim jurisdiction. Without effective enforcement, the creation of such a criminal liability would be of limited purpose. In this context also, a civil penalty may be more effective as it would potentially be easier to ensure enforcement in practical terms, for example a judgement in a UK court setting a particular penalty for failure to comply could be enforced against other assets held in the UK.

At a practical level, we have concerns about the drafting of paragraph 7(2) and (3) of the new Schedule 1A to the 2012 Act (found in schedule 4 of the draft Bill). The provisions would require the Keeper of the Registers of Scotland to refuse to register a disposition if the overseas entity has "failed to comply with the duty in Section 7 of the Registration of Overseas Entities Act 2018…".

In addition to our concerns set out in our response to question 15, we are concerned that this drafting could create uncertainty and increased risks to purchasers. The drafting implies that there is a difference between the submission and acceptance of the annual update (which may or may not be correct) and compliance with the duties to submit an annual update. If the first, wider interpretation is applied, then on any application for registration of a qualifying registrable deed, each applicant and the Keeper of the Registers of Scotland would need to check that an annual update had been submitted to (and we assume accepted by) Companies House, but also that the annual update complied with the duty in clause 7.

If all that is required is for the annual update to have been submitted to (and if relevant accepted by) Companies House, we consider that Paragraph 7(3) of Schedule 1A should state that. If there is to be a wider test, then we note that this is in effect imposing a duty on the Keeper of the Register of Scotland to investigate the substance of the annual update, which is not a duty imposed on the Keeper in relation to the initial application for registration of the overseas entity.

13. How should the Government ensure that all prospective and existing overseas owners of qualifying estates are made aware of the new register and its requirements by the time the register is operational or before the end of the transition period?

Some overseas owners may be informed of the changes by their legal advisors. Solicitors and other conveyancing professionals should therefore be made aware of the changes. We expect that in many cases they would take the initiative and inform overseas clients of the new obligations. Many professional bodies, membership organisations and individual businesses would be likely to circulate information on legal changes such as this in any case but BEIS could contact relevant stakeholders to ensure such

information is communicated if it was felt that a special approach might be needed for this particular measure. The creation of the register could be also publicised in materials relating to investment in the UK.

14. Will the draft Bill's objectives be achieved in a consistent manner throughout the UK despite differences in how property is bought and sold – and in the draft Bill's definitions of 'qualifying estates – in the different jurisdictions? Will there be a level playing field across the UK?

We have not identified any particular problems in relation to achievement of the draft Bill's objectives.

However, we consider that there is potential for some differences in the manner in which this will be achieved in the different jurisdictions. As different to England, Wales, and Northern Ireland, there will not on the face of the Land Register be a "red flag" showing that a title is currently held by an unregistered overseas entity. The reform of the Scottish Land Register by virtue of the Land Registration etc. (Scotland) Act 2012 incorporated as a principle that the title sheet should deal only with title matters. To include details of any registration of an overseas entity on the title sheet would therefore derogate from this principle.

We have previously stated that information in relation to the Register of Controlled Interest in Land should not be shown on the title sheet. However, we consider that if the title sheet was to contain details of either the Register of Controlled Interests or the Register of Overseas Entities, then it would be appropriate for it to contain both.

We consider that there is scope for additional delay in the conveyancing process where it is clear that a seller or a purchaser is governed by a foreign jurisdiction, but has not been registered as an overseas entity. In such circumstances, it will be necessary to establish that the seller or purchaser is not a registrable overseas entity. As mentioned above, that analysis is likely to depend upon a composite analysis of the effect of the UK Act, as interpreted under UK legislation; and the nature of the seller or purchaser in terms of the jurisdiction under which it was incorporated. This would almost certainly require input from lawyers in two different jurisdictions, which may create difficulties in reconciling two separate pieces of advice. In this scenario we would anticipate that there may be further delays if the Keeper were to carry out separate checks.

15. Are the exceptions to the restrictions on disposal sufficient to protect the rights of third parties? Should any other exceptions be included in the draft Bill?

We consider it necessary for there to be protection for those purchasing in good faith.

For example, we consider there is potential for difficulty for a purchaser in particular circumstances. In Scotland, the process of the registration of land can take a number of months. Within that period there is always a risk that the application is rejected and a purchaser has to re-present the application to the Keeper. While a solicitor may undertake all the necessary diligence at the time of purchase to establish that the seller is duly registered and its records are up-to-date, if the entity ceases to update or removes itself from the register after the date of settlement and the application is thereafter rejected, a purchaser may not be able to obtain valid title.

Such circumstances have the potential to result in the overseas entity both retaining the property and having the proceeds from the sale of that property: this seems counterintuitive. We therefore consider that there should be general measures to protect a good-faith purchaser.

16. Are the sanctions for non-compliance with information requirements proportionate and enforceable?

As referred to in our answer to question 12 above, we do not consider it appropriate for failure to provide an annual update timeously to result in criminal liability. It appears to be inappropriate for failure to provide an update to automatically trigger the same sanctions as providing false information. Careful drafting could mitigate against the chances of this distinction being open to abuse.

Delegated powers

17. Are the proposed delegated powers in the draft Bill appropriate?

As a matter of principle, we consider that where the Secretary of State is making regulations, these should be made following consultation with relevant stakeholders. We consider that clause 35 should be amended to reflect this.

Under clause 30(6) as currently drafted, the Secretary of State would have power to make regulations to determine the meaning of “exempt overseas entity”. We are concerned that this could raise key policy considerations and is not appropriate for the negative resolution procedure or indeed regulations. This goes to the heart of the issues the legislation is seeking to address and should be set out in the Bill itself.

Furthermore, as commented in the introductory section outlining our concerns around drafting, in Schedule 2, paragraph 23(4) and (5), we consider that further clarity is required in relation to the definition of foreign limited partner. It is not clear what “arrangements” means, nor the scope of characteristics which the Secretary of State might provide for in delegated regulations. It is therefore unclear if the proposed delegated powers could be considered appropriate.

18. Do the procedures selected (affirmative/negative resolution) for each power provide for sufficient levels of parliamentary scrutiny?

See response to question 17.

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