

# Transparency v privacy

*Laura Williamson highlights the pros and cons of the proposed register for foreign property-owning companies*



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**'The rationale given for focusing on real estate ownership is the frequent and sophisticated use of this asset class by criminals to hide the proceeds of crime.'**

**D**isclosure of beneficial ownership for foreign companies that own property in England and Wales is a developing area of law to watch. The vast majority of UK companies (with some exceptions for listed companies where there is not the same concern about control) have been required to keep a register of people with significant control (PSCs) since April 2016 and, by June 2017, should have submitted their register to Companies House, where it will be made available for public view.

The UK government is considering setting up a similar register for foreign companies that own property in England and Wales. With no firm plans yet in place, the time is ripe to look at the current position, to speculate on how it may change and to consider the practical implications from a commercial real estate perspective.

### **Why has the government brought in the PSC register?**

The PSC register was established in order to increase transparency about the ownership and control of companies registered in the UK. The regime also extends to UK-registered LLPs and *societates europaeae*. The UK government impact assessment carried out in September 2015 prior to implementing the new rules confirms that:

... the overarching policy objective... is to reduce crime and improve the business environment to facilitate economic growth through enhanced corporate transparency.

It is noteworthy that the UK is the first G20 member country to

create such a public register and has promoted the cause of transparency on the global stage. This can be traced back to the G8 summit held at Lough Erne in 2013 during the UK's G8 presidency, in which trade, tax and transparency were on the agenda. Following the Lough Erne summit, the G8 countries issued a list of core principles, which each nation should build upon to publish a national action plan. Key principles included:

1. Companies should know who owns and controls them and their beneficial ownership and basic information should be adequate, accurate, and current...
2. Beneficial ownership information on companies should be accessible onshore to law enforcement, tax administrations and other relevant authorities... This could be achieved through central registries of company beneficial ownership and basic information at national or state level... Some basic company information should be publicly accessible.
3. Trustees of express trusts should know the beneficial ownership of the trust, including information on beneficiaries and settlors. This information should be accessible by law enforcement, tax administrations and other relevant authorities...

This was a step along the road to the creation of the UK PSC register. Across the EU, these principles have also been developed by way of the Fourth Money Laundering Directive. This Directive requires EU member states to set up a register of beneficial

ownership information for entities incorporated within their territory by 26 June 2017. This register must be made available to law enforcement and other authorities, but the Directive does not require the register to be made public. Overall, this shows that the UK is a step ahead of the consensus in the EU and the creation of a fully public PSC register is due to a UK government policy position

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that has been consistent for several years.

### What is meant by 'beneficial ownership'?

The most appropriate definition in this context originates from the Financial Action Task Force and states that a beneficial owner is:

... the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.

This was the starting point for the statutory definition of a PSC in the Small Business, Enterprise and Employment Act 2015.

Applied to UK companies, this Act establishes a 25% minimum threshold for shareholdings and voting rights, so that a beneficial owner with a shareholding or voting rights below these thresholds (and who does not fall into any other category) is not required to appear on the register. The detailed guidance from Companies House states:

For most companies these will be people who:

- hold more than 25% of a company's shares
- hold more than 25% of a company's voting rights
- have the right to appoint or remove the majority of directors

There are two further, less common, options. These are:

- any individuals who have the right to exercise or actually exercise significant influence or control are PSCs
- where a trust or a firm meets one of the three statements above, any individuals with significant control or influence over that trust or firm are PSCs.

The 25% shareholding threshold was chosen due to its significance in company law, as this is the minimum level of shareholders required in order to block a special resolution of the members of a company. For LLPs the equivalent test is whether an individual holds rights over more than 25% of the surplus assets on a winding up.

The Companies House website gives further guidance for companies with complex structures and for all UK companies on how to meet the PSC register requirements in practice. In particular, if a UK company is owned or controlled by an overseas company then (aside from certain exceptions) the overseas company will not be entered on the PSC register. Instead the UK company is required to look through the chain and establish the identity of the individual with the ultimate ownership and control, and enter that person's details (if the above

tests are met). This means that the ultimate beneficial owner of an overseas group that includes a UK company subsidiary could be subject to entry on the PSC register.

### Will a similar register be brought in for foreign companies?

This question falls under the remit of the Department for Business, Energy and Industrial Strategy (BEIS). In March 2016 BEIS (then 'BIS') issued a consultation paper on the beneficial ownership of foreign companies, which included a chapter on the purchase and ownership of real estate in the UK by foreign companies. The intention was to consult upon the principle of establishing a register for foreign companies owning UK property. The consultation closed on 4 April 2016 and responses received have not yet been published by BEIS, although it is anticipated that a second consultation will be held on the details of how such a register would work.

The rationale given for focusing on real estate ownership is the frequent and sophisticated use of this asset class by criminals to hide the proceeds of crime. Moreover, the high value of property in, for example, the London market makes it possible for considerable sums to be laundered in one transaction. The paper includes a statement that over £180m worth of property in the UK has been investigated as suspected proceeds of corruption and over 75% of those properties used offshore corporate ownership, which may be 'the tip of the iceberg'.

Also flagged in the first consultation paper was the disparity between the levels of information available for UK and overseas companies respectively owning property in the UK. As it stands, a UK company that is a registered proprietor at the Land Registry is identified by their company number, which in turn can be used to access the PSC register information. Equivalent information is not available for foreign company registered proprietors, meaning that their

ownership structure is far less transparent.

The specific suggestion in this regard in the paper is:

... asking each of the registered proprietors of up to 100,000 titles that are currently registered to foreign companies to obtain a unique identifier from the foreign company beneficial ownership register and then provide it to the Land Registry within a reasonable time.

This would mean that all overseas owners of existing landholdings in England and Wales would need to undertake a two-step process, first providing beneficial ownership information to a central public register in order to obtain a unique identifier number, and then providing that identifier to the Land Registry in order for it to be entered onto the title register for their properties.

There would also be a similar requirement on new transactions, so that a foreign company would only be able to register a new interest in land in England and Wales by providing the Land Registry with its beneficial ownership register identifier number.

Proposed sanctions for non-compliance set out in the consultation paper are:

- applying sanctions similar to those of the PSC register regime, so that criminal sanctions are available against the company, its officers and/or the PSCs;
- enhanced criminal sanctions (for example a statutory presumption that a charging order will be imposed on property if a company or individual is fined as a result of a breach and/or daily fines); and
- suspending the unique identification number of the foreign company, so preventing a sale or charge of the relevant land until the number is restored.

There is an acknowledgement in the paper that it is more difficult to enforce criminal penalties against foreign companies for failure to comply with UK law. It is likely then that the sanctions will include some form of charging order or restriction upon dealing with the relevant property. This does seem to be a practical method of securing compliance but further details are likely to be included in the second consultation paper

Since then, the Brexit vote has dominated headlines and no second consultation has yet been issued by BEIS on implementing the foreign company register. However, the present UK government leadership has continued to promote corporate transparency. Sir Eric Pickles MP, while not a current cabinet member, has been dubbed 'the Prime Minister's anti-corruption champion' and attended the Paris Open Government Partnership Global Summit in

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(when published), as effective enforcement will be key to implementing the proposals.

In May 2016 (following publication of the first consultation paper), the then Prime Minister, David Cameron, hosted the Anti-Corruption Summit 2016 in London. The UK government press release confirmed that

... any foreign company that wants to buy UK property... will have to join a new public register of beneficial ownership information before they can do so. This will be the first register of its kind anywhere in the world. Crucially, it will include companies who already own property in the UK, not just those wishing to buy.

In his closing speech at the summit, David Cameron included a comment that, in practice, the support of professional service providers (lawyers, accountants and estate agents) is needed if anti-corruption legislation is going to take effect as intended. At the same time, a public statement of support for the aims of the Anti-Corruption Summit was issued and signed by, among others, prominent property organisations such as CBRE, JLL, Savills, Bilfinger GVA and Knight Frank.

December 2016 to reiterate the commitment to creating a public register of beneficial ownership information for foreign companies that own or buy property in the UK.

Likewise, HM Treasury published a consultation paper in September 2016 on the implementation of the EU Fourth Money Laundering Directive and confirmed that:

... the UK will now establish a public register of company beneficial ownership for foreign companies who already own or buy property in the UK...

So, the policy direction is unchanged, notwithstanding a change of Prime Minister and the ramifications of the Brexit vote.

### **Does this mean that all beneficial ownership structures in the UK will become public?**

No, in fact the UK government has taken a different line when it comes to UK trusts. Over the past few years it has lobbied in Europe against being required to create a public register of UK trusts. The rationale is that, under UK common law, trusts are often used for private matters and it would be disproportionate to require a public

central registry. During a House of Lords debate in 2014, Lord Newby stated that:

The Government oppose[s] the mandatory registration requirement for trusts... we consider registration of trusts to be a disproportionate approach and, in particular, one which undermines the common-law basis of trusts in the UK.

This approach has been successful and HM Treasury's September 2016

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consultation paper sets out the UK government proposals for beneficiaries of trusts in accordance with the Fourth Money Laundering Directive. These proposals will come into force from June 2017. The result is that trustees of any express trust will need to obtain and hold details of the beneficial ownership of the trust and have this information available for the authorities. The information will include the identities of:

- the settlor;
- the trustee(s);
- the protector (if any);
- the beneficiaries or class of beneficiaries; and
- any other natural person exercising effective control over the trust.

Further, if the trust 'generates tax consequences' (meaning that a trust liable to tax in the UK is required to submit a tax return under UK law), then the beneficial ownership information will also need to be held in a central register. However, the register will be operated by HMRC in order to

minimise the regulatory burden on trustees and the required information can be provided to HMRC at the same time as the relevant tax return. Moreover, this information will not be made public, although it will be available to the authorities.

#### **Is the PSC register likely to achieve its intended purpose?**

It is worth pausing to consider whether the PSC register is likely to achieve its intended purpose.

Yes, by definition, it means more information in the public domain, but how accurate is that information? The following issues have been highlighted in the press:

- There is no independent verification and the register relies upon self-reporting, which may mean that law-abiding companies will try to comply but wrong-doers will not.
- Companies House does not require money-laundering checks when a company is being set up so there are low barriers to the creation of new companies.
- Although there are hefty sanctions available for non-compliance (failure to provide accurate information on the PSC register is a criminal offence that may result in an unlimited fine and/or a prison sentence of up to two years), it remains to be seen whether effective enforcement is possible.

The PSC register data has been publicly available from 30 June 2016

and interested parties such as Global Witness have been reviewing the data as the register is populated. According to their research (published in November 2016), there are almost 3,000 overseas companies incorrectly listed as beneficial owners, which suggests that the exercise of looking through the chain to establish the identity of the ultimate beneficial owner has not been properly carried out across the board. It remains to be seen, however, to what extent enforcement action will be taken in practice.

The operation of the PSC register is due for review by the UK government in 2019, which will provide an opportunity to consider the issues around enforcement. However, it may be that decisions are made about the structure of a foreign company register before that review takes place.

#### **Is there anything practitioners should be doing now?**

From a practical perspective, consider the following:

##### **Is your UK company client aware of the PSC register requirements and, if applicable, has it complied?**

Hopefully, the answer to this is 'yes'. The requirement to maintain a PSC register has been in force since 6 April 2016. From 30 June 2016 it has been necessary to file this at Companies House at the same time as filing the company's annual confirmation statement (previously the annual return). As mentioned above, failure to provide accurate information on the PSC register is a criminal offence that may result in a fine and/or a prison sentence of up to two years.

Depending on the company structure, the PSC requirements can be quite complex, but there is detailed guidance available from Companies House. There will, however, be further changes to the regulations. In particular, there is an EU requirement that the information on the PSC register should be 'current', so it is likely that the obligation for annual reporting will shift to a shorter timescale, such as within six

months of a change to the PSC information.

**Are there steps your client can take to protect their personal privacy?**

The PSC register maintained by the company needs to include the usual residential address and date of birth for each PSC. However, the residential address should not be published on the public register and the date of birth information should be limited to the month and year. Further, individuals who may be at risk of violence or intimidation as a result of being on the PSC register can apply to Companies House to have their information protected, which might mean suppressing all their information or preventing their residential address from being shared with credit reference agencies. That said, the guidance suggests this would only be allowed in exceptional circumstances. The Global Witness statistics from November 2016 indicated that at that point only 30 individuals out of around 1.2 million listed beneficial owners had applied for and been granted this exemption.

Further, the existing regime for company director information contains some protection against a residential address being published, which should be noted on incorporating a company when a usual residential address for each director is supplied to Companies House, although should not appear on the public register. But, if the residential address is also nominated as a registered office or service address, it will be placed on the public register and will remain part of the public record even if the registered office or service address is subsequently changed. If your client has been in business for many years, they may be surprised how many residential and business addresses are traceable through the public register.

Finally, it is worth noting that in this era of identity theft it is also sensible to be cautious about allowing copies of a 'wet ink' signature to appear on the public record. Acknowledging this, the Companies House guidance

suggests using online filing via an authentication code where possible.

**The Land Registry: consider whether to exempt documents from the general right of inspection**

Always bear in mind that the Land Registry is a public register and there is a general right of inspection under the Land Registration Act 2002. Accordingly, when sending a

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document to the Land Registry, consider whether it contains commercially sensitive information that should be exempt from the general right of inspection. If so, you may wish to consider an EX1 application under the Land Registration Rules 2003 in order to omit that information from the version of the document that appears on the register. The Land Registry states that if such information already appears in the register it will not be removed. This means that it is important to get it right when making the initial registration application as it will be too late to make an EX1 application afterwards.

**Anti-money laundering: customer due diligence**

Consider your firm's anti-money-laundering procedures and make sure that they are consistent with current Law Society guidance. In particular, when setting up a company as a new client you will need to understand the beneficial ownership of that company. In the context of a group of companies this may mean asking your client to supply you with a structure chart and information so that you can be satisfied that you have an overall understanding of the ownership and control structure

of the client company. As it stands, a key defence against overseas companies carrying out money laundering via UK property is through professional services firms carrying out effective customer due diligence.

**Future UK government consultations**

As mentioned above, a second consultation is due to be published by the UK government on how to

implement a register for overseas companies owning land in England and Wales. It is likely that new legislation would be required because it would relate to companies that are not covered by the Companies Act 2006. It is worth keeping an eye on developments in this area as there may be a direct effect upon transactional property legal practice.

For example, if all existing overseas companies owning property in the UK are required to register beneficial ownership information with a central registry and provide a unique identifier to the Land Registry within a reasonable time, you should update any affected clients. Indeed, depending on the scope of your retainer, you may have an obligation to do so.

In addition, if there is a new requirement for your client to obtain a unique identifier before a property transaction can be registered, then this will need to be addressed at an early stage in order to avoid the consequences of delay. It may also become a matter to address when carrying out due diligence on purchase, ie checking that a property for sale by an overseas company is not subject to a sanction, such as a charging order or suspension of the identifier number. It remains to be seen, however, how the system will be designed in practice. ■