

Register of overseas entities: considerations for lenders

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A practice note on the key considerations for lenders, and in finance transactions generally, as a result of the establishment of the register of overseas entities.

The register of overseas entities was established under the Economic Crime (Transparency and Enforcement) Act 2022. The Act provides for the creation and maintenance of the register and contains requirements for overseas entities owning UK property to apply for registration and provide information about their beneficial owners.

Scope of this note

The *Economic Crime (Transparency and Enforcement) Act 2022* (ECA 2022) provides for the establishment of the long-awaited register of beneficial ownership of overseas owners of UK property (the Register). Under the ECA 2022, overseas entities owning or wishing to acquire certain UK property interests must apply for registration on the Register. The aim of the Register is to improve the transparency of foreign ownership of UK property and to tackle economic crime, and the ECA 2022 uses a mixture of land registration requirements and criminal sanctions to ensure compliance with its provisions.

Most of the provisions of Part 1 of the ECA 2022 relating to registration of overseas entities and creation of the Register came into force on 1 August 2022. However, the majority of the provisions in the ECA 2022 relating to land ownership and transactions (including *Schedule 3* to the ECA 2022) will be brought into force on 5 September 2022.

The introduction of the Register may have an impact on certain finance transactions involving an overseas entity owning UK property of which lenders should be aware. This note looks at the key issues for lenders to consider in relation to the Register and the requirements of the ECA 2022.

Some regulations are still to be made under the ECA 2022 and the Land Registry and Companies House are expected to publish guidance on this topic. The issues to consider may therefore evolve as further information is issued, and market practice develops.

For more information on:

- The Register, see *Practice note, Register of overseas entities: overview*.
- The effect of the ECA 2022 on land ownership and transactions, see *Practice note, Economic Crime (Transparency and Enforcement) Act 2022: property implications*.
- The criminal offences for non-compliance with the ECA 2022, see *Practice note, Registration of overseas entities under Economic Crime (Transparency and Enforcement) Act 2022: criminal offences for non-compliance*.

Register of overseas entities – key points to note

Companies House launched the Register on 1 August 2022. The Register will contain details of all overseas entities, and their beneficial owners, who own or wish to acquire a "qualifying estate" in UK land. The threshold for disclosure of beneficial ownership is closely based on the "persons with significant control" (PSC) regime for UK companies (for more information, see *Practice note, Register of overseas entities: overview: Identifying and obtaining information in relation to registrable beneficial owners of an overseas entity*).

The definition of "overseas entity" is widely drafted to include any legal entity (being a body corporate, partnership or other entity that is a legal person under its governing law) that is governed by the law of a country or territory outside the United Kingdom (*section 2(1), ECA 2022*) (see *Practice note, Register of overseas entities: overview: What is an overseas entity?*).

A "qualifying estate" is freehold property or a leasehold interest granted for a term of more than seven years (see *Practice note, Economic Crime (Transparency and Enforcement) Act 2022: property implications: Qualifying estate (land within registration requirement)*).

The key points to note in relation to the Register and the requirements of the ECA 2022 include the following:

- **Overseas entities must apply for registration**

Overseas entities who already own (and were registered as proprietor at the Land Registry further to an application made on or after 1 January 1999) or who wish to acquire a qualifying estate must identify their beneficial owners and apply for registration on the Register.

Note that an overseas entity that became a registered proprietor of a qualifying estate further to an application to the Land Registry on or after 1 January 1999 but before 1 August 2022 (the commencement date for the purposes of the ECA 2022) must identify its beneficial owners and apply for registration on the Register before 31 January 2023 (the end of the transitional period for the purposes of the ECA 2022).

For more information, see *Practice note, Register of overseas entities: overview: Which overseas entities must apply for registration on the Register?*.

- **Information required for relevant dispositions made on or after 28 February 2022 up to and including 31 January 2023**

Overseas entities are required to provide certain information to Companies House in relation to relevant dispositions of land made on or after 28 February 2022 and up to and including 31 January 2023 (the end of the transitional period) (*sections 41 and 42, ECA 2022*).

For more information, see *Practice note, Register of overseas entities: overview: Applications made during the transitional period: information about dispositions since 28 February 2022*.

- **Overseas entity ID**

Once registered, overseas entities will be allocated an overseas entity ID to evidence compliance with the new regime (see *Practice note, Register of overseas entities: overview: Registration and allocation of overseas entity ID*).

- **Updating requirement**

Registered overseas entities will also be required to update the Register (at least) annually (see *Practice note, Register of overseas entities: overview: Obligation to keep information updated*). Failure to keep the Register updated is an

offence, punishable by a daily fine of up to £2,500 (see *Practice note, Register of overseas entities: overview: Failure to comply with updating duty*).

Implications of the ECA 2022 regime for registration at the Land Registry

The provisions of the *ECA 2022* relating to land ownership and transactions are due to come into force on 5 September 2022. These provisions insert a new *schedule 4A* into the *Land Registration Act 2002* (LRA 2002) and, in summary, provide the following:

Overseas entity must be registered or exempt to acquire a qualifying estate

An overseas entity cannot apply to be registered as the registered proprietor of a qualifying estate at the Land Registry unless, at the time of application, the entity is either a registered overseas entity or an exempt overseas entity (*paragraph 2, Schedule 4A, LRA 2002*). For further information, see *Practice note, Economic Crime (Transparency and Enforcement) Act 2022: property implications: Acquisition of a qualifying estate by overseas entity (paragraph 2)*.

Land Registry must enter a restriction on title to each qualifying estate owned by an overseas entity

The Land Registry must enter a restriction on the title to a qualifying estate if an overseas entity is registered as its proprietor at the Land Registry further to an application made on or after 1 January 1999.

The restriction must prohibit the registration of any registrable disposition of the qualifying estate unless (subject to certain specified exceptions) the entity is a registered overseas entity or an exempt overseas entity at the time of the disposition (*paragraph 3, Schedule 4A, LRA 2002*).

Note that under transitional provisions, any such restriction in respect of qualifying estates acquired before 1 August 2022 will not take effect until after 31 January 2023 (see *Practice note, Register of overseas entities: overview: Overseas entities holding UK property acquired before 1 August 2022: transitional period*).

The Land Registry has published the form of the restrictions it must enter on the Land Register, and has detailed the evidence required to comply with those restrictions. For more information, see *Legal update, Register of Overseas Entities: Land Registry direction given under section 100(4) of the Land Registration Act 2002*.

Overseas entity cannot dispose of a qualifying estate without becoming registered proprietor

The ECA 2022 also stops an overseas entity avoiding the ECA 2022 regime by disposing of a qualifying estate without itself becoming the registered proprietor (*paragraph 4, Schedule 4A, LRA 2002*). For more information, see *Practice note, Economic Crime (Transparency and Enforcement) Act 2022: property implications: Registrable disposition by overseas entity entitled to be registered as a proprietor of a qualifying estate, but not registered (paragraph 4)*.

Effect of the ECA 2022 on a security interest over land

Restriction on title prevents registration of certain dispositions

The restriction entered by the Land Registry on the title to a qualifying estate owned by an overseas entity will prevent registration of a disposition of that estate unless (subject to certain specified exceptions (see *Specified exceptions to prohibition on registration of dispositions*)) the entity is a registered overseas entity or an exempt overseas entity.

This restriction will prevent any transfer, creation of a lease (for more than seven years) or creation of a *legal charge* in respect of the relevant property interest.

For more information on dispositions that will be prevented by such a restriction, see *Practice note, Economic Crime (Transparency and Enforcement) Act 2022: property implications: Dispositions prohibited by paragraph 3 restriction*.

Restriction prevents creation of a legal charge

It is important to note that the terms of the restriction entered by the Land Registry (see *Restriction on title prevents registration of certain dispositions*) will not prevent the creation of all types of security over a qualifying estate. The restriction only prevents the creation of a legal charge over a qualifying estate, (*section 27(2)(f), LRA 2002*). This is because the restriction prevents registration of the legal charge and until registration it will take effect only as an equitable mortgage.

So, even if a chargor is an overseas entity which is not registered or exempt (and none of the other specified exceptions (see *Specified exceptions to prohibition on registration of dispositions*) apply), a lender may still be able to take another type of security which does not require registration (such as an equitable charge) over a particular qualifying estate. However, a security interest over land short of a registered legal charge is a less desirable type of security for a lender to take and may well not provide a lender with the security it requires for the relevant financing. For more information on types of security that can be taken over land, see *Practice note, Taking security over freehold and leasehold property*.

Key concerns for lenders

Lenders with existing security over UK property owned by overseas entities and lenders looking to take security over UK property owned by overseas entities will be concerned about the impact of the requirements of the *ECA 2022* on the value of their security interests. Their concerns are likely to centre on the following issues:

- Whether the overseas entity concerned is a registered overseas entity or an exempt overseas entity.

If the overseas entity is neither, then a lender will only be able to take a legal charge or enforce its security if one of the specified exceptions applies (see *Specified exceptions to prohibition on registration of dispositions*).

- Whether security can be taken over a qualifying estate owned by an overseas entity in light of the prohibition on registration of relevant dispositions.

This will be an issue if taking the security interest involves registration of a relevant disposition and no specified exceptions apply. However, the prohibition will not apply if the overseas entity is a registered overseas entity or an exempt overseas entity.

- Whether security (pre-existing or to be taken) over a qualifying estate owned by an overseas entity can be enforced in light of the prohibition on registration of relevant dispositions.

This will be an issue if enforcing the security involves registration of a relevant disposition and no specified exceptions apply. Again, the prohibition will not apply if the overseas entity is a registered overseas entity or an exempt overseas entity.

Specified exceptions to prohibition on registration of dispositions

The following dispositions are specified exceptions to the prohibition on registration of certain dispositions and will not be prevented by the restriction entered by the Land Registry:

- A disposition made pursuant to a contract (which includes a document creating a charge) made before the restriction is entered in the register.
- A disposition made in exercise of a power of sale or leasing conferred on a registered charge-holder (or receiver appointed by such charge-holder).
- A disposition made by a specified insolvency practitioner in certain circumstances (which circumstances are expected to include a sale by a receiver or overseas insolvency practitioner but this will be set out in secondary legislation which has yet to be published).
- A disposition made further to a statutory obligation or court order, or occurring by operation of law.
- A disposition for which the Secretary of State has given consent.

(Schedule 3, paragraph 3, ECA 2022, inserting Schedule 4A (paragraph 3(2)), LRA 2002.)

For more information on these exceptions, see *Practice note, Economic Crime (Transparency and Enforcement) Act 2022: property implications: Dispositions prohibited by paragraph 3 restriction.*

So, from a lender's perspective, the restriction will not operate to prevent either of the following if one of the specified exceptions applies:

- Creation of a legal charge over relevant qualifying property interests.
- Enforcement of security over relevant qualifying property interests.

Practical implications for loan transactions

As a starting point, it is worth noting that the Register is only relevant for finance transactions involving qualifying UK real estate interests, more particularly those owned by an overseas corporate entity and where security is taken over those property interests.

Unsecured finance transactions, or those involving security over qualifying property interests but without a cross-border angle (in other words, where the group members or property owners are all UK individuals or corporate entities), are unlikely to be caught by the new regime.

However, even in an unsecured finance transaction or one involving security without a cross-border angle, the Register could still be relevant, for example, in an investment property transaction where registrable leases are granted or assigned to overseas entities (see *Investment property transactions where registrable leases are granted or assigned to overseas entities*).

Existing finance arrangements

In terms of existing loan relationships put in place before the ECA 2022 came into force (that is, before 1 August 2022), the key questions for a lender to consider are as follows:

- What happens if an obligor fails to comply with the new regime (that is, it does not become a registered overseas entity and is not an exempt overseas entity or does not comply with its updating obligations in relation to registration)?
- What issues arise if a lender takes new security over a qualifying estate?

Failure to comply with the new regime under existing finance arrangements

If an obligor fails to become a registered overseas entity and is not an exempt overseas entity, or does not comply with its updating obligations in relation to registration, a lender will need to consider whether the restriction on title will prevent it enforcing its security. In this scenario, if enforcing its security involves registration of a relevant disposition, a lender will need to determine to what extent it can rely on the specified exceptions referred to above (see *Specified exceptions to prohibition on registration of dispositions*) to ensure that it is able to enforce its security.

Note though, that as the qualifying estate will have been acquired before 1 August 2022, the restriction will only take effect after 31 January 2023 (see *Implications of the ECA 2022 regime for registration at the Land Registry*).

Practically speaking, lenders may (if resources allow) want to conduct an audit of their existing security arrangements to identify any security interests granted by an overseas entity over a qualifying estate.

In an ideal scenario, an overseas entity will comply promptly with the requirements of the Register (and become a registered overseas entity or is an exempt overseas entity) without lenders having to chase them to ensure compliance. However, it would be prudent for lenders to get in touch with any relevant overseas entities identified once they have completed their audit to request evidence of compliance. Lenders may be able to point to a further assurance type undertaking in existing loan documentation (for an example of such a clause, see *Standard document, Debenture: clause 21*) to encourage overseas entities to comply with the requirements of the ECA 2022.

Even without undertaking any such diligence, lenders will most likely be able to rely on the exception for existing contracts which precede any restriction being entered (see *Specified exceptions to prohibition on registration of dispositions*). Under that exception, lenders will be able to enforce security interests over relevant property interests owned by an overseas entity even if that entity is not a registered overseas entity (and cannot demonstrate that it is an exempt overseas entity).

New security is granted under existing finance arrangements

It is not unusual for new security interests to be granted under existing finance arrangements. Triggers for this might include any of the following:

- The acquisition of a new subsidiary which accedes as an additional obligor.
- An obligor accession exercise that is prompted by a subsidiary becoming a material subsidiary under a guarantor coverage covenant.
- The acquisition of new assets which need to be brought within the security net under the terms of the finance documents. Note that an overseas entity will not be able to acquire a qualified estate unless it is a registered overseas entity or an exempt overseas entity (see *Overseas entity must be registered or exempt to acquire a qualifying estate*).

If such a new security interest is taken after the Land Registry has entered a restriction on the relevant title, then a lender may not be able to take that security if the chargor is not a registered overseas entity or an exempt overseas entity. Also, a

lender may not be able to rely on the exception for existing contracts which precede any restriction (see *Specified exceptions to prohibition on registration of dispositions*). Conceivably, a lender might point to a condition subsequent or similar obligation under an existing loan document which pre-dates the restriction and imposes an obligation to grant the relevant security interest. However, there is no guarantee that the Land Registry will accept this when the lender seeks to register its security interest at the Land Registry especially if the security instrument itself post-dates the restriction.

Note again though, that if the qualifying estate the subject of the security interest was acquired before 1 August 2022, the restriction will only take effect after 31 January 2023 (see *Implications of the ECA 2022 regime for registration at the Land Registry*).

So, if the restriction on title has taken effect, and none of the specified exceptions apply, in this situation a lender will only be able to take a legal charge if the chargor is a registered overseas entity or an exempt overseas entity. Lenders should look to rely on any appropriate "further assurance" type undertakings in existing loan documentation to request that the property owner complies with the relevant registration or updating requirements under the ECA 2002. Ensuring that the property owner complies with these requirements should mean that the lender can take the security it wishes to take and should also avoid any difficulties associated with enforcing that security interest in future.

A lender may also face problems enforcing any such new security. If the relevant property owner fails to comply with the registration requirements, and the lender takes security over the qualifying estate anyway (note it cannot take a legal charge in this scenario), the lender may then face issues when it tries to enforce that security. A lender may be able to rely on one of the specified exceptions (see *Specified exceptions to prohibition on registration of dispositions*) in the event it tries to transfer the property pursuant to a security enforcement exercise. This does however pre-suppose that any lender seeking to enforce such security interest does so in the manner contemplated by the legislation. In many cases, lenders that enforce security will typically do so by appointing a receiver or an insolvency practitioner rather than by exercising any power of sale. As noted above (see *Specified exceptions to prohibition on registration of dispositions*), we await secondary legislation to understand how the insolvency practitioner exception will operate where security is enforced by a specified insolvency practitioner. Once known, lenders will need to ensure they are exercising their enforcement powers in accordance with the relevant legislation to benefit from this exception.

New finance arrangements

For new finance transactions that are put in place after the Register is established (that is, on or after 1 August 2022), the key questions for a lender to consider are as follows:

- What additional information (if any) should be sought from overseas property owners in respect of qualifying real estate interests?
- Should any additional representations or undertakings be sought as regards ongoing compliance with the requirements of the ECA 2022?

Condition precedent matters relating to the Register

On any new financing where security is granted over a relevant UK property interest owned by an overseas entity, a lender should undertake due diligence to ensure that the overseas property owner is registered on the Register (or is an exempt overseas entity) and has complied with its updating obligations if necessary.

As a condition precedent to drawdown, or accession to the finance documents by the relevant entity, a lender may request that the relevant overseas entity provides its overseas entity ID (see *Register of overseas entities – key points to note*) or provides evidence that it is an exempt overseas entity.

Failure to provide such information could impede both creation of security over the relevant property interest and also the transfer of that property interest on any subsequent enforcement of the security interest. A lender will prefer that a security provider is a registered overseas entity (or an exempt overseas entity) rather than having to rely upon one of the other specified exceptions mentioned above (see *Specified exceptions to prohibition on registration of dispositions*).

Additional representations and undertakings relating to the Register

We do not consider that it is essential for additional representations or undertakings to be included in facility agreements dealing with the requirements imposed by the ECA 2022. This is because compliance by obligors with the ECA 2022 will generally fall within the scope of a typical "compliance with laws" undertaking (see *Practice note, Finance documents: covenants: Compliance with law*), or potentially through representations which confirm compliance with any applicable laws.

Even where a lender is comfortable that an overseas entity has complied with the requirements of the ECA 2022 at the start of a new financing, it may wish to include an undertaking that the relevant entity will continue to comply with the annual updating requirements (in *section 7, ECA 2022*) throughout the life of the relevant facility. Where an overseas entity fails to comply with the updating requirements it will not be treated as a registered overseas entity until it remedies the failure. Consequently, if the lender needs to transfer a qualifying estate to enforce its security, it will have to rely on one of the other specified exceptions to do so. For more information on the updating requirements, see *Practice note, Register of overseas entities: overview: Obligation to keep information updated*.

Where a lender has particular concerns it may wish to include a specific undertaking to comply with the registration requirements under the ECA 2022 within a prescribed period. This might apply, for example, on a real estate finance transaction secured by UK property interests owned by overseas entities which have failed to comply with the requirements of the ECA 2022, and where the restrictions on the titles of those property interests have taken effect. In addition, in this scenario, a lender may also want to remove any grace periods or other material adverse effect-type qualifications from any events of default relating to compliance by group members with the requirements of the ECA 2022.

Other relevant considerations in finance transactions

Investment property transactions where registrable leases are granted or assigned to overseas entities

It is possible that a real estate financing may be put in place in respect of an investment property owned by a UK company, with security being taken over that property interest. On its face, there should be no immediate red flags arising from any such transaction so far as the *ECA 2022* is concerned.

However, the provisions of the ECA 2022 could become relevant in the following cases:

- The property owner may seek to grant a new registrable lease out of that property interest to an overseas entity.
- Alternatively, if the relevant property is already let to an existing UK tenant under an existing lease, that lease could be assigned to a new tenant that is an overseas entity.

In both cases, a lender may wish to specify that registrable leases (that is, those with a term of seven years or more) are only granted or assigned to an overseas entity that has provided its overseas entity ID and complied with the requirements of the ECA 2022 (or can demonstrate that it is exempt). Failure to do so could mean that the restriction that will be placed against the relevant leasehold title which is assigned or granted to such overseas entity could prevent enforcement of the lender's

security (if, for example, that security extends to an assignment by the freehold owner of its rights under any such leasehold interest) unless the lender can rely on one of the specific exceptions discussed above (see *Specified exceptions to prohibition on registration of dispositions*). Once again, the lender may also wish to include a specific undertaking which requires the relevant overseas entity to comply on an ongoing basis with the annual updating requirements as set out under the ECA 2022.

Discharging security over property interests owned by overseas entities

Issues may also arise for lenders where a loan that is secured against a qualifying interest owned by an overseas entity is repaid, but the overseas entity has failed to comply with the requirements of the ECA 2022. In that case, a lender would be prevented from re-conveying the relevant property interest to that overseas entity if a restriction has been placed on the title since the security was taken.

To address any such concerns when security is granted over a qualifying interest, a lender may look to qualify any covenant to release its security interest over any such property interest in the underlying security document so that its obligation to release the security only applies once the overseas entity is registered on the Register (or can demonstrate that it is exempt).

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