

IMPLICATIONS FOR SECURED LENDERS OF THE ECONOMIC CRIME (TRANSPARENCY AND ENFORCEMENT) ACT 2022

The Economic Crime (Transparency and Enforcement) Act 2022 introduces a new registration regime for overseas entities. Overseas entities which own or acquire UK real estate will need to register on a Register of Overseas Entities at Companies House, disclose their beneficial owners and keep their registration up-to-date. Failure to comply with the new regime carries consequences, including restrictions on the ability of an overseas entity to deal with its UK real estate, which could affect transactions involving, and security over, such real estate. In this briefing note, we consider the implications of the Act for secured lenders.

NEW REGISTRATION REGIME FOR OVERSEAS ENTITIES

The new registration regime introduced by the Economic Crime (Transparency and Enforcement) Act 2022 (the "**ECTEA**") is informed by the People with Significant Control regime which applies to English entities. However, while the disclosure rules of both regimes are very similar, the consequences for non-compliance are very different. In addition to fines and possible criminal liability, there will be restrictions imposed by the Land Registry on the ability of the "Overseas Entity" (see **Box 1**) to deal with its "qualifying estate" (see **Box 2**). The Register of Overseas Entities (the "**ROE**") opens on 1 August 2022 and accompanying Companies House provisions relating to the new register come into force on that date.

Overseas Entities who are existing owners of a qualifying estate or are acquiring a qualifying estate must register on the ROE and disclose their beneficial owners. For existing owners, the ECTEA provides for a six-month transitional period beginning with the day on which the Companies House registration rules enter into force (the "**Transitional Period**"). These existing owners must be registered on the ROE by the end of the Transitional Period (failure to do so is a criminal offence). The Transitional Period does not apply

Key takeaways for lenders

- An Overseas Entity should have an up-to-date registration on the ROE **before** it grants security over UK real estate.
- The ROE registration process should be initiated as soon as possible to mitigate any effect on the transaction timetable.
- Failure to register on the ROE may attract criminal liability and affect the ability to transfer the UK real estate and realise security over it.
- Specific documentary provisions in respect of the ECTEA may be desirable e.g. a condition precedent requiring evidence of registration on the ROE.
- Split commencement date: the Companies House provisions are in force and the Register of Overseas Entities opens from 1 August 2022, whereas the Land Registry provisions will be in force from 5 September 2022. The Transitional Period will run up to and including 31 January 2023.

to Overseas Entities which acquire a qualifying estate after the new rules come into force. These Overseas Entities will need to ensure that they are registered on the ROE prior to acquiring a qualifying estate. The ECTEA allows for regulations to specify classes of Overseas Entities which will be exempt from registration, however no such exemptions have been specified and the Government has indicated it does not intend to introduce any exemptions in the near future.

If an Overseas Entity has disposed of a qualifying estate between 28 February 2022 and the end of the Transitional Period, it is still required, before the end of the Transitional Period, to provide details to Companies House of its beneficial ownership as it was immediately prior to the disposition.

Overseas Entities must update their registration on the ROE at least annually. Failure to update is a criminal offence and the ECTEA also provides that the Overseas Entity is treated as unregistered for the purposes of the new Land Registry rules, which could have consequences for transactions e.g. if an Overseas Entity is granting a mortgage, the Land Registry restriction will apply (see below).

[See our other briefing note](#) for further details on the new registration rules at Companies House and the implications for borrowers.

NEW LAND REGISTRY RULES

The ECTEA makes changes to the land registration rules across the UK. This briefing only considers the changes made to the land registration regime in England and Wales. Different rules apply in Scotland and Northern Ireland.

The Land Registration Act 2002 is amended to include new provisions which deal with the ownership of registered land by Overseas Entities and registrable dispositions by them. These new provisions will come into force on 5 September 2022.

Every qualifying estate owned by an Overseas Entity will be subject to a restriction prohibiting the registration of the following dispositions at the Land Registry: (a) a transfer; (b) a grant of a charge by way of legal mortgage (a "**Legal Mortgage**"); and (c) a grant of a lease for more than seven years. For Overseas Entities who are existing owners of a qualifying estate, the restriction will apply to any applications made to register such dispositions made after the end of the Transitional Period.

The restriction is subject to exceptions (see **Box 3**). Where security is being taken over a qualifying estate, key exceptions will be the power of sale exception for holders of Legal Mortgages, the exception for Overseas Entities

Box 1 – "overseas entity"

- The ECTEA defines an "overseas entity" as a legal entity that is governed by the law of a country or territory outside the United Kingdom.
- "Legal entity" is defined as a body corporate, partnership or other entity that (in each case) is a legal person under the law by which it is governed.

Box 2 – "qualifying estate"

- The ECTEA defines a "qualifying estate" as: (a) a freehold estate in land, or (b) a leasehold estate in land granted for a term of more than seven years from the date of grant.

registered on the ROE, the exception for dispositions made in pursuance of a contract entered into before the restriction is entered in the register and the exception for insolvency practitioners, which we consider in more detail below. These exceptions should enable registration of security as a Legal Mortgage and enforcement.

A breach of the restriction on dispositions does not affect the validity of the disposition as between the parties. However, if the disposition is not registered at the Land Registry, there could be consequences for transactions e.g. a mortgage would not be a Legal Mortgage. It is also a criminal offence for an Overseas Entity to make a disposition prohibited by a restriction.

WHAT IS THE IMPACT OF THE ECTEA ON SECURITY OVER UK REAL ESTATE?

In general, the impact will vary depending on the type of security taken, the importance of real estate to the credit of the deal and the enforcement methods used.

Unless the Transitional Period applies, if an Overseas Entity does not have an up-to-date registration on the ROE (or is not exempt) at the time it grants a mortgage, the mortgage may not be registrable as a Legal Mortgage at the Land Registry as the restriction on dispositions will apply. In this situation, the mortgage would be an equitable mortgage and would not have priority over a subsequent Legal Mortgage.

This may have implications for enforcement as a Security Agent would not benefit from the power of sale exception to the restriction as it only applies to the holder of a Legal Mortgage. This would also be the case where a charge or equitable mortgage is taken over a qualifying estate (see below).

Even if the Overseas Entity subsequently registers on the ROE or updates its registration, this will not be an immediate "cure". This is because the exception to the restriction in respect of registered Overseas Entities only applies where the Overseas Entity was registered (or exempt) *at the time of the disposition* (i.e. the grant of the mortgage). In this situation, the Security Agent could consider requesting the grant of a supplemental mortgage (e.g. pursuant to a further assurance clause in the security document or facility agreement) once the Overseas Entity has completed or updated its ROE registration (as appropriate) which could be registered as a Legal Mortgage at the Land Registry.

Alternatively, the Security Agent could consider whether another exception would apply so as to allow registration of the mortgage as a Legal Mortgage

Box 3 – Exceptions to the restriction

- The relevant entity is a registered Overseas Entity, or is an exempt Overseas Entity, at the time of disposition. Note: there are currently no exempt Overseas Entities.
- The disposition is made in pursuance of a statutory obligation or court order, or occurs by operation of law.
- The disposition is made in pursuance of a contract made **before** the restriction is entered in the register.
- The disposition is made in the exercise of a power of sale or leasing conferred on the proprietor of a registered charge or a receiver appointed by such a proprietor.
- The disposition is made by a specified insolvency practitioner in specified circumstances (to be specified in future regulations). Note, as these regulations have yet to be published, the scope of this exception is currently unknown.

e.g. if the mortgage is granted as a condition precedent to a facility agreement which pre-dated the entry of the restriction, the exception in respect of pre-existing contracts may apply.

Before the end of the Transitional Period, a mortgage granted by an Overseas Entity which is an existing owner of a qualifying estate will be capable of registration as a Legal Mortgage even if the Overseas Entity was not registered on the ROE when it granted the mortgage. This reflects the fact that the restriction does not apply to such Overseas Entities until the end of the Transitional Period. However, the Land Registry has indicated that the application for registration must be made to it **before** the end of the Transitional Period.

WHAT DOES THIS MEAN FOR TRANSACTIONS?

Legacy transactions: for existing Legal Mortgages registered at the Land Registry, the power of sale exception will apply to enable their enforcement. This exception would apply even if the Overseas Entity is not registered on the ROE or its registration is not up-to-date.

For other types of real estate security such as charges and equitable mortgages, the restriction will affect their enforcement unless another exception applies (e.g. the insolvency practitioner exception, though the scope of this exception is currently unknown as the regulations for it have yet to be published). A further assurance clause may enable them to be "upgraded" to a Legal Mortgage for the purposes of enforcement. In the case of an equitable mortgage, the Security Agent could consider having it registered as a Legal Mortgage before the end of the Transitional Period, but this may depend on other factors, such as the commercial deal. If there is share security over the Overseas Entity, this may offer an alternative enforcement route.

Existing provisions in facility agreements may address registration on the ROE and the updating duty e.g. general representations, undertakings on authorisations and compliance with laws and conditions precedent requiring relevant authorisations. If a facility agreement is being amended and real estate is a key asset, consideration could be given to adding specific provisions addressing the new rules e.g. amending the further assurance clause to specifically reference a supplemental mortgage.

Ongoing and new transactions: fundamentally, ensuring that the Overseas Entity is registered on the ROE *before* it grants security over a qualifying estate is key as a mortgage would be registrable as a Legal Mortgage. It also avoids the Overseas Entity committing a criminal offence which could have regulatory, reputational and money laundering implications for lenders.

Financial penalties imposed on an Overseas Entity could be secured by a charge on the qualifying estate, which could also affect lenders.

Consideration should be given to specific documentary provisions. Where security is being taken over real estate or if real estate or rental income from leases of real estate held by Overseas Entities is a significant part of the group's business, evidence of registration on the ROE (or, if any exemptions are introduced, an exemption from ROE registration) should be a condition precedent to funding and to taking the security. This could be accompanied by an undertaking providing for ROE registration to be up-to-date at all times and for any Overseas Entity to register on the ROE before acquiring any qualifying estate. If a charge is being taken over real estate, a specific reference to a supplemental mortgage could be added to the further assurance clause to aid enforcement.

As part of the upfront due diligence, searches should be carried out at the ROE and the Land Registry. Registration on the ROE may need to be factored into the transaction timetable and more time may be required in the early stages as the new regime beds in.

NEXT STEPS

The Companies House registration regime comes into force on 1 August 2022 and the Transitional Period runs up to and including 31 January 2023. The split commencement date, with the new Land Registry rules not coming into force until 5 September 2022, provides some extra time for the Companies House regime to bed in, Overseas Entities to identify their beneficial owners and make their ROE registration applications and for lenders to become familiar with it. The ROE registration process should be initiated by borrowers as early as possible to mitigate any effect on the transaction timetable in the case of ongoing and new transactions and to ensure an Overseas Entity is registered before the end of the Transitional Period in the case of existing transactions. Lenders should also start to consider documentary provisions in respect of the new regime and be alert to developing market practice. Further regulations, as well as guidance on the new regime, are expected from Government and will hopefully provide some more colour on the regime.

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