International Capital Market Services Association

Technical Consultation on the Transposition of 5MLD
Assets & Residence Policy Team
HM Revenue & Customs
Room 3C/03
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Date: 14th February 2020

Dear Sirs,

HM TREASURY TECHNICAL CONSULTATION ON THE FIFTH MONEY LAUNDERING DIRECTIVE AND TRUST REGISTRATION SERVICE

Introduction

We welcome the opportunity to provide the views of the Trustee sub-committee of the International Capital Market Services Association on the technical consultation document published on 24 January 2020 in connection with the Fifth Money Laundering Directive ("**5MLD**") and Trust Registration Service (the "**consultation document**").

We refer you to our letter (**attached**) dated 7th June 2019 in connection with HM Treasury's consultation in respect of 5MLD in which we set out, among other things, our views on the transposition of 5MLD into English law.

Below you will find our responses in respect of questions one, two and three in the consultation document. We have also set out for your consideration at the end of this letter our views on an apparent inconsistency which our members perceive in the treatment of those trusts of which, for the purposes of Regulation 44(1) trustees must keep a written record containing certain information required by Regulation 45 and those trusts which would be excluded from the registration obligation arising under Regulation 45 by virtue of the exclusions referred to below.

In this letter where we refer to a Regulation this is a Regulation under The Money Laundering and Terrorist Financing (Amendment) Regulations 2019 ("**MLR**").

Should it be helpful for representatives of the Trustee sub-committee to meet with you to discuss our responses further or to address any questions you may have, we would be happy to arrange a meeting.

Questions: Who is required to register

Question 1 – Are there other express trusts that should be out of scope? Please provide examples and evidence of why they meet the criteria of being low risk for money laundering and terrorist financing purposes or supervised elsewhere.

Question 2 – Do the proposed definitions and descriptions give enough clarity on those trusts not required to register? What additional areas would you expect to see covered in guidance?

The view of our membership is that the trusts with which we are primarily concerned are captured in part in the exclusions set out in draft Regulation 45ZA(2)(f) and (g) insofar as the trust in question would fall within the definition of "type A trust". However, as we have sought to explain in more detail in the following paragraphs, we believe the drafting would benefit from some amendments which we consider are consistent with the Government's aim of ensuring only those trusts which are low risk for money laundering and terrorist financing purposes or supervised elsewhere should be excluded from the registration requirements which would apply otherwise.

In our view, similar exclusions to those set out in draft Regulation 45ZA(2)(f) and (g) should also be applied to type B trusts. As we seek to demonstrate, an illogical anomaly arises where a trustee, by virtue of being non-resident in the UK, but who nonetheless administers trusts whose assets and beneficial owners are, for all practical purposes the same or similar to those of a type A trust, is unable to avail itself of an exclusion that applies to the trustee of a UK trust.

Commentary on draft legislation

Regulation 45ZA(2)(f)

Under the current draft legislation, a trust is not a type A trust if it is:

> "*(f) a trust arising out of, or in connection with, a provision of a facilities agreement (or of a document ancillary to the facilities agreement) under which a credit facility is, or is to be, made available by an authorised person;*"

We are grateful to HMT for seeking to address concerns which we raised in our letter of 7th June 2019 regarding what we characterised as trusts arising in connection with secured lending transactions. These are typically trusts which arise in connection with syndicated or bilateral facility agreements under which credit facilities are arranged or extended by various parties. In that regard we consider that few amendments would be required to the introductory wording in Regulation 45ZA(2)(f) and we have suggested some amendments which we hope would be easily recognisable as consistent with HMT's aims.

Our principal concern with the proposed drafting is the category of persons by or through whom credit facilities may be extended. The term authorised persons is defined in Regulation 3 as "any person authorised pursuant to FSMA", presumably with the intention that persons who are already subject to some degree of regulatory supervision will be captured. While we agree that the status of the lender is an important consideration in determining whether or not the transaction is one which ought to fall within the registration requirement, we are nonetheless concerned that the scope of the authorised person definition is too narrow and would exclude a great many transactions which are not entered into for any of the purposes which MLR seeks to prevent. We have sought to expand the category of persons extending credit and also to include a reference to the trustee itself where such persons fall within the scope of the terms already employed within MLR (Regulations 8, 10 and 12). Our other proposed amendments are intended to ensure that the language is sufficient to catch all relevant trusts that would arise in connection with agreements under which credit is extended (for example, a security trust may be constituted under a separate intercreditor agreement or similar, separate, security document, rather than out of the facilities agreement

itself; or share trust and collection account trust arrangements that may arise in connection with structured finance warehouse facilities involving special purpose vehicles (SPVs) set up under a special UK taxation regime for securitisation companies). Our proposed amendments are set out below:

> "*(f) a trust arising out of, or in connection with* ***or which otherwise relates to****, an* ~~*provision of a facilities*~~ *agreement (or* ~~*of*~~ *a document ancillary to* ***or made in connection with an*** ~~*a facilities*~~ *agreement) under which****:***
>
> ***(i) a credit facility is, or is to be made available to a company which is taxed pursuant to the Taxation of Securitisation Companies Regulations 2006 (as amended); or***
>
> *(ii) a credit facility is, or is to be*~~*,*~~ *made available by* ***or has been arranged by or where the trustee is****:*
>
> ***(1) one or more relevant supervised persons;***
>
> *(*~~*2ii)*~~ *an* ***one or more*** *authorised person****s; or***
>
> ***(3) one or more persons authorised and subject to supervision by a supervisory authority of another country or territory***
>
> ***where:***
>
> ***"relevant supervised person" means a supervised person other than a third party to whom Regulation 39(4) applies; and***
>
> ***"supervised person" means a relevant person who is subject to these Regulations under Regulation 8 or a person referred to in Regulation 39(3)(b) or (c);***"

Our members consider that the above wording:

- is proportionate in that it focuses either on certain limited scenarios where the relevant type of borrower is a company falling within the special UK taxation regime for securitisation companies, or whether the lender, the arranger of the loan or the trustee are subject to anti-money laundering/terrorist financing supervision (for example those UK lenders that are not authorised persons but are financial institutions registered with HMRC);

- removes an imbalance which might otherwise arise in respect of other EEA lenders or arrangers;

- allows UK trustees to provide services in relation to transactions arranged outside the UK / EEA so long as the lenders or arrangers or the trustee themselves are relevant supervised persons or authorised persons; and

- allows trustees to place reliance on the arranger being a relevant supervised person or authorised person.

Regulation 45ZA(2)(g)

Under the current draft legislation, a trust is not a type A trust if it is:

"*(g) a trust arising out of, or in connection with, a provision of a subscription agreement (or of a document ancillary to the subscription agreement) under which bonds are, or are to be, issued, to—*

(i) an authorised person;

(ii) subscribers procured by an authorised person; or

(iii) a subscriber through a central securities depositary which is authorised under Article 16 of the CSDR or which has made an application for authorisation pursuant to Article 17 of the CSDR that has not been determined."

We are grateful to HMT for seeking to address concerns which we raised in our letter of 7th June 2019 regarding what we characterised as bond trusts. The term "bond trusts" as used in our previous correspondence is a shorthand term for a broader category of instruments and securities which is perhaps better described in the terms used in Regulation 32(2) of MLR and which reference instruments which fall within article 77 or 77A of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 and securities which fall within article 78 of that Order. We would request that an amendment is made to the wording in limb (g) such that it reads as follows:

*(g) a trust arising out of, or in connection with, or ancillary to, instruments or securities of the type specified in Regulation 32(2) ("**specified instruments**") issued or to be issued under an arrangement: ~~a provision of a subscription agreement (or of a document ancillary to the subscription agreement) under which bonds are, or are to be, issued, to—~~*

The wording used currently references trusts which arise "*out of or in connection with a provision of a subscription agreement*". Legally we consider this description may not operate as we believe you intended as the relevant trusts will not arise out of or in connection with the subscription agreement. Instead, some of the trusts will arise out of or in connection with the debt instrument or security which evidences the debt itself (for example a bond trust will arise under the bond trust deed, any security trust will arise under a deed creating security) and on certain transactions (in particular UK securitisations), various other types of trust arrangements will arise under other transaction documentation (we refer you to Appendix 1 at the end of this letter for illustrative examples and further background details on the latter). Our proposed amendment seeks to address this point while at the same time expanding the description of the instruments covered to those which are already in contemplation under the Regulation. As a general point, we think it is appropriate for HMT to consider that any exemption that seeks to exclude bond/security trusts that arise in connection with certain capital market transactions, should be wide enough to exclude other related or ancillary trust arrangements in that same transaction, given that such other trusts would not be created for any purpose other than to make the transaction structure work. Therefore, different trusts that may arise in connection with the capital market transaction in scope of the exemption should be analysed as a single arrangement and the relevant exemption ought to be drafted with this in mind. As noted above, our suggested amendments seek to address this.

We request that the list of entities by and/or to whom the securities or instruments are issued or will be issued is further amended, that a separate limb is added to accommodate capital market transactions that are listed on the relevant trading venues and we separately invite you to consider to take out of scope secured debt issues that fall within the "capital markets exception". Our proposed amendments are as follows:

"(i) that is, or is to be, listed and/or admitted to trading on a "regulated market" as defined in Regulation 3[1]; or

(ii) where the specified instruments are, or are to be, issued to or subscribers for the specified instruments are procured by an authorised person; or

(iii) where the specified instruments are, or are to be, issued to a "credit institution" or a "financial institution" as defined in Regulation 10; or

(iv) to which the capital market exception under section 72B of the Insolvency Act 1986 (as amended) applies; or

(v) where the trustee is a relevant supervised person or an authorised person; or

(vi) where the specified instruments are, or are to be, issued to subscribers through a central securities depositary or clearing and settlement system recognised by any central bank or monetary authority member of the Bank for International Settlements*; or*

(vii) where the specified instruments are to be issued by or borrowed by a company which is taxed pursuant to the Taxation of Securitisation Companies Regulations 2006 (as amended).

HMRC has the power to issue guidance about the meaning and application of the exemptions for the purposes of this Regulation 45ZA."

As you can see, in our suggested amendments we are seeking to use terminology consistent with the spirit and purpose of 5MLD and MLR or otherwise refer to other existing concepts in UK insolvency law and tax regulation that are also consistent with the spirit and purpose of 5MLD and MLR.

For example, the "regulated market" limb (i) was added to reflect that many capital market transactions, which we believe HMT intends to bring out of scope, will be listed/admitted to trading on the relevant markets, as defined in MLR, that are subject to sufficient scrutiny and disclosures.

The "credit institution"/"financial institution" limb (iii) seeks to reflect the commercial reality that capital market transactions, which we believe HMT intends to bring out of scope, will be more commonly placed with the institutional investors that are caught under these definitions, rather than with FSMA-authorised persons only.

The "capital market exception" in limb (iv) seeks to incorporate a carve out which is already envisaged by the Insolvency Act 1986 in respect of transactions having equivalent scope to those for which our members frequently act as trustee.

[1] Regulation 3:
"**regulated market**" – (a) within the EEA, has the meaning give by Article 4.1(21) of the market in financial instruments directive; and
(b) outside the EEA, means a regulated financial market which subjects companies whose securities are admitted to trading to disclosure obligations which are equivalent to the specified disclosure obligations.

With respect to the proposed limb (vi) above, our members are concerned that the exclusion proposed in the draft legislation does not capture sufficiently the securities depositaries and clearing and settlement systems through which many of the transactions they administer routinely clear. The wording used by HMT would, for example currently include Euroclear and Clearstream, two of the most commonly used CSDs for international debt instruments. However, the current wording would exclude The Depository Trust Company in the US which is a CSD through which thousands of debt instruments administered by our members commonly clear and which is under the supervision of the Board of Governors of the Federal Reserve System. In addition but of equal concern to our members is the fact that the current legislative references will cease to apply in their current form at the end of the transition period and may result, for example, in both Euroclear and Clearstream no longer falling under the exclusion, which would significantly undermine the effect of the exclusion. We have sought instead to refer to those central securities depositaries or clearing and settlement systems which are recognised by the central banks and monetary authorities who are members of the Bank for International Settlements ("**BIS**") alongside the Bank of England. It is our belief that the ownership of BIS and its mission to ensure monetary and financial stability through international cooperation provide comfort that sufficient governance is assured (through the Committee on Payments and Market Infrastructures) of those central securities depositaries or clearing and settlement systems administered under its guidance.

Limb (vii) that refers to the Taxation of Securitisation Companies regime will ensure that the UK securitisation structures, which commonly involve multiple trust arrangements (as illustrated in Appendix 1 at the end of this letter) are properly accommodated so that it is specifically limited to a well-established special taxation regime.

In relation to the suggestion that guidance could be issued, our members believe that it would be helpful to include a placeholder for additional guidance to be provided to provide flexibility for any other exemptions that may prove necessary or desirable in the future (in particular in the light of the potential uncertainties that may arise at the end of the transition period in the Brexit process). We note the analogy with the 'people of significant control' (PCS) regime under the Companies Act 2006, where such guidance is contemplated within the legislation and has subsequently been issued.

The exclusions referenced above which are currently only applicable to type A trusts should also apply to type B trusts. As we have mentioned earlier in this letter, there are circumstances where it would be illogical for one of the exclusions referenced above not to be equally applicable in respect of a type B trust. To illustrate our concern, we refer to a trustee which operates through a UK body corporate and trustee which operates through a London branch of an overseas corporation (both common scenarios among our membership). Each trustee agrees to administer a trust arising in connection with a Bond which is issued by a UK financial institution whose terms are set out in a New York law governed indenture (equivalent to an English law governed trust deed).

The "trust" which is administered by the UK body corporate trustee is, according to the definitions set out in MLR, a type A trust, being a UK trust which is an express trust (the terms of the indenture are clear that a trust arrangement is intended). This trust, however, can be excluded from the registration requirements otherwise applicable to the type A Trust because it benefits from an exclusion (under Regulation 45ZA(2)(g), either in its existing form (assuming certain other characteristics) or more certainly in the proposed amended form).

If the same trust is administered by the London branch of an overseas corporation then it is a "non UK trust". If the trustee can be said to enter into a business relationship in the United Kingdom with a relevant person (which would be the case in the example given) then it would be a type B trust, but would not benefit from any exclusion and would therefore require registration, which our members consider illogical.

Deadlines, data retention and penalties for non-compliance

Question 3 – Do the proposed registration deadlines and penalty regime have any unintended consequences that would lead to unfair outcomes for specific groups?

In the event that our suggestions in respect the scope of the current exemptions are adopted we consider that the proposed registration deadlines and penalty regime would be proportionate and fair. However, as we have alluded to in our previous correspondence with HMT, to the extent that uncertainty as regards the reporting obligations for trustees of the types of arrangements discussed above is not removed through proportionate drafting, we have grave concerns as to the ability of our members to meet the deadlines for effective remediation of their "back-book" of existing transactions for which they act as trustee and the significant financial and administrative burden that this will place on our members in order to provide HMRC with information which we strongly contend is of no practical utility to HMRC or HMT in combatting money laundering and terrorist financing.

Commentary on the inconsistency arising between Regulation 44(1) and Regulation 45

As referenced earlier in our letter, our members are concerned that the absence of any amendment to Regulation 44(1) gives rise to an inconsistency regarding those trusts which MLR would require to be registered and those for which trustees would be required to keep a written record. Currently, Regulation 44(1) requires the trustee of a relevant trust (as defined in Regulation 42(2)(b)) to maintain accurate and up-to-date records in writing of all the beneficial owners of the trust, and of any potential beneficiaries referred to in paragraph (5)(b), containing the information required by Regulation 45(2)(b) to (d) and (5)(f) and (g).

Two anomalies arise in respect of this requirement:

1. Trusts which are otherwise considered to be out of scope of the registration requirement, because they are not of a type which HMT considers should be subject to such requirements and which it is agreed pose no threat of a type which the legislation seeks to prevent, must nonetheless be captured in a written record which must be made available to certain parties (which process involves the collection of information which is not made available to trustees in the normal course of transactions that we are concerned with (e.g. tax identification numbers)); and

2. The information which would be required to be recorded in respect of such trusts is more extensive than the information which would be required to be registered for either a type A trust or a type B trust which, in either case, do not benefit from an exclusion.

Our members contend that it is entirely consistent with the Government's aims that the exclusions which extend to type A trusts and type B trusts under Regulation 45ZA should be incorporated into Regulation 44(1) in the following manner:

> 44.—(1) The trustees of a relevant trust must maintain accurate and up-to-date records in writing of all the beneficial owners of the trust, and of any potential beneficiaries referred to in paragraph (5)(b), containing the information required by Regulation 45(2)(b) to (d) and (5)(f) and (g) **provided that such obligation of maintenance does not arise where the relevant trust falls outside the definition of either a type A trust or a type B trusts due to the operation of Regulation 45ZA(2) or Regulation 45ZA(3)**.

As mentioned in the introduction to this response, should it be helpful for representatives of the Trustee sub-committee to meet with you to discuss our responses further or to address any questions you may have, we would be happy to arrange a meeting.

Yours sincerely,

Jillian Hamblin

Chair, ICMSA Trustee sub-committee

APPENDIX 1
BACKGROUND AND EXAMPLES OF TRUST ARRANGEMENTS IN STRUCTURED FINANCE TRANSACTIONS

Trust arrangements are commonly employed in a number of different contexts in UK structured finance transactions, which are driven by structural considerations in general and, in some cases, by the criteria stipulated by the rating agencies assigning credit ratings to the bonds issued pursuant to such transactions. The list below does not provide an exhaustive list of all possible trust arrangements, but highlights some of the most common ones. For example, in a typical UK securitisation, each transaction will have at least:

1. **bond trust**, whereby the SPV Issuer's covenant to pay under the bond terms and conditions is held on trust for the benefit of noteholders/investors with a corporate trust company performing the role of the Bond Trustee;
2. **Issuer security trust**, whereby the benefit of security created over the securitised assets and certain other rights under the transaction documents is held on trust for the benefit of noteholders/investors and certain other transaction parties, who are secured creditors, with a corporate trust company performing the role of the Security Trustee;
3. **share trust**, whereby the UK SPV Issuer is set up as a wholly owned subsidiary of an SPV holdings company whose one or two shares are held on trust for certain charitable and non-charitable class of beneficiaries, with the corporate services provider performing the role of the Share Trustee; in addition, when setting up a UK SPV Issuer and its holdings company, a series of (written) **trust arrangements for capitalisation monies** will also be put in place, with the corporate services provider acting as the relevant trustee;
4. **collection account trust**, whereby the originator declares a trust in favour of the SPV Issuer/Security Trustee over its interest in the collection account to the extent such interest is attributable to the securitised assets, which addresses the rating agency criteria requirements relating to the securitised assets isolation from the originator's insolvency and mitigation of commingling risk;
5. a series of **turnover trusts** will be provided for in the asset sale agreement and related servicing agreement dealing with monies received in connection with the securitised assets, or repurchased assets, to be held on trust where such monies cannot be immediately transferred to the relevant transaction party, such the SPV Issuer, the Security Trustee or the originator.

It should also be noted that certain types of structures would give rise to other trust arrangements, in addition to those that are typical for any UK securitisation, for example:

1. in *a UK true sale structure*, where the underlying contracts contain a prohibition on assignment, the asset transfer may be achieved instead via an **originator trust**, whereby the originator of the assets declares a trust over the securitised assets for the benefit of the SPV Issuer;
2. in a UK secured loan structure, in addition to the Issuer security trust, the security will also be created and held on trust at the Borrower level (**borrower security trust**), so that the Borrower Security Trustee (the role performed by a corporate trust company) will hold security granted by the Borrower on trust for the lender (i.e. the SPV Issuer); and
3. in a UK master trust programme structure, which is commonly employed for securitisation of UK credit card receivables and mixed portfolios of residential mortgages, the assets are sold to the **Receivables/Mortgages Trustee** who holds the securitised assets on trust for the benefit of the SPV funding entity and the seller.

International Capital Market Services Association

Consultation on the Transposition of 5MLD
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Date: 7th June 2019

Dear Sirs,

HM TREASURY CONSULTATION ON THE TRANSPOSITION OF THE FIFTH MONEY LAUNDERING DIRECTIVE

Introduction

We welcome the opportunity to provide the views of the Trustee sub-committee of the International Capital Market Services Association on the transposition of the Fifth Money Laundering Directive (5MLD) and HM Treasury's April 2019 consultation in respect thereof.

We refer you to our letter (**attached**) dated 10 November 2016 in connection with HM Treasury's consultation in respect of the Fourth Money Laundering Directive in which we set out, among other things, an explanation of how securities are held in International Capital Market transactions and a summary of structured finance and secured transactions in which trust structures are commonly employed.

Below you will find our responses in respect of the questions set out in Chapter 9 of the consultation.

Should it be helpful for representatives of the Trustee sub-committee to meet with you to discuss our responses further or to address any questions you may have, we would be happy to arrange a meeting.

Chapter 9: Trust registration service

64. ***Do respondents have views on the UK's proposed approach to the definition of express trusts? If so, please explain your view, with reference to the specific trust type. Please illustrate your answer with evidence, named examples and propose your preferred alternative approach if relevant.***

We have responded to this question in two parts. The view of our membership is that, in addition to considering the definition of express trusts, it is also necessary to clarify the definition which will be given under HM Treasury's implementation of 5MLD to "beneficial owners" in relation to which data is required to be held in the records of trustees and registered in the TRS.

EXPRESS TRUSTS

Scope

Our primary concern is that 5MLD requires ***all*** express trusts to be registered. There is no distinction drawn, for example, between those express trusts created before the regime comes into effect and those which will come into existence following implementation into UK law. As we explain more fully below, the absence of any language which seeks to restrict the obligation gives rise to an arguably unfeasible compliance burden and a significantly increased risk of criminal liability for trustees in respect of trusts which, as we will explain further below, ought not to be in scope of 5MLD in terms of meeting the objective of identifying money laundering and terrorist financing.

As HM Treasury observes in paragraph 9.14 of the consultation paper, the use of trusts is more widespread in the UK than in other EU jurisdictions and many arrangements that are essentially contractual in civil law jurisdictions would be categorised as trusts under English law. It follows that there is a risk that the registration requirement has inconsistent application across the EU and that the impact on the UK is disproportionate. We are aware, for example, that in the Netherlands the application of 5MLD is restricted to one type of trust like arrangement which is the most common structure (the mutual fund - "*fonds voor gemene rekening*"). We fully support and indeed consider it critical that, as set out in paragraph 9.14, the government explores how equivalent arrangements are treated in other EU Member States when clarifying the registration requirements to avoid such inconsistent application and the resulting compliance burden. A principled approach should be applied by the government to the trusts to be subject to Article 31, taking into account the fundamental purpose of 5MLD as well as proportionality. We consider that this should entail a tightly circumscribed definition of express trusts in the UK.

As we have sought to explain in our letter dated 10 November 2016 and our subsequent letters to HM Treasury dated 11 April 2018 and 18 December 2018, trusts are ubiquitous in English law governed commercial transactions, not least those bond and secured lending transactions of which our members act as trustee. The fact that many of these trusts are readily identifiable as such should not obscure the commercial reality that our members are not in the habit presently of systematically recording their commercial interests by reference to whether they employ a trust mechanism which might be within scope for the purposes of 5MLD's registration obligations. For our members to identify even the obvious express trusts, ***all*** their books of business will need to be examined for existing trusts. The scale of this task is enormous. Bond and security trusts can easily be numbered in the several hundreds of thousands, if not millions. Word search tools and AI enabled technology may be deployed to assist in this process, very likely at a significant cost. However, in addition, there remains the need then to systematise the information collection, determine the identity of beneficiaries (which may change frequently e.g. lenders in a syndicated secured loan transaction), and then record and register those details. In addition, the information may not be available to the trustee without enquiry of third parties. To use the example of a secured syndicated loan transaction, the security would be held by a security trustee on behalf of the lenders from time to time, but a facility agent, and not usually the security trustee, will be involved in recording any changes to the lenders, so the security trustee would need to seek that information from the facility agent. The enormity of this task should not be underestimated, requiring our members to resource entire teams for the sole purpose of collating documents and contacting third parties to extract or obtain the required information. We understand that the current TRS system will be enhanced with the registration requirements for registering all express trusts. The TRS registration system must be thoroughly tested and be robust to handle the anticipated

volumes to be managed through the portal, even more importantly due to the nature of the information required to be input.

Equally if not more troubling is that many trusts are not directly described as such in a trust deed. For example, as has been referenced in previous correspondence, many financing arrangements make use of a technique referred to as a "turnover trust". This is a contractual term by which a party who receives funds in circumstances not contemplated by the transactional terms agrees to hold those funds to the order of the party who is ultimately contractually entitled to them. Such provisions may or may not use the phrase "to hold on trust" but, whether or not such terms are used, English law will look to the substance of the arrangement and say that a trust has been created. Similar arrangements may exist in non-English law governed contractual arrangements without being characterised as a trust (and thereby escaping the requirement for registration under local implementation). The due diligence involved in identifying and reporting on trusts of this nature is, frankly, mind-boggling and since it may also be the case that these types of trusts never even come into operation (i.e. if funds are not received by any party in a manner not contemplated by the transactional terms), it is hard to see any purpose in registering them.

A similar "absence of utility" argument might be made in the context of both "bond trusts" and "security trusts". Typical bond trusts amount to little more than contractual undertakings, given to facilitate a financial arrangement. The most common example arises where a party makes a contractual promise to pay the trustee (our members) amounts which it is also obliged to pay to a third party (a bondholder). The trustee holds collateral promise to pay on trust for the "class" of bondholders, who in turn agree with both the covenantor and the trustee that only the trustee will be entitled to bring suit against the covenantor in the event it fails to pay either the bondholders or the trustee. Such trusts have no underlying aim of concealing money laundering activity or terrorist financing. They are merely a way of conveniently "collecting" all causes of action in one representative body in the event of a payment failure. Such arrangements exist under non-English law governed contractual arrangements and are not characterised as "trusts".

In a typical "security trust" an asset which is intended to secure an obligation (typically a payment obligation) is secured in favour of a trustee (our members again). This is most often to avoid the administrative inconvenience or legal impossibility of dividing that asset and securing the divided parts for the benefit of individual creditors. In this context the "security trustee" is merely a representative of the creditors wishing to derive a benefit from the protection afforded by the secured asset. Had the security been granted directly in favour of the individual creditor no trust (and thus no registration obligation) would arise. As with bond trusts, there is no attempt in such arrangements to conceal money laundering activity or terrorist financing. These are entirely legitimate and essential aspects of domestic and cross-border lending and capital markets transactions which are employed globally. Such arrangements exist extensively in other European jurisdictions without being characterised as trust arrangements.

For these reasons we question the practicality of the scope of the proposals as presently contemplated. So onerous is the task, we question whether the proposals are fair, for example rendering past activities illegal if unreported when the ability to track these requires so much cost and effort?

Clarity of meaning of "express trust"

We certainly need clarity over the meaning (and preferably a more narrowly defined meaning) of express trusts. A trust such as an unsecured "bond trust", where there is no transfer of property beyond contractual promises would seem to us to fall very clearly outside of the scope of the "activities" which are envisaged by

5MLD and should, we would argue, be excluded from any definition. We would argue further that any trust which involves the creation of a security interest for the benefit of financial creditors ought, similarly, to be excluded from the scope of "express trusts" as a record of the beneficiaries of such trusts serves, in our view, no useful purpose for the interested parties.

Proportionality

Paragraph 9.6 of the consultation paper notes that the government recognises that the NRA concludes that UK trusts present a low risk of money laundering and terrorist financing and is keen to ensure that the registration process – and any associated penalty regime – is applied proportionately. Requiring all express trusts, both historic and new, to be registered with the associated burden described above is not proportionate.

Summary

For all these reasons, our members are very concerned by the scope and uncertainty issues pertaining to "express trusts". We would enjoin HM Treasury to make their definition under UK implementing legislation as clear as possible, giving particular regard to proportionality.

We would suggest that the proposals only extend to express trusts created after the new regime comes into force and that these be itemised so that it is clear what is included and that any which are not listed will not be part of the regime. Trusts should only be registered where information on them can assist in targeting money laundering and terrorist financing – it is difficult to envisage how this can be the case with the trusts listed above. Accordingly, "turnover trusts", "bond trusts" and "security trusts" should be excluded.

BENEFICIAL OWNERSHIP

When implementing the trust record-keeping requirement, we would ask HM Treasury to clarify that "beneficial owner" and the requirement for the registration of "beneficial ownership" only extends to a natural person in accordance with 5MLD (see the references to "natural persons" in the preamble to the definition and in paragraphs (a) and (b) of the definition of "beneficial owner", particularly in the context of paragraph (b) relating to trusts). The Money Laundering Regulations currently refer to "individuals" which does not track the reference to "natural persons" in 5MLD and so it is unclear whether it would include legal persons as well as natural persons. Pursuant to 5MLD, if the settlor, trustee and/or protector are legal persons, they would ***not*** need to be recorded on the register. Likewise, if a beneficiary is a legal person, it would ***not*** need to be recorded on the register and where identified beneficiaries are not ***all*** natural persons, the record should only describe the class of beneficiaries and not give individual identities. Any natural person exercising ultimate control over the trust would be registered in accordance with paragraph (b)(v) of the definition of "beneficial owner". The PSC statutory guidance on the meaning of "significant influence or control" in relation to trusts may be instructive in determining whether a natural person has control over the trust for the purposes of (b)(v) albeit we would query the extent to which it would be possible for our members to discern the "natural person exercising ultimate control over the trust" without the extensive and costly due diligence already referenced.

It is our understanding that the approach we have suggested above reflects the German transposition of 4MLD. We are informed the German Regulations (*Gesetz über das Aufspüren von Gewinnen aus schweren Straftaten*) effective as of 1 October 2017 expressly clarify that the trustee data reporting requirements relate

only to "beneficial owners" who are *natural* persons and we assume a similar approach would be followed in respect of the German transposition of 5MLD. Our suggestion, if implemented, would promote a consistent application of 5MLD across the UK and other EU Member States.

65. ***Is the UK's proposed approach proportionate across the constituent parts of the UK? If not, please explain your view, with reference to specific trust types and their function in particular countries.***

No response

66. ***Do you have any comments on the government's proposed view that any obligation to register an acquisition of UK land or property should mirror existing registration criteria set by each of the UK's constituent parts?***

No response

67. ***Do you have views on the government's suggested definition of what constitutes a business relationship between a non-UK trust and a UK obliged entity?***

No response

68. ***Do you have any comments on the government's proposed view of an "element of duration" within the definition of "business relationship"?***

No response

69. ***Is there any other information that you consider the government should collect above the minimum required by 5MLD? Is so, please detail that information and give your rationale.***

No. We are of the view that a huge volume of data would be held by the government without a clear anti-money laundering / terrorist financing purpose. Such a huge volume of data would, in our view, have the potential to prevent or at least make more difficult the use of that data for its intended policy purposes, which is to say seeking to ascertain potential terrorist or money laundering purposes. For these reasons we consider that every effort should be made to focus the data collected pursuant to 5MLD to ensure its relevance and potential value.

70. ***What is the impact of this requirement for trusts newly required to register? Will there be additional costs, for example paying agents to assist in the registration process, or will trustees experience other types of burdens? If so, please describe what these are and how the burden might affect you.***

See our response to question 64 above. The scale of the requirement is immense in every respect, from the due diligence required to identify express trusts, the requirement to develop and build software and manual processes to capture required information and effectively process it for registration, the additional human resources and infrastructure required and the very significant costs involved in doing so. As professional trustees of bonds and security arrangements our members are particularly concerned that, to the extent the trusts they administer are not excluded from the definition of "express trust" and to the extent "beneficial

ownership" is not confined to natural persons in the manner suggested, they should only be required to register the "class of beneficiary" (e.g. "secured parties", "lenders", "bondholders" as the case may be) and not the individual identities of beneficiaries which are very difficult to determine and to update when they frequently change, especially on a backward-looking basis. The additional burden created by the obligation to update should also not be underestimated. In the context of a syndicated loan, for example, the identity of a lender beneficiary of a security trust can change frequently during the life of the loan as positions under the loan are traded, necessitating an almost constant monitoring of beneficial ownership and updating of the register. An exclusion for bond and security trusts in commercial transactions is preferable. This would also be consistent with the equivalent arrangement in other EU jurisdictions where contractual promises or security are held on behalf of a changing class of beneficiaries under a legal device which is not a trust (see the last sentence of paragraph 9.14 of the consultation paper) and thus would not require to be registered.

English Law governed trusts are ubiquitous in European financing arrangements and it is not unfeasible that the increased burden on professional trustees to fulfil onerous registration requirements and the huge cost of doing so (which would likely be borne by investors if not the trustees themselves) could interfere with the efficient operation of loan and capital markets, impacting pricing and competition and placing undue stress on these vital markets.

71. ***What are the implications of requiring registration of additional information to confirm the legal identity of individuals, such as National Insurance or passport numbers?***

See our responses to questions 69 and 64 above. Requiring additional information also adds to the diligence burden and associated costs referenced in our response to question 70. Our members have also expressed concerns regarding the data protection implications of being required to request and store personal data and the potential for this requirement to interfere with other obligations under data protection legislation such as GDPR as well as the further additional cost of ensuring voluminous additional amounts of personal information is held and processed in a compliant manner.

72. ***Does the proposed deadline for existing unregistered trusts of 31 March 2021 cause any unintended consequences for trustees or their agents? If so, please describe these, and suggest an alternative approach and reasons for it.***

As outlined in our response to questions 64 and 70 above, requiring existing trusts to be registered places a colossal and disproportionate burden on our members due to the omnipresence of English law governed trusts in a multitude of different financial transactions whose purpose is to assist the efficient operation of the global capital markets. We have therefore suggested in our response that the proposals only extend to express trusts created after 5MLD is implemented in UK law, that the types of trusts which are to be regarded as express trusts are expressly identified having regard to the last sentence of paragraph 9.14 of the consultation paper and that such express trusts should not include "bond trusts" or "security trusts". This would provide legal certainty by making it clear exactly what the registration requirement applies to and avoid excessive costs in diligencing the existence and details of historic trusts. In the alternative and in view of the very significant number of existing trusts potentially subject to registration, we are of the view that a deadline of 31 March 2021 to identify and register such trusts and their beneficial owners is wholly unrealistic and should be extended by a minimum of 12 months.

73. ***Does the proposed 30 day deadline for trusts created on or after 1 April 2020 cause any unintended consequences for trustees or their agents? If so, please describe these, and suggest an alternative approach and reasons for it.***

See our responses to question 64 and 72 above. Express trusts should be clearly delineated and only include trusts which are at risk of money laundering and terrorist financing which the legislation is primarily targeting.

74. ***Given the link with tax-based penalties is broken, do you agree that a bespoke penalty regime is more appropriate? Do you have views on what a replacement penalty regime should look like?***

No response.

75. ***Do you have any views on the best way for trustees to share the information with obliged entities? If you consider there are alternative options, please state what these are and the reasoning behind it.***

No response.

76. ***Do you have any comments on the proposed definition of legitimate interest? Are there any further tests that should be applied to determine whether information can be shared?***

The proposals are silent on the rights of individuals and legal entities to oppose the disclosure of their data to third parties claiming a legitimate interest. Given the volume of data (including personal data) that the government will hold, affected individuals and legal entities should be entitled to be notified of any request and have input (with a right of challenge) on the disclosure of their data.

77. ***Do the definitions of "ownership or control" and "corporate and other legal entity" cover all circumstances in which a trust can indirectly own assets through some kind of entity? If not, please set out the additional circumstances which you believe should be included, with rationale and evidence.***

No response.

78. ***Do you have any views on possible definitions of "other legal entity"? Should this be defined in legislation?***

No response.

79. ***Does the proposed use of the PSC test for "corporate and other legal entity" which are designed for corporate entities, present any difficulties when applied to non-corporate entities?***

No response.

80. ***Do you see any risks or opportunities in the proposal that each trust makes a self-declaration of its status? If you prefer an alternative way of identifying such trusts, please what this is and why.***

No response.

81. ***The government is interested in your views on the proposal for sharing data. If you think there is a best way to share data, please state what this is and how it would work in practice.***

As mentioned above in our responses to questions 69 and 76, a large volume of data including personal data will be held by government and there are currently no proposals in place on protections around it. This raises the question as to whether the GDPR and other personal privacy implications have been considered and also the risk of the data being vulnerable to hacking and security breaches. Robust protections are required to address these concerns. Article 31(7)(a) 5MLD provides for exceptional circumstances to be laid down in national law where there is an exemption from such access to all or part of the information on the beneficial ownership (e.g. where the beneficial owners is a minor or otherwise legally incapable). It is unclear from the consultation paper what the exemptions will be in the UK and further detail is therefore required on this.

As mentioned in the introduction to this response, should it be helpful for representatives of the Trustee sub-committee to meet with you to discuss our responses further or to address any questions you may have, we would be happy to arrange a meeting.

Yours sincerely,

Jillian Hamblin

Chair, ICMSA Trustee sub-committee

International Capital Market Services Association

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Date: 10th November 2016

CONSULTATION ON THE TRANSPOSITION OF THE FOURTH MONEY LAUNDERING DIRECTIVE

Dear Sirs,

Introduction

We welcome the opportunity to provide the views of the Trustee sub-committee (Trustee sub-committee) of the International Capital Market Services Association (ICMSA) on the transposition of the Fourth Money Laundering Directive (directive) and HM Treasury's consultation in respect thereof dated September 2016 (consultation).

We have set out below an explanation of how securities are held in International Capital Market transactions. The explanation applies to securities whether they are unsecured or secured, debt or debenture stock. We also set out a summary of structured finance and secured transactions in which trust structures are commonly employed. Finally, we list points arising out of Article 31 of the directive (Article 31) on which we request your clarification in respect of International Capital Market trusts "governed under our law", within the meaning set out in paragraph 10.13 of the consultation.

It would be very helpful for us to meet with you in order to discuss this letter or any questions you may have, and we would be happy to arrange a meeting.

About ICMSA

ICMSA www.icmsa.org is a London-based self-regulatory organisation representing international financial and non-financial institutions active in the provision of services to the International Capital Market.

ICMSA's membership includes universal banks, registrars, stock exchanges, law firms, International Central Securities Depositories (ICSDs) and other service providers specialised in specific product segments such as the processing of tax reclaims. The primary purpose of the association is to foster the highest standards in the practice and management of International Capital Market services, thereby facilitating the efficient functioning of the market.

In its day-to-day activities, ICMSA focuses on the operation of the International Securities Market (i.e. securities primarily issued and deposited with the ICSDs, Clearstream Banking S.A. (Clearstream, Luxembourg) and Euroclear Bank SA/NV (Euroclear Bank).

Membership of the Trustee sub-committee comprises corporate trustees active in the provision of services to the International Capital Market and law firms which customarily advise such corporate trustees. The references in this letter to a trustee or trustees are to corporate trustees which provide services to the International Capital Market including the members of the Trustee sub-committee. Terms not otherwise defined herein have the meanings set out in the consultation or the directive, as applicable.

The issues set out in this letter may also be raised directly by our members as part of the consultation.

How securities are held in the International Capital Market

Securities issued by borrowers in the International Capital Market are in bearer or registered form. They are customarily held in the form of global securities, but may be held in definitive form. In the case of registered securities issues, the global securities will usually be called "global certificates" or variations on that theme. We use "global security" as the generic term to refer to both global bonds and global certificates.

The following explanation applies to global securities whether they are unsecured or secured, debt or debenture stock.

A global security is issued by an issuer in respect of all or part of an issue and represents interests in the underlying securities in specified transferable amounts in one instrument.

Global securities originally came into being because they saved costs. There was no need for an issuer to go to the expense of proofing and security printing definitive securities, and paying agents and custodians charged a lower fee for paying agency or custody services if securities were kept in global form (no coupons to physically handle). In addition, where the conditions of the securities allowed for complicated or frequent exercise of holders' rights, as for example with the remarketing or bidding procedures in variable rate securities, it was administratively simpler and cheaper to use the procedures of the ICSDs and to ensure that securities were held in the ICSDs by keeping them in global form. Use of global securities is now the norm.

Global securities will be held in ICSDs, in order to facilitate clearance and settlement of transactions between investors through electronic book-entry changes in the accounts of such investors. The ICSDs with which most investors hold accounts are Clearstream, Luxembourg (which is operated out of Luxembourg), Euroclear Bank (which is operated out of Brussels) and the CSD The Depository Trust Company (which is operated out of New York).

The diagram in the Annex to this letter shows the layers in the chain of ownership for securities in the International Capital Market held in the form of global securities.

We note that the majority of International Capital Market debt transactions are not constituted through a trust arrangement but through a pure agency arrangement in which a fiscal agent is appointed to act as the agent of the issuer without any fiduciary duties towards the holders and where the arrangements described in this letter concerning global securities held in ICSDs will also apply.

Bearer securities in global form

The global bond is payable to bearer, so technically the bearer owns the legal title to the global bond. For a bearer security which is offered and sold only outside the United States to non-U.S. investors (under Regulation S under the U.S. Securities Act), generally, the global bond is held by a common depositary (in some structures called the common safekeeper) for Clearstream, Luxembourg and Euroclear Bank. The common depositary holds interests in the global bond on its books as the agent of Clearstream, Luxembourg

and Euroclear Bank only and does not have a direct relationship with or any duties toward the ultimate beneficiaries.

Clearstream, Luxembourg and Euroclear Bank in turn each divide their interests in the global bond between their members, which may include other depositaries, to whose accounts securities are credited and who, as against the ICSDs, are beneficially entitled to securities according to their records. The members may hold the securities for their own account or as custodian for the benefit of their clients as the beneficial owner or as sub-custodians for other custodians holding such securities on their books and records for the benefit of their clients as the ultimate beneficial owners.

Payments due under the securities represented by the global bond are credited to the correspondent bank accounts of Clearstream, Luxembourg and Euroclear Bank, which credits such sums to the member accounts with Clearstream, Luxembourg and Euroclear Bank for onward distribution to ultimate investors.

Securities may be transferred between accountholders of Clearstream, Luxembourg and Euroclear Bank either internally or to accounts from Clearstream, Luxembourg to Euroclear Bank and vice versa through the electronic bridge operating between the two ICSDs.

The global bond is made payable to bearer just like a bearer definitive security and, unless specific provision is made otherwise, the bearer of a global bond is treated as the legal owner, and the ultimate beneficial owners are as described above. In the case of a global bond held in Clearstream, Luxembourg and Euroclear Bank systems, the common depositary is the bearer and therefore the legal owner.

Where rights are exercisable by individual holders, the common depositary deposits the global bond with (or, more likely, to the order of) the principal paying agent for endorsement with a statement of the rights being exercised by reference to the relevant principal amount of securities.

Bearer securities in definitive form

Title to a definitive bearer security passes by delivery. The trustee does not possess information about the identity of beneficiaries of such securities, and it would not be feasible for the efficient functioning of the International Capital Market to require the trustee to obtain and hold such information.

Registered securities in global form

The global certificate is payable to a registered holder and title belongs to the person registered in the register maintained by the issuer or its agent (the registrar) as holding the securities. The registered holder is a nominee of a common depositary on behalf of the ICSD(s) with which the initial subscribers or subsequent purchasers of securities represented by the global certificate have accounts. As in the case of securities in bearer global form, neither the nominee nor the common depositary have a direct relationship with or any duties toward the ultimate beneficiaries.

Where rights are exercisable by individual holders, the common depositary merely acts as post box passing on instructions of the ICSD's accountholders to the principal paying agent by reference to the relevant principal amount of securities and ordinarily is not privy to the identity of the accountholders.

Registered securities in definitive form

As with a global certificate, title to a definitive registered security belongs to the person registered in the register maintained by the issuer or the registrar as holding the securities. The trustee does not possess

information about the identity of the persons registered in the register, which will change each time a security is transferred.

In the same way as for definitive bearer securities, in the case of definitive registered securities it would impede the efficient functioning of the International Capital Market to require the trustee to obtain and hold information about the identity of the beneficiaries.

In fact, it is a basic expectation in the International Capital Market that investor identity and positions held are subject to strict confidentiality and the applicable trading infrastructure is typically subject to similar requirements imposed by law.

Structured finance and secured transactions

In a typical commercial structured finance transaction (structured finance transaction), a special purpose vehicle (SPV) will issue securities and will use the proceeds of such issuance to acquire collateral (collateral). The SPV's obligations to holders of securities are limited to and secured by a security interest created by the SPV over the collateral in favour of a trustee or security agent. Amounts payable in respect of the collateral when received by the SPV are used to fund the payment obligations of the SPV under the securities and to meet other fees, costs and expenses owed by the SPV to various service providers. The security interest referred to above created in favour of a trustee is held on trust for the benefit of secured parties (Secured Parties), including the holders of securities. The trustee will hold information as to the relevant definition of Secured Parties. Securities issued under structured finance transactions are typically issued in global form, as explained above. Neither the SPV nor the trustee will have access to information about the beneficiaries.

On these and other types of commercial transactions involving the grant of security in favour of a trustee (security trust), the trustee may also hold security for Secured Parties other than the holders of securities, including lenders, swap counterparties and service providers such as account banks. Secured transactions may be structured such that there are no holders of securities, but only Secured Parties. In such circumstances, provided the Secured Parties are contractual parties to the transaction documents, the trustee may know the identity of such beneficiaries, although frequently (for example each time a loan is traded) the trustee may be unaware of changes in the identity of those Secured Parties and it would be administratively burdensome to require the trustee to maintain a record of such beneficiaries.

Anti-money laundering (AML)

AML checks are carried out within the ICSDs on the accountholders (even where accountholders are acting as custodians holding securities on behalf of third parties). Accountholders in turn carry out AML checks on their clients. Such process is repeated down to the ultimate level of beneficial ownership.

Transactions in the International Capital Market, whether securities issues, structured finance transactions or security trusts, are not conducted in cash. All subscriptions and transfers are carried out electronically through regulated banking systems where AML checks and monitoring are carried out by the regulated bank at the point of entry to the banking system.

Trustees required to have regard to the holders of securities as a class

In connection with the exercise of their functions, trustees of International Capital Market securities are required under the trust deed to have regard to the interests of the holders of securities as a class and not to have regard to the consequences of such exercise for individual holders or to the tax consequences for

individual holders. Accordingly, for every such securities issue, the trustee will hold information as to the class of securities in respect of which it is trustee but, as explained above, the trustee will not know the identity of the individual holders within that class, and the trustee may not have regard to the interests of individual holders.

Information about ultimate beneficiaries of the trust

The consequence of International Capital Market securities being customarily held in global form, as explained above, is that the trustee appointed in respect of such securities does not possess information about the ultimate beneficiaries of the trust who hold through the ICSDs, although the trustee will hold information as to the identity of the ICSD(s) and the common depositary. The trustee has no right to require the common depositary to disclose any information about its accountholders.

In the case of bearer and registered securities in definitive form, the trustee also is not privy to the identity of beneficial or even immediate holders and it would impede the efficient functioning of the International Capital Market to require the trustee to obtain and hold information about the identity of the beneficiaries.

Tax consequences

We note the meaning attributed to a trust generating tax consequences at paragraph 10.18 of the consultation. Trusts in the International Capital Market on which members of the Trustee sub-committee are appointed are typically structured so that they do not generate tax consequences. Typically the trust will not generate a liability to income tax or capital gains tax or inheritance tax liabilities. The position for investors themselves may differ and will be particular to their circumstances and their income from the investments may indeed be subject to tax. As explained above, the trustee will not have information about such investors nor give any consideration to the personal tax situation of investors.

Trustee sub-committee views on consultation questions

The Trustee sub-committee has no comment on consultation questions 1 – 60, 62, 63, 66 – 87.

Question 61: We would welcome clarification that the government's view is that the requirement of Article 31 that the trustee is to obtain and hold adequate, current and up-to-date information of trust beneficial ownership is not aimed at trustees in the International Capital Market or trusts used in a commercial context including structured finance transactions and security trusts, and accordingly will not apply to such trustees or trusts, save as set out in our response to Question 65.

Question 64: We would welcome clarification that trustees in the International Capital Market or trusts used in a commercial context including structured finance transactions and security trusts will not be required to provide the trust beneficial information to also be held in the central register, save as set out in our response to Question 65.

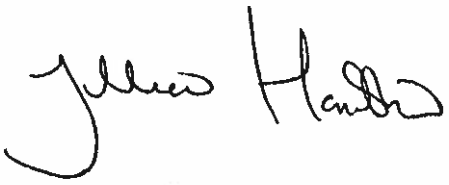
Questions 65: We would welcome clarification that, to the extent such trusts are in scope, only those International Capital Market trusts or trusts used in a commercial context including structured finance transactions and security trusts which generate tax consequences shall be required to provide to the central register information about their beneficiaries. We would also welcome clarification that any such requirement to provide to the central register information about beneficiaries would not apply in respect of such trusts created prior to the implementation into UK law of the directive.

As a further and separate point from the clarifications requested in respect of Questions 61, 64 and 65, we would welcome clarification, in context of the meaning of "governed under our law" set out in paragraph 10.13 of the consultation, if a foreign (i.e. non English) law governed trust would be in scope.

Meeting to discuss this letter or any questions you may have

As indicated above, it would be very helpful for us to meet with you and we would be happy to arrange a meeting.

Yours sincerely



Jillian Hamblin
Chairman, ICMSA Trustee sub-committee

ANNEX

Diagram showing the layers in the chain of ownership for securities in the International Capital Market held in the form of global securities.