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# 2016 Guernsey

# Funding Growth

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What impact will private equity have on Guernsey's trust industry?

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PAM INSIGHT

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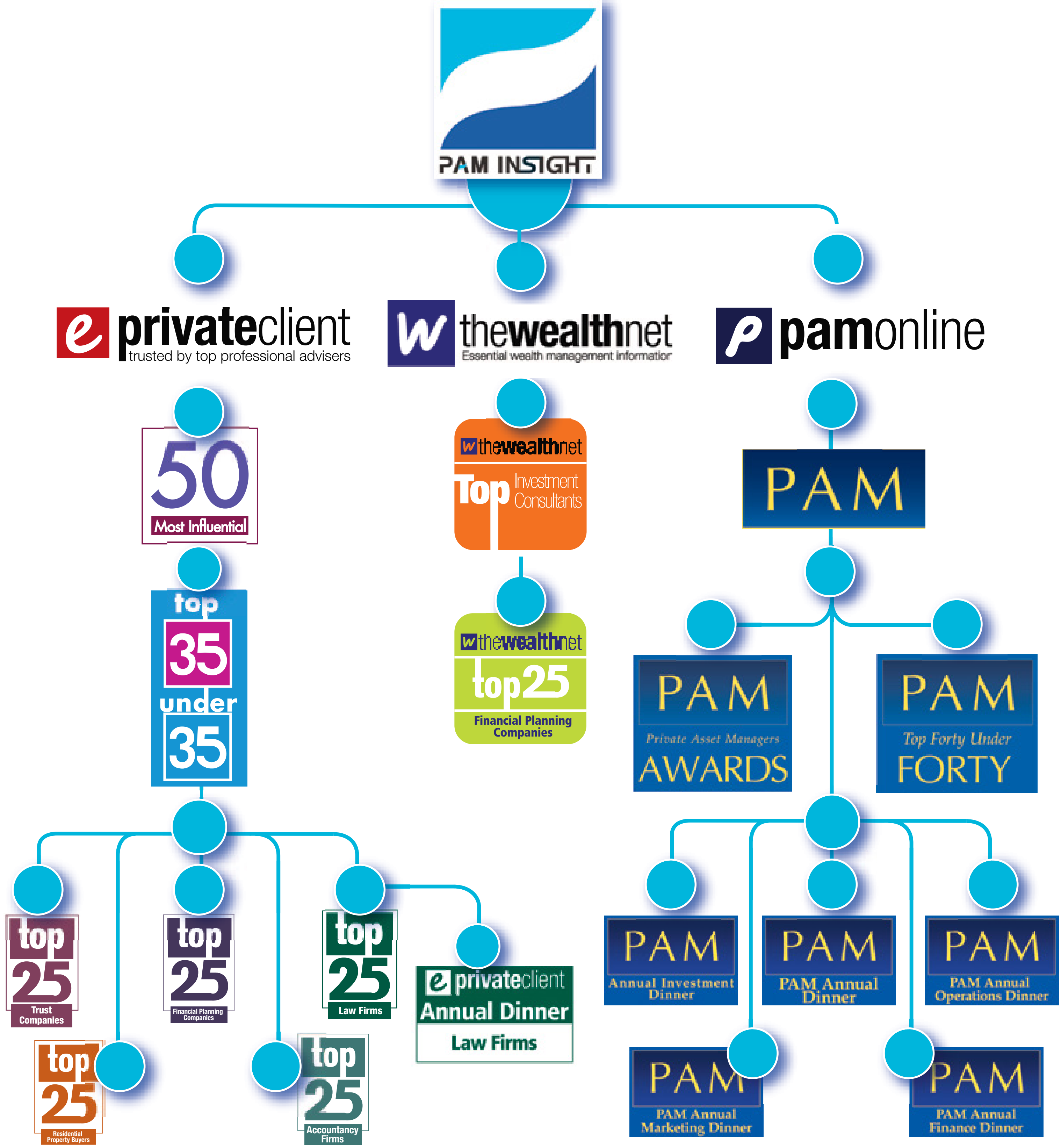


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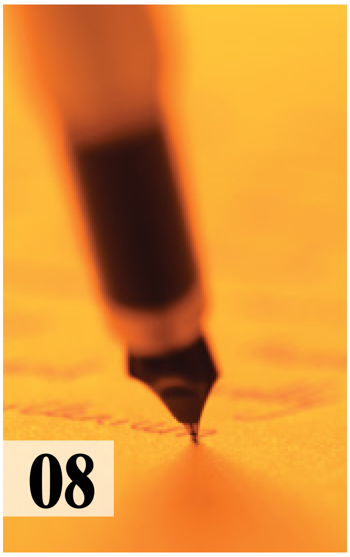



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## FEATURES

# A Brighter Future

The recent announcement of plans to open a representative office in Hong Kong during the first quarter of 2016 rounded off a particularly active 2015 for Guernsey's financial services sector, explains Guernsey Finance's chief executive Dominic Wheatley.

Dominic Wheatley

chief executive, Guernsey Finance

The Hong Kong office to be located at Three Pacific Place in Admiralty is Guernsey Finance's second overseas outpost, in addition to our Shanghai office which opened in 2008. It is ideally situated at the heart of Hong Kong's finance district and will further enhance our developing relationship with Hong Kong and its business community.

Our China representative, Wendy Weng, who is based in Shanghai, will use the office as a base from which to carry out further promotional activities concentrated on the wider South East Asia market, while it will also be utilised by the Guernsey Financial Services Commission (GFSC) to provide regulatory advice to those in the region who might be considering Guernsey-specific ventures.

The Hong Kong initiative follows the appointment in the autumn of Zoë Cousens as our first Middle East representative. Ms Cousens, who is based in Dubai, is now helping to promote Guernsey's financial services industry in the Middle East as an on-the-ground contact for Guernsey. She is now a key conduit for Middle Eastern firms and clients interested in Guernsey and will assist in hosting and arranging meetings, seminars or events for Guernsey businesses visiting the region.

Another exciting appointment for Guernsey sees Richard Le Tocq, who is also chairman of the Guernsey branch of the Institute of Directors, lead Locate Guernsey – the newly formed agency mandated to encourage and facilitate businesses and high net worth individuals (HNWIs) to move to the island.

Ahead of Mr Le Tocq taking charge it was reported at the end of October that Guernsey's Commerce and Employment Department had received more than 50 relocation enquiries from off-island businesses and individuals. Of these, five translated into actual relocations, with an additional 25 remaining live and investigating locating to Guernsey. In these instances, Locate Guernsey will assist by providing advice requested by enquirers and, if required, facilitate meetings and introductions to governmental and other contacts.

## Positivity

Across all the key pillars of our industry there have been positive stories to tell and examples of our standing within the mainstream of international finance.

One of the most demonstrable instances came in May when KPMG published its report, International Capital Flows. The report reinforced Guernsey's reputation as a leading funds domicile after revealing the extent to which the island facilitated the flow of capital globally, including £105 billion of investment in Europe – 49 percent of which originates from investors located outside Europe itself.

The report highlighted Guernsey as an integral conduit facilitating the raising of capital from investors in different countries, subsequently allowing for the redeployment of this capital into global assets. The report emphasised the fact that global investors are comfortable utilising Guernsey structures, in large part due to the island's reputation, regulatory track record and high standards of transparency. Similarly, it reaffirmed Guernsey's particular expertise in alternative investment assets – a key asset class for many investors.

## ESMA recommendation

This was followed in July by the European Securities and Markets Authority (ESMA) announcing its recommendation to grant Guernsey a 'third country' passport under the Alternative Investment Fund Managers Directive (AIFMD). Guernsey is one of only three jurisdictions to receive the recommendation, which, if approved by the European Commission, Parliament and Council in 2016, would further enhance Guernsey's position to distribute funds into Europe.

Guernsey has had its own opt-in equivalent AIFMD regime fully operational since 1 January 2014 in order to demonstrate the high standards that its funds industry works to, but the ESMA recommendation would further solidify this position and enable Guernsey to operate on a level playing field with its European counterparts once approved by the relevant European authorities – expected sometime in 2016.

> Across all the key pillars of our industry there have been positive stories to tell and examples of our standing within the mainstream of international finance

## Marketing leader

Within the ESMA advice the strong relationship between Guernsey's fund industry and the European marketplace was evidenced in data that showed Guernsey was the third largest non-EU fund domicile, behind the US and Cayman Islands, for the number of non-EU Alternative Investment Funds (AIFs) and non-EU Alternative Investment Fund Managers (AIFMs) marketing into the EU Member States of the UK, Ireland, Sweden, the Netherlands, Luxembourg, Finland, Denmark and Belgium for the nine-month period up to March 2015.

## OECD Convention extension

In August, a clarification from the Organisation for Economic Co-operation and Development (OECD) clarification, agreed by the UK's HM Treasury and Ministry of Justice, about Guernsey's position within the OECD further reinforced our standing within the funds arena.

The statement, agreed to inform EU and EEA authorities of Guernsey's position, states that:

*"The OECD Convention was extended to Guernsey on 20 July 1990. This means that the OECD Convention applies to Guernsey and it is part of UK's membership of the OECD. OECD decisions and recommendations apply to the same extent to*

*Guernsey as they do to the UK."*

The clarification over whether or not a fund's domicile is in the OECD has become increasingly important in order to meet requirements of certain market regulators. For example, in some jurisdictions there are prohibitions on the marketing of funds which do not originate from an OECD country.

**Fund migration**

More positive news for the funds sector came in Q4 with confirmation that two funds were re-locating to Guernsey.

VinaCapital Vietnam Opportunity Fund migrated its domicile from the Cayman Islands, while SafeCharge International Group Limited relocated its fund domicile from the British Virgin Islands. In explaining their decisions, both funds said Guernsey's well-established infrastructure for the administration of funds listed on the London Stock Exchange (LSE) was a key factor, as was the fact that having a Guernsey domicile would enable the company to enjoy greater exposure to potential investors.

**Banking moves**

Our banking sector has also been boosted in recent months.

Firstly, when the island's newest bank, FNB Channel Islands (FNBCI), officially opened for business in July. FNBCI, the Guernsey branch of FirstRand Bank Limited – South Africa's largest banks by market capitalisation – enhances FirstRand's presence in Guernsey as it already provided a wide range of fiduciary services through FNB International Trustees Limited.

This was then followed by ABN AMRO's announcement at the end of September that it was to transfer its Jersey private banking business to the Guernsey subsidiary.

**A fit for fintech**

In addition, last year saw Guernsey positioning itself to take advantage of opportunities in the digital age. A strategy document to guide the future of Guernsey's fintech sector was published by PwC and our Commerce and Employment Department in July. The paper included analysis of the Guernsey and international environment within the fintech sector to identify key market attributes and the future direction and involvement of local and off-island industry experts and stakeholders.

In Guernsey's favour is the fact that it is so well connected to the rest of the world, sitting at the centre of a hub of subsea fibre cables linking the UK with the Americas, Europe, the Middle East and Africa. This ensures Guernsey possesses the highly secure data connectivity, resilience and cyber security that the global finance sector and e-gaming industries require.

The GFSC's open door policy with fintech entrepreneurs also enables the Commission to work with practitioners to develop new regulatory responses where they are required to meet the needs of innovative products and emerging markets.

**Company Law updates**

In a move that impacts all sectors, updates to Guernsey's Company Law came into force at the beginning of September. Changes in legislation and associated regulations had made amendments to the Law necessary in order to address practical issues and to ensure that Guernsey remains a highly regarded and competitive jurisdiction.

Amendments were designed around feedback from industry users and now include companies being able to register an alternative name in a non-roman script i.e. using foreign characters.

Feedback from industry and practitioners is that the amendments have made a number of administrative processes more straightforward and corporate actions such as amalgamations, migrations and takeovers more efficient.

**Conclusion**

What is clear from this small snapshot of just some of the developments in the recent past is that Guernsey's finance industry continues to thrive and develop. This is most definitely an exciting and challenging time. Modern finance requires a combination of effective regulation, a robust AML regime, global standards of transparency, and an industry that delivers real substance, excellent advice and high quality service, within a stable political, financial and legal environment. Our continuing success is testimony to our ability to deliver consistently on all of these.

**Facts**

**156** registered trust companies

source: **Guernsey Finance**

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PAM INSIGHT

# Protecting a trust

Issues relevant to trust protectors have become a relatively hot topic offshore and entire books have, and no doubt will, be written on protectors. In light of an increasing number of protector disputes, Appleby's Adam Cole takes a high-level look at the nature of a protector's role and the relevant factors to consider should relations with a protector become strained.

Adam Cole

senior associate, Appleby

In essence the appointment of a protector provides a means of monitoring the actions of a trustee and checking that appropriate action is taken to preserve the trust fund. In order to carry out such functions, protectors may commonly be given "positive" powers such as the power to appoint and remove trustees and "negative" powers such as the right to withhold consent to capital distributions to beneficiaries. The role of a protector can, therefore, be a significant one in the context of the administration of a trust.

Protectors may be appointed to act in a fiduciary or non-fiduciary capacity. Where the settlor's intention in this regard is not clear, one will need to look at the nature of the particular powers given. As a rule of thumb, protectors will commonly have fiduciary obligations even if this is not expressly stated in the trust documentation. This is not always the case, however, and where, for example, the protector is also a beneficiary that expectation may be reversed. In any event we have seen a number of cases where the elements that may or may not point to a fiduciary role are in contradiction to one another and the position can very easily become one of nuance.

Protectors can play an important role in ensuring dialogue between the parties that are interested in a trust. When the office works well, it can be a successful channel for maintaining harmony in the midst of competing interests or views. This can be particularly important, albeit potentially more difficult, following the death of a settlor.

Protectors' powers mean that they can hold a large degree of influence over structures. Whilst this can undoubtedly be a positive factor, where the limitations of the role are not fully appreciated by those in office this can lead to significant problems for the administration of the trust. Such problems have been seen to materialise where, for example, a non-professional confidante of the settlor has been appointed and believes they are entitled to act in a quasi-trustee capacity.

**Resolving problems**

There are obvious reasons why it would not be appropriate for a trustee or beneficiaries to be able to remove a protector simply because a dispute has arisen. Where a protector has started to act in a matter that leads to a breakdown in trust and confidence, an extremely difficult position can, however, arise. Where such problems affect the ability of the trustee to act in the best interests of the beneficiaries there are steps that can be taken.

Parties should be mindful of the factors that the Court would consider in the context of an application to remove a protector. The threshold for removing a protector will naturally be a high one. It is a significant step to take and caution will be exercised by the Court before any order is made. Mutual hostility or distrust between the relevant parties will not suffice. A protector may quickly become unpopular as a result of decisions that do not find favour with beneficiaries or trustees and this would be no reason for a protector to step down or face forced removal.

The Courts will ultimately be guided by considerations over the welfare of the beneficiaries and the competent administration of the trust in their favour. Where a breakdown in relations has a significantly detrimental effect on the execution of the trusts and is likely to continue to do so, that would be a sufficient basis for the Court to exercise its discretion. It is not necessary that the protector bears the bulk of the responsibility for the breakdown in relations and the consequent difficulties caused for the trust, but such a situation will serve to fortify the conclusion that it is right for the protector to be removed.

Where circumstances of this nature arise, a protector would be well advised to walk before pushed. Where this does not happen, there is clarity on the circumstances in which the Court will exercise its jurisdiction to forcibly remove a protector. Whilst issues relevant to a protector's indemnities can serve to temporarily cloud matters, in our experience the desired result can be achieved without recourse to the Court. In the majority of cases it should, therefore, be possible to limit legal costs through an early dialogue with a protector's legal advisers.

Protectors' powers mean that they can hold a large degree of influence over structures. Whilst this can undoubtedly be a positive factor, where the limitations of the role are not fully appreciated by those in office this can lead to significant problems for the administration of the trust

# Trust Litigation in Guernsey

Litigation in the trust sector has seen a number of high profile cases in Guernsey and Bedell's Rupert Morris examines the impact two of these cases could have on trust work on the island

Rupert Morris
advocate, Bedell

2015 has been an eventful year for the Guernsey courts with a large number of important judgments having been delivered. The scope of such cases has covered many topics ranging from the application to English law trusts of the revised "Hastings - Bass" jurisdiction through to determining the nature of the law of contempt in private trusts proceedings. These decisions reflect the Bailiwick's continued importance as an offshore trusts jurisdiction and its contribution to international trust jurisprudence as a whole. It would be extremely difficult to do justice to each and every decision in a summary fashion. However, two cases are of particular global interest in the developing jurisprudence covering the topics of mistake and the duties of protectors.

## Mistake

In *Nourse v Heritage Corporate Trustees Limited and Concept Fiduciaries Limited* (Royal Court 01/2015) the applicant sought to set aside the settlement of the majority of his shareholding in a company into an employee benefit trust and sub-trust on grounds of mistake resulting from incorrect UK CGT advice provided in 2009. As now appears to be standard practice, HMRC were notified of the application however, in this instance, chose not to make any submissions or take part.

The Royal Court confirmed that it would apply English Law principles on the law of mistake, as now settled by the UK Supreme Court decision in *Pitt v Holt* [2013] UKSC 26. The test for setting aside a transaction in Guernsey now mirrors that in England & Wales – namely that there must be a causative mistake of sufficient gravity (and not merely ignorance or inadvertence) as to some matter of fact or law which it would be unconscionable to leave uncorrected.

The Judgment is of particular note given the consideration by the Jurats (the arbiters of fact in the Royal Court) of the possibility raised by the UK Supreme Court in Pitt as to whether relief should be refused on public policy grounds were the transaction to have involved a tax avoidance scheme that had gone wrong.

In *Nourse* the Jurats held that they did not regard the fact that the applicant was participating in a scheme to avoid the payment of taxes in the UK as any reason to refuse to grant the relief sought in Guernsey and, in the absence of any suggestion that the transaction was tainted with any illegality, found that it appeared to be a perfectly legitimate arrangement and accordingly set it aside.

**Protectors**

In *In the matter of the K Trust* (Royal Court 31/2015) the Court was asked to remove a protector at the instance of a trust's beneficiaries. The protector, a close friend of the late settlor, had taken a hands on approach to her duties following his death, leading to a breakdown in her relationship with the beneficiaries to such an extent that the current trustee considered that the trust had become unworkable. Additionally the protector was reluctant to resign until a suitable replacement of her choosing was appointed and she received a suitable indemnity against future liabilities (a matter upon which the trust deed was silent).

In the absence of Guernsey authority, the Royal Court rejected the Manx position of *Re Papadimitriou* [2004] WTLR 1141 which suggested that a court would only remove a protector "when that was essential to prevent a trust failing". Instead, whilst acknowledging that this was not a jurisdiction to be exercised lightly, it took guidance from, respectively, the Jersey and English cases of *In the matter of the A Trust* [2012] JRC 169A and *Letterstedt v Broers* (1883) LR9 App Cas 371, finding that the guiding principles for removal of a protector are akin to those for removal of a trustee. In granting the beneficiaries' application the Royal Court held that a protector might be removed where it appears clear that his/her continuance would be "*detrimental to the execution of a trust*" or otherwise damaging to the welfare or interests of the beneficiaries.

Of particular note is the Court's consideration of the nature of a protector's powers, relevant to the question of whether he/she would be entitled to be indemnified out of the trust fund. Generally, where a protector provides a degree of oversight of a trust, these powers have been assumed to be fiduciary rather than personal. However, in Guernsey at least, there is some debate due to s.15(2) of the Trusts (Guernsey) Law 2007 which suggests that the opposite might be true in the case of certain reserved powers.

The Guernsey Court held that, a protector's duties, and indeed to whom such duties might be owed, will need to be assessed on a case-by-case basis (as in Jersey in *In the matter of the Bird Trust* [2003] JRC013) by reference to the construction of the trust instrument itself. Here, it formed an "*overall impression*" from the trust's terms that the protector's office had been endowed with fiduciary rather than personal powers. However, relevant to the Court's decision was the fact that the trust had been settled prior to the 2007 Law coming into force, when no provision similar to s.15(2) was enacted. This suggests that the position might be different for trusts settled or powers exercised by protectors after that date, remaining, a potential area of concern for protectors in Guernsey, particularly as any implied right of indemnity is entirely dependent upon their powers being fiduciary in nature.

**Facts**

**£84 billion in bank deposits**

source: **Guernsey Finance**

# Coping with CRS


The tax authorities in the Crown Dependencies sent the first set of US FATCA reports, compiled by financial institutions in their respective jurisdictions, to the US Internal Revenue Service on 30 September 2015. Now the Crown Dependencies' financial institutions are preparing to report under the Common Reporting Standard (CRS) due to be introduced for on 1 January 2016. As an "early adopter" of CRS Guernsey-based Carey Olsen senior associate, Laila Arstall, considers the likely impact of CRS on Guernsey's financial institutions.

Laila Arstall

senior associate,
Carey Olsen

The Common Reporting Standard (CRS) is a regime for Automatic Exchange of Information (AEOI) which builds on the intergovernmental agreement to implement US FATCA. It is designed to be broad in scope and takes in three dimensions:

- The financial information to be reported relates to Reportable Accounts and includes all types of investment income but also account balances and the proceeds of sale of financial assets;
- The financial institutions that are required to report under the CRS include banks, custodians, brokers, certain collective investment vehicles, trust and corporate services providers;
- Reportable Accounts include accounts maintained for individuals and entities and there is a requirement to look through passive entities to report on the individuals who are seen as ultimately behind these structures.

This summer financial institutions in Guernsey filed their first set of reports with their local tax office (ITO) to comply with US FATCA. The reporting period covered 1 July 2014 - 31 December 2014. That data was then transmitted by the ITO to the US Internal Revenue Service. This is just the start of the long journey of annual AEOI because, in 2016, financial institutions will need to file reports in respect of accounts maintained for UK tax residents under UK FATCA (for 2014 and 2015) as well as under US FATCA (for 2015) and start collecting data in respect of account holders that are resident in jurisdictions that have committed to CRS (for 2016).

At its meeting in Barbados at the end of October 2015, the Overseas Economic Cooperation and Development's (OECD) Global Forum announced that a total of 96 jurisdictions have committed to CRS and Guernsey is one of the early adopters.

**Compliance with CRS engages a wide range of expertise**

Meeting the challenges of the CRS impacts on many aspects of financial services provision. The burden of collating and reviewing the data required to identify Reportable Accounts primarily falls on the compliance departments of Guernsey-based financial institutions that process and store client due diligence for anti-money laundering (AML)/know your client (KYC) purposes. The more jurisdictions with which Guernsey enters into exchange agreements, the more clients and structures to be reviewed and, potentially, the more reports that have to be filed. The onus of collecting financial data to be included in reports falls on those preparing accounts for the relevant structure. However, in many cases, identifying the extent of interests held in a Reportable Account will require input from those actively involved in the management and administration of the structure to be reviewed. CRS, like US FATCA, requires interests held by settlors, protectors, shareholders and lenders, and those who exercise ultimate effective control over a structure, to be reviewed. This has thrown up substantive issues that require further investigation into the legal nature and roles played by interested parties.

Although there are no notification requirements included as part of domestic law to implement US and UK FATCA in Guernsey, legislation to implement CRS includes the requirement to notify affected individuals that information relating to their accounts will be reported to the ITO. The onus of ensuring timely and appropriately drafted communications with affected account holders will fall on relationship managers and client-facing employees of financial institutions as they deal with an increasing number of enquiries from account holders and their advisers.

All this has placed additional demands on budgets and staffing resources leading to increased costs and pressure on the bottom line. Those

> Identifying the extent of interests held in a Reportable Account will require input from those actively involved in the management and administration of the structure to be reviewed

financial institutions that have already geared up for US and UK FATCA are well placed to meet these challenges as they leverage up on their experience. Certainly, a financial institution that is part of a multi-jurisdictional structure is able to draw on support from members of its wider group. For independent financial institutions, regular and on-going training seminars provided by advisers in the field, and representative bodies that are keen to maintain Guernsey's reputation as a premier centre for financial services, have contributed to the up-skilling of the island as it faces new challenges ahead. Where necessary, Guernsey-based financial institutions have been reaching out to experts in this fast-evolving area to assist with substantive issues of interpretation, staff training and the preparation of client communications. At the same time service providers already active in the compliance field have been extending their offering to include data collection and preliminary screening to help clients meet their obligations under third-party service agreements.

**Impact on Guernsey's Tax Administration**

The ITO has actively engaged the finance industry as it develops domestic law and guidance to implement the various AEOI regimes. The most recent consultation on CRS closed on 23 October 2015 and was accompanied by draft legislation to implement CRS with effect from 1 December 2015 so that systems can be put in place from the start of 2016. The cost, in terms of time and man power to process industry's input, draft guidance and liaise with the OECD and other competent tax authorities while participating in the ever-expanding programme of peer reviews conducted by the Global Forum, has undoubtedly had an impact on the cost of tax administration in Guernsey. This is in addition to the costs associated with developing Guernsey's Information Gateway Online Reporting system (IGOR) through which digital reports will be filed. Accordingly, in its 2016 Budget Report, the States of Guernsey have authorised a further £235,000 in additional costs to cover the recruitment staff to implement the different AEOI regimes and support costs associated with domestic ICT systems used generally by the ITO. This is on top of funds previously allocated to cover systems to cope with the introduction of FATCA in 2014.

In the longer term, with the influx of more data from around the world, tax authorities will soon be in a position to learn more about the financial affairs of their residents whose affairs involve assets and structures based in a foreign jurisdiction. Those tax authorities that have an extensive network of Tax Investigation Exchange Agreements (TIEAs) will be able to pursue specific enquiries where appropriate. Consequently Guernsey, along with other CRS participating jurisdictions, may find themselves dealing with an increasing number of TIEA requests which would require local tax offices to use their domestic powers to obtain information or documentation in response to appropriately framed requests. To this end HMRC issued a notice in mid-September this year saying that the information it will be receiving under CRS will be used "immediately and effectively alongside all the other data that HMRC holds to build a more complete picture of UK tax pairs with offshore assets".

By the same token, as Guernsey has entered into reciprocal agreements for the exchange of information in respect of assets held overseas by Guernsey tax residents, ITO will be receiving financial information about its own tax payers; this could, potentially, lead to the recovery of unpaid taxes which would certainly go some way to redressing Guernsey's 2015 budget deficit of £20 million.

The CRS, like other AEOI regimes, presents challenges at various levels of the financial services industry. Many Guernsey financial institutions are well placed to meet these challenges having had the benefit of preparing for FATCA and filing the first returns earlier this year. Both the ITO and local industry have spent time and resources putting in place appropriate procedures and personnel with a view to maximising operational efficiencies while standardised practices still evolve. It is clear that Guernsey is set to meet the challenges that CRS presents with the benefit of the island's collective knowledge, experience and wisdom.

**Facts**

**819 captives & cells registered**

source: **Guernsey Finance**

# Guernsey's growing funds sector

## A growing fund industry can only benefit Guernsey as a whole explains Andrew Maiden of Moore Management

Andrew Maiden

funds director,
Moore Management

For over 50 years Guernsey has been a well-established offshore finance centre, and its fund industry continues to go from strength to strength. As at the end of September 2015, the net asset value of all funds under management and administration in island stood at £224.8 billion, spread across 1,045 funds approved for domicile or servicing in Guernsey. These assets were split across the three main fund regimes – closed ended, open ended and non-Guernsey schemes – and it was pleasing to see growth in all three categories during Q3 2015, supporting the mantra that Guernsey offers a diverse range of funds.

Guernsey has a long history of being self-governed and self-funded, and is politically and economically stable. Indeed, it was recently announced that Guernsey has retained its AA+ credit rating from the international credit rating agency, Standard & Poor's.

The close proximity of Guernsey to London and other major financial cities in Europe, coupled with its reputation as a financial service centre of excellence, make it an ideal fund jurisdiction for investment into Europe – not only from European investors but also from further afield, including the US, Asia and Africa.

The Guernsey regulator, Guernsey Financial Services Commission (GFSC), has adopted a pragmatic approach to fund regulation and implemented a world class regulatory framework and standards which offers flexibility to fund structures and provides confidence to investment managers that fund structures in Guernsey are well supported by the GFSC.

Guernsey has not rested on its laurels when it has come to maintaining its high standards of regulatory framework and transparency. In July 2015, the European Securities & Markets Authority (ESMA) advised extending the Alternative Investment Fund Managers (AIFM) third-country passport to include Guernsey, making it one of only three jurisdictions to be endorsed. It is expected that the island will receive a positive assessment from MONEYVAL following their latest visit, supporting the global transparency standards which Guernsey has adopted. The jurisdiction has committed to the early adoption of the Common Reporting Standard (CRS), the global standard for the automatic exchange of information developed by the OECD. It has also signed an agreement with the US to report under a Model 1 FATCA Intergovernmental Agreement, with a similar agreement signed with the UK.

Guernsey offers a full broad range of fund structures, including private companies, partnerships, unit trusts, protected cell companies, incorporated cell companies and limited liability partnerships.

The fund administration and servicing expertise in Guernsey is second to none. There is a wide variety of excellent fund administration service providers, legal and tax advisers and accountants to

support all types of fund, from the small private structures to large FTSE listed vehicles. Guernsey is renowned for having a highly-skilled and internationally-minded professional workforce with a service culture.

Historically, Guernsey has been very good at developing new fund offerings in order to capture growth areas. The growth of private equity and closed ended listed structures is a demonstration of the island's versatility and ability to adapt to changing demands. More recently this growth has expanded to capture real estate, fund of funds, debt, infrastructure and other alternative fund structures.

The world now moves at a faster pace than ever before and Guernsey will need to continue to move with the times in order to keep facilitating the demands of the ever-evolving fund market. The challenge for Guernsey will be to find the next fund product line, take the lead with the legal and regulatory framework and promote the island as the jurisdiction of choice. The global fund industry is massive and Guernsey has so far excelled at being a master of specific fund product lines rather than a 'jack of all trades'.

Being an island with a population of circa 60,000 does offer up some challenges, with the biggest being the ability of businesses to source a high calibre of professional to service its growing fund industry. Efficiencies in processes and advancement in technology will help ease this problem. However, as fund structures become more complex and there is a greater focus on higher corporate governance standards, the need for well-trained professionals in Guernsey will increase. This, I believe, will ultimately require changes to the Guernsey housing licensing regime, with steps already being taken by the States to alleviate this potential problem.

Despite the global political and economic climate, introduction of the CRS and uncertainty surrounding the growth of emerging economies, there will still be an appetite and opportunities for fund structures – especially with money coming from Asia into Europe and with the expansion of investment in and out of Africa. Technology will undoubtedly play a part in fund structures, with investors having far more say in what they invest their money in. I have no doubt that Guernsey will continue to redefine itself in order to maximise opportunities, be a competitive and innovative jurisdiction and retain its status as a leading jurisdiction for funds.

# THE RISE of private equity

How has the increase in private equity investment in the trust sector in the Channel Islands and beyond impacted the industry and what will the consequences be, asks Michael Betley of Trust Corporation International

Michael Betley

group chairman, Trust Corporation International

The entrepreneurial spirit has much to do with the successful evolution of the trust sector in Guernsey which has developed beyond all recognition from its embryonic state in the late 1960s. It started with the arrival of the first of many international merchant banks on the island.  External demand created opportunities which spawned the offshore trust industry and has shaped the sector into what it has become. One of the more recent catalysts of change has been the increasing influence of private equity firms (PE) interested in the sector not for its product set but for its investable qualities. The simple operating models and stable cash flows are particularly attractive and easy for PE to exploit. It is the more mature

The simple operating models and stable cash flows are particularly attractive and easy for PE to exploit

and scalable investment funds sector which has seen the most significant investment activity of this sort and gives an indication of how PE may end up influencing the less mature trust sector. Whether you view the private equity influences positively or negatively, you cannot ignore their presence or influence in the ongoing transformation of the industry.

The early investors in the sector were the banking institutions who were attracted by the ability to "harvest" assets and charge the same client for a range of services and financial products. This cross-selling opportunity and cross-border regulatory arbitrage meant that banks were able to move clients from one jurisdiction to another to minimise the increasing regulatory burden whilst still retaining the multiple income lines. During the 1990s, changes to international accounting standards and practices meant that the big international accounting firms who had in-house trust companies sought to divest themselves of those businesses to enable them to continue to represent global audit and advisory clients unencumbered by potential conflicts. The likes of Royal Bank of Canada seized on this as an opportunity to acquire professionally owned and run trust businesses starting with the acquisition from PwC of Abacus Financial Services and later Regent Trust Company from Ernst & Young. Kleinwort Benson entered the fray and acquired Orbis Management from KPMG in a competitive bidding process. It has only been since the global financial crisis starting in 2008 that private banks more clearly understood what "fiduciary risk" meant and there has been a full scale retrenchment of private banks from non-core business including divesting their trust businesses.

Guernsey is currently home to 156 regulated trust companies that are authorised to provide a range of professional services. In addition to the usual creation and management of a variety of different holding and trading vehicles, trust companies are developing more specialised investor-orientated services, managing family offices, creating pension products and establishing global custody and unregulated lending platforms. The excellent service level systems which are in place have provided trust companies with new market opportunities and greater potential for growth. Many structures have a lengthy life span which means there is considerable annuity value in the predictable income streams. Whilst not all 156 licensees will necessarily have a physical presence in Guernsey, they have the ability to undertake regulated activities from the island. Many of the licensees have acquired a fiduciary licence so that they can undertake ancillary regulated activities which may simply be a by-product of their core offering. For example, a number of collective investment scheme administrators who are regulated under a different regime may also have a fiduciary licence to allow them to provide a fuller range of services unconstrained by the peculiarity of Guernsey's division based regulatory regime. A number of licensees may also be "managed trust companies" which are owned by non-Guernsey based practices or institutions who engage a Guernsey manager to administer their own book of business from the island. Recent statistics show that 44 percent of trust companies are manager-owned locally. The other major ownership categories are international financial groups (27 percent) and those owned by international legal and accounting practices (15 percent).

It is interesting to note that during the initial transitionary phase following the introduction of the Fiduciary Regulations in April 2001, there were 160 trust companies with an additional 34 pending applications awaiting approval. The transitioning of the trust sector into regulated business created immediate opportunities for consolidation and, by 2003, the number of full fiduciary licensees had reduced to 151. In over a decade, therefore, and with the current number of 156 operators within the trust company space, the sector has remained largely static. In the 10 years to 2015, reported turnover in the sector has increased by 494 percent but over the same period the number of trustee appointments within the trust sector has diminished by 29 percent. Business is clearly becoming more profitable. It is this impressive growth trajectory which is at the heart of why PE finds the trust sector so attractive. There remains more buyers of trust businesses than active sellers, however, there continues to be M&A activity despite what the statistics might infer. Whilst the headline numbers have remained largely static over the last decade, there has been consolidation but the pace of innovation and change has attracted new entrants too.

Prior to the Fiduciary Regulations, business practices and anti-money laundering procedures were not embedded within the firms and a considerable amount of remedial work was needed to bring not just the client book up to the new regulatory standard, but the businesses themselves. The introduction of the Fiduciary Regulations was a welcome benchmark for private equity houses as whilst client and business remediation would still take some time to work its way through the system, it offered the opportunity for external investors to have confidence in investing in a more transparent and compliant book of business. The emergence of PE as an interested investor in this sector started to take hold soon after regulations came in. The first obvious private equity deal was the creation of Equity Trust by Candover Investments plc who saw the potential to create an international business platform by bolting together a number of separate Crown Dependency and international trust and corporate service businesses, starting with its acquisition of Insinger de Beaufort. Candover sold Equity Trust in 2010 for an enterprise value of EUR 350 million suggesting it had achieved a 24 percent uplift in value over that period.

It is not just PE seeking investment targets which is at play as businesses themselves seek financial backing to help deliver their strategic plans. Successful businesses can outgrow their management, others can reach their growth ceiling due to capital constraints and, often, business ownership and succession drive management to seek funding options. The apparent abundant capital available to many PE houses is an attractive source of finance to help management and business owners achieve their aims and overcome growth hurdles. PE can help stimulate expansion and diversification, incentivise employees and re-invigorate stagnating businesses. However, PE invariably comes at a cost. Ultimately this means the loss of control so that choosing the right PE firm to properly align the capital providers with the management strategy is key.

Whilst PE has been the dominant player in consolidating the trust sector in Guernsey, new capital providers are emerging. Private or family investment offices are entering the market, attracted by the stable returns and easily understood businesses. Such investors are likely to be less demanding regarding management change, targeted returns and more sympathetic to management objectives. An interesting new development adopted earlier this year by the Sanne Group, was the first independent fund and corporate service provider to list on the London Stock Exchange. Following its IPO, Sanne is currently trading at 22 times its enterprise value showing how it is possible to stimulate the capital value of businesses. This is at a time when there has been a wholescale divesting programme by international banks of their trust companies, including the likes of Royal Bank of Canada who until this year had probably acquired more trust business than any other. Is this likely to be cyclical? I have no doubt these financial institutions will return to the sector as senior management reappraises its risk and return objectives over the next 5 to 10 years. As a consequence, there remain continuing opportunities for trust businesses to nurture their future either alone or as a target for savvy investors wanting to participate in stable income from growing businesses. This is a positive outlook for Guernsey and its trust sector with a significant number of quality businesses within the industry. PE has undoubtedly fine-tuned business models to make them attractive investment targets, but it is the businesses themselves who must continue to make their offering compelling by evolving and creating future demand.

Whilst PE has been the dominant player in consolidating the trust sector in Guernsey, new capital providers are emerging. Private or family investment offices are entering the market, attracted by the stable returns and easily understood businesses

# STRUCTURES FOR ASIAN CLIENTS

Working with clients around Asia, and structuring with a variety of offshore laws, we are finding an increasing interest in using Guernsey law structures. Ogier's Lara Mardell looks at why this is, looking at key drivers for Asia-based clients and how Guernsey law trusts and foundations can be used to achieve their goals.

Lara Mardell

head of private client and trust - Asia, Ogier

Clients in Asia often have successful family businesses and need to structure appropriately to help achieve a smooth transition in the running of the business when the founder passes away. These clients will usually wish to maintain control of the business, rather than cede control to a trustee. Many clients we find are also concerned to limit beneficiary rights to information and to challenge the structure, and a number want perpetual trusts.

In addition, many of the very wealthy business owners here are interested in benefitting charities or philanthropic organisations, and may even wish to set up their own organisation but prefer to structure such an organisation outside their homeland.

Many clients in Asia are interested in very long term succession planning, and prefer not to have a limit imposed on the duration of the trust, so this is often a key appeal of Guernsey law

### Business succession planning

There is a proverb in China that 'wealth does not survive the third generation.' Research has backed this up showing that family businesses frequently struggle or fail in the years following the death of the founder, when ownership and control of the business is split between a number of family members.

A traditional trust structure, where family members enjoy the economic benefits of the family business, but a trustee maintains control, will help to mitigate this problem but is unlikely to be what the founder wants – he will probably wish to maintain control of business decisions himself while he is able to, and to name successors to do this afterwards.

In theory a trust using a traditional law such as English law could be established where the settlor reserved the power to be, or to appoint, a director of a company owned as part of the trust fund. However, there are concerns that without specific legislation addressing the matter this might give rise to trustee liability issues, might cause the settlor to be deemed to be a trustee, or could even jeopardise the validity of the trust.

The Trusts (Guernsey) Law 2007 (the Law) provides expressly that a settlor may retain such powers (and a number of others) without this invalidating the trust or causing the settlor to be a trustee. The Law states further that a trustee acting in accordance with such a power does not act in breach of trust. A Guernsey reserved powers trust can therefore be an ideal vehicle for holding the family company, while allowing the directors of that company to maintain day to day control of it. Such a structure will also enable the directors to make decisions in regard to key matters such as listing the family company.

An alternative to a reserved powers trust is establishing a private trust company (PTC), with the settlor and others of his choosing on the board, to be the trustee, rather than a professional. This way the settlor and his family have direct involvement in the operation of the trust. Guernsey's PTC regime does not require direct regulation of a PTC. Another alternative is the Guernsey foundation (discussed below).

An additional benefit of using a Guernsey law trust is that Guernsey permits perpetual trusts. Many clients in Asia are interested in very long term succession planning, and prefer not to have a limit imposed on the duration of the trust, so this is often a key appeal of Guernsey law.

### Limiting beneficiary rights to information and to challenge

Settlors in Asia are often concerned to limit beneficiaries' rights to information regarding trust assets and terms. Guernsey has specific trust legislation which can assist with this. Where a trust deed limits a beneficiary's right to information as to the state and amount of trust property, the Law states that a beneficiary seeking such information must apply to court for it and show that the provision of information is necessary for the proper disposal of any matter before the court, for the protection of the interests of any beneficiary or for the proper administration or enforcement of the trust.

A Guernsey foundation can be structured so that beneficiaries have no right to information at all (see below).

## Philanthropy

Guernsey is an attractive option to philanthropists in Asia. Guernsey is a well regulated jurisdiction, with stable government and the rule of law and an independent judiciary. It also has a strict licensing regime for fiduciaries and an independent financial services regulator, and offers a wide range of high quality service providers and legal advisers.

A number of structures are possible for charitable purposes, including charitable trusts. Guernsey also offers non-charitable purpose trusts, which can be established for purposes which do not need to qualify as charitable, and which will be enforced by an enforcer. These can be particularly useful for general philanthropic purposes. A Guernsey foundation can be established for charitable or non-charitable purposes.

Guernsey charities have to comply with a specific registration regime. Guernsey also has a licensing regime in respect of non-profit organisations generally, which is likely to add gravitas to such an organisation and provide reassurance to those establishing them.

## The Guernsey foundation

A foundation is a corporate entity with trust features. Being a corporate entity the foundation itself holds assets (rather than a trustee which holds assets in its capacity as trustee of a particular trust). It is controlled by a council (which is similar to the board of directors of a company). The legislation specifically contemplates and permits retention by the 'founder' (equivalent to a trust's settlor) of material involvement in decision-making - for example the founder can sit on the council, with at least one other person who may be appointed by the founder.

A foundation can be established for beneficiaries or purposes or both. Where a foundation is established for beneficiaries, the beneficiaries can be 'enfranchised', in which case they have a right to information, or 'disenfranchised', where they have no such rights. Where there are no 'enfranchised' beneficiaries, or where the foundation is established for purposes only, the founder needs to appoint a 'guardian' to enforce it.

The only requirement for a Guernsey fiduciary to be involved is that where neither a councillor nor the guardian is a Guernsey licenced fiduciary the foundation needs to have a Guernsey resident and licensed fiduciary as registered agent.

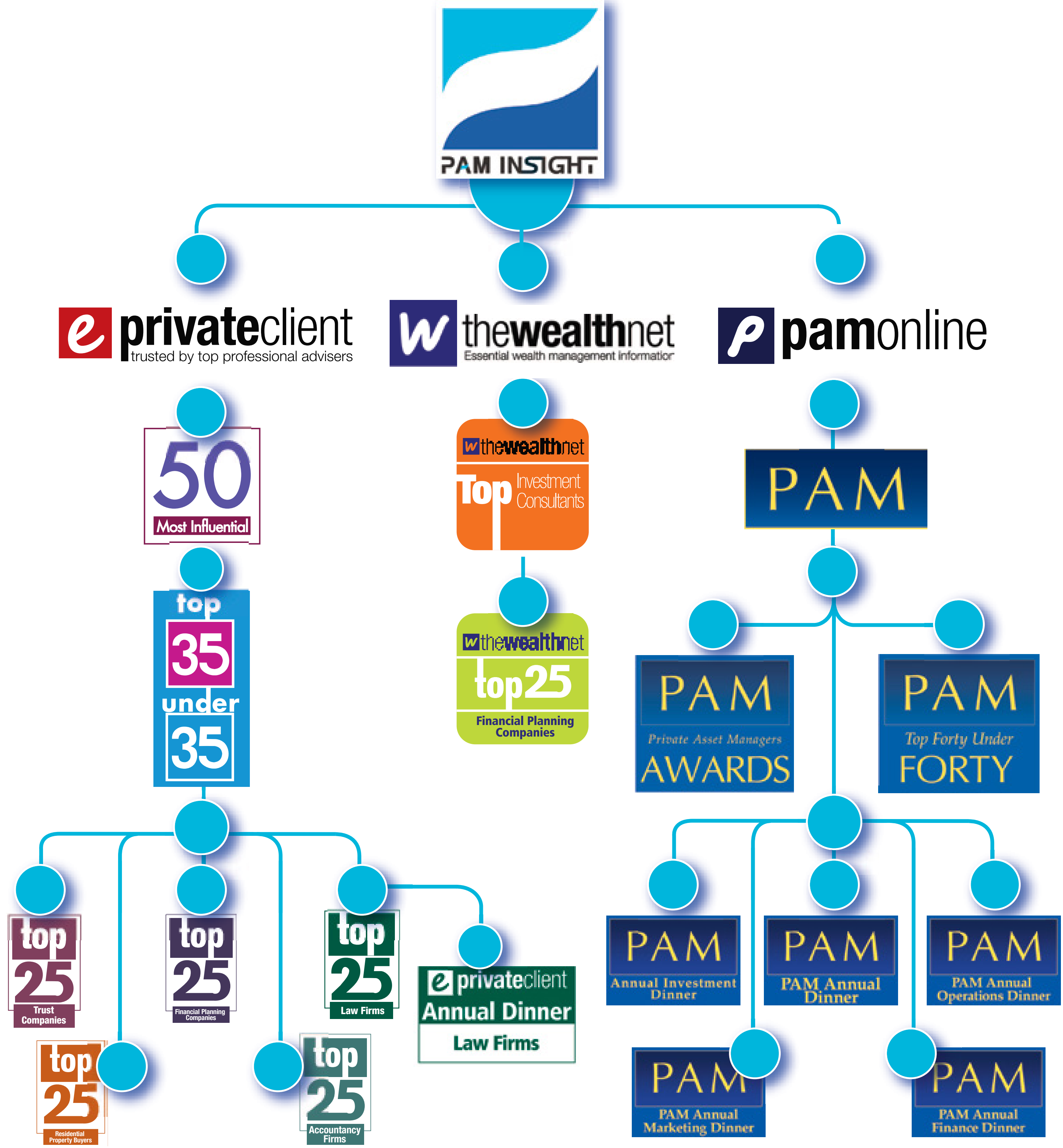
With its ability to offer the founder direct involvement in control of the foundation, while potentially limiting beneficiary rights to receive information, the Guernsey foundation is well suited to many Asian clients. It also offers a single-layered alternative to a trust with a PTC as trustee.

## The benefits of Guernsey law

Guernsey law trusts and foundations are an ideal way for Asia-based clients to establish structures for succession planning or philanthropy, while maintaining appropriate control of their assets. Guernsey firewalls help to enhance asset protection, and where a trust is used there is no limit imposed on the duration of the trust. Guernsey trust law offers settlors the option of limiting beneficiary rights to information, and the Guernsey foundation enables this to be removed altogether.

Guernsey is also a low tax jurisdiction, where structuring can be achieved in a tax neutral manner, and is well regulated, and well placed to deal with the increasing compliance requirements in the form of FATCA and the Common Reporting Standard. We expect to see increasing interest in the jurisdiction from Asian clients.

*a wealth of knowledge – a knowledge of wealth*

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