

Introduction to trusts for private bankers

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Introduction

1. This material is not for specialist trust lawyers. Instead it is intended to be an introduction to the subject for private bankers and other investment professionals for whom trusts are relevant because (a) your clients have trusts, (b) your clients ask you about trusts and/or (c) you otherwise come across trusts in your professional lives.
2. Trust law:
 - (a) is based upon a combination of legislation and case law; and
 - (b) differs as to its detail in each jurisdiction, but has common principles.

What is a trust?

3. A trust exists where a person (known as a trustee) holds or has vested in him legal title to property not for his own benefit but:
 - (a) for the benefit of any person (known as a beneficiary) whether or not yet ascertained or in existence; and/or
 - (b) for the attainment of any purpose.
4. A trustee must in the execution of his duties and in the exercise of his powers and discretions:
 - (a) act:
 - (i) with due diligence;
 - (ii) as would a prudent person;
 - (iii) to the best of his ability and skill; and
 - (b) observe the utmost good faith.

5. A trustee must carry out and administer the trust in accordance with its terms (subject to compliance with mandatory law).
6. A trustee must always act in the interests of the beneficiaries or achieving the purposes.
7. A trust is not a legal entity.
8. A trust is not a contractual arrangement.

Parties to a trust

9. The settlor:
 - (a) Establishes the trust;
 - (b) Transfers assets to the trustee to be held on trust;
 - (c) Ceases to own the assets after transfer;
 - (d) May be a beneficiary of the trust;
 - (e) May be a co-trustee of the trust;
 - (f) May retain some control over the trust.
10. The trustee:
 - (a) Holds legal title to the trust assets;
 - (b) Must hold the assets in accordance with the law and the terms of the trust for the benefit of the beneficiaries and/or the purpose of the trust;
 - (c) Is responsible for administration of the trust;
 - (d) Has certain minimum obligations.
11. The beneficiaries:
 - (a) Have beneficial interest in trust assets (or at least a right to be considered for benefit in a discretionary trust);
 - (b) Have a right to enforce the terms of the trust in event of breach of trust by the trustee;

- (c) Their interest in the trust is personal property.
12. The protector:
- (a) Is not mandatory;
 - (b) Is appointed to protect the interests of the beneficiaries;
 - (c) Is not a trustee.

Basic requirements

13. For a trust to be valid it requires three factors to be sufficiently clear and certain:
- (a) Certainty of intention to create the trust.
 - (b) Certainty of objects. It must be possible to ascertain the beneficiaries/purpose. For example, a trust for “my tall friends” would be uncertain and so invalid.
 - (c) Certainty of subject. It must be possible to ascertain the trust property.
14. There must be a trustee.
15. Assets must be transferred to the trustee.
16. A trust generally need not be in writing (but there are some exceptions to this and it is normal for a trust to be in writing).

When will you encounter trusts?

17. Even if you are not a trust law specialist it is still likely that you will come across trusts on a regular basis and will need to have an understanding of how they operate. For example, you may become involved in:
- (a) Trustees buying or selling assets;
 - (b) Clients receiving or buying assets from, or gifting or selling assets to, trustees;
 - (c) Purpose trusts and charitable trusts - often used for specific transactions e.g. to hold the shares in an orphan SPV;
 - (d) Companies owned by a trustee entering into transactions;

- (e) Unit trusts as investment fund vehicles.

Types of trusts

18. Trusts are very flexible and there are many different types. Some examples are:
- (a) Unit trusts;
 - (b) Discretionary trusts;
 - (c) Fixed interest/life interest trusts;
 - (d) Purpose trusts;
 - (e) Charitable trusts;
 - (f) Reserved powers trusts;
 - (g) BVI VISTA trusts;
 - (h) Cayman STAR trusts.

Myths and misconceptions about trusts

19. There are numerous myths and misconceptions about trusts. Some significant examples are set out below. They are not true.
20. The settlor has no control over the trust assets.
- (a) No.
 - (b) Just because the settlor transfers the assets to the trustee does not mean that the settlor can no longer have any involvement or control over those assets.
 - (c) There are numerous ways that settlor can retain control. These include:
 - (i) Reserved powers trust - the settlor reserves to himself (or a third party he trusts) power to make decisions on certain issues (e.g. investment of the trust assets).
 - (ii) BVI VISTA trust - the trust assets are held in a BVI company. The BVI company is owned by the trustee, but is managed and

controlled by its directors (who can include the settlor or any other person).

(iii) Protector provisions - the terms of the trust can provide that certain trustee decisions (e.g. investment of the trust assets) require consent of the protector (who can be the settlor or any other person).

(d) However, must ensure that retention of control does not invalidate trust or cause other issues.

21. The trust can not be changed in the future.

(a) No.

(b) The trust deed can be amended in any way, at any time and as many times as permitted by the terms of the trust deed.

(c) The trust can be revoked and the assets returned to the settlor if permitted by the terms of the trust deed.

22. The trustee could use the trust assets for its own benefit.

(a) Not legally.

(b) The trustee must act in accordance with:

(i) trust law;

(ii) the trust deed;

(iii) the best interests of the beneficiaries.

(c) The trustee can not act for its own benefit.

(d) Professional trustees in many countries are regulated (e.g. BVI, Cayman, Guernsey, Jersey).

(e) The Beneficiaries and the settlor have legal rights if the trustee breaches its duties - then can go to court to get a remedy.

23. The trustee could act contrary to the terms of the trust deed.

(a) Not legally.

- (b) The trustee must act in accordance with:
 - (i) trust law;
 - (ii) the trust deed;
 - (iii) the best interests of the beneficiaries.
 - (c) The trustee can not act for its own benefit.
 - (d) Professional trustees in many countries are regulated (e.g. BVI, Cayman, Guernsey, Jersey).
 - (e) The beneficiaries and the settlor have legal rights if the trustee breaches its duties - then can go to court to get remedy.
24. A trust is just like a bank account.
- (a) No.
 - (b) A trust can be used to hold assets like a bank account, but is not a bank account.
 - (c) The parties to a trust (the trustee, settlor and beneficiaries, etc) must comply with the terms of the trust and with trust law when dealing with the trust assets.

Uses of trusts as part of wealth management

- 25. Trusts are extremely flexible. Accordingly, trusts can be used in an extremely wide range of ways to assist clients as part of wealth management.
- 26. Asset holding. Trusts can be used as a vehicle to simply hold assets.
- 27. Tax efficiency. Depending on the particular country where the settlor and the beneficiaries are resident and the law governing the trust, trusts can potentially be used to reduce taxes. Sometimes by changing the nature of the asset owned or the funds earned. Sometimes by dividing or re-directing income. Sometimes by deferring recognition of income or gains.
- 28. Creditor protection. Trusts can be used to hold assets outside the ownership of the settlor and potentially beyond the reach of the settlor's creditors.

29. Succession planning. Trusts can be used as a mechanism to transfer assets to family members in a more effective way than by will or by gift. Trusts can allow the transfer to occur gradually and/or at the time which is most appropriate for the family members involved.
30. Avoiding asset fragmentation. Trust can be used to hold assets and many different family members can benefit from those assets without dividing the assets and distributing them between different family members. For example, a trust can retain a majority holding in a family company and many family members can be beneficiaries of the trust and thereby benefit from the earnings arising from the holding while avoiding fragmenting ownership between the family members and losing the majority control of the family company.

How to talk to clients about trusts

31. No client wants a trust - but they do want the things that a trust can achieve.
32. Ask your client questions - find out more about your client and their needs.
33. Is your client concerned about:
 - (a) Succession planning - possibly a trust to hold assets until his children reach a certain age or achieve a certain milestone.
 - (b) Creditor protection - possibly a trust to hold certain key assets (e.g. the family home and a "rainy day" fund) in case of creditor claims.
 - (c) Probate - holding shares in an offshore company would require offshore probate on your client's death. If the shares were held in a simple trust, no probate would be required - saving many months and many thousands of dollars in fees.

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