A serious talk about the future

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"We need a serious talk, like what mummy says when she has to explain to the kids why daddy is going to be in the papers the next day". – Malcolm Tucker "The Thick of It"

I have always enjoyed the phrases used by brokers, estate agents and others when they describe negative events in positive terms. A slump in house prices becomes a "once in a generation buying opportunity", a market crash becomes "a needed correction enabling the market to return to fundamentals, demonstrating the benefits of pound cost averaging". Bad news is only bad news when you admit it.

Then there are the code words. My personal favourite is "challenging", a wonderfully positive upbeat word, generally describing a situation so dire that the speaker cannot even begin to refer to it by name. In other words it is a "Lord Voldemort" event. On other occasions the comments are correct yet the sentence is unfinished. For example one commencing "We have many options open to us to deal with this situation" often lacks the key final words "none of which have worked before nor show any sign of being more successful this time".

There are others which need a phrasebook to assist translation. One such is "We have seen a dampening of demand" which translates as "did anyone see where our customers went?" Another is the delightful "we have been engaged in positive dialogue with our regulators" which often means "they have agreed to stop beating us with sticks and will now only be using their fists".

I will try in this article to avoid the above euphemisms. In doing so, I may appear negative however I am anything but that. It is simply a "serious talk".

The era of the "bulk buy" international business companies is over. Whether it is Delaware or anywhere, the world of people who are directors of hundreds of companies and where there are streets comprised of buildings practically built entirely of company name plates, is inevitably drawing to a close. Ultimately their demise will be missed by a few, such as the manufacturers of brass plates, but it heralds a much more interesting time.

One of the causes of this, about which much has been written in this periodical and others, is the impact of international information sharing and greater disclosure. I know the hard-core survivalists still gamely rail against it like some fur clad Montana mountain-man does against the "US Gvnrmnt poisng the wata" but that battle is over. It was a battle I had sympathies with, but unless "The Trump" makes it to the White House (in which case we have much bigger things to worry about and living on a small island in the middle of nowhere might become the safest place for you as well as your trust) the battle is lost, get over it and move on.

So, new structures must be tax transparent, fiscally efficient, flexible, cost effective and responsive to client needs. They also have to have client trust. After the horrors of recent times with rampant miss-selling by large financial institutions, trust is not a common commodity. For some, safeguarding against such risks has become the paramount goal. This presents a problem for some smaller firms established in international finance centres which are less well known and therefore, despite their excellence, have difficulty demonstrating their trustworthiness.

How can this be overcome? One route is via an effective but light touch regulatory cover. Let me illustrate using one area of significant growth, that of the family office. I am using Gibraltar as an example, it is not the only one but it is where I live and earn my income.

Virtually all family offices utilise trust structures (and/or foundations). Last year, the Gibraltar Government introduced the Private Trust Company (PTC) Act, which provides greater regulatory protection and is aiming to attract potential clients seeking to benefit from a higher level of control in the management of a trust and a safeguard against fiduciary risk.

While, previously, it was possible for any limited company to act as a trustee, provided it was not engaged in licensable activity, the PTC Act 2015 sets out a specific legislative framework within which the PTC is formally recognised and can operate. Appointing a PTC as a trustee of a trust, or group of trusts under the same family, delivers numerous benefits such as being easily integrated with other family entities such as an existing company or philanthropic organisation, with a view to:

- consolidating several family trusts under one umbrella for increased efficiency in asset management and protection;
- retaining more family control over a trust's investment and distribution decisions;
- ensuring continuity for families by resolving any trustee successor issues which may arise over the lifetime of a trust;
- providing more robust protection from fiduciary risk thereby easing liability concerns for individual family members named as trustees; and
- allowing for long-term structural and administrative flexibility, meaning that a PTC can adapt to changing family circumstances and wishes.

The registration system is voluntary, so as to avoid putting at a disadvantage those PTCs for whom the associated registration and renewal fees may be disproportionate to the size of the trust. However, there are specific requirements which must be met. For example, the company can only provide trustee services to the Designated Individual and their nuclear family - this includes spouses, civil partners, children and other remoter issue. Also, crucially, the PTC must appoint a Gibraltar-Registered Administrator and hold at least one Board Meeting each calendar year at the registered office with the Registered Administrator in attendance. The result is an attractive, light touch regime.

Opportunities for structures which meet changed needs also include the introduction of foundations where a traditional civil code product can be adapted and utilised in a common law environment. In Gibraltar, new legislation is currently in preparation, following an initiative by the Society of Trust and Estate Practitioners (STEP). Under these proposals a foundation can be set up for any purpose and can hold property in its own name. Upon transfer, any property becomes the property of the foundation by operation of the law, separate from the estate of the founder or any of the beneficiaries. It therefore has the legal personality of a company with the flexibility of a discretionary trust. It can also be redomiciled.

Furthermore it can be set up with or without beneficiaries. Beneficiaries can be granted rights but can also be deprived of all rights. Its usefulness for the family office both generally and in dynastic planning is therefore clear.

Another development gaining greater use is the Limited Liability Partnership (LLP). An LLP is not legally a partnership. It, like a company, is a corporate body with a continuing legal existence independent of its members, formed where two or more persons come together for the purposes of carrying on a lawful business, with a view to profit. Generally, partnership law does not apply to LLPs. LLPs have the legal capacity to do anything that a natural person can do and exists wholly independently of its members and changes to its membership structure. It has an open ended and indefinite existence, and will continue until it is wound up.

The LLP is a very flexible vehicle and has been primarily designed with professional service providers in mind, whose partners may potentially be at risk from the careless or accidental negligence of a colleague. However, the Limited Liability Partnership is also available in respect of any type of trade, profession and occupation business including in the family office sphere. A further benefit in Gibraltar and a number of other jurisdictions is that whatever agreement which may be in place between the members remains confidential between the members who are free to agree between themselves the terms of their relationship. The internal affairs of an LLP are ordinarily set out in an agreement. Even though the Act and the Regulations envisage that an LLP agreement will be the norm, there is no requirement for this to be in place. In lieu of having an agreement, there are a number of "default" provisions prescribed by the Regulations which apply.

Under the terms of the Act, members are given limited liability without having to issue share capital, whilst having no restriction on the number of members who may form part of an LLP. By analogy, in the case of a General Partnership, all partners are liable for its debts and obligations whereas, in the case of a Limited Partnership, limited partners are protected by limited liability provided that they do not undertake any management functions. All members in an LLP may undertake this without losing their limited liability protection. However, an LLP may also be appropriate for a partnership where some partners are not actively involved.

Unlike a conventional partnership with unlimited liability to creditors, the liability of a member is limited to that expressly provided for in the agreement. The basic principle, and frequently the driving factor of a conversion to limited liability, is that the liability of a member is limited to the assets that they put into the Limited Liability Partnership, their capital contribution and undrawn profits, unless the members have agreed otherwise.

These and similar structures elsewhere present a sophisticated solution for the needs of the new breed of clients which smaller centres are attracting. Add to this the other new products and services, such as the new opportunities for protected cell companies as the range of activities they are permitted to do increases. Add to this the development of local stock exchanges, providing fast and cost efficient ways to list debt securities and funds. Then include their potential (due to their ability to adapt swiftly to change) to support crypto currency and block chain developments and you have a powerful new array to enable these centres to resume their dominant role as innovators and facilitators in the world's financial markets.

So why is this a serious talk? In an article I wrote for *Offshore Investment* last year, I spoke of the need for the smaller international finance centres to be disruptive in the sense that Uber and modern technology have been. To be disruptive of current norms and comfort zones. This requires being at the cutting edge of areas such as block chain and the new quasi corporate structures I have described above. Such an approach is challenging and carries risk. It is a risk I believe is manageable but we must be committed to achieve our goal. In other words, we have to get serious. A "serious talk" doesn't have to be a depressing one but it has to be had.