

## Offshore trusts

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### INTRODUCTION

This briefing is intended to provide a general overview of some of the factors to be considered by clients and their advisers in the establishment of a private wealth trust in the British Virgin Islands, Cayman, Guernsey or Jersey.

This briefing is accurate as at January 2022 and should not be regarded as specific legal advice applicable for any particular circumstances. Equally it is not intended to be comprehensive in its scope and it is recommended that a client seek legal advice on any proposed transaction prior to taking steps to implement it.

A series of detailed briefings on other connected issues and in respect of individual jurisdictions have been prepared by Ogier and are available on request.

### Introduction to the trust concept

A trust is a legally binding arrangement whereby a person (known as a settlor) transfers assets to another person (known as a trustee) who is entrusted with legal title to the trust assets, not for his own benefit, but (in the context of a private wealth trust) for the benefit of other persons (known as beneficiaries, who may include the settlor) or for a specified purpose.

The terms and rules upon which the trustee is to hold the trust assets will normally be contained in a document called the trust instrument. This is for the benefit of all parties as it will ensure that the settlor, the trustee and the beneficiaries know precisely what their respective rights and duties are. The trust instrument will usually provide that the trustee has the power to manage the trust assets in accordance with the terms of the trust instrument and the governing law of the trust.

In addition to the trust instrument it is also usual for a settlor to indicate to the trustee his wishes as to the future management and disposition of the trust fund in a less formal manner.

His expression is often contained in a letter of wishes which, although not legally binding, will generally be considered by the trustee to be of persuasive effect when performing its duties (for example, considering whether to make a distribution out of the trust fund).

## **THE COMPONENTS OF A TRUST**

### **The settlor**

Once a trust is created the settlor will have divested himself of legal ownership of the trust assets. The settlor may be a beneficiary and, in certain circumstances, he may also act as a co-trustee. The settlor may also retain a degree of control over the trust by reserving the exercise of certain powers to himself (or a third person), such as the power to approve distributions, the power to appoint and remove trustees and the power to revoke the trust.

However, it is essential to the validity of a trust that the settlor actually disposes of himself of the trust assets.

### **The trustee**

Legal title to the trust assets is vested in the trustee under the obligations imposed by the trust and it is responsible for the administration of the trust. A trustee must act with due diligence, as would a prudent person, to the best of its ability and skill and must observe the utmost good faith. A trustee must exercise its powers solely for the benefit of the beneficiaries. The trust assets, however, constitute a separate fund and do not form any part of the trustee's own estate.

### **The beneficiaries**

The beneficiaries are the persons entitled to or who may benefit from the assets held on trust. As stated above, the settlor may himself be one of the beneficiaries. In order for a trust to be valid there must generally be sufficient certainty as to the identity of the beneficiaries. An express power for the addition of further persons to the class of beneficiaries may, however, be included in the trust instrument. The beneficiaries may enjoy equal or unequal benefits, as the trust instrument prescribes or, in the case of a discretionary trust, as the trustee may determine. It is also possible to include in the trust instrument a power to exclude beneficiaries from future benefit.

### **The trust fund**

The assets constituting the trust fund may be of any type of movable or immovable property (with certain exceptions in particular jurisdictions, for example land in Jersey cannot be directly

held by a Jersey trustee). Further assets may generally be added at any time after settlement of the initial assets. Indeed, a common arrangement is to establish a trust with a nominal initial amount and subsequently to add more substantial assets. These would therefore not need to be specified in the main trust deed.

### **The protector**

It is not essential for the validity of a trust that there be any protector. However, in order to counterbalance the wide discretionary and fiduciary powers conferred on a trustee it is often found useful for the settlor to appoint a trusted friend or professional advisor, or even himself, to act as a protector of the trust. In such cases the consent of the protector will generally be required before the trustee may exercise certain strategic powers under the trust instrument. On the protector's death, incapacity or resignation, his powers can be passed on to another person.

## **FORMS OF TRUST**

Various types of trust have been developed over time and the most appropriate structure for the settlement will depend on the settlor's particular circumstances and objectives. Some of the more common types of trust are described below.

### **Life Interest Trust**

Under a life interest trust (also known as an interest in possession trust) the principal beneficiary will normally be granted a vested interest in the income of the trust fund throughout his lifetime and the discretion of the trustee regarding the disposition of the trust fund will be limited. For example, the trust instrument may specify that the trustee is required to distribute all of the income of the trust fund to a particular individual during that person's lifetime and subsequently to distribute the capital of the trust fund in fixed proportions to named beneficiaries (such as the settlor's children).

### **Discretionary trusts**

The discretionary trust provides maximum flexibility and is often the most efficient structure for both settlor and beneficiaries. Under the terms of a discretionary trust the trustee is given wide discretionary powers as to when, how much and to which beneficiaries it should distribute the income and capital of the trust. Such a form of trust is useful where at the time of creation of the trust the future needs of beneficiaries cannot accurately be determined. The beneficiaries are not regarded as having any direct legal rights over any particular portion of the trust fund but only a right to be considered to benefit when the trustee exercises its discretion.

## **Revocable trusts**

Although for tax and other reasons it is generally desirable for a trust to be constituted as an irrevocable settlement, in certain circumstances the settlor may require the additional comfort of knowing that he has retained the power to revoke the trust and enforce the return of the trust fund. Any of the above trusts can be drafted on a revocable basis. However, careful consideration should be given to the possible consequences of a revocable trust because, under the jurisdiction of the settlor's domicile, residence or nationality, revocation may negate some of the expected benefits of creating the trust.

## **Reservation of powers**

Although once a settlor creates a trust he is deemed to have divested himself of legal ownership of the trust assets, a settlor may wish to reserve for himself certain powers. This type of trust is often referred to as a "reserved powers trust". Most commonly, settlors will wish to reserve powers in the area of investment. Other powers that can be reserved (or granted to someone else) include the powers to revoke, vary or amend the terms of a trust or any trusts or powers arising wholly or partly under it, to advance, appoint, pay or apply income or capital of the trust property or to give directions for the making of such advancement, appointment, payment or application, to appoint or remove any trustee, enforcer, protector or beneficiary, and to change the proper law of the trust.

## **Charitable purpose trusts**

Generally, in order for a trust to be valid there must be identifiable beneficiaries. In brief, the onerous duties imposed upon trustees are owed to the beneficiaries and without ascertainable beneficiaries who may enforce these duties against the trustees a trust will not be upheld. A long held exception to this general rule has permitted trusts to be established in favour of charitable purposes. In such instances a representative of the state is tasked with the role of enforcing the trustee's duties and obligations.

## **Non-charitable purpose trusts or STAR trusts**

Many offshore jurisdictions (including Jersey, Guernsey and the British Virgin Islands) have amended their legislation to permit the creation and enforcement of non-charitable purpose trusts, ie trusts in which property is held by trustees on trust to carry out specific purposes which do not qualify as charitable purposes. This new type of trust is often simply referred to as a "purpose trust". All the usual rules for trusts apply save in two respects.

First, the trust instrument must set out the particular purpose or purposes for which the trust has been established.

Second, the trust instrument must provide for a person whose duty it is to enforce the trust in relation to its non-charitable purposes. This person is called the "enforcer" and must be a person different from the trustee or trustees. Although an enforcer may be likened to a protector, the role of an enforcer is essentially quite different. Non-charitable purpose trusts enable the fulfilment of purposes which are not charitable in the strict sense but are, or may be, beneficial or philanthropic in a wider sense. Important commercial advantages may also be obtained by the use of such trusts.

Cayman has gone further with provisions introduced in the Special Trusts (Alternative Regime) Law 1997 (now incorporated in the Trusts Law (2017 Revision)). "STAR trusts" (as they are known) may be established for charitable or non-charitable purposes but can also have named beneficiaries (together with, or in place of, the purposes). STAR trusts fall outside of the Cayman perpetuity rules and so can exist indefinitely.

The regime provides that no beneficiary under a STAR trust has any right to take court proceedings to enforce the accountability of the trustee or any right to be involved in, or informed about, the conduct of the trust and that all rights of that description are to be the exclusive concern of an "enforcer" - a person or persons chosen by the settlor. This ability to disempower beneficiaries, coupled with the ability to set up STAR trusts with beneficiaries (and no purposes) provides a powerful alternative to a typical discretionary trust.

In Jersey and Guernsey it is acceptable to have trusts for both purposes and for beneficiaries.

S84 of the BVI Trustee Ordinance (1/11/1993) applies to BVI purpose trusts created 1/3/2004 S84A was then enacted and effective from 1/3/2004 and updated by BVI Trustee Amended Act 2013.

### **BVI VISTA trusts**

The Virgin Islands Special Trusts Act 2003 (as amended) created a special trust (known as a "BVI VISTA trust") in the British Virgin Islands. A VISTA trust is used purely for the holding of shares in a British Virgin Islands Business Company, although this company can of course hold other assets, and enables a trustee holding such shares to distance itself entirely from the management of the company in which the shares are held. Where the trust instrument contains a provision applying VISTA, the trustee will hold the shares "on trust to retain", and this duty will take precedence over any duty to preserve or enhance the value of the shares. The responsibility for managing the company lies with the directors and the directors only (although the trustee may be given limited powers for appointing or removing directors and the trust deed can provide for circumstances when it will be required to intervene in the company's affairs).

Such legislation circumvents the ongoing problem in other jurisdictions with regard to trustees'

liability in relation to such high-risk assets as private family company shares.

BVI VISTA trusts may be particularly well suited to the holding of family companies, and high-risk investments such as art collections. They can also be useful to hold a portfolio of investments when the settlor wishes to retain investment power.

## **USES OF OFFSHORE TRUSTS**

The range of uses to which a trust may be put is still being developed, but flexibility and confidentiality are the principal advantages that a trust has over other legal forms designed to hold, preserve and transfer wealth. The trust concept has proved to be enormously adaptable and is widely used in financial planning.

Such is the flexibility of a trust that it would be difficult to define its potential uses comprehensively, but some typical applications are explained below.

### **Preservation of wealth**

Trusts may be used to preserve the continuity of ownership of particular assets, such as a business, within a family. By vesting legal ownership of the assets in the trustee, the relevant individuals may be able to continue to benefit from the assets, whilst avoiding fragmentation of ownership amongst a large number of second- and third-generation beneficiaries. The use of a trust may avoid, on the death of a beneficiary, the risk of a share of assets becoming owned outside the family, and thus enables settled assets to be preserved intact for the benefit of future generations.

### **Forced heirship**

Where a settlor properly disposes of assets during his lifetime by settling them on trust, the trust assets will not form any part of the settlor's estate upon his death. This may enable a settlor to avoid forced heirship rules which may be mandatory under the laws of his domicile, residence or nationality and which would otherwise dictate the persons to whom and proportions in which a settlor's estate will devolve.

Jersey, Guernsey, BVI and Cayman laws all provide that (with certain limited exceptions) a lifetime transfer of assets to a trust governed by their law will not be set aside under that law because it defeats a person's rights under the forced heirship rules of another jurisdiction.

### **Succession planning**

The effect of a trust is to divest the settlor of ownership of the settled assets. Accordingly, upon

the death of a settlor there will be no need to obtain a grant of probate or similar formalities in order to deal with the trust fund. A trust therefore provides an efficient vehicle for the transfer of beneficial ownership interests on the death of a settlor. Further, because the interests of a beneficiary under a discretionary trust will not constitute a separate asset, a trust structure may mean that stamp duty or inheritance taxes that would otherwise be payable on the death of a beneficiary will not apply. In addition, a trust can be used to hold shares in a company owning immovable property, rather than directly in the real property itself, with the effect of transforming characterisation of an interest from immovable to movable, which can present attractive opportunities for tax and financial planning. A trust may also be used to protect financially unsophisticated beneficiaries and to make financial provisions for the improvident.

### **Asset protection**

Historically some trusts have been established for protecting assets from risk. In a modern context, trusts may be employed to hold assets in a secure and stable political environment. The use of a trust in conjunction with an underlying company can be used to convert an onshore asset into an offshore one and to interpose an additional layer of confidentiality in a chain of ownership. The use of the trust and company combination may also enable trust assets to be held in a jurisdiction that does not recognise the trust concept. Such an arrangement may be attractive to a lender for the purpose of obtaining security against assets. Trusts can also safeguard assets against strategic risks, such as confiscation or expropriation by the state in the country of the settlor's domicile, residence or nationality. As a further protection, a modern trust instrument can provide for the proper law of the settlement to be moved to another jurisdiction in the event of political or strategic emergency in the country of the trustee's residence.

Trusts can also be used to help protect assets against the potential future liabilities of a settlor or beneficiary, including, in some circumstances and with appropriate advice and structuring, those arising as a result of divorce proceedings.

### **Commercial trusts**

The variety of means to which a trust may be put in the commercial context has only been partly realised. Offshore trusts have been used for many commercial purposes including the following:

- as a unit trust for the collective investment of capital;
- in Eurobond issues, the interests of investors may be regulated pursuant to the terms of a debenture trust deed;
- in off-balance sheet transactions, the share capital of an "orphan" special purpose vehicle may be held by a trustee under the terms of a purpose trust;

- in an inter-creditor agreement, the rights of one creditor group may be subordinated to the rights of other creditors and regulated under the terms of a subordination trust forming part of the overall security package;
- asset securitisation schemes have been structured to provide for mortgages and receivables to be held pursuant to the terms of a trust; and
- employee share option and executive incentive schemes (as well as regular pension schemes) will benefit from being established in a politically stable, fiscally neutral jurisdiction.

## **CREATION OF A TRUST**

It is preferable for a trust to be created by the execution of a formal written instrument so that all parties will know exactly what their respective rights and duties are. Trusts created in writing may be effected either by a settlement signed by both the settlor and the trustee, or by a declaration of trust signed by the trustee alone. Following execution of the trust instrument a trust will come into existence upon settlement of the initial property, which may be supplemented later. Lawyers in the Ogier group are able to assist with preparation of all of the appropriate documentation.

## **CHOICE OF DOMICILE - POLITICAL AND ECONOMIC STABILITY**

### **British Virgin Islands**

The British Virgins Islands is a British Overseas Territory with a strong constitutional relationship with the UK. It is responsible for its own internal self-government, most notably in relation to taxation. The British Virgin Islands has an independent legal system based largely on that of the UK, with most law derived from English common law, and the final appeal remains to the Judicial Committee of the Privy Council. The British Virgin Islands has developed into a well-established jurisdiction for financial services as a result of the government's commitment to business.

### **Cayman**

The Cayman Islands is a British Overseas Territory and although a governor is appointed by the British government there is a large measure of internal self-government. However, the British government retains responsibility for internal security, defence, external affairs and the appointment of certain public officers, including judges.

The Cayman Islands has a well-developed and experienced court system which has been tested with large commercial cases, including the massive BCCI liquidation. The final court of appeal is

the Judicial Committee of the Privy Council in London and it is common practice for counsel from the UK to appear before the Cayman Islands courts on major litigation matters. Caymanian legislation dealing with commercial matters is specifically relevant to its role as an offshore financial centre and the general law is derived from English common law.

## **Guernsey and Jersey**

Guernsey and Jersey do not form part of the United Kingdom. Each is a self-governing dependency of the British Crown. By constitutional convention established over some 500 years, each jurisdiction has complete autonomy in all matters of internal government, including taxation. The legal systems are separate but similar, derived in part from the customary laws of Normandy but strongly influenced by English law in company, commercial and trust matters. The Judicial Committee of the Privy Council remains each jurisdiction's ultimate court of appeal.

Prior to the UK's departure from the European Union (the EU), the Jersey and Guernsey's relationship with the EU was set out in Protocol 3 of the UK's 1972 Accession Treaty. The Islands' relationship is now enshrined in our membership of the UK-EU Trade and Cooperation Agreement, which was reached prior to the end of the Transition Period on 31 December 2020.

## **INTEGRITY AND REPUTATION**

Jersey, Guernsey, BVI and Cayman are all highly regulated jurisdictions, where all professional trustees offering services to the public are required to be licensed.

## **TAX NEUTRALITY**

### **British Virgin Islands**

British Virgin Islands trusts are exempt from all British Virgin Islands taxes provided that no beneficiaries are resident in the Islands and that the trust does not conduct any business or own any land in the jurisdiction.

### **Cayman**

There are no corporation, capital gains, income, profits or withholdings taxes in the Cayman Islands. Moreover the government may give an undertaking that no taxes will be imposed in the Cayman Islands for a fixed number of years. The period of the undertaking depends on whether a company, partnership or trust is used and will usually be renewed at the end of such period.

There are no exchange controls; the local currency is tied to the U.S. dollar, which is freely accepted and used within the local economy.

## Guernsey and Jersey

Where all of the beneficiaries of a Guernsey or Jersey trust are resident outside of Guernsey or Jersey respectively, the trust will be exempt from assessment both in respect of Guernsey or Jersey income tax on income arising outside the Island and income on bank deposit interest arising inside Guernsey or Jersey. For practical purposes, therefore, the trustee may make distributions out of a trust fund established in Guernsey or Jersey without any withholding or deduction for income tax. There is no inheritance, wealth, gift or capital gains tax or equivalent forms of indirect taxation charged on the creation or transfer of assets to a trust. In this respect Guernsey and Jersey trusts may differ from trusts created under the laws of other jurisdictions, such as Bermuda and Liechtenstein.

In some circumstances there may be taxes arising in another jurisdiction on the transfer of assets into a trust, or distributions out of it, so where necessary appropriate tax advice should be sought. For some trusts, the European Savings Directive may also be applied.

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Ogier is a professional services firm with the knowledge and expertise to handle the most demanding and complex transactions and provide expert, efficient and cost-effective services to all our clients. We regularly win awards for the quality of our client service, our work and our people.

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## Meet the Author



[Matt Guthrie](#)

Partner

Guernsey

E: [matt.guthrie@ogier.com](mailto:matt.guthrie@ogier.com)

T: [+44 1481 752342](tel:+441481752342)

## Key Contacts



James Campbell

Partner

Jersey

E: [james.campbell@ogier.com](mailto:james.campbell@ogier.com)

T: [+44 1534 514230](tel:+441534514230)



Catherine Moore

Partner

Guernsey

E: [catherine.moore@ogier.com](mailto:catherine.moore@ogier.com)

T: [+44 1481 752364](tel:+441481752364)



Anthony Partridge

Partner

Cayman Islands

E: [anthony.partridge@ogier.com](mailto:anthony.partridge@ogier.com)

T: [+1 345 815 1810](tel:+13458151810)

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