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Guernsey private trust companies and foundations

Service area / Trusts and Private Wealth
Legal jurisdiction / Guernsey
Date / May 2022

Introduction

Private trust companies ("PTCs") have been widely used in international structured finance transactions for many years and they are now increasingly being used by high net-worth private clients, who prefer to establish their own PTC to act as the trustee of their family trusts rather than transferring assets to an offshore professional trustee company.

With the introduction of foundations as an alternative type of structure to companies, the trustee can be formed as a private trust foundations ("PTF") instead of a PTC, offering increased choice to the client.

To help guide this choice, this briefing note considers key issues relating to the establishment and use of a PTC or a PTF in the context of private wealth management. References to "PTVs" are to both PTCs and PTFs.

Regulation

The Regulation of Fiduciaries, Administration Businesses and Company Directors, etc (Bailiwick of Guernsey) Law, 2020, as amended (the "Fiduciaries Law") is the principal legislation which regulates Guernsey's trusts and corporate service providers. Amongst other things, it requires any person who carries on, by way of business, certain regulated activities in or from within the Bailiwick of Guernsey, including the provision of trust and foundation services, to be licensed by the Guernsey Financial Services Commission (the "Commission") under the Fiduciary Law.

The Commission issued updated guidance in November 2021 that a PTV may be acting by way of business even if it is merely acting as a conduit and paying fees on to a third party.

In order to avoid any doubt over whether it requires a licence to conduct its activities a PTV may apply to the Commission for an exemption from the requirement to obtain a licence provided:

- it acts as trustee only in respect of a specific trust or connected trusts;
- it does not advertise or market its services to the public;
- it is administered by a company which is itself licensed under the Fiduciaries Law; and
- the licenced administrator of the PTV confirms to the Commission that it will retain sufficient knowledge and information about the PTV's ownership and control structure and about its activities to be satisfied that:
  - the PVC is effectively administered and governed; and
  - the PVC complies with relevant laws and regulatory requirements.

This may be achieved for example by the provision of a director on the board of the PVC or the provision of an authorised signatory, along with close monitoring and oversight of the PVC.

A one off fee is payable with the application. If successful, operational and cost advantages for the PTV in securing an exemption from the Commission can include the following:

- when an exemption is given there are no annual fees to pay and no requirement to capitalise the PTV in a particular way;
- there is no requirement to submit to the Commission copies of documents in relation to the trust or trusts in respect of which the PTV is to act as trustee; and

- a PTV is not a "financial services business" for the purposes of Guernsey's anti-money laundering legislation and there is no requirement for a PTV to make annual returns to the Commission in relation to its activities or to have a dedicated money-laundering or compliance reporting officer.

Licensed fiduciary record-keeping

Under the Fiduciaries Law, the Commission may request a licensed administrator of a PTV to provide certain information in respect of the PTV, including beneficial ownership information on the PTV itself, its directors or councillors, its controllers, and on the settlor, beneficiaries and protector (if any) of the trust(s) of which the PTV is trustee. This requirement applies whether the PTV holds a licence issued by the Commission or holds an exemption from the need to hold one, and whether the PTV acts by way of business or not.

PTC

The ownership structure of a PTC

As an alternative to a company limited by shares, a PTC may be incorporated as a company limited by guarantee. Membership interests in a company limited by guarantee may be held by the individual establishing the trust (the "settlor") or members of the settlor's family where this is appropriate.

Where a PTC is constituted as a company limited by shares the shares may be owned in a number of different ways depending on tax considerations and the settlor's circumstances. The principal options are set out below.

Individual

Whilst it is possible for an individual, such as the settlor or a member of the settlor's family (or his/her nominee), to be the shareholder of a PTC, such an arrangement can give rise to concerns upon the individual's death.

One concern is practical and relates to probate requirements in respect of the individual ownership of the PTC's shares. The second concern relates to succession and the suitability of those person(s) to whom the PTC shares devolve upon the individual's death.

Purpose Trust

In view of the problems associated with ownership by an individual of the shares of a PTC, a PTC is usually an 'orphaned' structure so that its ownership is not attributable to any particular person.

The shares of a PTC are therefore often held under the terms of a charitable or non-charitable purpose trust (the "Purpose Trust"). Where there is doubt about whether a charitable purpose trust will be used for genuine charitable purposes, a non-charitable purpose trust may be used.

If a Guernsey non-charitable purpose trust is used, an enforcer must be appointed to enforce the stated purpose of such trust. The enforcer must be a separate entity from the trustee of a non-charitable purpose trust. The enforcer does not need to be licensed by the Commission if it is not acting as an enforcer by way of business. For example, a family member could act as the enforcer, although thought should be given to succession if that is the case.

The trustee of the Purpose Trust (the "Trustee") may be unconnected with, and located in a different jurisdiction, from the administrator of the PTC. The division of roles in this way may assist with separating out the respective rights and responsibilities within the structure.

Foundation

A foundation can be established with the sole object of holding the shares in a PTC.

A foundation is incorporated on the instruction of a founder and like a company has its own legal personality and can exist indefinitely. However, unlike a corporate structure, a foundation is neither owned by the founder or by anyone else. Therefore ownership issues will not arise in the context of a foundation.

If a foundation is used, a guardian must be appointed to ensure that the purpose of the foundation is carried out. The guardian need not be licensed by the Commission if the guardian is not acting as guardian by way of business. For more about foundations see paragraph 4 of this guidance note.

Incorporating a PTC

A PTC can be incorporated with or without limited liability in any part of the world and is usually incorporated using standard private company memorandum and articles of incorporation (or the equivalent). Its name cannot include any reference to trusts or trustees although it may use the initial PTC in its name.

Composition of the board of directors

The choice of the board of directors of a PTC is a key issue. The settlor may wish to control the composition of the board of directors and/or may wish to be a member of the board so that the settlor participates actively in the decisions made by the PTC in relation to the underlying trusts and their assets.

Control of the board of directors can be structured through the constitutional documentation of the PTC and/or through the terms of the Purpose Trust, which holds the shares of the PTC. It may be that the Trustee is required under the terms of the Purpose Trust to seek the approval of the settlor or a nominated other, such as a protector or the enforcer (in the case of a non-charitable purpose trust), in relation to the appointment or removal of directors of the PTC. Alternatively, the Trustee could be required to follow the directions of the settlor, the protector or the enforcer (in the case of a non-charitable purpose trust)in relation to the composition of the PTC's board of directors.

Whatever structuring and mechanisms are used in relation to the appointment or removal of directors (and indeed other aspects of the management of the affairs of the PTC), a

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prevailing issue for advisers to the settlor, the Trustee and the PTC is for the settlor to understand how the balance of power will work in practice so that there are no surprises for the settlor, or indeed other family members, once the structure has been established and is in operation.

The directors should be selected based on knowledge and experience although selection is also likely to be influenced by tax considerations and the protection of privacy. Concern can arise if one or more of the directors of the PTC is resident in an unfavourable tax jurisdiction and adversely affects the location of the PTC's management and control or even the tax residence of the underlying trusts or the tax situs of the assets in those underlying trusts. Issues may also arise if a director is subject to domestic legislation which can be used to obtain detailed information about the PTC, its underlying trusts and their assets.

Where family members participate as directors, conflicts of interest need to be managed and this can be addressed in the constitutional documentation of the PTC, for example by regulating voting rights on decisions which could raise concerns where the personal interests of a director could conflict with the interests of the PTC during the course of its business.

As a matter of Guernsey company law, if none of the directors of a Guernsey PTC is resident in Guernsey then the PTC will require a Guernsey licensed fiduciary to act as a resident agent to hold the PTC's records in the jurisdiction.

Directors' liability

One reason for the increased use of PTCs in Guernsey results directly from the abolition of the statutory guarantee which was historically imposed upon trust company directors under the Trusts (Guernsey) Law, 2007 (as amended). As a result of the abolition, the risk of personal liability under Guernsey law has been reduced significantly and therefore lay directors, such as family members, are more willing to act as directors.

Some judicial discussion has taken place about the liability of a director of a trust company and whether "dog-leg" claims are sustainable under Guernsey law. "Dog-leg" claims are based on the notion that the duties owed by a director to a company may, in certain circumstances, be regarded in law as an 'asset' of the trust of which the company is trustee. Whilst such claims have not been ruled out as legally untenable, they are certainly very difficult claims to construct and pursue.

Insofar as there are concerns about possible personal liability on the part of directors of the PTC, this can be addressed through the provision of appropriate director and officer insurance.

Using a PTF

Legal personality

A Guernsey foundation has legal personality but does not have shareholders. It holds assets in its own name on behalf of beneficiaries or particular purposes, or both. A Guernsey foundation cannot carry out any commercial activities. These attributes make it an ideal vehicle to act as a PTF. A PTF which is established in Guernsey must have a guardian whose role is to ensure that the purpose of the foundation is carried out.

Establishing a PTF

A PTF may be established in any part of the world which has legislated for the establishment of foundations. A Guernsey PTF comes into being upon its constitutional documents (the Charter and the Rules) being registered on the Guernsey Register of Foundations. A Guernsey PTF's name cannot include any reference to trusts or trustees but may contain the initials PTF.

Composition of the council

A Guernsey PTF is managed by a council comprised of at least two councillors, unless the constitution allows a single councillor. The settlor may wish to control the composition of the council and/or may wish to be a member of the council so that the settlor actively participates in decisions made by the PTF in relation to the underlying trusts and their assets.

Control of the council can be structured through the constitutional documentation of the PTF.

Whatever structuring and mechanisms are used in relation to the appointment or removal of councillors (and indeed other aspects of the management of the affairs of the PTF), as in the case of a PTC a prevailing issue for advisers to the settlor and the PTF is for the settlor to understand how the balance of power will work in practice so that there are no surprises for the settlor, or indeed other family members, once the structure is in operation.

The councillors should be selected on the basis of their knowledge and experience although selection is also likely to be influenced by tax considerations and the protection of privacy. Concern may arise if one or more of the councillors of the PTF is resident in an unfavourable tax jurisdiction, which residence adversely affects the location of the PTF's management and control or even the tax residence of the underlying trusts or the situs of the assets in the underlying trusts. Issues may also arise if a councillor is subject to domestic legislation which can be used to obtain detailed information about the PTF, its underlying trusts and their assets.

As is the case for PTCs, where family members participate as councillors, conflicts of interest need to be managed and this can be addressed in the constitutional documentation of the PTF, for example by regulating voting rights on decisions which could raise concerns where the personal interests of a councillor could conflict with the interests of the PTF during the course of its business.

As a matter of Guernsey foundation law, if none of the councillors of a Guernsey foundation is a Guernsey resident then the PTF will require a Guernsey licensed fiduciary to act as a resident agent to hold the PTF's records in the jurisdiction.

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Councillors' liability

Insofar as there are concerns about possible personal liability on the part of councillors of the PTF, this may be addressed through the provision of appropriate insurance.

Settlor involvement

Whether the PTC is structured as a foundation or a company, settlor involvement in the PTV can be achieved in several different ways and, dependent upon tax advice, that involvement usually takes one or more of the following forms. The settlor could be involved:

- as the person vested with reserved powers under the terms of, and/or the protector of, the underlying trusts of which the PTV is trustee;
- as a member of the board of directors of the PTC;
- as a member of the council of the PTF;
- as a member of an investment committee established to consult with the board of directors or the council (as the case may be) of the PTV regarding certain significant decisions affecting the underlying trusts, such as investment policy or the sale of family businesses;
- as protector or enforcer (in the case of a non-charitable purpose trust) of the Purpose Trust which holds the issued shares of the PTC;
- as guardian of the foundation which holds the issued shares of the PTC; and/or
- as guardian of the PTF.

The settlor could also own the shares or membership interests in the PTC but this may have undesirable tax and succession consequences.

Operation and funding of a PTV

The licensed fiduciary which provides administrative services to the PTV will need an adequate and timely flow of information about the nature and conduct of the PTV's business in order to provide its services and support the PTC in its activities. The mechanism by which information is provided by the directors or councillors in respect of the PTV's activities to the administrator is generally a practical matter and varies between service providers.

Where a director of or from a licensed fiduciary is appointed to the board of the PTC or the council of a PTF he or she will wish to ensure that the PTV is acting in a manner which accords with the terms of the underlying trusts of which the PTV is trustee, that professional advice is sought where appropriate and that proper records are kept of the decisions taken by the PTV.

If there is a desire in due course to switch the administration of the PTV to a different service provider (or indeed to a different jurisdiction) this can, subject to the terms of the documentation in place, be easily achieved by terminating the administration agreement and putting a new one in place with the new service provider.

Changing the Trustee should also be straightforward given the limited assets (namely, the issued shares of the PTC) held by the Trustee.

If the PTC is an 'orphaned' structure, thought must be given to the way in which the PTC will be funded. Similar considerations apply to the funding of a PTF. It is often preferable, where possible, for a structure to be self-sufficient financially (so it can be kept in good standing). To achieve this, the PTV needs to be sufficiently capitalised (if a PTC) or endowed (if a PTF) or be able to discharge its running costs from the underlying trust(s) by, for example, invoicing for trustee services.

Family awareness

Family awareness of the PTV and the manner in which the structure as a whole is intended to operate is also a key issue for a settlor. One way of communicating the settlor's wishes is to agree a family charter which provides a formal statement of the role, investment principles and philanthropic intentions of the PTV structure which is established.

A family charter can encourage a uniform approach to the family's affairs from beneficiaries and other participants, such as non-family directors of the PTC or non-family councillors of the PTF (as the case may be), thereby reducing the scope for dispute amongst family members at a future date.

Tax treatment of a PTV

Whether the PTV is structured as a foundation or a company, the tax treatment of the PTV will be the same in Guernsey. This is because for the purposes of taxation, foundations are treated like companies in Guernsey. Accordingly, the PTV will be regarded as tax resident in Guernsey if it is incorporated as a company, or registered as a foundation, in Guernsey. A foreign established PTV could also be regarded as tax resident in Guernsey if its central management and control is in Guernsey. In either case, assuming the PTV does not have any taxable income of its own (as opposed to income generated in the trusts(s) of which the PTV is trustee) the PTV should not be liable to tax in Guernsey.

Tax filings of a PTV

With the exception of economic substance requirements, a PTV has the same obligations as a PTC in respect of tax filings. Accordingly, the PTV will be required to file an annual tax return including accounts, which in practice should be relatively straightforward given that the PTV's activity would be restricted to being the trustee of the underlying trusts and that any income in the PTV itself (as opposed to the income in its underlying trusts) is defrayed in covering its ongoing costs and third party expenses.

Where the PTV which is tax resident in Guernsey meets the criteria to be classified as a financial institution for the purposes of the OECD's Common Reporting Standard (the "CRS") as implemented in Guernsey the PTV will have certain reporting obligations under the CRS in respect of natural persons who hold, or are controlling persons, of entities that hold interest in the PTV and are resident in a jurisdiction that

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has also adopted the CRS, unless a relevant exemption applies. The PTV will also be obliged to gather due diligence materials in respect of those individuals and be required each year to report certain information in relation to those individuals to Guernsey's Revenue Service in the prescribed format. That information may then be transferred to the tax authorities of other CRS participating jurisdictions in accordance with applicable international exchange arrangements.

If the PTV does not meet the criteria to be classified as a financial institution for CRS purposes, then the PTV will be classified as a non-financial entity, and as such will not in itself be required to comply with CRS reporting and due diligence obligations, but may be required to provide a self-certification of its status, including details of, and due diligence materials relating to any controlling person holding interest in the PTV, together with supporting due diligence, to a financial institution at which the PTV holds a financial account.

The US version of CRS, FATCA, follows the same approach as the CRS, although the terminology used is different. Under FATCA, a PTV will be either a foreign financial institution or a non-financial foreign entity. Essentially, the classification, due diligence gathering obligations and the reporting obligations are the same as under the CRS, where reportable persons are either residents or citizens of the US for the purposes of tax reporting under FATCA.

Economic substance

Guernsey's economic substance requirements do not apply to foundations, whether established in Guernsey or elsewhere.

Whilst in principle Guernsey's economic substance requirements apply to companies that are tax resident in Guernsey, they only apply to those companies carrying on certain activities that bring the company within scope of economic substance rules. Acting as a trustee is not in itself an activity that falls within the scope of economic substance requirements. If the PTV were to conduct other activities that bring it within scope, this would be a matter for which specific advice would be required.

Conclusion

Guernsey's legal, regulatory and tax framework, together with the resident administration expertise, makes Guernsey an excellent choice for establishing a PTV.

A PTV provides a flexible and relatively portable way in which to arrange bespoke trustee services. A PTV offers a convenient platform from which family members can participate in a meaningful way in the management of underlying assets.

A PTV may be of benefit in relation to reducing cost and improving protection from fiduciary risk. It may also be of use where the choice of licensed fiduciaries is limited due to the nature of the underlying assets (e.g. trading companies).

Particular care needs to be taken with regard to the initial structuring of the PTV. It is critical that the rights, powers and responsibilities vested in particular parties are fully understood (particularly during the lifetime of the settlor and in the future) and Carey Olsen's experienced team of fiduciary lawyers can guide the parties through this.

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