

## **PALLADIUM GUIDE TO BRITISH VIRGIN ISLAND TRUSTS**

### **1. Introduction**

Palladium's principals offer their services to you not only with drafting any kind of British Virgin Island trust but also with acting as trustee, wither through its British Virgin Island private trust company or through its sister trust company incorporated in New Zealand.

British Virgin Islands trusts are still the world's foremost choice of trust for the internationally spread high net worth family and the jurisdiction's reputation for excellence and professionalism in the trust industry is still unparalleled.

The general principles of British Virgin Islands trust law are derived from those of English trust law. The principles of both English common law and equity, as supplemented by British Virgin Islands statute, are applicable. The original British Virgin Islands Trustee Act (the "Act"), which was based on the English Trustee Act 1925, has now been updated by the Trustee Amendment Act 1993 (the "Amendment Act") which became law on 1 November 1993.

Most of the provisions of the UK Recognition of Trusts Act 1987 have been extended to the British Virgin Islands so that the majority of the provisions of the Hague Convention on the Law Applicable to Trusts and on Their Recognition apply to British Virgin Islands trusts.

Prior to 1 November 1993, trust deeds and subsidiary trust documents had to be registered and filed in accordance with the requirements of the British Virgin Islands Registration and Records Act, but the Amendment Act has now exempted the following from registration and filing:

- all deeds creating trusts;
- all deeds of appointment made pursuant to the terms of a trust; and
- all other deeds executed by trustees, settlors and beneficiaries pursuant to the powers and discretions specified in the instrument creating a trust (including deeds and documents executed before 1 November 1993).

**Note:** When considering setting up a British Virgin Islands trust, in addition to obtaining advice from a qualified British Virgin Islands practitioner, a prospective settlor should always obtain legal and tax advice from advisors in his country of domicile, residence and nationality, as well as in the jurisdiction where the beneficiaries are resident and where assets which are proposed to be placed in trust are located.

### **2. The Meaning of a Trust**

The Amendment Act states that the term "trust" refers to

"the legal relationship created, either inter vivos or on death, by a settlor when assets have been placed under the control of a trustee for the benefit of a beneficiary or for a special purpose"

and states that a trust will have the following characteristics:

- (a) the assets constitute a separate fund and are not part of the trustee's own estate;
- (b) title to the trust assets stands in the name of the trustee or in the name of another person on behalf of the trustee; and
- (c) the trustee has the power and the duty in respect of which he is accountable to manage, employ or dispose of the assets in accordance with the terms of the trust and the special duties imposed on him by law.

The reservation by the settlor of certain rights and powers, and the fact that the trustee may himself have rights as a beneficiary, are not necessarily inconsistent with the existence of a trust.

A British Virgin Islands trust is not a separate legal entity (although the International Business Companies Act specifies that for the purposes of that Act, a trust may be "a person"), rather it denotes a contract between the trustees and beneficiaries (amongst others) in relation to predetermined property.

Those not familiar with the concept of a trust may be concerned that the transfer of the ownership of their property to trustees may afford them with little protection. It is, however, a basic rule of trust law that the trustees of a trust must obey the provisions of the trust instrument with respect to both the entitlements of the beneficiaries and the trust's administration. The beneficiaries of a trust are protected by a robust body of legal rules imposing very strict duties on the way in which trustees administer trusts. Indeed, if the trustees do not observe these rules, a beneficiary may apply to the Court for an order compelling them to do so.

Trust law also imposes "fiduciary duties" on trustees so that they may only benefit from the trust, and charge fees, to the extent that the trust instrument permits them to do so. Any other benefits received must be passed on to the beneficiaries. Trustees are not permitted to deal with trust assets for their own direct or indirect advantage and must not only exercise all the powers conferred upon them in the best interests of the beneficiaries, but must act prudently in the management of trust property. Beneficiaries are also entitled to be provided with copies of the accounts of the trust.

If a settlor wishes to have the power to replace the trustees with other trustees this can be retained by him or conferred on a protector in whom various specified powers can be vested for the beneficiaries' protection. (For further information on Protectors, see paragraph 13 below.)

### **3. The Use of Trusts**

By means of a trust, the legal title to assets passes to the trustees who will hold them on behalf of the beneficiaries until the assets are finally distributed to them. A trust can, and often does, last a number of generations.

Trusts can therefore be used, amongst other things, for the following purposes:

- to mitigate or avoid tax;
- as an instrument of estate planning;
- to avoid disruption on death;

- to protect assets (for example, from exchange control or other government interference);
- for the protection of the weak and to preserve family wealth against dissipation;
- to circumvent forced heirship provisions which prevail in 26 out of the 27 nation states in the EU – only the UK does not have forced heirship rules;
- as a confidential way of holding assets;
- to run an individual's business or to own shares in a company;
- to benefit charitable and non-charitable purposes; and
- as a flexible way in which to hold assets.

#### **4. Trusts Governed by British Virgin Islands Law**

A British Virgin Islands trust is a trust governed by British Virgin Islands law. The Amendment Act provides that a trust instrument may expressly provide that the trust's governing law is that of the British Virgin Islands. If there is no such statement in a trust instrument, its governing law will be that of the jurisdiction that may reasonably be inferred from the terms of the trust as being its governing law. If no such reasonable inference can be drawn from the trust instrument, the trust's governing law will be the law with which the trust is most closely connected, with reference in particular, to the following factors:

- the place of administration of the trust as designated by the settlor;
- the location of the assets of the trust;
- the place of residence or place of business of the trustees; and
- the objects of the trust and the places where they are to be fulfilled.

The Courts of the British Virgin Islands will have jurisdiction in relation to a trust whose governing law is stated to be that of the British Virgin Islands, even if it has no other real connection with the British Virgin Islands (and regardless of where the trustees, settlor or beneficiaries are resident). The British Virgin Islands Courts will also have jurisdiction where:

- the trustee of the trust is resident in the British Virgin Islands;
- any corporate trustee is incorporated or registered to do business in the British Virgin Islands;
- any trust property is situated in the British Virgin Islands (but only in respect of such British Virgin Islands property);
- the administration of the trust is carried on in the British Virgin Islands; or
- the British Virgin Islands Court thinks it appropriate.

#### **5. Migration of Trusts**

The governing law of a trust may be changed to that of another jurisdiction, but only where:

- there is express power enabling this to be done in the trust instrument; and
- the new jurisdiction recognises the validity of the trust and the respective interests of the beneficiaries.

The governing law of a trust may similarly be changed from the law of a foreign jurisdiction to that of the British Virgin Islands. In this case, however, there is no corresponding requirement that the law of the jurisdiction from which the trust is changed must recognise the change.

A trust instrument may also allow for an automatic transfer and vesting of assets from one trustee to another trustee in a different jurisdiction upon the occurrence of certain events (for example, the introduction of exchange controls, etc.).

## **6. Who may be a Settlor?**

Any individual of sound mind over 18 years of age may be a settlor of a British Virgin Islands trust. Depending on the powers conferred upon it by its constitution or by-laws, a corporation may also be a settlor. In addition, persons other than the original settlor may contribute property to the trust fund (unless they are precluded from doing so by the terms of the trust instrument).

A trust may be established by way of:

- a unilateral Declaration of Trust, executed by the trustees only (leaving the settlor anonymous); or
- a Deed of Settlement executed by both the settlor and the trustees.

If a unilateral Declaration of Trust is executed, it is prudent for the settlor to execute a separate Deed of Declaration so as to ensure that the trust is properly constituted.

## **7. Who may be Trustees?**

Any individual, being an adult of sound mind may be a trustee. For a British Virgin Islands company to be a corporate trustee, it may either obtain a licence to carry on trust business under the British Virgin Islands Banks and Trust Companies Act or it may do so as a private trust company. A corporate trustee may act alone or jointly with an individual or individuals.

In relation to trusts created after 1 November 1993, a decision of the majority of the trustees will be binding, subject to any contrary provision in the trust instrument. Trust instruments may also provide for the exercise of any of the trustees' powers to be reserved by a managing trustee. The effect of this is that none of the other trustees will be liable for a default by the managing trustee in relation to the exercise of such powers.

## **8. What property may be subject to a British Virgin Islands Trust?**

Property of all descriptions, wherever located, may be subject to a trust (unless the property is "inalienable" or is land situated outside the British Virgin Islands and the trust's terms are inconsistent with the laws of the country or state in which the land is located. British Virgin Islands land and mortgages may only be held in trust if the provisions of the Non-Belongers Land Holding Regulation Act are satisfied). The following, in particular, can normally be made subject to a trust:

- cash;
- investments such as shares, debentures, etc.;
- debts and other liabilities;
- copyright and other intellectual property;

- interests in trusts and other equitable interests;
- chattels such as jewellery, furniture and other valuables; and
- land and buildings (subject to the above caveats).

Trusts are often established with only a nominal contribution to the trust fund (for instance, a cash sum of US\$100), with more substantial property being added subsequently by a Deed of Addition.

## **9. Who may be Beneficiaries?**

The following may be beneficiaries of a British Virgin Islands trust:

- all individuals (including unborn persons, minors and persons of unsound mind);
- a corporate body capable of holding property;
- a settlor;
- a trustee;
- charitable organisations and purposes, and
- (since 1 November 1993) non-charitable purposes (for further information on Non-Charitable Purpose Trusts, see paragraph 10.4 below).

## **10. Types of Trusts**

### **10.1 Discretionary trusts**

Most British Virgin Islands trusts tend to be discretionary trusts. These are trusts in which the distribution of capital and income between beneficiaries is at the discretion of the trustees, with the result that no beneficiary is entitled to call on the trustees to distribute capital and income. If the terms of the trust allow it, the trustees may not be obliged to pay out capital or income to any of the beneficiaries for the entire perpetuity period of the trust (for further information on Perpetuity Periods, see paragraph 11 below).

A trust's income may be accumulated for the whole of the period of the trust's duration unless the trust instrument specifies that there is to be a shorter accumulation period. The class of beneficiaries is generally defined with reference to a wide class of persons born within the perpetuity period, although it may include corporations, charitable organisations and/or purposes. Power is generally conferred on the trustees to add further beneficiaries at a later date and to remove beneficiaries from the class of current beneficiaries.

In view of the extent of the discretion conferred upon the trustees, a settlor will generally provide the trustees with a non-binding letter setting out his wishes on matters such as distributions and the investment of the trust fund. The trustees are obliged to consider such wishes and will generally act in accordance with them, if they are reasonable and practicable in the prevailing circumstances.

### **10.2 Fixed trusts**

These are trusts under which a beneficiary is entitled to the income from the whole or a fixed share of the trust fund regardless of whether he will also become entitled to a fixed share of the capital of the trust fund (for example, on attaining a specified age or on the happening of a particular event).

Settlements may change from one category to another during their existence and it is possible for settlements to be both fixed and discretionary.

### **10.3 Charitable trusts**

Fixed or discretionary trusts may be set up to benefit charitable purposes or organisations. Such trusts are not subject to the rule against perpetuities (see paragraph 11 below) and may last indefinitely. Charitable purposes include:

- the relief of poverty;
- the advancement of education;
- the advancement of religion; and
- any other purpose benefiting the public.

The purposes of such trusts must be exclusively charitable and must come within the legal definition of a benefit to the public.

### **10.4 Non-charitable purpose trusts**

By virtue of the Amendment Act, a British Virgin Islands trust (a “purpose trust”) may be created for any purpose, whether or not charitable, provided that the purpose is specific, reasonable and possible and not immoral, contrary to public policy or unlawful. The purpose trust must not be one which is for the benefit of particular persons or of some aggregate of persons ascertained by reference to some personal relationship.

A purpose trust must have at least one trustee who is a “designated person”. The following persons are designated persons:

- a barrister or solicitor practising in the British Virgin Islands;
- an accountant practising in the British Virgin Islands who qualifies as an “auditor” for the purposes of the Banks and Trust Companies Act, 1990;
- a licensee under the Banks and Trust Companies Act, 1990; or
- such other person as the Minister of Finance may, by order, designate.

In addition, the purpose trust instrument must:

- (a) appoint a person to enforce the trust (the “enforcer”) and provide for the appointment of a successor to such person. The enforcer must either be a party to the trust instrument or consent in writing to the designated trustee enforcing the trust;
- (b) specify the event upon the happening of which the trust will terminate; and
- (c) provide for the disposition of the surplus assets of the trust (if any), upon its termination.

Purpose trusts may be created for purposes which are partly charitable and partly non-charitable (provided they satisfy the requirements set out above) as well as for purposes which, although generally accepted as philanthropic, do not satisfy the legal definition of a

charitable purpose (for example, a trust promoting a political agenda). Purpose trusts are increasingly used commercially to hold shares in companies where the primary intention is to retain the shares rather than to benefit any individuals. In this context, it is essential that a genuine purpose should be stated in the trust instrument and that funds should actually be applied for the said purpose.

A British Virgin Islands purpose trust may exist in perpetuity.

#### **10.5 Resulting and Constructive trusts**

Trusts known as “resulting trusts” will arise when a person to whom assets have been transferred is required by the principles of equity to hold such assets on trust for the transferor (or for the person who provided the funds for the transfer) or his estate.

A “constructive trust” is one which arises by operation of law and not as a result of the intention of the parties. Such a trust occurs when a person holding property does so in circumstances in which in equity and good conscience the property should be held or enjoyed by another. As a result, the courts will compel him to hold that property on trust for that other person.

Resulting and constructive trusts are outside the scope of this guide. Please contact Palladium Corporate Services directly if you require further information on these.

#### **11. The Perpetuity Period**

This is the period which determines the maximum duration of the trust. By law, all trust assets must “vest in interest” by the end of the perpetuity period. This means that before the perpetuity period expires all the persons who will share in the trust fund and the shares that they will take must be fixed and determined, so that no element of contingency or uncertainty remains.

Since 1 November 1993 it is possible for the perpetuity period to be a fixed term not exceeding 100 years. It is also still possible to define the perpetuity period as one commencing on the date of the trust’s creation and ending 21 years after the death of the last survivor of a class of persons alive at that date. The class named as “lives in being” need have no connection with the trust. Trust instruments often define the perpetuity period with reference to the descendants of King George VI of England alive at the date of the trust instrument.

The Amendment Act has also introduced “wait and see” provisions and other provisions alleviating the rigidity of the common law rules relating to perpetuity and remoteness of vesting.

## **12. The Trust Instrument**

The trust instrument sets out the terms of the trust and the trustees' powers. Although the Trustee Act contains general provisions with respect to trustees' powers and duties, these are rather restrictive. A trust instrument will usually, therefore, expressly provide the trustees with wide powers of administration and investment, as well as detailing the procedures relating to the retirement of trustees and appointment of new trustees.

Trustees are now specifically permitted by statute to invest any portion of the trust funds in any kind of investment, wherever the investment is situated, and to make changes to investments. The trustees are required to exercise these powers using the diligence and prudence of a reasonable man. These statutory powers are subject to any contrary provisions contained in the trust instrument. The trust instrument should also specify if the trust is to be irrevocable. If not, it should contain provisions setting out the manner in which its terms can be revoked or amended.

The Amendment Act contains a schedule of commonly used administrative provisions and standard powers which can be incorporated into British Virgin Islands trusts by reference.

## **13. Protectors**

A trust instrument may contain provisions relating to the appointment of a protector of the trust (or a similar person referred to by some other name) and the appointment of a successor protector. The instrument may specify that certain powers conferred upon the trustees (such as powers to advance capital and income to beneficiaries) may only be exercised with the protector's consent and may confer upon the protector the power to remove trustees and replace them. The protector may also be specifically empowered to exclude any beneficiary as a beneficiary of the trust and to include any person as a beneficiary of the trust in substitution for or in addition to any existing beneficiary.

The Amendment Act gives statutory recognition to the office of protector. Now, where a trust instrument provides that exercise of trustees' powers and discretion is subject to the protector's previous consent, and if such consent is obtained, the trustees cannot be held liable for any loss caused by their actions.

A protector may now exercise certain specified powers in relation to a trust. Unless the trust instrument provides otherwise, he shall not, however, be deemed to be a trustee and will not be liable to the beneficiaries for the bona fide exercise of such powers. The powers in question are:

- determining the jurisdiction whose law shall be the governing law of the trust;
- changing the forum of administration of the trust;
- removing trustees and appointing new and additional trustees; and
- withholding consent from specified actions of the trustees either conditionally or unconditionally.

On setting up a trust, it is advisable for the settlor to prepare a memorandum specifying whether the powers which have been conferred on the protector have been conferred upon him in a fiduciary or

personal capacity, the reason for his appointment, and how the settlor would expect him to exercise his powers.

Typically, a protector will be someone wholly separate from the settlor and beneficiaries of the trust and is nearly always a trusted friend of the settlor or a professional protector. Palladium's protector entity can act as a protector to trusts also.

#### **14. Exclusion of Forced Heirship Provisions**

In relation to transfers and dispositions made after 1 November 1993, British Virgin Islands law now provides that a settlor or any person domiciled outside the British Virgin Islands who transfers or disposes of personal property to a trust, is deemed to have the capacity to make such disposition or transfer if at the time of the disposition or transfer he was of full age and sound mind according to the laws of his domicile.

No rule in force under the law of a person's domicile relating to inheritance or succession shall affect the validity of the transfer or disposition or otherwise affect the validity of a trust. This provision applies to both lifetime and testamentary transfers and dispositions

#### **15. Asset Protection**

As a matter of British Virgin Islands law, any conveyance (other than a conveyance for value to a bona fide purchaser without notice), made with intent to defraud creditors is voidable at the instance of any persons thereby prejudiced.

#### **16. Applications to the Court for Guidance**

Any trustee is able to apply to the British Virgin Islands Court for its opinion, advice or directions on any question relating to the management or administration of a trust.

### **Why set up a trust in the British Virgin Islands?**

#### **A Political and economic stability**

The British Virgin Islands is a British Overseas Territory with a long history of political stability. The Government consists of a British appointed Governor, who is the representative of Her Majesty the Queen, and 13 constitutionally elected members of a Legislative Council. Elections are held at least once every 4 years. The legal tender of the British Virgin Islands is the US Dollar. There are no exchange controls in the British Virgin Islands.

#### **B Taxation**

Provided that a trust does not own land or carry on a business or trade in the British Virgin Islands:

- \* the income of the trust in the hands of a trustee will be exempt from income tax;

- \* any beneficiaries not resident in the British Virgin Islands will be exempt from British Virgin Islands income tax on payments received by them from the trustees of British Virgin Islands trusts;
- \* no estate tax, inheritance tax, succession tax, gift tax, rate, duty, levy or other charge is payable by beneficiaries who are not resident in the British Virgin Islands in respect of any distribution to them by the trustee of any trust; and
- \* any trust that does not have beneficiaries resident in the British Virgin Islands will be exempt from stamp duty in respect of the trust instrument and all other deeds and instruments will be exempt from stamp duty.

All British Virgin Islands trust instruments executed after 1 February, 1994 are liable to a trust duty of US\$50.

### **C Confidentiality**

There are no longer any filing or registration requirements for trust instruments, ancillary trust documents, trust returns or accounts in the British Virgin Islands; nor does a trust's name have to be approved. As mentioned above, the terms of a trust can be set out in a Declaration of Trust so that the settlor's name does not appear in the document.

### **D A Pre-Eminent Offshore Financial Centre**

The popularity and success of its International Business Companies Act has placed the British Virgin Islands in the forefront of locations for offshore company incorporation. The jurisdiction has a reputation for integrity, flexibility and responsiveness to the interests of the financial services industry. Pursuant to the terms of the Banks and Trust Companies Act, 1990, and Financial Services Commission Act, a Director of Banking and Fiduciary Services has been appointed to ensure the proper administration of companies carrying on trust business from within the British Virgin Islands. In order to maintain the integrity of the jurisdiction, the British Virgin Islands was swift to pass its own Proceeds of Criminal Conduct Act in 1997.

A branch of the Society of Trust and Estate Practitioners (STEP) was formed in the British Virgin Islands in 1997. The Branch, which is very active, provides a forum for professionals to discuss trust law and assists in maintaining practitioners' standards by way of education and training.

**IMPORTANT NOTE: SEE NEXT PAGE**

**This article must not be relied on by anyone settling a BVI trust as each trust must take into account of the individual circumstances of the settlor on each occasion.**

**If you would like further information on British Virgin Islands Trust law or details of how Palladium can help you with your trust enquiries, please contact Palladium.**

Palladium Corporate Services LLP provides a range of services in jurisdictions across the globe including: corporate services, trust and fiduciary, fund and legal services in the BVI and Anguilla.

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