Key advantages of the Cayman Islands' unique STAR trusts

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or many years, the Cayman Islands has been the jurisdiction of choice for establishing trust arrangements. Its laws are perhaps the most commonly used internationally, and the very fact that it is the choice that underlies financial investment vehicles holding billions of dollars in assets all over the world demonstrates the faith placed in it by experts and investors.

The trust law of the Cayman Islands is founded on the principles of English common law, with the benefit of many of the statutory modifications made in England and some unique to the Cayman Islands.

The first Cayman statutory modifications were introduced in 1967, based mainly on those introduced in England in 1925. Later modifications have been skilfully made to ensure Cayman Islands law meets the needs of the modern client, while not trying to be so innovative that aspects of it might be viewed by foreign courts as having dubious effect or validity. The principle behind reform has been to limit modifications to those that do not offend the principles of traditional trusts law and that will be respected by the courts and authorities of most other jurisdictions. The result is a body of statutory provisions and case law that is the envy of the world.

Cayman legislation is backed by a highly regarded judiciary whose decisions have established significant case law, followed in many jurisdictions. Cayman has an abundance of high-calibre professionals, including lawyers and accountants, to ensure there is no shortage of professional assistance. In addition, many leading banks and financial institutions that conduct trusts business have a Cayman trust company or licensee available for clients, to ensure the all-important nexus between the governing law of the trust arrangements and the location of the trustee is preserved.

Cayman Islands institutional trustees are regulated by the Cayman Islands Monetary Authority, and the strict licensing and management requirements imposed on corporate trustees ensure internationally recognised industry standards are maintained.

Among the statutory modifications introduced in the Cayman Islands, there is no legislation that might be interpreted as inappropriately protecting insolvent persons from creditors, and Cayman has preserved the common international standard limitation of six years in relation to acts regarded as ‘fraudulent dispositions’ (the expression not implying any criminal intent). However, the jurisdiction has innovative legislation carefully crafted to enable clients to set up trust arrangements that may be firmly insulated from the claims of persons under foreign laws imposing forced-heirship and other property rights, and also from the claims of capricious and indolent beneficiaries or others.

The Cayman Islands was the first jurisdiction to introduce legislation to allow the establishment of non-charitable purpose trusts, under the STAR regime. A unique element of the STAR regime is the ability to mix trusts for non-charitable purposes, charitable purposes and persons within the same structure, arguably providing, for example, the most innovative foundation for the establishment of philanthropic structures of any jurisdiction. Cayman also, uniquely, has an ‘exempted trust’ regime, under which trusts can be registered and offered an undertaking that no taxes will be charged on them from within the Cayman Islands for 50 years, even if the jurisdiction were to introduce direct taxes affecting trusts (currently there are none). Both the STAR and exempted trust regimes can also be used to restrict rights to information, and to place enforcement rights in a third party.

These are only a few advantages of setting up trust arrangements in the Cayman Islands. Many of the world’s wealthiest individuals have done so, especially those with philanthropy in mind, placing their faith in the laws and well-regulated fiduciary marketplace. A crucial aspect of planning for the internationally mobile wealthy client is finding a jurisdiction that is not only well regulated, with sound but innovative legislation to assist with modern planning, but that also has an impeccable reputation among governments and regulators around the world. The Cayman Islands is just such a jurisdiction.

Nigel Porteous is Chairman of STEP Cayman Islands and the Global Head of Maples and Calder’s Trusts and Private Client Practice

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The trust sector, supported by STEP, plays a key role in the Cayman Islands’ financial services industry and, thus, the Cayman Islands’ economy. Contributing to our multi-billion-dollar GDP, and also adding to our high concentration of professionals per capita, trusts are one of the reasons why Cayman is a leading international financial centre.

To maintain and enhance that position, the 2015 agenda for the Cayman government includes amendments and new legislation that will stimulate the trust industry, and further strengthen our stable economy.

The government is currently in discussions with industry partners – including STEP Cayman Islands, through the Cayman Islands Financial Services Legislative Committee – on amendments to its Trusts Law.

These amendments are intended to address certain historical anomalies in the original legislation that have emerged over time. The amendments will increase Cayman’s attractiveness for international trust practitioners and clients.

These trust-specific legislative developments demonstrate the value of the government’s strong working relationship with industry, which allows Cayman to efficiently identify, develop and implement legislative enhancements that strengthen its services and products.

More legislative amends
The government’s slate also includes the development of two significant pieces of financial services legislation that will enhance our jurisdiction overall. First, we are modernising Cayman’s intellectual property regime, through enhanced copyrights and trademarks protection. In accordance with the outcomes of international research, we expect a positive correlation between the strengthening of IP rights and Cayman’s economic growth.

The passage of these laws will follow several major laws or amendments that were enacted in 2014, including the Contracts (Rights of Third Parties) Law, the Mutual Funds Law, and the wholesale revision of the Exempted Limited Partnership Law, which provides a product that better manages the increasing complexity of transactions undertaken in the Cayman Islands.

Operationally sound
While our legislative approach is indeed proactive, the government is also fully aware that the operations supporting our laws must be exceptionally strong to deliver total value for our clients. With that in mind, Cayman has made important improvements in technology.

The General Registry has received overwhelmingly positive feedback regarding the Cayman Online Registry Information Service (CORIS). Subscribers to CORIS have the benefit of tracking their submissions and easily retrieving documents, but perhaps the biggest benefit to industry is that, by going paperless, our companies registry has significantly reduced turnaround time.

Our financial services industry regulator, the Cayman Islands Monetary Authority
Cultivating relationships that last

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Think global. act local: Wayne Panton

(CIMA), has also announced technology upgrades: the first phase of the Regulatory Enhanced Electronic Forms Submission system, known as REEFS, is now being piloted. Rollout is expected later this year. This new online system will give CIMA analysts more time for financial oversight and review.

**Finances in fine fettle**
In addition to legislation and operations, the strength of a jurisdiction is demonstrated by the health and stability of its public finances. Because the government has had the courage to make tough, yet correct, decisions, Cayman continues to operate with a fiscally prudent budget, and, just as importantly, our current financial position provides a sound platform for future growth.

In pointing out our fiscal stability, I note that this government has kept its pledge to the financial services industry not to introduce new fee increases, and that we are considering rolling back several fees that were introduced in the past.

That said, Cayman has been able to carefully manage its revenue streams and move towards meaningful budget surpluses. Our projected operating surplus of USD128 million for the 2014-2015 budget year is supported by forecasts that show steady growth, and surpluses are expected to reach USD168.3 million in 2017-2018. Consistent surpluses allow Cayman to have sufficient cash balances to meet required cash reserves.

This financial stability lets the government pursue various infrastructure projects, such as the expansion of Grand Cayman’s international airport, the establishment of a cruise berthing facility, and the implementation of waste-to-energy technology.

**Information exchange**
Turning to global matters, Cayman’s significant work in the area of exchange of information (EOI) for tax purposes has resulted in an extensive network of more than 70 information-exchange relationships, all of which are in line with the global standard. This network includes partners covered by the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters, as well as 35 bilateral agreements.

Last October, we joined representatives from more than 50 countries and jurisdictions in signing the OECD Multilateral Competent Authority Agreement (MCAA), which sets the worldwide standard for the automatic exchange of information among tax authorities.

The strength of our EOI position is based on our consistent global engagement in these matters over decades, as a result of which Cayman has experienced reputational benefits. Because of its efforts, Cayman was designated ‘largely compliant’ in the November 2013 rankings of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum). The UK and the US were also rated as largely compliant.

Furthermore, Cayman continues to be a member of the OECD Peer Review Group, and the 19-jurisdiction Steering Group of the Global Forum. We also are privileged to be vice chair of the Peer Review Group.

Cayman’s engagement in international regulatory initiatives also includes agreements with the US and UK under the US Foreign Account Tax Compliance Act; participation since 2005 in the EU Savings Directive; and membership through CIMA in the Offshore Group of Banking Supervisors; Working Group on Cross Border Banking; Caribbean Group of Banking Supervisors; and the Association of Supervisors of Banks of the Americas.

Based on our legislative and regulatory framework, it’s clear that Cayman is a progressive jurisdiction. The government has a strong track record for thinking globally and acting locally, in response to international financial services initiatives.

**Beneficial ownership**
We are applying this same process to the subject of beneficial ownership. Following a period of international public consultation, on 30 December last year the government published a report stating that we will continue our current method of providing beneficial ownership information to law-enforcement, tax and regulatory authorities through corporate service providers.

Our stance is validated by the fact that Cayman’s regime is firmly in line with the G20’s High-Level Principles on Beneficial Ownership Transparency, issued in November 2014. In other words, we align with principles that the G20 countries themselves uphold as the standard. Cayman’s current system is also consistent with the global standard, as defined in the Financial Action Task Force Recommendations. Nevertheless, we will honour the pledge we made in our beneficial ownership consultation report, in that we will further improve our regime. In light of the evolving international discussions currently taking place, Cayman has identified specific steps – including enhancing the accuracy, accessibility, availability, and monitoring and enforcement of ownership information – that will further strengthen our beneficial ownership framework.

**Bright future**
With our legislative achievements and developments, operational efficiencies, fiscal stability and international engagement, Cayman is confidently poised to become an even stronger international financial centre.

One of the key reasons for this confidence is the strength of our professional corps. I noted earlier that Cayman has one of the highest concentrations of professionals per capita in the world. In fact, according to 2012 data from our Economics and Statistics Office, we have more than 560 lawyers, 900 accountants, 200 STEP practitioners and 110 certified financial analysts living in our islands. We are fortunate to attract top talent to our shores, many working for the world’s leading firms in law, accounting and corporate services.

While we are understandably proud of what Cayman has achieved through collaboration between government and industry, we reserve special recognition for the professionals who work in Cayman’s financial services; they are a key differentiator for our jurisdiction.

With this firmly in mind, the government acknowledges the contributions of STEP Cayman Islands to the professional and economic development of our jurisdiction. We look forward to continuing our strong relationship with STEP, for the advancement of the trust sector and for the edification of Cayman as an international financial centre.

Wayne Panton is the Cayman Islands’ Minister for Financial Services, Commerce and Environment

Wayne Panton
Families from Latin America (LATAM) face myriad challenges when it comes to estate planning. Some of these challenges stem from the peculiarities of the laws in their home country and where their assets are located. For example, families from LATAM are typically compelled to deal with issues such as forced heirship, community property and spontaneous changes to tax laws and reporting requirements. Many wealthy families from LATAM must also contend with US federal tax issues, which often arise when either a family member is or becomes a US person or a family member acquires property located in the US. Through the use of appropriately tailored tax- and estate-planning structures, these issues can be adequately addressed.

Behind the firewall
There are numerous international financial centres throughout the world, many of which aim to fulfill the needs of private clients and families from LATAM. The Cayman Islands, for example, stands out as one of the most suitable jurisdictions for the establishment of estate-planning and business-succession structures for many LATAM families. The Cayman Islands is not only one of the largest financial centres in the world, but there are also many sophisticated professionals working in the jurisdiction in both the trust and banking businesses. It also has favourable trust laws and a highly regarded legal system.

While there are numerous laws in the Cayman Islands that are beneficial to a person from LATAM who wants to create a trust, one significant advantage to using the Cayman Islands as a jurisdiction for trusts is the existence of its so-called ‘firewall’ legislation. In short, this type of legislation purportedly enables a person to achieve their estate-planning goals under the auspices of Cayman Islands law, as opposed to the local law in their home country, which may otherwise prohibit that from happening. A frequent example of this arises in the context of forced heirship. Forced heirship essentially provides for a mandatory system of inheritance for a person’s property upon their death, with particular relatives (typically the person’s spouse and children) inheriting a specified portion of the person’s assets outright and free of trust. The intended effect of the Cayman Islands firewall legislation is to put the settlor of the trust in a position to be able to freely dispose of their property, unfettered by any testamentary mandates prescribed by the laws of another jurisdiction.

Another advantage to using the Cayman Islands as a jurisdiction for trusts is its proximity to LATAM, which could be an important benefit. Although routine trust administration can usually be dealt with by telephone or email, it may be necessary or desirable to have meetings in person. Although this is particularly the case after the occurrence of a major event (such as the death of the settlor), it is advisable for trustees to meet in person with the settlor and beneficiaries of a trust periodically while the trust is in existence.

Cayman Islands law provides LATAM families with an array of trust options, and, for those families with members who are

Safe harbour: Hal J Webb and Alexandre M Denault explain the advantages of Cayman Islands trusts for families from Latin America
Safe harbour: Hal J Webb and Alexandre M Denault

US persons, several of those options work well together with the planning that needs to be done for the transfer of wealth from the foreign family members to the family members who are US persons. For example, a number of LATAM families have used Cayman Islands reserved-powers trusts, and some LATAM families have chosen to use a Cayman Islands private trust company (PTC) as the foundation of their estate-planning structure.

A PTC is essentially a trust company that is formed by a family and dedicated to serving as trustee of trusts created solely by members of that family. Cayman Islands PTCs are regulated or overseen by the Cayman Islands Monetary Authority. Although PTCs are not an appropriate fit for all families, a PTC normally becomes a viable option when planning for trusts that will hold assets of substantial value or special assets. While there are numerous variations in the way that a PTC can be operated and managed, Cayman Islands law is uniquely suitable for this purpose. In a typical Cayman Islands PTC structure, a Cayman Islands STAR trust is created to be the shareholder of the PTC. The PTC, in turn, serves as the trustee of related trusts, where the settlor of each trust typically reserves certain powers over the trust. The trusts themselves frequently own various forms of property, such as financial assets, real estate, business interests, art, aeroplanes and yachts, often through holding companies.

Tax protection

If a member of a family from LATAM is or becomes a US person, special provisions should be incorporated into trust documents to avoid unnecessary exposure to US federal tax of each trust typically reserves certain powers over the trust. The trusts themselves frequently own various forms of property, such as financial assets, real estate, business interests, art, aeroplanes and yachts, often through holding companies.

If a member of a family from LATAM is or becomes a US person, special provisions should be incorporated into trust documents to avoid unnecessary exposure to US federal tax issues, the trust and corporate documents will also probably need to contain provisions to address the tax issues and reporting requirements in the family members’ places of fiscal residence and the places where the assets are to be owned by the trust or an underlying company are located.

Most Cayman Islands trusts that are used for estate-planning purposes are classified as ‘trusts’ under US federal tax law. This seemingly obvious point is actually quite important from a US federal tax law perspective. LATAM families often consider forming private foundations or other similar entities as estate-planning vehicles without realising the potential pitfalls, particularly when US federal tax issues arise. The difficulty is that, under certain circumstances, foundations can be classified as corporations (as opposed to trusts) under US federal tax law. Needless to say, misclassification of an entity can lead to catastrophic US federal tax consequences. While US federal tax law does recognise the ability of a foundation to be classified as a trust, and in some cases it may be more appropriate to use a foundation instead of a trust, it is usually preferable to use an entity recognised as a trust under local law, such as a Cayman Islands trust.

The Cayman Islands has signed an intergovernmental agreement with the US to implement the US Foreign Account Tax Compliance Act (FATCA). This should generally make compliance with FATCA easier for Cayman Islands trusts with US beneficiaries.

Overall, the Cayman Islands legal infrastructure provides LATAM families with a uniquely receptive and sturdy platform on which an estate-planning and business-succession-planning structure can be built, especially when either unfavourable home country laws or US federal tax issues are involved.
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The trust law that the Cayman Islands inherited from England and Wales has stood the test of time, and provides a flexible method of holding and managing property for persons present and future. It is useful and popular – except with some tax authorities. But it does have some limitations, and it is unduly prone to litigation. So, after careful thought, Cayman has provided an alternative regime that can be adopted by a simple declaration in the trust instrument.

The STAR regime
Under the STAR regime (named after the Special Trusts (Alternative Regime) Law, 1997), any obligation may be annexed to property by transferring the property to a trustee on the terms of a trust instrument that tells the trustee what it must do with the trust property. That is what the STAR law means when it says that the objects may be ‘persons or purposes or both’. The trustee may be given a single task or several tasks, to be carried out simultaneously or successively.

These tasks may involve distributions to particular people or they may involve other kinds of benefits. They may be philanthropically motivated, to benefit the public or a section of it. But none of these are requirements – the tasks need not be beneficial to anyone. The tasks may be of a commercial nature – e.g. to use the trust property to make a loan or to repay a loan; or to carry out a business plan; or to provide security for obligations. For both private and commercial clients, this trust obligation is usually to be preferred to a contractual commitment.

If the settlor of a STAR trust wants to give powers to beneficiaries or protectors, they can give any task to the power-holder, just as with the trustee.

The settlor of a STAR trust does not need to worry that there is an overriding obligation to act in the interests of beneficiaries, or that the court may reach a different view of what is in the interests of beneficiaries. The overriding obligation of a STAR trustee is to carry out the stated tasks.

Other advantages
STAR trusts are not subject to the rule against perpetuities. Nor are they subject to the same strict rules about certainty of objects; the trust instrument can provide its own mechanism for resolving uncertainties.

STAR law enables settlors to tailor or even exclude the rights of beneficiaries to receive trust accounts and information, and also to confer such rights on non-beneficiaries. Correspondingly, the settlor can modify or exclude rights of enforcement and confer such rights on non-beneficiaries. Among other things, this enables settlors to provide for alternative dispute resolution, through mediation or by arbitration.

Unsurprisingly, STAR trusts are very popular, and the lack of litigation suggests they are less prone to difficulties and disputes.
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Super structures

Christian Stewart surveys sophisticated Cayman Islands trust structures for the family firm

A Cayman Islands private trust company acting as trustee of several family discretionary trusts – one for each branch of the family and each governed by the Cayman STAR regime – can offer a very sophisticated structure to support the effective long-term governance of a family firm.1

The three-circle model

When a trust is being designed to own or control a family firm, the three-circle model should be used as a framework for designing the trust and even for considering the right kind of trustee.2 The three-circle model explains that a family firm is a complex system comprising of a ‘family circle’, an ‘ownership circle’ and a ‘business [or management] circle’. Because of the complexity, conflict can be expected. From a trustee’s perspective, family firms are risky assets – only one-third survive into the second generation and only 10 per cent make it to the third generation.

The three-circle model holds the key to increase the chances of family firm success

A checklist for trust structure design

When one or more discretionary family trusts are being designed to own a family firm, certain key points, covered by the following checklist, should be factored into the overall design of the structure:

MANAGEMENT

- Management should ideally be based on competence.
- Compensation and promotions should be based on merit and performance.

more formalised governance structures, policies and processes intended to:

- clarify the boundaries between family, ownership and business issues;
- ensure there are communication and decision-making forums for each of the three circles; and
- ensure there is a balance between the competing interests of (i) family and business, and (ii) ownership and business.3

Two very important concepts in the continuity of family firms are: first, that governance structures, policies and processes have to be designed based on, and in a manner that is congruent with, the unique culture, dynamics and skills of the specific business-owning family;4 and, second, emotional commitment.

Emotional commitment means that family members who are not engaged in the management of the business (those who are ‘outside’ the business) are willing to continue to provide ‘patient capital’ for the business and are willing to support the family’s continued ownership of the business. Emotional commitment means ensuring that family members who are outside the business have a voice, there are meaningful roles for them to participate in, they are educated to be effective owners and they are ‘free to go’ if they wish.

The three-circle model holds the key to increase the chances of family firm success
CEO/MANAGING DIRECTOR
If the CEO or managing director is a family member, they should be someone who knows how to:
► hold themselves accountable for their performance;
► cultivate family emotional commitment; and
► listen to the family stakeholders before making a decision.

COMPANY BOARD
The company board should:
► be supportive of the CEO, and hold the CEO accountable;
► include non-family, non-executive directors;
► act as a ‘balancing point’ between the interests of the ‘outside beneficiaries’ and the ‘inside beneficiaries’;
► have a way to communicate with the family member beneficiaries;
► ensure that succession is being addressed;
► ensure that there is an agenda of planning for and creating policies to address the typical conflicts that can arise between (i) family and business and (ii) ownership and business; and
► have its role articulated in appropriate governance documents.

THE TRUSTEE(S)
The trustee or trustees should be:
► excellent at performing the technical aspects of being a trustee;
► able to hold the company board accountable;
► able to help assess the capabilities of the individuals who are appointed to the board;
► able to help ensure that the agreed corporate governance arrangements are being complied with;
► ensure that there is an agenda of planning for and creating policies to address the typical conflicts that can arise between (i) family and business and (ii) ownership and business.

PROTECTOR COMMITTEE
While being careful not to encroach into the trustee role, and mindful that it is probably a fiduciary role, the protector committee should:
► be able to play the ‘family elder’ role and bridge the communication gap between generations within the family;
► be able to help to mediate if there are any conflicts within the family;
► ensure that the beneficiaries have their own communication forum;
► be able to act as a bridge between the beneficiaries and the trustee; and
► have its role articulated in appropriate governance documents.

THE BENEFICIARIES
Even in the case of a discretionary trust, beneficiaries should:
► view themselves collectively as the economic owners of the business;
► be emotionally committed to the business;
► respect the boundary between ownership and management;
► have a way to exit from the trust – to ‘cash out’ their interest;
► have a communication and decision-making forum; and
► have a voice in relation to the ownership-level issues for the business.

Focusing on the trustee role
Family firms are risky assets from a trustee’s perspective and the reality is that it is hard to find professional trustee companies that would be willing to meet the criteria for trustees set out in the above checklist. If you can find a professional trustee company that is willing to meet these criteria, then that trustee will be offering to provide a very valuable service. However, given the difficulty of easily finding professional trustees who are willing to take on such a role, families may instead make use of a private trust company (PTC) and design the role of the PTC and its board based on the above checklist.

If a PTC is chosen as the trustee, care has to be taken to ensure that there is substance in the operation of the PTC. The Cayman Islands offers a first-class regulatory regime for PTCs, with the ability to select between applying for a restricted trust licence for the PTC or becoming a registered PTC.

Part of demonstrating ongoing substance in the operation of the PTC will be regular board meetings for the directors of the PTC, demonstrating excellence in trust administration. However, where the trustee is a PTC – and recognising that the biggest risk to family firms is likely to be family conflict – the directors of the PTC have full freedom to set their own agendas for their meetings and to include on those agendas a regular review of progress on any work that needs to be done in implementing the kinds of policies and planning that can help to mitigate conflicts between (i) family rules and business rules and (ii) ownership and management. Where there is a PTC, its directors can view the PTC as being both (a) a trustee with trustee duties and (b) effectively a holding company, the board of which is charged with responsibility for oversight of the operating-level board.

The right to cash out
One of the advantages of using a trust to own a family firm is that the trust helps to consolidate voting control and to mitigate the impact of fragmentation of the shares. On the other hand, trust or no trust, ‘pruning the tree’ is a proven pathway to family firm continuity.
One approach is to establish separate trusts for each branch of the family – so that a compensated exit can at least occur on branch basis. If there will be multiple family trusts involved, this may be another good reason for opting for a PTC as trustee – the need for multiple, tailored family trusts for each branch can justify the costs of establishing and running a PTC structure with good substance to it.

Another reason for having separate trusts for each family branch is that it is not uncommon to find that different individuals within a family have different ownership philosophies. Some will see themselves (and the trusts set up for their family branch) as being long-term ‘stewards’ of their shares in the family business; others will see their share ownership in purely financial terms, as though the shares are just another form of investment. Stewards are likely to be motivated by such non-financial factors as family values and legacy – for example, whether the company can provide employment opportunities for their own children in the future.  

**STAR to the rescue**

While there are advantages to using trusts to own a family firm, there can also be some disadvantages with the traditional discretionary trust. One of those disadvantages has just been highlighted. In the context of family firms, it is very common to find that some of the family members who want to put their shares into trust (if not all of the family members) will have a stewardship mindset. They view their shares in more than financial terms. If they own the shares outright, a steward will want to take into account such non-financial factors as family values and their concept of family legacy in deciding how to exercise their voting rights. However, when a traditional trust owns the shares in a family firm, they are fiduciaries and must focus on the question of what is in the best interests of the class of beneficiaries as a whole.  

This is one area where the Cayman Islands STAR trust comes to the rescue, in allowing mixed person and purpose trusts to be created that can include as a purpose the continuity of a family business. 11 If the trustee is a PTC incorporated in the Cayman Islands acting as trustee of a Cayman STAR trust, with a class of discretionary beneficiaries being the members of one branch of the family, and with an overriding purpose of ensuring continuity of the family firm, then the directors of the PTC would be obliged to think about more than just the financial implications of a proposal if they were to find that a prospective investor had taken an interest in buying the family company.  

**Tailoring beneficiary rights**

A STAR trust also allows the possibility of further tailoring of traditional beneficiary rights – for example, to limit the group of beneficiaries who have the right to enforce due administration of the trust or to limit those beneficiaries who have the right to access trust information. This ability to tailor could be helpful to allow a protector committee to act in such a way as it thinks fit to further the mission and vision for the company, without being as concerned about the likely fiduciary nature of its role. 12 It could also be used to ensure that there is clarity and precision as to those family members within a particular family branch who have the right to enforce due administration and the right to information.

However, Antony Duckworth, in STAR Trusts, 13 wrote that ‘… one hopes that settlers will be carefully advised before proceeding in this way’. Likewise, from a family business perspective, while there can be benefits in avoiding the potential ‘anarchy’ of a traditional discretionary trust, this is an area where very careful planning will be required to ensure that the outside beneficiaries still have a voice, still have a forum and will still remain emotionally committed to the business. If long-term family firm continuity is a goal of the family, balance between the interests of the ownership circle and the management circle should be designed into the structure, including at the level of the protector committee.

**STAR trusts allow mixed person and purpose trusts to be created that can include as a purpose the continuity of a family business**

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1. ‘STAR’ refers to the Special Trusts (Alternative Regime) Law, 1997. 2. The three-circle model was developed by Renato TagURI and John A Davis. It is examined in detail in the STEP Advanced Certificate in Family Business Advising. 3. As each of the three circles is always changing, so the balancing act needs to be ongoing – or at least there needs to be a mechanism whereby the balance can be reset periodically. 4. See the article ‘Culture does indeed eat structure for breakfast’ by Matthew Wesley, accessible at www.thewesleygroup.com/blog 5. See ‘The Wisdom of Elders’, Christian Stewart, STEP Journal, July 2014. 6. Ownership of the PTC itself (for which there are a number of options) is outside the scope of this article. 7. See ‘Next gen stewards or inheritors?’, Christian Stewart, Campden FB, February 2010 8. An example of a hybrid trust for the purpose of continuation of a family business is referred to in STAR Trusts by Antony Duckworth (Gostick Hall Publications, 1998) at pages 69–70. 9. By limiting the group of persons who have the right to enforce the terms of the trust 10. Pages 70–71

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What should our clients be doing to reduce the likelihood of ending up in a family dispute, ensure any dispute that does arise is resolved as cost-effectively as possible, and minimise any adverse publicity for the family? It is possible to manage these risks through careful drafting and appropriate selection of the jurisdiction of the trust’s proper law.

**Jurisdictional considerations**
Planning for dispute resolution is relevant even before drafting begins. While the laws of many trust jurisdictions have much in common, the way in which those jurisdictions deal with disputes varies. When selecting the proper law of the trust, consideration should be given to:

- **Whether the jurisdiction** has a court system able to efficiently manage complex commercial disputes. The Financial Services Division (FSD) of the Grand Court of the Cayman Islands was established to handle complex commercial disputes arising out of the financial services industry, including international trust disputes. Each FSD matter is assigned to a specific specialist FSD judge, who will manage the proceedings to ensure efficient progress of the claim.

- **Whether the jurisdiction** has a significant and developed body of trust-related case law that can be relied on in future, similar cases. The *Cayman Islands Law Reports* include a number of significant trust decisions that have been cited internationally, and the substantial body of trust case law from England and Wales, and other common-law jurisdictions, is persuasive in the Cayman Islands.

- **Whether advocates from** outside of the jurisdiction are allowed to conduct hearings and trials. It can be a problem in certain jurisdictions for outside counsel to be admitted and to conduct the advocacy at trial, which may prevent a party from having their choice of advocate. In Cayman, it is a straightforward process for specialist expert advocates (such as London QCs) to be admitted for particular cases, with the admission effected at a short pre-hearing or by videoconference.

- **Whether there is robust ‘firewall’ legislation** in place. Firewall legislation serves to protect offshore trusts from attack by the application of foreign heirship or matrimonial rights. Cayman was the first to introduce such legislation, and the statutory provisions have been robustly applied by the Cayman courts. Cayman’s legislation is far-reaching and requires all questions relating to Cayman trusts to be determined according to Cayman Islands law. It also precludes the recognition or enforcement of a foreign judgment that is inconsistent with the firewall protections enshrined in the legislation.

- **How easy (and cheap)** it is for trustees to seek guidance from the courts where an issue arises in the administration and management of the trust. In addition to a common-law right to invoke the court’s supervisory jurisdiction, a Cayman trustee has a statutory right to apply to the Cayman court, without instituting suit or needing to seek leave to serve foreign beneficiaries.
In the Cayman Islands, various cases provide clear legal authority for the position that properly drafted no contest clauses are valid, enforceable and not contrary to public policy.

out of the jurisdiction, for an opinion, advice or directions on any question regarding the management or administration of the trust assets. The Cayman court has construed this statutory right very broadly and, accordingly, a trustee may seek the court’s guidance whenever faced with a momentous or problematic decision in conducting the affairs of the trust.

Drafting considerations

NO CONTEST CLAUSES

Given the impossibility of preventing family disputes, it is important when drafting a trust instrument to ensure provisions are included to prevent the trust from being drawn into a family dispute, or to protect the trust assets if the trust does become embroiled. That is the idea behind ‘no contest’ clauses. A no contest clause is often included in a lifetime trust. At its simplest level, it operates to forfeit the interests of a beneficiary who is involved in a challenge to that trust, theoretically motivating that beneficiary to undertake careful consideration before commencing a challenge.

From a trust law perspective, a no contest clause has the potential to come into conflict with the core duties of the trustee, and the beneficiary’s right to enforce the trusts of a settlement if the trustee failed to discharge those duties. It also has the potential to be considered void for public policy reasons (the public policy requirement being that one should not seek to preclude a challenge before the court on justifiable grounds).

In light of the above, there is considerable doubt in some jurisdictions as to the validity and enforceability of no contest clauses. In the Cayman Islands, the case of AN v Barclays Private Bank and Trust (Cayman) Ltd and Others,1 and the more recent case of AB Jnr and Another v MB and Others,2 provide clear legal authority for the position that properly drafted no contest clauses are valid, enforceable and not contrary to public policy.

As a result of the judicial support afforded to these clauses in the Cayman Islands, their use is now widespread and they are common features of modern Cayman trusts.

STAR TRUSTS

The Special Trusts (Alternative Regime) Law, 1997 (which gives us the name ‘STAR trust’), now incorporated into Part VIII of the Trusts Law (Revised), introduced STAR trusts into the law of the Cayman Islands. They are unique to the Cayman Islands.

STAR trusts are a form of special trust that can be used as a non-charitable purpose trust or beneficiary trust. In a dispute-resolution context, STAR trusts are notable for allowing the settlor to remove the beneficiaries’ rights to information and beneficiaries’ enforceable rights of action against the trustee. Instead, the settlor appoints an ‘enforcer’ and that enforcer’s duty (in most cases) is to enforce the terms of the trust.

In cases where a settlor is concerned about future family disputes, it is often prudent to use a STAR trust, rather than an ordinary trust.

ARBITRATION CLAUSES

In common with most jurisdictions, litigation remains the principal method for resolving disputes in Cayman. This is partly because of the accommodating approach shown by the Cayman courts to parties that require confidentiality or flexible timetables. However, as general awareness and appreciation of alternative dispute resolution mechanisms grow, settlers are increasingly including arbitration clauses in their trusts.

Resolving a dispute through arbitration offers the benefit not only of confidentiality and flexible timetables, but also the ability to minimise the possibility of jurisdictional challenges, satellite litigation and successive appeals. It also allows the parties to select their own arbitrator according to expertise in the relevant area.

In the Cayman Islands, the Arbitration Law, 2012 introduced a modern, flexible, framework for arbitration, based on the United Nations Commission on International Trade Law (UNCITRAL) Model Law, and some aspects of the equivalent UK law.

The Arbitration Law, 2012 imposes a duty of confidentiality on the parties, and the proceedings are conducted in private. There is no public record of arbitral proceedings or public statements of the parties’ respective positions, nor any public hearings or reported judgments. The definition of what constitutes ‘confidential information’ is broad, and includes all documents and evidence produced for the purposes of the proceedings, notes or transcripts of the proceedings, rulings and awards made by the arbitral tribunal, and information relating to findings. Disclosure of confidential information is only permitted if authorised by the parties or in the case of certain limited public interest exceptions, and the parties and the tribunal must take reasonable steps to prevent the unauthorised disclosure of information by third parties.

Of course, arbitration is only appropriate for the resolution of certain disputes between parties and cannot replace sanction hearings or Beddoe-type relief. Moreover, the lack of ability to appeal may be considered a disadvantage to the process.

Conclusions

George Bernard Shaw wrote that ‘a happy family is but an earlier heaven’. Unfortunately, when a settlor finds that all is not happy within the family, it is often too late to introduce protections into existing structures. While clients may hope that their families are and will remain happy, we, as advisors, need to plan for a time when all is not well. In doing so, we are able to implement structures that are robust in the face of challenge and that may even prevent that challenge in the first place.

1. See RBS Coutts (Cayman) Ltd v W and Others [2010] (2) CILR 348
2. [2007] WTLR 565
3. Unreported, 18 December 2012
Wealthy individuals have been investors in collective investment vehicles for many years. Often they are seed investors whose investment provides a fund manager with sufficient mass to launch a fund, or they could just be one of many investors investing alongside other wealthy individuals and institutions.

The turmoil in the financial markets in recent years has presented unprecedented challenges to collective investment vehicles and, therefore, to wealthy individuals as equity holders. Investors suffered huge losses, valuations were suspended, and redemptions were suspended or limited via the imposition of ‘gates’. Wealthy investors realised that their level of wealth or relationship with the manager did not in itself give them preferential treatment; they could not be paid in priority. Wealthy investors were left disillusioned by the limited amount of information they received and by the lack of influence they had over service providers.

As a result, there has been an increased drive among wealthy investors for collective investment vehicles to be structured in a way that focuses on their interests, not those of other investors or the manager. There are many reasons why high-net-worth individuals should consider setting up their own personalised investment vehicle. A Cayman Islands structure is invariably the best option.

**Why set up your own investment vehicle?**

**ISOLATION FROM OTHER INVESTORS**

With their own investment vehicle, the client can structure the fund exactly how they wish. The client can determine the terms and get precisely what they want. The terms may include the right to choose the investment manager, determine the investment manager’s fees and remove the investment manager when the client chooses. In addition, the fund’s investment objective and restrictions can be changed to meet the client’s wishes. The family investors can retain the right to withdraw money when they wish. Of course, this would all need to be properly documented and be in compliance with the relevant laws and regulations in any applicable jurisdictions.

Furthermore, as far as the outside world is concerned, while the client’s affairs are ring-fenced in a separate fund vehicle, the client as investor can be given the right to information in whatever form and at such times as they require. They may also be involved in decision-making. Many high-net-worth clients wish to know the family’s wealth, which can be spread across a great many investments in many locations, at regular intervals and in an easily digestible form. Having a dedicated mechanism to value such assets can be important to a wealthy family.

**CONFIDENTIALITY**

The fund will make the investments and not the client. Many wealthy individuals will frequently make investments through holding companies located in suitable jurisdictions. The use of a separate legal entity to invest may provide additional confidentiality, reduced liability and, if the fund is regulated, can add a level of sophistication that may speed up the underlying investment process by virtue of streamlined due diligence. To the investee, the investor would be a regulated fund.

**POOLING OF FAMILY WEALTH**

Pooling of assets (and pooling of wealth) can result in economies of scale in terms of investment due diligence and other operating costs (including tax advice). Tax may be deferred by investment gains and income receipts such as dividends being received by a fund located in a tax-neutral jurisdiction. Pooled (and, therefore, increased) wealth gives additional purchasing power. This may result in lower investment costs (such as subscription fees) and more investment choice by virtue of the greater wealth providing access to markets to which the investors on their own would not have access. Investors can also be given exposure to a diversified portfolio without having to replicate each separate investment themselves. If the fund has ten investments,
then an investment in the fund gives indirect exposure to the performance of the same ten investments.8

Investments are more easily bought and sold via a single entity rather than by each family member separately. As discussed below, a formalised fund structure may keep family members out of the buying and selling process.

By using a family fund vehicle, a particular member of the family can be given responsibility to manage the assets of other family members. This can be an objective particularly with families that have adopted one of the forms of Shari’a law (where, for example, the eldest son is to manage the family assets for his mother and siblings) but can also be used where family members wish to entrust another family member with asset management.

DISTANCE FAMILY MEMBERS FROM THE ASSETS

A patriarch or matriarch can enable family members to benefit from the economic success of the family but be isolated from the underlying assets. The family members own an interest in the fund, not the particular asset. The underlying assets will be freed from the issues that can affect individual family members, such as death, divorce and incapacity. If a family trust is used, the family members will benefit as beneficiaries of the trust and not as investors in a family fund vehicle. In addition, certain investors can participate in the fund without having any managerial responsibility, such as by the use of non-voting shares or limited partnership interests.

Family members should be given a certain responsibility for part of a family’s wealth so that they feel enfranchised and take responsibility for their own actions. It is also recognised that certain assets may be difficult to pool, such as particular works of art with ties to certain family members and properties used by some but not all family members.

FLEXIBILITY

The operation of the fund can be as simple or as complex as the particular family requires. But it is essential to have clear documentation. Many patriarchs and matriarchs believe that family members all get along and want what they want. This is seldom the case and it is important to have a plan in place should anything happen to the head of the family. An off-the-shelf company is not the way to proceed and advice should be obtained. As a bare minimum, the fund should consider the following:

▶ How will new investors be admitted, if at all? Frequently, investors will want to invest in specie by contributing already held assets. Consideration should be given to transfers by existing investors in whole or in part. Regulatory considerations will be necessary if, for example, there is any form of offer or solicitation to invest.

▶ How will investors be able to exit? Redemptions by investors, repurchases by the fund and transfers to third parties will need to be considered. Typically, these funds are very private affairs but it is essential that there are ways to return value to an investor. For example, the family member may have creditors (including a divorcing spouse) who need to be paid or the family members or different branches of the family may wish to separate their affairs. What begins as co-investment by two siblings initially can result in multiple co-investment by cousins in only a generation or so – with very different family dynamics. However, an exit does not have to result in the sale of any underlying assets, if, for example, one family member can purchase the interest of another. The most common mechanism to deal with these issues is a combination of transfer restrictions, pre-emption rights, put options, call options, and drag and tag provisions.

▶ Valuation. This is essential in respect of the two points above but also in respect of any fees being paid to a manager or service provider. Certain assets are often hard to value (private equity, art, wine, etc) but there does need to be an agreed process.

▶ Decision-making. Determining which family members will be given which roles and whether or not any external decision-makers will be engaged is a key part of the structuring process.

With the correct planning, a family fund can offer many advantages. Clearly this comes at a cost so, for a single family vehicle, the family’s wealth would certainly be in the ultra-high-net-worth bracket. However, in the longer term a manager (whether or not a family member) may gain such a track record that other investors wish to join the fund. A number of fund managers and multi-family offices began with a single client who became comfortable with allowing others in. With the right segregation, a family may find that the costs of the fund can be borne by other investors and the family wealth managed for free.

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1. Including their holding companies, trustees of family trusts and the investment arms of family offices.
2. A provision that limits redemptions to a certain value or percentage of an investor’s holding.
3. This can be achieved with differing class rights but often is based purely on an informal understanding or ‘gentlemen’s agreement.’
4. Subject to any licensing regulations.
5. The regimes vary from jurisdiction to jurisdiction but, in the Cayman Islands, regulation can be easily achieved. The Cayman Islands is the leading location for offshore investment funds to be domiciled. Such funds can be structured as limited companies (including segregated portfolio companies), limited partnerships and unit trusts.
6. There can be no guarantee that information about the fund’s investors will not be required.
7. Subject to the particular circumstances of each investor.
8. It is possible to structure different portfolios with different participation rights in underlying investments.
9. For example, separate classes of interest with different fees.
Health City Cayman Islands is a new medical facility that is about to revolutionise the way health care is provided not only to Cayman Islands and Caribbean residents, but also to those in North America and beyond. Initially a 108-bed hospital that specialises in cardiac surgery, cardiology, orthopaedics, pulmonology, medical oncology and paediatric endocrinology, Health City Cayman Islands will eventually be one of the largest hospital complexes in the western hemisphere, with 2,000 beds planned under a phased approach to be implemented over the next ten to 15 years.

A new approach to health care
Escalating health-care costs globally, along with drastic increases in non-communicable diseases in recent years, have forced governments and the medical sector to re-examine health-care provision.

World-renowned cardiac surgeon Dr Devi Shetty, Chairman of Narayana Health in India, one of the parent companies of Health City Cayman Islands, recognised the desperate need for affordable health care for the citizens of India over a decade ago. Since then, Dr Shetty has overseen the construction of 26 hospitals across 16 cities in India, all providing affordable, high-quality health care not only for the country’s residents but also for those who travel from all over the world to access it.

Health City Cayman Islands is Dr Shetty’s first project outside India, opened in early 2014 in partnership with Ascension Health, a non-profit, faith-based health-care organisation headquartered in St Louis, Missouri.

Reaping the benefits
This year saw the very first open-heart bypass surgery, valve replacement and successful artificial heart pump installation take place in the Cayman Islands. Local and overseas patients have enjoyed the facility’s top-quality services at a fraction of the cost of the same procedures in North America, with patients undergoing a range of diagnostic procedures, executive health checks, and operations.

Dr Shetty earmarked the Cayman Islands for the global expansion of his unique health-care model for a number of reasons. Cayman’s sophisticated infrastructure and the ease with which it can attract quality professionals were both important, as was its proximity to the US and Central America.

A unique methodology
Health City Cayman Islands follows the innovative medical and business practice guidelines pioneered by Narayana Health. The hospital works on the premise that high volume will drive prices down and at the same time improve the performance of its surgeons. The surgeons have worked in high volumes and are highly proficient in their respective fields.

Health City Cayman Islands aims to reduce the time a patient stays in hospital, and thereby the associated costs, through the use of technology and process re-engineering. Telemedicine is also incorporated into pre- and post-procedure care of patients.

Administrators are very much involved in the financial running of the hospital. They are given a daily profit and loss calculation, with updates sent electronically through mobile devices, a concept that has assisted parent company Narayana Health to stay ahead of its competitors.

Its parent company’s strategy of keeping an asset-light model has worked in Health City Cayman Islands’ favour by keeping operational costs low. Other contributors to a healthy bottom line include an innovative infrastructure that requires lower capital costs while also reducing operational costs. Ensuring that insurance companies and others are part of the health-care offering at Health City Cayman Islands has also been an important economic factor contributing to the overall reduction of health-care costs at the facility.

The project ties in neatly with Ascension Health’s concept of population health, rooted in its mission to care for the whole person: body, mind and spirit. Part of this concept involves the development of clinically integrated systems of care – i.e. creating networks to develop and improve communication, collaboration and sharing of data, thereby creating uninterrupted health care.

This collaborative approach, working in tandem with the patient and their care-givers, means Health City Cayman Islands can offer a comprehensive programme for the successful recuperation of its patients.

Taking all these strategies into account, Health City Cayman Islands is able to reach its goal of providing quality health care at an affordable price.

Shomari Scott is Marketing Director of Health City Cayman Islands

Shomari Scott offers an overview of the innovative Health City Cayman Islands medical facility
Lean and mean

Martin Trott and Matthew Wright on the merits of ‘entity rationalisation’ in an increasingly regulated world

As corporate holding costs continue to rise and regulation of companies around the world increases, the need for trustees and advisors to critically assess the size and purpose of their group structures has never been more pressing. Entity rationalisation is a process that helps clients assess their structural effectiveness and enables a reduction in costs, risk and overall structural friction.

The process involves, firstly, a diligence phase to identify inefficiencies and assess the costs and benefits of entity types and domicile, followed by the use of various restructuring options, including re-domiciliation, wind-down services (solvent and insolvent) and mergers to ‘tidy up’ the client’s structure. This will often involve entities in multiple jurisdictions and so require coordinated planning to bring about the agreed changes. The need is often identified after a corporate event such as a merger or acquisition, when there is focus on integrating operations and central functions. There is also a current trend of adding more sophistication to legacy structures and applying a more critical review to the overall effectiveness of each entity, the jurisdictions being used and the overall resulting structure and operational procedures.

Entity rationalisation is important for the following reasons:

- **Complex, cumbersome structures** are often difficult to manage and lead to management time being diverted from important business issues.
- **Maintaining a multitude** of entities is costly (this includes government, regulatory, audit, director and registered agent fees, and tax liabilities).
- **There can be** a loss of confidence in the structure and the accuracy of information.
- **The increasing regulatory** burden from both domestic and foreign authorities is driving a need for simplicity and greater transparency.
- **Overly complex structures** can create the perception of opaqueness and secrecy among service providers and counterparties.
- **Jurisdictions** may undertake regulatory or legal framework changes that make them more or less effective than competitor regimes for stakeholder purposes.
- **A critical review** will highlight intra-group inefficiencies and areas where synergies can be made to reduce overall group costs.

Entity-rationalisation projects usually follow a series of discrete stages, depending on specific needs. The initial information gathering focuses on a deep understanding of the legal and operational structure, including a full needs assessment in conjunction with trustees, directors and service providers. This is then followed by a cost-benefit analysis to compare the potential savings to the costs of carrying out the rationalisation, using an overall return-on-investment approach. Certain situations warrant a review of the customer and supplier bases within the group to highlight inefficiencies or, for example, where group companies have different trading terms with the same stakeholder. Once entities have been identified for jurisdictional transfer, closure or other restructuring remedies, a carefully managed action plan of re-domiciliation, mergers, liquidations (or strike-offs) can be executed.

As well as cost reductions and risk mitigation, those carrying out an entity-rationalisation project often benefit from:

- **A better understanding** of the make-up of their group and how it is best structured to align it with the business strategy.
- **An improvement in** long-term business performance by deploying staff and operations in a better way around the group.
- **Streamlined governance and** improvements in control of the group.
- **Solutions to stakeholder** challenges (e.g. contract disputes, threatened litigation) and to unnecessary intra-group trading.

Tried and true laws and processes allow entities to migrate efficiently to the Cayman Islands. Cayman also has effective laws and best-in-class service providers and processes to allow wind-up, mergers and restructuring of continuing entities, as well as to best service the ongoing structure.

Service providers can aid their clients by proactively reviewing structures and making recommendations for improvements. Helping clients take a critical look at their group structures and streamlining them demonstrates a trusted business relationship and often leads to other advisory opportunities. It is also an excellent way of utilising the STEP international community in a way few other projects can achieve.

*Martin Trott and Matthew Wright are Insolvency Practitioners and Directors of RHSW Caribbean*
Intelligent and insightful offshore legal advice and fiduciary solutions. Offshore is our domain.

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For STEP Cayman, our primary purpose is to support our members in their careers, providing qualifications and professional development, sharing knowledge and technical expertise, and protecting their reputation by maintaining high professional standards.

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