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Investment Funds as Complements to Trust Structures

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Wealth planning solutions almost invariably include a trust. For many wealth planners and clients, the trust is the gold standard; a tried and tested solution supported by comprehensive, modern legislation and an abundance of jurisprudence.

Having said that, one size does not fit all. The days when matters were straightforward and a will trust or stand-alone trust was sufficient seem to be a distant memory. In today's world, with families domiciled or residing, and holding different types of assets, in multiple jurisdictions, together with the ongoing attempts from the developed world to reduce budget deficits through initiatives such as the Foreign Account Tax Compliance Act ("FATCA") and the Common Reporting Standard ("CRS"), clients are demanding, and practitioners are being forced to develop, more complex and robust asset protection and estate planning solutions.

In recommending alternatives, one of the key matters to be addressed is the optimal manner of holding and managing the underlying assets. For some, one or more private investment entities may be sufficient. For others, a private investment vehicle may not be sufficient, and an added layer of structure and protection may be necessary. In this very common scenario, a Bahamian investment fund is one option.

Investment Funds

For Bahamian law purposes, an investment fund is a unit trust, company, partnership or investment condominium ("ICON") that issues equity interests, the purpose or effect of which is the pooling of investor funds with the aim of spreading investment risks and achieving profits or gains from the acquisition, holding, management or holding of investments.*

The advantages offered by an investment fund include, facilitating the management of assets of multiple classes within a single regulated structure, accurate ongoing asset valuation, the conferral of differing control and income rights on different family members and the negotiation of fee arrangements based on the pooling of underlying assets. Each of these advantages will be considered in turn.

Regulated investment holding/ management vehicle

An investment fund is a regulated vehicle through which the assets of multiple family members (for example, multiple siblings or the settlor and his children) can be pooled and invested. A Bahamian investment fund which meets the prescribed requirements is licensed by the Securities Commission of the Bahamas (the "SCB"). A professional fund (which is offered to sophisticated/accredited investors only) or a Specific Mandate Alternative Regulatory Test (SMART) Fund is licensed by the SCB or by an investment fund administrator holding an unrestricted license issued by the SCB.

Management of Different Asset Classes

As an alternative to forming separate investment vehicles for different types of assets, an investment fund is an efficient vehicle for managing different classes of assets within the same structure. There are no restrictions on the asset classes or investment objectives for Bahamian funds. The investment objectives and policies can be drafted to suit the particular fund. In most instances, these are very broadly drawn to allow the greatest flexibility. However, any restrictions should be articulated.

In order to control the extent to which family members are entitled to participate in the returns and/or losses from different assets, the constitutive documents for the fund can be drafted to provide for different classes of shares linked to different asset classes. Where there are substantial variances in risk or volatility relating to different assets in the fund, if the fund is structured as a company, it can be registered as a segregated accounts company so that the assets and liabilities linked to each segregated account (or cell) are legally segregated from the assets and liabilities linked to each other segregated account. A practical matter to consider with segregated portfolio entities is that they are more complex to administer, involve increased regulatory costs on a per segregated account basis and some counterparties are not familiar with the concept of a segregated cell entity resulting in more onerous due diligence requirements.

Retention of Investment Control

Clients who wish to remain actively involved in the management of their assets may continue to manage the assets which have been contributed to the fund through the formation of an investment management or advisory entity to serve as investment manager or investment advisor to the fund, so long as the management entity can demonstrate that it possesses the relevant expertise and experience to satisfy the "fit and proper" requirement for all service providers to an investment fund. It must however, be ensured that the investment manager discharges its functions in accordance with the terms of the investment management/advisory agreement and the investment objectives and policies of the fund. The directors, general partner, trustee or governing administrator of the fund must receive reports from and/or meet with the investment manager from time to time to ensure that they are able to properly discharge their duties to the fund.

Independent Asset Valuation

An investment fund provides a vehicle for the ongoing independent valuation of its underlying assets. The constitutive documents and offering documents of an investment fund generally provide for the calculation of the fund's net asset value at prescribed intervals selected by the client.

Separation of Control and Economic Rights

Investment funds enable the separation of control and economic rights in respect of the underlying assets in the fund through the creation of different classes of shares. In a straightforward investment fund, there will be two classes of shares, management shares, with voting rights, which are commonly held by the investment management entity (which is controlled by the settlor or patriarch of the family) and investor shares, with economic rights, which are commonly held by the beneficiaries, children of the settlor, other family members or trustee of a family trust.

A fund is sufficiently flexible so that the rights and restrictions attaching to each class of shares can be tailored to suit the relevant structure so long as these are clearly set out in the memorandum and articles, trust instrument, partnership agreement or regulations and the offering document of the fund.

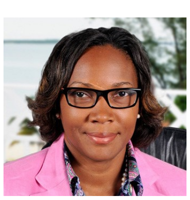
Techniques that are commonly utilized include, conferring different redemption rights on different classes of shares to control the income received by children, siblings or trustee from the underlying assets or restrictions on the percentage of the overall net asset value or a specified amount that can be redeemed on any particular redemption day.

Efficiencies from pooling

Due to the pool of assets held in the fund, it may be possible to negotiate more favorable rates for professional services such as administrators, based on the total AUM of the fund, than might otherwise be the case if those services were provided in respect of portions of those assets.

In summary, any wealth management and estate planning solution must be tailor made, robust, flexible and workable from a practical perspective. It should be based upon sound professional legal, financial and tax advice. Bahamian investment funds can be a useful component of a comprehensive structure.

**Section 2, Investment Funds Act, 2003 (the "IFA")*



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