Vistra 2020
The disruption advantage: opportunity in a changing world
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It’s a pivotal time for the Corporate Services industry1. Amid simmering trade wars, nationalist politics and an unstable economic climate, 75% of executives believe they are facing an unprecedented level of uncertainty.

In this climate, the business facilitation services provided by the industry and its international finance centres (IFCs) have rarely been more critical. Yet the landscape is far from straightforward. Over the last 18 months, the populist backlash against poorly defined ‘elites’ – catalysed by high-profile data leaks – has intensified.

In turn, pressure from angry populations, exploited by electoral politics, is enabling distortions in policy making. This includes an overemphasis of regulation on offshore – rather than onshore or mid-shore – jurisdictions, which are foremost in the public mind thanks to negative publicity. Already, 76% believe governments have underestimated the challenge that transparency measures place on global businesses.

Nonetheless, our research suggests that concerns about the imminent demise of globalisation have been premature. It may be true that politics is becoming more inward-looking – evidenced memorably by President Trump’s rejection of the ‘ideology of globalism’ in his second address to the United Nations (UN) – but businesses are becoming more globalised than ever before. Ultimately, in an industry that is inherently international in outlook, our findings point to confidence in the future and in the ability to drive growth. Wherever there is legitimate interest in achieving global scale, there is an opportunity for corporate service providers.

In this study – which draws on the insight of some 800 industry figures, making it our most ambitious in the Vistra 2020 series to date – we focus on three trends that are defining today’s industry: how the sector is changing to meet an evolving geopolitical system, how regulation is becoming increasingly politicised, and how businesses across the industry may be sleepwalking into technological disruption.

As we explore in depth, there are as many challenges as there are opportunities. There are more questions than there are answers.

As ever, we trust you enjoy this report and would be delighted to hear your views and discuss our findings in more depth.

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1 We define the ‘Corporate Services industry’ as providing specialised trust, fund and corporate services to corporate and private clients as well as alternative investment managers who are seeking global outsourcing expertise and support.
Since our last report, the West’s major power centres have seen the consolidation of a new style of politics. In the wake of a popular reaction against globalisation and inequality, the vision of trade integration and deregulation – an article of faith for decades – is coming under fire.

On one level, anti-globalisation sentiment stems from broad dissatisfaction with the economic consequences of an inter-connected world. At its most extreme, it also incorporates a more general protectionist outlook, a bias for national populations through the exclusion of ‘outsiders’, and a conviction – often informed by the ‘fake news’ and biased commentary prevalent on social media – that there is something inherently suspicious about wealth and privacy.

As we explore in section 2, the ongoing adjustment to globalisation is creating political pressure for governments to reassert their role in establishing rules for business. Such developments are unsettling the commercial playing-field. In the words of a partner at a corporate law firm in London: “The private sector has globalised but governments haven’t. That induces stress as governments decide how best to cooperate – and national interest figures into that.”

All of this has sharp implications for the financial flows mediated by the Corporate Services industry. In an industry that has already seen widespread transformation, driven by consolidation at the service-provider level, alarm bells are ringing. For our respondents, the industry’s global reach is also its greatest strength. Asked in our survey to identify some of the main benefits it creates, they point to its enablement and support of capital flows, global growth, integration of the trade cycle, and free trade [Figure 1]. These views are broadly consistent across regions – in terms of the relative importance of each benefit – although we do see some variations. Caribbean respondents are, for example, stronger in their advocacy of the contribution that the industry makes to global growth – with 70% in agreement that this is a positive outcome of Corporate Services – perhaps reflecting their closeness to growing outbound flows from China and knowledge of how these are channelled to destinations worldwide.
With these broad sentiments in mind, it is telling that just 23% of respondents say they are ‘very confident’ in the ease of doing business across borders during the next 12 months – which represents a fundamental requirement for our industry.

A quick review of the geopolitical situation sheds light on their concerns.

United States – the great step-back

In the United States (US), President Trump is challenging the rules under which trade and investment have been managed for decades. He is reorienting policy in a more closed and US-centric direction, reshaping the country’s relations with rivals and allies alike. An instance of this is his preference for bi-lateral rather than multi-lateral deals, evidenced by the country’s withdrawal from the Trade-Pacific Partnership and the trade war he is waging with China, which is escalating through tit-for-tat impositions of tariffs.

China – an evolving opportunity

The impact of China’s growth in recent years has been remarkable. Its outbound investment could reach US$2.5 trillion over the next decade and remains a key driver of activity in the industry. In the eight months to August 2018 alone, Chinese firms invested in 4,309 businesses in 153 countries worldwide and its companies are responsible for more than 40% of the US$1.5 trillion mediated through the British Virgin Islands (BVI). As the Belt and Road initiative is rolled out, the country’s global influence continues to grow. Nonetheless, President Xi’s China is not without its challenges for the industry: our respondents do, for example, have concerns about how policy in the country will affect business, as we explore in the ‘Centres of future growth’ section below.

Europe – seeds of an identity crisis

Europe faces its own challenges. In the United Kingdom (UK), the Conservative government is struggling, in the face of media scrutiny, to deliver a coherent Brexit, reflecting popular appetite for a more inward-focused stance and raising questions over the country’s trading relationship with the rest of the world.

“Certainly, in Europe, we’re staring down the barrel of Brexit,” says a managing partner at a Jersey-based law firm. Whatever the outcome, the industry will be forced to, and will, adapt. “It’s going to create more cost for companies as they’re going to have to double up on regulation,” adds a capital markets adviser based in the UK.

The European Union (EU) is divided over its own future. A group of former eastern bloc countries are pushing against values held sacred in Brussels, and nationalist politicians are on the rise in many countries. Globalisation remains out of favour. “I’d say the sentiment is towards the opposite of globalisation,” says the capital markets adviser. “Countries are more focused on their own economy than the global economy, like we’ve seen with the UK.”

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2 China’s outbound investment could reach $2.5 trillion over next ten years (Linklaters)
3 China’s Jan-Aug FDI rises 2.3 percent (CGTN)
4 China, Hong Kong the biggest source of funds mediated through British Virgin Islands, study says (South China Morning Post)
Eyeing opportunity: The industry reacts

How is the Corporate Services industry responding to this intersection of political and economic factors?

The good news, as our research makes clear, is that the mood is one of optimism above all. Despite understandable caution about the challenges ahead, industry professionals are confident in their ability to generate growth and satisfy client demand.

Globalisation may have its critics, but they haven’t stopped businesses from becoming more international in their outlook and ambitions. This inevitably translates into a need for local knowledge and expertise, which is amplified by geopolitical uncertainty and complexity – both of which reliably drive demand for the experience and counsel provided by corporate service providers.

As figure 2 illustrates, respondents are broadly upbeat about their short-term prospects: 83% are confident in their ability to satisfy clients’ expectations; 74% are confident in their own organisation’s growth prospects.

Similarly, the macroeconomic outlook is an obvious concern. As we set out in figure 4, developments in the global economy – along with changing regulation, which we come back to in the next section – are seen as the most pressing challenges by a majority of respondents: 53% and 62%, respectively, expect these to have a major impact on business. Conversely, respondents are significantly less worried about the factors that they can manage, control and plan for: the threat of new competitors, reputational risk, and changing client expectations.

Our data suggests that respondents become less confident when they start looking beyond their own businesses. If they can rely on their internal expertise and agility to satisfy client demand, there is little they can do about the outlook for their industry or domestic market, or the ease with which they can do business across borders. Unsurprisingly, as highlighted in figure 3, we find this final point most marked in the UK, where businesses will – to a greater or lesser extent – need to adjust to the post-Brexit playing-field during 2019. Just 13% of UK businesses are very confident in this area of their business, for example, compared with 23% of the total sample.
At worst, we could suggest that the data shows complacency among our respondents. As demonstrated in many other sectors – notably banking, insurance and media in recent years – it can be a serious mistake to underestimate the threat of new competitors, especially those using disruptive technologies to rethink existing business models (as we explore further in section 3). Complacency may also be evident when respondents in Europe tell us they are feeling less concerned than their peers elsewhere about the impact that changes in the global economy will have on their business, as illustrated by figure 5.

**Jurisdictional rankings: Challenging preconceptions**

When we look at changing attitudes towards individual jurisdictions, the degree of variation since our last report – at least at first glance – appears limited. Our data uncovers some telling variations, however. Asked to rank jurisdictions by popularity, our respondents’ top 10 is as set out in figure 6.

Even allowing for compositional changes in our sample – which has a proportion of Asian respondents that is approximately 10% higher than last year – the rankings tell us two things. Firstly, as discussed in previous Vistra 2020 reports, the trend toward onshore and mid-shore is continuing, with the top five dominated by IFCs either in or close to the world’s political centres. Secondly, a small number of traditional offshore jurisdictions – specifically the BVI and the Cayman Islands – are performing well and bucking the wider trend away from offshore.

Why is this? Our view is that these jurisdictions’ popularity reflects a growing preference for tried-and-tested service at a time of economic uncertainty. Both have earned themselves a reputation in a specific niche, with growth in the BVI and the Cayman Islands driven by expert capabilities in incorporations in the former and fund structuring in the latter. The two jurisdictions are also established trade routes for Asian businesses, which have seen more significant growth than other regions and – as we have observed in previous reports – still have a relatively strong demand for offshore and are loyal to IFCs that provide consistently high service.
Overview of the top three jurisdictions

**Hong Kong: Winning business from offshore**

Hong Kong is not without its critics. A significant minority (33%) of respondents believes that political upheaval has affected its reputation as an IFC. But any harm has been offset by Hong Kong winning business from offshore regions, particularly among clients in Asia (see figure 7 for a breakdown of how different regions view the jurisdiction).

Moreover, Hong Kong appears to be an attractive platform for many of China’s growing cohort of high net worth individuals (HNWIs). “They are quite happy to bank with a Hong Kong bank, and some of them even want to get a Hong Kong residence,” notes a banking executive based in the territory. “We have lower taxation here, and a stable legal system.”

The increasingly sophisticated needs of these individuals are a key factor. As a generation of Chinese HNWIs start to think about succession planning and asset diversification – services that are well-established among peers in other regions – they are often turning to service providers in Hong Kong. “Taxation and the Common Reporting Standard (CRS) is a factor,” says the executive, “and considering how to maximise profits, as well as family planning and tax efficiency.”

**BVI: Shifting tides**

The BVI is a good example of industry resilience and ‘anti-fragility’ in the face of hostile opinion. Following the Panama Papers in 2016 and the Paradise Papers in 2017, many could have expected the jurisdiction to fall in the rankings. Yet it remains at number two in our list, and is currently experiencing growth in new incorporation volumes: 11.2% in the first nine months of 2018 over the previous year, in our own portfolio (a good proxy for the industry), much of it reliant on Chinese investment.

Indeed, where the BVI is seen as challenged, this is more about perception than the quality or prospects of the jurisdiction. “The number of incorporations is going up,” reports one senior legal executive. “BVI companies are commonplace in many corporate holding structures.”

The executive goes on to note, however, that the “jurisdiction does need to focus on perception in order to maintain status as a top offshore jurisdiction.” We see, for example, changing sentiment taking its toll, particularly in Europe, where the concept of offshore has been losing currency in recent years (Figure 8).

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1 Mainland companies make up half of listed firms at HKEX (China Daily Hong Kong)
2 Huge number of Chinese tech unicorns likely to IPO in Hong Kong in 2018, says JPMorgan Asia-Pacific chief (South China Morning Post)
3 Hong Kong needs more than tax breaks for the aircraft leasing hub to get off the ground (South China Morning Post)
Such uncertainty helps explain why the country has fallen from its place at the top of the rankings [Figure 6]. When we last carried out our survey, in late 2016, there was arguably greater optimism than there is now about the outcome of the withdrawal negotiations. Today, respondents take a dimmer view of Brexit’s implications. Only 35% expect the UK to become more open to the industry and IFCs after Brexit, with negative emotions running particularly high in the Caribbean – largely comprising British Overseas Territories’ (BOTs) respondents in our sample – which will undoubtedly be caught in the ‘Brexit crossfire’ [Figure 10].

According to one senior figure based in the country, Europe is already something of a ‘dead zone’ for him. “Marginal advantages get swept away,” he says. “Hostilities are so great that, when people analyse their reputational risk in terms of being found to have a company offshore, that becomes a story in itself and has negative connotations.”

The UK: Brexit looms

In the years before the country’s EU Referendum, the UK’s favourable corporate tax rate and flexible labour legislation meant it was steadily gaining in popularity as an IFC. Today, it remains an attractive jurisdiction, particularly for respondents based in Europe, but many believe that the country is inflicting self-harm through its decision to leave the EU [Figure 9]. “We could have seen a lot of on-shoring of businesses back in the UK,” says one expert based in the country. “But all those plans are on hold.”

This view is in contrast to previous speculation about London becoming ‘Singapore on Thames’, providing a low-tax environment combining unilateral free trade agreements with limited EU regulations. If the country cannot provide attractive conditions for business, we could expect to see a greater number of organisations using Luxembourg or Frankfurt as their European headquarters. This is a trend that has been evident recently among some Asian financial services firms, such as Bank of Singapore’s decision to open a wealth management subsidiary in Luxembourg – the first time a Singaporean bank has set up an operation in the country.
If respondents are broadly confident in their ability to satisfy client demand and grow their businesses, where will the next wave of growth come from? To answer this question, it’s perhaps best to consider the industry through three lenses: the originating markets where clients are based and have their headquarters, the regional hubs and conduit IFCs they use for proximity to markets and for specific corporate services, and the destination markets where they are pursuing overseas growth [Figure 11].

**Centres of future growth: Tomorrow’s opportunity**

In essence, what we find mirrors our earlier assessment that an uncertain, complex environment is presenting a strong opportunity for the industry – albeit one that is overshadowed, yet again, by negative commentary about IFCs, corporate service providers and the inherent worth of globalisation in general.

If we think first of originating markets, the industry would be hard pressed not to feel some alarm at President Trump’s protectionist rhetoric and the internal policies his administration is implementing – the outcomes of which might foreshadow a reduction in flows out of the US. In our survey, for example, 48% believe the US Tax Cuts and Jobs Act will make companies and individuals based in the US less likely to use IFCs.

Yet the potential of the US, as an originating market, remains strong. UNCTAD statistics of foreign direct investment (FDI) flows out of the country show an increase of 21.9% between 2016 and 2017, highlighting its ongoing interest in cross-border trade. Furthermore, in the first six months of 2018, the Cayman Islands – largely favoured by US funds – saw incorporation-volume growth of 40% compared to the previous year.

A parallel could be drawn with concerns about China as an originating market, specifically that outbound flows will be affected by economic and regulatory upheaval. Our respondents worry that a slowdown in the Chinese economy will have an impact on the number of its HNWIs using IFCs – an opinion held by 53% of all respondents. There is also an expectation, among 62% of respondents, that China will increase its scrutiny of funds moving to IFCs [Figure 12]. The proportion of respondents anticipating this increases the closer you get to the territory and is particularly acute in Hong Kong and Singapore – at 68% and 78% respectively – both of which have a high familiarity with Chinese business.

**Facilitation of capital flow from originating markets to destination markets**

<table>
<thead>
<tr>
<th>Region</th>
<th>% Respondents Agreeing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall</td>
<td>62%</td>
</tr>
<tr>
<td>Asia</td>
<td>70%</td>
</tr>
<tr>
<td>UK</td>
<td>61%</td>
</tr>
<tr>
<td>Europe (excl. UK)</td>
<td>55%</td>
</tr>
<tr>
<td>Middle East*</td>
<td>54%</td>
</tr>
<tr>
<td>Caribbean</td>
<td>47%</td>
</tr>
<tr>
<td>Americas*</td>
<td>46%</td>
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</tbody>
</table>

* indicates lower sample size

Source: Vistra
Despite this, however, we have already reported incorporation-volume growth in the BVI and the contribution that Chinese investors would have made to that result. We have also alluded to Chinese activity in Hong Kong and its growing influence through the Belt and Road initiative. China will not diminish in importance in the years to come.

Looking now at conduit IFCs and regional hubs, centres that position themselves as the ‘go-to’ for specific services have a growing advantage over their rivals when attracting business from both newer and more established originating markets – something we noted in previous Vistra 2020 reports. As well as the Caribbean examples mentioned above, this could apply to Ireland for aircraft leasing\(^8\) and Luxembourg for onshore funds. Jurisdictions in the Middle East can also stand to benefit from providing services that meet demand for wealth services. The UAE is on the upswing, asserts the managing partner of a wealth advisory firm with operations in Dubai and Abu Dhabi. “They have added flexible new tools to a centre that has genuine substance,” he says. “The toolbox makes it super attractive.”

A consultant based in the UK agrees. “I think Dubai is probably rising,” he says, before adding that Mauritius has become very popular as a gateway into Africa, helped by efforts to differentiate its services. “One, it’s got the most double tax treaties with Africa,” he explains. “Two, it’s got a regulatory framework, which is in theory very similar to the UK’s, so people are quite comfortable with it. It’s got a pretty developed banking system. And it’s positioning itself as a financial services hub.” Other prospective African service centres should beware: “It’s by far the most popular jurisdiction for Africa from our perspective, way ahead of the Seychelles and other markets.”

As new centres rise, others inevitably decline. A partner at a global asset management consultancy picks out Cyprus as an example of this: “It still attracts Russian attention or Greek attention, due to legacy, but it’s no longer considered heavily.” We would note that the impact of sanctions on Russia is likely to have an ongoing impact here. It is also worth stressing that conduit and IFC hubs will see a larger or smaller amount of business depending on the strength of flows from individual originating markets and their preference for using offshore or mid-shore jurisdictions to facilitate their expansion into destination markets. European originating markets are less likely to use offshore centres, for example, as outlined earlier.

Regulation will also continue to have an impact, as we explore in greater depth in section 2. It is worth flagging here, however, that respondents expect a great deal of variation in the extent to which different jurisdictions will be affected – as highlighted in figure 13. Overall, and notwithstanding the recent strong growth, our respondents continue to predict that the BVI will be most negatively affected by changing regulation, followed by the Cayman Islands – while the US, and other onshore and mid-shore large financial centres, are expected to most benefit.

\(^{8}\) Aircraft leasing worth more than €500m to Irish economy (Irish Times)
Section 2: The populist rulebook

“I don’t believe in regulation for regulation’s sake, but I 100% believe in setting standards and holding service providers to account for the provision of those standards.”

Legal Executive, Cayman Islands

In recent years, the Corporate Services industry has been subject to an extraordinary amount of regulatory change. After extensive reform and pressure to increase transparency, with several initiatives still in the process of implementation, how much further can regulation go?

Perhaps, like so many other challenges to the industry, the ‘dizzying pace’ of transparency drives will come and go.

After all, many in the industry would argue that regulation has already resolved or undermined the industry’s most problematic legacy issues, including the perception or otherwise of tax evasion and money laundering. Some 74% tell us they are ramping up their investments in compliance and, as a result, will be able to demonstrate that they and their clients have nothing to hide, whether moving money across borders or establishing trading companies in new jurisdictions. Indeed, corporate service providers and IFCs are arguably in a position to use measures that were once considered existential threats – not least CRS, Foreign Account Tax Compliance Act (FATCA) and public registers of beneficial ownership (BO) – to legitimise their services in the light of mainstream opinion.

It is also encouraging that the industry has become adept at meeting the regulatory expectations placed upon it, as our research makes clear. The majority expect a modest impact from government actions to boost transparency, suggesting they have already adapted to meet expectations. Moreover, 78% tell us they are confident in their ability to achieve timely and consistent compliance with new regulations, even though similar proportions admit that the speed and frequency of change is a challenge. And, even though 76% of respondents expect full implementation of CRS in the coming years, they predict its impact will not be as significant as they did in 2017 – for which it rated 3.3 out of 5 compared to 2.6 this year [Figure 14]. Similarly, more respondents expect beneficial owner information to become publicly available in the near future, yet are likewise expecting less of an impact from such a development.

After all, it’s not as though regulators are becoming more sympathetic to the plight of the industry: 85% expect the political pressure that has forced greater scrutiny of tax and financial data to continue unabated, even though the clear majority believe that governments have underestimated the challenge that automatic exchange of information places on their business.
A regulation official based in Paris is clear in his diagnosis: “Treaty shopping was one of the serious deceptions of the international tax environment. To invest in India, someone could buy in Mauritius. To invest in Europe, they would buy in the Netherlands – purely shell entities with no substance, and they didn’t pay withholding tax in the countries where they did business. That is a cost of billions and billions of Euros.” He’s direct about the size of the change he’d like to see: “It’s over. This is over. That’s big.”

Again, however, businesses across the industry could point out that they have already passed stringent tests to show high-levels of compliance with international standards.

The danger of politically expedient policymaking

For many, the growing worry is that the driving force of regulation has shifted. In places, we could suggest that regulation has gone from being an initiative driven by the regulator’s office into a political exercise – even to the extent of pandering to the populism discussed earlier in this report. The industry’s current bête noire is the UK’s proposed public register of BO, which BOTs are expected to adopt. The UK legislation has been designed to force these IFCs to make public, by the end of 2020, the names of individuals behind the vehicles they host, rather than just commit to deliver them to law enforcement and authorised agencies when requested.

The objections are many: disrespect of privacy; the imposition of rules in the face of local opposition; and disproportionate measures that are nonetheless unlikely to eradicate tax evasion and corruption as it mirrors a system in the UK that relies on self-reported and unverified data. Our survey respondents see the measure in an overwhelmingly poor light. A total of 58% see it as negative, with just 13% describing it as positive.

Upholding the level playing-field

As well as remaining balanced in their scrutiny of Corporate Services, relative to other industries, we would urge governments to ensure that their regulatory efforts focus, above all, on maintaining a level playing-field and avoiding jurisdictional bias. Accusations of hypocrisy could be made against governments that compel foreign companies to comply with strict regulation while protecting national business interests.

These concerns are fed by measures such as the EU’s proposed ‘blacklist’ of jurisdictions it considers uncooperative on tax issues, which has been criticised for forcing non-EU jurisdictions to change their domestic laws in ways that do not mirror international standards – while currently exempting its own members from the blacklist. Similarly, while FATCA requires offshore financial institutions to send Americans’ tax data to the IRS, the US has not signed up to CRS.

There is an important question to ask here: if governments allow an uneven playing field, and may even benefit from it – as the US has, arguably, by deciding not to sign up to CRS – how much further will jurisdictional bias and ‘tribalism’ go? Simply put, what does it mean for the future, and for our industry, if a trading bloc can change the laws of other countries based on standards to which it does not hold its own members?
A Corporate Services paradox

Considering the escalating media, political and regulatory scrutiny that the industry is under, combined with the pressures of an uncertain macroeconomic environment, we could argue that IFCs and the Corporate Services industry more broadly have never been so misunderstood – but neither have they been so vital.

For those in the industry, its benefits are clear and numerous – from the sectoral and geographic expertise its experts bring, to the risk management function it serves in financing large investment projects and global trade flows.

Even the much-maligned service the industry provides in assisting with tax efficiency is overwhelmingly beneficial to ordinary citizens. The majority of UK workplace pensions schemes are structured offshore, for example. This means – in effect – that many pensioners need IFCs to continue operating as they are in order to maintain their standard of living. As one industry insider puts it: “If you structure through offshore vehicles it means that you only pay tax in the jurisdiction where the company is. So, let’s say you have a company in the UK, of course they pay corporate tax over their profits, but the profits after tax are then distributed to the ultimate owners. And the ultimate owners are often pension funds.”

At bottom, IFCs and their accompanying corporate services providers lower the cost of capital. By providing secure and reliable investment channels, and by charging low or no corporate tax, they facilitate billions in investment that would otherwise not achieve the required rates of return. As an industry expert based in the UK puts it: “They give a safe, cheap way of getting an optimal capital allocation around the planet.”

This is, in essence, a redistributive function, and one that aids global development. Chinese Belt and Road investments in Central Asia, for example, are facilitated by jurisdictions whose tax neutrality and legal certainty simplifies the process of moving money across borders. “It helps get money from people who have already got it to other parts of the world where they are short of capital,” says the expert.

It’s also worth stressing that, amid the challenges that regulation is responsible for creating, there is opportunity in the ensuing complexity. For an industry that thrives on helping clients navigate a difficult landscape, as we have already mentioned in this report, there is considerable promise. Put bluntly, greater regulation and complexity equate to higher earnings per client. As a private client based in Sweden tells us, “Complexity is growing all the time and many companies are active in many different areas of the world, with different rules and regulations. So, there are good business prospects going forward.”

There is even a recognition among regulators, perhaps grudging, that IFCs have a key role to play in facilitating business in a complex world. As the regulation official we spoke to says, “Yes, it is true that companies have to thrive in an environment which is more complex, that some of the legal structures can be challenged, that not all countries implement completely the rule of law and that it’s more of a challenge, so yes, it’s a more difficult environment. That’s the best I can do to stretch myself to be sympathetic.”
Reframing the dialogue

If the industry is increasingly vital yet fundamentally misrepresented, how should it respond? A first step could be to recognise and appreciate the benefits that are to be found in effective regulation, welcoming all that is good. Only then should businesses allow themselves to become more outspoken – in a constructive way – in their criticism of specific measures that it considers unfair or unnecessarily harsh. And, finally, the industry should not give up on the public relations (PR) war, to win over governments and policymakers as well as existing and prospective clients – even if that seems today to be an uphill struggle.

Recognising the value of good regulation

Most in the industry are happy to acknowledge the value of effective regulation, and the space it creates for the industry to go on to greater success.

Our own view, after almost nine years of Vistra 2020, is that regulation has ultimately not curtailed growth so much as enabled it. The picture is not completely black and white – larger organisations may have benefited more overall, with some modest-sized outfits being squeezed out by the higher regulatory bar, while some smaller jurisdictions have struggled to comply – but regulation has not hindered growth as much as its critics have alleged, and many corporate service providers are bigger than ever.

An industry expert we spoke to agrees on the benefits of effective regulation: “It’s making IFCs more popular with the legitimate businesses and less popular with the criminals.” In the long run, this should help the industry enhance its reputation in the public eye, whatever the costs now.

...while calling out regulation that goes too far

Those in the industry are comfortable with regulation that meets policy aims without damaging their ability to do business. It is important, for example, that new regulation serves a clear purpose and is not formulated purely ‘for new regulation’s sake.’

Often with this in mind, many of the industry figures we spoke to for this research say they would like to see a more nuanced approach from regulators. “There are so many facets to the industry that you can’t say one bucket fits all,” says a senior legal figure based in the Cayman Islands. This sets the industry apart from other highly-regulated sectors, in her view.

This is a common theme in the industry. There is a risk, if regulation is applied indiscriminately, that it damages the industry’s ability to perform its critical economic function while further tarnishing its reputation.

“I would encourage the OECD to look at the industry a little bit more specifically,” adds the legal executive in the Cayman Islands, “rather than with just a broad brush of saying this group is a white or grey list. They need to look at what type of business is going through there, and what the purpose of that business is.”

Ramping up the PR battle

The industry is concerned that misunderstanding of what it does and the contribution it makes to economic growth is feeding the populist backlash and thus influencing the pace and direction of regulation.

An industry expert in the UK takes an extreme view: “The British government and the EU – I’m not so sure about the US – are out to get the IFCs,” he says. This chimes with some in our survey, where 21% of respondents expect companies to stop registering or domiciling themselves in IFCs between now and 2025.
Yet some in the industry recognise that part of the problem is its lack of urgency in highlighting the progress it has made towards legitimising operations.

In Europe, there has been a focus on ensuring companies have a genuine presence and employees on the ground. Similarly, corporate service providers are more active in screening organisations for their level of compliance, and discriminating against those that do not meet expectations.

At the same time, the industry could do more to advocate for its own value. “The offshore world has been far too complacent in explaining to voters how cross-border finance benefits them,” says a UK legal expert. “The vast majority of funds in a cross-border environment are institutional. Probably the dominant portion represents pension and investment savings for so-called ordinary people. But they have no idea that they have a personal stake in the offshore game.”

Finally, as a wider point, the industry risks losing the semantic battle if it is not careful. The term ‘tax haven’ is used by critics of the industry and invokes thoughts of barely legal piggy banks for wealthy individuals. Where it can, the industry should continue to object to this term and explain why it is no longer appropriate as a description of what it does. “It would be better to call them tax highways,” suggests a London-based industry expert. Like the highways of old, IFCs and the Corporate Services industry provide a safe channel as capital travels round the world.

Update on funds

In our last report, we wrote about developments in the world of alternative investment funds. Today, private equity is still growing as a driver in the industry, in terms of new business (through related administrative services) and also in defining how the industry is shaped.

At the same time, if we look again at the potential impact of Brexit on the asset management sector, we see that significant challenges remain. In the UK, the world’s second-largest asset management centre, the government has cautioned that firms could lose the right to service European clients following the UK’s departure from the EU and Alternative Investment Fund Managers Directive (AIFMD). Two years after the Brexit referendum, around one in three of 40 asset managers with significant operations in the UK had already started making contingency plans to move parts of their operations to Dublin and Luxembourg.

Meanwhile, there are calls for equivalence arrangements to be put in place to ensure cross-border flows. At the time of writing, these questions are putting additional pressure on the need for the UK and EU to agree a mutually satisfactory deal. For now, the industry must wait and see.

\[\text{Brexit contingencies: asset managers put plans into action (Financial Times)}\]
Section 3: 
Sleepwalking into disruption?
The unmet value and threat of new technology

“Companies and asset managers are very complacent about disruption. They say they don’t have the money to invest or just don’t want to do it.”

Partner, Global Asset Management Consultancy, Singapore

The third major trend confronting the industry, as highlighted by our research, comes from ongoing technological innovation. The industry’s perception of the role technology will play and its implications for profitability are shifting and picking up pace.

One of the key findings in our survey is that respondents are increasingly upbeat about the prospects of technology delivering efficiency savings, with 78% taking that view.

That said, our results suggest complacency about how disruptive this wave of change is likely to be. It is our view that any such complacency should be challenged. Just 20% of respondents expect technological change to have a notable impact on their business, for example. There is also little concern shown about the threat from new entrants.
If we look at the different technologies that businesses are exploring [Figure 15] we find mobile applications are the technology being investigated most frequently, across all regions. But, after mobile applications, interest in disruptive technologies falls off. Big data and Artificial Intelligence (AI) attract some attention, but ‘none of the above’ comes fourth in the list among technologies respondents are working with. More respondents are doing nothing than are studying or adopting any of the disruptive technologies mentioned.

<table>
<thead>
<tr>
<th>Technologies currently being used or explored</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mobile applications</td>
<td>50%</td>
</tr>
<tr>
<td>Big data &amp; analytics</td>
<td>29%</td>
</tr>
<tr>
<td>Artificial Intelligence/Blockchain</td>
<td>23%</td>
</tr>
<tr>
<td>Robotic process automation</td>
<td>22%</td>
</tr>
<tr>
<td>Predictive analytics</td>
<td>18%</td>
</tr>
<tr>
<td>Threat intelligence platforms</td>
<td>9%</td>
</tr>
<tr>
<td>Augmented reality</td>
<td>22%</td>
</tr>
<tr>
<td>None of the above</td>
<td>2%</td>
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</tbody>
</table>

Disrupting the Corporate Services industry

Today, the focus for many in the industry is firmly on bread-and-butter issues such as automating ‘know your customer’ and anti-money laundering requirements, rather than on more exotic technologies such as AI and blockchain. “AI in Corporate Services, no,” says a senior figure at a global asset management consultancy. “Data mining, definitely.”

Compliance, in particular, is an attractive area for disruption within Corporate Services. In the words of an interviewee who works for a law firm in the BVI, it is “the most inefficient, unfit-for-purpose process that most businesses engage in today.” It is ripe for innovation. “A great deal of it is around identity and address verification, and shuffling pieces of paper backwards and forwards. I certainly see a world in which compliance is a smartphone-driven, more accurate, much more portable and much more efficient process.”

At the same time, for some IFCs, technology promises competitive advantage. An interviewee based in the Cayman Islands points to one example: “Singapore has a vested interest in tech. The regulator, Monetary Authority of Singapore, knows that in order to become a financial powerhouse, they need to make it easier for people to do business in Singapore. That doesn’t mean they drop the regulations, but that they look at how they can bring in technology to make it easier.”

With applications such as robo-advisory and biometrics pushing at the door – all of which could have transformational implications for the Corporate Services industry – businesses may be too blasé. A relatively promising 22% is looking into blockchain, which suggests some progress – considering the radical nature of the technology – but this is still relatively low considering the potential upheaval that cryptocurrencies could create in the industry.

By assuming that new business models will not push out incumbents, or by restricting their technology innovation to small-scale and administrative activity, businesses may be opening themselves up to an existential threat. For an illustration of how quickly disruption can spread, they should consider the impact of fintech players – such as Monzo, Circle and nutmeg – on the traditional banking industry.
When it comes to digital disruption of the Corporate Services industry, there’s a temptation to look at flashy new technologies making the headlines and believe the hype. Our survey suggests that most are avoiding this temptation, though there was a spike among respondents in Asia of interest in blockchain technology.

An industry expert based in London strips the question back to basics: “Some people think this stuff’s going to be absolutely revolutionary and change whole business models. I think that they should get to what the essence of the business models are. All these things make it more efficient but the basic thing, that money is being pooled or that risk is being transferred, that’s still happening. That’s mainly what customers are paying for. There’s nothing in the blockchain or any technology that changes that underlying fundamental economic function that has been performed.”

**Taxing tech**

The technology question goes beyond how corporate service providers will use digital solutions to enhance their own operations and value chains. Technology companies increasingly dominate among multinational corporations, and business is increasingly virtual rather than physical. In these circumstances, old rules about global taxation no longer serve.

“You have Netflix operating in many, many countries without any physical presence, and clearly the rules were designed one century ago”, says the regulation official in Paris. This has shifted priorities among governments and regulators. Countries where the world’s leading producers of goods and services predominantly resided in the past were keen to tax those companies themselves, and were less keen to have their services taxed where they were consumed. Now, governments are seeing large areas of activity go under-taxed because the producers reside elsewhere.

This raises an important role for IFCs, which could resolve many of the tax-related issues created by the technology industry. Rather than customers, these companies’ users are ‘part of the production process’, as a legal executive explains. “That screams out for the place where you would pull them all together, one that has to be a tax-neutral jurisdiction.”
As the industry responds to geopolitical upheaval, as businesses and jurisdictions come to terms with the demands of new regulation, and as radical technologies come on stream, the Corporate Services industry is going to become rapidly more challenging – and even richer with opportunity.

In this environment, we believe the world needs the Corporate Services industry more than ever before. And it’s up to the industry to make governments and individuals recognise the positive impact it makes.

Will this happen? We have good reason to suspect that it will. Many in the industry are optimistic about what they can achieve, and for good reason. But it won’t be easy: there are plenty of unfamiliar new challenges around the corner, as we set out in our predictions for the coming year.

The tech wake-up call is coming

If we could predict exactly how new technologies will impact the industry and its clients, then we would be a different business ourselves. But there is no doubt to us that the industry has yet to feel the force of disruption, whether that’s linked to data analytics, AI or the maturation of cryptocurrencies. Worryingly, however, our findings suggest that many in the industry are unprepared, even complacent, about the threat and opportunity of new technology. If they are not careful, they may soon find themselves scrabbling to catch up, or fighting for survival.

Conclusions and predictions

“I’m optimistic about growth prospects for the industry, though it’s going to be through a very different model than what we have lived with to date.”

Legal Executive, London
Politicised regulation will continue in the short term

Our hope is that cooler, technical heads will prevail and that industry regulation will lose its political edge. But it seems more likely that governments will continue to target the industry with crowd-pleasing transparency drives, at least in the short term. These regulations may create opportunity for some, but conditions for the near future are far from ideal, particularly when political expediency is compounded by tribalism and jurisdictional bias. As a result, privacy and public disclosure rules are likely to become even more of a competitive background for jurisdictions over the coming years.

The PR war will turn a corner

The good news is that anti-globalisation rhetoric is likely to become less heated in time. Globalisation may have its critics, but it’s here to stay. There is also plenty to say in its favour, not least that it has lifted hundreds of millions of people out of poverty around the world. For these reasons, despite pessimism from interviewees that the industry is ‘losing the PR war’, we believe that public sentiment is starting (slowly) to change. There is, for example, greater awareness among individuals that they and their pension funds directly benefit from the efficiencies provided by the industry. At the same time, work is being done to demonstrate the positive outcomes that the industry creates for individual jurisdictions, such as by supporting infrastructure. There is still some way to go before the public is more supportive or understanding of the industry, evidenced by the fact that electorates are currently voting against their own financial benefits. Still, we are hopeful that change is coming – and politically-motivated regulation will inevitably soften as a result.

Responding to wider trends, the industry will continue to change shape

The industry has evolved significantly in recent years. Our view is that client demand for scale, in addition to ongoing private equity ownership, will drive further consolidation among corporate service providers, potentially including the emergence of an equivalent to the ‘big four’ that dominate the audit industry. Private equity ownership is necessarily time-bound, and in some cases, the exit strategy for owners may increasingly become an IPO, which will create its own challenges as businesses strive to ensure their books are as clean as they can be. As we have speculated before, changing conditions may also give rise to consolidation among jurisdictions, as some jurisdictions struggle, or choose not, to keep up with the burden of ongoing regulatory change.

Emerging markets will increase in importance

In the immediate future, outbound markets will continue to represent a major source of growth, especially as geopolitical and economic developments compel clients in emerging markets to seek out a wider range of sophisticated services. Volatility in the oil market, for example, is creating demand for structuring services in the Middle East as returns become less predictable. At the same time, firms based in India are increasing their overseas investments, broadening their spread across geographies and sectors. Furthermore – and despite speculation in the media about a potential downturn – it is abundantly clear that China’s global influence will grow significantly in the years to come. As mentioned earlier in this report, however, established jurisdictions – notably post-Brexit UK – cannot assume that they will remain the most attractive destination for this business.
List of acronyms & abbreviations

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
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<tbody>
<tr>
<td>AI</td>
<td>Artificial Intelligence</td>
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<tr>
<td>AIFMD</td>
<td>Alternative Investment Fund Managers Directive</td>
</tr>
<tr>
<td>BO</td>
<td>Beneficial Ownership</td>
</tr>
<tr>
<td>BOTs</td>
<td>British Overseas Territories</td>
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<tr>
<td>BVI</td>
<td>British Virgin Islands</td>
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<tr>
<td>CRS</td>
<td>Common Reporting Standard</td>
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<tr>
<td>EU</td>
<td>European Union</td>
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<tr>
<td>FATCA</td>
<td>Foreign Account Tax Compliance Act</td>
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<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
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<tr>
<td>HNWI</td>
<td>High Net Worth Individual</td>
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<tr>
<td>IFC</td>
<td>International Finance Centre</td>
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<td>IPO</td>
<td>Initial Public Offerings</td>
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<td>IRS</td>
<td>Internal Revenue Service</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<tr>
<td>PR</td>
<td>Public Relations</td>
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<td>UAE</td>
<td>United Arab Emirates</td>
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<td>UK</td>
<td>United Kingdom</td>
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<td>UN</td>
<td>United Nations</td>
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