Vistra 2020
The Uncertainty Principle

The State of the Trust, Fund and Corporate Services Industry 2017: Transformative Factors, Adaptation, and Growth
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Since our last report, *The New Normal*, the world has undergone major geopolitical, geostrategic and economic shifts. The combined impact of these changes, as well as an eroding sense of confidence in ‘expert’ political or financial prognostication, all have swept away the idea of ‘normal’, and especially of a reliable status quo. If anything, the only thing predictable about world events these days is the unpredictability of their outcomes.

The effects of this uncertainty are playing out in the Trust, Fund and Corporate Services industry across the board. Although almost everyone we spoke to at length for this year’s report reaffirmed their optimism about the future of the industry, longtime readers may spot notable changes in results from years past.

Readers may also notice a shift in the branding behind the 2017 report. That is because OIL, the longtime thought leader of the report and leading company formation specialist, has rebranded to Vistra.

This heralds an exciting new chapter for Vistra. In operating as one united business, we combine our resources to lead as a global service provider in international incorporations, trust, fiduciary, and fund administration services.

A few other elements have changed as well. We broadened the geographical scope to include more opinions from Europe, where some 46% of respondents are based. About 30% are based in Asia, 18% in the Americas (mostly in the US), and the rest in the Middle East and other parts of the globe. We also continue to include a wide span of industry segments; Law, Corporate Services Provider/Consulting Firm, Accounting/Taxation, Banking/Financial Advisory, Investment Management, Regulatory Agencies, Supranational Organisations, and Academia.

We also increased the sample size of our annual survey by nearly half, to almost 600 respondents [Figure 1]. As with previous years, we conducted qualitative interviews with C-suite industry executives from around the globe. We combined assessments derived from those talks with close analysis of the quantitative data from our annual survey. The expansion of our sample size, of our industrial and topical scope, and of our geographic span, all helped yield rich and nuanced insights for the 2017 report.

We trust you will enjoy the read and welcome any feedback on how the report can be improved.

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**Foreword**

**Welcome to the Vistra 2020 report for 2017, *The Uncertainty Principle*.**

Since our last report, *The New Normal*, the world has undergone major geopolitical, geostrategic and economic shifts. The combined impact of these changes, as well as an eroding sense of confidence in ‘expert’ political or financial prognostication, all have swept away the idea of ‘normal’, and especially of a reliable status quo. If anything, the only thing predictable about world events these days is the unpredictability of their outcomes.

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This heralds an exciting new chapter for Vistra. In operating as one united business, we combine our resources to lead as a global service provider in international incorporations, trust, fiduciary, and fund administration services.

The rebranding constitutes more than just a name change, however, we are broadening the scope of the historical ‘Offshore 2020’ report to represent the wider industry(s) in which Vistra operates. For example, in this year’s report, we have briefly touched on some topical issues in the alternative funds industry.

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**Jane Pearce**
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2011 | 92
2012 | 155
2013 | 228
2014 | 284
2015 | 320
2016 | 593

**Figure 1 Survey sample size**

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We trust you will enjoy the read and welcome any feedback on how the report can be improved.
Introduction

“The uncertainties mean [some] of the deals we see in Europe will be put on the back burner until we know more.”

Private Equity Fund Executive, New York

When we last closed our annual assessment of the International Financial Centre (IFC) and Trust, Fund and Corporate Services industry, we did so with a note of cautious optimism. The regulatory dread was fading as the industry practitioners got to the good, great business of adapting to ‘the new normal.’

But a year later, consistency has given way to uncertainty, the ripple effects of which are being felt both onshore and offshore. For example, uncertainty about the global economy, immigration, terrorism, Russia, the Chinese economy, and the stability of the EU, have all helped foment considerable shifts in the global geopolitical landscape.

“I’ve stopped predicting,” one funds specialist told us shortly after the US presidential election in November. “Clearly, my crystal ball needs servicing.”

That election, Brexit, the Italian referendum, and the rise of Geert Wilders and Marine Le Pen in Europe all point to large-scale unease with the status quo. They also reflect the concurrent prominence of a more populist, protectionist, anti-globalisation, and anti-offshore/private equity attitude taking shape in the West. Indeed of the nearly 600 corporate services industry executives who took part in our survey this year, 71% agreed that globalisation is at least ‘slightly under threat’ [Figure 2].

Figure 2  Threat to globalisation

Source: Vistra
Such a shift in the public appetite for cross-border flows unsettles an industry predicated on the robustness of globalisation; our success depends on cross-border transactions and international supply chains, as well as free trade and investment.

As this anti-globalisation zeitgeist becomes more widespread, as well as increasingly influential on world elections, cross-border flows could become so maligned that “taking your wallet on an overseas flight becomes a crime,” joked one expert. Rising disdain for borderless activities could lead to more regulations, more nanny-state oversight, and more ‘gotcha’ hit pieces that mislead the public and further feed the beast.

Anti-globalisation attitudes are nothing new. But we must note the sheer speed and force of these attitudinal shifts, as well as the policies they help usher in.

“It’s a strange time,” said one industry expert in Dublin. “I’ve been in this business for 15 years, and the last two have exponentially flown by, unlike we’ve ever seen. If that is combined with US tax reform, it’s really going to put everything upside down.”

For seven years now, Vistra 2020 has taken the temperature of the industry. This year, increasingly heated debates about politics, wealth, taxation, trade, inversions, privacy, and regulation are creating a fever pitch about the future of the industry and IFCs... so much so, in fact, that the percentage of respondents predicting the end of offshore by 2020 nearly quadrupled to 18%.

That said, more than half of the respondents firmly believe that demand for the industry and IFC services will either increase or simply shift in jurisdictional preferences, and nearly all of the largely C-suite practitioners we spoke to at length reaffirmed their optimism about the future of the industry.

More changes are on the horizon though, this September, dozens of countries will for the first time have to exchange information with other countries in accordance with the Common Reporting Standard (CRS) mandated by the Organisation for Economic Co-operation and Development (OECD). The group’s other major regulatory scheme, Base Erosion and Profit Sharing (BEPS), is coming into full swing as well. As of February 2017 writing, the French, German, and Dutch elections all loom. Brexit is being negotiated and a new US president has just begun taking critical decisions about trade, China, and taxation.

For this year’s report, we focus on how these changes might unfold, and what their hypothetical consequences on our industry might be.

Every year we are surprised by some of the results. This year is no exception.
Overall Outlook

“I think [the uncertainty] can work in our favour. We’ve had a tumultuous vote in the UK, a president of unknown pedigree in the US, more unpredictable elections coming up. Every time leadership changes, so does the environment... What clients are looking for is stability, and the IFCs are going to be little islands of calm.”

Attorney, UK Law Firm

Uncertainty, unpredictability and instability: if events over the past year have proven anything, it is that volatility will be at the fore as we speed towards 2020.

Politics has perhaps been the most visible stage for the theatre of change, and some in the industry are putting activities on hold as they await the next act.

“There will always be [for example] good French investments, but at this point in an uncertain future... maybe we sit back and watch a bit,” strategised a private equity fund executive in New York City.

Banks, fund managers, and investors in the UK are exploring options as they wait to see how (or if) Brexit will unfold. Companies with an international presence, both large and small, are watching how the Apple case in Ireland will play out. Similarly, the industry is wondering about President Trump’s tax and trade policies and how hard his administration will crack down on offshore inversions.

Says one fund manager in the US, “The last thing most investors want is uncertainty and unpredictability.”

Of course, uncertainty is not confined to Europe or the US. Indeed, it plays out in the East: as its economy slows, China is cracking down on capital flight;
foreign exchange reserves are falling; the renminbi is depreciating; and rising US interest rates are impeding China’s management of its burgeoning debt. The result, those in the region tell us, is that China’s wealthy are seeking out arbitrage strategies.

China’s increasingly regulated environment also is affecting Hong Kong’s long-term prospects as an offshore powerhouse. And in India, Prime Minister Narendra Modi’s sudden ‘anti-corruption’ campaign against larger rupee notes may be an experimental harbinger of what is to come: a cashless society in which governments have much more access to compulsory digital transactions conducted by citizens. In late January, in fact, the European Commission issued a ‘Road Map’ to initiate continent-wide legislation against cash.

Then there is uncertainty within the industry itself, specifically as regards regulations. For example, uncertainty about the coming impact of CRS – which interviewees deem ‘more dangerous’ to the industry than the US Foreign Account Tax Compliance Act (FATCA) – is creating anxiety among some providers, as well as among clients seeking tax-efficient strategies. Most dangerous of all, perhaps, is the push towards registries of beneficial ownership (BO), which many in the media not only agitate for, but would like to see made public.

Industry scandals no doubt help their case. By selectively highlighting outlier cases, many reporting on the Panama Papers pushed the tired narrative that the system rewards the wealthy by victimising those less fortunate, thereby bolstering the perception that all offshore activities are wrong. Never mind that the ultra wealthy – and this is just the top 1% – pay 39% of the taxes in the US, and a similar percentage in the UK.

And never mind that there were enormous errors committed in the so-called reporting of, say, David Cameron’s involvement. Such errors contributed to the public’s misunderstanding about, and rancour over, the legitimacy and benefits of the industry. London wealth advisor James Quarmby did his part to correct the fallacy, famously schooling the BBC on air about the difference between a trust and a corporation.

“The real economy may be slowing down, but hedge fund managers prefer volatility,” said one such manager in Hong Kong.

Tax planners also might benefit from the exact regulations that make their jobs harder: “Tax planning is becoming a lot more transparent. What comes with that is more work, more activity, and more services needed,” said one planner.

And in a time of political and economic unrest, ultra high net worth individuals (UHNWI) may find more need for wealth managers, as well as for stable jurisdictions.
As we said earlier, despite the uncertainty – or perhaps because of it – the majority of respondents believe that over the next five years, demand for international corporate services is unlikely to change. Twenty percent even believe demand will actually increase, although an equal percentage believe demand will decrease [Figure 3].

“The industry is under great threat from misguided politicians and regulatory malcontents. This is a potent mix.”

General Consul of Investment Management/Funds Firm, HK

![Figure 3 Demand scenarios - industry most likely to face over next 5 years](source: Vistra)
These numbers reflect a similar result from last year; nearly six in ten of our respondents from 2015 believed that demand for services would either stay the same or grow approaching 2020.

But where those services occur could indeed change over five years. It surprised us to see the most negative view about demand coming from respondents in Asia, with 26% ascertaining that it will drop [Figure 4].

For example, the combined market new incorporation (NI) volume of the BVI, Cayman Islands, and five other jurisdictions dropped significantly between 2013 and 2016P, from 97,272 to 71,834. The biggest decline occurred between 2015 and 2016P.

We maintain that economic and geopolitical unsteadiness are in part driving these numbers.

Among all respondents, in fact, ‘political uncertainty’ received an average ranking of 3.5 on a scale of 1 (least important) to 5 (most important) as a constraint to business [Figure 6].

In 2015, the frothiness of the Asian economy led to a buoyant outlook by the majority of our Asian respondents. This year’s dimmer view perhaps can be attributed in part to the increasing scope and complexity of the regulatory environment mandated by the Chinese government. We will explore Hong Kong and Singapore’s prospects in a moment.

Overall, more than half of this year’s respondents see business shifting away from traditional offshore centres. Some 40% see it shifting onshore or midshore, and 14% see activity jockeying among traditional offshore locations.

“There’s an increasing appetite for top-tier offshore and onshore,” said one expert, citing “Ireland, Cayman, to some extent Bermuda, Jersey, Hong Kong, Singapore and even Delaware continue to increase in market share as well.”

Still, demand for offshore incorporations is down across the board [Figure 5].
Also driving business down are regulations that force us to do business with one hand tied behind our backs.

Although we noted earlier the collective dread around CRS, a.k.a. ‘GATCA – Global FATCA,’ equally impactful on business is the likely implementation of registries of BO, especially if they become public.

Most respondents (58%) think such information should remain with providers and given to authorities upon request [Figure 7]. But the same percentage also expect that by 2020 we will see central, non-public registries [Figure 8].

That is similar to last year’s expectations (59%). However, the real surprise is the number of respondents who expect to see registries of *publicly available* information by 2020; the percentage of responses saying yes nearly tripled, from 16% to 42% [Refer to Figure 8]. And such a scenario, the same respondents said, represented by far the biggest potential impact on their businesses. We will address this further in the privacy section of this report.

![Figure 7 Availability of BO](source: Vistra)

<table>
<thead>
<tr>
<th>Likely by 2020</th>
<th>Likely impact on business (5 – most important)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Full implementation of CRS</td>
<td>77% 2016 3.3 2015 2.2</td>
</tr>
<tr>
<td>Industry disrupted by technology driven innovation – will lower costs &amp; change business model</td>
<td>60% 2016 3.2 2015 —</td>
</tr>
<tr>
<td>Central (non-public) registry of BO</td>
<td>58% 2016 3.0 2015 3.0</td>
</tr>
<tr>
<td>Global tax accounting standards</td>
<td>42% 2016 2.8 2015 2.7</td>
</tr>
<tr>
<td>Publicly available BO information</td>
<td>42% 2016 3.2 2015 4.1</td>
</tr>
<tr>
<td>Uniform global (non-tax) regulation such as licensing of corporate service providers</td>
<td>38% 2016 2.6 2015 2.6</td>
</tr>
<tr>
<td>End of the use of offshore structures</td>
<td>18% 2016 3.3 2015 4.3</td>
</tr>
</tbody>
</table>

![Figure 8 Which of the above are likely by 2020, and which will cause the most impact to business](source: Vistra)
The Zeitgeist

Why such an increase in the expectations of publicly available information, something that ‘would have been unthinkable even 10 years ago’ according to a UK-based interviewee. Those we spoke to largely blamed the populist zeitgeist, which they believe kicked into high gear with the release of the Panama Papers and the US presidential and Brexit campaigns, and is underscored by a ‘rising populist, quasi-socialist attitude and a resentment of wealth.’

“[The Panama Papers] fanned the flames of righteousness and gave weight and urgency to the idea of such registries,” said one respondent. “People are offended by money, and one is not allowed to offend in this day and age of political correctness.”

Hon. Wayne Panton, Cayman Islands’ Minister of Financial Services, recently addressed ‘stubborn misperceptions’ about jurisdictions such as his at a panel discussion hosted in February 2017 in Brussels at the Centre for European Policy Studies.

“We have evolved our tax system to suit our needs, as is our right. And we have never designed the system to compete with tax systems in any other jurisdiction,” he explained. “But nevertheless, we are often seen as a tax competition threat – and this clouds the reality that our system supports rather than harms other jurisdictions.”

That clouded reality informs the push for, and impact of, blacklists. The upcoming EU blacklist, for example, is viewed with ‘wariness’ by respondents; no one would name specific jurisdictions in jeopardy, but the consensus was that offshore would be scapegoated more than onshore.

“[Such a list] can have a seismic effect in those jurisdictions,” said one respondent in one such locale.

A prominent industry researcher lobbed accusations of “strong double-standards in play. I think, increasingly, you do see criminals shifting to the use of onshore vehicles, like British or US companies, precisely because of the great stigmatisation of offshore.”

“It’s just a lot easier to put pressure on the Caymans and face down the Caymans than it is the National Association of Realtors,” he added. Blacklists, he said, go after the little guys because they are easy targets.

“We are on whitelists around the world,” added a hedge fund manager in Cayman Islands. “Now again, there’s lots of discussion about Cayman Islands being put, in fact, on a blacklist simply because it has a zero-tax regime.”

Added a hedge fund manager in Jersey, “The Channel Islands, for example, and other offshore centres are being used as a bit of a punching bag by politicians around the world. But Delaware is alleged to be the biggest tax haven in the world… and it’s off limits for criticism.”

Adding to the frustration is the thanklessness of rigid perpetual compliance. No matter what certain jurisdictions do to fight illegal activity, the public perception effects of J’accuse! seem unmitigated.

“We cannot achieve transparency outcomes until we stop basing global initiatives on alternative facts posing as unassailable truths,” Hon. Panton stated during the panel discussion in Brussels.

“No recent international measures have been given the chance to work before other initiatives are introduced,” he further attested.

An academic researcher we interviewed expressed a similar viewpoint, as well as certain scepticism about efficacy.

“Maybe the dull work of implementation and enforcement is less amenable to exciting media releases. But if you’re interested in curbing or reducing money laundering, tax evasion or so on, enforcement and implementation are the name of the game.”
The regulatory, economic, and geopolitical climates all have swayed our survey rankings this year from last year. (Again, do keep in mind that more survey and interview respondents came from the West than did so last year.)

As we noted earlier, some 40% of survey respondents believe that there will be no change in demand for new structures over the next five years, but instead that there will be a shift from offshore to other offshore or to onshore/midshore jurisdictions [Refer to Figure 3].

“IT’s where the tide is going,” concluded a funds expert in Dublin.

This view is definitely reflected in the rankings, which shows meaningful evolution from last year [Figure 9].
For six years, ‘The Big Four’ have consistently outranked other jurisdictions. Hong Kong and Singapore stood as the most important leading into 2020, followed closely by the BVI and Cayman Islands.

But this year’s results show a marked shift; Hong Kong still does well, and the BVI ranks third again, but Cayman Islands is sixth and Singapore seventh. And even though only 8% of survey respondents were based in the UK, their jurisdiction is rising in prominence.

“UK’s future depends on how interesting or uninteresting it becomes outside of the EU,” mused one respondent.

Watching closely and affected no matter what happens with Brexit are those in the Crown Dependencies (CDs) and Overseas Territories (OTs).

“We in Cayman are the children caught in a nasty divorce,” said one fund manager there. “We don’t get much say. We’ll simply be downstream victims of the arrangements’ shortcomings.”

Unlike in the UK, CDs, and OTs, uncertainty seems to be helping, not hurting, the US. It trumped Western Europe in the survey.

Respondents credit a “perception of [President] Trump being pro-business, and therefore less hysterical about offshore.”

“Anyone with that kind of wealth is going to have some exposure offshore,” added a fund manager. “Not that they’ll be advocates for offshore, but they’ll see that no focus is brought to the area.”

“The US will see significant growth in the next five years as a capital market,” added another investor in Europe. “It may be a bit early to tell what Trump’s going to do, but it could be that as a nation, the US is too big to fail.”

“It’s really hard to vote against the US, given the size, the internal contiguousness, and the innovation of the market,” added a private equity executive in New York who just relocated from Singapore. “If you had a choice between investing in a business in still a tightly-knit US – albeit one that’s less pro-free-trade – or investing in a comparable business in France on a fragmented continent, you would pick the US twice out of three times.”

The US also might see a short-term boost from the fact that providers are wary about CRS, something the US refuses to join.

“There’s short-term appeal for the private client, that you can maybe buy a few more years financial privacy if you go [to the States],” said one service provider in Cayman Islands.

Even with the rise of the US, European jurisdictions did quite well in this year’s survey. Luxembourg performed three times as well as the Netherlands. Although this could be due to the fact that 13% of survey respondents hailed from Luxembourg and only 3% from the Netherlands, it also is consistent with previous years’ results.

This isn’t to paint a rosy picture for either jurisdiction, though. Industry experts in the Netherlands tell us they are nervous about the election and a possible ‘Nexit’ if Mr Wilders wins. Both countries face increasing pressure from an anti-offshore/onshore EU. In other words, “opportunities are strong, but there’s definitely potential for things to go in the wrong direction,” said one industry executive with employees in the region.

In their favour are their strengths. The Netherlands holds its own due to being “in the top jurisdictions of a favourable tax climate and an open tax authority that’s willing to think proactively,” said one Dutchman who works in the US on international tax arrangements.

Added a fund manager, “I think that the pattern we’ve seen over the last few years has been a growth of parallel structures for managers across, broadly, those three different domiciles. So, onshore Europe in Luxembourg, offshore Europe in the Channel Islands, and Cayman Islands and Delaware for North America.”

What do the survey results imply for traditional offshore powerhouses such as the BVI and Cayman Islands?
Last year, we wrote that clients in the East still wanted ‘a BVI,’ especially as a conduit jurisdiction. This year, however, we’re seeing an uptick in an ongoing trend of solely using Hong Kong.

This shift is largely due, say tax experts in the region, to Chinese crackdowns on offshore and on tax efficiency.

“Yes, [BVI is] still the top four but may be tailing off a little bit,” said one corporate registration provider in Singapore. “My Chinese clients know they’ll need to pay at least some tax. So they go through Hong Kong to get some benefit while satisfying tax authorities.”

Regulations also drive the shift. Multinational companies are increasingly choosing to establish business substance in Hong Kong because tax treaties between China and Hong Kong, or China and Singapore, require substance in order to invest in China and Chinese companies.

“They definitely prefer establishing substance in Hong Kong, with its legal channels, than in China,” said a service provider in Singapore. Still, the BVI is ‘an embedded brand’ and still the go-to for most structuring conduits.

“To put it in perspective, we’re (BVI) still going to incorporate roughly 35,000 companies,” said one BVI official.

And Hong Kong has some long-term hurdles to overcome. For example, domiciled funds, especially institutionalised ones, remain relatively expensive to set up. The BVI and Cayman Islands also offer more comfort to those looking for ex-China legal systems, especially as Hong Kong’s free trade and court systems come under increasing pressure from Beijing.

Currently, though, Hong Kong still outperforms its regional competitor, Singapore. So do the UK, the BVI, the US, Luxembourg, the Netherlands, and Cayman Islands, which this year all outranked Singapore.

Many blame the recent Indonesian tax amnesty that caused “everybody to scramble to report offshore activities to the Indonesian government. They’re worried about information exchanges, or being slapped with a hefty penalty,” said a legal expert in the region. Singapore, others added, has been undergoing what Switzerland experienced in the ripping away of banking privacy.

“Singapore is both over- and under-regulated,” said a tax attorney based there, “it recently fell a number of spots on the global competitiveness survey, and the capital it had been pulling in from China, Indonesia, and Malaysia is drying up.”

Singapore, however, still is expected by some we spoke to in the region to eventually take business from Hong Kong.

“One of the things I heard a long time ago, and I’m always struck by how correct it is,” said a general counsel in the region, “is that in China, it’s not a lack of law; it’s that there are too many laws and you don’t know, at any given point, which ones are going to be enforced. That could hurt Hong Kong.”

This is especially true going into year 2047. The full unification with China may “sound like a long way off,” said one investor, but “the political landscape is a little bit shaky,” said a legal expert in Singapore.

“I do hope Hong Kong continues to be this amazing free port for globalisation, but if you’re going to make a decision, maybe you’d choose Singapore.”
The good news first, despite complaints about the increasingly costly and time consuming regulatory environment, as well as fears about crackdowns on the industry, a strong 82% of survey participants see no end to the use of offshore structures by 2020 [Refer to Figure 8].

Still, regulations are having an impact. Part of it, participants acknowledged, may be positive.

“A lot of the planning gets very cute,” said a compliance specialist in Asia. “Just because something works on paper doesn’t mean it works anymore.” Regulations can help enforce impeccable, and more realistic practices.

Still, FATCA, UK FATCA, the EU’s Alternative Investment Fund Managers Directive (AIFMD), the UN’s Anti-Money Laundering (AML) Convention, and the OECD’s BEPS action plan and CRS all continue to put downward pressure on the industry.

Although everyone suffers from the cost of compliance, here again, traditional offshore centres may suffer more than others. When weighing the effect of regulation, the BVI (63%), Seychelles (56%), Mauritius (51%), Cayman Islands (53%), Guernsey (44%) and Jersey (44%) all received high levels of responses indicating adverse effects [Figure 10].

Even when responses are broken down by region, all agree that traditional offshore centres, the BVI and Cayman Islands, could continue to come under the most adverse pressure from regulations.
CRS is perhaps set to shake things up the most this year. It establishes automatic information exchange among participating national revenue bodies. Like FATCA, there is an information flow, but unlike FATCA, where the flow is a one-way street towards the Internal Revenue Service in the US, CRS is a two-or-more-way street.

More than 100 countries – save the US – have signed up. Early adopter jurisdictions begin reporting in June 2017, and information exchanges among competent authorities will commence in September 2017. Some 77% of respondents – 5% more than last year – believe that by 2020, CRS will be fully implemented.

Although CRS is a global initiative, it remains unclear whether other major countries will send information to the US if nothing is received in return. As we wrote last year, “Will [the US absence from CRS] serve to weaken FATCA... or merely to increase the number of hoops jurisdictions must jump through? That all remains to be seen.” And it still does.

Either way, the looming burden of ‘FATCA + CRS = bloody compliance costs’ has this year’s respondents seeing CRS as a significant burden. On average, they rank the idea of full implementation a 3.3 on a scale of 1 (strongly disagree) to 5 (strongly agree) in terms of business constraints. And in interviews, providers stated that the impending CRS regime could render compliance ‘a true nightmare,’ and turn private individuals away from traditional offshore jurisdictions. They are also skeptical about how CRS will ultimately work.

Offers a survey respondent, “I have strong doubts about how local tax authorities in different countries will manage those enormous amounts of information.”

Still, “we are building the pipelines, the common transmission system,” said a high-ranking official from the OECD, “and massive progress is being made.”

Logistics aside, four concerns rest with CRS. One is that the US may asymmetrically benefit from not joining, thanks to a perception of opacity.
A second one has to do with the erosion of privacy, part of a macro campaign to create complete transparency in the industry.

“We have a crazy situation in which countries with little respect for data, privacy, and data protection have signed up to CRS,” said a tax attorney in London. “The possibilities [for abuse] are endless.”

Thirdly, eagerness to capture more taxation gains will not just hamper, but eventually make impossible, the ability for businesses to engineer tax efficiency.

Indeed, the OECD official called the difference between tax avoidance and tax evasion ‘semantics.’ He prefers to frame tax efficiency planning in terms of black (evasion), white (full compliance), and grey, where “you can be in dark grey, where you’re really testing the legislation, or in light grey.” The goal of CRS, BEPS, and other initiatives is to largely eliminate the grey at a supranational level. Loopholes run “contrary to the spirit of the law” he said. “[These new regulations are] a signal to taxpayers that there is a change in paradigm.”

“If some jurisdictions just clean up their legislation, but then they don’t clean up their business,” the official added, “then they will be hit one way or another and lose it all.”

Statements like that one have pressured low-tax jurisdictions in particular to join CRS. For this reason, more than a few experts deem CRS ‘more dangerous than FATCA’ to the industry’s prospects, introducing the fourth concern, that CRS is yet one more step towards a consolidated tax authority designed to eliminate low-or-zero-tax regimes.

Indeed, in the quantitative survey, 42% respondents thought it possible to have global tax accounting standards by 2020... a first step towards a single tax authority.

Additionally, nearly 50% of respondents either agree or strongly agree that by 2020, the globe will be a network of Tax Information Exchange Agreements (TIEA) which will entwine all major offshore financial centres into a global tax data sharing agreement. Still, 27% of the respondents are neutral on the subject, and another 23% either disagree (17%) or (6%) strongly disagree [Figure 11].

Although acknowledging the drumbeat, a compliance general counsel in Asia pointed out the difficulty of implementing such a scheme.

“In the US, you don’t have a single tax rate,” he observed. “In Europe, they struggle with it. How do you reconcile the US, Europe, Japan, and China? Could they agree on a single tax? How do you allocate it?”

Still, respondents do not discount bureaucrats’ ambitions to decrease the global tax gap. In fact, according to OECD Secretary General, Angel Gurría, CRS already has shrunk that gap by more than €50 billion. And he made that assessment a full year before reporting was set to start.

“One of their proposals is a common consolidated tax base in the EU, which is completely the opposite of protectionism sovereignty,” comments one respondent in London, an attorney. “Is there going to be a moment in the next 12 months that the EU gets [another] slap in the face? [Nexit? Quitaly?] By jurisdictions saying, ‘You’re going too far. I’m not going to give up my sovereignty.’?”

In the meantime, complexity not only with CRS, but with BEPS, continues to cause consternation among respondents.

We asked the OECD official if building such complexity into the system was a deliberate strategy to thwart tax planners.

“No, because our strategy is to promote certainty,” he responded. The complexity of existing international rules, double taxation treaties and the like, he said, has
created an environment that has “facilitated avoidance… To kill these complex instruments, we’ve developed complex draft legislation that will level the playing fields among taxpayers.”

We will take that as a yes.

Because both BEPS and CRS and their incumbent issues are coming into full bloom this year, it’s no surprise that, just as with 2015, new regulations currently are considered the top constraint to business.

This result varied only slightly when broken down by region [Figure 12].

Additionally, of the seven regulatory factors we asked about as likely by 2020, five ranked at least a 3 on a scale of 1 (least impact) to 5 (most impact) in terms of impact on business [Refer to Figure 8].

This reflects last year’s survey finding that regulations had for the first time become a bigger constraint to business than previous hurdles such as competition and pricing.

This is telling. As of this year, AML and Know Your Client (KYC) processes, as well as the difficulty of opening and maintaining a bank account, have further edged out competition and pricing.

The biggest impediments to success, in other words, come not from within the industry, but from without.

![Figure 12](image-url)
When examining the underlying drivers of the industry, the fundamentals remain the same. But probe beyond the surface level and two key macro drivers emerge… one old, and one new.

Before we examine those two macro drivers, however, we must note that traditional drivers of business do indeed continue to hold court. Last year, wealth planning slightly edged out asset protection, emerging market wealth, and increased client sophistication as important drivers to business.

This year, wealth planning came out on top again, followed by asset protection, privacy and client anonymity, and growth in the funds industry (and then emerging market wealth). When broken down by region, increased client sophistication proved to be a primary driver as well [Figure 13].

"All parts of the asset management service area will have to step up. Technology will flow-up quite quickly."

FinTech CEO, Jersey
Indeed, respondents predict that as clients become more sophisticated, especially in emerging markets they will want more complex ‘solution packages’, said a service provider in Singapore. “It won’t be just incorporation and done.”

Such packages, she said, might combine incorporation, trusts, wealth planning, and asset protection with technology such as robo-advisory. Technology, it turns out, is one of the two macro drivers we unearthed.

The other is privacy. What is particularly interesting in this year’s results is that, whether due to an uptick in regulations, bad publicity from the Panama Papers, an increase in awareness about hacking or some combination of all three, privacy and client anonymity is now officially a key driver of business. This ‘old’ driver is finding new life shaping multiple levels of the industry. On a minor level, protecting what is left of privacy is increasingly important, and industry experts already are ramping up cybersecurity.

“The client is educated and understands that privacy and data safety is key,” said one service provider in Asia.

The industry’s response to the erosion of privacy, however, will play an even bigger role in how services take shape over the next few years.

Privacy – an ‘old’ driver with new repercussions

While the days when we could protect and completely assure client privacy are long gone, our industry still considers privacy a flashpoint. In our interviews, for example, by far the most passionate comments made addressed the systematic obliteration of privacy in the pursuit of tax gains.

Privacy is a human right, at least as delineated by the UN Universal Declaration of Human Rights. But we now live in a world where a desire for dignity, and a reticence to publicly denude oneself, immediately garners suspicion.

It is not just confined to the world of finance; ‘I have nothing to hide’ has become a mantra of sorts as tech-obsessed consumers willingly hand over details about their health, their comings and goings, their internet searches, their email contents, their text messages, their current locations, and even their immediate feelings to myriad corporate and government interests.

But ‘I have nothing to hide’ is a red herring. Its utterance immediately legitimises the search – and the intrusion – in the first place. It implies there is something wrong with the very notion of privacy, which is a dangerous premise.

An increasingly lax stance towards privacy in the general public may be the result of naivety about the intentions of the data seekers. It may stem from a desire for convenience, or from a general sense that if no one has any privacy, then the playing field has been levelled.

But this laxity is, in our view, an insidious development that has allowed governments, journalists, and the general public to conflate privacy with ill-intentioned secrecy, and to methodically obliterate the idea of personal human dignity, replacing that dignity with ‘data’ that must be offered in service to the state.

“Some of my clients have moved from Sweden to the UK, as they don’t want everyone in their village to know how much they’ve earned,” said a prominent legal expert in London. “Your neighbours can look up how much you’ve earned, what deductions you’ve claimed. They know to the penny what you’re worth.”

If such knowledge gets out in, say, Medellin, Manilla, Moscow, Myanmar, or Mianzhu, the consequences could be grave. It is not unheard of for a child to be kidnapped and ransomed because private family financial information had been disclosed.
“How confident are you, as a wealthy Colombian, that the CRS report made by your Swiss bank to the Colombian government is only going to be used for legitimate tax appraising purposes?” queries an attorney.

“In China – and Russia too – rich people do have this unfortunate habit of being purged or imprisoned,” agreed a prominent academic, one who generally is not the biggest cheerleader for offshore.

“People tend to assume that the rest of the world is like the US, Australia, Denmark, and most of it is not,” he added. “People in most other countries have the sneaking and probably correct suspicion that their governments don’t care about them that much, and are not above entirely violating the rule of law when it suits their purposes.”

And if a citizen wants to open a bank account in Switzerland, or incorporate in the BVI?

As the prominent OECD official admitted “A government can always decline a request for data, but automatic exchanges of information are different, because you don’t know what you’re sending.”

In other words, not only are we being forced to share what once was indeed considered private, but now we do not even know what is being shared about us.

Government officials, of course, claim the mantle of righteousness and insist that all of this data collecting – FATCA, UK FATCA, CRS, KYC, BEPS, etc., is done to prevent fraud, money laundering, and tax evasion.

But they do not dare request the same kinds of disclosures for domestic activities. Even in Scandinavia, one is not compelled to hand over checking or savings account details.

If a US person keeps assets in Colorado, even if invested as cash into a marijuana dispensary, this is ostensibly allowed because the assets are domestically held. Sending the same assets to Cambodia to invest in a factory, and protecting them with a legally robust BVI structure, however, might be greeted with disdain by those who equate offshore with criminal activity.

That attitudinal zeitgeist was noted by our respondents, who rank current levels of client privacy between a 1 (fully private) and 3... and see it in five years’ time as collapsing to somewhere between a 5 and 8 [Figure 14].

The results perhaps reflect the unrelenting march towards registries of BO. As stated earlier, about 60% think there will be a central (non-public) registry of BO by 2020 and rank business impact a 3 out of 5 (most impact). Forty-two percent think the registries will be publicly available and rank the impact on business slightly higher at 3.2. This is a significant shift in opinion from 2015, where only 16% of respondents thought registries would be publicly available, and ranked the potential impact on business as 4.1 [Refer to Figure 8].

In other words, more people seem to believe that privacy will be further eroded but are less perturbed by its potential impact. Perhaps they see revenue potential in embracing the inevitable and turning it to their advantage, as we will explore in the technology section below.
Still, the European Data Protection Supervisor (EDPS), for one, seems to recognise the slippery slope that ever widening data capture boundaries could approach. In January 2017, the EDPS released an opinion regarding the European Commission’s aim at ‘tackling directly and incisively tax evasion’ by expanding the AML Directive to include purposes that went well beyond the scope of AML and terrorism investigation.

“Processing personal data collected for one purpose for another completely unrelated purpose infringes the data protection principle of purpose limitation, and threatens the implementation of the principle of proportionality,” stated the EDPS.

In other words, amassing and processing relevant data for the specific purpose of countering terrorism and money laundering is acceptable. But doing so just in case there might be some random, theoretical tax evader in the bunch is invasive, violating the financial privacy of the many in pursuit of the few.

Avoiding such scenarios undergirds the purpose of limitation principle; personal data may only be collected for specified, explicit, and legitimate purposes.

And this is precisely the issue with the rise of technology in relation to privacy – once people start amassing huge amounts of data, there is the potential to invent reasons to dig into it and possibly abuse it. The same applies to the idea of public registries. Once the information is out there, people or campaign groups with an agenda can find ways to manipulate that information to support their narratives.

The EDPS’s statement also recognises a second, equally important principle, that of proportionality. Proportionality demands that in the case of competing values, a measure should not go beyond what is required to attain a legitimate goal, and it also weighs whether the claimed benefits exceed the cost.

In the case of public registries of BO, the claimed benefits absolutely do not exceed the cost. Again, the very real threat to the safety of those individuals named, as well as to their families, immediately cancels the legitimacy of what would likely turn into a public witch hunt. So do the possibilities of identity theft and public harassment.

Most we spoke to vehemently oppose public registries, citing as their main concern the safety of their clients and a lack of confidence in the provision meant to protect safety by not making certain data public. They also note that forced transparency limits corporate play-books, as strategies will be exposed to their competitors at all times.

Reflecting those conversations, most in the quantitative survey (58%) think that such information should remain with licensed and regulated service providers, and be provided to authorities only upon request [Refer to Figure 7].

Their objections may hold little sway with regulators. And sadly, once privacy is gone – especially in this digital age – it is gone for good.

Technology

One would be remiss to note any drivers of business – or garner any predictions about the future of the industry and IFCs – without mentioning technology, the ‘new’ macro driver that undergirds everything from regulations to business opportunities. It is technology that allows for automatic exchanges of data. It is technology that allows the swift and complete erosion of privacy. It is technology that allows for immediate sways in the global market. And without digitalisation, BEPS, CRS, FATCA and the like would be very difficult to implement.

The inexorable decline of privacy, the ‘old’ macro driver, coupled with advances in technology, allows service providers to create disruptive – read: money making – opportunities. We are also early enough in the disruption that new players might still meld the evolving relationship between people, technology, and money.

Nearly 60% of respondents think that by 2020, technology will disrupt the industry with innovation that will lower costs and fundamentally change business models, and most see that as having some-to-moderate impact on business [Refer to Figure 8].
But even here, there’s uncertainty.

“There’s always a degree of nonspecific froth in relationship to technological change,” said an English wealth manager. “A lot of people talk about FinTech and Big Data. They’re aware that something important is happening, but they’re just not quite sure what.”

“FinTech, for example, inspires talk about disruption with a capital D,” mused a fund manager in the US. “I think it will be a series of small, lowercase d disruptions.”

Those lowercase d disruptions will likely change the face of banking as we know it going into 2020 and beyond.

“Why on earth would anybody need a bank? You have an electronic wallet. You’ve got a phone,” said a banker in Dubai.

Wealth managers will need to change course as well. “The old, relationship-intensive model is on the verge of destruction,” relayed a private banker in Hong Kong.

Whereas wealth managers are “limited by their capacity between their two ears, for us, the whole shift will be to harness the power of the Internet and a degree of artificial intelligence to understand clients by their inputs.”

Big Data can create predictive models based on a client’s inputs. Every question they answer will prompt more algorithms. And their responses will be cross-referenced against everything on the web about them, from Facebook and LinkedIn accounts to email content… and perhaps even what their refrigerators and restaurant delivery apps reveal about their eating habits at home.

“If we can start to ‘Big-Data collate’ all those touch points, especially as the ‘Internet of Things’ comes into play and collects multiple dimensions of data, then we’ll have a better understanding of a client than a single touchpoint such as a Managing Director has,” the banker concluded. In turn, he added, people will seek out such services, knowing that they will be immediately bespoke.

Yes, privacy really is dead. We mourn this but also recognise the need to adapt and turn technology into a legitimate driver of business.

Cryptocurrencies and the blockchain continue to make headlines, but those we spoke to remain skeptical about how revolutionary they might be to the industry.

“I could imagine blockchain making KYC easier,” said a compliance expert. “But as Matt Levine said, you don’t need the blockchain to make loan settlements take less than a month.”

Where technology will be disruptive with a capital D, he predicted, is robots. “And people know it.” This, he said, undergirds the unease, the uncertainty, and the urgent desire for change among the general populace.

“People underestimate the number of things they do better than robots,” he said. “But robots will keep disrupting what people do. We’ll see more robo-advisors, robo-investment bankers, robo-lawyers, robo-doctors.”

And although over the past 30 years we have seen a growth to capital, he continued, “the average person’s income has become stagnant. But capital assets and things that help you stay at the top of the pile, like education, are becoming more expensive.”

Technology, not policy, is what feeds and will continue to feed “the sense people have that things are not working, this hopelessness and dismay. People are not ignorant. They just understand their own circumstance. Wagner actually wrote a book about this; robots would do everything, and people would sit around creating art. We’re moving towards that, and I don’t think we’re ready, especially as regards wealth allocation.”

Just as those who recognise the intersection of technology and the loss of privacy are capitalising on the possibilities, though, others in the industry are acknowledging this bleak view about robots and are figuring out ways to capitalise on ‘the inevitable.’

For those in the industry looking for new niches, said a CEO of an investment group specialising in FinTech, the field is wide open.
“For example, wealth management studies show there’s only US$60 billion in total assets under management (AUM) by robo-advisors within the US$70 trillion asset management industry\(^1\). The potential for growth is enormous,” he emphasised.

A recent McKinsey & Co. forecast predicted the development of an eventual US$13.5 trillion in AUM in funds managed by robo-advisors\(^2\), just in the US. That number could go even higher if Artificial Intelligence and other technology move robos beyond passive investments, said the CEO. And although startups might struggle, the big boys ‘will just buy them.’

Our results are consistent with these kinds of predictions. In our survey, we asked about the intersection of technology and business.

Some 45% either agreed or strongly agreed that access to portfolio-level data will become the norm [Figure 15].

The kind of digitalisation that allows that scenario will expand to other corners of the industry.

KYC by voice recognition – which at least one prominent global bank already employs – will increase, said a service provider in the United Arab Emirates.

“I’m convinced 30 years from now, nobody will carry a passport anymore. You’ll get a chip like my dog and cat have,” he predicted.

A note of caution, all of this swirling data will allow authorities more access to what their citizens are doing with their money, especially if governments follow Prime Minister Modi’s lead and force a cashless society that further destroys privacy. We asked about authorities accessing real-time data, and most respondents agreed or strongly agreed.

“It’s not a question so much of if as when,” said one respondent. In other words… maybe not by 2020... but it could very well happen.

The implication here is significant for the industry. Business models around tax efficiency will either need stronger technological tools, or must eventually be scrapped.

On the macro level though, the biggest threat to business might be summed up as follows: “what will be the biggest technology danger that’s going to affect the whole world economy?,” said the service provider in Dubai.

“If everything is going to be dependent on data, and your fingerprint is in a database somewhere, and your iris scan is in a database somewhere, then the next biggest step is if you control the data in the database, you’re king of the world.”

“China will control the database,” the expert warns. “the industry must prepare for that.”

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1. Bernstein says the future of Robo-Advice is bright, but there’s a catch (Bloomberg)
2. Citi: Robo-Advisers will never take the place of traditional investment managers (Bloomberg)
The Effects of Uncertainty on Alternative Investment Funds

“We’re definitely saying that if there’s a spectrum for risk, let’s not go to the very aggressive end [until there’s more certainty with Brexit]”

Director of Tax, PE & VC Firm, US

The uncertainty of the political and regulatory environment also is affecting some in the Alternative Investment Funds (AIFs) world, both from the perspective of enabling smooth transactions across Europe and from a tax perspective via BEPS.

Regarding the first point, although AIFs are domiciled and marketed around the globe, Brexit is creating uncertainty in Europe. There is a growing appreciation of the complexity of obtaining access to the EU single market through either the passporting or equivalence regimes.

Most pressing in terms of repercussions is access to the EU; British entities need to be able to raise funds from European investors, negotiate and complete new deals, and service their existing portfolios and invest money back into Europe. A loss of access, either at the point of exit or over the long-term, would substantially impact businesses in the UK and Europe.

Not being able to interact with Europe in an efficient manner would hamper the UK industry in particular; in 2015, for example, some 26% of funds raised by the
UK private equity and venture capital industry came from the rest of the EU.

Some options for Britain’s quandary do exist, although how feasible any of them are is in question.

For example, a faint possibility exists for ‘passporting’: since the 2013 implementation of the EU’s AIFMD, EU fund domiciles have promoted the perceived advantages of establishing fund managers in the EU under AIFMD, which allows a pan-European passport.

Non-EU-member states are allowed passporting rights as well, so long as they are part of the European Economic Area (EEA) (e.g. Iceland, Norway, and Liechtenstein) and incorporate relevant EU legislation into the agreement. The passport is not yet available to other non-EU managers.

In 2016, however, the European Securities and Markets Authority (ESMA) took the first step towards expanding the passport to non-EU, non-EEA ‘third countries.’ ESMA formally confirmed five such nations as meeting the technical regulatory standards to allow them to market funds in the EU using a possible ‘third country passport,’ one which has yet to become available to non-EU AIFMs.

This begs the question as to how effective passporting has been in practice. Has it really had the effect of removing discriminatory national application requirements across the EU? And will future EU regulation become even more onerous without the benefit of the UK’s tempering influence?

Clearly, the AIFMD framework is essential to those asset managers marketing to a significant volume of continental EU investors, but how important is an EU AIFMD passport to a manager looking to raise funds globally?

Those questions aside, it is doubtful as of this writing that the UK will join the EEA. Classic passporting therefore likely will not occur.

“It’s sort of a binary choice between passporting and control of immigration,” said one British lawyer. “They’re not going to get both.”

A second option bandied about in the press would be the achievement of equivalence, wherein countries recognise one another’s standards as roughly the same, thus allowing cross border flows.

In theory, the UK could retain access to the EU without having to jump through EU jurisdictional and regulatory hoops. But EU law allows declarations of equivalence to be revoked with only 30 days’ notice... hardly promoting a stable financial environment.

A third scenario allows access to EU markets (and other markets) via the National Private Placement Regime (NPPR). Many EU countries have regimes that have been thoroughly tested and can be navigated efficiently by well-prepared managers. The UK as a third country could access these.

Even if the third country passport under the AIFMD does indeed become available, and even if Britain qualifies, such a solution would only be a stopgap, say some experts – ESMA has suggested that NPPRs disappear three years after the third country passport is created. Surely a well-functioning European NPPR will help maintain global capital flows and can co-exist alongside passporting?
The Uncertainty Principle

If and until Brexit occurs, the UK will remain beholden to the laws and regulations mandated by the European Union; in other words, for the next two years or so, there is no uncertainty when it comes to compliance.

The current passporting regime under the EU’s Markets in Financial Instruments Directive (MiFID) will be modified but still in place under MiFID II if and when Britain actually leaves the EU. One benefit of the timing, and of the UK’s ongoing compliance, noted a fund manager in a CD, is that the UK “will be equivalent at the point of exit. The question will be how that’s going to be dealt with politically, which isn’t clear at the moment.”

Politics may indeed stymie progress by Britain to achieve equivalence after that point of exit. To wit, a number of CD offshore centres such as Guernsey, the Financial Times wrote in July 2016, “copied almost every comma of a European law on hedge funds in its own rule book” to gain equivalency from ESMA.

“But at the last minute,” said another English lawyer, “ESMA held back… You saw definitive evidence over politicisation of the process... a foretaste of what’s going to come for the UK.”

Others agreed. Added another legal expert, “I’m not optimistic that the UK will develop frictionless trading relationships with Europe or even equivalence, which was not designed to facilitate an exiting member to maintain full access to Europe.”

As a hedge fund manager put it, Britain will likely “have to pay a contribution, not too dissimilar from what they paid before, and follow EU rules or come close to them, without having any say over them. It’s a very unattractive position for the UK.”

This also begs the question, will future EU regulation become even more burdensome without the benefit of the UK’s tempering influence?

Additionally, even if equivalence is achieved, it can be quickly and easily revoked. And if equivalence is not achieved, it is unclear whether an AIFMD Third Country Passport would be introduced or granted at all in this political environment.

### Parsing Politics

AIFs also are dealing with a different aspect of political and regulatory uncertainty. In 2015, the OECD published 15 recommended Action Points to protect the tax base, offer certainty and predictability to taxpayers, eliminate double non-taxation, and provide comprehensive consensus-based rules to address BEPS.

It also includes terms to ‘clarify that tax treaties are not intended to create opportunities for non-taxation or reduced taxation through tax evasion or avoidance.’ (Note again the equivalence in the OECD’s eyes between tax avoidance and tax evasion.)

Dialogue around Action Point 6 recently reaffirmed that collective investment vehicles (CIVs) should be entitled to tax treaty benefits; however, these new treaty provisions do not currently extend to non-CIV funds (i.e. AIFs).

The issue – how to provide appropriate treaty access for the broad range of non-CIVs, including AIFs, without giving rise to treaty abuse.

The alternative funds industry will argue that the use of holding companies by private equity funds does not, in fact, represent treaty abuse. In fact, currently under

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3. Preventing the granting of treaty benefits in appropriate circumstances, Action 6 – 2015 final report (OECD)
Action Point 6, the potential for double taxation exists for all investors, and especially for pension funds and pension beneficiaries.

“Pension funds should not be subject to layers and layers of tax,” said one private equity expert we interviewed. Many we spoke to pointed out that because pension funds represent the largest grouping of investors into AIFs, pensioners in the UK and US would likely bear the brunt of this possible double taxation. They also expressed concern about possible restrictions on the international flow of capital, as well as the investment into private equity funds.

We also interviewed a leading architect of BEPS, who stated that measures already have been taken to mitigate any negative impact. The discussion, he said, “merely highlights a problem that has always been around… and may be an incentive for countries to solve it.”

The idea that “pensioners will have to pay twice is not the case,” he reiterated.

Others disagreed. “Action Point 6 is firing a big cannon at a little problem,” argued one fund manager in the Netherlands.

Most fund managers we spoke to are worried that the media and thus the general public hold a skewed view of the funds industry’s contribution to the real economy.

“Even my mother criticised me when I worked for a private equity fund,” said one Dutch respondent. “I had to explain to her that my father’s pension derived in part from those profits. And that the big profits often come from acquiring assets nobody else dares to touch.”

“But it’s difficult to relay the complexity of the system. People don’t understand funds. Yes, people get richer, but it’s mostly about creating value, which is something people generally don’t see.”

Misconceptions also include the tax status of funds. Again, the use of holding companies by private equity funds is not ‘treaty abuse’, insist our experts. “Tax is always paid at some part of the process,” said one.

“The idea that these funds could actually bring benefits to a regular person is just beyond the pale for most politicians; it doesn’t play well politically,” added a legal expert in Cayman Islands. “I think even if it’s not misunderstood, it’s certainly mis-reported.”

Added a private equity investor in New York, “Although investments in debt aren’t returning what they should be, private equity still generates returns that make up for the depressed returns of a lot of other pieces of the portfolio.”
Predictions Going into 2020

“The worrisome trend is people are becoming scared and protective. You would do business with a company in Europe. You don’t trust them anymore and they don’t trust us anymore. The changes in the world that are going on, on a geopolitical basis, they’re tremendous, and under-estimated.”

_Wealth Manager, London_

As we delineated at the beginning of this report, a host of factors are driving the uncertainty that pervades markets the world over. Here we tease them out and predict where they may be going as we approach 2020.

**Anti-globalisation, Protectionist Attitudes will Intensify in the West**

Connected to the idea of uncertainty around the globe is the vigorous debate over the merits of globalisation and free trade. Again, although arguments for and against globalisation are not new, the animosity is becoming more intense, and the stakes much higher.
“It’s clear that there is a battle of ideas going on at the moment that has never really gone away,” said one British lawyer.

The anti-globalisation and anti-free-trade rhetoric is said to have helped usher in both Brexit and the Trump administration. But if OECD-type countries were to retreat and put up barriers, i.e., be less willing to invest in cross-border transactions, then that could have a profound impact on the entire industry.

In the funds world, said one such manager in Singapore, the strategy is caution; “let’s say there’s a fund that’s raised in the middle of next year. If they manage their investment period correctly, they might still be investing by the time a potentially different administration comes in. Because they have a long investment period, the need to be so event-driven in the way they behave is attenuated.”

In the East, attitudes are changing as a beneficiary of globalisation becomes an originator.

“China is just beginning its journey to globalisation. Most of its entities once operated locally. Now they are looking at outbound investment [and expansion] overseas,” said a tax specialist in the region. This is especially true in terms of foreign direct investment (FDI) into European tech and finance companies.

“The best-run Chinese companies are the most ambitious ones,” added a private equity fund executive with extensive experience in the region. “Understand that there’s a market for corporate control in the West. They do not see there’s any reason why they shouldn’t be able to participate.”

Part of the tech FDI strategy is to “own everything... but also learn and master everything,” said a service provider in Dubai with extensive international investment banking experience.

The level of anger about globalisation in the West is not as widespread in China, added a Hong-Kong-based investor.

“Of course, there’s an underlying millennial population that’s a little bit disenfranchised, but it’s not a mainstream movement in the same way that you’ve seen in Europe and in the US.”

Globalisation from China into the West, predicted a Beijing-based expert, “is one of the big trends that’s going to dominate the economic view of the world over the next few decades.”

The OECD and Others will Push for Tighter Regulations and Complete Transparency, including Universal Public Registries of Beneficial Ownership

The battle of ideas about globalisation is but one part of the larger battle over capitalism, and specifically, over how much sovereignty individuals and companies have over their income.

In 2016, for example, socialist-leaning Senator Bernie Sanders narrowly missed becoming the Democratic Party’s candidate for President of the US. This scenario would have been unthinkable even a decade ago. But in an age of entitlement and of economic volatility, and with dominant media outlets the world over leaning left, a state-centric viewpoint has become more and more normative.

Deep grooves continue to divide, if we may be simplistic, those who value markets, capitalism, and sovereignty from those who want others to subsidise enormous state welfare programs. Whereas the left tends to value economic equality, the right tends to value economic liberty. Call the difference in terms equality vs. equal opportunity. One simply cannot have absolute equality and absolute liberty in the same moment.

This is an overly simplistic view at face value, but much of the rage, riots, and ‘resistance,’ for example, by the Left in the US and elsewhere speak to a deep-seated sense of injustice over economic inequality.
This rage is emblematic of a deep global divide, say our experts, which will further empower supranational organisations to agitate, in myriad ways, for individuals and companies to ‘pay their fair share.’

Although regulations and the push towards transparency have already eroded the industry’s self-determinative powers, “never say never about what a third party institution might or could do,” warned a FinTech executive in Jersey.

The rage may be confined to the West at the moment. And it is largely Western institutions, NGOs, and other players who have argued for increasing levels of transparency in the industry. But one could successfully argue that it is emerging markets who have felt the brunt of this push.

“Delaware is alleged to be the biggest tax haven in the world, but it is off limits for criticism,” as mentioned earlier by a fund manager. Its relative lack of transparency is part of its appeal for non-US investors.

Smaller, less wealthy, less protected jurisdictions which largely depend on the industry and therefore must comply with expensive, onerous regulations and threats of blacklisting, can end up suffering in comparison. This is especially true in emerging markets, where governments such as China, Indonesia, and Malaysia’s are increasingly keen on knowing the financial goings on of their citizens.

Emerging markets will likely become the new targets of NGOs and others. A recent report by Transparency International, wrote one publication, ‘reveals that emerging market multinationals are far from responsible global citizens.’

Most worrisome is the idea that as technology feeds and supports this desire for transparency, wealthy people in non-democracies will suffer as their privacy erodes.

Brexit – Beyond Funds

Brexit was perhaps the first in a line of dominoes inspired by – and then further instigating – uncertainty about the status quo.

We have talked about how the funds industry might be affected by a possible exit, but what of the rest of the industry? Here are a few mid-term scenarios our respondents envisaged.

Although parts of Europe might indeed benefit from possible changes to Britain’s relationship with the EU, entire industries such as banking and insurance likely will not descend upon Frankfurt, the Netherlands, Luxembourg, etc. in full force. Those cities lack the capacity to absorb the sheer number of people and businesses involved, “and might not want them,” said one Irish service provider.

“The Irish regulator may not be as open-armed as one might have thought to some of these big banks and big balance sheets flooding in,” he said.

It is also possible – though not probable – that the UK will look more kindly on the OTs and CDs.

“When the UK was more aligned with the EU,” said one legal practitioner in London, “they demonstrated credentials in that arena by flogging the offshore centres in public… a self-harming proposition. But, that was partly rooted in their alignment with EU and Cameron’s need to show that he was not part of that crowd.”

“Of course, we’ve had a big, huge change in that over the last year. I think the UK is much more conscious of what they need to do to make their way in the world outside Europe. The CDs and OT facilitate that.”

Regardless of how the UK interacts with the CDs, said a practitioner in the Channel Islands, “We’re all gearing up as if we are Brexiting. We can tailor our laws and regulations, and innovate very easily. We are able to be the port in a storm to give the certainty that the UK doesn’t have at the moment.”

4. New study calls transparency, anti-corruption efforts in emerging markets ‘Pathetic’ (Sustainable Brands)
Still, how much will the UK need to play by the rules of the bloc? That, onlookers say, “depends on whether they’re going to have a harmonious exit from the EU. If they think they can preserve harmony, they will cooperate on the EU agenda. If the climate deteriorates, then being a spoiler in the EU tax cartel would be very attractive positioning for them. My personal view is that divorces are never easy, particularly where large sums of money are at stake.”

Lastly, how will Brexit affect non-dom status in the UK? Likely not at all, said a number of London-based experts who cover the subject.

“I’m an expat myself,” said one Dutch fund manager in the UK, “and I’m not worried at all. The last thing they want is for wealth to leave the UK.”

**IFCs will Become More Vocal**

In previous reports, we noted the need for the industry to become more proactive about presenting an alternate view of offshore, one that better defended against hostile attacks and promoted offshore’s contributions to the global economy.

Every year or two, it seems, some ‘leak’ emerges and shines a harsh spotlight on parts of the industry with which most of us do not engage. In 2013, it was the Portcullis Trustnet data leak. Then it was the Lux Leaks, followed last year by the Panama Papers.

Repeat an aphorism often enough and it becomes part of the public lexicon. ‘Offshore is bad,’ for example, which gives government leaders more support to enact draconian regulations.

That’s why we predict that a polite defence no longer will be effective enough. Not anymore. More leaks and hit pieces will come along, and we must be ready.

Explaining the merits of IFCs – as we did last year in detail – falls on deaf ears when the audience is adamantly anti-wealth. And in an age where a committed socialist nearly became nominee for President of the US, such an audience is growing.

“Rich people and their contribution to our economy is not valued,” agreed a prominent private wealth advisor in London. “You know that you’re a target.”

“We’ve tried to deliver the message [about the merits of IFCs] to Washington, to London, to Brussels,” said a fund manager in Cayman Islands. “And it’s not enough. And now people don’t want to rock the boat.”

They don’t want to rock the boat because of the “whiff of bullying” by the bigger players, said the London advisor.

He is adamant that “we need spokesmen to be out there and say, ‘Hold on a minute. This stinks of hypocrisy. Our standards are way better than those larger countries doing the complaining.’”

**Consolidation will Continue**

Consolidation will certainly continue on the service provider level, but in rare cases perhaps on the jurisdictional level as well.

Historically, smaller jurisdictions have not embraced working together. But upward compliance has helped the Channel Islands, according to those we spoke to there. As of this writing, they were exploring an agreement between the Channel Islands Securities Exchange and the Bermuda Stock Exchange to explore synergies and economies of scale.

Still, just as has already happened with smaller service provider businesses, the increased burden of regulation and compliance costs could cut entire jurisdictions out of the system altogether. Nauru is but one previous example.
The industry today is unrecognisable from what it was even a decade ago. Whether we are discussing connectivity or the regulatory space, 2017 is a very different world from 2007.

Despite the uncertainty and changes, however, we believe the industry will thrive.

Regulations, for example, eventually will become ‘old hat, just as FATCA already has done,’ once kinks are worked out.

Privacy is fast eroding, and we are loathe to relent on the fight to protect its legitimacy. Still, as technological advances force the issue of digital transparency, we will see innovative, transformative solutions not dependent on confidentiality.

Additionally, the more transparency is demanded by governments, the more their arguments against the legitimacy of the industry will diminish. The data will prove that what we do occurs legitimately, for useful and often publicly beneficial purposes (such as increasing pension yields). At some point, opponents will have to recognise the rightful place of an industry that facilitates essential capital flows across borders.

Until that enlightenment occurs, however, we need to be adamant in our defence, and perhaps even our offence. We must call out hit pieces for what they are – personal anti-wealth crusades masquerading as ‘objective journalism.’ If financial and investigative journalists truly want to promote what’s good for society, they’ll defend the principles of free markets undergirded by sound globalisation. They will recognise the contributions of the industry.

Our industry bolsters the global economy; it facilitates exchanges, prevents extra layers of taxation, presents neutral venues, and protects investors with robust legal systems. We must be more proactive about delineating these points to those who don’t wish to listen. And that means becoming more aggressive and voluble.

Given the uncertainty of global geopolitics, technology, and regulations, it won’t necessarily be easy for the industry to flourish.

Technology, especially in FinTech, is still nascent. Although this encourages those with vision and initiative to help shape the next steps, it’s accompanied by inevitable regulatory, financial, and logistical stumbling blocks.

Social unrest and deeply held, contrasting views about free markets, trade, and cross-border flows will continue to shape both policy and attitudes about the free movement of money over the next few years. Governments struggling with debt will likely continue to enact ham-fisted currency controls and levy ever more complicated regulatory requirements at our industry.

And then there is the social zeitgeist.

So, yes, obstacles present themselves. But they have done so before. And the reason the industry looks so different from what it did even a decade ago is that we have always found ways to adapt… and even thrive.

The future, we maintain, looks bright. It is certainly full of possibilities for innovation. In the meantime, Vistra will continue to track industry trends. We welcome new discussions on where we all could – and should – be headed, and we welcome your comments.
# Glossary & Definition

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Definition</th>
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<tbody>
<tr>
<td>AIF</td>
<td>Alternative Investment Fund</td>
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<td>AIFMD</td>
<td>Alternative Investment Fund Managers Directive</td>
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<td>AML</td>
<td>Anti-Money Laundering</td>
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<td>AUM</td>
<td>Asset Under Management</td>
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<tr>
<td>BEPS</td>
<td>Base Erosion and Profit Shifting</td>
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<tr>
<td>BO</td>
<td>Beneficial Ownership</td>
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<td>BVI</td>
<td>British Virgin Islands</td>
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<td>CIV</td>
<td>Collective Investment Vehicle</td>
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<td>CDs</td>
<td>Crown Dependencies</td>
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<td>CRS</td>
<td>Common Reporting Standard</td>
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<td>EEA</td>
<td>European Economic Area</td>
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<td>EDPS</td>
<td>European Data Protection Supervisor</td>
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<td>ESMA</td>
<td>European Securities and Markets Authority</td>
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<td>EU</td>
<td>European Union</td>
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<td>FATCA</td>
<td>Foreign Account Tax Compliance Act</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>IFC</td>
<td>International Financial Centre</td>
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<td>KYC</td>
<td>Know Your Client</td>
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<tr>
<td>MiFID</td>
<td>Markets in Financial Instruments Directive</td>
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<tr>
<td>NGO</td>
<td>Non-Governmental Organisation</td>
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<tr>
<td>NI</td>
<td>New Incorporation</td>
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<td>NPPR</td>
<td>National Private Placement Regime</td>
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<tr>
<td>OECD</td>
<td>The Organisation for Economic Co-operation and Development</td>
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<td>OTs</td>
<td>Overseas Territories</td>
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<td>PR</td>
<td>Public Relations</td>
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<tr>
<td>TIEA</td>
<td>Tax Information Exchange Agreement</td>
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<td>UHNWI</td>
<td>Ultra High Net Worth Individual</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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