

CHAPTER IV: PANAMANIAN TRUSTS

1. Definition and Concept

The concept of TRUST in Panama revolves around the conveyance of property to fulfill an object previously set forth by the founder of the trust.

In Latin America, a commonly accepted definition of a trust is: A juridical business whereby one or more goods are transferred to one person in order for that person to administrate it or to transfer it and with the proceedings of such activity fulfill an object established by the settlor for his own benefit or the benefit of a third party.

Our Trust Law defines it as “A juridical act by virtue of which a person identified as the settlor transfers goods to another person, identified as the trustee, to administer or dispose of the said goods in favor of the settlor or a beneficiary that may be the same as the settlor”.

We define the Trust as “a juridical act that entails the specific and written declaration of the will of a person identified as the settlor, whereby he/she conveys the title of a good to another individual identified as the trustee, and, as a result, the latter is obliged to administrate or dispose of the said good as agreed in and according to the terms of the commission, in the interest or the benefit of the transferor or of a third party identified as the beneficiary”.

The trust contract involves the assignment of rights and a trust covenant, where the trustee receives a commission to fulfill certain object set forth in the contract. As a result of this set of contracts, the trust is considered a hybrid contract instead of a typical contract.

The fundamental problem to resolve with the trust is conciliation of the trustee rights and those of the settlor and of the beneficiary, considering that it is impossible, from a conceptual point of view, to organize a double title, as in the English Law. Aiming that end, clauses have been created in the trust deed with limitations for the trustee, stating that even if he is the owner with respect to third parties, he has not disposition powers, except for those granted under the constitutive act or by provision of the law.

2. Objects

In general, the main object of a trust is that the involved property, which title has been transferred, becomes an independent estate, administered or disposed of by the trustee, in accordance with the instructions of the settlor.

Our legislation makes possible that, regardless of kind or nature, all goods, present or future, may constitute a trust: cash, franchises, assets with or without right to vote, bonds, chattels or possession right thereof, patents rights, trademarks, trade or firm names, real estates or possession rights thereof, insurance policies, promissory notes, bills of exchange, warehouse warrants, among others. Furthermore, addition of goods after setting up the trust is allowed, subject to trustee’s approval.

The notion that goods of a trust constitute an autonomous estate, separated from the assets owned by the trustee, implies that such estate is excluded from general guaranty with respect to creditors of the trustee, for the trust estate is registered separately in the accounting books in order to avoid confusion with other goods owned or administrated by the trustee. This results in tax advantages and actual protection of assets in the event of seizures or injunctions by third parties. The trustee seeking for a personal credit cannot place the good or goods he holds in trust as collaterals.

Trust estate is also excluded vis-à-vis the creditors of the beneficiaries in view that the beneficiaries are not the owners of the goods in trust and are limited to the expectation of transfer of said goods, or of part of them, and/or to receive from time to time the yield thereof; consequently, creditors of the beneficiaries have no right over the goods, exception made of the seizure or injunction of yield thereof actually received by the beneficiaries.

Only exceptions to this principle of separation occurs when seizures or injunctions originate obligations concerning damages resulting from the implementation of the trust, or by third parties in case of fraudulent retention or conveyance of goods and damaging effects on their rights.

3. Essentials of a Trust Deed

- Complete and clear designation of the settlor, the trustee and the beneficiaries.
- Designation of the substitute trustees and/or beneficiaries, if any.
- Description of the goods or the estate of the trust.
- Statement of the will to set up a trust.
- Powers and obligations of the trustee.
- Prohibitions and limitations imposed on the trustee for the discharge of the office.
- Rules governing accrue, distribution or disposition of the goods, rent and yield of the estate.
- Place and date of the setting up of the trust.
- Designation of the resident agent in Panama (a Panamanian attorney-at-law or a law firm that shall endorse the trust deed).
- Domicile of the trust in the Republic of Panama.
- Declaration stating that the trust is set up in accordance with the laws of the Republic of Panama.

Additionally, the trust deed may include all the clauses deemed convenient by the settlor or the trustee, provided that such clauses correspond with morals, the laws and the public order.

4. Practical Ends and Applications of a Trust

- Managing, conservation or administration of the estate.
- Investment of the estate.
- Protection of the beneficiaries.
- Benefit from an advantageous tax regime.
- To keep confidentiality or the secret with respect to the ownership of the estate.
- To reduce to a minimum the expropriation risk.
- To guarantee obligations.

5. Management and Administration

The settlor may transfer to a trustee all kinds of goods, from an apartments building to a sum of money deposited in a banking institution, to be administrated by said trustee in the established manner, conducting all the necessary acts to achieve the object set forth:

payment of taxes, indemnities, collection of rents, among other related acts, for the term agreed or until some specific event and, afterwards, all the goods of the estate shall be delivered to the beneficiaries.

6. Investment

This refers to the managing of the goods through investments which yield goes to the beneficiaries. In general, investment trusts require trustees with specialized professional skills, for their duty is to increase the value of the estate and obtain the best possible yields to which purpose the settlor grants to the trustee discretionary powers.

Usually this kind of trust entails portfolio managing, implying that trustee's duty include selling and buying in a specific securities market, seeking to increase the value of the assets without stop producing a certain rent.

7. Beneficiaries Protection

Panamanian legislation on trusts does not include provisions limiting their duration and, consequently, trusts shall continue in force for the time specified by the settlor, including –for example- the possibility that trustees continue with the administration of the trust estate in favor of the beneficiaries even after the death of the settlor.

This continuity guarantees a better protection of the interest of the beneficiaries, especially in the case of testamentary trusts, where transfer of goods occurs through a document with “testament” effect that enters in force on the date of the settlor's death. Its duration covers the space of time established in the trust deed.

Testamentary Trust are designed to protect the children and the wife of the settlor, with an effort to keep a way of life, taking care of factors as: education, necessities, healthcare, among other related matters. However, a trust may also be set up to be effective among the living and, at the same time, to stipulate or include instructions as to what shall the trustee do in case of death of the settlor.

These trusts may be set up along with a life insurance policy subscribed by the settlor.

8. Tax Advantages

Our legislation on trusts establishes that the acts of constitution, modification or liquidation of a trust, as well as the acts of transfer, conveyance or encumbrance of the estate of a trust and the rent thereof, or any other act concerning them, are exempted from taxes, contributions, rates or charges in the Republic of Panama, as long as the following requirement are met:

- The trust goods are located abroad.
- The moneys deposited as trust are not the product of rents derived from Panamanian sources or taxable under Panamanian laws.
- The shares or securities of any kind issued by corporations which rents are not derived from Panamanian sources, even if said moneys, shares or securities have been deposited in the Republic of Panama.

Exemptions hereinbefore do not apply when the goods, moneys, shares or security mentioned in 1, 2 and 3 are used in transactions that are not exempted from taxes, contributions, rates or charges in the Republic of Panama.

Furthermore, considering that the goods of the trust constitute an independent estate, or are separated from the personal estate of the trustee (it is always advisable to set forth this in the trust deed), the latter is not liable for taxes, rates or other charges caused by

the said goods, but the said taxes, rates and other charges correspond to the trust and are normally paid separately by the trustee.

Consequently, it is possible that through the transfer to a trustee of certain income producing assets, even if the trustee acts under the same jurisdiction as the settlor, a reduction in the applicable income tax qualification of the assets given in trust may be achieved, a situation that may be favorable for the settlor, for the beneficiaries or for both.

9. Confidentiality and Secrecy Policy

Our Trust Law has provisions that engage the trustee to keep confidentiality with respect to trust operations of the clients.

In the other hand, trusts set up under the laws of the Republic of Panama, with the exception of trusts concerning real estate located in Panama, are not subject to recording in the Public Registry of Property and, therefore, the identity of the settlor and the identity of the beneficiaries may remain a confidential matter since disclosure is not mandatory.

Furthermore, corporations may act as settlors, or be beneficiaries, and, if desirable, identity of settlor or identity of beneficiary are better protected.

Trust may be set up to hold shares of a corporation (bearer shares or registered shares) in which case, the owner shall legally relinquish title of the stock (under revocable or irrevocable conditions), without relinquishing control over the assets of the corporation, whether acting as authorized signer in bank accounts of the corporation, or by means of a legal power to act on behalf of the corporation, while limiting the powers of the trustee to that of a simple stockholder; a trust so set up may also include testamentary provisions and, therefore, offer to the settlor the additional advantage of neat and prearranged disposition of concerned assets in the event of death, while avoiding the designation of another authorized signer for the purposes of the bank accounts of the corporation.

In the case of an Assets Trust, the settlor may be the same owner or stockholder or a holding company owner of the stock of the other corporation. The beneficiary may be the same holding company or the stockholder of a different corporation.

10. Exceptionally flexible procedures to shift jurisdictional subordination

Under Panamanian legislation, trusts, and its estates, may be transferred or submitted to the law or jurisdiction of other State, as agreed in the corresponding trust deed.

This provision looks forward to assure to the settlor, the trustee and the beneficiaries of a Panamanian trust that said trust and its assets (in case they were not abroad yet) may be changed to another country, out of necessity or convenience, in which case the seat shall lose jurisdictional powers to execute any act against such trust or its assets.

Concerning the very transfer act, considering that the Panamanian trust is a private instrument, with no need for recording in the Public Registry, its transfer to another jurisdiction is normally a simpler and clearer proceeding than the corporation related proceeding.

11. Warranty with respect to Obligations

Today, banking and financial institutions resort more frequently to trusts as an instrument to guarantee their clients' obligations. Primarily, this is aimed to separate the assets that guarantee an obligation from the ownership of the person who is using it

and/or is assuming the obligation so, in case of non compliance; it will be easier for the institution to reclaim the good with no concern with respect to other creditors of the debtor.

This instrument is preferred over the establishment of a collateral or a mortgage over the good object of the financing or the debt, to guarantee obligations because is more rapid and economic, avoiding expensive, and usually slow, judicial action for the auction of the collateral or the hypothecated good, for in this kind of trust specific instructions are provided in case of failure to redeem the obligation for the trustee to sell directly the concerned goods to recuperate the credit. The good object of the trust is excluded from the sphere of action of the other creditors and of the creditors of the trustee, as it is a separate estate.

12. Causes for Liquidation of a Trust

- Achievement of the objects.
- Impossibility of achieving objects.
- Resignation or death of the beneficiary, when there is no substitute.
- Total loss or liquidation of the estate of the trust.
- Confusion into one person with respect to the quality of sole beneficiary and of sole trustee.
- Any other cause set forth in the Trust Deed or the Law.

13. Constitution Expenses

In order to promote the international trusts under the Panamanian legislation, our regulations exempt from taxes all the trusts organized with assets located abroad, provided that the trust does not produce rents from a Panamanian source.

Contrary to Panamanian corporations and private interest Foundations, trusts that resort to Panamanian laws are not subject to the payment of annual rates to the Panamanian government.

Concerning fees for the constitution of a trust, they vary according to the kind of trust and the particular needs of the client. Resident agent's fees include an annual charge, usually moderated, to be received by a Panamanian attorney-at-law or a Panamanian law firm.

Trustee charges will depend, among other things, on the prestige, experience and skills of the trustee, on the amount of time dedicated to discharge the office, and on the responsibility, importance and the kind of services to be performed.