

# The use of offshore SPVs in Shariah compliant transactions post-FATCA

In recent years and in the wake of the global financial crisis, international financial centers (IFCs) such as the British Virgin Islands (BVI) and the Cayman Islands (Cayman) have faced unprecedented political and regulatory pressure from governments and international organizations to open up and become more transparent in their business practices. LOUISE GROOM, JOANNA HOSSACK and IAN MONTGOMERY discuss the implications for their position as domiciles for Shariah compliant SPVs.



## OFFSHORE CENTERS

By Louise Groom, Joanna Hossack & Ian Montgomery

The impression given by certain governments and exacerbated by the media is that these jurisdictions are secret tax havens where trillions of dollars earned from illegal activities are stashed away. IFCs fit the bill as a useful scapegoat for issues that have often arisen as a result of wider inadequacies in the financial markets. It is time to dispel the myth that IFCs exist in order to shelter assets from onshore taxation, and to explain why they are vital for international structures.

### The impact of FATCA

Since the implementation of the Foreign Account Tax Compliance Act (FATCA) in the US and similar legislation in other jurisdictions, many people are confused and wary of falling foul of the new reporting requirements. We contend that investor concerns are unfounded and that IFCs serve many purposes beyond simply providing tax neutrality in cross-border transactions.

### Developed business law

In many developing countries, business law is still in its infancy and courts are inexperienced in dealing with complicated corporate matters. There are often significant opportunities for investing in the infrastructure of such countries, for example in the past few months we have seen a clear appetite for Islamic finance emerging across various African nations.

In the construction of a large infrastructure project, the project company will often be incorporated in an IFC. This is because an IFC offers

the benefit of a developed legal system. Access to a neutral jurisdiction that has certainty of legal interpretation, an up-to-date statutory and regulatory framework and sophisticated courts provides comfort for businesses seeking to invest in developing countries, in spite of any perceived shortcomings in the local legal system.

**“ IFCs have shown themselves to be adaptable and open to new innovations, especially in the Shariah space, often amending their legislation in response to a specific need ”**

In many jurisdictions (including, but not limited to, certain jurisdictions in the Middle East), local companies are subject to restrictions, such as who can own shares, the number and classes of shares that can be issued and the type of activities that can be carried out. As a result, offshore entities are often vital for cross-border transactions involving these jurisdictions and are often used as holding vehicles/joint venture vehicles, particularly where there are international investors.

### Flexible legal framework

IFCs have shown themselves to be adaptable and open to new innovations,



especially in the Shariah space, often amending their legislation in response to a specific need. Cayman is known to be the pre-eminent jurisdiction for incorporating Sukuk issuers and funds; other territories are positioning themselves in the Takaful market and in the future we may even see IFCs used in the collection and distribution of Zakat. In addition, recent amendments to companies' legislation in Cayman now make it permissible for a Cayman Islands company to have two names, one in English and one in Arabic if desired.

IFCs will continue to offer more groundbreaking legal entities and regulatory environments to attract business, as adaptability and flexibility are two of their key features.

### Privacy

IFCs are used by companies, investment fund managers and individuals to structure their affairs privately for legitimate reasons, such as security, protection of investment strategy, trade and business and to avoid press and other outside attention. BVI and Cayman already maintain client information on ultimate beneficial owners to the highest of international standards (but keep this information confidential) and the overriding feeling is that they have found an appropriate balance between a client's right to privacy and the regulatory needs of onshore governments.

*continued...*

Continued

## Transparency

Cayman and BVI have always been popular jurisdictions for Islamic finance, the fundamental principles of which are openness, transparency, the promotion of fairness and the treatment of money merely as a means of transfer rather than an asset to be accumulated. It is therefore not surprising that Cayman and BVI, along with other leading IFCs, have been shown to be more compliant in terms of transparency and sharing of information than many onshore jurisdictions. The foremost IFCs are more compliant than almost all OECD countries in respect of meeting the requirements of the Financial Action Task Force, the multilateral body that sets international standards for anti-money laundering.

## Tax neutrality

Of course big business is often motivated by the desire to pay minimal tax; it would be naïve to suggest otherwise. We only need to look as far as Delaware (a state famous for its business-friendly corporation tax regime) to see that companies will choose to be incorporated in the least expensive available jurisdiction.

“ IFCs will remain vital components of international structures, even in the face of mounting pressure from onshore governments ”

But it is important to acknowledge the difference between legitimate tax planning and illegal activities such as avoiding tax and hiding profits. So long as there are different tax rates in different countries, IFCs will serve as neutral conduits for the flow of money. Indeed, international trade is facilitated by tax-neutral entities which serve to aggregate assets and capital. This capital is usually injected back into the very

onshore jurisdictions that have declared their intention to clamp down on the use of IFCs.

## Conclusion

IFCs are more compliant with international regulatory requirements than they are portrayed to be. The benefits of using an entity incorporated in an IFC (including ease and speed of incorporation, general corporate flexibility, ability of decisions to be made at board level, ease of appointing and removing directors and the possibility of keeping assets out of the reach of local laws for succession planning purposes) are such that they will remain vital components of international structures, even in the face of mounting pressure from onshore governments. ☺

*Louise Groom is a partner and Joanna Hossack is an associate at Harneys based in Cayman while Ian Montgomery is an associate in BVI. They can be contacted at [louise.groom@harneys.com](mailto:louise.groom@harneys.com), [joanna.hossack@harneys.com](mailto:joanna.hossack@harneys.com) and [ian.montgomery@harneys.com](mailto:ian.montgomery@harneys.com) respectively.*

## BELGIAN ECONOMIC MISSION IN MALAYSIA SEMINAR

### Shariah compliant investments in Belgium: scope & opportunities

Belgium is a strategic location in the center of Europe, bordering the Netherlands, Germany, Luxembourg, and France and is at the heart of 3 main European cultures: Germanic, Latin and Anglo-Saxon. Brussels is the capital of the European Union and its 27 markets! The Belgian government wishes to strengthen the relationship between Belgian and Malaysian companies in all sectors.

Within the framework of the Cooperation Agreement between the Federal Government and the Regions, a Belgian economic mission presided over by HRH Princess Astrid, Representative of His Majesty the King, will be held in Malaysia and Singapore from the 22<sup>nd</sup> to 28<sup>th</sup> November 2014.

During this mission, ISFIN will organize a seminar *Shariah compliant investments in Belgium: scope & opportunities* » in cooperation with the official Belgian authorities, Afschrift law firm (Belgium), Azmi & Associates (Malaysia) and Al Maalya (Belgium).

This seminar will showcase the multiple investment opportunities available in the Belgian market which comply with Shariah requirements.

ISFIN is the world's leading platform for law firms specializing in Islamic Finance, investments from and to the Muslim world and the Halal industry. The alliance covers more than 75 jurisdictions around the world.

ISFIN's membership is composed of the most innovative and highly regarded independent law firms, audit & accounting firms and real estate companies in their field.

To attend, please contact Zineb Bensaid, Senior Consultant for ISFIN at [zb@isfin.net](mailto:zb@isfin.net)