

# DEVELOPMENT OF PRIVATE WEALTH MANAGEMENT IN UKRAINIAN BUSINESS ENVIRONMENT

## Andrei LIAKHOV



*PARTNER WITH SAYENKO KHARENKO. DR. LIAKHOV'S EXTENSIVE EXPERIENCE INCLUDES ADVISING BOTH REGULATORS AND MARKET PARTICIPANTS ON ALL ISSUES RELATING TO SECURITIES REGULATIONS ON THE INTERNATIONAL AND DOMESTIC LEVELS. ANDREI ALSO ADVISES ON WEALTH MANAGEMENT, DEBT RESTRUCTURING, MERGERS AND ACQUISITIONS PROJECTS*

## Alina PLYUSHCH



*COUNSEL WITH SAYENKO KHARENKO. MS. PLYUSHCH REGULARLY ADVISES CLIENTS ON CORPORATE RESTRUCTURING, SHARE AND ASSET SALE, JOINT VENTURES, PRIVATE PLACEMENT AND CAPITAL MARKETS TRANSACTIONS AS WELL AS ON PRIVATE WEALTH MANAGEMENT ISSUES, SETTING UP TRUST STRUCTURES, FOUNDATIONS AND SEGREGATED PORTFOLIO COMPANIES*

Private Ukrainian business is approximately 20 years old, which means that the majority of Ukrainian entrepreneurs are first generation businessmen who were concentrated on creating wealth and paid little attention to issues of structuring and managing wealth and of succession. Having created considerable wealth Ukrainian business is slowly but surely starting to search for effective wealth protection and wealth management mechanisms.

We have recently noticed growing interest on the part of large and mid-sized businesses in private wealth management advice and services. The Ukrainian business environment makes wealth preservation and protection a number one priority. The numerous Ukrainian wealth holding and management structures using Cypriot, BVI and a variety of Caribbean companies with nominee shareholders proved to be ineffective for the long term wealth protection, management and succession tasks, the principal of which are to: (i) establish transparent and effective ownership and management structures for the business; (ii) optimise taxation at the intra-group level while performing intra-group distributions such as payment of dividends, interest and royalties; (iii) protect interests of the beneficial owners; and (iv) protect the business from corporate raids and other external interference.

Our experience demonstrates that holding structures utilising trusts and/or foundations is, probably, the best option to achieve these goals, secure succession and effectively manage created wealth.

## A CONCEPT OF TRUST

Trust is a legal relationship where one person (Settlor) transfers his legal title to assets to another person (Trustee) pursuant to a binding agreement (a trust deed) and the Trustee holds and manages the assets for the benefit of the third parties (not necessarily the Settlor) — beneficiaries of such trust.

The main characteristic of a trust is that the absolute title to assets is divided into legal title (transferred to the Trustee) and beneficial title (retained by the beneficiaries).

Generally there are two types of beneficiaries — beneficiaries of capital (having beneficial interest in the assets transferred into trust) and beneficiaries of income (having beneficial interest in the income generated from trust assets).

The most appropriate form of trust enabling the proper management and protection of the assets of a private business is a discretionary trust (where trustee has unfettered powers to deal with the trust assets). A discretionary trust is backed by a detailed letter of the Settlor's wishes on how to deal with the trust assets. The letter of wishes may be reviewed on a regular basis (e.g. annually). Furthermore, the trust deed of a discretionary trust could nominate a separate person to control the activities of the Trustee (Protector).

The trust deed and the letter of wishes, which are prepared by the Settlor together with the Trustee, concerns the succession process and other wealth management issues such as distribution of the trust assets and income both during lifetime and after the death of the principal beneficiaries.

This enables: (i) regulation of the succession of the trust assets by the beneficiaries (spouse, children, grandchildren, other relatives of the principal beneficiary and other persons); and (ii) establishment of the procedure for transfer of the beneficial interest to the assets to the heirs of the initial beneficiaries.

For this purpose in the letter of wishes principal beneficiaries may provide for any succession procedure of the trust assets and change it at any time at their own discretion.

Trust structures are exempt from inheritance tax since no legal title passes on death of either the Settlor or the principal beneficiary. When this happens the Trustee will continue to hold the legal title to the trust assets while the beneficial title will pass to other beneficiaries listed in the letter of wishes. This enables the Settlor/principal beneficiary to nominate any person (not only the immediate relatives) as the beneficiary and such person will be able to derive economic benefit from the trust assets without incurring inheritance tax liabilities, which could be substantial.

## A CONCEPT OF FOUNDATION

Foundation is an incorporated legal entity of independent non-commercial nature, established to manage the assets received from the Founder or from the third parties and acting for the benefit of the Foundation beneficiaries, the list of which is provided by the Founder.

By its nature, the Foundation combines the characteristics of both a trust and a private company.

There are two main types of Foundations: (i) charitable Foundation; and (ii) private Foundation.

A charitable Foundation is established for the purpose of raising funds for the announced charitable causes.

A private Foundation is established by the Founder (a particular person, a range of persons or a family). The Founder of a private Foundation also designates persons who shall be beneficiaries of the Foundation. The Founder may also be a beneficiary.

The Foundation is incorporated in the form of a separate and independent legal entity. The activity of the Foundation is governed by the laws of the place of incorporation, its Charter and by-laws.

**SAYENKO KHARENKO**

10 Muzeyny Provulok,  
Kiev, 01001, Ukraine  
Tel.: **+380 44 499 6000**  
Fax: **+380 44 499 6250**  
E-mail: **info@sk.ua**  
Web-site: **www.sk.ua**

**S**ayenko Kharenko is Ukraine's leading law firm with an internationally oriented full-service practice and a Ukrainian law representative office in London.

In 2013, Sayenko Kharenko collected the national Law Firm of the Year Award three times, having been recognized Ukraine's best team both by IFLR European Awards 2013, Who's Who Legal Awards 2013, and Yuridicheskaya Practika Legal Awards 2013. The firm remains the unrivaled leader in Ukraine by project volume, and has been named No.1 in terms of the number of the largest projects in Ukraine for nine years in a row, according to Top 50 Law Firms research by Yuridicheskaya Practika Publishing.

The firm specializes in complex cross-border and local transactions and regularly handles the largest and most innovative projects in the areas of:

- Antitrust
- Banking and finance
- Capital markets
- Corporate and M&A
- Debt restructuring
- Government relations
- IP
- Investment projects
- International arbitration
- International trade
- Labor and employment
- Litigation
- Real estate
- Taxation
- White-collar crime

About its Private Wealth Management Group

Sayenko Kharenko advises clients on a variety of private wealth management projects, assisting with tax, regulatory and other issues to prevent loss of private capital. The firm's team develops and implements effective tax optimization, risks mitigation and assets management and protection strategies. Sayenko Kharenko's lawyers help clients with developing wealth management and corporate structures for business; drafting required documentation; supporting corporate restructurings and fund-raising processes following corporate restructurings.

The Foundation is similar to a private company, except for (i) it is a non-commercial legal entity and is not intended to make profit; and (ii) it has no shareholders or participants, but the beneficiaries have an interest in its capital.

Foundation may enter into contracts in its own name (e.g. buy or sell property), open and operate bank accounts and own shares/interest in other legal entities. The non-commercial nature of a Foundation does not prejudice the legal capacity of subsidiary companies owned by the Foundation. Income received from such subsidiary companies is transferred to the Foundation in form of dividends and may be divided among the beneficiaries of the Foundation.

**DIFFERENCE IN MANAGING A FOUNDATION AND A TRUST**

The difference between managing a Foundation and a trust is that the Founder/the principal beneficiary of the Foundation may directly participate in decision-making and amend the Charter and by-laws of the Foundation.

The managing body of the Foundation — the Council may not act in breach of the effective Charter and by-laws of the Foundation e.g. change the nature of the Foundation's activities or principles of investment and has fiduciary duties to the Foundation. On the other hand, the Trustee of a trust is obliged to act only for the benefit of the beneficiaries and is liable to them for such trust's activity, while a Council of the Foundation acts only in accordance with the provisions of the Foundation's Charter and by-laws and bears no liability should the actions of the Council contradict the interests of the beneficiaries.

**CORPORATE RESTRUCTURING**

The Cypriot financial crisis of 2013 and the new double taxation treaty be-

tween Cyprus and Ukraine which entered into force on 1 January 2014 raising the withholding tax rate from zero rate caused Ukrainian business to look for alternative cross-border structures.

Currently, the interests of Ukrainian business are focused on other jurisdictions such as the Netherlands, Estonia and Hungary due to the preferential provisions of the respective double taxation treaties entered into by Ukraine with these countries. Furthermore, the Ukrainian government announced that double tax treaties with Malta and Ireland providing favourable tax rates shall be ratified shortly.

Having the above in mind we think that while Cyprus will remain popular jurisdiction for cross-border structures the interest in structuring through the Netherlands, Estonia, Malta and other EU jurisdictions with favourable tax regimes will continue to grow for the foreseeable future.

**CONCLUSION**

The development of Ukrainian business requires structuring and introduction of corporate governance and private wealth management systems. We notice a growing need to introduce these systems at the owner's level. The age of first generation entrepreneurs is also pushing them to look into re-structuring of their businesses in order to secure their family interests for years to come.

A reliable and effective solution to achieve these goals is creation of a cross-border structure with a trust or foundation at the top. Such structuring provides for transparent and reliable ownership and a control system for the business, helps to protect the interests of the beneficiaries, facilitates optimisation of group taxation levels. Furthermore, the structuring of private wealth through trusts and foundations helps to procure a reliable system of family wealth management and has been proved to preserve wealth for future generations.