Tortillas and Turpentine

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When I arrived in the Cayman Islands in 1979 one of the books I brought with me from London was the fourth edition of *The Modern Law of Trusts* by David Parker and Anthony Mellows. In their preface, the authors said that it was important for readers to be aware that the law of trusts was constantly developing. I can see from reading the current ninth edition that this turned out to be an understatement; the statutes, it seems, cannot keep pace with the case law. The fourth edition had 415 pages whereas the current edition has 979 pages.

This demanding branch of the law has antecedents that, in Britain, go back even before time immemorial, that date determined in the Middle Ages as the limit of legal memory (which was, in fact, 3rd September 1189, when the reign of King Richard in England began). In England the trust's predecessor, the use, began to feature in law in the second half of the 14th century. Even then, one of the objectives of the use was to avoid taxes, much to the chagrin of the Crown; when it was eventually replaced by the trust in the early part of the 17th century, it just made the matter of taxes even more vexatious. Today, trusts are being targeted again, this time not by monarchs but by cash-strapped governments who have found their treasuries empty after the global economic crisis which began in 2007.

Trusts today are big business but not in Latin America where they must vie with foundations which are far more popular. The reverse is true in some offshore common law jurisdictions where the ubiquitous trust now has foundations quietly nibbling away at its prominence in estate planning as jurisdictions introduce foundation laws and trust officers begin to get familiar with the concept.

Trust officers worldwide now have their own society based in the United Kingdom called the Society of Trust and Estate Practitioners (I became one of its members in 1992) which now plays a leading role in training these professionals, some of whom, I'm sure, read this journal. Even if trust officers who are members of STEP in Latin America spend more of their day with foundation charters and regulations rather than trust deeds, the society is certainly contributing to a firm understanding of a fiduciary's responsibilities as well as a deeper appreciation of the virtues of trusts. There are members in Argentina, Belize, Brazil, Colombia, Ecuador, Mexico, Panama and Uruguay; Panama, according to STEP's 2010 directory, has more (50) members than the combined total of the other seven jurisdictions. Uruguay is second with 19 members which, like Panama, is a banking centre (although I believe the largest regional concentration of trust companies can be found in Panama).

Bankers and trustees share common ground and as both a practitioner and a former bank and trust company regulator I have encountered businessmen, regardless of nationality, anxious to acquire either an offshore bank or trust company licence. In many cases, the motives have had more to do with egos than enterprise, as if the licence was a badge of success to be worn with entrepreneurial pride. Trust business and banking can prove to be precarious professions when you stray from the fundamentals and although the capital requirements for an offshore trust company versus a bank are normally far less difficult to meet, it doesn't mean that the responsibilities and risks are less onerous. Remember, too, as I wrote in my February, 2008, column (A Different Kettle of Fish – Issue 183) tortillas and trusts do have something in common: their meaning depends on where you are. Whilst you may be able to redomicile your trust to southern climes, you can't do the same with the personnel who manage it, so I advocate the importance of qualified professionals, whether STEP members or not.

Trusts can be an attractive source of funds for banks with investment arms but how expert is the banker qua trustee? Many Swiss bankers are wary of them, as their Latin American counterparts should be for the same reason: they are interlopers in the civil law system and can prove to be problematic. Even so, regardless of any other considerations, I have always argued that just because the applicant for a trust company licence is a bank, this is not sufficient reason to short-circuit essential elements of the licensing process. The same attention given to a bank's capital by regulators should be paid to the ability of the applicant to provide an adequate level of expertise in fiduciary matters. If the expertise, like a bank's capital, is inadequate, then a licence should not be granted. Walter Bagehot, in his classic 19th century work "Lombard Street: A Description of the Money Market", was spot on: "Common sense teaches that booksellers should not speculate in hops or bankers in turpentine; that railways should not be promoted by maiden ladies, or canals by beneficed clergymen…".

Banking, like trust work, should not be left to amateurs. Is it not, then, the irony of ironies that skilled bankers in onshore financial centres, some of them with large egos, have been instrumental in the present sad state of affairs? When looking at the future, who could have imagined Robert Zoellick, the World Bank president, would apply the 1980s Latin American term La Década Perdida (Lost Decade) as a future scenario for some of today's developed economies, swamped by debts and living beyond their means? In Spain this month bulls will be stampeding in the Pamplona bull run, part of the annual San Fermín festival, but not, I very much doubt, on Wall Street or European financial markets.

Some ten years ago it was all so different: Europe was confident, buoyant and expanding whereas Latin America was in the doldrums. Now the emerging markets (a term coined by Mr Antoine van Agtmael who heads Emerging Markets Management with about USD13 billion of investments) are experiencing never-before growth with their consumers having outspent Americans since 2007; in 2009 their share of global consumption was 35% whereas America's was 27%. Economic growth between 2010 and 2015 for several Latin American countries will be healthy, according to figures released by the International Monetary Fund, with Panama having the highest growth in 2011 (6.3%) and 2015 (6.5%) with this year's leaders being Peru (6.3%) and Brazil (5.5%).

In that same February, 2008, column I argued that the familiar boom-and-bust cycles in Latin America were giving way to long-term investment opportunities. Lessons from the 1980s have been learned and if Brazil, as I suggested in last month's column (Brazil: The Future Arrives - Issue 207), is more self-assured, so are its banks and those of other countries in and beyond the region whilst many of those in the west lie prostrate. Mr Zoellick thinks that growth in developing economies will average around 6% this year and next, which will probably be twice that of high-income countries, with Latin American countries and those in east and south Asia boosting their growth prospects by investing in infrastructure such as transport, energy, water and urban centres.

What, however, about a bombast bubble? Enrique V. Iglesias, the former president of Inter-American Development Bank, cautions Latin Americans not to become over-confident. Luck has played a large role in their good fortune (such as the commodity boom driven by Asia with near-zero US interest rates flooding the continent with cheap money) bolstered by banks which applied orthodox lending policies and concentrated on their own domestic markets as they licked their wounds from previous downturns and kept away from the sub-prime junk that proved fatal in the west. But fast economic growth has its dangers because a rising middle class will spend more and can the ratio between bank deposits and credit demand be kept within prudent parameters? The continent that is now moving out from the darkness of the past must avoid stumbling in the sunlight.

Reading Parker and Mellows (and similar works) keeps the feet of trust professionals such as myself firmly on the ground and is a reminder that there is always more to learn. Smug trustees and bankers (I recommend Bagehot's Lombard Street to them) on the other hand are dangerous and they should heed the words of Johann Wolfgang von Goethe, Germany's 16th-century natural philosopher: "There is nothing more frightening than ignorance in action".

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