

STEP JOURNAL

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The blind trust

Explaining that a blind trust may be blind, but in Israel it is not a trust.

The issue of blind trusts has recently been placed on the Israeli public agenda by Prime Minister Benjamin Netanyahu when he requested permission of the Authorisations Committee of the Israel Securities Authority to make several changes to the makeup of his investment portfolio. The issue of blind trusts has also been discussed in the US with respect to the many assets held by unsuccessful presidential candidate Mitt Romney outside US borders. US media have suggested that such a blind trust is a deception, as the role of trustee is held by Mitt Romney's personal attorney. The reasoning behind a blind trust, of course, is to prevent situations that may cause a conflict of interest for politicians regarding management of assets in their possession upon assuming elected position.

The blind trust legislation was enacted initially in the US *Ethics in Government Act of 1978*. The Act does not use the term 'blind trust' specifically, yet it creates a legal structure commonly known as a blind trust. According to the Act, among the requirements for a state official to hold assets are: the trustees must be independent of the official, the trust must be free of restrictions on sale or transfer of assets, and the official is to receive no information except for quarterly updates on cash value and income or loss, which is needed for filing income tax returns.

In Israel the blind trust is regulated by the *Notice of Rules to Prevent Conflicts of Interest by Ministers and Deputy Ministers of 2003* (the Notice), enacted following the conclusions of the Usher Committee. Section 16 of the Notice provides:

'(a) Within 60 days of his appointment, the minister shall transfer the funds and securities owned by him and his family members to a public and independent trust company, which shall hold and manage them in a "blind trust".

'(b) The Minister and his family members shall not provide the trust company with any instructions regarding which securities to hold and which securities to sell or purchase, except for a one-time instruction, prior to the commencement of providing the service, regarding the types of portfolio investment, and regarding the maximum amount of each type in relation to the value of the portfolio, or instruction that those shall be determined at the trust company's discretion.

'(c) The trust company shall not provide the minister and his family members with any information regarding deals in the securities as long as the official holds office; the only information to be provided shall be the total value of the securities, the realised gains, and the tax paid as a result of these gains.'

The Notice does not define the meaning of 'blind trust', yet it places the phrase in quotation marks in the section quoted above. An examination of other legislation suggests that the term 'blind trust' is not defined in Israeli law at all, and it can be concluded that the term is not referring to a trust as defined in the *Trust Law of 1979*. This conclusion derives from a closer inspection of the *Trust Law of 1979*, and of the *Agency Law of 1965*.

Section 1(a) of the *Agency Law* provides: 'Agency is the grant of power to an agent to perform - in the principal's name or in his place - a lawful act in respect of a third party,' whereas s2 provides: 'A

person's agent has the same status as the person himself, and an act of the agent, including his knowledge and intent, binds or entitles the principal, as the case may be.' It can thus be inferred that the agency cannot place restrictions on the principal with respect to their assets. Furthermore, according to s14, the agency terminates upon its cancellation by the principal or the agent, or upon the death of any of them. Hence, upon the death of the principal, those assets that are held by the agent can be transferred to their new rightful owner only by a probate order.

The *Agency Law* also enforces a loyalty fiduciary on the agent, as stipulated in s8: 'When a person has taken upon himself to be an agent, he shall act in a fiduciary capacity to the principal and shall act in accordance with his instructions...' In Hebrew, the terms 'fiduciary' and 'trust' are both translated as '*ne'emanut*'. This might explain the use of the word 'trust' in the term 'blind trust'. In fact, in Israel, the 'blind trust' is a temporary agency settlement, valid as long as the official holds office, and terminated upon the official's release from duty. Should the official die while still in office, the *Succession Law* applies to the blind trust's assets, and a court ruling would be necessary to distribute the assets to the deceased official's successors.

The *Trust Law* creates a completely different structure from the agency, as s1 provides: 'A trust is a relationship to any property, by virtue of which the trustee is bound to hold the same or to act in respect thereof in the interest of a beneficiary or for some other purpose.' Section 2 stipulates: 'A trust is created by law, by a contract with a trustee or by an instrument of endowment.' Unlike an agency, once a trust is created, its administration, and occasionally its ownership, is transferred exclusively to the trustee in accordance with the trust purposes. This signifies that the settlor's control over the trust assets is taken from them upon establishing the trust, and, at the time of death, the trust assets are not considered to be among the estate assets - a succession procedure in court is not required for their distribution.

It is clear from the spirit of the rules that the intention is to separate the elected official from assets and from the portfolio manager for the term of office. Once the elected official's term comes to an end, the assets will be returned to their owner, and the 'blind trust' will be terminated. Furthermore, should the official pass away before the end of their term, the 'blind trust's' assets cannot be transferred back to their family without an inheritance procedure, such as a probate order. This outcome is in line with section 14 of the Agency Law, as mentioned above, and it shows that the connection between the official and the assets is not completely severed by the 'blind trust'.

Based on the above it can be inferred that, despite the terminology, which suggests this structure is a form of a trust, it is not in fact a trust, but an agency/fiduciary relationship.

60-second interview with Alon Kaplan

How did you hear about STEP and why did you join?

I met a colleague from Switzerland, Dr Froeip. He was already a STEP member in 1993 and, on his recommendation, I joined STEP in 1994.

What has being a member meant to you over the years since the Society's inception, and does it mean the same today?

It means a lot more. When I joined, there were fewer than 2,000 members, mostly in England and Wales. Today STEP has more than 18,000 members based in 84 countries, and this creates important opportunities to communicate with professionals and experts in the field of trusts and estates.

Branch development is key to STEP's international growth. As STEP Israel's founder, how did you build the branch to what it is now?

The branch was developed by direct communication with banks, trust practitioners, lawyers and accountants. An important element is our traditional annual conference, which has been taking place for the past 14 years. We plan on celebrating the 15th anniversary of the branch in June 2013.

What are the current priorities and focus for the branch?

Keeping up to date with current developments in legislation and court precedents relating to taxation of trusts, anti-money laundering law and tax law. The branch is investing special effort to run educational courses for students of the STEP diploma.

How important is STEP's presence in Israel?

STEP is recognised as an important professional society by the Israel Law Society and the government. Members of STEP have participated in a government committee dealing with the preparation of the law for taxation of trusts, which was finally enacted by the Israeli parliament.

Private client practitioners comprise a broad spectrum. What do you think links practitioners and STEP members around the world?

Private client practice has a nature of international aspects involving laws of more than one jurisdiction. Communication between STEP members worldwide enables us to get and provide important legal and tax information as a service to our clients.

What's the best STEP event you've attended?

I attended the STEP Private Client Awards in London last month. It was an extraordinary opportunity to meet STEP members from around the world at an event where top companies for trust and estate practice receive awards.

The 2012 STEP Israel annual conference was another great event, where we had 290 delegates, of which 70 were from overseas. It was a two-day programme with representation of professionals from Israel, Switzerland, Gibraltar, the UK and the US.

What are the main challenges facing your organisation and practitioners at the moment?

The main challenge is to retain and increase the number of members in the Israel branch and continue the development of the educational programme for the STEP diploma.

How will you deal with these challenges?

Organising quarterly seminars for STEP members, recruiting new members from the law and accounting professions, and requesting existing members to introduce STEP to their colleagues.

What else is keeping you busy at the moment?

Teaching at the LLM course at the Faculty of Law of the Tel Aviv University, writing articles and writing my PhD thesis for Zurich University.

What's been your career highlight?

Serving on the government committee as a STEP representative and the preparation of the law for taxation of trusts in Israel. Recently, my firm became a partner in the international Morgan and Morgan group and their Israeli office in Tel Aviv.

Who has been your greatest mentor and why?

STEP President Geoffrey Shindler, who has devoted energy and time to help me develop the STEP Israel branch and the educational programmes of STEP in Israel.

What's your favourite quote?

In 1994, I wrote a book titled *Israel Law and Business Guide*, and put the following Bible quote on the first page: 'Ye shall have one manner of law, as well from the stranger, as one of your own country: for I am the Lord your God.' (Leviticus XXIV, 22)

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