

Bahrain family business: a solution in trusts

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Unlike in the United Arab Emirates, Bahrain's personal status law is uncodified, and the Sharia courts are responsible for applying the Islamic principles of inheritance on a case by case basis. This means that when a senior member of a family business passes away, family members who disagree on matters of succession, find themselves embroiled in lengthy and costly court proceedings.

According to a recent family business survey , 53 per cent of family businesses believe that succession planning is a key challenge for them over the following two years of growth. Families face a myriad of issues and complications by not having a succession plan in place including: the gradual dilution of the founding fathers' visions for their business from one generation to the next; and a stagnation of business whilst family members dispute inheritance issues. This, in turn, may heavily impact the prosperity of the business. Whilst inheritance laws do provide for certainty to some extent, they may detrimentally affect the smooth transition, and more importantly the long-term continuity of the business.

The transition phase from one generation to the next is complex, particularly when this results in the division of a company's shareholding between siblings or other family members, making it difficult to reach common decisions and hindering the day to day running of the business. One way of circumventing these issues is by having a trust in place. Trusts in Bahrain are regulated under Decree Law No.23 of 2016 on Trusts (the 'Trusts Law').

The Trusts Law defines a trust as a legal relationship created by a settlor, in his lifetime or upon his death, whereby business and/or personal assets are placed under the control of a trustee (or in the name of a third party on behalf of the trustee) either for the benefit of a beneficiary (or group of beneficiaries), or for a specified charitable/non-charitable purpose. A trust instrument must:

1. be in writing (trust deed);
2. identify the settlor and the trustee(s);
3. identify the purpose of the trust or the beneficiary;
4. identify the trust property;
5. specify the duration of the trust, the maximum term being 100 years; and
6. identify duties and powers of trustee.

An essential characteristic of a trust is that it allows for the separation between legal ownership and beneficial interest. A trustee is appointed to manage the trust's property and/or assets on behalf of the beneficiaries (i.e. the specified family members). Further, a trust enables the ring-fencing of family assets, in that they are separated from any other assets that the trustee holds, and are not part of the trustee's estate. The powers that can be given to trustees include managing, employing or disposing the assets in accordance with the terms of the trust.

In fact, the settlor has a substantial amount of flexibility in deciding on the terms and conditions of the trust deed including (without limitation): the extent of the beneficiaries' interests (for example entitlement of income and capital from the business); provisions relating to governance; and restrictions on the sale, transfer or encumbrance of assets, all of which may be tailored in line with the particular needs of each separate family business. Where families are conscious of, and want to uphold the religious aspects of succession, the trust may be structured in accordance with religious principles under Sharia.

Additionally, the settlor may specify certain powers which are to be reserved to himself (such as the power to remove or appoint a trustee or beneficiary). However, this reservation must not jeopardise the independence of the trustee or state that the trustee's powers are conditional upon the settlor's prior approval. Alternatively, the trust instrument could provide for the appointment of a 'protector' instead, whose consent must be obtained by the trustee in specified circumstances. Significantly, the Trusts Law allows foreign participation, whereby the settlor and beneficiaries may be foreign nationals and trust creators have the option to choose the jurisdiction in which the trust will be governed, allowing for further flexibility and freedom of contracting.

Trustees are licensed and regulated by the Central Bank of Bahrain ('CBB') and must notify the settlor, the protector (if any) and the beneficiaries, of any matter that has a tangible effect on the value of the trust property or on investing the trust property. Any one of the settlor, the protector (if any), the beneficiaries or the CBB has the right to question the trustee and the trustee must permit the foregoing to have access to the accounts, documents and records of the trust. This should be of comfort for family businesses that may be hesitant to leave the running of the business to a third party. Furthermore, a register of trusts is maintained by the CBB which records the identity of the settlor, the trustee(s), the beneficiaries and any protector and contains a summary of the terms of the trust instrument. Information is provided on a confidential basis and only the settlor, the trustee(s), the beneficiaries and the protector have access to it.

To conclude, the establishment of a trust instrument as a long-standing holding structure contributes to providing stability and mitigating risks as well as providing a solution to ensure the longevity of local family businesses from one generation to the next, and the protection of their assets.

Al Tamimi & Company's [Corporate Commercial](#) and [Corporate Structuring](#) team regularly advises on [Family Business Structuring and Trusts](#). For further information please contact [Foutoun Hajjar](#) (f.hajjar@tamimi.com) or [Rad El Treki](#) (r.eltreki@tamimi.com) or [Layla Alalawi](#) (l.alalawi@tamimi.com).