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Commentary on Matters Offshore

Open Doors and Insects

During the course of the last few years this newsletter has often commented on confidence tricksters. Trust Services, S.A. has also published full-length articles on the subject (such as “The Silence of the Scams”). These con merchants so often, unfortunately, play a core role in many disastrous offshore financial activities and this quarter’s newsletter is going to focus on the subject once more, including related matters.

Very often, the bizarre is a feature of the trickster’s plot, as in the case of Babadi Cisco, better known in business circles as the Cisco Kid. A cowboy in more ways than one, Cisco is described as a magician and holder of Nigerian, Ghanaian and other West African passports. He performed his “magic” on the Dubai Islamic Bank where he apparently hypnotized several members of senior management who then opened the bank vaults, handing over, in their trance-like state, cash and gold bars worth tens of millions of dollars. Investors may not be exactly mesmerized by the offshore financial services centres, but they are attracted to them because they offer facilities that are often unique and unavailable elsewhere. Confidentiality still plays its part, particular for those Americans who believe that the initials DC after Washington stand for Diluting Confidentiality. Unfortunately, they will not only find bankers but bamboozlers as well waiting to help them. Confidence tricksters follow the money and so offshore centres are a natural magnet. Illusion is employed frequently by them in much the same way as it was by Mobutu Sese Seko who ruled

Zaire for over 30 years and who might have robbed a country rather than individuals, but he had the art of illusion off pat. When he was overthrown in 1996 and journalists gained access to his palace, the chandeliers, Ming vases, antique furniture and marble floors turned out to be either plastic or cheap reproductions of the originals. When the game is up it is so often the same situation with the offshore fraud: on closer examination the supporting structure is just a façade. It brings to mind Deng Xiaoping who said that China’s open door policy might be good for the economy, but it also allows insects into the house.

It is due to the level of frauds which have been perpetrated that a large and increasing number of offshore centres are suffering from, what I term, commercial SARS. In the case of the offshore centres, however, the term has no bearing whatsoever on health risks but stands for Severe Acute Regulatory Syndrome. Regulatory controls have been put in place to thwart the dishonest (as they should be) but which, in practical terms, so often hamper the operations of honest practitioners who are already increasingly burdened by regulations related to such issues as money laundering and terrorism. So the fraudster’s impact on offshore business has been two-fold: he has tarnished the reputation of offshore centres and, in many instances, increased the degree of regulation beyond what is needed. They may not be “the lice on God’s scalp” Victor Hugo referred to in his books and pamphlets criticising some of Napoleon III’s priestly sycophantic supporters, but the sentiment felt must surely be the same



for many offshore professionals when it comes to those rogues who most certainly are a blight on the reputation of the offshore services sector. Bearer shares are often the joker in the con artist's pack of cards and, as such, they have been misused, abused and have caused a great deal of problems. They have probably had their worst effect when used in estate planning: seen as a quick fix in testamentary terms (avoiding the need for a trust or will), they have, more often than not, made matters worse. The Book of Common Prayer puts it rather nicely: "We have left undone those things which we ought to have done and we have done things which we ought not to have done". In order to equip yourself against the machinations of the mountebank, it is helpful to not only have at least a grasp of the role bearer shares should play, but to also understand some of the fundamentals applicable to company and fiduciary structures, both of which are central to most offshore strategies.

To start, let's go to the pyramids of Egypt as opposed to the pyramid schemes of swindlers. Cleopatra paid divers to put fish on the hooks of Mark Antony's rods when he went fishing in the Nile because, besides wanting to keep him on her own hook, she believed in leaving nothing to chance. It's the same with estate planning: try and leave as little as possible to chance. So many people put off attending to their testamentary affairs and as a result of this wills, trusts and foundations are spoken about more than dealt with. I understand the aversion: it's a grim business but, as John Maynard Keynes said, in the long run we are all dead. Woody Allen, on a lighter note, quipped that he was not afraid to die, he just didn't want to be there when it happened. I agree with Woody, but it's what happens afterwards that matters. Assets may pass into the hands of people you wouldn't wish to give a smile to, let alone any of your assets. So one of the initial questions a practitioner should ask a new corporate client is: what's going to happen to the shares of the company we are managing for you if something happens to you? Companies are a staple of

offshore planning today even although J. B. Priestley considered them as part of "a shoddy, greedy profit-gobbling system" and Adam Smith said that they were "by-words for greed, sleaze and corruption". Many readers may well ask themselves what has changed since then.

In the early days of offshore centres, a strong belief took hold that bearer shares could replace a will, trust or foundation because, after all, bearer certificates were easily passed on and whoever held the certificate owned the shares. Today, it is fair to say that this belief is no longer widespread and there is an awareness that bearer shares, like trusts and foundations, have been used for purposes for which they were never intended. Bearer shares are as old as the concept of companies and, originally, were the normal way in which ownership rights were established. The certificate did not record the owner's name and was deemed to be owned by the person possessing the certificate, the bearer, in other words. Whomsoever had the certificate controlled ownership and, like the cash in your pocket, it was very easy for a certificate to exchange hands. Gradually, however, certificates recording the name of the owner became the norm until the point was reached where some countries, including many states in America, no longer permitted the issue of bearer shares.

Clearly, bearer shares are the handiest form of transfer, but they can also be the most hazardous means of ownership. Inevitably, with their misuse offshore in particular, there is an increasing number of court cases around the world in which ownership of bearer shares is being fiercely contested. The litigation, if more than one jurisdiction is involved in a dispute, can be especially slow and costly. If the truth be told, however, much of the litigation could have been avoided if the parties had acted responsibly and been properly advised in the first place. The fraudster, on the other hand, will encourage the use of bearer shares if it is expedient for his purposes, having no regard whatsoever for the possible consequences. In many instances, bearer shares are held by third parties on the



strength of a verbal agreement with the owner. I cannot image a more precarious arrangement and, as Sam Goldwyn once observed, a verbal contract is not worth the paper it's written on. It is little wonder that onshore professionals are highly suspicious of bearer shares with all the horror stories which crop up frequently.

What has to be appreciated is that it is one thing to hold bearer shares of a multinational company (provided the certificates are held in a safe and secure facility) but when bearer shares give access to other personal assets (such as those held in a private individual's offshore company) then a different perspective is needed. So if you believe in magic wands and the tooth fairy, you may still think that anyone presenting bearer share certificates of an offshore corporation will be automatically recognised as that company's new owner and, therefore, of all its assets, such as bank accounts, stock portfolios and a finca in Panama. You would be foolish to think so, if you are dealing with responsible professionals. But provided that you follow the cardinal rule: control and correct paperwork, it is still feasible to use bearer shares when, for example, there is perhaps one specific asset such as a piece of undeveloped land; bearer shares in such a case – and subject to a simple trust – may not only reduce paperwork and save subsequent property transfer costs, but can provide, if desired, a greater degree of confidentiality.

Being a Bit of a Payne

In matters concerning estate planning I strongly believe in Henry Thoreau's advice: "simplify, simplify". This is especially so in the case of trusts and foundations which are greatly exploited by the confidence tricksters whose intention in such cases is more likely to be: "mystify, mystify". There is such a tendency today to lose sight of the essentials, with some professionals playing word games, looking for Enronesque escape hatches. This is especially so in those legal systems where form rather than substance predominates. Overdoing things brings to mind the US Senate committee testimony given by John Ashcroft. The US

Attorney General had just completed a statement, the length of which brought thoughts of a Fidel Castro political speech to mind.

"Thank you, Mr. Attorney General, for that extensive opening statement," began Judd Gregg, a New Hampshire Republican. "It does remind me a bit of a fellow I used to represent when I was practising law named Oscar Payne. He went to church once and it appeared he was the only one at church. And the minister spoke, did three readings from the Bible, and they sang four hymns, and did a sermon – and a full sermon – it was a very good sermon. And they had the offering even. They passed the plate. And at the end of the service, the minister went to the front door and said to Oscar, as he walked out – shook his hand – "Oscar, what did you think?" And Oscar said, "Well, when I go down to my field, if I only find one stalk of corn I don't dump the whole load of manure on it." "

But sometimes complexity dictates more, rather than less. If so, then, ahead of following the advice of someone who is perhaps more interested in your chequebook than your welfare, you should consider a number of issues, whether you are contemplating a trust or a foundation. Firstly, the distribution of funds to beneficiaries. Are they to be discretionary or fixed and what powers, if any, are to be granted to third parties if distributions are to be discretionary? Then there's management's administrative powers as well as their rights and duties. These should be spelled out to avoid possible disputes down the road because tacit understandings are just not good enough. Also, the appointment or removal of management and management's powers of delegation are two very important issues. And although often overlooked, management's exposure to compromise can be a factor because one needs to be mindful of conflicts of interest (such as where a trustee may also serve as banker or accountant, for example). The recent Wall Street analyst precedent is best avoided. There is also the matter of choosing which jurisdiction's law should apply, although in nearly every instance this is only of concern in the case of trusts. It is common, for example, to



have a jurisdiction's law applicable to a trust even although the trust's administration is carried out in another jurisdiction. Sometimes it is considered prudent to locate the trust's records (administrative and accounting) in a place which perhaps has superior laws of privacy, although not necessarily a better trust law. In other situations a particular trustee may be preferred who happens not to be located in the jurisdiction whose law applies to the trust. Two other important considerations are the trust's or foundation's duration and possible revocation; a provision for the amendment to the terms of the trust or foundation might also be desirable. Last, but by no means least, the way the assets are to be invested has to be thought through. Often the trustee has no investment expertise and a reliable adviser, therefore, is needed. If an adviser is appointed, should decisions be made solely by him or in conjunction with management?

You should hasten slowly and, as with bearer shares, which may be expedient for someone else's purposes, don't be encouraged to accept a stereotypic deed which purportedly covers all

contingencies. More and more people are looking at the possibilities of having assets held offshore and so the opportunities for the tricksters abound. With little effort, however, you can find the right professional guidance to address all the issues mentioned. Otherwise, you will need the forethought of Cleopatra as well as the ability to detect the purveyors of falsehoods. Many people have been fooled more than once in their dealings offshore and, if you are one of them, you can perhaps seek comfort in the fact that one American study determined that even experts in their respective fields can suffer from an important deficiency: they fail to learn from experience. Another study, this time in the United Kingdom, concluded that only two groups of people, in fact, seem to learn from experience: weather forecasters and professional bridge players. Apparently, that is because they get feedback quickly and often. But Shakespeare knew a thing or two about human nature, long before there were any studies, when he observed that the world is a "great stage of fools". The trick is to stay off-stage, in the wings, if you can.

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Engaging an offshore representative is an important decision and we advise all persons to seek appropriate legal and tax advice from professionals licensed to render such advice before making offshore commitments.

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