



## TRUST SERVICES, S.A.

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Professional Firms, Institutions and Individuals since 1981*

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### OFFSHORE PILOT QUARTERLY

#### *The Wild West Indies*

Dictators and despots, particularly in the early part of this century, have frequently spoken about a new world order. The phrase was used recently - not at a political rally - but during a conference celebrating the first anniversary of the establishment of the Financial Services Commission in Jersey in the Channel Islands. The speaker was John Moscow who has been mentioned in previous issues of this newsletter. Mr. Moscow is the deputy chief of the investigations division of the New York district attorney's office who successfully prosecuted the collapsed Bank of Credit and Commerce International. In his speech, he was talking about the various bank secrecy statutes of foreign countries that, in his view, were no longer needed in today's world of international finance. I must admire his temerity in delivering such a message in Jersey, which is one of the inner temples of offshore banking. Mr. Moscow went on to say that if we are to prevent criminals from getting control of the world, a new set of rules must apply and he quoted Thomas Jefferson in support of his argument: "Eternal vigilance is the price of liberty." The liberty of other nations is recognised by two pieces of American legislation: The Foreign Sovereign Immunities Act and the Act of State Doctrine which

cover the sensitive subjects of confidentiality and taxation laws enacted by foreign countries. The two Acts are supposed to bring objectivity to the argument when the United States is considering the activities and practices of foreign countries and they affirm, firstly, any foreign government's right to pass laws establishing its own policy regarding fiscal and privacy matters and, secondly, they acknowledge that the decisions made are beyond the reach of the United States courts. These two pieces of legislation are not required reading, it would seem, for members of the investigations division of the New York district attorney's office.

Predictably, on the matter of money laundering, Mr. Moscow, in his Jersey speech, attacked places that he described as "legal quirks", including, the Cayman Islands and Antigua. Perhaps the Financial Services Commission on Grand Turk should recommend to the Executive Council that the jurisdiction change its name to the Quirks and Caicos Islands? But in mentioning the Cayman Islands and Antigua in the same breath, Mr. Moscow intimates that there is no regulatory distinction between the two and in doing so he displays an ignorance - innocent or otherwise - that is shared by many. The comparison is the same as that of chalk with cheese. Mr. Moscow



and his advocates see the Caribbean, however, as a vast watery wild west where uncontrolled cowboys ride the range. Financial Services Centres in the Caribbean fall into two categories: dependencies, such as the Cayman Islands, and independent countries, such as Antigua and Barbuda. The dependencies are overseas territories of countries that are members of the European Union and which have been highlighted frequently in the Offshore Pilot Quarterly. Their regulation and supervision has been influenced and guided by an expertise that, in most cases, was imported decades ago from Europe. Even the Organisation for Economic Co-operation and Development (the grouping of industrialised countries) has recognised that in the region some centres are better regulated than others. One east Caribbean government official recently said that the Cayman Islands, with its long history of offshore finance, has continuously upgraded its legislation and is in far better supervisory shape than Antigua which has, in his opinion, weak regulation at the root of its problems. In the case of money laundering, the American State Department said in a March report this year that Antigua is “one of the most attractive centres in the Caribbean for money laundering”. It has been said that Antigua’s 50 or so offshore banks are not tightly regulated and reports abound that it is a popular meeting place for Russian, Italian and Colombian gangsters involved in drug smuggling and arms running. American banks have been told to apply “enhanced scrutiny” to customers’ dealings in Antigua and the United Kingdom has pressured the island into closing down 9 banks. Accepting that no offshore

financial services centre is free from blemish, it is still unfair and unrealistic to tar them all with the same brush. I have another quote from Thomas Jefferson which should have been heard by those who attended the Jersey celebrations: “The natural progress of things is for liberty to yield and government to gain ground”.

### ***He Hath Foundeth it Upon the Sleaze***

The motto of the Cayman Islands, “He hath foundeth it upon the seas”, should be changed to the title of this segment if comments coming from the United States government and other quarters are to be believed, following the John M Mathewson affair. This year is the 100<sup>th</sup> anniversary of the birth of Alfred Hitchcock and Ernest Hemmingway and the bureaucrats seem to have been imbued with their respective spirits of suspense and vivid penmanship when it comes to the Mathewson story which is, admittedly, a fiction writer’s dream. Gloatingly, Robert Jordan, an FBI agent, proclaimed, “The Cayman Islands are no longer the safe haven they once were”. Maybe not for the 1500 or so U.S. citizens in about 20 American states who could eventually be charged with tax evasion because of Mathewson, but the Cayman Islands are alive and well; the scandal and the embarrassment which it has caused will pass over the islands like a tropical storm. It should be noted that the Inspector of Banks in the Cayman Islands had already shut down Mathewson’s bank, Guardian Bank & Trust Limited, 3 years ago, because of irregularities; it joined 3 other banks which have been liquidated because of similar concerns. Why Mathewson, the disgraced banker, kept vital client computer records in San Antonio, Texas,



is unknown to me. One could speculate that these records were kept as a potential bargaining chip (which, as it turned out, they most certainly proved to be) or, perhaps, the motive was more sinister, such as a source of blackmail. Whatever the reason, the records were stumbled upon by FBI agents when the 71 year old Mathewson was arrested in 1996 as a result of an unrelated nationwide investigation into a cable piracy operation. Because of the computer records, Mathewson was able to plea-bargain his way into receiving only a probationary sentence after being found guilty of federal conspiracy and money laundering charges. It has been estimated that the final total of recovered tax funds from Guardian Bank & Trust Limited will be about \$300 million. The U.S. government has already recovered \$50 million in back taxes and penalties. The financial fiasco does raise an important issue, one which will be mentioned again later on: should Americans entrust their personal offshore business to Americans or others who have strong connections with America? Moving your bank account *in*, rather than *from*, the Cayman Islands might be wise. It was the fallibility of man, and not the vulnerability of Cayman, that is at the heart of the Mathewson business. Cold comfort for Dr. Jeffrey Lavigne, a depositor of Guardian Bank & Trust Limited and a U.S. surgeon who treats hemorrhoids. He has seen the bottom fall out of his world – in more ways than one.

#### ***Rye Comment***

In previous issues I have mentioned the increasing control over offshore activities being exercised by the European Union because of its mandate.

The United Kingdom has, in the past, reminded its dependencies that directives (tantamount to orders) from the Commission of the European Union might compel compliance – regardless of the United Kingdom's stance. So it comes as no surprise to find that the Brussels-based European Commission has referred the United Kingdom to the European Court because it has failed to enforce four important company law directives in its dependency, Gibraltar. Without going into great detail, the directives related to the presentation and disclosure of company accounts. In the European Union itself, these particular directives have already been adopted (in some cases, as long ago as the 1980s) but Gibraltar has dragged its heels because of worries over the harm compliance might do to its reputation as an offshore financial services centre. Consequently, the United Kingdom will now be required to explain why the directives have not been implemented. Those dependencies nestling in the Caribbean take note: in the bureaucratic scheme of things, it is a small leap from a rock near Spain to a sandy beach in the Caribbean. Unions, whether they be European or otherwise, can still be inhibiting as well as suffocating and are often, in fact, monopolies – if not in name. History has many examples and one which I think is apposite is the whiskey war which raged in America one hundred years ago. Ironically, at its core, were two trusts – cousins to the offshore variety that today are the bane of tax collectors in developed countries. But beyond that tenuous connection, the two similarities which struck me were, namely, independence and quality. They came to mind at a recent conference here in Panama when I listened to a



representative of the Financial Services Commission in Gibraltar speak of his jurisdiction changing from a pure traditional offshore financial services centre into a European offshore financial services centre. It was losing its independence (perhaps he was mindful of those four company law directives) and it was diluting its quality as a financial centre by creating a blend of customary offshore financial services and standard onshore controls. This fate, I believe, will be shared by many overseas territories with filial ties to Europe. In the case of those whiskey trusts, some independent distilleries remained outside their control just as sovereign offshore financial services centres today remain beyond the perimeter of mainland officialdom and can offer pure, not blended, offshore financial services.

Aficionados of whiskey know that 95% of malt whiskey goes into blends and only 5% is bottled as pure single malt. Will this ratio of purity and dilution eventually apply to offshore financial services centres as well? It is a sobering thought.

***Wealthy Expatriates, Terrorists, Convicted Criminals and other Undesirables***

Excluding the European Union, there is a great deal of uncertainty over the unpredictable direction that the attitude of governments of developed countries is taking towards financial services that are controlled offshore. Money laundering and tax avoidance (the latter, until recently, an acceptable practice) are phrases that are becoming synonymous with one another. Even those wishing to avoid taxes in America by relinquishing their U.S. citizenship will not escape

without being stigmatised. Senator Daniel Patrick Moynihan has said that if a wealthy U.S. person gives up his citizenship, primarily for tax reasons, he could be permanently barred from re-entering the country. He referred to an immigration statute that “adds wealthy expatriates to the list of terrorists, convicted criminals, persons with communicable diseases” who could be subject to permanent exile from the United States. Even those Americans who live overseas and who remain citizens but have been less than diligent in filing their income tax returns of late could be in for a rude awakening. Passports, not seized bank records, are going to be the weapon used against them. When American expatriates apply for new passports, their tax status is going to be checked. Initial target countries where expatriates are living will include the United Kingdom, Canada, Mexico, Germany and Switzerland. Around 200,000 Americans live in London, making the United Kingdom home to one of the largest American communities outside the United States. Because U.S. citizens have to provide their social security number when renewing their passports, it will be easy to cross-reference records with tax returns. The haul anticipated by the Internal Revenue Service runs into billions of dollars, against which the tax recoveries arising from the defunct Guardian Bank & Trust Limited will pale into relative insignificance. There are 30,000 U.S. expatriates living in Switzerland and it is reckoned that just under half of them have failed to file tax returns. Some of these tax dodgers might be alarmed to learn that although the taxes are not owed to Switzerland, certain Swiss banks are collaborating



with U.S. customs and tax officials. The only institutions implicated up to now in this collaboration are those with a presence in America and it strongly suggests to me that if you are an American, it might be wiser – as in the case of Guardian Bank & Trust Limited - not to choose an offshore service provider which has close links with America, where pressure (subtle or otherwise) can be exerted and over which you will have no control whatsoever.

Certainly the rules are changing and offshore financial services centres everywhere will find the odds increasingly stacked against them. Every political and commercial trick in the book, supplemented by propaganda

of questionable accuracy, will be employed. Which independent centres will survive is a hard question to answer with any certainty. In the regular Latin American column which I write for the South African Institute of Bankers I have said that a crystal ball might help when trying to predict the pace and direction of change in South America: it's equally so in the case of the offshore financial services industry. "Tentative date depending on sighting of the moon", was the imprecise phrase used earlier this year in trying to establish the date of an Indian holiday. Most of us in the industry would be happy with that degree of certainty when trying to guess who those offshore survivors might be.

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