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OFFSHORE PILOT QUARTERLY

Commentary on Matters Offshore

September, 2008.

Volume 11

Number 3

The Evil that Walks Invisible

Ben joined me for coffee recently and brought along a friend, Simon (not his real name). Those of you who have read the Offshore Pilot Quarterly for several years will recall my infrequent mention of Ben in the past and our occasional meetings for coffee. I had never met Simon but he came across as a mild-mannered Englishman, perhaps in his late 60s, whose demeanour suggested a background in either accountancy or law. Neither was the case, as I subsequently learned, and during a varied career as a banker he had been at one time a financial services regulator. He was in Panama for a few days and Ben, a friend of his from the past, thought I might like to meet him as we had much in common, each having been involved with the regulation of financial services in the Caribbean. We had, in fact, both been contracted by the British Foreign and Commonwealth Office and whereas Simon had taken over from someone, I had been engaged, inter alia, to establish a regulatory authority and recommend appropriate legislative improvements. And although he had a path to follow and I encountered virgin terrain, we found a lot of similarities with our respective island experiences.

Just that week, I told them both, I had read about one financial services jurisdiction whose companies had been involved in the laundering of some \$36 billion from the former Soviet Union; that is an amount that could finance the present Panama canal expansion project at least six times over. In this same jurisdiction, Russian officials had used

companies to unlawfully divert \$15 million in international aid meant to fund a safety upgrade of former Soviet nuclear power plants and in another case an individual had set up more than 2000 companies, established bank accounts for them without disclosing identities, and then passed some \$1.4 billion through the accounts. It turned out, in fact, that one of those companies had received over 3,700 suspicious wire transfers which, during a two-year period, added up to just over \$81 million. But the authorities could not pursue this case because they were unable to discover who owned the company due to the lax laws of the jurisdiction. With examples such as this, was it any wonder that the wrath of the United States Senate (expressed recently and publicly in vociferous terms) was aroused, when it is already trying hard to stop offshore financial abuses, especially tax evasion, perpetrated by American citizens? The US jails more people than any other country and, for the first time in its history, over one in every 100 of the nation's adults is in jail, according to the Pew Centre, described as a fact tank that provides information on the issues, attitudes and trends shaping America and the world through public opinion polling. There are over 2.3 million adults (China has 1.5 million) in jail and the prison population has almost tripled in 20 years.

One could ponder that the Senate should count itself lucky that only around 20% (see the June, 2006, OPQ issue) of Americans have passports: just imagine the trickery they might get up to if they could actually travel to the world's international



financial centres and take a more hands-on role in those abuses?

Democratic Senator Carl Levin, chairman of the sub-committee on investigations of such offshore abuses, has not minced his words in some recent, and public, outbursts: “Tax havens are engaged in economic warfare against the United States... The iron ring of secrecy around tax haven banks and their deceptive banking practices enable and encourage tax cheats to hide assets”. Not to be outdone, the sub-committee’s ranking Republican, Senator Norm Coleman, declared that foreign banks were acting as “Al Capone safe houses for evading taxes”.

The US and all the developed nations are right to try and discourage financial misdeeds perpetrated beyond their borders because of slack rules, but such efforts should not allow a smoke screen to descend that obscures the need for similar remedial efforts to be made onshore.

John Milton, the seventeenth century English poet, may have observed that “neither man nor angel can discern hypocrisy, the only evil that walks invisible;” but its presence is palpable today in the case of mainland attitudes towards offshore financial business. We’ll come back to those double standards at the end of this newsletter and, meanwhile, just keep in mind Mark Twain’s words: “Get your facts first, and then you can distort them as much as you please”.

Blowing the Whistle

Using the word “offshore” is now becoming less in vogue, bearing in mind that it has been a flag – depending on your perspective and also your experience – for shady dealings. Even the International Monetary Fund, which since 2000 has had a separate assessment programme for offshore financial centres in place, has decided to close it which will “eliminate the need to maintain a potentially discriminatory list of offshore financial centre jurisdictions”. Defining the varieties of financial centres, however, is becoming a little complex and applying the nomenclature “tax haven” is even more difficult to nail down; for some, Senator Levin’s country qualifies as a tax haven.

There are, in fact, just two international centres that can be described as Global Financial Centres, according to a report published earlier this year which was commissioned by the City of London. Those centres are London and New York which met the criteria and scored the most points in the key five areas: people (talent), business environment, market access, infrastructure and general competitiveness. The report mentioned four other categories of centre, namely, the International Financial Centres which are involved with high-volume cross-border transactions (Hong Kong, for example, undertakes a large amount of Asian financial activity), followed by niche, national and regional (within a country’s borders) centres.

Niche centres have developed a particular product, such as private banking in Zurich, reinsurance in Bermuda and producer-owned reinsurance companies in the Turks & Caicos Islands. National centres, on the other hand, conduct the largest portion of a country’s financial business; but sometimes a large country will have more than just one such centre and the choice then seems to depend on the city which predominates in foreign exchange transactions. The fourth and final category, regional financial centres, are centres within a country where a large amount of a particular region’s financial activity takes place. Perth has become the financial capital of Western Australia, for example, with a strong presence of bankers and mining companies.

We were engrossed in discussing the subject of financial services, with its many facets, and we ordered more coffee. While we waited for it Simon remarked on some of the frustrations he had experienced and likened them to being a referee on a football field with the public sector at one end and the private sector at the other. Frequently, both scored own goals and whilst the rules of the game were clear, not everyone followed them; and when the referee used his whistle, it was often ignored. It seemed also that red cards were acknowledged on a selective basis because some offenders played on regardless. As he continued, I began to compare his regulatory experience to that of Penelope in Homer’s Odyssey, she who patiently keeps the suitors at bay for three years, craftily unpicking at



night what she has woven by day. Only in this instance, it was Simon who had been weaving whilst others did the unpicking. I recognised and sympathised with a fellow weaver.

Confusion sometimes arises over where ultimate power resides in respect of those islands whose flags, in some cases, incorporate the Union Jack and promote themselves as financial service centres. The most important point is that they do not possess absolute sovereign independence – whilst accepting, at the same time, that some enjoy more independence than others. This is an issue which has been raised before in the OPQ. The UK has 9 such islands, a mix of Crown Dependencies and Overseas Territories, whose populations, like the international financial services they offer, vary. Alphabetically, the islands comprise: Anguilla (13,500), Bermuda (63,500), British Virgin Islands (27,000), Cayman Islands (48,300), Channel Islands (200,000), Gibraltar (28,700), Isle of Man (80,000), Montserrat (4,800) and the Turks & Caicos Islands (30,600).

Like populations (given here in round figures) and services, the quality of regulation found can also differ. Even if every island had good laws, without good regulation (and regulators) they will not achieve their (sorry, Simon) goal.

Perhaps if Senator Levin could allocate more time to addressing the loopholes in America's financial services industry, especially when it comes to transparency (read on), the British government could allocate equal time to effectively tackling the contentious offshore island issues which, ultimately, are its responsibility.

Slitting Throats

It is over 15 years since I last walked through the portals of power on my official visits to the FCO in London, but I have maintained a continuing interest in its affairs as they relate to regulation of those island finance centres. So it was with great interest that I sat down and read the House of Commons Committee of Public Accounts report issued in May which, inter alia, considered the FCO's oversight of offshore financial services in the Overseas Territories. I would suggest that for many ex-regulators reading the report who have worked in

one or more of those territories, and who had gone out to do a job, rather than keep one, the comments of the late H. L. Mencken, that literary curmudgeon, would ring true: "Every normal man must be tempted, at times, to spit on his hands, hoist the black flag, and begin slitting throats".

I had followed up on Simon's analogy by reminding him that the referee in his regulatory game of football had more than just the players at both ends of the field to contend with; there was the Football Association as well, only in his scenario that would be the FCO. You only had to read the May report to see that. Emotions, not economics, may have the greatest impact on stock markets but in the case of regulation it is, like most fields of endeavour, always personalities, not practicalities, that too often prevail. The report recognises how acute this aspect can become, noting how a system of government operating in a small community, where friendships and family ties are more concentrated, can lead to conflict of interests.

Personally, it was the words uttered by Edward Leigh, Chairman of an earlier meeting of the Committee of Public Accounts, on 10th December, 2007, and mentioned in the report, which caught my attention. It was a question directed at Sir Peter Ricketts, the Permanent Secretary of the FCO, who was attending as a witness, and it was this: "Tell us exactly what is happening in the Turks and Caicos Islands and [give us] reassurance that you have got a grip there, please".

I could have helped Mr. Leigh with that question. I also suspect that parts of my answer would have been helpful to Jamaica (see the January issue of our regional newsletter, Letter from Panama) as well as Trinidad and Tobago where international financial centres are in the works.

Ben said that he had read where Jamaica might focus its offshore services on the sport and entertainment sector. An enthusiastic Dr. Trevor Thomas, who is an international tax consultant, apparently envisages Jamaica as a financial centre for the stars which, in turn, could attract lesser known entertainers; he supported his reasoning by quoting the Frank Sinatra fan who said that "What's good enough for Ol' Blue Eyes is good enough for me". I know this much: setting up a Jamaican



finance centre could lead to a lot of black eyes for its government if it is not careful.

We had finished our second cup of coffee and it was time for me to go.

“You must tell us more”, Ben added as he scraped back his chair, “about the Turks and Caicos, I mean”.

“Hopefully before Simon leaves I’ll be able to.”

We got to the door, shook hands, and then Simon said: “That jurisdiction you mentioned, involving over \$36 billion in money laundering out of Russia. You never said which centre it was”.

“I can tell you that none of the members on Senator Levin’s sub-committee would need passports to visit it, because those abuses all took place in the US,” I replied.

I went on to tell them that the 2000 companies I had also talked about were set up in Delaware and the Russian revelations involved companies registered in Nevada and Pennsylvania.

I remarked that it seems that the crack in Pennsylvania’s Liberty Bell is slight when compared to the one in its company registration system. Nationwide, the US forms nearly 2 million

companies each year and US Department of Homeland Security Secretary, Michael Chertoff, has complained that “In countless investigations where the criminal targets utilise shell corporations, the lack of law enforcement ability to gain access to true beneficial ownership information slows, confuses or impedes the efforts by investigators to follow criminal proceeds”. So shell companies are not all offshore.

In fact, back in 2006, the Financial Action Task Force on Money Laundering, the leading organisation in its field, issued a report which criticised the US for failing to be able to obtain beneficial ownership information. I told Ben and Simon that the FATF had asked the US to correct this deficiency by July, 2008, the very month the three of us were meeting for coffee.

“There’s still two weeks to go”, Simon said wryly and we laughed.

Then we all went on our way and as I walked back to my office thoughts of Milton, Twain, black flags and slitting throats were fixed firmly in my mind.

Offshore Pilot Quarterly has been published since 1997 by Trust Services, S. A. which is a British-managed trust company licensed under the fiduciary laws of Panama. It is written by Derek Sambrook, our Managing Director, who is a former member of the Latin America and Caribbean Banking Commission as well as a former offshore banking, trust company and insurance regulator. He has over 40 years private and public sector experience in the financial services industry. Our website provides a broad range of related essays, including our other newsletter, Letter from Panama, which focuses on Latin America and is also written by Derek Sambrook

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