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Commentary on Matters Offshore

Coffee with Ben

My friend arrived late with profuse apologies. It had not been an inconvenience for me, however, as I had spent my time looking out across the expanse of blue ocean in front of the bay, to the islands beyond, enjoying the vista. After a busy day, as dusk fell, it had been nice to relax for 15 minutes or so. We ordered coffee and Ben returned the copy of the speech which I had given him earlier in the week.

"The message comes across loud and clear at any rate", he said, referring to the speech which had been made by José Miguel Alemán, the Minister of Foreign Relations of Panama, at the October International Bar Association Conference in Durban, South Africa. The theme of the speech concerned the contentious subject of Panama's position regarding the international tax co-operation initiative of the Organisation for Economic Co-operation and Development. In his speech the Minister confirmed Panama's willingness to co-operate with the OECD provided it recognised Panama as a sovereign state rather than confusing its identity with that of a dependency of another country which had a purpose-built offshore financial services industry.

"You see, there's an important issue here," Ben continued. "Let's not forget a fundamental difference, which the Minister touched upon, between Panama and, say, the Cayman Islands. In the case of Cayman it was as if Walt Disney went in there and created "Offshore World". Long before that, when Cayman had more mosquitoes than dollars booked through its banks, Panama had the very same tax system in place that it has today".

I took the first sip of coffee and thought how he was absolutely correct. It is ironic to think that what could be termed the "Cayman problem" arose as a result of past government policy in Europe which encouraged many dependencies to build up offshore financial services industries; it was potentially an important source of employment and revenue for the particular dependencies and, therefore, the answer to less reliance on funding from home governments. It was a good idea: offshore financial services were, in a sense, confined to the skills of practitioners and filing cabinets with an infrastructure capable of being housed on a bank's premises or in a lawyer's offices. No industrial pollution or need for large areas of land to be used.

But the issue which has now come to the fore and which has upset the balance of things is taxation. Britain, as a member of the OECD and the European Union, has been criticised in particular because of the tax policy in some of its dependencies. The situation can no longer be swept under the carpet. Panama, in contrast, whilst a member of the United Nations, is neither an OECD or EU member and, as the Minister in his speech stressed, plots its own destiny and determines its own laws. It was amusing to read recently that the Cayman Islands might not co-operate over the European Union's Savings Tax Directive which calls for exchange of information when Britain, with the stroke of a pen and an Order in Council, could compel its dependency to comply.

"Perhaps the system of taxation hasn't changed in Panama", Ben went on, "but what has certainly changed radically over the years is the supervision of offshore financial services. I know that from my own experiences. People are beginning to complain about the difficulties now encountered opening bank accounts in countries such as the United States. Some of them should try to open one here".

"The requirements in Panama certainly rival any in Europe", I said, stirring my coffee, "but at the same time I accept that the caution displayed by the Panama banks, underpinned by the rules set by the country's Superitendency of Banks, is admirable as well as understandable because of the large number of banks operating in Panama and the country's role as a regional offshore centre".

"On this question of supervision", Ben said, "the OECD, it seems to me, has opened up a Pandora's box".

"It has", I replied, "and it's a classic example of what I call the law of unintended consequences. What has come to light is the fact that many OECD countries need to take lessons from some of the offshore centres when it comes to controls. In Britain and America, for instance, it's easy to set up companies within 24 hours and provide little or no information about ownership to the formation agents. Delaware law, for example, doesn't require the agents to know who beneficially owns a limited liability company".

"That's not all", Ben added, "I read recently that the OECD's offshoot, the Financial Action Task Force, has said that all FATF member countries must be sure that their banks know the owners of their corporate clients. Isn't that stating the obvious? Any member with banks in its territory not doing so should be blacklisted. You mentioned bank due diligence in Panama – and I've seen what that involves from your website – so I can just imagine any local bank's reaction to that FATF remark".

"That's true, Ben, and did you know that bearer shares are not an offshore phenomenon? You can have bearer shares issued in such places as Austria, Belgium, Germany and Switzerland".

"Speaking of Switzerland", Ben said, "their trust regulation is non-existent, and here's the FATF recommending that the trustees, settlors, protectors and beneficiaries of trusts everywhere should be registered. First regulation then registration, I would say".

I mentioned that America and Britain have already said that registration of trusts is a non-starter and, tapping the copy of the Durban speech, went on to comment that no wonder the Foreign Minister was concerned over double standards.

"The now-famous level playing field term", my friend responded.

"Exactly. And we've only scratched the surface of what that entails before Panama commits to the undertaking concerning the OECD initiative it signed back in April this year. Just look at the song and dance going on between Switzerland and the EU at the moment over sharing tax information – and that was before the Americans scuppered the whole process by saying they would not participate. Their agreement was one of those crucial to the EU having cross-border information-sharing in place before 2003, the deadline set following a tortuous process that has been going on for 2 years now". Six countries outside the EU (Switzerland, the United States, Liechtenstein, Monaco, Andorra and San Marino) had to agree to sharing information before any agreement could be implemented.

"Anyway", I went on, "this issue of fairness, or equitable treatment as the Minister put it, is very important in the case of Panama which, unlike many offshore centres, has a long-standing genuine tax system in place. It is not cosmetic and is essential to the country's financial health. Taxes are territorial, meaning that income earned outside the country isn't taxed; this gives Panama a competitive advantage where over 75% of the gross national product comes from the services sector. In fact, about 80% of the government's revenue is earned from taxes and tax on income makes up about 40% of that total. Income tax for both individuals and corporations can be in the range of 30% and it should be remembered that evasion of Panamanian taxes is a crime and can lead to imprisonment".

It was easy to understand why the Foreign Minister observed that OECD members such as Luxembourg and Switzerland had been critical of the initiative and why the dialogue between the OECD Secretariat and the offshore jurisdictions had been difficult and frustrating at times. Even so, he had said that Panama will co-operate within the boundaries of fair play in which the sovereignty of states is respected and all participants, whether members of the OECD or not, are dealt with on an equal footing. He did point out, however, that Panama would not be forced to collect taxes on behalf of a foreign government and intended to protect its economy from being compromised as a result of favourable treatment given to any participants in the OECD initiative.

Ben and I spent another 10 minutes on the topic which ended with me reminding him that although the OECD, with a staff of 800 at its Paris headquarters, serves as a think-tank, a sounding board for international policies and a negotiating forum, it is, nonetheless, a bureaucracy so the tax initiative, besides anything else, is going to present certain challenges for the 41-year-old organisation. Hard decisions lay ahead and bureaucrats don't like making them so let's hope that the tendency is not to take a leaf out of Lord Tyrrell's book. Tyrell was a British ambassador in France and generally confined himself to initialling official papers submitted to him. On one occasion, however, a file which he had initialled was returned to him with a note saying, "This requires a decision". Lord Tyrrell wrote back, "Yes it does" and returned the file.

Web of Deceit

George Bernard Shaw opined that those with the power of accurate observation are commonly called cynics by those who have not got it. Whilst acknowledging that no one can get it right every time, I also recognise that a healthy dose of scepticism, perhaps not cynicism, when dealing with offshore matters can prove invaluable. One of the reasons Ben had asked to have coffee with me, other than to return the copy of the Durban speech, was to get my advice about an international investment company which, in his words, "had a really first class website".

"Tell me, Ben, did the website include the names, professional background and physical location of the business?"

"No, it didn't", he confessed, but went on to say that there was an e-mail address included to which enquiries could be sent. The absence of certain fundamental information, I explained, doesn't prove wrongdoing, but it should put you immediately on guard because a reluctance to lay bare any background on the principals behind the business, or even show the address from which their company operates, can suggest that there is a sinister reason for not doing so. After all, the internet is the ideal environment for the con-artist. Earlier this year a website was established, purportedly belonging to South Africa's central bank (also known as the Reserve Bank). But there was certainly nothing reserved about the way the rogues behind it operated. Recipients in Britain and America were sent e-mails saying that Reserve Bank funds could be diverted to them; if they had any doubts they could visit a website (also fictitious) of a law firm which would prepare all supporting documentation. The recipients were warned about sharing this privileged information with others and were then invited to send "facilitation payments" to anonymous bank accounts. In some instances, up to $200,000 was lost by individual victims.

Honest people, naturally, receiving the e-mails would have pressed delete faster than you could have said Enron, but the case does illustrate the dangers lurking out there on the internet – whether those conned are honest or not. The Reserve Bank hoax certainly puts another African ploy in the shade: the perennial Nigerian advance-fee fraud, also known as the 419 scam after the number of the Nigerian law which prohibits it.

The whole issue of appearance and reality brings to mind the case of Thérèse Daurignac who was born in 1856 in France and who grew up in abject poverty. Thérèse retreated into a world of illusion in the same way as her penniless father had done as an antidote for the harsh reality of life and she spoke of vast wealth almost within her grasp. Her father's brother, Gustave Humbert, on the other hand, was destined to become a minister of justice in France's Third Republic and was to provide the platform from which Thérèse's grand schemes were to be launched. She secured her position by marrying Gustave Humbert's son, Frédéric. This fortuitous circumstance illustrates an important issue and over a second cup of coffee with Ben, as we talked about the deceptive qualities of websites and some of those creating them, I told him how one of the well-worn tools in the swindler's tool kit was respectability by association. Credibility can be gained by latching on to an unsuspecting source with excellent credentials, which is precisely what Thérèse did.

She spoke of a large inheritance given to her by an American billionaire with the implication that he, in fact, might be her real father. Her promised wealth comprised bonds which today would have had a value of US$3 million but which were, for the moment, locked away in a strong box. Thérèse now sought to borrow money, with the contents of the strong box as collateral, from the gullible. Incredibly, this maestro of contrivance was able to obtain money for 20 years until the strong box, supposedly holding the bonds, was eventually opened up to reveal only a button and one Italian coin. Thérèse served five years in jail for fraud and afterwards was never heard of again. Many of her victims were ruined and some even committed suicide. She was also a huge embarrassment to the French government of the day, not just because of the family connection with the minister of justice, but also due to the fact that the government had espoused high ideals of democracy and a desire to root out all scandal.

H.L. Mencken said that cynics smell flowers and look for the funeral; it would be a pity to take that harsh a view of life, but I reminded Ben that being a bit of an offshore doubting Thomas, as I had said before, can be as useful as a computer's virus shield sometimes. We had finished our coffee and lights now dotted the islands beyond the bay. A neon sign was flashing nearby and it occurred to me as we stepped outside that lights of a different kind were perhaps flashing red in Ben's mind as well.

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Bankers
HSBC Bank PLC
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Auditors
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Physical Address: Suite 522, Balboa Plaza, Avenida Balboa, Panama, Republic of Panama.
Mailing Address: Apartado 0832-1630, World Trade Centre, Panama, Republic of Panama.
Telephone: (507) 269-2438 – Telefax: (507) 269-4922
E-mail: marketing@trustserv.com Website: www.trustserv.com