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OFFSHORE PILOT QUARTERLY

Views and News on Matters Offshore

King Con

It is tempting to gloat over yet another massive onshore – as opposed to offshore - money laundering case following the revelations surrounding the \$4 billion (an amount similar to the one that the European Union plans to give to the 5 western Balkan countries) estimated to have been filched from Nigeria's public coffers by that country's former dictator, General Sani Abacha, during his four-and-half year rule. He must surely be crowned the current king of chicanery. Since his death from a heart attack in mid-1998, the money laundering web spun by Abacha and his cohorts has begun to unravel. \$300 million of the stolen money passed through London either from, or going to, Switzerland. The total amount deposited and left in UK banks may never be known. But what is known is that both the UK banks and authorities have left themselves exposed to harsh criticism. The fact that the UK bankers were manipulated by nefarious Nigerians merely confirms what we all know: that banking systems everywhere, onshore and offshore, are vulnerable. But what is emerging from the botched Abacha case is not the degree of bank vulnerability, it is, rather, the inconsistency, so far, in the degree of co-operation being given to the Nigerian government. The slow motion response onshore is the exact opposite of the rapid offshore actions taken by Switzerland, Luxembourg, Liechtenstein and Jersey in the Channel Islands in the search for Nigeria's state funds. In fact, it was through the efforts of Switzerland's Federal Banking Commission that the money trail found

its way to the doors of the banks in the UK. It is estimated that more than \$50 million in cash alone was brought into the UK by various means, including caseloads of bank notes.

All of this is bad timing in the wake of the black list issued by the Financial Action Task Force, a group set up by the Organisation for Economic Co-operation and Development, which, inter alia, seeks to raise the standards of co-operation between international regulators. The official UK response, so far, following the Swiss investigations has been lukewarm but the Financial Services Authority (the UK's banking regulator) is now examining the situation in conjunction with the banks involved. It was last year that the Nigerian government employed the services of a respected Swiss advocate, Enrico Monfrini, to approach the UK, Nigeria's former colonial power, and other main financial centres to try and track down the stolen money. But the UK would not freeze bank accounts at that time because no criminal proceedings had been started in Nigeria and until they were, no action could be taken. The uniqueness, however, of this particular situation cannot be ignored: there is a surfeit of detailed documentation and the theft concerned public funds of a country whose finances are in a perilous state, such that its financial stability is also at issue. Exceptional circumstances dictate exceptional measures.

Meanwhile, the Panamanian government has unanimously endorsed new legislation, putting Panama on a par with international money laundering regulatory standards. The maximum penalty for money laundering has been increased



and the definition of money laundering has been expanded. Now all serious crimes, rather than just drug trafficking offences, fall within the ambit of the new legislation and it is not just banks and trust companies that must report suspicious activities. Casinos, estate agents, insurers, the stock exchange, companies in the Colon trade free zone and even the national lottery must report transactions of more than \$10,000. This should please Rodrigo Rato, Chairman of the Financial Action Task Force, who visited Panama earlier this year. The government's Financial Intelligence Unit expects to investigate perhaps 3 times as many cases as it did last year. The country clearly wishes to preserve its banking sector and have its financial services industry grow; it has demonstrated in absolute terms, a willingness to co-operate. Panama will, nevertheless, continue to have problems with money laundering, which is not surprising, when, according to the International Monetary Fund, between 2 and 5 per cent of world gross domestic product originates from criminal activities. Still, what Panama – and every offshore centre that stands in the shadow of one or more of the OECD-inspired black lists – should expect is to be encouraged, not discouraged, by example. A recent British Council survey showed that Nigerians had the warmest attitude towards Britain. That may soon change, at least as far as its government goes.

The M Factor

Mr. Robert Mugabe, the President of Zimbabwe in Central Africa, and John M. Mathewson, the ex-Chairman of defunct Guardian Bank & Trust (Cayman) Ltd., have something in common. Being in the United States subjected them to that country's legal system. In the case of Mugabe, who was visiting New York earlier this year, lawyers invoked the terms of the Alien Tort Claims Act, a 211 year-old law that permits foreigners to pursue human rights violations in the American courts. The plaintiffs are victims of state-sponsored violence and are seeking damages of \$400 million. Mathewson, in stark contrast, was embroiled in taxes and such matters as money laundering as opposed to

murder. What is the relevance of this to matters concerning offshore financial services? It's very simple: if you don't want the laws of a particular country to pierce a hole in your hermetically-sealed offshore structure, consider the circumstances of the persons managing that structure. Don't assume that because the offices are offshore, the managers and executives cannot still be a source of compromise in your own jurisdiction.

It is understandable that lonely Americans, for example, in a foreign country will seek solace in familiar surroundings. It mightn't be home, but the taste of a McDonald's hamburger somehow brings home a little nearer. It's a comfortable feeling. Maybe some of the customers of Guardian Bank & Trust (Cayman) Ltd. felt that way when they did business with the Cayman bank. "Big John", as Mathewson was called, perhaps personified a Big Mac. If so, they forgot what being "offshore" means. I do not intend to rehash the Mathewson affair which has been analysed, scrutinised and dissected since the Chicago builder-turned-bank-Chairman probably became the most valuable single source to date of information for the prosecution of Americans for tax evasion. Mr. Mathewson, a 60% shareholder of Guardian Bank & Trust, is an American and when he was arrested in 1996 for facilitating money laundering, he was living in San Antonio, Texas. He not only provided a wealth of documentation, he revealed many of the tactics used for keeping the funds disguised, including the use of offshore credit cards. Enter the McDonald's factor, which can be a boon in the fight against crime, but can be a serious drawback for the individual wanting to sever the umbilical cord between domestic and international business affairs. It does seem a pity that so many people going offshore ignore the M factor, bearing in mind the abundance of able financial professionals with no personal connections whatsoever with the jurisdiction of their client. It has become common for plaintiffs to pursue related parties (no matter how tenuous the circumstances) when they cannot take direct action against the party they feel has aggrieved them. You can see the approach at work every day: co-trustees or protectors of foreign trusts,

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for example, who share a common country of residence with a trust settlor or beneficiary. These connections can be much like stepping stones that can lead those with sufficient animus and determination across the once-assumed secure moat.

It is, therefore, important to study carefully the antecedents of the offshore provider that you choose: are there stepping stones that can potentially compromise you? Maybe foreign hamburgers are an acquired taste, but it can be well worth the effort if you don't want your carefully concealed offshore assets delivered on a plate, as it were, back home.

Cards, Rubies and Catastrophes

Finally, a few words on the recurring theme of ability. You might wonder if a background in home building qualifies you for the hands-on chairmanship of an offshore bank and trust company. In the case of John Mathewson, we must assume that it was considered irrelevant. I hope that the houses he built are stronger than the house of cards that Guardian Bank & Trust (Cayman) Ltd. ultimately became. And you might also wonder if international bank regulation should be in the hands of inexperienced government officials, as was the case on the Caribbean island of Grenada in 1997 where a bank's capital adequacy was satisfied on the strength of an engraved ruby worth \$25 million. Audited accounts were never issued by the bank and the location of the ruby cannot be established. A gem of a story, indeed.

Ability must match the needs of the task, but it continues to be ignored either by design or default. The world of offshore financial services is becoming more complex and the need, therefore, has never been greater for recognising that those managing and regulating assets must possess the proper skills. In the public sector there is often a strong tendency to approach a problem by applying untested theory instead of seeking expert advice from those who have to deal with the problem on a daily basis. U.S. Air Force aircraft engineer Captain Edward Murphy observed that "if there are two or more ways of doing something, and one of them can lead to catastrophe, then someone will do it". This

safety-critical engineering hypothesis, known internationally as "Murphy's Law", is constantly validated by many bureaucrats. In the case of the tax black list of the Organisation for Economic Co-operation and Development, for example, Jeffrey Owens, the OECD's head of fiscal affairs, has now accepted that consensus rather than confrontation is the way forward in dealing with the 35 jurisdictions on the list. "We have got the message", he says, acknowledging that a greater effort in communication is needed on the part of the OECD. The Commonwealth, a body with filial ties to Britain, and whose members account for more than two-thirds of those on the black list, says that the OECD tax drive needs more careful study and that the economies of some small island states could be ravaged. Captain Murphy might have used the word "catastrophic" to describe the effect. On average, 30 per cent of the gross domestic product of each jurisdiction on the OECD list is derived from offshore financial activities, but judged on events so far, this has not registered with the Establishment, that amorphous assembly of bureaucratic committees, sub-committees and various bodies that are invisible, unaccountable but enormously powerful. It will be one of many issues, however, which are going to arise as this ill-advised initiative attempts to impose global tax uniformity. The Establishment's talking heads are going to be very busy.

In the private sector the offshore landscape is strewn with victims of bad advice and incompetence, those root elements of inexperience. Many of the wounds, however, are self-inflicted by not taking sufficient care in the first place. Wouldn't it be innovative, therefore, if one of the offshore governments issued a financial services advisory with their immigration cards? It need only contain a simple text along the following lines:

"We hope you enjoy yourself with us, but please exercise caution if you plan to attend to personal financial affairs during your stay. You have already taken the most important step by intending to visit the people you may wish to do business with. Here are some more:



1. Only deal with those holding proper licenses. If you have any doubts in this regard, please contact our financial services authority.
2. You should ask if the business is audited and who the auditors are. If an international firm does the audit, this should provide a good degree of comfort without the need, perhaps, for further enquiry.
3. Ask about the qualifications of the management, the extent of their experience and find out how long the business has been in operation. Consider asking for references if you have not already received a recommendation from a reliable source.

Professionals will not be offended by your cautious approach.

4. Costs are always an important factor, but fees shouldn't be the basis upon which you make your choice. What is cheap might be costly in other ways.
5. Ensure that you have obtained any necessary legal and tax advice in your home jurisdiction ahead of time. If not, don't commit yourself until you have."

It wouldn't just be a public service initiative, it would be a way of helping to protect the jurisdiction's reputation. But it requires a practical approach: the antithesis of untested theory, the common preference of bureaucrats.

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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.

Bankers

HSBC Bank plc

Dresdner Bank Lateinamerika AG

Auditors

Deloitte & Touche

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

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