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A Step in the Right Direction

The Steering Committee of the 10th Caribbean Conference of the Society of Trust and Estate Practitioners invited me to speak in May. It was the first time that the annual event has been held in Panama and whilst readers are, in varying degrees, familiar with Panama, this may not be so in respect of STEP.

It is a professional body formed 17 years ago with its headquarters in London in the United Kingdom and a membership comprising practitioners who specialise in trusts and estates, executorships, will writing, administration and related taxes. The Society has 74 branches in more than 35 countries, including Canada, several European countries and the United States of America.

Full members of STEP, who are awarded the designation TEP (trust and estate practitioner), include many of the most knowledgeable and experienced practitioners in the fields of trusts and estates; they make available special expertise in estate and succession planning, domestic and offshore trusts, trust and estate litigation and tax planning. Members must comply with a Continuing Professional Development regime and there is both a professional standards committee and a published Code of Conduct.

A number of international speakers at the STEP conference presented papers on a wide variety of subjects to over 300 delegates. The collective talent of the visitors from across the globe who came to Panama was very impressive and for my part I was soon reminded of Mark Twain's definition of education: that which reveals to the wise, and conceals from the stupid, the vast limits of their knowledge. I must confess that by the end of the conference I felt more educated than I did stupid.

The other local speaker invited to talk, Dr. Jaime Aleman, a distinguished lawyer and former President of the International Lawyers Association of Panama, discussed the fundamentals of trusts whereas I had been asked, inter alia, to consider whether civil law countries understand and apply Anglo-Saxon trust principles and whether or not the essence of the common law trust has a firm hold throughout the region.

Inevitably, some of the additional issues raised in my speech have been covered before in previous OPQs. Taxes is one and readers of my speech might detect a whiff of bureaucratic hypocrisy regarding them. It brings to mind Ferdinand Mount, the author and intellectual, who had this to say about the late political philosopher Michael Oakeshott: "What does Oakeshott teach us then? Well, I think that as a general rule there are no general rules, and therefore that we should pay close attention to the particular rules of the game we happen to be playing." Taxes certainly appear to qualify.

The remaining content of the newsletter, except for those words in brackets, is taken from my speech.

Taxes, Drugs and Women

In today's environment clashes over trusts and taxes are like hurricanes in the Caribbean: both are inevitable. And what a storm. With its higher profile, Panama's offshore activities have caught the eye of the OECD [Organisation for Economic Co-operation and Development] in relation to the organisation's concerns about fair tax competition world-wide. At this point I am reminded of a

verse from a song about Americans fleeing their country for tropical climes that I heard frequently on the radio in Grand Cayman after I moved there nearly 30 years ago. It went: "Some of them are running from lovers, leaving no forward address. Some of them are running tons of ganja. Some are running from the IRS". The song was written by Mr. Buffett, not the sage of Omaha, but his namesake, Jimmy, the troubadour of Mississippi. Perhaps women and ganja are still strong motives for going offshore, but I wouldn't say that taxes were. Either in Cayman or Panama.

Today 80% of my clientele are concerned with non-tax issues whereas back in the 1970s the same percentage was definitely seeking tax relief. Confidentiality, succession, asset protection and international asset diversification have taken over as priorities for Jimmy Buffet's Americans, not to mention the nationals of other countries.

The OECD's list of tax havens, as we know, contains over 30 jurisdictions and only 3 of these have not given undertakings to co-operate long-term with the harmonisation of international tax policies. The rebels are Monaco, Andorra and Liechtenstein – the latter having been in the spotlight in recent months following the fall-out with Germany over its secrecy laws. The Crown Prince of Liechtenstein argues that it's about culture and not collection of taxes and that privacy is there for those who place a high value on it. This is a debate to which the perpetuity rule [a rule barring trusts from being perpetual] definitely does not apply.

The whole OECD tax harmonisation exercise, however, has succumbed to self-interest and contradictory signals which has made both real progress and the work of the OECD's Global Forum on Taxation very difficult.

Panama, for its part, however, objects to being lumped in with what, for want of a better description, it sees as manufactured tax havens. By comparison, Panama's economic development as well as its tax laws are, to quote the government: "a consequence of history and not of initiatives to help evade taxes in other parts of the world". Panama has assured the OECD that it will continue in good faith as a member of the Global Forum but it has also said that its willingness to co-operate will not come at the expense of relinquishing its sovereign right to conduct its international agenda as it pleases. The government has also said that if, at the end of the day, even-handedness is not applied to all jurisdictions, then the conditions will not exist, and I quote, "in order to develop effective commitments between the OECD and Panama".

Even-handedness presents a problem when we take into account the rebel Gang of 3 already mentioned and the fact that 3 OECD members, Austria, Luxembourg and Switzerland, have bank secrecy laws. Austria, a member also of the European Union, has them enshrined in its constitution. And don't forget the very tight bank secrecy laws in Cypress and Singapore.

Panama's territorial tax system harks back to a time long before so-called tailored tax havens existed. The country has never focused on traditional offshore financial services for revenue any more than it has, until recent times, on tourism; more than half the banking business today is domestic and although traditional offshore banking and related services make their contribution, one that is growing, they are not the economy's driving force. Its economic success, unlike some of its Caribbean counterparts, has not been dependent on the attraction of beaches and bank accounts.

Personally, and perhaps not the majority view, I would like to see Panama remain a minor IFC [International Financial Centre] and continue its economic growth with a blend of canal-related and commercial banking business plus associated services such as corporate and fiduciary management. The bright lights of success in offshore services can have a downside, as the Crown Prince of Liechtenstein can attest to.

Cannons and Capitalism

Trusts in Panama, however, like tamales, have a distinct flavour. I remember many years ago, a South American telling me that the Latin American equivalent of the trust was the bearer share. And certainly bearer shares remain popular in the region, despite their oft-quoted sinister connotations. Transferring ownership upon demise as easily as you would the bearer bank note in your pocket is very attractive but for me the basic question raised by bearer shares is this: how secure is the chain of control between death and onward delivery?

A trust law was passed in Colombia in 1923 and Panama quickly followed suit in 1925. The 1925

law was replaced by a new one in 1984 which has since been amended to streamline some procedures. But blending this offspring of English equity with a civil law system, such as the one Panama has, was never going to be easy. And certainly Francis Maitland's [the British 19th century legal historian] version of a trust found itself an interloper confronting a legal system brought from Spain by the conquistadores.

The Swiss, on the other hand, have put out the welcome mat for trusts and then appear to have dealt with them in their midst by having their governing law situated elsewhere, such as the Channel Islands, displaying Switzerland's traditional stance of neutrality when conflict arises.

How then, did the trust get here? Simply put, the driving force was competition, rather than coercion. In an effort to lure capital, principally from the United States of America, it was considered necessary to offer investment vehicles, such as trusts, that Americans frequently used and were very familiar with. Trade and investment were the spur, so it was the power of capitalism and not, as in southern Africa, the cannon [British domination] that brought about the fideicomiso, which is the Spanish translation of the Latin word fideicommissum, and is the closest translation one gets for the word "trust" in Spanish.

It is not surprising that Panama's own trust law should follow fast on the heels of Colombia's because of the American presence here, referred to earlier. Not only did America complete the canal, it then controlled it right up to midnight on 31st December, 1999, when it was handed over to the Panamanians along with the immediate surrounding land known as the Canal Zone. America had exercised sovereignty over the Zone and ordinary Panamanians were denied access. Senator John McCain, the Republican Senator running for President, was born in the Zone without any subsequent negative effect on his status as a US citizen. The Zone really was a piece of America and nothing proves it better than that.

Further study of the commercial motive behind the fideicomiso reveals how in Latin America it has traditionally been used for business rather than family purposes with banks or financial institutions often managing commercial investment funds. In Mexico, for instance, only banks can act as trustees and the law prohibits the trustee from being a beneficiary of the trust. The trust, in other words, is seen as a practical, financial investment vehicle.

Last year in a STEP Journal article I suggested that although Panama does have trust legislation, I believe that any sudden surge of trust business in the future would be confronted with library shelves containing few trust legal precedents. This will change over time and especially as more international business takes place with foreign trustees who begin to use Panama more frequently. STEP has a key role to play in this. Besides STEP, Panama already has very strong business ties with the UK, home of the trust. Britain is the country's largest investor and there is even a Panama British Business Association for which I serve as Treasurer.

Speaking of poorly stocked library shelves, the same precedent problem applies to foundations set up in those common law offshore jurisdictions which have now incorporated them into their legislation as part of a drive to be all things to all men.

But let me say at this point that when the Panamanians passed a foundation law in 1995, like the title of a John Lennon book, it threw a Spaniard in the works. As it happens, a rather appropriate term in this case because the foundation concept is something the conquering conquistadores, who brought their laws with them, would have understood.

Understandably, therefore, this civil law creature has found more regional favour than the trust. Reluctantly, and whilst appreciating that my view may be contentious, I can see, even as a trust aficionado, why the Panamanian foundation with its codified, simplified and straightforward law could present real competition for its Anglo-Saxon cousin. In many ways it evokes a time when trusts and the rules surrounding them were less complex.

Hard to Swallow

But despite everything, the fideicomiso and England's marvellous idea have much in common and all of my remarks should be seen as complementing those of Dr. Aleman who spoke to you yesterday. In either case, and in simple terms, a bond is created between the giver and the receiver for the benefit of someone else. Civil law has the principle of unjust enrichment and common law has equity. The principles of equity,

as we know, were first applied by a Chancellor who was more often a clergyman of high rank who followed the procedures of the ecclesiastical courts. He reached his conclusions by exercising his moral conscience and put aside legal rules and decisions. The decisions were more influenced by common sense than common law. Herein lies the key and the connection between unjust enrichment, equity and trusts.

If equity concerns matters of conscience then unjust enrichment sits comfortably alongside it. In fact, it was Lord Wright in the English case of Fibrosa Spolka Akcyjna v. Fairbairn Lawson Combe Barbour Ltd. who recognised this, and I quote the judge's words: "any civilised system of law is bound to provide remedies for cases of what has been called unjust enrichment or unjust benefit, that is to prevent a man from retaining the money of or some benefit derived from another which it is against conscience that he should keep". Unquote.

Just in April we had a high profile example of this philosophy when the European Court of Justice delivered a judgement based on the principle of unjust enrichment but in a case involving a British plaintiff and British defendant. The court ruled that Her Majesty's Revenue and Customs should refund some 3.5 million pounds in VAT overpaid by the British company, Marks & Spencer, on the sale of chocolate teacakes. [The decision, if not the cakes, must have been hard to swallow for the tax collectors] but one thing is for sure: the outcome did, indeed, prove to be sweet revenge for M&S.

I have been at home in either the civil or common law systems as a trustee because whether it's trusts, fideicomisos or foundations the common denominator is the word fiduciary and its application. So English equity and civil law may be awkward bedfellows but there is no reason why Panamanian and foreign practitioners cannot share a mutual understanding, if not a language, in the case of trusts and fideicomisos. I have called this the Casablanca Rule because the fundamental things apply as time goes by or as Seneca the Elder, centuries ago, so wisely put it: "certain laws have not been written but they are more fixed than all the written laws."

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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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