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Client Memorandum

'All the better to get the facts. I just want to get the facts, ma'am.' **Sgt Joe Friday, Dragnet**

An investigation of the Cayman Islands' International Cooperation Regime

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Of the offshore financial centres, the Cayman Islands has the longest history of cooperation with international law enforcement, regulatory and tax authorities. The startpoint can be dated to the 1970's, at the very origin of Cayman's emergence as a financial services centre.

Exhibit One routinely but perversely cited by the high tax anti-capitalist movement in the bank secrecy hall of horrors, is invariably the *Confidential Relationships (Preservation) Law*. Proof positive, it has been claimed, of Cayman's obsessive and impenetrable secrecy. Really ? Has anyone read it ? Apart from the fact that the absence of bank secrecy would be the real anomaly (see more below), the Law's enactment in 1976 was a direct reaction to the US authorities' strategy of arresting Cayman Islands professionals at US immigration.

While the Law did indeed put common law, or *Tournier*, confidentiality on a statutory basis and criminalise its breach, as important, from the legislature's perspective, was the establishment of defined gateways for disclosure of confidential information, utilization of which was authorised. These gateways were specifically referable to Cayman's understanding, ever pragmatic, that it would need to retain the ability to cooperate, in a rules-based manner, with foreign law enforcement and regulatory authorities. The Hansard is instructive – this, from the mover of the Bill, the Hon. V.G. Johnson, then Financial Secretary:

'…the financial operation [i.e. the financial service sector] *is something that is fully supported by Government because it is today a big part of the economy and as such it should be safeguarded. But in the same token [sic], the Government is also very concerned that we do not preserve criminals in the operation and there should always be the mechanics in whatever system of confidentiality provided to deal with dishonest operations.'*

Indeed, the Bill was referred to London and, via the Embassy in DC, to US authorities, out of a concern that the proposed legislation be construed as appropriately protective and not provocative. It was the prevailing view of the House, fortified by feedback from London, that the Law struck the necessary balance and it thus passed.[1] Even so, the Law was amended in 1979 to include two more disclosure provisions: an articulated Grand Court gateway and recognition of lawful channels for divulging confidential information in accordance with the terms of other legislation – of which there proceeded to be, not to put too fine a point on it, a lot.

[1] Interestingly, the Law was not well received by Cayman's legal fraternity, who objected to being covered by it and further had issues with drafting aspects – largely addressed by the government in a series of amendments during passage. In high dudgeon and sympathy with the Law Society, the Second Elected Member for Bodden Town, G. Haig Bodden proclaimed in theatrical fashion: *'…I think that coming down to the close of the life of this legislature* [general elections were imminent] *that it has produced on its dying bed the worst piece of legislation to come before this House.'*

Subsequent judicial comprehension of the *Confidential Relationships (Preservation) Law* was consistent. As the Jamaica Court of Appeal in *Re Carver* observed, quoted with concurrence by the US Court of Appeals, 11th Circuit, in its 1984 judgement in *In re Grand Jury Proceedings the Bank of Nova Scotia*:

'*It would therefore appear that the policy of the legislature is that the Confidentiality Laws of the Cayman Islands should not be used as a blanket device to encourage or foster criminal activities….[T]here is nothing in the statute* [i.e. the Confidential Relationships (Preservation Law)] *to suggest that it is the public policy of the Cayman Islands to permit a person to launder the proceeds of crime in the Cayman Islands, secure from detection and punishment.'*

So much for the original sin. As no-one has ever been prosecuted under the Law and its primary application has been information disclosure, the practical impact of the recently announced repeal and replacement with a *Confidential Information Disclosure Law* is the transparency equivalent to a bulldog repealing its tail.

Next up was *The Evidence (Proceedings in Other Jurisdictions) (Cayman Islands) Order, 1978*, which came into force in 1980. This gave effect to the 1970 *Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters*, ratified by the UK in 1975 and extended to the Cayman Islands by the 1978 Order. The Order, which remains in force, applies to both civil and criminal proceedings and enables the provision of documentary and other forms of evidence to requesting foreign courts or tribunals.

The environment that lead to the enactment of the *Confidential Relationships (Preservation) Law* also produced in 1982 the so-called 'Gentlemen's Agreement' (an optimistic description, as it turned out) which attempted to establish a procedure to be followed by US law enforcement authorities in obtaining information from the Cayman Islands. The respective approaches to the Agreement were asymmetric: the US regarded it as informal, non-binding and experimental and in fact never confirmed it, whereas Cayman took the opposite position. This was hardly a satisfactory state of affairs for either party and so the US on the one side and the UK and Cayman on the other continued to work on a negotiated solution.

This produced, two years later, a formal agreement by way of an Exchange of Letters (colloquially known as 'the Narco Agreement') between the UK Secretary of State for Foreign and Commonwealth Affairs and the US Ambassador in London, on law enforcement assistance from the Cayman Islands in relation to narcotics activity, pursuant to the *UN Single Convention on Narcotics Drugs, 1961*. This 1984 agreement was implemented in Cayman via the *Narcotics Drugs (Evidence) (United States of America) Law, 1984*, and afforded US prosecutorial authorities full access to information and testimony from the Cayman Islands for the purposes of the US prosecution of narcotics offences or connected ancillary civil or administrative proceedings. While the Agreement was somewhat lop-sided in favour of the US, it did include, in Article 6, a circumscription on the US' use of unilateral measures, which had been a source of friction.[2]

This cooperation channel was evidently highly effective: In a 1986 speech to the American Bar Association, the then UK attorney-general, Sir Michael Havers, reported that evidence secured via the Narco Agreement had been instrumental to the success of major US federal investigations and prosecutions in relation to drug trafficking.[3]

The 1984 agreement expressed the intention of the parties to progress in short order to a full-blown law enforcement treaty. This duly led to the 1986 Mutual Legal Assistance Treaty (the first with a Caribbean jurisdiction; ratified by the US in 1990 by a Senate vote of 99-0; 1 senator absent), and the implementing *Mutual Legal Assistance (United States of America) Law, 1986* (MLAT Law), which replaced the 1984 precursors and likewise afforded full access to information but in to addition a wide array of other forms of assistance, and for a much-expanded range of criminal offences – in fact any punishable by more than

[2] See W.C. Gilmore, *Mutual Assistance in Criminal and Business Regulatory Matters*, Cambridge University Press, 1995.
[3] Ibid

one year's imprisonment under the laws of both jurisdictions -- and the specifically imprinted offences of racketeering, narcotics trafficking, insider trading, fraudulent securities practices and foreign corrupt practices. Tax offences were expressly excluded, except in relation to the promotion of fraudulent tax shelters and the submission of false income tax returns with respect to unlawful proceeds of the criminal offences covered by the treaty. In the attendant Washington Post story *'Cayman Islands Gives U.S. Access to Bank Records'*, Cayman's Governor Peter Lloyd was quoted as stating that the treaty was *'a sign to the world that the offshore outlaw has no home in the Cayman Islands'* while Cayman would remain protective of legitimate privacy.[4] The treaty is still very much in force and remains the primary cooperation channel for US law enforcement authorities for non-tax matters, averaging about 13 US assistance requests per annum since 1990.

Next enacted was the *Misuse of Drugs (international Cooperation) Order 1991* under which, starting with the UK and then expanding in 1998 to all Vienna Convention countries, Cayman was able to assist international law enforcement authorities in relation to restraint and confiscation orders in narcotics matters.

The 1988 *UN Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances* (known as the 'Vienna Convention'), extended to Cayman by the UK in February 1995, ushered in further upgrades to Cayman's international cooperation regime, via two new laws. The *Proceeds of Criminal Conduct Law, 1996* [5] established Cayman's 'all-crimes' anti-money laundering regime including comprehensive know-your-customer and suspicious activity reporting requirements and for the purposes of international cooperation, corresponding capacity to restrain and/or confiscate criminal proceeds. The *Misuse of Drugs (International Cooperation) Law, 1997* (MDICL) enabled the Cayman Islands to provide wide-ranging legal assistance, including the provision of information, in relation to money laundering and other criminal drugs matters, to the 146 Vienna Convention countries. In 2004, the MDICL was replaced by the *Criminal Justice (International Cooperation) Law* (CJICL), which expanded the regime to include assistance at the investigative stages for non-drug offences (excluding tax offences) in addition to drug offences. The Office of the Director of Public Prosecutions reports that the CJICL is now the main avenue of assistance to foreign law enforcement authorities.

It is topical to note specifically that Cayman's international cooperation regime has long been able to handle corruption matters, because the offence's inclusion under Cayman's domestic Penal Code brought it within the ambit of the existing cooperation channels by operation of the dual criminality principle.[6] Further, In 2008, Cayman introduced the *Anti-Corruption Law* which replaced the Penal Code provisions and gave effect to the 2003 *UN Convention Against Corruption* (extension by the UK to Cayman requested and pending) and the 1997 *OECD Convention on Combatting Bribery of Foreign Public Officials in International Business Transactions* (extended to Cayman by the UK in 2010). The *Proceeds of Crime Law, 2008*, in support, enhanced Cayman's abilities to issue provisional restraint orders in aid of foreign law enforcement authorities, often important in the particular circumstances of corruption cases.

On the regulatory side, regulation of Cayman's diverse financial services sector was consolidated under the Cayman Islands Monetary Authority, established by eponymous law in 1996 as an independent regulator. The law was significantly upgraded in 2000 by the *Monetary Authority*

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[4] See Ilene Katz Kobert and Jonathan D. Yellin, *The United States Treaty with the United Kingdom Concerning the Cayman Islands and the Mutual Legal Assistance in Criminal Matters: The End of Another Tax Haven*, 19 U. Miami Inter-Am.L. Rev 663 (1988). A revealing title.

[5] Now the Proceeds of Crime Law, 2008. By virtue of the 1996 law, Cayman was the first regionally and among the first worldwide to criminalise money-laundering on an 'all-crimes' basis i.e. on basis of all serious crimes, not limited to narcotics offences.

[6] Note that 'foreign corrupt practices' was one of the imprinted offences covered by the 1986 MLAT with the US. Notable cross-border corruption cases in which the Cayman courts have provided assistance include the expeditious restraint and return of: i) US$40m defrauded from the Chilean state-owned copper conglomerate by an employee (*In Re Codelco*, 1999 CILR 42); ii) over US$30m defrauded from the Kuwaiti Investment Authority by a director (*In Re Al Sabah,* 2002 CILR 148); and iii) US$44m to the Peruvian government, being corruption proceeds from activities of the then head of the Peruvian National Intelligence Service (pursuant to letter of request from Peruvian Court).

(Amendment)(International Cooperation) Law to make cooperation with overseas regulatory authorities an express function of the Authority and to give it the powers and competencies to do so – including powers to obtain information from any relevant person and provide it to a requesting overseas counterpart to enable it to exercise its regulatory functions including associated enforcement actions. The provisions related to the international cooperative function were further refined in 2002 and 2007. Since 2000, the Authority has handled over 1900 such requests for assistance.[7]

But what then of cooperation in tax matters. Is there any truth here to the allegations of 'secrecy' ? Cayman's historic position in relation to international cooperation on tax matters was the product of two well-recognised international legal principles: dual criminality and the 'revenue rule' (both tied to the concept of state sovereignty). The dual criminality principle requires that international cooperation in criminal matters be based on the subject offence being an offence in both the requesting and the requested jurisdiction; in Cayman's case, having no direct taxes, it would thus not have an offence of evasion of such taxes. The revenue rule, as manifest in a centuries-long line of English cases and reflected in the commonly cited 1955 House of Lords case *Government of India v Taylor*, is that countries do not, outside of specific treaty arrangements, assist foreign governments either directly or indirectly, in the enforcement of revenue measures.

Thus the Cayman position was consistent with international standards. However, in 1998 the OECD launched its maladroitly named *'Harmful Tax Competition: An Emerging Global Issue.'* Notwithstanding the pejorative branding of competition, the OECD initiative was successful in relation to 'tax havens', as defined, *inter alia*, by a lack of effective exchange of information on tax matters.[8] Cayman perceived this as a markedly hostile change in climate as opposed to passing weather and responded accordingly.

In May 2000, therefore, the Cayman Islands was one six countries which gave an 'advance commitment' to the OECD on transparency and exchange of information on tax matters, under the auspices of the OECD campaign to promote new international standards in that area.[9] Specific note was taken of the OECD's member country survey/report published in the same year, *Improving Access to Bank Information for Tax Purposes*, which stated that *'[b]ank secrecy* (sic) *is widely recognised as playing a legitimate role in protecting the confidentiality of the financial affairs of individuals and legal entities..;'* and '...*a fundamental requirement of any sound banking system.'* So not a bug then, but a feature, as they say.

The same OECD report supplied empirical confirmation that Cayman was not a rogue actor but was in fact operating within the prevailing OECD norms: all OECD states had bank secrecy provisions, in the vast majority by express legislation, and only exchanged information on tax matters in the context of a treaty – typically, the OECD model double taxation agreement (DTA) – and, somewhat ironically, strong confidentiality protections for any information exchanged. In the circumstances, the orchestrated outrage directed at Cayman and indeed other offshore financial centres which happen to be small islands for 'bank secrecy', was and continues to be, arbitrary and discriminatory.

Being an advance commitment country helped secure Cayman the seat at the table it wanted in the development of the new standards. Cayman was one of eleven non-OECD participants which together with the key OECD member states developed the 2002 OECD model agreement for on-request exchange of information in tax matters.[10] In the process Cayman, in concert with a number of other jurisdictions,

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[7] Cayman Islands Fact Sheet, Ministry for Financial Services.

[8] In a sort of Catch-22, under the OECD rubric, to be allowed to be a 'tax haven', you had to comply with the new OECD regime, but if you complied with the new OECD regime, you would no longer be a 'tax haven'.

[9] In doing so, Cayman avoided blacklisting, the cosh of choice for the bona fide marauding multinational horde. Not long after the launch of the harmful tax competition initiative, the leader of the charge, Fran Horner, became Sister Francis Celine of the Holy Spirit, having joined a Carmelite Order in the US. To date OECD protagonists Jeffery Owens and Pascal Saint-Amans have not.

[10] The model itself represented the treaty exception under the revenue rule and Article 5 thereof deals with the dual criminality principle by setting it aside – or in any event, an ultra- strict - equivalence construction of it. While Cayman does not have an offence of income tax evasion. It does have, for example, a common law offence of defrauding the revenue.

successfully pushed the case for a level playing field in implementation -- an argument that, to the OECD's great discomfiture, gained considerable traction from the glaring fact that OECD member states Switzerland and Luxembourg had publicly declined at the time to participate in what were, in their view, dangerously unpleasant exchange of information exertions.

Cayman proceeded to implement an exchange of information regime for cooperation in tax matters by negotiating a series of bilateral tax information exchange agreements (TIEAs) based on the OECD model, beginning with its major trading partner in financial services, the US, in 2001 (in force for criminal tax matters from 2004 and for other tax matters from 2006) and introducing the *Tax Information Authority Law, 2005* which established the actual cooperation mechanism, based on the successful MLAT framework.[11] Cayman now has entered into 36 such bilaterals, covering all major trading partners, and negotiations are pending with 15 additional countries.[12] For the period 2009 – 2015, Cayman dealt with 185 requests under its TIEAs.

Also in 2005, Cayman introduced the *Reporting of Savings Income Information (European Union) Law*, which provided for automatic reporting of savings income held in the Cayman Islands and beneficially owned by EU residents from the 27 (now 28) EU member states, in accordance with agreements executed between the Cayman Islands and each EU member state.

In the next significant developments regarding Cayman's international cooperation in tax matters, in 2013, Cayman entered into (impressively labyrinthine) agreements with the US and the UK (the 'FATCA' agreements) for the automatic provision of information and enacted corresponding implementing legislation. The US' success in rolling out FATCA gave a boost to the OECD's own automatic exchange of information project, the Common Reporting Standard (CRS), which it duly released in 2014 as the global standard (with genuflections towards the US' unilateral activity). In 2014, Cayman along with 50 other countries committed as an early adopter to the CRS, which now covers over 100 participating jurisdictions, and became a party to the Convention on Mutual Administrative Assistance in Tax Matters.[13] Cayman's corresponding implementation legislation followed in 2015.

The *Confidential Relationships (Preservation) Law, 1976* ushered in a sustained period of constructive engagement on evolving cross-border issues in financial services and progressive reinforcement of Cayman's international cooperation regime, across law enforcement, regulatory and ultimately tax matters. As a result, Cayman has a fully articulated and effective international cooperation regime that is compliant with international standards – in relation to which Cayman has frequently been a leader, despite the Sisyphean nature of the task.

Precisely none of Cayman's international cooperation channels are frustrated by so-called 'bank secrecy' or absence of information. And we don't just say this -- the IMF in 2005, the CFATF in 2007 and the OECD in 2012 have said this in the course of formal and published external assessments of Cayman's regulatory, AML/CFT and tax exchange of information regimes respectively. The US authorities have identified Cayman as 'one of our best partners' among offshore jurisdictions.'[14] Quoting from the executive summary of the most recent of the external assessments, the OECD Phase 2 Peer Review Report, in which Cayman achieved ratings of 'compliant' or 'largely compliant' against the 10 assessment criteria: *'Overall, the feedback from peers was positive and some* [exchange of information] *partners of*

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[11] The US Department of Justice had been attempting to negotiate the full inclusion of tax offences under the MLAT and was reportedly not amused when the US Treasury swooped in and secured a TIEA. From Cayman's perspective (which, it must be confessed, did feature privately a certain degree of amusement over the alleged internecine dust-up), the TIEA represented the global standard and ticked a number of policy boxes that the DoJ formulation did not.

[12] 29 of the bilaterals are in force. Among them are 'mini-DTAs' secured from the Nordic Group (Denmark, Norway, Sweden, the Faroe Islands and Greenland) and the UK. It is not clear whether the 15 pending negotiations will be overtaken by the CRS.

[13] For the record, the UK Secretary of State for Foreign Affairs entered two reservations on behalf of the Cayman Islands, being that Cayman would not provide i) assistance in the recovery of tax claims or of administrative fines or ii) any form of assistance in relation to 'non-Federal' taxes.

[14] Cited in US Government Accountability Office's 2008 report on the Cayman Islands for the US Senate Committee on Finance (GAO-08-778)

the Cayman Islands praised its clear and coherent communications during the course of a request as well as the quality of its cooperation and speed in response times.'

The persistent braying from extreme left wing high tax anti-capitalist NGOs about 'secretive tax havens' as somehow vectors of mass economic destruction that must be exterminated can, as against reality, be appropriately regarded as superstitious, fact-impoverished and not un-deranged. Better the foundation of The Dalek School of Foreign Relations than a sensible basis for global policy.

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