ANGUILLA FINANCIAL SERVICES COMMISSION

ANNUAL REPORT 2013

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CHAIRMAN'S REPORT

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Chairman of the Board of Directors

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It is an interesting thing to reflect on a year that has passed. One gains the benefit of hindsight and can re-evaluate decisions made with the luxury of knowing how things ultimately turned out. Sometimes, outcomes take longer than just a year or two to emerge, sometimes decades.

Way back, when Anguilla decided to establish itself as what, in those days, was called an "offshore centre" and these days is termed "international financial centre," phrases such as "nominee director," "booking centre," "brass plate," "shelf company" and "shell company," were commonplace internationally used terms. Company formation agents in onshore and offshore jurisdictions circulated lists of aged companies, charging more for companies with 2 or 3 years of audited accounts, more for those with interesting names - words like "International" or "Global", "Insurance" or best of all "Bank". Good jurisdictions, like Anguilla, shied away from these names requiring evidence (such as a banking licence) to justify consenting to names which contained certain words. Some jurisdictions did not even require a company name to include words that indicated it was a company – e.g. no "Limited" or equivalent – so one could have a confusing situation where a bank account in the name of "John Smith" was actually an account for a company named "John Smith" and that company was actually owned by Fred Jones. Who would know? We are talking about practices pre anti money laundering standards, now a long time ago, decades ago.

In those days there was little mutual legal assistance between jurisdictions and most countries, onshore or offshore, required fairly tight grounds to be met before they could extend co-operation in criminal matters. However, the drafting of the grounds – the way the law worked - left offshore jurisdictions in effect being seen as pockets of secrecy. No secrecy laws needed to have been actively enacted, it was just the way things shook down.

Take a scenario where Country A had victims of, say, an investment fraud. The fraudster might also live in Country A or if he was rather more sophisticated, would live in Country B. The fraudster formed an offshore company in Country C of which he, secretly, was beneficial owner, but the company was "fronted" by dummy directors resident in Country D. He held out to his victims that he worked for an exciting offshore investment firm that gave great service and good returns, typically his card would name him as "Investment Advisor", or "Client Relationship Manager".

In those days most onshore countries had less developed tax regimes than today, and if tax paid money was placed offshore and income earned offshore, the pot and its growth did not owe tax onshore until or unless it was repatriated to the home state. This gave people the opportunity to have an offshore "nest egg" and was attractive to many, in these days before the now common principle of being taxed on worldwide income.

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Were these soon-to-be-duped investors stupid and greedy? Before explaining how the fraud took place, let us take a moment to remember the UK tax regimes of the day.

It is unimaginable today, but in 1971 a welcome measure was introduced in the UK CUTTING the top rate of income tax on earned income to 75%. On top of that a surcharge of 15% kept the top rate on investment income at 90%. In 1974 the rate went back up to 83%. With the investment income surcharge, this raised the top rate on investment income to 98%, the highest permanent rate since the war. This applied to incomes over £20,000 (equivalent to £186,150 as of 2015). In 1974, 750,000 people were liable to pay the top-rate of income tax.

Margaret Thatcher reduced personal income tax rates during the 1980s. In the first budget after her election victory in 1979, the top rate was reduced from 83% to 60% and the basic rate from 33% to 30%. The basic rate was also cut for three successive budgets - to 29% in the 1986 budget, 27% in 1987 and to 25% in 1988. The top rate of income tax was cut to 40% in the 1988 budget. The investment income surcharge was not abolished until 1985.

This is the backdrop to the era when international financial centres like Anguilla were designing their economic model. It made sense to set up as a company incorporation centre. Lots of business was to be won helping people lawfully shelter their assets against ferocious domestic tax regimes. It was a business with a low local foot print, needing few staff beyond the companies registry, and one which potentially delivered high Government revenues.

However, back to the scenario. Hiding among the legitimate clients, some clients were not so benign. The fraudster in our scenario would painstakingly tell potential investors that they must make their cheque out to the company and post it along with an application form direct to the offshore jurisdiction. They faithfully followed instructions, wholly unaware that he was the beneficial owner. If they were wise investors they might do a company search: they typically received a certificate of good standing and would not be able to discover the names and addresses of directors or shareholders as these were not (and still are not) publicly listed, much less could they (nor can they) discover the name of the beneficial owner. Indeed it would not occur to most onshore investors that the beneficial owner could be someone other than the listed shareholder.

So, holding a certificate of good standing, they dutifully posted their money away. It would be received at the company administrator's office and staff would either pay it into the bank account which they opened and ran for the beneficial owner to which they or he would typically be signatories, or post the cheque to him back in country A or B. Using his own signatory powers under a power of attorney or his powers to instruct his administrator, the beneficial owner of the company (in this scenario, the fraudster), would arrange for the monies to be paid to another account. It is stolen as simply as that. The investors of course soon start to write to the registered office, they complain, they get a local lawyer. No one can lift the corporate veil and find out who the beneficial owner is. Finally, they contact the police.

Now came an interesting issue. In the old days, as stated earlier, international co operation in criminal matters was limited. Most jurisdictions required reciprocity and often dual criminality, most police forces needed some element of local standing before launching an investigation. Typical local standing could be that:-

a) complainants were nationals of or resident in the jurisdiction. In our scenario, the victims were onshore investors.

b) the perpetrator was a national of or resident in the jurisdiction. In our scenario, the "perp" was all onshore.

c) the offence was committed in the jurisdiction. In our scenario, the offence is fraud, and it happened

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onshore.
So the old models which triggered international co-operation were seldom met in cases where the only link with the offshore jurisdiction was that it held key evidence linking the perpetrator with the crime.

Time has moved on and one might wonder why these topics merit space in a regulatory annual report now, decades later.

The reason is fundamental to Anguilla's future economic success.

Although the regulatory, law enforcement and international tax frameworks have moved on, the fundamental services provided by Anguilla's finance industry have not. The predominant activity is still the incorporation of offshore companies; the role of the local service provider is still predominantly that of a registered agent providing in practice little more than a registered office.

Most Anguillian companies are formed by or for overseas incorporators, with few Anguillian businesses having direct relationships with the beneficial owner.

The Anguillian businesses which are forming companies themselves make only a small margin on top of the cost of incorporation. Where they are acting as a registered agent, the fee they are paid is insignificant compared to the liability they incur under current anti-money laundering requirements.

Historically, a small margin might have been disappointing but it was still a fee which pretty much represented pure profit. Today however – and indeed since the introduction of the Proceeds of Crime Act (POCA) in 2009 – Anguillian businesses have had an obligation to comply with "Know Your Customer" standards, the cost of which exceeds the profit margin of many of these firms. This results in a product which is non-economic. The core offering – the sale of non-resident companies on a registered agent/registered office only business model – is not viable in the modern world. The cost of due diligence is greater than the profit margin.

It is essential that Anguillian financial services businesses develop added value services (full administration, book keeping, accounting, provision of professional directors, nominee shareholders, company secretary, etc) to raise their income in a manner that generates sufficient income to fulfil their obligations and manage their risks. In particular they must be able financially to undertake the due diligence and monitoring required by POCA, while holding sufficient information to enable them to render the beneficial owner compliant in terms of his own tax obligations. The tax standards of the world are increasingly requiring that control of a company is evidenced to have been located in a particular jurisdiction before allowing that jurisdiction to be recognised as its tax residency. In addition to whether the client structure is compliant with the new standards, without detailed knowledge and records of the assets held within the company, the capital and interest accumulating, the distributions made, etc., the Anguillian business will have great difficulty in reporting the correct tax related information under the various tax initiatives – including FATCA, GATCA, Common Reporting Standards and a full suite of Tax Information Exchange Agreements, all now, or soon to be, in force. Failure to report these properly in some cases brings the Anguillian business itself into non-compliance, not only the tax payer himself.

Ultimately, Anguilla's key risks arise from operating the very low footprint model originally designed and identified as attractive. The risk is that the habit of running corporate service provider businesses which provide clients very little by way of real presence, local control, record keeping, etc., results in the island being associated with hiding the identity and affairs of beneficial owners and the follow through reputational damage.

The model needs to change. Business must reinvent itself, find new products and services and in the meantime comply with the legislation in force.