

The Panama factor: offshore investment in an era of unprecedented tax transparency



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Offshore centres should be more proactive in presenting their case to the public, the Legal Week Offshore Investment Forum heard

The Panama papers featured heavily during *Legal Week's* inaugural Offshore Investment Forum in London.

Delegates at the half-day event, which was held at the Sofitel London St James, agreed that the drive for transparency and the exchange of information between offshore and onshore

tax authorities would only intensify in the aftermath of the leak of 11.5 million files from Panama law firm Mossack Fonseca.

But there were also calls for the offshore centres to be more proactive in presenting their case to the public.

Ross Webber (*pictured above*), chief executive of the Bermuda Development Agency, said the Panama papers controversy presents Bermuda with: "An opportunity to differentiate ourselves from those jurisdictions that can't claim our longstanding, blue-chip record of transparency and compliance; an opportunity to explain the basic economics of globalisation; and an opportunity to clarify that our regulatory and business ecosystem is pragmatic and appropriate."

He was also keen to point out that several of his "jurisdictional cousins" might apply the same approach.

Attended by funds specialists, lawyers from international law firms and general counsel, the forum addressed a broad range of issues including funds regimes in different jurisdictions, the growth of insurance-linked securities, the impact of increased regulation and the effects of global tax transparency.

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Stephen Sims, who heads the European investment management group at Skadden Arps Slate Meagher & Flom, said one of the continuing attractions of offshore centres was that "the legislators listen". He added: "The regulators are very approachable, you can get hold of them and get an answer."

He said speed was also a factor. "How long does it take to get regulated as a manager in the UK at the moment? Many months," he continued. "There are fast-track procedures in a number of offshore jurisdictions, where it takes only a couple of weeks for the due diligence to be completed."

Elizabeth Denman (*pictured below*), a Bermuda-based director at Conyers Dill & Pearman, highlighted the transatlantic tension between flexibility and regulation: the "quick and

snappy" US model of regulation, versus the European model, "which is becoming increasingly regulated". She added: "The offshore centres have to decide how to be all things to all people."

On the issue of privacy, she pointed to peer reviews undertaken by the Organisation for Economic Co-operation and Development (OECD), in which the British offshore dependent territories scored very high marks for having robust and transparent systems in place on beneficial ownership.

Meanwhile, there was plenty of evidence that the offshore funds market is continuing to evolve, with insurance-linked securities (ILS) as an asset class coming under the microscope. "In its purest form, an ILS transaction involves creating a fluid vehicle through which the capital markets can access risk," said Greg Wojciechowski, president and chief executive officer of the Bermuda Stock Exchange. "They provide fuel for the reinsurance industry."



The best-known vehicles are catastrophe bonds, or 'cat bonds', which enable institutional investors to invest in insurance companies that face claims from businesses affected by large-scale natural disasters. Simultaneously, risk managers gain insurance coverage and immediate access to capital in the event of claims. Critically, from a regulation viewpoint, the rights of investors are always subordinated to the rights of the cedant or sponsor (the insurance or reinsurance company) under the contract for risk transfer, said London-based Mayer Brown corporate partner Colin Scagell.

A panel discussion followed on private debt funds. Macfarlanes partner Alex Amos highlighted the growth of direct lending funds, which are of increasing appeal to several types of asset manager, including hedge funds. Ajay Pathak, a London-based funds partner at King & Wood Mallesons, said there are two key drivers fueling their growth: the continued pressure on European bank balance sheets has caused a reduction in available lending; and simultaneously there is increased investor appetite, with institutional investors in particular viewing private debt as an asset class in its own right.

On the issue of fund structure and domicile, large US sponsors typically use a combination of Cayman, Delaware and Bermuda jurisdictions, according to Dechert partner Gus Black; however, US managers are increasingly looking at European structures for a parallel European fundraise. Amos concurred, indicating that European sponsors tend to favour the Channel Islands and more recently, Luxembourg, which is attractive because of investor familiarity and its extensive treaty network.

Regulation of direct lending across the jurisdictions of Europe varies widely, according to Black, although there are efforts underway to harmonise the position. Most significant is the Capital Markets Union – a European Commission plan to improve access to capital by mobilising capital flows. Debt funds are seen as part of the solution, with regulator the European Securities and Markets Authority attempting to drive harmonisation. The funds panel agreed that, in principle, and most likely in practice, debt funds will also be subject to Alternative Investment Fund Managers Directive regulation, and hence it is too early to say whether further specific legislation in this area would be helpful.



After examining the origins of global tax transparency, the tax panel discussed how this ideal has gained significant traction since the crisis: first via OECD tax information exchange agreements, which were quickly followed by the US Foreign Account Tax Compliance Act 2010. This, in turn, was a catalyst for 53 countries to agree Automatic Exchange of Information (AEOI), known as the Common Reporting Standard (CRS). In addition, there is the current, and continuous, OECD-led global fight to combat tax evasion and tax avoidance

through the OECD's Base Erosion and Profit Shifting regime. "We are looking at transparency and automatic information exchange on a global scale," said Steven Rees Davies, a corporate partner at Appleby Global.

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Ross Munro, global head of fiduciary at Harneys, said: "In terms of tax transparency, the early adoption of CRS was a very clear signal from the major offshore centres: we are very serious about tackling tax evasion. We don't see AEOI as a problem for the underlying client base."

Although he predicted that AEOI will inevitably add to costs, implementation will also drive fund volume to those offshore centres that have the established expertise to manage the reporting – a relatively small number of international offshore centres.

At the same time, Munro cautioned about a new blacklist agreed by European Union finance ministers, and likely to be announced before the end of the year: "The criteria used to establish any blacklist is critical. In terms of where funds are domiciled in international offshore centres, simply being a tax-neutral jurisdiction with no or low taxation on corporate profits should not be a factor for a jurisdiction being put on a blacklist."

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