The Caribbean – From One Blacklist to the Other

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Introduction

In this article, we describe some of the legacy issues that the Caribbean islands have to deal with in terms of money laundering reputation. Many of them were listed as "uncooperative" by the Financial Action Taskforce. Even though they have been removed from the money laundering black list, several of them are still "countries of primary concern" according to the U.S. State Department. Also, a recent U.S. Senate report and proposed legislation brings another negative label to the fore front: Many Caribbean countries are considered "offshore secrecy jurisdictions" by the IRS. This issue may also have far going implications for banks located in the Caribbean area.

NCTT list

It is now more than eight years ago that the global money laundering watchdog Financial Action Task Force, in an effort to crack down on countries with lax money laundering controls, named and shamed 15 countries on the money laundering "blacklist". According to the FATF these tax and bank secrecy havens and loosely regulated offshore financial centers, have "serious systemic problems" with money laundering controls. It said the countries must "improve their rules and practices as expeditiously as possible" or face revolutionary sanctions that could include restrictions or prohibitions on transactions between their institutions and those in FATF member countries. Of the 15 "non-cooperative" (NCCT) countries included on the initial list of June 2000, five were located in the Caribbean: Bahamas, Cayman Islands, Dominica, St Kitts and Nevis, St Vincent and the Grenadines. Later, in 2002, a sixth Caribbean island, Grenada, was added to the list.

Improvements, but not yet low risk

Because of significant improvements in their AML controls, all Caribbean countries were removed from the NCCT list by the end of 2003. Many Caribbean islands, issued strict Know Your Customer laws, that sometimes go beyond what is required in the European Union and the U.S. Another example is that in 2001, the Central Bank of the Bahamas enacted a physical presence requirement that means "managed banks" (those without a physical presence, only represented by a registered agent such as a lawyer or another bank) must either establish a physical presence in The Bahamas (an office, separate communications links, and a resident director) or cease operations. The transition to full physical presence is complete. Some industry sources have suggested that this requirement has contributed to a decline in banks and trusts in the Bahamas from 301 in 2003 to 139 as of June 30, 2007.

Yet, many financial institutions located in the U.S., Canada and Europe still consider many Caribbean islands as high risk for money laundering. The mere fact that the countries were removed from the NCCT list, the fact that they all have mutual legal assistance treaties, they all criminalized money laundering beyond just drugs, and beefed up their money laundering laws, does not make them low risk in the eyes of many. Limited regulation of offshore sectors, bearer share companies, inadequately regulated economic citizenship programs, and other factors still contribute to some islands' money laundering vulnerabilities.

Let's take a look at several Caribbean jurisdictions, and see where they stand in terms secrecy laws, possibilities for offshore banking and other factors that would make them attractive for drug (and other crime) money managers.

Country	**Ever on NCCT list**	**Egmont FIU**	**Record large trans-actions**	**Secrecy Laws consistent with FATF40**	**Listed as offshore secrecy jurisdictions by the IRS**	**Listed as "country of primary concern" in INCSR**
Antigua and Barbuda	No	Yes	No	Partially compliant	Yes	Yes
Bahamas	Yes	Yes	Yes	Largely compliant	Yes	Yes
Barbados	No	Yes	Yes	Partially compliant	Yes	No
Cayman Islands	Yes	Yes	Yes	Yes	Yes	Yes
Dominica	Yes	Yes	Yes	N/A	Yes	No
Dominican Republic	No	No	Yes	N/A	No	Yes
Grenada	Yes	Yes	No	N/A	Yes	No
Jamaica	No	No	Yes	N/A	No	No
Netherlands Antilles	No	Yes	Yes	N/A	Yes	No
St. Kitts and Nevis	Yes	Yes	Yes	N/A	Yes	No
St. Vincent and the Grenadines	Yes	Yes	Yes	N/A	Yes	No

Trinidad and Tobago	No	No	Yes	Partially compliant	No	No

The sources for the findings in this table are:

- 2007/2008 Financial Action Taskforce Country Reports and Mutual Evaluation Reports
- 2008 International Narcotics Control Strategy Report by the U.S. Department of State
- NCCT (Non Cooperative Countries and Territories) lists issued by the Financial Action Taskforce
- 2007 U.S. Senate Stop Tax Haven Abuse Act

The tax evasion angle

The OECD's list of 35 offshore jurisdictions or its subsequent list of uncooperative tax havens is often consulted by banks around the world to see if a higher "money laundering" country risk should be assigned to a particular country. To avoid being included on the list of 35 offshore jurisdictions, several Caribbean countries, including Bermuda, the Cayman Islands, gave the OECD signed commitment letters in early 2000, promising to provide effective tax information exchange in criminal and civil matters by certain dates.

But…there is another list. Each year, the United States loses an estimated $100 billion in tax revenues due to offshore tax abuses. The U.S. Senate has long had an investigative interest in U.S. taxpayers who use offshore tax havens to hide assets and evade taxes. The Senate has investigated if and to what extent so called "tax haven banks" are assisting U.S. taxpayers to evade taxes, in particular by urging U.S. clients to open accounts abroad, assisting them in structuring those accounts to avoid disclosure to U.S. authorities, and providing financial services in ways that do not alert U.S. authorities to the existence of the foreign accounts. So, the U.S. came up with its own "black list." In the 2007 Stop Tax Haven Abuse Act, introduced by Senator Levin, and Obama, amongst others, many Caribbean countries were listed as "offshore secrecy jurisdictions" (see table above).

However, we have to remember that tax shelters do not only include countries in the Caribbean. Recently, in February and May 2008, several large tax scandals involving Switzerland and Liechtenstein made headlines. The first scandal erupted after a former employee of a Liechtenstein trust company provided tax authorities around the world with data on about 1,400 persons with accounts at LGT Bank in Liechtenstein. The second tax scandal broke when the U.S. arrested a private banker formerly employed by UBS AG on charges of defrauding the U.S. tax authorities (IRS) of more than $7 million in taxes owed on $200 million of assets hidden in offshore accounts in Switzerland and Liechtenstein.

On July 17, 2008, the U.S. Senate Permanent Sub Committee on Investigations held hearings on this topic and issued a 114-page report called "Tax Haven Banks and U.S. Tax Compliance". Although the report mainly focuses on two countries in Europe, namely Switzerland and Liechtenstein, the report also underscores the role of the Caribbean in international tax evasion scandals. In a (real-life, not hypothetical) case described in the report, the U.S. tax evaders had set up Bahamas corporations, which were used to conceal the ownership of assets. In the names of these companies, bank accounts were opened in the Bahamas, Switzerland and other countries. Interestingly, the report shows that –as a result of better tax cooperation between the US and the Bahamas- the accounts were moved from the Caribbean to Switzerland. As a result of the tax treaties Barclays decided in 2001 to close all of its Bahamas accounts with U.S. clients. According to the Senate Report, some account managers located in the Bahamas were trying to get transferred to Switzerland, and move their clients' accounts to the Barclays Swiss office.

Possible implications for Caribbean banks of Stop Tax Haven Abuse Bill

Section 102 of the above described Stop Tax Haven Abuse bill contains an innovative approach to combating tax haven abuses. If approved, this section would build upon existing Treasury authority to apply an array of sanctions to counter specific foreign money laundering threats by extending that same authority to counter specific foreign tax administration threats.

In 2001, the USA Patriot Act gave U.S. Treasury the authority under 31 U.S.C. 5318A to require U.S financial institutions to take special measures with respect to foreign jurisdictions, financial institutions, or transactions found to be of "primary money laundering concern." Once Treasury designates a foreign jurisdiction or financial institution to be of primary money laundering concern, Treasury can impose a range of requirements on U.S. financial institutions in their dealings with the designated entity. For example requiring U.S. financial institutions to provide greater information than normal about transactions involving the designated entity, or even prohibiting U.S. financial institutions from opening accounts for that foreign entity. In some instances Treasury has employed special measures against an entire country, such as Burma, to stop its financial institutions from laundering funds through the U.S. financial system. More often, however, Treasury has used the authority surgically, against a single problem financial institution, to stop laundered funds from entering the United States. The provision has clearly succeeded in giving Treasury a powerful tool to protect the U.S. financial system from money laundering abuses.

The proposed bill would authorize Treasury to use that same tool to require U.S. financial institutions to take the same special measures against foreign jurisdictions or financial institutions found by U.S. Treasury to be "*impeding U.S. tax enforcement.*" Treasury could, for example require U.S. financial institutions that have correspondent accounts for a designated foreign bank to produce information on all of that foreign bank's customers. Or, the U.S. Treasury Department could prohibit U.S. banks or other financial institutions from opening accounts for a designated foreign bank, thereby cutting off that foreign bank's access to the U.S. financial system. These types of sanctions could be as

effective in ending the worst tax haven abuses as they have been in curbing money laundering. In addition to extending Treasury's ability to impose special measures against foreign entities impeding U.S. tax enforcement, the bill would add one new measure to the list of possible sanctions that could be applied to foreign entities: it would allow Treasury to instruct U.S. financial institutions not to authorize or accept credit card transactions involving the designated foreign jurisdiction or financial institution. Denying tax haven banks the ability to issue credit cards for use in the United States, for example, would be a powerful new way to stop U.S. tax cheats from obtaining access to funds hidden offshore, including in the Caribbean.

Conclusion

Multiple factors still make the Caribbean an interesting corridor for tax evasion schemes. In some Caribbean countries, including Antigua and Barbuda, Aruba, intermediaries such as lawyers and accountants are not covered by the money laundering laws. Often, these "gatekeepers" are used to set up corporate vehicles that help hide the beneficial ownership of assets. These assets may be earned or obtained legitimately, but individuals may seek ways to hide them from the tax authorities to avoid paying taxes on them. Some Caribbean countries, including for example Dominica, permit "shelf companies" or ready-made offshore companies. Shelf companies can be incorporated with a nominee director and nominee shareholder, and are for sale for immediate use. IBCs are often not required to have a physical presence and are restricted from conducting local business activities. St Vincent and the Grenadines still allow bearer share companies.

Because of these, and other concerns, the U.S State Department still calls several Caribbean countries "countries of primary concern", and the IRS considers many Caribbean countries "offshore secrecy jurisdictions". So, even though they are no longer on the NCCT list, Caribbean nations still have money laundering and tax evasion challenges to deal with. In the absence of a NCCT list, U.S. banks may use the IRS and State Department list to assign "country risk." Treasury Department may also –if the Stop Tax Haven Abuse Bill were approved – issue "Special Measures" affecting Caribbean Banks. All this means that Caribbean countries will stay "high risk" for a while.

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