



Ruling Affirming Legitimacy of Tax Avoidance

In what could be termed a landmark decision, Justice K. Neville Adderley, in a recent ruling, stated that the G-20 and the Organization for Economic Cooperation and Development ("OECD") should not be eager to assume wrongdoing on the part of individuals making use of Bahamian offshore financial institutions. In a case involving the Fraudulent Dispositions Act 1991, as well as numerous allegations of dishonesty, deceit and conspiracy, Justice Adderley meticulously outlined the history of the action within his 109 page Ruling.

The alleged fraud in this case related to transactions totalling more than US\$150 million and involved multiple jurisdictions including Ecuador, the Netherlands Antilles, the British Virgin Islands and Florida. Despite the numerous jurisdictions involved, and the fact that most of the witnesses spoke Spanish, The Bahamas was selected as the forum for the hearing, primarily because the governing law of many of the contracts in question was that of The Bahamas.

The principal defendants in this case were members of a prominent Ecuadorian family, who had over time, amassed substantial wealth from their involvement in real estate, trade and agriculture. Certain Ecuadorian laws of the 1980's, which precluded Ecuadorian citizens from holding US bank accounts, coupled with the nation's social instability during that era, made depositing wealth offshore an attractive wealth protection mechanism. The facts of the case suggest that the

family members were also the principal owners of certain financial institutions with financial instruments from one of these institutions being transferred to another family owned bank.

The Plaintiffs claimed that the Defendants engaged in numerous transactions which essentially amounted to the stripping of over US\$150 million from the said financial institutions in exchange for what turned out to be worthless instruments referred to as Global Depository Receipts ("GDRs"). The Plaintiffs alleged, *inter alia*, that by engaging in these transactions, the Defendants were in breach of their fiduciary duties as trustees as they were essentially acting on both sides of the transactions. The Plaintiffs contended that the Defendants both authorised and approved the various transactions without regard to the interests of depositors.

At paragraph 49 of his Ruling, Justice Adderley took judicial note of the fact that the financial services sector is the second most important industry within The Bahamas. He further stated that, by the time of the alleged transactions, The Bahamas had gained a reputation as a tax-free jurisdiction and its financial institutions had created numerous products designed for the lawful avoidance of taxes and wealth management. These financial products had become attractive to individuals and institutions in high tax jurisdictions, including Ecuador. Justice Adderley cautioned that the tendency to attach the label of fraud to persons

utilising offshore tax-free jurisdictions should be avoided. Justice Adderley went on to declare, at paragraph 51 of the Ruling, that it is a long standing tradition of English and international law that individuals should be free to utilise offshore jurisdictions to lessen their tax burdens so long as they did not attempt to evade taxation.

Justice Adderley proceeded to opine that the relatively recent establishment by the OECD of the black list, grey list and white list, represents a manifestation of the frustration of high tax countries' inability to keep pace with the ever evolving financial products being offered in financial centres such as The Bahamas. Justice Adderley appears to suggest that the development of the black, grey and white lists are mechanisms to indiscriminately target offshore jurisdictions without regard to whether or not the products that they offer are lawful or legitimate. In an effort to compel disclosure by offshore jurisdictions, the OECD has mandated that countries sign Tax Information Exchange Agreements ("TIEAs"), failing which sanctions are imposed which Justice Adderley described as "damaging". At paragraph 54 of the Ruling, Justice Adderley stated definitively that the Court cannot accept that merely failing to disclose the details of offshore tax avoidance mechanisms to one's

government can in and of itself be an indication of fraud.

In ruling in favour of the Defendants, Justice Adderley held that, based upon the facts of the case, it was apparent that the Defendants honestly believed that the instruments which they traded had value. At paragraph 309 of his Ruling, Justice Adderley concluded that the Defendants' acts were not designed to defraud, but rather, that when the various transactions were made, the Defendants honestly and reasonably believed that their strategy had the agreement of the relevant authorities.

Justice Adderley's Ruling contains a firm defence of The Bahamas as a legitimate offshore financial centre. While, clearly not condoning unlawful activities or impropriety, Justice Adderley drew a firm distinction between tax avoidance and tax evasion. The former he declared to be entirely legitimate and in fact supported by the prevailing case law of several jurisdictions. While it may be arguable that the distinction between legitimate tax avoidance and tax evasion is being eroded gradually elsewhere, for certain policy reasons, this recent Ruling by Justice Adderley appears to signify that the distinction is still one of importance in The Bahamas.

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