October 2009

Updater

Current developments in Cayman's legal and regulatory environment

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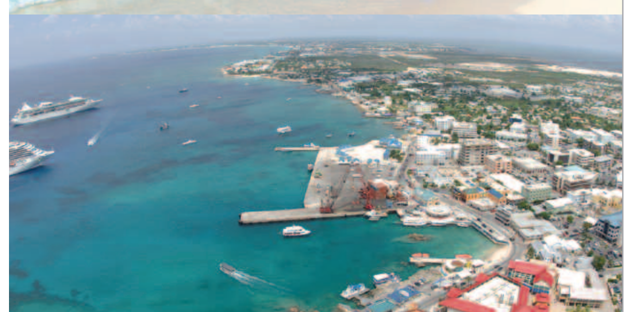

Feedback welcome.
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Cayman in calm waters

In recent weeks Cayman has received a lot of adverse coverage in some sections of the international media as reports of its domestic budgetary difficulties have been relayed by journalists and commentators with anti-Offshore Financial Centres agendas. In short, Cayman's financial position is sound and its business model as a tax neutral structuring and administration centre is not being revised. International clients can be assured that the integrity of the structures they have established in Cayman is completely unaffected by Cayman's domestic fiscal issues. A brief summary of the background and facts is set out below.

Cayman is an overseas territory of the United Kingdom (UK) and as a result is subject to oversight from the UK on certain domestic matters. This oversight provides Cayman, in certain circumstances, with the benefit of additional security of its budgetary affairs. Under the Public Management and Finance Law, Cayman is conditionally required to meet certain key criteria relating to its debt to asset ratio, debt service ratio and reserves to cover operating costs. These criteria have been established to safeguard the fiscal prudence upon which Cayman's public finances are managed. If any of these criteria are not met or if the relevant ratios are exceeded, then the Cayman Government requires the consent of the UK Government to undertake any new borrowing. Currently Cayman's debt as a percentage of GDP is 24%. This compares very favourably to many leading G7 economies, such as the UK, France and the USA where the relevant debt to GDP percentages are respectively, 55.5%, 73.9% and 90%.

The global economic recession has impacted the Cayman Government's revenues as the number of new funds, finance and corporate vehicles established over the last year has reduced significantly from the very high volumes of recent years. Tourism and real estate spending in Cayman has also reduced during this period. This contraction in revenue flows has coincided with significant funding obligations incurred as a result of a number of local infrastructure projects initiated by the previous elected government. As a result the Cayman Government suffered a short term cash flow problem which it sought to rectify by obtaining private sector borrowing. In accordance with the Public Management and Finance Law, permission for this borrowing was requested from the UK Government. At this point economic considerations were complicated by political issues, as the UK Government suggested that Cayman broaden its revenue base by imposing a traditional direct tax system. After some negotiation (and a lot of misleading media reports and commentaries concerning direct taxes and Cayman's financial position - the term "bankrupt" was inaccurately and pejoratively used by some) the UK Government consented to Cayman's reduced borrowing request. Since its election in May 2009, the new Cayman Government has initiated some significant cost cutting and inward investment projects. The new Government has proposed a budget which will bring Cayman back within the debt ratios and operating reserve criteria mandated by the Public Management and Finance Law. The revenue raising measures in the budget are fee and consumption taxes. Furthermore, Cayman has undertaken to conduct a study over the next 18 months to consider whether or not to broaden its domestic tax base by imposing a property tax and a payroll tax on local residents. Such measures (if introduced) would only affect local residents. It is worth noting that Bermuda, BVI and the Bahamas all have one or both of these measures in place.

In conclusion, Cayman has been affected by the global recession, and like many larger economies, it has needed to cut back its spending and increase its revenue. Fortunately, unlike many of the larger economies, Cayman has constitutional impediments which prevent it from incurring unsustainable levels of national debt. The oversight from the UK Government has provided a safety check to ensure that Cayman's fiscal prudence remains intact. As a result, and contrary to the impression created by some media coverage, Cayman has retained its AAA rating with Moody's. The domestic economy is stable and the outlook for international business structured in Cayman remains very positive.