

# Tipping point

Seychelles wants to make the leap into value-added offshore financial services

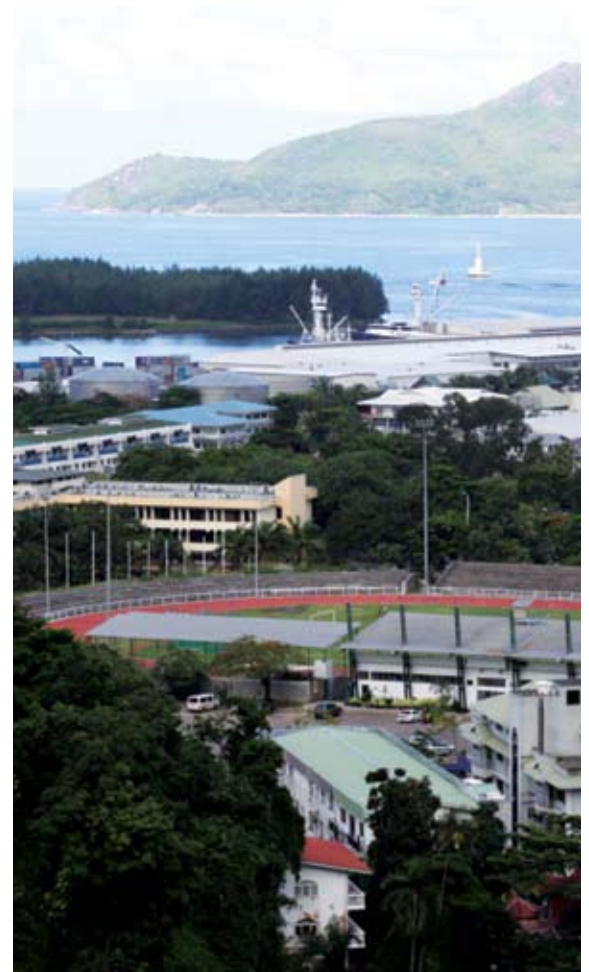
December 19, 2009 was a red letter day for Seychelles: The IMF came through with a US\$31 million loan facility to support the country in its ongoing economic reforms. While the money was important, the statement made through this agreement was invaluable. It was a clear signal to the international community that Seychelles has come through its debt crisis and is back on an even keel.

The country's offshore finance sector has been largely insulated from the difficulties of the last two years – the majority of tax-efficient structures are non-residential – but industry participants were celebrating nonetheless.

“Seychelles had the offshore instruments but the domestic environment was not necessarily that appealing,” said Conrad Benoiton, managing director of the Seychelles office for international law firm Appleby. “Offshore business requires an affinity with institutions such as the central bank and the judiciary. The significant shift in monetary and fiscal policy amounts to a guarantee that the offshore sector is viable.”

Benoiton, who recently left a job at the Seychelles central bank to head up Appleby in the jurisdiction, cites the IMF's support – and the confidence it engendered – as the clinching factor in the law firm's decision to open an office.

Its arrival is significant. Seychelles boasts two international banks (Barclays and BMI), two international accounting firms (KPMG and BDO), but until Appleby set up shop it had yet to attract one of the “magic circle” offshore law firms to its shores. It is hoped that the presence of one of the



industry's top names will draw in more high-end clients keen to use the sophisticated portfolio of products that Seychelles has spent the last two years developing.

“The arrival of Appleby will certainly raise the profile of the jurisdiction and we hope to see more business coming in through the presence of such a substantial law firm,” said Neil Puresh, director of Intercontinental Trust (Seychelles), a

## ► Light at the end of the tunnel: How Seychelles rescued its economy

In August 2008, Seychelles was staring into an economic abyss. One month earlier the government had failed to make its payments on a tranche of foreign private debt and Standard & Poor's had responded by slashing the country's credit rating to selective default.

Several factors were blamed for pushing Seychelles to the brink – rising commodity prices that caused a spike in inflation, and a drop off in vital tourism revenues – but the roots of the problem extended far deeper. As the IMF put it, “Seychelles' economic and financial crisis of 2008 reflected a decades-long pursuit of unsustainable policies and rising structural distortions.”

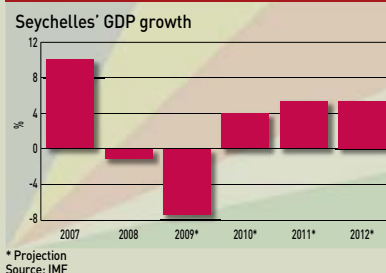
The pace of reform was too slow to address the imbalances and the government, keen to maintain the value of the Seychelles rupee, introduced foreign exchange restrictions. All the while, in-

ternational capital markets were being tapped to cover public spending – Seychelles was digging itself into a hole.

The IMF stepped in with a US\$26 million standby arrangement conditional on action being taken to revive the economy. In December 2009, satisfied with the rate of progress, the IMF canceled the standby arrangement and agreed to a US\$31 million three-year financial support package. The economy is expected to contract by 7.5% in 2009, an improvement on the 10.7% contraction projected in June. GDP growth is likely to return in 2010.

“The macro leverage of Seychelles has undergone a complete turnaround and lending agencies have come back

### Revival period





**BACK ON TRACK:** Seychelles has dealt with its most pressing economic problems

field by volume and Seychelles went from 2,617 IBC incorporations in 2002 to a peak of 13,751 in 2008. The typical source of demand was Europe, but Seychelles' efforts to market itself in Asia, and particularly China, appear to be bearing fruit. Martin Crawford, CEO of Offshore Incorporations Limited, says his firm saw Chinese demand for Seychelles structures (the bulk of them most likely IBCs) jump by more than 60% in the calendar year to December 2009.

"The growth was from a pretty low base, but given the troubles of 2008 and 2009, a 60%-plus increase is impressive," Crawford said.

Seychelles has much to recommend itself to Chinese investors – unlike Caribbean jurisdictions, it has its own Chinese embassy, which expedites the process if company documents require official certification – but the advantages are not restricted to setting up an IBC in double-quick time. Seychelles also offers a Companies Special License (CSL), the principal attraction of which is that it allows investors to take advantage of a string of double taxation agreements, including one with China.

The CSL is more expensive and more complex than the IBC, and it requires a larger amount of administration. Alongside trusts, foundations, mutual funds and hedge funds, it is the kind of value-added product the jurisdiction wants to promote.

A total of 202 CSLs have been set up in Seychelles since the structure was

introduced in 2004. Trusts have been around for 15 years and there are 368 of them, while foundations, the legislation for which was only passed at the end of December, have yet to get off the ground. There are two funds, both domestic in origin, and about half a dozen licensed fund administrators in one form or another. Other parties are interested but the global economic crisis forced many funds to reassess their priorities.

### Sourcing expertise

If Seychelles is to gain momentum in these value-added areas, Appleby alone is not enough. The local industry consensus is that further steps must be taken to improve the jurisdiction's infrastructure so it meets the requirements of international bankers, lawyers and accountants.

Top of the list is an amendment to existing rules that prevent foreign lawyers from practicing in Seychelles unless they retrain in the local system.

"Seychelles is not going anywhere as an offshore center without building expertise and capability," said Simon Mitchell, a consultant to Mayfair Trust, a corporate services provider. "Most local lawyers aren't experienced in corporate and finance matters, but if a Seychelles structure is being used in a transaction overseas, legal opinion is required."

Under the proposed Legal Practitioners' Bill, foreign lawyers would be able to operate in Sey- >>

corporate services provider.

Seychelles made its name in the offshore industry as a location for International Business Companies (IBCs). The lowest common denominator product available, IBCs are popular because they are quick and cheap to set up, involve minimum disclosure and incur no tax.

Jurisdictions measure success in this

and reviewed the country quite favorably," said Conrad Benoit, managing director of Appleby Seychelles and formerly an official at the central bank. "All that is down to the measures the government has entered into under the IMF programs."

In addition to a restructuring of public debt, reforms included the removal of

foreign exchange and interest rate restrictions, the reintroduction of monetary policy and a broadening of the tax base. Civil servant numbers were cut and government spending programs reformed. Steps have also been taken to make the public sector more transparent.

Seychelles' medium-term strategy is one of consolidation and further reform. More can be done to raise public sector productivity, restructure debt and strengthen financial discipline. Alterations to the business tax are likely to continue and be joined by a personal income tax and a value-added tax.

There's no room for complacency but Seychelles can look back on the progress of 2009 as a job well done. "The government has turned the fiscal situation around," said Peter Burian, direc-

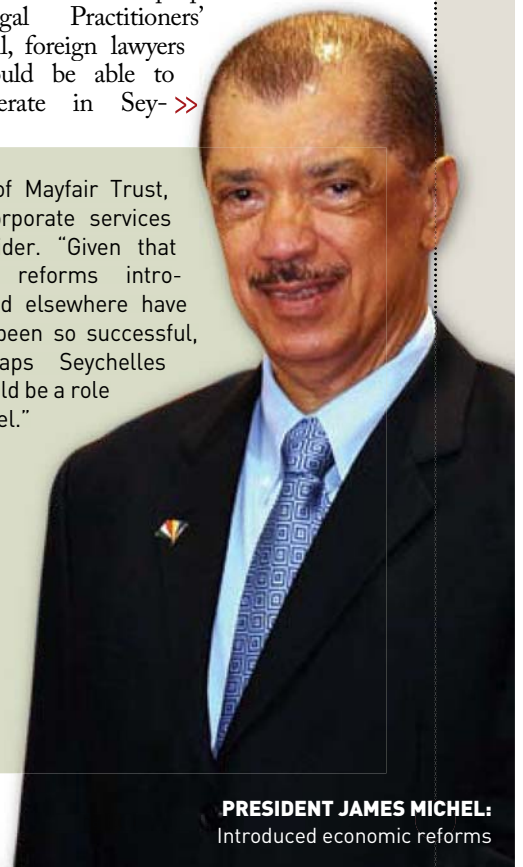
tor of Mayfair Trust, a corporate services provider. "Given that IMF reforms introduced elsewhere have not been so successful, perhaps Seychelles should be a role model."

### Over the worst

Seychelles' consumer price index



\* Projection  
Source: IMF



**PRESIDENT JAMES MICHEL:**  
Introduced economic reforms



**BARCLAYS:** One of Seychelles' two international banks. More are wanted

>> chelles provided they are limited to finance-related work. In addition, all lawyers – foreign and domestic – would qualify for certain tax breaks, much like those already enjoyed by corporate services providers.

Measures have already been put in place to cultivate a new generation of international-standard local lawyers. The University of Seychelles, which was only founded in September of last year, will offer a three-year Bachelor of Laws program in conjunction with the University of London. “What the community still needs is a pool of well-qualified locals who can slot neatly into firms in Seychelles,” said John Esther, senior corporate manager at Barclays Bank Seychelles and an alumnus of the University of London’s law program.

### Leading by example?

All kinds of incentives and encouragement can be offered to attract foreign expertise, and Seychelles is exploring possibilities, particularly on the banking side where capacity is limited. It need only look at fellow Indian Ocean financial center Mauritius for an example of how savvy marketing and strong infrastructure can deliver the goods.

“You have all the established tax managers and banks in Mauritius, and our clients say the telephones are better and the internet is better,” said a Seychelles corporate service provider who asked not to be named. “I have a lot of respect for what Seychelles has done so far, but it needs to get an undersea optic fiber cable in place as soon as possible.”

Crucially, Mauritius also appears to have succeeded in making the transition to value-added products. According to Puresh of Intercontinental Trust, where once Mauritius relied on GBC II companies (an equivalent of IBCs) as its primary business, in the last two years the GBC I structure, which is much like a CSL, has exhibited stronger growth.

Not everyone is complimentary, though. Jacques Scherman, managing director of Sovereign Trust (Hong Kong), says the jurisdiction’s desire to climb the value chain has led to a build up in unnecessary bureaucracy. While service levels remain high, legislation has been introduced with little forethought about implementation, and the cost of compliance has rocketed. He believes that Seychelles is in a position to capitalize on these shortcomings.

“We have clients with Mauritius companies who want to move out, but they need a place with the same level of service and in the same time zone, and without the higher fees and levels of administrative complexity,” Scherman said.

Striking a balance between regulato-

ry and market requirements is the ethos on which much of Seychelles’ offshore legislation is based. The process of introducing a new product starts with a careful analysis of the jurisdictions that have been most successful with the structure in question. Seychelles then takes those ideas and tries to develop them further.

The Seychelles foundation, for example, draws heavily on the structure used by Panama with a view to mirroring its robustness under attack. However, the minimum capital requirement to set up a foundation is much lower than in Panama to appeal to a wider client base. Similarly, the Seychelles funds legislation is modeled on that of Cayman, but Hong Kong, Singaporean, Australian and South African nationals, as well as locals and citizens of the US, UK and Canada, can serve as auditors. This is intended to make the product more Asia-friendly.

Mitchell of Mayfair Trust is the architect of several recent pieces of offshore legislation, but he believes Seychelles would be best served now by perfecting its existing product portfolio rather than adding to it.

“The core products will remain companies, trusts and foundations; and then you have mutual funds, insurance and securities,” he said. “I don’t think we’re missing anything, it’s more a case of refinement. The devil is in the details.”

### Tough sell

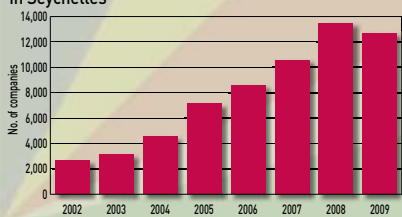
Regardless of the relative strength of Seychelles’ structures, selling them into the international market is a challenge. The offshore world is largely governed by preconception and habit: To win over a fund manager, for example, you must not only convince him of the merits of Seychelles, but also that these merits are worth more than tried and trusted Cayman. It is a lengthy process.

Appleby’s Benoiton believes the decade will be one of specialization as Seychelles shifts away from IBCs towards more substance-based products, led by the CSL. Puresh of Intercontinental Trust, on the other hand, is tentative, stressing that much remains to be done.

“The government has to get more bilateral agreements in place and modernize existing legislation, while the private sector needs to educate staff so they understand products and are able to promote them better,” he said. “We are at a critical point where we must decide where we want to go.” ♦

### Success story

New international business companies set up in Seychelles



Source: SIBA

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# Two-way street

Seychelles hopes tax treaties will allow it to be more than just another country's collection agent

The crackdown on offshore financial centers, initiated by the Organization for Economic Cooperation and Development (OECD) in April 2009, was the starting gun in a frenzied race for compliance. Jurisdictions were placed on one of three lists – white, gray and black – depending on their transparency and cooperation over tax matters. Gray-listed offshore financial centers (OFCs) rushed to sign the 12 tax information exchange agreements (TIEAs) required to move up to white.

As of January, Seychelles hadn't signed a single TIEA – and yet the jurisdiction met all the OECD's requirements from the get-go. This is because the Seychelles government has eschewed basic tax information exchanges in favor of double taxation agreements (DTAs), of which it has 12.

"A TIEA just does one thing: It provides for exchange of tax information between the two countries. For a place like Seychelles that doesn't levy tax on foreign-sourced income and a place like the UK, it's a one-way benefit – Seychelles is helping the UK authorities collect tax," said Simon Mitchell, a consultant to Mayfair Trust, a Seychelles corporate services provider.

## Better deal

A DTA includes all aspects of a TIEA – Article 26 concerns the exchange of tax information – and then some. Under a DTA, Seychelles can take its investment structures onto the territory of the counter signatory and benefit from the offsetting of tax liability. This effectively opens up new channels for the offshore business sector.

The Seychelles Companies Special License (CSL) exists for this very purpose. Only tax resident enterprises – not the plain-vanilla international business companies (IBCs) designed for

## Seychelles Double Taxation Agreements

Ratified DTAs	Date of implementation
Barbados	Feb 2008
Botswana	Jun 2005
China	Jan 2000
Cyprus	Nov 2006
Indonesia	May 2000
Malaysia	Jul 2006
Mauritius	Jun 2005
Oman	Jan 2004
South Africa	Jul 2002
Thailand	Apr 2006
UAE	Apr 2007
Vietnam	Jul 2006

Note: There are unratified DTAs with Belgium, Qatar and Zimbabwe  
Source: Seychelles International Business Authority

broad use and minimal disclosure – can benefit from DTAs. Using a CSL, an enterprise is able to avoid Seychelles' 40% local business tax rate in favor of a 1.5% levy. In this way, the structure is both tax-efficient and subject to sufficient regulatory scrutiny. Amongst other things, companies must file audited accounts, hold annual meetings and submit names of directors and shareholders to the government registry.

Neil Puresh, a director at corporate services provider Intercontinental Trust (Seychelles), notes that the CSL has been particularly successful when used with the Seychelles-Indonesia DTA, which reduces the withholding tax on outbound dividend payments from 20% to 10%. "There have been quite a number of registrations from our point of view," Puresh said.

Chinese CSLs are not quite as popular, which is generally put down to competition from other OFCs – Hong Kong and Singapore both have DTAs with China and they take the bulk of the holding company business – and unfamiliarity. But Seychelles has the edge over its Asian rivals on dividends. Firms in all three jurisdictions are taxed 5% on dividend payments generated by mainland Chinese enterprises, rather than the standard 10%. However, if a Hong Kong or Singaporean company's holding in the Chinese enterprise exceeds 25%, it doesn't qualify for the tax break. A Seychelles firm can benefit from the discount regardless of the size of its shareholding.

"It is a very niche area. Investors that have less than 25% ownership are most likely to be mutual funds and private equity funds," said Peter Burian, a director at Mayfair Trust. "It takes time for a structure like this to establish itself and it's really a matter of promoting it effectively."



**FINE BLEND:** Seychelles combines historical awareness with a progressive attitude

Another reason for the slow uptake in China is that until 2009 there was no need for investors to channel their money through tax-efficient vehicles. That changed with the introduction of the Enterprise Income Tax Law. First of all, companies based offshore that are effectively managed in China are counted as tax-resident enterprises. Second, non-tax resident enterprises (a company with a CSL is effectively managed in Seychelles) have to pay the 10% withholding tax on dividends.

A DTA is the logical way around these requirements, but it is still early days. The State Administration is still in the process of clarifying the finer points of the new law. Once investors know where they stand – and the authorities become more zealous in their enforcement of the rules – offshore restructuring will become a pressing issue.

“Seychelles will see more business coming out of China because the atmosphere in China is headed in the direction of using OFCs that have tax treaties with the country,” said Martin Crawford, CEO of Offshore Incorporations Limited. “The CSL will grow in popularity.”

#### A few flaws

The DTA approach is not perfect. Tax treaties have a tendency to draw attention if overused, resulting in investigations by the tax authorities of those they suspect of abusing the system.

The Seychelles-China treaty has a long way to go before it attracts this kind of scrutiny, but there are other pressures. According to Mayfair Trust’s Mitchell, there is talk of the OECD raising its compliance requirements. Rather than settling for 12 DTAs, the organization might insist on more agreements and that they must be with OECD member nations, in which event none of Seychelles’ existing treaties would qualify.

“Some countries don’t see a DTA with Seychelles as being necessary, because of the trade, engagement and investment potential,” said Conrad Benoiton, managing director of the Seychelles office for law firm Appleby. “If we can’t get a DTA then we would negotiate a TIEA. Our long term strategy is not to provide an evasive environment. If information is required, we will provide it.” ♦



**TRADING TIME:**  
The Seychelles stock exchange is a work in progress

## If you list it, they will come

### The Seychelles securities exchange

It seems illogical that an isolated archipelago nation with a population of just 80,000 would ever be able to launch a securities exchange – there wouldn’t be enough liquidity to make trading worthwhile. Yet the Seychelles bourse is well on the way to becoming a reality.

The man behind the project is Richard Bonnichsen, an executive with Anglorand Group, a major South African brokerage. “I visited Seychelles four years ago and was told they had all the legislation in place from 1995 but hadn’t done anything about it,” Bonnichsen recalled. “We said, ‘Why don’t we look at getting it going?’”

Anglorand’s proposal envisages a two-tier system: A bourse focused on niche products for Seychelles’ offshore sector would generate the cash and subsidize a local exchange tacked on the side.

Conrad Benoiton, managing director of law firm Appleby in Seychelles, was until recently with the central bank department responsible for overseeing the securities industry. He expects the licensing of stock exchange operators – there must be three founding members – to be completed in the first quarter of 2010. “We will see the emergence of a stock exchange serving small domestic operations but also having an added offshore element, which

would in my view be the running element,” Benoiton said.

Anglorand wants this offshore element of the exchange to be dedicated to contracts for difference (CFD), a kind of derivative that allow investors to take long or short positions on underlying financial instruments such as a stocks. CFDs, which are traded on margin, are particularly popular in the City of London where they are used to hedge against exposure to equities. There is no requirement to own the underlying shares, so in theory CFDs can be based on any global index, commodity or currency.

The bulk of CFD trades are over-the-counter (OTC) between a client and a financial institution. Australia is the only country that offers exchange-traded CFDs, and the idea is that Seychelles would become the first to offer the products in a tax-efficient environment.

“Following the financial crisis, there is increasing pressure to get OTC products cleared on an exchange,” said Bonnichsen. “That is what we are trying to do.”

The exchange would be fully automated, making manpower limited, but Bonnichsen believes it could raise the bar across Seychelles’ financial sector as a whole, bringing in demand for new and sophisticated ancillary services. ♦