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Cayman Islands

30 September 2014

Dear Sirs

Re: Public Consultation: Charities Bill, 2014 (the "Bill")

We refer to the consultation paper issued by the Portfolio of Legal Affairs on the Bill and the proposed regulation of Cayman Islands charitable organisations (the "**Consultation Paper**").

The Caymanian Bar Association Council ("**CBA Council**") acknowledges and supports the commitment to globally accepted and practiced standards in the fight against money laundering and terrorist financing and recognises the importance of transparency in that regard. However, trying to make such initiatives the central focus of the Bill, which is intended to regulate voluntary organisations in the Cayman Islands, is misplaced.

For the reasons summarised below, the CBA Council would not recommend the enactment of the Bill in its present form. The intent of the comments in this letter is to raise matters of principle rather than drafting points, which cannot usefully be made when there are many fundamental concerns about the scope and practicalities of a regime along the lines of the Bill.

The Cayman Islands have a long and broad tradition of voluntary fund raising for all manner of worthy causes. This is a critical component of the Cayman Islands society which does not operate a formal, state funded welfare system. In other jurisdictions that do, and have to fund social programmes from government revenues, the primary benefit of charitable status is tax exemption. The position in the Cayman Islands is quite different given the absence of taxation from which exemption could be conferred or any other material advantage of being a charity *per se*. In fact, true charities (i.e., organisations with exclusively "charitable" purposes) are rare. Most organisations in the Cayman Islands that would colloquially be described as "charitable" actually are not. We will refer to such organisations herein as Voluntary Organisations or "VOs".

1 Genesis of the Charities Bill

- 1.1 As a starting point, it is critical to the review of the Bill to understand its primary objectives or genesis. The Cayman Islands does not have a history of charity legislation nor does it have legislation governing the regulation of local VO's as other countries in the Caribbean region have. While the CBA Council supports the notion that some level of regulatory regime should be introduced, to what extent this may be imposed is debatable and consideration should be given to how existing and future VO's will be affected (i.e., additional administrative requirements, costs incurred for adhering to stringent requirements and achieving a satisfactory level of transparency expected for a regulated VO). Currently, many existing Cayman Islands VO's would be categorised as "unsophisticated". For smaller, less sophisticated VO's, the proposed requirements will undoubtedly be construed as burdensome and in some instances, largely unachievable.
- 1.2 In comparison to other jurisdictions, such as Bermuda which recently repealed and replaced its 1978 charities legislation, the existence of statutory regulation is not, by any means, a new concept. From a Cayman Islands perspective, however, this is not the case and as such, clarification should therefore

be sought as to whether existing VOs are slated to be "grandfathered" into the provisions of the Bill or whether the provisions will apply across the board to all existing and future VOs from the outset.

1.3 The 2010 Report published by the Cayman Islands Law Reform Commission¹ (the "**Commission**") provides that the genesis of the Bill was a recommendation that legislation be formulated to regulate charities. Such legislation is to include provisions relating to the establishment of a permanent charities register into which the names of all charitable associations should be entered. The intention of the registration process is to facilitate accountability for funds and donations received by charitable organisations. However, the Commission also recognised that the works of charitable organisations are essential to the development of any society and the legislation should embody the ability for charities to operate in an environment which remains "free" and "independent".

1.4 In the 2010 Report, the Commission took account of the recommendations of the Financial Action Task Force ("**FATF**").

The FATF Special Recommendation VIII (SR VIII)² provides that:

"Countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism. Non-profit organisations are particularly vulnerable and countries should ensure that they cannot be misused:

- (i) by terrorist organisations posing as legitimate entities;*
- (ii) to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset freezing measures; and*
- (iii) to conceal or obscure the clandestine diversion of funds intended for legitimate purposes to terrorist organisations."*

The objective behind SR VIII therefore is to ensure that non-profit organisations are not used by terrorists as a cover for or as a means of furthering the financing of terrorist activities. To facilitate the implementation of this recommendation, the FATF has developed suggested practices that would assist jurisdictions in the prevention of terrorist exploitation of legitimate charitable non-profit organisations. Some of these practices include a requirement that an oversight authority for charitable organisations be established, charitable non-profit organisations register with a designated authority, financial and personnel records be maintained and mechanisms to investigate abuses of charitable organisations be introduced."

1.5 The Caribbean Financial Action Task Force ("**CFATF**") also evaluated the current licensing and registration systems of the Cayman Islands and concluded that such systems required strengthening in accordance with SR VIII. Specifically, the CFATF pointed to the absence of an authority to monitor the operations of non-profit organisations.

1.6 Several measures³ were recommended by the CFATF to protect and enhance the efficiencies of the charitable non-profit sector. These include -

- "(a) developing a supervisory programme for NPOs⁴ in order to identify non-compliance and violations;*
- (b) establishing systems and procedures to allow information on NPOs to be publicly available;*

¹ The Law Reform Commission: Review of the Law Regulating Charitable Organisations in the Cayman Islands Final Report 31 March 2010, p. 5.

² Ibid., p. 18.

³ Ibid., p. 19.

⁴ Non-profit organisations.

- (c) *putting in place points of contact or procedures to respond to international inquiries regarding terrorism related activity of NPOs; and*
- (d) *facilitating outreach programmes to the NPO sector with a view to protecting the sector from terrorist financing abuse."*

1.7 The Commission expressed an intention to formulate proposals which would give effect to these practices and recommendations, as it is believed that adoption of the measures stipulated will facilitate the preservation of the positive international standing of the Cayman Islands in its efforts to counteract all forms of terrorist and money laundering activities.

1.8 The objectives of the Bill would therefore appear to be as follows:

- (a) to introduce appropriate measures to minimise the risk of Cayman Islands VOs being used to support terrorism or any other illegal activities;
- (b) to achieve compliance with FATF requirements; and
- (c) to reduce the risk of charitable donations being mismanaged or misapplied.

1.9 These are valuable objectives. However, the Cayman Islands already possess sufficient laws⁵ to address these matters as well as comprehensive regulation, diligently enforced to ensure international compliance and maintain a high level of transparency and accountability alike.

2 The Proposed Bill

2.1 The proposed Bill is complex and, if enacted in its present form, will adversely affect charitable/voluntary activities in the Cayman Islands. The Bill makes little effort to identify the differences between public, private and exempt VOs. The Bill also goes substantially beyond the scope of recommendations of both the FATF and the CFATF, creating danger for an overly regulated, draconian-type regime which could potentially stifle the free and independent environment in which VOs are recommended to operate.

2.2 The scope and scale of perceived risks to Cayman Islands VOs should be based on evidence and an analysis of where identifiable practical risks are of a legitimate concern or actually exist. We are not aware of any VOs in the Cayman Islands being used as conduits for the purposes of funding terrorism or any other illegal activities but we understand the need to be preventative rather than reactive.

2.3 We believe that in the voluntary sector (i) concern should be focused more on how funds and resources are applied and, only where the level of funds demands such scrutiny, should the focus be on where the funds originate and, (ii) to the extent that funds are spent in the Cayman Islands, this should be dealt with as a domestic concern, not an international one.

2.4 The Bill seeks to introduce a new and much broader statutory definition of "charity", which may or may not be a good thing of itself, but the draft also provides that funds may not be raised from the public **UNLESS** for purposes falling within the expanded heads of charity **AND** for which there is a "public" benefit. It can therefore be concluded that the Bill would appear to criminalise any other form of public fund raising - for example an appeal to finance medical treatment or an educational opportunity for a particular individual. If the purpose of the Bill is to regulate the raising of funds by the voluntary sector generally, then that is how it should be constructed and the definition of what is or is not specifically charitable as opposed to more broadly philanthropic efforts becomes largely irrelevant, particularly if there are no positive benefits derived from being a charity as such.

⁵ Monetary Authority Law (2013 Revision), Companies Law (2013 Revision), Proceeds of Crime Law, 2008 and the Terrorism Law (2011 Revision).

- 2.5 Legislation that prescribes the purposes for which individuals or organisations may donate their own money would represent an overly restrictive and fundamental change to both to the legal and social environments in the Cayman Islands.
- 2.6 VOs in the Cayman Islands have not become the sort of industry that charities, non-profits, NGOs etc. are in many other places. While many of the larger VOs may have employees, they still tend to be heavily reliant on volunteers at all levels and are not staging posts in political or public service careers. It is important to recognise that the work of VOs in the Cayman Islands is essential to the development and growth of the Cayman Islands. The services and assistance provided by VOs in the Cayman Islands cannot be replicated by the Cayman Islands government. The costs alone, not to mention the human resources to provide such services, are prohibitive.

3 Consequences to Avoid

Given the genesis of the Bill, the 'evil' that it is to cure and the nature of the Cayman Islands society, it is important to ensure that the Bill is the solution. The Bill and, ultimately, with any charities law, should, in attempting to provide a solution, strive to avoid the creation of unnecessary hurdles and side effects, such as:

- 3.1 overburdening the public sector in terms of cost and resources to implement the mechanics necessary for overseeing regulation;
- 3.2 creating a complex regime, which becomes a recurrent source of external criticism when not administered and enforced rigorously;
- 3.3 creating a moral hazard by high levels of supervisory responsibility and heavy filing requirements;
- 3.4 excessive cost to the voluntary sector⁶;
- 3.5 demotivation of major private donors, most of whom do not wish to see more than the reasonable minimum of what they give being consumed by red tape and consider themselves capable of determining the appropriate degrees of transparency and accountability in the specific case;
- 3.6 stifling small scale fund raising activities in the community. These are often relatively informal, even spontaneous, and often involve children learning to help others. These activities should be positively encouraged, not inhibited; and
- 3.7 discouraging individuals from contributing to the day to day management and operation of VOs by making the attendant obligations and liabilities overly burdensome.

4 Practical and Administrative Concerns

- 4.1 These are too numerous to list exhaustively, but as overriding matters, any proposed legislation for the voluntary sector should:
- (a) start with clear evidence and analysis of any genuine evil;
 - (b) within the specific context of the Cayman Islands, its political and social structures identify what practically might be done through local legislation that would actually mitigate that evil;
 - (c) be something that can be realistically and properly administered with necessary financial and human resources committed to it;

⁶ The Commission estimated that there are 240 organisations in the charitable sector in the Cayman Islands to which the proposed Bill might apply. Taking that figure as an example, if all such organisations were audited at \$10-15k per annum that is \$2.5-3.5m diverted annually from the underlying causes of these organisations, even if gross contributions are not adversely affected.

- (d) be founded on a proper cost/benefit analysis against the background of a government trying to reduce unnecessary expenditure; and
- (e) not have collateral detrimental social effects disproportionate to the benefits of a new law.

4.2 Other particular problems with the Bill include:

- (a) good works falling outside the proposed concepts of charity and public benefit becoming illegal;
- (b) people in the habit of making donations themselves being caught within the definition of being a charity themselves and falling within the regime;
- (c) the Registrar having too many proactive obligations and responsibilities both in terms of determining whether something should be registered and subsequently monitoring it;
- (d) below a certain level, what is gained by maintaining records of all donations? The names and addresses of anyone putting a dollar in a collection plate are "easily ascertainable". The question is the purpose served;
- (e) inquiry provisions potentially impose high degrees of obligation on fiduciaries. Whether or not broadly reasonable depends on whether they are of universal application. The resources of a large and formalised organisation will be very different from countless smaller, but worthy endeavours;
- (f) requiring every person soliciting (e.g., anyone rattling a tin) to have an agreement with the relevant charity and for the Registrar to have been given prior written notice is impractical and unnecessary. There is also no need for yet another offence in Section 21 of the Bill: if money is raised and duly handed over to the charity, no harm done - if it is not, it will be fraud, theft, obtaining money by deception, conversion and/or unjust enrichment etc. Sections 21 and 22 of the Bill appear to have been lifted from legislation aimed at third party fundraisers of the sort not seen in the Cayman Islands, who are often compensated, and quite different from the voluntary help typical in the Cayman Islands;
- (g) maintaining accounts should not be required at all below a specified level. Where that level is exactly is debatable. Likewise audits⁷ at a higher threshold if at all. Arguably the need for an audit should continue to be driven by donors, not statute;
- (h) the purpose of the Section 30 exemptions are relatively clear, however, the drafting is not. If an organisation that would otherwise be included in the definition of charity is considered to be adequately regulated elsewhere, it should simply be removed from the scope of the Bill completely. Language which expressly lists those exempt charitable organisations and community boards created by statute, schools, public and private hospitals and churches should be included for avoidance of any doubt. Any other types of charitable organisations or VOs later established which may be considered exempt from registration; such exemption should only be granted by an order made by the Attorney General. Another suggested category of exempted charities could be those which have no permanent endowment or those with an income of less than \$100 per annum; and
- (i) the language of Section 31 of the Bill is oppressive and unworkable. A short term activity, certainly below a certain size, should not require prior approval from the Registrar and certainly not custodial sanctions for breach. How long is it likely to take for the Registrar to

⁷ This will depend on the finances of the VO. If a VO raises funds for specific events/causes during its financial year, pays out those funds and only maintains a minimum existence, how will it be able to afford an audit?

process an application for a car wash or a cake stall? At the very most, this should only be a notification requirement, though to what real benefit is questionable.

5 Alternative Approach

In light of the numerous potential dangers and concerns highlighted above, it is strongly recommended that the objective of the Bill be further considered. Only by understanding the problem that the Bill is to cure will we find a workable solution.

We therefore recommend the following alternatives:

- (a) Clarification that the existing suspicious transaction reporting regime should apply to VOs.
- (b) Registration regime for VOs over a certain size.
- (c) Availability of centralised data in respect of who is doing what on a material scale within the voluntary sector.
- (d) Companies Law-type requirements for maintaining proper books and records.
- (e) Regulatory powers of investigation on reasonable suspicion of misfeasance.
- (f) Mechanisms for criminal and civil proceedings. Existing law relating to fraud and theft etc., enforced by the Royal Cayman Islands Police Service, should be sufficient to address criminal matters. Law officers should be able to litigate fiduciary aspects and claims in tort etc. requiring civil action.

5.2 A threshold should be established for those VOs of more than a certain size (i.e. those within a higher annual income bracket), whether technically defined as "charitable" or not, should be required to register (to the extent that they are not already governed by an acceptable legal regime whether it be locally or internationally). Registration should not be subject to discretionary approval and involve filing of prescribed particulars as follows:

- (a) name of VO;
- (b) address of VO;
- (c) objects of VO;
- (d) identity of fiduciaries (trustees, directors, principals etc. depending on legal form); and
- (e) constitutional documents⁸.

5.3 The Registrar issues a certificate of registration in the name of the VO and supplies a registration number.

5.4 Registered VOs should be required to:

- (a) maintain proper books and records;
- (b) operate within the scope of its prescribed objects/matters reasonably ancillary to attaining them;
- (c) comply with the suspicious transaction reporting requirements of the Proceeds of Crime Law;

⁸ Though, the ability to have access to such documents might suffice.

- (d) retain details of all payments/wire transfers made outside of the Cayman Islands; and
 - (e) file an annual return summarising (i) income and receipts, (ii) expenditure (in direct furtherance of objects and on administrative and other costs etc.) and (iii) assets and liabilities.
- 5.5 All VOs (whether registered or not, including those ad hoc individual efforts) should be subject to the rules relating to the activity of fund raising in a reasonable and honest manner.
- 5.6 Powers for the Registrar to investigate the affairs of the registered VO on reasonable grounds if there is evidence or suspicion of misfeasance and to make an application to court for receivership or other remedial orders including an ultimate cy-près type power if it is not practicable to revive the VO.

We would be pleased to meet at any time to discuss further our concerns expressed above.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Brett Basdeo', with a stylized flourish at the end.

Brett Basdeo, 2014-15 Vice President

For and on behalf of
Caymanian Bar Association Council