The Ugland House in Grand Cayman is used as the address for 12,748 companies.

# THE $150 BILLION SHELL GAME

**More than 150 U.S. companies, including Coca-Cola and Intel, have subsidiaries in the Cayman Islands. That costs the U.S. billions in lost taxes.**

By David Evans

On a January afternoon in George Town, the capital of the Cayman Islands, the sun beats down on three cruise ships anchored at Hog Sty Bay. Along the waterfront on Church Street stands a green-trimmed, white, five-story office building called Ugland House. From the outside, there's no way to see it's the official address of 12,748 companies. Ugland and other office buildings in George Town are home to subsidiaries of more than 150 U.S. corporations, including Coca-Cola Co., Intel Corp. and 10 more of the 30 companies in the Dow Jones Industrial Average.

Parmalat Finanziaria SpA, the Italian food company that collapsed in December after telling investors it had lied about its finances, used three Cayman subsidiaries to misrepresent assets, according to Italian prosecutors. Enron Corp., the Houston-based energy company that went bankrupt in December 2001, used 441 Cayman affiliates to help hide $2.9 billion in losses, U.S. Senate investigators say.

Scores of the biggest U.S. companies use havens like the tax-free Cayman Islands, a British crown colony 150 miles southwest of Cuba, to escape billions of dollars in U.S. taxes, says Senator Byron Dorgan, a Democrat from North Dakota.

Twenty-four of the 100 largest contractors with the U.S. federal government—including Altria Group Inc., Oracle Corp. and Procter & Gamble Co.—have subsidiaries in the Caymans, according to a March report by the General Accounting Office, Congress's investigative arm. Those 24 companies received a total of $35 billion from the U.S. government in 2001, the GAO found. "They are shortchanging our country even as they profit from it," says Dorgan, 62, the top Democrat on the Competition, Foreign Commerce and Infrastructure Subcommittee of the Committee on Commerce, Science and Transportation.

Oracle spokeswoman Deborah Lilienthal says the database software maker's Cayman subsidiary owns a minority share of a foreign company she declined to disclose. Procter & Gamble spokesman Douglas Shelton says the household goods maker's Cayman subsidiary is an inactive holding company. "We're currently exploring dissolution of that entity so it doesn't raise questions in people's minds," he says. Altria spokesman Tim Kellogg says the food and cigarette maker's Cayman subsidiary is a holding company.

The 100 U.S. contractors own 464 subsidiaries in offshore tax havens, according to the GAO report. The offshore subsidiaries often serve the sole purpose of allowing companies to avoid paying U.S. taxes, says Senator Carl Levin, 68, a Democrat from Michigan. "Many are little more than a post office box set up to allow corporations to move profits to the low- or no-tax havens rather than reporting that income to the United States," he says.

J.P. Morgan Chase & Co. estimated in a June study that $650 billion of profit earned abroad by U.S. companies over decades had never been taxed by the U.S. That's up from a cumulative total of $500 billion cited by J.P. Morgan in a study a year ago. In 2001, almost half of the money U.S. companies earned outside the

PHOTOGRAPH BY BRIAN SMITH

U.S.—47 percent—was accounted for in offshore tax havens such as the Cayman Islands, which has no corporate income tax, says Martin Sullivan, 45, a former U.S. Treasury Department economist, citing Commerce Department data. As a result, companies didn't have to pay the 35 percent U.S. corporate income tax.

The tax haven units held only 12.6 percent of the companies' foreign plants and equipment and 9 percent of their foreign employees, says Sullivan, who now writes a column for *Tax Notes,* a weekly journal. In other words, U.S. companies were avoiding not only U.S. taxes but taxes in other countries where they made and sold products, Levin says. "When $250 billion of the $880 billion in foreign bank deposits within U.S. banks is attributed to the Cayman Islands, to connect the dots you've got to ask questions about the extent of tax dodging in that country and other tax havens," Levin says. Sullivan says his research shows the Caymans are being used for U.S. tax avoidance.

David James, vice president of research at James Investment Research Inc., which manages $650 million, says he has mixed feelings about companies that use the Cayman Islands to avoid U.S. taxes. "As an American, I hate to see it happen," he says. "As an economist, I see it as a sign U.S. taxes are too high. As a shareholder, I favor lowering taxes to boost the bottom line. If they can move to Mars and reduce taxes further, that would be fine."

James Investment, based in Beavercreek, Ohio, holds 24,000 shares of Seagate Technology Inc., the world's largest computer disk drive maker. Seagate, based in Scotts Valley, California, incorporated in the Cayman Islands in 2000. The company reduced its taxes in fiscal 2003 to an effective rate of 2.9 percent, or $19 million on profit of $660 million, according to its 2003 annual report. Seagate's taxes included foreign taxes paid of $40 million and a U.S. tax credit of $21 million, according to the report.

U.S. Senator **Byron Dorgan** says too many companies abuse accounting rules to avoid taxes.

KATHERINE LAMBERT

Spokesman Guy Cantwell says about 69 percent of the company's revenue comes from outside the U.S.

Coca-Cola, the world's largest soft-drink maker, manufactures syrup in two Irish plants owned by Coke's Cayman-based subsidiary, Atlantic Industries. Coke, based in Atlanta, saved $500 million in U.S. taxes last year by earning 63 percent of its income through foreign subsidiaries, according to its 2003 annual report. Coke used the Cayman subsidiary to sell syrup to customers in 75 countries and avoid paying U.S. taxes on earnings from more than $1 billion in revenue last year, according to a person familiar with Coke's finances. Coke spokesman Ben Deutsch says the company doesn't comment on tax strategies for competitive reasons.

"When companies, including great companies like Coca-Cola, decide they want to minimize their participation in the payment of taxes for that which we enjoy in this country, it bothers me," Dorgan says.

**'We have to get on top of corporate accounting and manipulation of corporate books for the sole purpose of reducing taxes,' Senator Charles Grassley says.**

Intel, the world's biggest computer chip maker, uses a Cayman subsidiary to run plants in Ireland, which has a 12.5 percent corporate income tax. Intel, using its offshore units, avoided $792.6 million in U.S. taxes from 2001 to 2003, according to SEC filings. Asked why Intel, based in Santa Clara, California, has a Cayman subsidiary, spokesman Chuck Mulloy says, "I can only assume it's for tax purposes." He adds, "Unless we absolutely need it onshore, we'll keep it offshore to avoid paying a 35 percent tax." Intel Chief Executive Officer Craig Barrett declines to comment, Mulloy says.

Seagate incorporated in the Caymans to reduce its taxes, spokesman Brian Ziel says. "The competitive benefits relate both to taxes saved on certain income earned outside of the United States and the ability to efficiently deploy assets around the globe to remain competitive," he says.

Other U.S.-based corporations incorporated in the Caymans include Fresh Del Monte Produce Inc., the world's third-largest banana producer, which is actually headquartered in Coral Gables, Florida, and Transocean Inc., a drilling company with an $8.2 billion market value, which is actually based in Houston. Del Monte spokeswoman Dana Weinstein declined to comment. Transocean wrote in a 1999 SEC filing that it had incorporated in the Caymans to lower its taxes.

Intel is part of a group of U.S. companies called the Homeland Investment Coalition that supports Congressional proposals to allow the billions of dollars in overseas profits to be repatriated for one year in exchange for paying a 5.25 percent tax.

The coalition, which has hired PricewaterhouseCoopers

LLP to lobby the U.S. Congress, presents the proposal as an idea that would benefit both the companies and the country's economy. It says the repatriated money would be used to create jobs, fund pension plans and pay off debt. Few of these dollars would ever be brought back to the U.S. and taxed if the one-time tax break isn't approved, the coalition said in an April 28, 2003, letter to Congress. J.P. Morgan estimates $425 billion would be repatriated. That would result in $22.3 billion in U.S. tax revenue, using the proposed 5.25 percent tax rate. That figure represents 17 percent of the $132 billion in U.S. corporate tax revenue in fiscal 2003, according to the Congressional Budget Office.

Forty-five percent of U.S. corporations with revenue exceeding $50 million or assets of more than $250 million paid no federal income tax in 2000, according to the GAO study. That has increased each year since 1996, when it was 33 percent, a GAO study found.

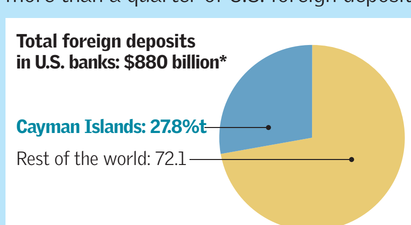
"There's no reliable data on how many offshore subsidiaries serve as tax dodges versus valid business outlets," Levin says. "But recent research does show that U.S. businesses are reporting more and more of their profits in tax havens while paying less and less in U.S. taxes."


Some of the research Levin refers to is by economist Sullivan, who analyzed Commerce Department data and found that profits for Cayman subsidiaries of U.S. companies are soaring. They earned $5.1 billion in 2001, up from $300 million in 1993, he found. Revenue for the Cayman units rose to $12.5 billion from $2 billion, while their assets increased to $141.8 billion from $9 billion eight years earlier, Sullivan found.

Companies focusing on tax avoidance by shifting income to tax havens don't impress all investors, says Lynn Yturri, who oversees $500 million at Columbus, Ohio–based Banc One Investment Advisors, which manages more than $150 billion. "Conservative tax strategies are what investors are looking for, not gimmicks," he says. "Investors are going to discount the stock of companies that don't pay their fair share of taxes." Yturri cites Stanley Works, the largest U.S. maker of hand tools, which in August 2002 abandoned plans to change its legal address to the tax-free island of Bermuda from New Britain, Connecticut. Stanley shares have risen 25 percent since that decision.

Presidential candidates John Kerry, a Democratic senator from Massachusetts, and Republican President George W. Bush disagree about how much tax U.S. corporations should pay the U.S. Kerry, 60, says he would require U.S. corporations to pay U.S. taxes on all exported products regardless of where they're made or sold. "American companies should pay taxes on their profits in the same way whether they earn them in Bangalore or Buffalo," says Kerry aide Jason Furman, 33, who was a staff economist on President Bill Clinton's Council of Economic Advisers.

**Imbalance** The Caymans account for more than a quarter of U.S. foreign deposits.




*As of February. Figures do not add up to 100 due to rounding.
Source: U.S. Treasury

Kerry would also allow a one-time tax bonus for U.S. companies: If they bring previous foreign earnings into the U.S., corporations could pay a 10 percent tax rate on that money rather than the current 35 percent. In the future, he would use the new taxes on foreign income to help lower the U.S. tax rate to 33.25 percent—minus credits for taxes paid to other countries.

President Bush, 57, unlike Kerry, doesn't want U.S. companies' foreign subsidiaries to pay U.S. taxes if they already pay foreign taxes, says Tara Bradshaw, a U.S. Treasury Department spokeswoman. Bush opposes a tax break for repatriated profit because it would be unfair to U.S. companies that already paid the full 35 percent tax rate, she says. Imposing income taxes on foreign subsidiaries of U.S. companies would place them at a disadvantage with competitors that don't pay U.S. taxes, she says. "This would be a serious blow to U.S. businesses seeking to compete in the global marketplace."

A practice called transfer pricing may be the key to how U.S. corporations avoid taxes in the U.S. and other countries, Dorgan says. The accounting practice lets companies buy and sell products and services with their own offshore subsidiaries and set prices themselves. Companies abuse transfer pricing by shifting profits overseas to avoid U.S. taxes, Dorgan says. They set artificially high prices for imports and artificially low prices on exports, he says.

In a March report on financial crime and international law enforcement, the U.S. State Department cited examples of transfer pricing abuses, without naming companies. It said one company claimed to import dish towels from Pakistan for $153.72 each; another reported it had imported briefs and panties from Hungary for $739.25 a dozen; a third claimed it had paid $4,896 a unit for metal tweezers imported from Japan. The report also cited a company claiming to export toilet bowls to Hong Kong for $1.75 each. The State Department report called those prices absurd and ridiculous.

The fabricated high prices of imports let companies report artificially high expenses in IRS tax filings. The exaggerated low prices of exports allow companies to report smaller profits to the IRS. "Criminal individuals, corporations and other enterprises engage in abnormal international trade pricing that transfers value and/or reduces U.S. tax liability," the State Department report said.

Transfer pricing abuses by corporations cost the U.S. Treasury $53 billion a year, according to Professor John Zdanowicz of Florida International University in Miami. He says tracking a product used in transfer pricing transactions between U.S. companies and their subsidiaries in the Caymans and elsewhere is difficult. "Where it really comes from and where it's really going, nobody knows, because of the secrecy," he says. The $53 billion in lost U.S. taxes results from more than $150 billion of profit from improper transfer pricing, Zdanowicz says. "It's a $150 billion shell game," he says. Zdanowicz and Simon Pak, now at Penn State University in Great Valley, Pennsylvania, were granted $2 million by Congress in 2001 to do a more complete study of transfer pricing abuses. The economists' earlier study was cited in the March State Department report. The professors say they expect to complete their research this year.

**'I'd like to see just a small dose of patriotism with some of these companies,' Senator Byron Dorgan says.**

"We have to get on top of corporate accounting and manipulation of corporate books for the sole purpose of reducing taxes," says U.S. Senator Charles Grassley, 70, a Republican from Iowa and chairman of the Senate Finance Committee. "It's not any different than going overseas to set up a shell corporation. That is a shell game."

As long as U.S. companies are permitted to use loosely defined transfer pricing rules, massive tax evasion will continue, Dorgan says. "The IRS is staggering around in a fog here," Dorgan says. "They don't have a ghost of a chance of addressing these issues. And the growth in avoided taxes is scandalous."

Companies trading with their own foreign subsidiaries accounted for 46 percent of the $1.33 trillion in goods imported to the U.S. in 2001 and 31 percent of the $731 billion in exports that year, according to Commerce Department data. Under IRS rules in place since 1991, companies can negotiate with the IRS to determine transfer prices. Companies and the IRS sign contracts called Advance Pricing Agreements, which, like tax returns, are confidential.

"Transparency ought to be the name of the game," Grassley says. "There's got to be some check upon bureaucrats making decisions that lack oversight and the insight into public accounting. Obviously, it's not something that's very good the way it is."

The Caymans provide near-total financial secrecy for companies, banks and accounts. There are more than 500 banks and trust companies with deposits of more than $1 trillion in the Cayman Islands, according to the Cayman Monetary Authority. That's more deposits than there are in New York City, says Manhattan District Attorney Robert Morgenthau. The Cayman Islands are about one-third the size of New York City. "While some of this money may be there for legitimate purposes, much of it has been put there to avoid taxes and responsible regulation in this country," Morgenthau, 84, says.

The Caymans and its financial services industry profit from U.S. corporate accounts even while the Caymans collect no taxes. Cayman banks and related companies provide more than 10 percent of the islands' jobs, according to the government. The Caymans are home to about 200 licensed mutual fund administrators, who manage fund offices in the Caymans, more than 3,000 hedge funds, the Cayman Islands Stock Exchange and offices of the four largest international accounting firms.

In the Cayman Islands, the names of company officers, directors and owners are, by law, secret. The Caymans are home to about 40,000 residents and an equal number of foreign-owned companies. The only public information available from the government's General Registry is a company's local address and date of incorporation. That information can be obtained for $18 through a personal visit to the agency's public information counter on North Church Street, across the road from the harbor in George Town.

U.S. citizens are required to pay U.S. income tax on their earnings above $80,000 around the world, even if they live and bank in the Cayman Islands. If they don't pay U.S. taxes, they can be prosecuted for criminal tax evasion. More than 20 U.S. citizens have been convicted of tax evasion since 1996 after hiding money from the IRS in Guardian Bank in the Cayman Islands. John Mathewson, 76, the owner of the bank and a U.S. citizen, pleaded guilty to money laundering in August 1997. As part of a plea agreement with U.S. prosecutors, he turned over the names of more than 1,000 U.S. citizens suspected of using his bank to evade U.S. income taxes.


The Cayman Islands have about 40,000 residents and the same number of companies.

BRIAN SMITH

The rules are different for U.S.-based multinational corporations; they don't have to pay any U.S. taxes on profits earned from sales by their Cayman subsidiaries unless the money is brought back to the U.S. Under U.S. law, U.S. companies can use Cayman subsidiaries and transfer pricing rules to shift sales and profits from other countries, thus reducing their overall tax burden.

Four companies alone have accumulated a combined total of more than $75 billion in earnings untaxed by the U.S.: Hewlett-Packard Co., Merck & Co., Pfizer Inc. and Coca-Cola, according to their most-recent annual reports. Pfizer spokesman Paul Fitzhenry declined to comment. Merck spokesman Tony Polhoros says the company's decisions are in the best interests of U.S. employees and investors. "The earnings retained by our international subsidiaries include profits reinvested to expand our global sales," he says. Hewlett-Packard spokesman Brian Humphries declined to comment.

Atlantic Industries, the Cayman-based subsidiary of Coca-Cola that operates two factories in Ireland, exports more than $1 billion of its syrup annually, according to John Whelan, CEO of the Irish Exporters Association. Atlantic's profit, which isn't made public, is taxed in Ireland and not at all in the Caymans or the U.S.

## Cayman Contracts With Terrorist States

On April 13, 2003, President George W. Bush accused Syria of having weapons of mass destruction. "We believe there are chemical weapons in Syria," he said on the South Lawn of the White House. Secretary of Defense Donald Rumsfeld, appearing on CBS's *Face the Nation* the same day, said busloads of Syrians were sent to Iraq to kill Americans. "Reasonable people don't want to be associated with a state that's on a terrorist list," Rumsfeld said. "Who in the world would want to invest in Syria?"

Six weeks later, on May 31, Devon Energy Corp., an Oklahoma City–based oil and gas producer, entered a partnership with the Syrian government to spend $17 million to search for oil in Syria, according to company filings with the U.S. Securities and Exchange Commission. Theodore Kattouf, then U.S. ambassador to Syria, attended the contract signing in Damascus. Devon channeled the business through a Cayman Islands subsidiary.

Devon's work in Syria didn't mark the first time a U.S. company won a contract through a Cayman subsidiary in what the U.S. called a terrorist state. A Halliburton Co. subsidiary sold $33.6 million in products and services to Iran in 2001, according to filings with the SEC. Vice President Dick Cheney was chief executive officer of Houston-based Halliburton, an energy services and engineering company, from 1995 to 2000.

Iran is blacklisted by the U.S. as a terrorist state, which means U.S. companies are forbidden from accepting contracts from Iran. The Halliburton unit that won the contract in Iran was incorporated in the Cayman Islands and therefore wasn't subject to U.S. law, Halliburton says.

"All of Halliburton's business is clearly permissible under applicable U.S. laws and regulations," says Wendy Hall, a Halliburton spokeswoman. "If Congress decides to change the laws and provisions, Halliburton will, of course, comply."

Cheney spokesman Kevin Kellems says that before he was vice president, Cheney usually opposed economic sanctions. "He believed they were rarely effective and they often discriminated against American companies," he says.

In February, the U.S. Senate Finance Committee, chaired by Republican Charles Grassley, sent a letter to the Treasury Department asking if Halliburton was being investigated for violating U.S. sanctions. The committee also wrote letters to ConocoPhillips and General Electric Co. asking about their revenue from terrorist states, including Iran and Syria.

"If these companies are going through the backdoor to invest in terrorist nations, Congress must take action to immediately close, lock and seal those doors," said Senator Max Baucus, 62, of Montana, the senior Democrat on the committee.

The Finance Committee didn't challenge Devon's contract with Syria. Congress and President Bush put restrictions on U.S. companies working in Syria—such as barring exports from the U.S. to Syria, except for food and medicine—without banning them from working in that country.

"We entered Syria with the support of the U.S. government," says Brian Jennings, 43, Devon's chief financial officer. Jennings says that by using a Cayman subsidiary in Syria, the company can finance that operation with profit earned in China without first paying U.S. taxes on it.

Halliburton is the 30th-largest military contractor, with fiscal 2001 federal contracts of $534.2 million, according to a March study by the General Accounting Office, the auditing arm of Congress. Halliburton has 13 subsidiaries in the Caymans, two in Liechtenstein and two in Panama.

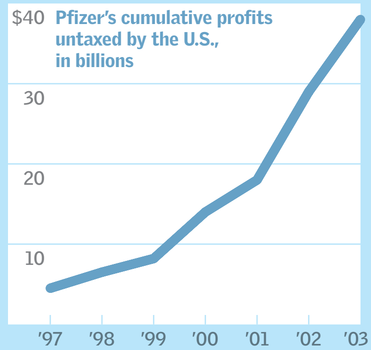
General Electric, the world's largest company by market value, has sold locomotives in Syria; in Iran, it sold medical equipment, provided oil and gas services and contracted to build hydroelectric generators, according to the Senate Finance Committee. ConocoPhillips, the largest U.S. oil refiner, runs a gas processing plant in Syria, the committee said. "We comply strictly with U.S. law in sales to Iran," says GE spokesman Gary Sheffer. "If Congress decides to change the law, we'll comply."

ConocoPhillips spokesman Sam Falcona says the company talks with U.S. officials to keep up with the rules. "We are in full compliance with the letter and spirit of U.S. laws," he says.

DAVID EVANS

Coke's Cayman subsidiary exports soft-drink concentrate to 75 countries on four continents, including China, Japan and Russia, according to Coke's annual report. By declaring its intent never to repatriate $8.2 billion of foreign profit to the U.S., Coke has avoided paying any U.S. taxes on it. Instead, the company reinvests the profit overseas through such units as the Cayman subsidiary, according to its annual report.

**Tax relief** Pfizer has amassed almost $40 billion in offshore profits.




Source: Company SEC filings

Atlantic Industries' investments include partial ownership of two of the world's largest independent Coca-Cola bottlers: Athens-based Coca-Cola Hellenic Bottling Co., which operates in 26 countries—including Greece, Italy, Nigeria and Russia—according to its annual report, and Mexico City–based Coca-Cola Femsa SA, which operates in eight Latin American nations—including Argentina, Brazil and Mexico—according to its annual report. The profit from those investments isn't taxed in the U.S. because Atlantic is based in the Caymans, and the money isn't returned to the U.S.

With the offshore tax savings and other tax breaks such as losses on Latin American investments, the company's effective U.S. tax rate was reduced to 20.9 percent for 2003, according to its annual report. Coke's tax savings came as the company's board of directors—which includes Warren Buffett, 73, the world's second-richest person—told shareholders in its annual report that it had scaled back work in high-tax nations, firing a total of 3,700 employees in the U.S. and Germany last year. Buffett declines to comment, his assistant Debbie Bosanek says.

Buffett's Berkshire Hathaway Inc., an insurance and investment company, has no Cayman subsidiaries. Berkshire paid $3.8 billion in U.S. taxes in 2003, or 32 percent of its earnings, SEC filings show. In his annual letter to shareholders in March, Buffett said the Bush administration was wrong to let U.S. companies play accounting games with the tax code and avoid U.S. taxes. "Today, many large corporations—run by CEOs whose fiddle-playing talents make your chairman look like he is all thumbs—pay nothing close to the stated federal tax rate of 35 percent," Buffett wrote.

## 'As an American, I hate to see it happen,' says one fund manager. 'As a shareholder, I favor lowering taxes.'

Berkshire Hathaway, Coca-Cola's largest shareholder, owns 200 million shares, or 8.2 percent, of Coke, valued at about $10 billion.

Citigroup Inc. says in SEC filings that it would have to pay $1.8 billion in U.S. taxes if it brought back $5.8 billion it keeps offshore. Oracle says it would have to pay $691 million in taxes if it brought home $3.1 billion that escaped U.S. taxes abroad. Other companies, such as Apple Computer Inc., drugmaker Schering-Plough Corp. and Intel, say they can't figure out how much they would owe.

Intel runs its largest microchip manufacturing site outside the U.S. in Leixlip, Ireland, on a former stud farm. The $5.5 billion plant is owned by Cayman subsidiary Intel Ireland, spokesman Mulloy says. The 360-acre site has 4,700 employees. Mulloy says 70 percent of Intel's sales are made outside the U.S. He says the company is legally keeping its tax bill as low as it can. Intel had accumulated $7 billion in overseas earnings not taxed by the U.S. as of Dec. 31, 2003, SEC filings show. Mulloy says Intel's foreign earnings never taxed by the U.S. helped pay for the Ireland plant's construction. "Generally, we try to use the cash we generate offshore for offshore purposes," he says. By investing offshore earnings outside the U.S., Intel can legally avoid paying U.S. taxes.

Intel's then vice president of tax, licensing and customs, Robert Perlman, 60, told the U.S. Senate Finance Committee in March 1999 that Intel would have been better off incorporating in the Cayman Islands when it was founded in 1968. "Our tax code competitively disadvantages multinationals simply because the parent is a U.S. corporation," Perlman testified.

Dorgan says that perspective is unpatriotic. "Well, maybe he should just change the language and say if we can find ways to not support our country and our government through the paying of taxes, our company would like to do it," Dorgan says. "I'd like to see just a small dose of patriotism with some of these companies because they do well as American companies, they're protected by our military, they access all our transportation, our education facilities and so on. They want all the benefits of American citizenship except that of paying taxes."

Parmalat, Italy's largest dairy company, filed for bankruptcy in December after saying one of its Cayman subsidiaries didn't actually have $4.9 billion Parmalat had previously told investors it did. Parmalat used the Cayman shell companies to create billions of dollars of nonexistent assets, Parmalat said in December. They included Epicurum, a hedge fund that supposedly held an investment from Parmalat valued at more than $600 million. In fact, the fund existed on paper only and was worthless, Italian prosecutors say. Also Based at Ugland House was Bonlat Financing Corp. Parmalat said it had falsely told investors that subsidiary possessed billions of dollars of certificates of deposit at Bank of America.

Enron, the world's largest energy trader until 2001, set up 441 companies in the Cayman Islands as part of a massive accounting fraud, according to Senate investigators. Former CEO Jeffrey Skilling was charged with federal criminal fraud and is awaiting trial. Former Chief Financial Officer Andrew Fastow pleaded guilty in federal court to securities fraud in January and was sentenced to 10 years in prison.

Cindy Scotland, executive director of the Cayman Monetary Authority, the independent agency charged with policing financial institutions on the island, says the Caymans have stiffened regulations in the past three years. The government enacted tough anti–money laundering laws that include possible jail terms for lawyers and accountants who don't report money laundering, created an independent monetary authority to oversee financial institutions, mandated licensing for securities dealers and required more identity and background information from anyone opening a bank account, she says. Financial scams, such as those by Parmalat, rarely originate on the island, she says. "None of that fraud was actually created here," Scotland says. She says no jurisdiction could ever entirely prevent fraud.

Even so, the Caymans have agreed to provide information only upon request of U.S authorities. Strict Cayman secrecy laws remain in place, says Reuven Avi-Yonah, professor of international tax law at the University of Michigan Law School in Ann Arbor. "The likelihood U.S. officials would know what to ask for is very low," he says.

Maples and Calder, the largest law firm on the island, is headquartered in Ugland House. Law books on a shelf in the boardroom include the five-volume set *Money Laundering, Asset Forfeiture and International Financial Crimes* by Fletcher Baldwin Jr. (Oceana Publications, 1993). Litigation partner Andrew Jones, 54, says the firm set up five Parmalat-related entities at the law firm's address.

As for U.S. tax revenue, fraud isn't the culprit; abuse of the laws is, says Douglas Shackleford, a business professor at the University of North Carolina in Chapel Hill. U.S. multinational corporations will continue to legally stash profits overseas, out of the IRS's grasp, unless the U.S. changes the rules of the international tax game, he says.

"As long as there's a Cayman Islands, there'll always be some guys who'll give you secret banks and no taxes," Shackleford, 45, says. "They're the leak in the bucket."

Until the U.S. removes incentive for companies to shift income to low-tax or no-tax places, companies like Coca-Cola and Intel will have little reason to change their strategies.

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BLOOMBERG TOOLS

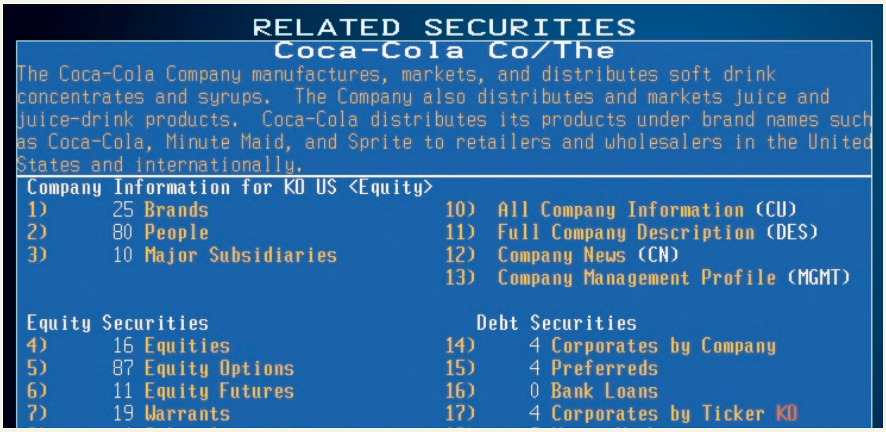
## A Closer Look at Offshore Subsidiaries

Twelve of the 30 companies in the Dow Jones Industrial Average have subsidiaries in the Cayman Islands, according to filings with the U.S. Securities and Exchange Commission. Type INDU <Index> MEMB <Go> for a list of the index's members, including their percentages of weight in the index, numbers of shares in the index and last price quotes. Click on a ticker, such as KO UN for Coca-Cola Co., and select DES from the pop-up menu for a description of the company. Type RELS <Go> for a menu of related securities, as shown below, and then type 3 <Go> for a listing of some major subsidiaries.

In addition to the Dow members, 24 of the 100 largest contractors with the U.S. federal government have subsidiaries in the Caymans, according to the General Accounting Office, the auditing arm of Congress. Type USLE <Go> and click on General Accounting Office to access the GAO's Web site for information on its reports and other publications. Type ITAX <Go> for a menu of Web sites related to U.S. income taxes, including the U.S. Internal Revenue Service and U.S. Department of Treasury sites.

Company filings with the SEC show that in addition to gaining tax benefits, incorporating in the Caymans can help a company avoid U.S. securities laws intended to protect investors. To access filings for a specific company, type the ticker followed by <Equity> CF <Go>. For example, type FDP US <Equity> CF <Go> to list Fresh Del Monte Produce's filings.

MARY K. WOOD




For a map of the Caribbean, type MAPS <Go> 14 <Go>.