*THE ROLE OF OFFSHORE FINANCIAL CENTRES IN GLOBALIZATION

by

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Abstract

Capitalism is inherently crisis-ridden, but shows little sign of exhausting itself. It continues to develop new ways of reinvigorating itself and generating economic returns for capital. Globalisation is considered to be the most advanced phase of capitalism. The Offshore Financial Centres (OFCs) are an integral part of globalisation. They facilitate growing mobility of finance by facilitating no/low tax, no/low regulation, secrecy and anonymity to enable footloose capital to roam the world. Their policies play a key role in tax avoidance/evasion, money laundering, flight of capital, degradation of regulation, instability and economic underdevelopment, and have serious consequences for people everywhere. Professional intermediaries, such as accountants and lawyers, play a key role in the development and expansion of OFCs. Despite the veneer of liberal democracy, some OFCs are captured by the finance industry and advance the interests of financial capital. Many OFCs are nurtured and protected by leading Western hegemons with developed capital and financial markets. This paper encourages scholars to study the operations, functions, policies and politics of OFCs by drawing attention to their significance and impact on societies.

THE ROLE OF OFFSHORE FINANCIAL CENTRES IN GLOBALIZATION

INTRODUCTION

Capitalism is a crisis-ridden, but a dynamic economic, social and political system (O'Connor, 1987). Far from exhausting itself, it continues to develop new and novel ways of reinvigorating itself and generating returns for capital. 'Globalization' is considered to be the most advanced phase of capitalism (for a review see Waters, 1995). Whilst scholars disagree about its extent, significance and direction, there is considerable agreement that relatively easy mobility of finance across porous territorial boundaries, with the aid of information technologies, is central to the processes associated with contemporary forms of capitalism (Leyshon and Thrift, 1997). Offshore Finance Centres (OFCs; also known as tax havens) play a key role in facilitating growing mobility of finance and shaping complex webs of interactions and relationships involving the nation-states, multinational corporations, a wealthy elite and ordinary citizens (Hampton, 1996; Hampton and Abbott, 1999; Picciotto, 1999; Hampton and Christensen, 2002).

Since the 1980s, the number of OFCs has doubled from about 30 to more than 60[1]. Most (but not all) are sparsely populated small island states, or enclaves in Europe[2], the Americas[3], Indian Ocean[4] and Australasia[5] (see Financial Stability Forum, 2000; International Monetary Fund, 2000). Many are British Crown Dependencies, or former colonies, and are generally protected by Western hegemons with major capital markets. In the absence of major industries, abundant natural resources, or marginalisation in the world markets, many smaller states have traded their sovereignty to facilitate mobility of capital. The OFCs are characterised as jurisdictions that attract a high level of non-resident financial activity. These include, to a varying degree, low/zero taxes on business or investment income, no withholding

[1] The exact number depends upon definitions (for some issues see Blum, 1994; Doggart, 1997; Diamond and Diamond, 1998; Musalem and Luca, 1999)
[2] For example, Gibraltar, Guernsey, the Isle of Man, Jersey, Liechtenstein, Switzerland, Luxembourg, Malta and Monaco.
[3] For example, Aruba, the Bahamas, Belize, Bermuda, the British Virgin Islands, the Cayman Islands, Netherlands Antilles and Turks and Caicos.
[4] For example, Mauritius and Seychelles.
[5] For example, Cook Islands, Nauru, Marshall Islands.

taxes, light and flexible incorporation and licensing regimes, light and flexible regulatory regimes and flexible use of trusts and other special corporate vehicles. Corporations and financial institutions can trade without having any physical presence. Their affairs are protected by strictly enforced secrecy and anonymity laws (Financial Stability Forum, 2000; International Monetary Fund, 2000). In OFCs, the volume of non-resident business substantially exceeds the volume of domestic business[6]. The OFCs secure global business through the provision of trust and company administration and specialised services, involving banking[7], shipping, corporate consultancy, structured financial transactions, insurance and mutual fund administration. Companies and wealthy individuals claiming 'residence' in tax havens rarely physically locate or trade there, but the 'brassplate' facilities enable them to avoid taxes and regulations of host countries.

The anonymity, low taxes and light regulations instituted by the OFCs are attractive not only to capital escaping territorial jurisdictions, but also to speculators and criminals (UK House of Commons International Development Committee, 2001; United Nations Office for Drug Control and Crime Prevention, 1998). The OFCs hold about 50% of all the cross-border assets (IMF, 2000). Almost one-third of the world's Gross Domestic Product (GDP) and half of global monetary stock passes through tax havens at some stage (Oxfam, 2000; Errico and Musalem, 1999; Cassard, 1994). US corporations and a rich elite have deposited some $800 billion in the Cayman Islands alone (or some US$20 million for each person living there), representing nearly 20% of all the bank deposits in the USA[8]. The OFCs are hosts to some US$6 trillion of wealth (UK Home Office, 1998), nearly ten times the value of all companies quoted on the London Stock Exchange. Much of the money is booked through shell companies, which conceal the destination of cash and the identity of its true owners.

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[6] The term 'offshore' is not necessarily restricted to tiny or remote islands. It can also be applied to any location (e.g. New Jersey, Delaware, City of London) that seeks to attract capital from non-residents by promising low/no taxes, low regulation, secrecy and confidentiality.

[7] In offshore locations banks are generally exempt from "reserve requirements, banks transactions are mostly tax-exempt, or treated under a favourable fiscal regime, and they are fee of interest and exchange rate restrictions. Moreover, in many cases, offshore banks are exempt from regulatory scrutiny with respect to liquidity or capital adequacy. Information disclosure is also low" (Errico and Musalem, 1999, p. 6)

[8] Evidence to the US Senate's Permanent Subcommittee on Investigations on 18 July

The activities of offshore financial centres enable capital to increase its rate of return, but also have major economic, social and political consequences for people in other jurisdictions. They are considered to be a threat to the global financial system because of a "greater leeway for balance sheet management, granted by favourable regulatory frameworks in OFCs, makes offshore banks potentially more vulnerable than onshore banks to solvency and foreign exchange risk" (Errico and Musalem, 1999, p. 4). In the words of Hutton and Giddens (2000), "They distort the global economy, allow the rich to avoid taxation and also help authoritarian regimes. So many dire political leaders and oligarchies have bled their countries dry by siphoning off funds abroad. Tax havens, countries with anonymous bank accounts and so forth are deeply implicated in this" (page 38). The OFCs have "undermined national governments' abilities to impose higher taxes both on individuals and companies, has facilitated money laundering, and other illegal activities, and has weakened the power of both national and international supervisory bodies to regulate the financial system" (Hampton, 1996, p. 2; also see Organisation for Economic Co-operation and Development, 1998**).**

The OFCs offer a window for studying contemporary forms of capitalism and globalisation. Their policies renew dynamism of capitalism but also have consequences for distribution of wealth, jobs and development of social infrastructure in other jurisdictions. This paper is organised into three further sections. The first section draws attention to the operations and policies of OFCs that facilitate tax avoidance, economic underdevelopment and financial crime. The policies of OFCs raise questions about their governance, local politics and regulation. Therefore, the second section provides a case study relating to Jersey, a UK Crown Dependency, protected by the UK government. It is implicated in numerous episodes of flight of capital, moneylaundering and tax avoidance. It also hired its legislature to enable major accountancy firms to write their own laws on auditor liability (Cousins et al., 1998, 1999; Morris and Stevenson, 1997). The third section concludes the paper with a summary and discussion. It also suggests ten areas of research to enrich debates about OFCs and globalisation.

2001 (http://www.senate.gov/~gov_affairs/071801_psimorgenthau.htm)

OFFSHORE FINANCIAL CENTRES IN A GLOBALISED WORLD

The emergence of OFCs has a complex history (Palan, 2002; Doggart, 1997). Some (e.g. Switzerland) have a long history of facilitating banking secrecy, which others (e.g. Bahamas, Liechtenstein, Montevideo; Luxembourg; also Delaware, New Jersey) have sought to emulate (Robinson, 1995). Others (e.g. Liberia, Panama) provided escape from regulation (e.g. for shipping) in various onshore jurisdictions (Carlisle, 1981). Some emerged because of interstate rivalries and novel interpretations of taxation laws (Picciotto, 1992). The nation state's attempts to control domestic economy inevitably gives rise to some discontents. In this environment, some smaller states (Liechtenstein, Monaco) have traded their sovereignty to attract and shelter 'hot money' (Robinson, 1995). Lawyers associated with Mafia drafted the financial legislation of some of the Caribbean havens (Naylor, 1987). Nevertheless, the emergence and expansion of OFCs is best understood within the dynamics and contradictions of capitalism. The policies pursued by major western states to simultaneously constrain capital (e.g. through domestic regulation) and encourage its global development have created the space for the emergence of the OFCs.

Ever since its inception, capitalism has been a dynamic economic system seeking out new opportunities for making profits. In search of higher economic surpluses, lower costs/taxes, compliant regulation and new markets, capital (aided by numerous agents) roams the world. Nearly 150 years ago, Marx and Engels observed that "The bourgeoisie cannot exist without constantly revolutionising the instruments of production, and thereby the relations of production, and with them the whole relations of society. ….. Constant revolutionizing of production, uninterrupted disturbance of all social conditions, everlasting uncertainty and agitation distinguish the bourgeois epoch from all earlier ones. All fixed frozen relations, with their train of ancient and venerable prejudices and opinions, are swept away, all new-formed ones become antiquated before they can ossify. All that is solid melts into air, all that is holy is profaned ….. The need of a constantly expanding market for its products, chases the bourgeoisie over the whole surface of the globe. It must nestle everywhere, settle everywhere, establish connexions everywhere. … All old-fashioned national industries have been destroyed or are daily being destroyed. They are dislodged by

new industries, whose introduction becomes the life and death question for all civilized nations ….” (Marx and Engels, 1998, p. 6).

In advanced capitalism, the liberal state plays a major role in fostering the conditions for capital accumulation in both the domestic and international spheres. It is dependent upon the revenues (e.g. taxation levied upon wages, profits, expenditure) generated by 'private' capitalist enterprises for its own survival. However, the capitalist economic system (national and global) is marked by an inherent 'crisis. Therefore, to create confidence in the system, the state is obliged to enact a wide variety of crisis-management processes (e.g. investigate corporate failures/frauds, protect property rights, control crime, regulate/deregulate, impose social obligations) for the long-term interests of capital (Offe, 1984; Habermas, 1976). Capital needs and depends upon various forms of state regulation to maintain the conditions of accumulation, to manage crises, to rationalise market excesses, to liberalise domestic economies, and smooth the way for international capital investment at home and abroad.

Domestic politics endeavours to keep capital and economic activity under control, not merely to protect the interests of citizens, but also to facilitate and foster the conditions in which private accumulation can flourish. Such policies, however, do not constrain the globalizing logic of capital. The footloose capital, wherever possible, seeks to gain competitive advantage by conducting business under conditions of confidentiality and secrecy, with minimum public disclosure and accountability, in accommodating jurisdictions that ask few questions but provide political stability. Such processes are aided by a variety of professionals (e.g. accountants, lawyers) who play a 'creative role' in structuring transactions and strategies to secure optimal economic advantage for capital. Professionals are highly rewarded for constructing new legal ways of avoiding regulation, costs and taxes (McCahery and Picciotto, 1995). They place novel interpretations upon the fluid concepts of territorial boundaries, legal personality, business entities, residence, domicile, citizenship and nationality to enable capital to escape domestic politics and shelter in favourable offshore jurisdictions (Picciotto, 1999).

Since the late nineteenth century, under pressure from major corporations and their wealthy owners, nations began to accept the principle that 'flags of convenience' could be granted to ships doing business in other nations (Carlisle, 1981). Some shipping companies exploited this to legitimise payment of low wages, avoid regulation (e.g. liquor prohibition laws, health and safety laws) and taxes. Since the 1920s, the U.S., the UK and Scandinavian companies have used Panama and Liberia to register their ships and establish 'residence'. As a result, according to the contemporary concepts of 'residence' and 'domicile', the shipping profits could not be taxed in the US or the UK and payment of dividends to non-residents could be made without the deduction of a withholding tax. After the Second World War, the new generation of oil tankers bringing crude oil from the Middle East, were mainly registered in Panama, Liberia and Honduras. They guaranteed anonymity to owners and zero taxation for foreign earnings of companies registered there. Of course, ships had no physical contact with Panama or Liberia, since they were permanently at sea and their trade remained elsewhere. Nevertheless, by placing novel or 'fictitious' interpretations to the legal concept of 'residence', the companies and their owners were able to claim exemptions from the UK/USA laws.

The late nineteenth century rulings by British courts had considerable impact on business tax liabilities and the emergence of tax havens (Picciotto, 1992; 1999). In particular, the courts held that where companies traded abroad but were controlled by individuals belonging to a governing body (e.g. board of directors) based in England, the companies were considered to be 'resident' in England and therefore liable to pay taxes in England on their global income. This aggrieved some shareholders and directors who financed the companies but did not live in England. Soon they manufactured situations where companies traded in England but were not controlled by a governing body based in England. Thus under the rules of 'residence' they escaped British income and corporate taxes. The court rulings had an impact not only on Britain, but also on the jurisdictions (and traditions) of the countries making up the British Empire. Such ideas have been enthusiastically followed and developed by many tax havens keen to secure business (in the form of registration fees) by providing 'residence' to companies. By the 1920s, the principle was further extended by Switzerland, which added banking secrecy and the provision of offshore corporations, and "dummy" directors to become a major location for asset protection.

The legal fiction was that the companies were Swiss and thus protected by Swiss laws, but their assets were located in foreign countries and the companies mainly traded with non-residents (Faith, 1982).

Since the 1920s, wealthy UK, Canadian and US citizens have formed offshore trusts and holding companies in the Bahamas and the Channel Islands to protect their wealth from taxes (Picciotto, 1992, 1999). From the 1920s, to escape local solvency and minimum capitalisation requirements, major transnational corporations (TNCs) formed captive insurance companies in offshore locations, such as Bermuda and the Cayman Islands. This enabled them to avoid taxes and regulation and generate considerable cost savings (Hampton, 1996). Such trends have continued to the present day. After the Second World War, American TNCs assumed a powerful role in exporting capitalism and rebuilding the economies shattered by war. The US government was not keen to permit companies to export capital and stifle the domestic capital markets and investment. Therefore, the investment abroad was often in the form of loans and retained earnings to finance local expansion. The profits of foreign subsidiaries were only subject to US taxes when repatriated as dividends. Such tax exemptions financed investment abroad and also encouraged companies to develop a creative network of fictitious subsidiaries for minimising tax liabilities at home and abroad (Picciotto, 1999). The subsequent tax treaties between various nations permitted TNCs to deduct charges for interests and costs for managing companies, before any tax obligations could be worked out. With the acceleration of Foreign Direct Investment (FDI), a large number of jurisdictions began to offer facilities to TNCs to avoid taxes and regulation. From the 1950s, a number of small islands states, often lacking natural resources and unable to compete with larger nations for economic resources, began to offer suitable facilities to companies.

In the 1960s and 1970s, many US banks formed branches in tax havens to book Eurocurrency loans and avoid US taxes and regulation of capital flows (Hampton, 1996, p. 17). During the 1960s and the 1970s, the US attempts to regulate capital (for example, by imposing capital controls, cash reserve requirements on demand deposits and capped interest rates on time deposits) played a significant role in emergence of offshore interbank market (Cassard, 1994). The emulation of similar controls by major industrialised nations further expanded the offshore market ((Errico and

Musalem, 1999, p. 16). The expansion of OFCs was further aided by the emergence of the Eurodollar market. By going offshore, companies and wealthy individuals could avoid onshore securities and exchange control laws. Banks operating from tax havens could also make savings by avoiding the need to maintain reserve ratios. The lower regulatory requirements resulted in less staff and further savings in operating costs. The mobility of capital was further aided by the collapse of the Bretton-Woods fixed-exchange rate system and relaxation of exchange controls on movement of capital.

OFFSHORE FINANCIAL CENTRES AND GLOBAL MOBILITY OF CAPITAL

Tax Avoidance

The avoidance of taxes enables capital to raise or maintain its rate of return. Armies of accountants and lawyers, charging £400-£500 an hour, devise tax avoidance and evasion schemes to enable major corporations (and the rich) to avoid UK taxes through nominee companies and offshore trusts. They assist in the setting up and fronting of bank accounts, shell companies and trusts in tax havens. As one tax expert put it, “I have never come across any reason for people to set up an offshore trust other than to avoid UK tax. The people who used them saved very substantial sums” (The Times, 10 July 2000).

In some OFCs, banks which are no more than “closets with computers” (Financial Times, 26 May 1998, p. 7) can be formed for a capital of just £500 (Euromoney, 1 Feb 2002) and move money around the globe, with ease. Companies can be formed with no fuss and bank accounts can be opened with e-mails and minimal checks. Local nominees can easily be found to front shell companies, or ‘brassplate’ operations[9] and enable companies to establish ‘residence’ or meet some other qualification and opt out of taxes from their home country or countries where they substantially trade. Places like the Cayman Islands are attractive because they have a developed banking and financial centre, but no income tax, corporate, inheritance, or

[9] The tiny island of Sark (part of the Channel Islands) does not permit motorcars on its single road, but its 575 residents hold more than 15,000 nominee company directorships between them. One Sark resident is a director of 2,400 international companies (UK Home Office, 1998, para 11.2.3; The Guardian, 20 November 1998,

property taxes[10]. There is no requirement for companies to publish any financial information. George Town, the capital of Cayman Islands is the world's fifth largest banking centre. It boasts nearly 600 banks and trust companies, including 47 of the world's largest 50 banks, though only 50 actually have a physical presence there. Only 31 banks are authorised to trade with the residents of the Cayman Islands. The island has some 45,000 registered companies whose only business is outside the country[11].

Monaco, with an area of 476 acres, is the home of numerous millionaires. It does not have any income, wealth, capital gains or inheritance taxes and tax evasion is not considered to be an offence. It is virtually impossible to trace transactions to Monaco's 340,000 bank accounts as the government strictly enforces its banking secrecy laws and does not co-operate with other countries. Tax avoidance schemes manufactured in Monaco are costing Britain some £1 billion each year in lost tax revenues (The Observer, 24 November 2002).

Belize is best known as the home of Lord Michael Ashcroft, a member of the UK's House of Lords. It entices US companies and citizens by stating that "… judgments of U.S. Courts are not recognized in Belize. …. the consequences of marriage or divorce are not recognized or enforceable in Belize. …. the claims of creditors in an insolvency are not recognized in Belize. … there are NO TAXES of any kind whatsoever assessed on offshore Trusts or International Business Company's formed in Belize. …. there is no annual reporting required of any kind whatsoever. …. there is no minimum capitalization requirement for a Belize Trust or International Business Company. …. you can be completely anonymous while maintaining complete control over your offshore Trust or International Business Company [12]". For only $1,500 International Business Companies (IBCs) can be formed to establish residence and

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p.4).

[10] Its revenue is primarily derived from 20% import duty and fees for facilitating secretive bank accounts.

[11] Long Term Capital Management, a business which speculated on stock and financial markets and collapsed with billions in debts is incorporated in the Caymans but managed out of offices in Connecticut (The Times, 22 July 2000). To prevent investors from losing their money and creating a domino effect, the US Federal Reserve spent some US$3.5 billion to bail it out.

[12] http://eclientservices.com/ (accessed on 6 December 2001).

enable companies and wealthy individuals to avoid taxes and regulation in their host countries[13]. The Belize government granted a 30-year lucrative tax concession to Carlisle Holdings, the company operated by Lord Ashcroft. The company has little trade in Belize. It provides staffing, cleaning and security services to corporate and municipal organisations, including some Hollywood studios. Carlisle's tax-free status in Belize has saved the company an estimated £13.7 million since 1997 (Financial Mail on Sunday, 20 January 2002, p. 5; The Guardian, 25 July 2001, p. 10).

The OFCs facilitate wealth transfers from citizens to capital and a wealthy elite. Consider the case of News Corporation, the corporate empire of Rupert Murdoch. The Murdoch empire operates from a web of some 800 subsidiaries, many registered in offshore tax havens, such as the Cayman Islands, Bermuda, the Netherlands Antilles and the British Virgin Islands. These places ask no questions, promise secrecy and have no requirements for public filing of audited financial information. For the four years to 30th June 1998, it generated pre-tax profits of A$5.4 billion but paid tax of only A$325 million, an effective tax rate of only 6% (The Economist, 20 March 1999, pp. 83-84). A major reason for this is the establishment of 'residence' in offshore tax havens with artificially low taxes.

In Britain, the Murdoch empire includes newspapers such as *The Sun*, the *Sunday Times*, *News of the World* and *The Times* and the satellite television station BskyB. A trawl through the 101 subsidiaries of the UK holding company Newscorp Investments for an 11-year period to 1998 shows that the business had profits of some £1.4 billion, but paid little or no British corporation tax. At the going British corporation tax rate of 30%, Newscorp Investments should have paid tax of more than £350 million, large enough to abolish tuition fees for university students (The Guardian, 21 July 2001, p. 1), to finance seven new hospitals, or build 50 secondary schools, or 300 primary schools (The Economist, 20 March 1999, p.83-84). By making use of offshore tax havens, Newscorp Investments paid virtually no corporation tax in Britain[14].

[13] In common with other OFCs, Belize raises revenues by levying annual registration fees on companies.

[14] A secret international task force of investigators, involving tax investigators from Australia, UK, Canada and the USA, was set up to examine why Newscorp pays virtually no tax. The politicians fearful of a backlash in the Murdoch owned newspapers backed-off and did nothing (The Independent, 4 February 1998, p. 1 and

Newscorp has not done anything illegal. It is certainly not alone in using 'residence' in offshore tax havens to reduce its tax obligations. Richard Desmond owns a huge publishing and sex empire. His business includes the *Daily Express*, *Sunday Express* and the *OK!* Magazine, *Asian Babes* and *Channel X*. His two main UK holding companies Northern & Shell Group and Portland Investment Limited are owned by trusts in Guernsey, a Channel Islands tax haven. For the period 1992 to 1999, their combined turnover was £301 million, with gross profits of £91 million and net profits of £5.6 million. The audited accounts show that the companies paid a total of £200,000 in tax, an effective rate of only 3.6%, one-tenth of the 30% UK corporate tax rate (The Observer, 24 December 2000, p. 18).

Companies do not just book their profits in OFCs, they also use offshore facilities to save on payroll taxes as well. Barclays Capital, the investment arm of Barclays Bank, paid its staff bonuses through a complex offshore structure. The scheme, believed to be developed by PricewaterhouseCoopers[15], pays annual bonuses to staff through Abacus Corporate Trustee Limited; a Jersey based company (The Telegraph, 14 November 2002). The employees in the scheme appear to forego bonuses in return for units, priced at 1p each, but redeemable at £100 over a ten year period. The scheme does not save employees any tax, but saves employers some 12% of the payroll taxes.

Rugman (2000) notes that there are "3,600 [US] corporations located in the US Virgin Islands and in Barbados with only a few dozen employees processing invoices" (p. 32). This enables them to claim 'residence' and reduce their tax bills and thus compete on advantageous terms with their international competitors. Companies such as Boeing, Caterpillar, Chevron, Daimler-Chrysler, Eastman Kodak, Exxon, General Motors, Microsoft and others, have set up skeleton operations in offshore havens to enable them to slash their tax bills (Rugman, 2000, pp. 22-23). By creating nearly 900 subsidiaries in offshore tax havens in places such as Cayman Islands, Turks and Caicos, Mauritius, Bermuda and Barbados, Enron wiped out its American taxes and

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[15]Offices of Ernst & Young and Coopers & Lybrand (now part of PricewaterhouseCoopers) were raided by the UK's Inland Revenue as part of its criminal investigations into tax avoidance schemes, often involving offshore

reduced taxes on its overseas operations in India and Hungary. In the US, Enron paid taxes in only one of the years from 1996 to 2000 (New York Times, 17 January 2002).

In the US, nearly a quarter of the top 500 companies paid no tax in 1998 (New York Times, 17 January 2002; Daily News, 18 January 2002). 135 of the top 250 companies paid tax at less than half the going rate (McIntyre and Coo Nguyen, 2000). Some US companies use offshore havens to enact aggressive transfer pricing policies. A favourite tactic is to over-invoice imports and under-invoice exports, resulting in tax savings of some $53 billion each year (Pak and Zdanowicz, 2002). Most tax avoidance/evasion schemes involve the use of offshore companies, trusts, artificial transactions and clever financial engineering.

The offshore activities give capitalism new dynamism and generate additional profits, but also leave major social scars. They do not enable elected governments to eradicate poverty, fight environmental degradation, finance education, healthcare, pensions and much needed social infrastructure. Germany is estimated to be losing some US$15 billion in tax revenues annually to undeclared personal savings held in offshore bank accounts (Christensen and Hampton, 1999). The US is estimated to be losing some $70 billion of tax revenue[16] each year due to offshore hidden assets, large enough to finance free healthcare for all US citizens. A report by Deloitte & Touche, taking account of tax avoidance schemes run by companies and wealthy individuals, estimates that Europe may be losing £100 billion a year of tax revenues (Financial Mail on Sunday, 25 November 2001, p. 10). Britain may be losing around £85 billion (Mitchell and Sikka, 2002) a year in tax avoidance/evasion (that amounts to a lot of hospitals, schools and pensions).

Economic Underdevelopment

Offshore tax havens facilitate economic underdevelopment by encouraging tax avoidance and flight of capital. They facilitate novel business vehicles, such as the International Business Company (IBC) and tax-exempt companies, to enable

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companies (The Times, 20 October 1997, p. 48).

[16] Evidence given by US Senator Carl Levin to the Permanent Subcommittee on Investigations on 18 July 2001(http://levin.senate.gov/floor/071801cs.htm);

companies to book their profits in OFCs even though they have little business in those offshore havens. The secrecy and poor regulation in OFCs enables corrupt leaders and businessmen to steal money and stunt the economic development of their countries.

The use of offshore tax havens by global corporations is depriving developing countries of some $50 billion of tax revenues each year[17], large enough to free them from foreign aid, rising debt and poverty. According to Oxfam (2000) "Tax havens provide companies and wealthy individuals with a way to escape their tax obligations. This limits the capacity of individual countries to raise revenue through taxation, both on their own residents and on foreign-owned capital. This undermines the ability of governments in poor countries to make vital investments in social services and economic infrastructure upon which human welfare and sustainable economic development depends. It also gives those TNCs which are prepared to make use of international tax avoidance opportunities an unfair competitive advantage over domestic competitors and small and medium size enterprises. The offshore world provides a safe haven for the proceeds of political corruption, illicit arms dealing and the global drugs trade, thus contributing to the spread of globalised crime and facilitating the plunder of public funds by corrupt elites. This contributes to increasing criminality and hampers the development of transparent budget processes in poor countries. ….. The offshore system has contributed to the rising incidence of financial crises that destroy livelihoods in poor countries. Tax havens and OFCs [Offshore Financial Centres] are now central to the functioning of global financial markets. Currency instability and the rapid surges and reversals of capital flows to developing countries have become defining features of global financial markets in recent years and have contributed to financial crises. Following the recent crisis in East Asia, the Indonesian economy underwent a severe contraction and the number of people living in poverty doubled to 40 million" Oxfam (pp. 1-2).

By liberalising their economies, countries also embrace the full effects of tax havens. Following the collapse of communism, Russia has been encouraged to embrace market capitalism and facilitate movement of capital. For every dollar of inward investment during the 1990s, it lost between ten and twenty dollars to offshore

[17] This does not take account of tax evasion, under reporting of profits or the use of

accounts held by a wealthy elite (Christensen and Hampton, 1999). The Russian economy has been crippled by the flight of some £16.5 billion each year to tax havens (The Times, 9 June 2000). The US Treasury claims that some "$70 billion left Russia in 1998 for offshore accounts in Nauru[18], which has 10,000 people, one main road and 400 banks"[19].

It is estimated that in 1999, corrupt political leaders stashed away US$20 billion in Swiss bank accounts, where secrecy is guaranteed (The Economist, 16 January 1999). In 1997, the Pakistani authorities tried to sequester the assets of £940 million from its former premier, spread out in nine countries, including Switzerland. Part of the money was alleged to be a bribe from a Swiss company *Cotecna Inspection SA*, a wholly owned subsidiary of *Societe Generale de Surveillance*, a company that helps developing countries to avoid fraud and evasion of taxes (Financial Times, 23 September 1997). In Mexico, the former President's brother has been convicted of taking large bribes from drug traffickers. The proceeds were laundered through banks based in Switzerland. The assets frozen in Switzerland amounted to $132 million. More accounts were probably held under assumed names (The Economist, 16 December 1995).

Money Laundering

According to the United Nations Office for Drug Control and Crime Prevention (1998), "The common denominator in money-laundering and a variety of financial crimes is the enabling machinery that has been created in the financial havens and offshore centres" (p.8). According to law enforcement agencies, "modern economic crime - the kind that ruins lives and destabilises countries – necessarily involves money laundering, which in turn, requires bank secrecy[20]. You cannot avoid money laundering if you have bank secrecy. It is inappropriate for international lawyers and bank regulators, especially in the offshore banking system, to defend in the abstract

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transfer pricing to siphon off profits and tax obligations.

[18] Nauru is located in the South Pacific. It measures eight square miles, requires no disclosures and has no taxes (The Guardian, 14 July 2001).

[19] http://www.cnn.com/2001/World/asiapc/auspac/06/25/nauru.laundering/index.html, accessed on 23 August 2001.

[20] The Isle of Man claims to have no secrecy laws, but banking licence holders have a duty of confidentiality to their customers (The Times, 28 September 2001, p. 31).

that which is in reality used to corrupt the public and private lives of major industrial nations" (John Moscow, Deputy Chief of Investigative Division, New York District Attorney's Office, quoted in Cahill (1997).

According to some observers, “Trusts in the offshore haven in Central America are among the most secretive financial instruments in the world, making Belize the ideal place for today’s buccaneers to bury their treasure” (The Times, 25 November 1999). By sheltering behind Monaco’s banking secrecy, Red Mafia has used banks in New York to launder £6 billion of hot money (The Times, 7 February 2000). Banks in London and the Isle of Man have been part of a very elaborate US $7 billion moneylaundering operation (The Times, 18 February 2000). The secrecy provided by the Marshall Islands (measuring 30 miles long and 400 yards wide) has also enabled the Russian Mafia to launder money (The Times, 30 September 2000).

Offshore companies in Switzerland and Gibraltar, established by UK chartered accountants were used to pay bribes to officials to secure cable-laying contracts for telephone and television (Serious Fraud Office Report 2000/2001, pp. 36-37). In another case involving Gibraltar, former City broker Lewis Daulby and Lee Rosser, one-time precious coins dealer, set up Cavendish Wine Merchants in 1994. It offered private investors opportunities to buy stocks of alcohol products as an investment. Investors were tempted with promises of very high returns (18% per annum) which never materialised. The business cash was transferred to Gibraltar and a new company was registered in the Dutch Antilles. Daulby and Rosser were sentenced to prison for five and seven years respectively for fraud (Serious Fraud Office Report 2000/2001, pp. 31-34). Switzerland’s secrecy and concerns for the ‘private’ interests of the rich enabled the Nazis to hide their gold for more than 50 years (The Times, 30 September 2000.). Former Nigerian dictator General Sani Abacha stashed away $4 billion by using banks in Switzerland and London (The Times, 15 October 1999; 5 September 2000).

Accountancy firms have used the secrecy provided by offshore places to launder money. Mitchell et al. (1998) document a case where accountancy firms used 27 companies registered in London and offshore jurisdictions to launder money. Robert Morgenthau, New York District Attorney, told (18 July 2001) the US Senate’s

Permanent Subcommittee on Investigations that a Big Five accountancy firm enabled a crooked debt to set up a shell company in Antigua. The shell company went under the name of Merlin Overseas Limited. There was no actual physical business in Antigua and it consisted of little more than a fax machine in a Caribbean office of Price Waterhouse. "The firm's employees served as managers and directors of the company. The payments arranged by the accounting firm on behalf of the crooked debt trader included bribes paid to a New York banker in the name of a British Virgin Islands company, into a Swiss bank account; bribes to two bankers in Florida in the name of another British Virgin Islands corporation and bribes to a banker in Amsterdam into a numbered Swiss account" (cited in Mitchell and Sikka, 2002, p. 15). "This accounting company was complicit", said Robert Morgenthau[21]. "They facilitated hiding of bribes that were paid to bank officers, and they provided the officers and directors for those phoney companies" (New York Daily News, 10 January 1999).

More than $1.5 trillion a year (roughly equal to the Gross Domestic Product of France) is estimated to be laundered, much of it through tax havens that ask no questions and rarely co-operate with international regulators (Financial Action Task Force, 1999; Mitchell et al., 1998; Mitchell et al., 2002). This enables some entrepreneurs to avoid regulation, taxes, undermine governments, and weaken the citizen-state contract. The proceeds can also be used to recruit private armies, fund gangsters, prostitution, and narcotics and undermine social order. This inevitably raises questions about the politics, regulation and governance of OFCs.

JERSEY: A CASE STUDY

Footloose capital just does not escape to any old jurisdiction. It seeks out locations that offer political and economic stability and pliability to enable it to present a respectable public front. In an uncertain global world, it seeks out jurisdictions that are protected by major hegemons, but have the appearance of being independent and autonomous. It wants locations that appear to be open and democratic, but whose regulatory arrangements are not too demanding. One such place is the island state of

[21] Morgenthau asked Price Waterhouse in Manhattan for help in reaching the people behind Merlin, but the help was not forthcoming. They were told that the Price

Jersey (part of the Channel Islands), a British Crown Dependency (or a British Overseas Territory). The UK government refers to Jersey as the "top division" of offshore financial centres (UK Home Office, 1998), but it has been criticised by the Organisation for Economic Co-operation and Development (OECD) for engaging in 'harmful' tax competition (OECD, 1998). Others claim that it is flying the "flag of fiscal freedom (or piracy)" (The Times, 27 June 2000, p. 23) and is a 'pariah' state (Jersey Evening Post, 30 October 1998, p. 2). It is frequently implicated in episodes of tax avoidance/evasion and financial crime (Mitchell and Sikka, 2002) and has hired out its legislature to accountancy firms to enable them to write their own legislation, shielding them from lawsuits (Cousins et al., 1998, 1999; Mitchell and Sikka, 1999; Morris and Stevenson, 1997).

A focus upon the governance and regulation in Jersey enables a deeper appreciation of the politics of globalisation, mobility of capital and the kind of political stability that footloose capital so craves. This next section sketches out some aspects of the governance of Jersey.

Jersey: The Island

Jersey is located 14 miles (20 km) from the coast of France and 100 miles (160 km) south of mainland Britain, and is just a forty-five minutes flight from the City of London, a major international financial centre. The island has a population of nearly 87,000 (Jersey Evening Post, 23 October 2001) and a total area of 45 square miles, (9 miles x 5 miles) or 116 km square.

Jersey is neither part of the UK nor a member of the European Union (EU) and is therefore not subject to any British and/or European Union laws. The UK has, however, negotiated a special status to enable Jersey to enjoy favourable trading terms with the EU, but without the commensurate social, economic and political obligations. Under the constitutional arrangements, "the United Kingdom Government are responsible for defence and international relations of the Islands, and the [UK] Crown is ultimately responsible for their good government. It falls to the Home Secretary to advise the Crown on the exercise of those duties and responsibilities. The United

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Waterhouse in Antigua is not the same legal creature as the one in New York.

Kingdom Parliament has the power to legislate for the Islands, but it would exercise that power without their agreement in relation to domestic matters only in most exceptional circumstances" …. "[The UK] Parliament does have power to legislate for the Island without their consent on any matter in order to give effect to an international agreement" (Hansard, House of Commons Debates, 3 June 1998, cols. 471 and 465).

Since the 1960s, Jersey has actively adopted measures to turn itself into an offshore tax haven (Hampton, 1996). It is now the home of some 40,000 registered companies (and numerous unregistered trusts), the large majority of which are tax-exempt or subject to special non-resident tax regimes (UK Home Office, 1998). It boasts financial deposits of some £400 billion, but many of the businesses are "brass plate" operations formed to avoid taxation and regulation in other countries. There is no requirement for companies to publish audited accounts. Jersey has no inheritance or capital gains tax. It offers 20% income tax, but in reality the wealthy can negotiate a far lower effective rate of tax, or devise schemes to avoid any payment (Mitchell and Sikka, 1999). Some "wealthy residents have admitted …. that they have not paid income tax for a number of years" (Jersey Evening Post, 29 August 2001).

Jersey provides special business vehicles such as the tax–exempt companies and International Business Companies (IBCs) to enable multinational companies to book their profits and pay low taxes at rates ranging from 0.5% to 2% on income generated outside the island (Jersey Evening Post, 20 March 2002, p. 33). A former economic adviser to the Jersey government said, "I sat across the table and negotiated a mutually acceptable tax rate with the bank's representatives. The bank was seeking to book £600 million in profits after a one-year trial. At the end of the meeting they agreed to book £60m in the first year at a tax rate of 0.5 per cent. Such meetings were not uncommon and were conducted in complete secrecy" (The Observer, 17 November, 2002).

Agriculture and tourism once dominated the Jersey economy, but have increasingly been displaced by the finance industry[22]. The fees levied upon the finance industry

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[22] "Finance has eaten away at this Island [Jersey] like the first little black and white

may be providing as much as 90% of the government revenues (Hampton and Christensen, 2002). In the race to the bottom, in November 2002, to match the announcements by the neighbouring islands of Guernsey and the Isle of Man, Jersey announced that it would cut corporation tax rate for non-resident companies to zero (Jersey Evening Post, 22 November 2002; 25 November 2002). This reduces the government's revenues by some £200 million, but it hopes that more companies would register in Jersey to make good the projected shortfall.

Governing Jersey

Jersey has universal suffrage and a system of government that bears the hallmark of liberal democracies. Most noticeable features are the absence of general elections and 'opposition' in parliament, easily available record of major parliamentary debates, overlapping business and governmental interests, concentration of power, and the absence of various checks and balances commonly found in liberal democracies. Experienced observers say that "For over a century Jersey's ruling elite has had an unchallenged monopoly of power ...... With no clear division between the legislature, judiciary and executive there is an absence of checks and balances" (The Independent, 22 November 1998, p. 23). In the words of a former senior civil servant, "the Island had no real democracy, the States could no longer govern effectively, politicians and civil servants lacked an understanding of economic fundamentals, and government incompetence 'smacks of corruption' to most ordinary residents" (Jersey Evening Post, 6 April 1999). Some claim that "Jersey is an Island that until two decades ago lived off boat-building, cod-fishing, agriculture and tourism. It is run by a group who, although they form a social and political elite, are mostly small business owners and farmers who now find themselves overseeing an industry of global scope involving billions of dollars. By and large..... they are totally out of their depth" (Wall Street Journal, 17 February 1996.

Jersey has a single chamber Parliament, the States of Jersey. It consists of 53 directly or indirectly elected members, plus representatives of the UK Crown. There are 12 Senators, 29 Deputies and 12 Constables. Jersey's 12 Senators are elected on the

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computer game, Pacman, to the detriment of other Island staple industries" (Jersey Evening Post, 31 October 1998, p. 11).

Island wide basis for a six-year term, and half of these retire every three years. The 12 Constables are the civic heads of one of the Island's 12 parishes. They are not elected on any common electoral cycle. The roles and constituencies of various elected representatives overlap. At no time are all the members of Jersey states simultaneously elected i.e. there is no general election. Recent elections show that voter apathy (or satisfaction) is high. In the 1999 elections, some constituencies had a turnout of just 1% (Jersey Evening Post, 22 November 1999, p. 10) and some Members of the States were returned unopposed (Jersey Evening Post, 3 November 1999).

The UK Crown appoints the Lieutenant Governor, the "military commander" of the Island, now a liaison between the UK Crown and the Jersey States. Under the constitution he has a right of veto if Crown interests are involved. Jersey States also has other UK Crown appointees, such as the Bailiff (always a male lawyer), the Deputy Bailiff, the Solicitor General, the Attorney General and the Dean of Jersey (head of the Anglican Church in Jersey). The Bailiff, Sir Philip Bailhache, besides being the Speaker and the President, is also the President of the Royal Court. He is the leading judge on the Island. He hears major legal cases and represents Jersey on economic and external relations matters. His brother, William Bailhache, is the Attorney General and prosecutes cases in the courts presided over by the Bailiff[23].

Jersey does not have political parties and the machinery that goes with them. Thus there is no coherent programme of reform, or contestation of government policies. Individuals seeking to be elected do so as independent candidates rather than as members of political parties though some candidates form mutual alliances. At election times, they are not entitled to equal free access to radio or television, or free

[23] In sharp contrast to the legal principles established by the January 1999 House of Lords' judgement in *re Pinochet* (http://www.parliament.the-stationery-office.co.uk/pa/ld199899/ldjudgmt/jd990115/pino01.htm), the Bailiff claims that "there is no risk of bias by his presiding in a prosecution that has been brought by his brother, the Attorney-General" (Jersey Evening Post, 16 March 2000. p. 4). The Bailiff's role has been problematised by the judgement of the European Court of Human Rights in the case of *McGonnell v The United Kingdom* which argued that who has a direct interest in the passage of legislation should not judge any case concerning the application of that legislation.

mail shots. The manifestos seem to be more about 'personality politics'[24] than about financial, global, or tax issues. The independent election candidates are no match for those with close connections with big business as it can always find someone to distribute the election leaflets.

To oversee the £400 billion finance industry, part-time members of the Jersey States are entitled to a salary of £27,781 and expenses of £9,276 to cover telephone, postage and transport costs (State of Jersey, 2001; Jersey Evening Post, 28 November 2001, p. 2). Whilst pursuing their business interests, they meet, on average 3-5 days a month. They are poorly resourced and lack researchers to support them in their efforts to scrutinise the policies of the executive. They could be advised and briefed by pressure groups and new social movements (e.g. environment, trade unions), but pressure groups are not well organised. Campaigners for change are easily ostracised by the ruling elite. Jersey's only newspaper, the *Jersey Evening Post* (JEP), is owned by a senior member of the government with considerable local economic and political interests. The local radio and television, also finds it easier to follow the official line and rarely subjects the government to critical scrutiny (Mitchell and Sikka, 1999)

Instead of a Cabinet system of government, Jersey is governed by a Committee system. All members of the Jersey States are members of one or more of the 24 Committees (most committees have seven members, many committees also have sub-committees) governing the island. The public cannot attend their meetings, examine their agendas, minutes or policy papers. Each Committee (e.g. the Finance and Economics Committee) has a President (usually a Senator) who is the visible face (or a Minister) of power. All members of the Jersey States are effectively ministers or part of the executive. Due to these arrangements, Jersey has no official 'Opposition' in parliament and there is little effective scrutiny of legislation, policies or the government. Members of one Committee are generally reluctant (though there are some exceptions) to critically scrutinise legislation proposed by another. There is no equivalent to US Senate hearings or the UK Parliamentary Select Committees to scrutinise legislation or the executive. There is no written record of parliamentary

[24]For example, one Constable (elected unopposed) claimed that he "enjoyed low-water fishing and was well known in the farming community. He was known in the Island for his award winning dahlias" (Jersey Evening Post, 12 October 1999, p. 4)

debates relating to major Bills. Jersey States requires people to pay £10 for each audiocassette of the parliamentary debates.

All Jersey politicians are in business for themselves. They draft, refine and pass legislation. They have also sat on regulatory bodies, effectively acting as 'gatekeepers' adjudicating on complaints and malpractices. For example, Senator Frank Walker was a director of Barclays Bank and simultaneously President of the Finance and Economics Committee (FEC) i.e. the Finance Minister. He has also simultaneously the chairman of the Financial Services Commission (FSC), an authority responsible for regulating banking practices. In the Bank of Cantrade episode, one time President of the FEC, Senator Pierre Horsfall had been a non-executive director of the Bank (Hampton and Christensen, 1999).

The above governing arrangements provide political stability and respectability that global capital so much craves. Jersey’s ruling elite responds to criticisms by denying that there is any problem and then demonises reformers (Jersey Evening Post, 19 June 1996, p. 17; 22 October 1998, p. 8; 31 October 1998, p. 11; Mitchell and Sikka, 1999; Mitchell, Sikka and Willmott, 2001). However, external pressure and increasing visibility of Jersey in tax avoidance, money laundering, drug trafficking and regulation degradation (e.g. UK Home Office 1998, United Nations Office for Drug Control and Crime Prevention, 1998; Organisation for Economic Co-operation and Development, 1998) has potential to erode the respectability and stability that footloose capital so prizes. A PricewaterhouseCoopers partner said, “it is apparent that outside pressures have a far greater impact on the [finance] industry than was previously the case and, therefore, how our government responds to that pressure is of increasing importance[25]”. As a spokesperson for Jersey's finance industry put it, "First and foremost there has been demand to more effectively respond to the threat posed by external sources. It began primarily with the UK government and its announcement on Edwards [see below] and the review that followed. Since then, there has been the Financial Action Task Force, the European Union, the United Nations, and of course the OECD. There were also other 'thorns in the side' of the industry, including Austin Mitchell, MP, various university professors who seemed to have spent an inordinate

[25] http://www.thisisjersey.com/finance/finance_16.html, accessed on 17 September

amount of time studying the threats posed to the world from offshore jurisdictions, New York Police authorities, new pressure groups such as Attac, and at one time even past and present members of the States of Jersey! ..... this has forced a rethink both by government and the industry" (http://www.thisisjersey.com/finance/finance_30.html, accessed on 1 October 2001).

On 2nd March 1999, the States of Jersey formed a 'Review Panel on the Machinery of Government[26]' under the chairmanship of Sir Cecil Clothier to consider possible reforms[27]. Its terms of reference did not require any consideration of the role of Jersey in facilitating economic underdevelopment in other jurisdictions by encouraging flight of capital and global tax avoidance. Its recommendations[28] (published in December 2000) encouraged Jersey to legitimise its status by adopting some aspects of the Westminster model of liberal democracies. At the time of writing (February 2003), these are still being debated and so far none have been implemented.

The State of Financial Regulation

During the 1990s, Jersey attracted considerable negative publicity because of concerns about money laundering, banking frauds (Morris and Campbell, 2000; Hampton and Christensen, 1999) and non co-operation with the US law enforcement agencies[29] (The Observer, 22 September 1996, p. 19). It hired out its legislative

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2001.

[26] Jersey's ruling elite did not favour an independent inquiry, for example, through a Royal Commission (Jersey Evening Post, 30 June 1998) because "this would be an open invitation to people like Austin Mitchell and others who have no particular love for Jersey institutions to interfere in our process of government. ..... A Commission would be foolish, but doing nothing would also be foolish ......" (Jersey Evening Post, 7 July 1998, p. 3)

[27] The author gave written and oral evidence to the Clothier Committee.

[28] They seem to be concerned about the welfare of business. For example, the report notes, "Because of its post-war development as a modern financial services centre, Jersey today has amongst its population an unusually high proportion of well qualified business and professional people. In most cases, the nature and extent of their other commitments would deter them from seeking election to the States, but the more open pattern of policy determination we envisage here would afford them a better opportunity to contribute if they wished to the development of public policy, through the submission of evidence or even as special advisors to Scrutiny Committees" (States of Jersey, 2000, p. 39).

[29] As the New York Assistant District Attorney pursuing frauds by the now defunct Bank of Credit and Commerce International (BCCI) put it, "My experience with both

apparatus to Price Waterhouse and Ernst & Young to enable them to write the designer liability laws. A dissenter was 'indefinitely suspended' from parliament whilst another one was persuaded to leave the Island (Cousins et al., 1998; Mitchell and Sikka, 1999). The European Union (Hampton and Christensen, 1999) and the UK Parliament also urged the government to clean up the UK Crown Dependencies (UK House of Commons Public Accounts Committee, 1998). In anticipation of a blacklisting of Jersey by the OECD (OECD, 1998), the UK government, apparently without any prior consultation with Jersey[30], ordered a review[31] of Jersey's system of financial regulation[32].

Under pressure from the Jersey authorities, the review did not look at the system that facilitates tax avoidance/evasion for footloose capital. It ignored the social costs of Jersey's role as an offshore finance centre, even though the terms of reference mentioned 'economic well-being of the Islands themselves and the United Kingdom'. The civil service and courts play a crucial role in the drafting, enactment, implementation and enforcement of regulations relating to secrecy and the provision of tax-exempt business vehicles for non-residents. Yet they too were excluded from the inquiry. The UK government gave no undertaking to publish any detailed report, though a Home Office press release stated that "Although this is an internal review, we intend to publish a summary of its main findings" (press release dated 20 January 1998). However, following a widely reported leak[33], the UK government eventually

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Jersey and Guernsey has been that it has not been possible for US law enforcement to collect evidence and prosecute crime. In one case we tracked money from the Bahamas through Curacao, New York and London, but the paper trail stopped in Jersey and Guernsey ……. It is unseemly that these British dependencies should be acting as havens for transactions that would not even be protected by Swiss bank secrecy laws[29]" (The Observer, 22 September 1996, p. 19).

[30] The investigation also covered the entire Channel Islands and the Isle of Man.

[31] The review was carried out by Andrew Edwards, formerly a Director and Deputy Director at the UK Treasury and Chairman of the Whitehall Principal Finance Officers' Committee (UK Home Office Press Release, 20 January 1998).

[32] The Jersey establishment normally responds to such external pressures by claiming that the UK is interfering in its internal affairs (Financial Times, 22 January 1999; Morris and Campbell, 1999; Morris and Campbell, 2000).

[33] The report was leaked on the website of the Association for Accountancy & Business Affairs (AABA) and received considerable press coverage (for example, The Guardian, 26 September 1998, p. 1, 14 and 22; Sunday Business, 27 September 1998, p. 6; Financial Times, 12 October 1998, p. 9; Sunday Telegraph, 1 November 1998; Jersey Evening Post, 26 September 1998, p. 1; 5 October 1998, p. 1-2; 6 October

published the [Edwards] report (UK Home Office, 1998).

The report[34] (UK Home Office, 1998) contained over 150 proposals for reform and stated that Jersey lacked some basic financial regulation. For example, it did not have independent regulation of the financial sector, a depositor protection scheme, an independent ombudsman to resolve disputes, anti crimes legislation, adequate consumer protection laws, complaints investigation procedures, an ombudsman to adjudicate on complaints and protocols for co-operation with external authorities and much more. Jersey does not require companies to file audited financial information and regards this as a key magnet in attracting footloose international capital. Edwards recommended that "all limited companies … be required to keep audited accounts and to file them publicly, with much abbreviated requirements for small companies"(para 10.10.7). Edwards also applied this principle to asset holding companies, especially given the high risk that such companies could be exploited as vehicles for money laundering by non-residents (paras 10.10.10 -10.10.11).

With acknowledged financial deposits of some £400 billion, a small unit within the civil service regulated Jersey's financial sector. It simultaneously acted as promoter, defender, prosecutor, regulator and judge. The chief regulator was Senator Frank Walker, President of Jersey's powerful Finance and Economic Committee (Finance Ministry). In 1998, in anticipation of criticisms from Edwards, Jersey formed, what it claimed was an independent regulatory body, the Financial Services Commission (FSC). Senator Frank Walker remained its chairman until external pressure forced his

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1998, p. 6; The Isle of Man Examiner, 6 October 1998, p.1; Guernsey Evening Press, 6 October 1998, p. 1; Manx Independent, 9 October 1998, p. 5; The Money Laundering Bulletin, October 1998, p. 1 and 4).

[34] The report crafted in careful civil service language largely endorsed the status quo. It classified Jersey as in the "top division" of offshore finance centres without making any comment about whether this was good or bad. An open criticism would have acknowledged that Britain had failed to provide good governance of the island, and that the existence of tax haven like Jersey encouraged flight of capital and forced British people to pay higher taxes. The initial leaked version of the report was considerably more critical than the published report but was watered down following behind the scenes lobbying by the Island's politicians and civil servants (Willoughby, 1999; Morris and Campbell, 2000). It was warmly received by Jersey's ruling establishment. The tentative nature of the report was described by some commentators as "perilously close to a whitewash" (Morris and Campbell, 1999, page 63).

replacement[35] (Financial Times, 30 July 1998, p. 11).

Jersey (and many other tax havens) permits the use of nominee directors in respect of companies incorporated elsewhere and thus conceals the identity of the owners. Edwards suggests a three pronged attack. First, a regime of licensing and supervision applying the criterion that only "fit and proper" persons in terms of integrity, solvency, competence and track record be permitted to act as nominee directors. Secondly, a Code of Conduct for Directors which would, inter alia, require them to be aware of who owns the company, the nature of its business, its financial position and to have full and up to date information and ensure that the company is not being used for illegal purposes. Thirdly, as a general principle Directors should be obliged to refrain from holding an unreasonable number of Directorships, though no specific ceiling should be set. Annual returns would be required from those providing Directors' services specifying the ownership, place of incorporation and principal activities of the companies they serve as Directors (para 11.2.19).

Jersey's ruling elite was not happy with the proposed reforms and decided to 'cherry pick'[36]. It refused to accept "that all private companies should be required to prepare and publicly file audited accounts" (States of Jersey, 1999, para 3.11.2). In relation to offshore trusts, Edwards essentially endorsed their continued use as vehicles for tax avoidance shrouded in secrecy, and suggested a series of measures designed to safeguard the interests of beneficiaries. Despite this, Jersey claimed that the proposals were based on misconceptions of Jersey law and hence "unnecessary" (States of

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[35] In anticipation of criticisms from Edwards, Jersey created the independent Financial Services Commission (Financial Services Commission (Jersey) Law 1998). A commitment was made to hive off the promotional role to a separate distinct body (Jersey Financial Services Commission, 1998). A separate enforcement department has been created within the Commission entrusted with responsibility for all enforcement matters and co-operating with overseas' regulators (Jersey Financial Services Commission, 1999). But the FSC is full of political appointees. The majority of Jersey based representatives are composed of the retired Chief Adviser to the Jersey Government, with the remaining three drawn from the Island's legal, accountancy and banking "pinstripe" infrastructure, which earns its living off and is consequently in a client relationship with the offshore finance industry.

[36] Through discussions with the UK officials, Jersey was made well aware of the changes needed to secure removal from the OECD blacklist and started work on some aspects before the publications of the Edwards Report. When the report was published, it was able to claim that it was already voluntarily introducing changes.

Jersey, 1999). Rather than more stringent direct regulation of companies and trusts, Jersey promised to licence corporate and trust services providers and require them to accept a Code for the sound conduct of business. By March 2002, some 50% of the trusts operating from Jersey remained unlicensed (Jersey Evening Post, 15 March 2002, p. 19). As regards information about registration of foreign companies incorporated in Jersey, the government resolved to provide information on a restricted basis i.e. only to those "who need and wish to know" (States of Jersey, 1999, para 3.11.3). It agreed to hire just four additional staff to act as regulators and refused to repeal its confidentiality laws.

Under international pressure, Jersey has enacted the "All Crimes" money laundering legislation (The Proceeds of Crime (Jersey) Law 1998), which, on paper at least, will considerably facilitate international co-operation by Jersey in the pursuit of financial crime generally ((Draft International Co-operation) Jersey Law 2000). A Financial Crime Unit has been established but it falls a long way short of the blue-print specified by Edwards: it is a *police* unit composed of ten police officers, one customs official and a financial analyst to deal with financial flows of £400 billion. Nevertheless, Jersey introduced some reforms sufficient to enable it to come off the OECD's blacklist. Sponsors of international capital have further endorsed this respectability. For example, Jersey has been awarded a " Group 1" jurisdiction rating by the G7s Financial Stability Forum on the basis of its co-operation with other jurisdictions and the quality of its regulation (Pratt, 2000). At the same time, the influential US Bureau for International Narcotics and Law Enforcement Affairs has designated Jersey a jurisdiction of "primary concern". This means "the volume of money laundering continues to be substantial and continued vigilance and effective enforcement by the government is essential to successfully combat money laundering" (US Department of State, 1999), albeit tempered by the Bureau's praise by stating that "Jersey has developed a comprehensive money-laundering regime and has clearly demonstrated the political will to ensure that its financial institutions and services industry is not used to launder money. Jersey's key to success in preventing its offshore financial sector from being used to launder money will be in the continued force with which it implements the new legislation and regulations" (US Department of State, 2000).

Despite some reforms, secrecy and confidentiality facilitated by Jersey continues to attract footloose capital. For example, in 1999, the International Monetary Fund (IMF) launched an investigation after £30.4 billion of Russian money turned up at a small Jersey company called Fimaco (Financial Times, 12 February 1999, page 2). Fimaco was established for Russian clients in 1990 and administered by the local law firm, Ogier & Le Cornu, although in practice very little was done locally. Michael Birt, one of the partners in the firm, was (until 1994) one of the directors of Fimaco. His role was nominal, but the same Michael Birt subsequently became the Island's Attorney-General and is currently its Deputy-Bailiff. Despite being a director of the company, he denied any knowledge of the affairs of Fimaco. The director of Jersey's Financial Services Commission claimed that whilst Fimaco had done nothing illegal, it helped to "pull the wool over the eyes of the IMF[37]".

In April 2002, Jersey's Attorney-General refused to co-operate with a Spanish investigation into alleged irregularities in the affairs of Banco Bilbao Vizcaya Argentaria (BBVA), the countries second largest bank. It was alleged that BBVA held a number of offshore accounts which were excluded from its books for a decade (Jersey Evening Post, 12 April 2002). Jersey based company, Mahonia, is implicated in the opaque financial transactions involved in the collapse of the US energy giant Enron (Financial Times, 14 January 2002). Some £200 million of the cash stolen by the former Nigerian dictator, General Abacha, went through banks in Jersey (The Guardian, 5 October 2001, p. 12).

SUMMARY AND DISCUSSION

Capitalism is crisis prone, but remains a dynamic system. Far from exhausting itself, it continues to find new ways of reinvigorating itself and earning returns for capital. Globalisation and contradictory economic policies pursued by the nations-states have released capital from the prison of national territorial boundaries. Offshore tax havens play a key role in the global mobility of capital through competitive deregulation. They provide secrecy, low/no tax and low regulation to enable capital to roam the world. Accountants, lawyers and bankers play a key part in facilitating a creative use of the concepts of 'residence', 'domicile', 'jurisdiction' and legal personality. Nation

[37] http://jerseyeveningpost.com/99_09_28/news7.html.

states lose billions of pounds of tax revenues through carefully crafted tax avoidance schemes. Such taxes would enable populations, often on the edge of subsistence to develop local social infrastructure, education, clean water, sanitation facilities and healthcare, but multinational use fictitious 'residences' in offshore havens to deprive developing countries of tax revenues. In populist press, corrupt leaders are blamed for the plight of many developing countries. It rarely notes that the corrupt activities are facilitated by or encouraged by secretive tax havens protected by Western governments.

Rather than relating development and expansion to the globalising logic of capital, some have explained the emergence and development of the OFCs as a reaction to the high tax and high regulation regimes created in onshore jurisdictions. Such claims are problematic because OFCs have expanded during the time of deregulationist regimes (e.g. Thatcher, Reagan), abolition of exchange controls and reduced tax rates. For example, in Britain the top rate of income tax has been reduced from the punitive 1970s figure of 83% to the present 40%. Corporation tax has been reduced from 52% to 30%, the lowest ever. This has not curbed the mobility of capital or persuaded companies to pay up their share of designated taxes. As a result, the total tax take (as a % of the GDP) from business has fallen from 3.6% in 1996 to 2.8% in 2002 (The Guardian, 13 November 2002). In the US, in 1960, corporations paid 24% of all federal taxes, compared to 12% in 1996 and 8% in 2002[38]. The loss of taxes means that elected governments are unable to fund the desired social infrastructure and public services.

By registering in tax havens, multinationals are able to reduce their tax bills/costs, increase their profits/dividends and returns to stockholders. The host country raises some revenues (e.g. through low taxes or registration fees) to finance its local infrastructure. However, the value-added component of a transaction being routed through, for example, the Caymans Islands, does not lie with any wealth creating activity performed there. It nests instead in tax avoidance, or in the secrecy space afforded by routing the transaction through the offshore circuits (Hampton and Christensen, 2002). The cost of this is borne by citizens in other places. By claiming

[38] http://www.citzenworks.org (accessed on 7 December 2002).

‘residence’ in offshore havens, multinationals do not abandon markets and monopolies in other jurisdictions. Often money itself does not physically move to tax havens, it is merely booked there. They merely secure “fictional” residences in offshore places (Roberts, 1994) rather than de facto abodes. Despite huge amounts of finance passing through them, the OFCs are not associated with major advances in science, engineering, mathematics, electronics or education. Even the most successful ones, at best, play a supporting role to developed financial markets in London, New York and Tokyo. In essence, the OFCs are charging rents for enabling companies to incorporate and park their profits in those jurisdictions.

The offshore interface may attract little attention from accounting and finance scholars, but it plays a major role in flight of capital, global financial crises, transfers of wealth, increasing poverty and social inequalities. The IMF acknowledges that “Offshore banking has certainly been a factor in the Asian financial crises. It also played a significant, but not a catalytic, role in the recent Latin America crises. …. During the 1995 Argentine banking crisis, offshore establishments of Argentine banks a prominent although not a catalytic role in creating financial difficulties. Estimates of Argentine creditor and depositor losses from the failure of offshore establishments ranged from US$3 billion to US$4 billion ….. Most of the losses are attributed to shell branches in the Caribbean” ((Errico and Musalem, 1999, p. 4 and 36). In the early 1990s, Venezuelan bankers used some 3,500 offshore corporations in Aruba, Curacao and elsewhere to transfer capital, resulting in the collapse of one-half of the banks in that country, and a major disaster for the people, their savings, investments and pensions[39].

The secrecy and low regulation facilitated by OFCs also attracts money launderers and financial crime. Complex corporate structures and a labyrinth of transactions, nominees and uncooperative regulators are encountered in the processes that seek to trace the monies. In the words of a former assistant director of the UK’s Serious Fraud Office, “Tax havens are little more than booking centres. I’ve seen transactions where all the decisions are taken in London but booked in the tax havens. In my experience, all you get in return is obstruction of legitimate investigations” (Accountancy,

[39] http://www.senate.gov/~gov_affairs/071801_psimorgenthau.htm

December 1998, p. 21). Fraud occurs both onshore and offshore. The difficulty is that the offshore places are poorly regulated and lack the institutional structures to deal with it. The preoccupation with secrecy makes investigation and prosecution especially difficult since many of the offshore havens are dependent upon international finance which values secrecy.

The OFCs and the mobility of capital poses fundamental challenges to any notion of democracy. For example, citizens may elect governments with a mandate to make increased investment in healthcare, education, pensions and public services by increasing taxes on corporations and wealthy citizens. Such parties, whilst continuing to enjoy the social infrastructure, markets and profit making opportunities, can scupper government plans and policies by seeking shelter in the fictional spaces provided by OFCs and avoiding their share of taxes. The ability of multinationals to structure their affairs via tax havens also provides them with a significant tax advantage over their nationally or locally based competitors. Local competition, no matter whether it is more efficient or innovative than its multinational rival, will be competing on an uneven field. The logic of this uneven competition requires either that all businesses ultimately move offshore in order to compete on a level basis, or that onshore tax authorities adjust their tax policies to place a greater burden on other factors of production (particularly labour) and onto consumption (Christensen and Hampton, 2000).

The case of Jersey shows that the OFCs are protected by major Western hegemons. The veneer of liberal democracy helps to gloss over its 'capture' and dependence upon financial capital. The close relationship between big business and politics helps to provide the suffocating political stability that capital so craves. The fiction is that Jersey is an autonomous island state that is neither part of the UK, nor the EU. However, this in/out status is full of ambiguities. The UK retains powers to launch investigations into Jersey's affairs, appoint its head of state and also negotiate lucrative commercial arrangements for its benefit with the EU. In recent years, the UK government has sought to pressurise Jersey to reform its system of financial regulation and present a respectable face to the world (UK Home Office, 1998) rather than curb its role in facilitating flight of capital and global tax avoidance. The reform of tax havens requires multilateral co-operation. It is noticeable that the OECD

(OECD, 1998) is focusing upon 'harmful tax competition' rather than the liberalist ideology of competition that encourages flight of capital and global tax avoidance that is undermining developing nations and democratic choices made by citizens.

Finally, this paper would like to suggest ten possible areas for future interdisciplinary research.

1. The expanding power of the OFCs calls for fresh evaluations of the theories of the state. It is now commonly assumed that the liberal state legitimises the power of capital by imposing some social obligations upon it (e.g. taxes, need for major companies to publish audited accounts). However, the case of OFCs shows that the state avoids imposing regulation and taxes on capital to smooth its ability to amass economic surpluses. Indeed, the state goes to considerable lengths to facilitate secrecy and virtually no public accountability. Tax havens have been selling their sovereignty to financial capital. In return for fees for locating 'brassplate' operations, the OFCs also hire out their legislature to major corporations to enable them to draft desired laws (e.g. in Jersey, the limited liability partnerships legislation was drafted by Ernst & Young and Price Waterhouse). Major businesses have used these laws to squeeze concessions from other states (Cousins et al, 1998; Mitchell et al, 2002). The contradictions and tensions call for a review of the theories of the state.

2. Places like Jersey are protected and nurtured by the UK government. The UK government instituted inquiries to persuade Jersey to strengthen its system of financial regulation, but carefully avoided any focus on its role in global tax avoidance and subverting regulations in other places. It would be useful to document the way major states nurture and shield tax havens. Major nations certainly have powers to shackle tax havens. For example, after the September 11th, 2001 attacks on New York, the US government wanted information on the financial links of Osama bin Laden and his organisation. The trail pointed to the Bahamas. When a Bahamas bank refused to open its records, the U.S. had it cut off from the world's wire transfer systems and the bank changed its mind within hours (Daily News, 18 January 2002). However, the same political will is absent

in checking the global mobility of capital facilitated by tax avoidance/evasion, banking secrecy and regulation hopping.

3. It would be useful to develop case studies focusing upon the role of various OFCs in globalisation and their governance. This would help to increase visibility of a trade that receives little attention in accounting and finance journals.

4. Financial intermediaries (e.g. accountants, lawyers, bankers) play a key in constructing 'fictional spaces' of tax havens, exploiting tax loopholes and structuring transactions so as to avoid taxes and regulations. Yet little is known about how these professional intermediaries operate in offshore jurisdictions even though they indulge in dubious practices (Mitchell and Sikka, 2002). It would be helpful to document the role of accountancy firms in oiling the wheels of tax havens.

5. What is the impact of OFCs on developing countries? A report by Oxfam showed that the amount of tax avoided by major corporations in developing countries is roughly equivalent to foreign aid received by them. As a condition of financial support/loans, the World Bank and the International Monetary Fund demand that developing countries engage in 'structural adjustments', devalue their currencies and curtail subsidies for farming, food and other essentials. Yet these institutions have failed to examine the impact of tax havens and major corporations in stifling economic development of emerging economies.

6. What is the extent of tax avoidance by companies? It would be useful to develop models that estimate it. Another approach would be to examine published financial statements of global corporations and scrutinise the instances when they pay taxes at less than the going rate of corporate taxes. Such information could become a powerful catalyst for debates about wealth transfer, the corrosive effects of globalisation and provide counter information whenever governments claim to be unable to finance healthcare, education and public services.

7. How can major companies indulging in ingenious tax avoidance schemes be called to public account? The traditional accounting standards do not require

corporations to publish any information about tax avoidance schemes or aggressive transfer pricing policies, often routed through tax havens. Perhaps, concerned scholars would consider co-operating with NGOs and develop alternative accounting standards that privilege common social interests rather than the narrow economic interests of capital. The public provision of information has capacity to stimulate debates about democratic control of capital.

8. The case of Jersey suggests that ordinary people seem have received little benefit from its tax haven status. For example, the influx of financial capital has distorted the local housing market. In December 2002, modest starter homes were priced at £255,000, well beyond the reach of many young people. Despite huge wealth, there is no 'unemployment benefit' for the unemployed and "there appear to be large numbers of people who are having difficulty in paying for even the necessities of life" (Jersey Evening Post, 29 September 2001). Some "10,000 Islanders are living in relative poverty .... double the number estimated in 1996" (Jersey Evening Post, 12 February 2002). Since 1992, the local levels of pollution have increased by 11% (Jersey Evening Post, 10 January 2002). Seasoned observers note that "even minimal levels of consumer protection is conspicuous by its absence", and that the "Jersey consumer has long had a rough deal at the hands of certain unscrupulous businesses" (Jersey Evening Post, 9 January 2002). Jersey has done little to prevent "powerful companies from blackmailing the public" (Jersey Evening Post, 15 September 2001). It would be useful to document the effect of tax haven status on the local social policies.

9. Researchers should develop multilateral policies to shackle capital. Perhaps, no bank should be allowed to have brass plate operations anywhere in world. Where companies are avoiding taxes through artificial transaction and shell companies located in offshore havens, the host countries should levy taxes based upon estimated local revenues, market shares and profits. Those refusing to pay taxes should not be allowed to trade in the host jurisdictions, receive any government contracts[40] or public subsidies. Accountants and lawyers drawing up tax evasion

[40] On 31 July 2002, the US Senate voted to bar companies located in offshore tax havens from securing military contracts (New York Times, 1 August 2002).

schemes through artificial companies and creative financial transactions should be made personally liable for the lost taxes.

10. How might the power of OFCs in encouraging flight of capital, degradation of regulation and negatively affect the state-citizen contract in other jurisdictions be constrained or even curbed? Perhaps, they need to be given economic aid to develop alternative industries. The terms of the world trade could be restructured so that smaller states can develop niche markets. Perhaps, people need to take direct action by shunning the goods and services of banks and companies that hide behind secretive offshore operations.

The above proposals may do little to bring capital under the control of domestic and multilateral politics. However, they do have the potential to stimulate debates about globalisation and the role of OFCs in enabling capital to rampage all over the globe, pit one nation against another, nullify local democracy and destroy the lives of people everywhere.

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