

The Future of Financial Services in the Caribbean¹

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Were it not for the threat to the Caribbean's financial services sector posed by the OECD, I believe that the Caribbean would now be in a far more competitive position in the provision of global financial services than it was before.

Few can argue with any credibility that the anti-money-laundering regimes in all but a small number of Caribbean countries are not now entirely consistent with the highest international standards. Most of our jurisdictions are in full compliance with the criteria set by the Financial Action Task Force established by the G7 countries as a sister to the OECD.

The criteria for judging the compliance of jurisdictions were tough. They required a comprehensive review of laws, regulations and practices to ensure adherence to international best practices including rules for reporting and investigating suspicious activities, the requirement to know beneficial owners of bank accounts and international business corporations, and to share information on criminal matters.

In the case of my own country, Antigua and Barbuda, the Prime Minister, Lester Bird, established a Working Group, under my chairmanship, to study our arrangements against the FATF criteria and to recommend any changes required to our legal, supervisory and enforcement regime that might be necessary to ensure compliance. As a consequence of that work, Antigua and Barbuda overhauled many of its laws, strengthened its supervisory capacity and enhanced its investigative facilities. Subsequently, we were found by the FATF to be a fully co-operative jurisdiction in the fight against money laundering and we were never 'named and shamed' on its list. Other countries that were listed undertook the tough task of similarly overhauling their systems.

Undoubtedly, compliance with the FATF criteria has cost every Caribbean country dearly. Many financial institutions and international business corporations have left our jurisdictions because they did not like our new regimes, or we struck them from our registers for non-compliance

¹ This paper is based on a speech given by His Excellency Sir Ronald Sanders, Chief Foreign Affairs Representative of Antigua and Barbuda, to the PriceWaterhouseCoopers Conference on Financial Services Investment Practice held in Nassau, Bahamas, 7 September 2001.

with our new rules and regulations. Governments lost much-needed revenue from licence fees, and our economies also lost much-wanted jobs for our people. In addition, governments have faced increased costs by strengthening supervisory, regulatory and investigative mechanisms. But at the end of the day the countries that have complied with the FATF criteria have made themselves more reputable and reliable, and therefore more attractive to legitimate business. In the long run, it is legitimate business that will sustain our economies, provide jobs and increase revenue.

However, like the sword of Damocles, a threat still hangs over the financial services sector of the Caribbean, because of the so-called 'Harmful Tax Competition Initiative' of the OECD. But the Caribbean region is in a far better position today to resist that threat than we were a year ago.

Two principal factors have led to our strengthened situation.

The first is the universal recognition and acknowledgement of the considerable strides that several of our jurisdictions have made in establishing regimes to effectively combat money laundering and other financial crime. Today, the Caribbean cannot be described by any objective standard as a 'haven for crooks and money launderers'. Indeed, most of our jurisdictions are now in the forefront of the battle against money laundering with some of the most stringent legislation in the world on our books.

The second is the significant work done by representatives of our governments to sensitise the international community, including the new government in the USA, to the wrongness of the OECD's original initiative. That included much work to inform members of the US Congress and Senate and the new US Government of the serious flaws in the OECD initiative.

I believe it is true to say that the intervention of the US Secretary of the Treasury, Paul O'Neill, caused the OECD to amend its Initiative. While there were other countries, such as Canada, that earlier saw the wisdom of change, they lacked the strength to resist the domination of the OECD by the 15 EU countries who have been the driving force behind this scheme. These factors have led to a significant modification within the OECD of the so-called 'Harmful Tax Competition Initiative'.

We have now entered the final phase of an unfortunate confrontation between the OECD and over 30 jurisdictions around the world that they have targeted as so-called 'tax havens'. In less than three months time, on 30 November,² the OECD plans to 'name and shame' these jurisdictions

² *Editorial note:* The OECD deadline was extended to 28 February 2002 in November 2001.

as practising 'harmful tax competition' unless they publicly state their agreement to eliminate aspects of their fiscal arrangements that the OECD alone has determined to be harmful. If, by 30 April 2003 at the earliest, they have still not complied with the OECD's demands for changes in their fiscal systems, the 30 OECD member countries will apply sanctions against them as they see fit.

Originally, this 'naming and shaming' exercise was due to take place in 2000. But, in the wake of strong resistance from the targeted jurisdictions and an international campaign in which the matter was raised in almost every global forum, the OECD agreed to delay 'naming and shaming' until 31 July 2001.

In the interim, a Joint Working Group of OECD and non-OECD countries was established in January 2001 under the co-Chairmanship of the Prime Minister of Barbados, Owen Arthur, and the Australian Ambassador to the OECD, Tony Hinton. That Joint Working Group, of which I was a member, met twice, first in London in January 2001 and then in Paris in March 2001.

The point of the Joint Working Group was to try to seek ways in which confrontation could be avoided and the concerns of the OECD about what it called 'harmful tax competition' could be met in a mutually satisfactory manner. As a starting point, both sides in the Working Group agreed on the need to address three broad principles. These were: non-discrimination, transparency and effective exchange of information. However, that was as far as agreement went.

The OECD members of the Working Group expected the targeted jurisdictions to simply accept the OECD definition of these principles and, therefore, the manner in which they would be applied, while the non-OECD members anticipated that the three principles would be defined by agreement.

Further, the non-OECD members expected that the two sides would discuss the establishment of a truly international forum, in which all interested countries and institutions would be represented, to determine, in a democratic manner, how these three broad principles would be applied equally and universally with representative machinery for monitoring implementation and deciding on measures to address non-compliance by all countries, large and small.

The OECD countries, however, were adamant that its own ironically named Global Forum on Taxation would be the only forum in which the matter would be discussed. The only concession that they made to membership of the forum was that targeted jurisdictions would be allowed to

participate, but only after they had blindly accepted the OECD's definition of the three broad principles and publicly declared their acceptance. I need hardly say that the discussions were stalemated and the members of the Joint Working Group left Paris no nearer to resolving the impasse than when we started.

Amazingly to us, 17 questions which we posed to the OECD in written form, and which they promised to answer while we were in Paris, were still unanswered five months later when Ambassador Hinton, as co-Chair of the Joint Working Group, wrote to Prime Minister Arthur, the other co-Chair, to forward a set of responses. These 17 questions were designed to ascertain from the OECD whether or not its own member states would be bound by the same rules that were being applied to the targeted jurisdictions. The answers, none of which was plain and explicit, clouded the issues even more and gave rise to deeper suspicion about the motives behind the OECD's 'harmful tax competition' scheme.

In any event, the OECD decided to extend the deadline for 'naming and shaming' from 31 July to 30 November 2001 and to delay the imposition of sanctions until 30 April 2003 at the earliest when they would also be applied against their own defaulting members. In addition, according to the letter written by Ambassador Hinton to Prime Minister Arthur and circulated to the members of the Joint Working Group, the OECD has also decided to remove one of their criteria in naming a jurisdiction as a 'tax haven'.

One of the OECD criteria for deciding whether or not a jurisdiction is a 'tax haven' was whether or not it has a regime that facilitates the establishment of entities with 'no substantial activities' in the country. Such entities were regarded as 'ring-fenced' if the tax regime it enjoyed was available only to non-resident investors or if its activities were limited to international transactions. That criterion has now been eliminated.

Essentially what the OECD is now seeking from us is a commitment to two things. The first is effective exchange of information in both civil and criminal tax matters when it is relevant to a *specific* tax investigation or examination. According to the OECD, appropriate safeguards will be implemented to ensure that information is used only for the purpose for which it is sought.

The second is adherence to standards of transparency which the OECD has not attempted to define in their communications with our jurisdictions, but which has been detailed by US Treasury Secretary Paul O'Neill in a statement to a US Senate Committee.

The US Treasury Secretary says 'transparency means two things: (1) the

absence of non-public tax practices, such as secret negotiation, or waiver, of public tax laws and tax administration rules; and (2) the absence of obstacles, such as strict bank secrecy or the use of bearer shares, to obtaining financial or beneficial ownership information within a jurisdiction'.

Jurisdictions that make commitments to the OECD on these two matters will have a year in which to develop plans to implement them. The OECD would like commitments to these two matters to be made before 30 November 2001 when it plans to 'name and shame' jurisdictions by publishing a list of what it calls 'unco-operative jurisdictions'.

The OECD's communications have also indicated that OECD countries will not apply sanctions against non-OECD countries any earlier than they would apply such sanctions against their own members. No date has been given for the application of such sanctions, but in his statement to the Senate Committee, the US Treasury Secretary indicated that this would not be 'until April 2003 at the earliest'. On the face of it, the two matters on which the OECD is now seeking commitments may not appear contentious. Indeed, on the basis of the definition of transparency given by the US Treasury Secretary, none of our jurisdictions in the Caribbean should have any difficulty.

Certainly, none of our jurisdictions make secret tax deals with investors, nor is any government authorised to waive public tax laws and tax administration rules. With respect to strict bank secrecy or the use of bearer shares as obstacles to obtaining financial or beneficial ownership information, the new legislation and regulation established by most, if not all, our jurisdictions under our anti-money-laundering regimes ensure that there are no such obstacles.

With regard to effective exchange of information, under Tax Information Exchange Agreements or Mutual Legal Assistance Treaties, many of our jurisdictions already co-operate with some OECD countries, particularly the USA and Canada. Therefore, the principle of information exchange in specific cases where it is relevant to a tax investigation or examination is not a problem by itself. The real problem is that there is no clear or accepted international definition of what 'civil' means, and no explicit description of how the information would be exchanged. As usual, the devil may be in the detail, and jurisdictions will want to size up that demon before deciding to live with it.

The OECD also states that the two principles, exchange of information and transparency, will be focused on geographically mobile services, including financial services, shipping, distribution services, service industries and company headquartering.

In its communications, the OECD has indicated that jurisdictions that make a commitment will be invited to participate in the OECD's Global Forum Working Group which is addressing these two principles. As far as it goes, this appears a more reasonable proposition than the original 'Harmful Tax Competition Initiative' which attempted to dictate the tax economic systems and structures of other nations for the benefit of the OECD's member states. The original scheme sought to limit the authority of non-OECD governments and legislatures over their own countries' tax economic systems and structures through the constraints of a framework set by the OECD.

But a fundamental difficulty still remains. It is one that has far-reaching implications and it is by no means limited to this particular initiative of the OECD. The difficulty simply put is this. Should 41 jurisdictions around the world accept that the OECD has the right or authority to set itself up to make tax rulings which they expect non-members to follow? By doing this, would these 41 jurisdictions, targeted by the OECD as 'tax havens', not be opening the floodgates to a raft of other demands by an organisation with no authority except the coercive power of its member states?

We must recall that the OECD is a multinational grouping of 30 countries. It is not an international organisation and it has no legal authority to speak for the world or to establish rules, norms or standards for any state except its own members. Nonetheless, it is now dictating terms on what, in short, could be described as cross-border tax matters. Even with the helpful intervention of the new US Government, and the subsequent modification of the original initiative, the threat of sanctions has not been removed. In other words, the OECD is still determined to invoke economic power to force surrender wherever it meets resistance.

Recently, the OECD launched a wide range of papers on e-commerce to develop global approaches to a number of e-commerce issues including fiscal matters. One of the initiatives is to develop a new fiscal approach to indirect taxation of e-commerce. This will require non-OECD suppliers to register in each OECD country for indirect tax payments and to pay indirect taxation in each of the OECD countries to which they export goods and services through e-commerce. It is envisaged that this will create substantial hurdles for small developing country entrepreneurs seeking to use e-commerce to overcome market access barriers of distance and cost into major OECD markets. The EU countries would not be subject to such taxes within the EU boundaries due to harmonisation of indirect taxes. Hence this would mainly affect developing country e-commerce exporters.

In addition, the 1998 OECD report flagged that manufacturing industries in developing countries would be addressed later. Many of our countries give fiscal incentives and have special legal and fiscal regimes to attract investment to particular sectors such as hotels, export processing zones and manufacturing. The extension of the scope of the OECD initiative beyond geographically mobile services would affect most, if not all, our countries.

It is significant that in the summary of modifications to the tax haven work which the OECD has circulated to our jurisdictions, it continues to assert that the modifications do not 'affect the application of the 1998 Report' whose criteria for identifying tax havens 'remain unchanged'. This assertion emphasises that while the OECD has made a tactical withdrawal on one front, it has not abandoned the battlefield altogether and may be merely postponing a further onslaught until after it has secured an opening into our camp and weakened our capacity for resistance.

Our governments cannot disregard this important dimension of the problem. They will have to take serious account of it in reaching a decision about whether or not to make a commitment to the OECD on the two remaining aspects of the so-called 'Harmful Tax Competition Initiative'. By the same token, they will also have to carefully consider the consequences to their economies of the application of sanctions by the members of the OECD who are more important partners to us in financial services. The key players in this regard are the USA, Canada and the UK.

What Sanctions Would be Applied?

The US Treasury Secretary told the US Senate Committee that the work in the OECD to refine the identification of appropriate sanctions is still at an early stage, but that some of the measures already identified have been part of the international tax policy of the USA and other OECD countries for many years. They include enhanced audit and enforcement activities with respect to transactions and jurisdictions which may be used by their taxpayers to evade tax, and no tax treaties, such as double taxation agreements. This probably means that the recent financial advisories, applied to and then lifted from several of our jurisdictions after the FATF exercise on money laundering, would be reinstated. Mr O'Neill also pointed out that the sanctions envisaged by the OECD would require legislation in the USA and therefore would have to be approved by Congress.

The OECD currently has a team in the Caribbean which will be visiting several jurisdictions in an attempt to persuade them to make a commit-

ment to the 'harmful tax' project based on the modifications that have been made.

It should be noted that these modifications have not yet been approved by the OECD Council which does not meet until later this month. Indeed, the modified proposals that I have outlined have not yet been de-restricted by the Council. I suspect, therefore, that this is the first time that any Caribbean government representative is discussing the modified proposals with any section of the private sector. Yet, in less than two months, the OECD expects governments to make commitments which they have not had the opportunity to fully discuss in their countries with their social partners.

Representatives of OECD governments and the OECD Secretariat have assured me in several fora over the last few weeks that there will be no change to the modified proposals.

So, the question is – where do we go from here?

Let me say at the outset that my own jurisdiction, Antigua and Barbuda, is not a non-cooperative jurisdiction. Based on the consultations within the non-OECD members of the Joint Working Group, I feel I can say beyond fear of contradiction that all the targeted jurisdictions are ready and willing to co-operate with the OECD in trying to find a mutually acceptable way of dealing with the issues of exchange of information and transparency.

On 30 August, I met Ambassador Hinton of Australia, the co-Chair of the Joint Working Group of OECD and non-OECD countries, and representatives of the OECD Secretariat headed by Jeffrey Owens, the Head of the Centre for Tax Policy and Administration, specifically because I wanted to explore any avenues that might exist for taking this project forward in a co-operative manner.

They were anxious to point out to me not only the modifications that have been made to the Harmful Tax Competition Initiative, but also the fact that they were offering technical and capacity-building assistance to jurisdictions that made a commitment. I had to respond to them that technical and capacity-building assistance, while helpful, was more for their purposes than for ours. Of far greater importance to us would be measures that would encourage our jurisdictions to look more favourably on giving a commitment to the world's 30 richest nations. Essentially, from their standpoint, this project is about pursuing their taxpayers who, they believe, may be evading the payment of their taxes.

We do not know that their premise is correct. And, indeed, neither do they. For instance, US Treasury Secretary Paul O'Neill himself told the

US Senate Committee that ‘it is impossible to quantify precisely the extent to which US taxpayers are using offshore entities to evade their US tax obligations’. The information, he said, is ‘anecdotal’, but he believes that the ‘potential’ is significant.

The OECD is expecting our jurisdictions to institute measures and practices to facilitate a hunch that some of their taxpayers may be evading taxes. However, these measures may have the effect of causing perfectly legitimate activities to leave – or not come – to our jurisdictions simply because they want to maintain the privacy of their business. In other words, our financial services sector and our economies could suffer real hardship because of the desire by OECD countries to seek out possible tax evaders, rather than known tax evaders.

In my view the OECD project would have a better chance of success if the OECD countries were to demonstrate a readiness to deal effectively with the problems they create for our jurisdictions. For instance, the OECD could implement a number of confidence-building measures. Among these would be:

- ✧ A clear declaration that the OECD will shelve its 1998 Report which details arbitrary factors for identifying ‘tax havens’;
- ✧ A plain statement that the OECD will not extend the scope of the Initiative beyond geographically mobile services to include legal and fiscal regimes which attract investment;
- ✧ An invitation to all interested countries to join its Global Forum Working Group whether or not they make a commitment to transparency and effective exchange of information. In this way, the non-OECD countries would be able to see at first hand the nature and scope of the discussion and might be encouraged to join voluntarily and not by coercion. They could also make a constructive contribution to the elaboration of the two principles and their application;
- ✧ The unequivocal withdrawal of any list intended to name jurisdictions as ‘unco-operative’.

Such confidence building measures would demonstrate good faith by the OECD countries and would show that it has departed from its previously flawed process of forcing other countries to accept standards and practices unilaterally devised by the OECD.

The second measure that the OECD countries should consider is the establishment of double taxation treaties with jurisdictions that commit to transparency and effective exchange of information. Such treaties would help to attract investment and improve the economies of the tar-

geted jurisdictions. Again, this would show good faith by the OECD countries.

Whether or not the OECD would be willing to consider and implement these measures is anybody's guess. But we in the Caribbean should put it to them strongly as a condition of any commitment we might make now or later.

The OECD has a team touring the Caribbean trying to secure commitments in advance of the 30 November 2001 deadline for publishing its list of unco-operative jurisdictions. These conditions should be put to the OECD firmly, and governments should carefully consider whether to give any commitments before the OECD Council gives an undertaking to satisfy them.

It may be that the OECD will proceed to publish their list on 30 November on which the 35 jurisdictions will appear as non-co-operative in their harmful tax competition scheme. If they do so, they will be naming jurisdictions that have been recognised and acknowledged to be fully co-operative in the frontline of the battle against money laundering. We can hold our heads high on that score. Our collective transgression – if transgression it is – would be that we simply do not accept that the OECD has any legal right to unilaterally devise schemes that they seek to impose upon others in order to deal with their own taxpayers who, on anecdotal information only, they believe to be evading taxes.

The truth is that 80 per cent of the total offshore financial services industry is located in the OECD countries, excluding their colonies. The remaining 20 per cent is in the non-OECD countries with even this segment dominated by a few large centres such as Hong Kong and Singapore which, conveniently, the OECD has not named as 'tax havens'.

This means that less than approximately 10 per cent of offshore business in the world is done in our jurisdictions. The law of averages suggests, therefore, that very little tax evasion money is in the Caribbean. Much of it may well be in the OECD countries themselves.

It is noteworthy that on the money laundering side, while much publicity surrounds illegal activity uncovered in the Caribbean, the actual incidents and sums involved are a tiny fraction of the numerous incidents and vast sums of money discovered in the OECD countries.

I have no crystal ball that can foretell the future. But I do know that we in the Caribbean have the same right as every other country to compete in the financial services sector globally. Our well-educated populations, their high propensity for computer literacy, the relatively lower costs of

business in our jurisdictions, our first-class telecommunications and our low tax levels give us the chance to compete efficiently.

In the last 18 months, we have moved rapidly to a well-supervised financial system onshore and offshore. Most, or all, of our countries now meet the highest international standards. With the transparent accounting practices that meet international best practice and global standards, such as those which PriceWaterhouseCoopers and other reputable auditors provide in our region, we should not hesitate or waiver in our resolve to continue to grow this important sector in the interest of our people, the OECD notwithstanding. We should proceed to do so.