The unfair fight

The hypocritical stance by the OECD represents the developed nations' inappropriate pressure on less developed nations to adopt compliant tax regimes, argues *Dr. Angelo Venardos*

The OECD is the most well-known of a group of international bodies, which includes the Financial Action Task Force (FATF), Financial Stability Forum (FSF) and International Monetary Fund (IMF) which together set out to regulate (directly or indirectly) global capital mobility and tax regimes.

In the 1998 report *Harmful Tax Competition: An Emerging Global Issue*, the OECD acknowledges that countries should be free to design their own tax systems. This must be according to internationally accepted standards, but such standards are non-existent and seem to be determined solely by high tax and onshore countries that are afraid of tax competition.

The OECD report pays little regard to the well-established rule of international law, which says that one state cannot enforce the tax laws of another. This rule recognises the territorial application of tax law.

When the OECD produced another report, in 2000, entitled *Towards global tax cooperation: Progress in identifying and eliminating harmful tax practices*, it was revealed that the OECD was treating its member states quite differently from the unilateralist and arbitrary stance taken with the targeted jurisdictions. First, while the targeted jurisdictions were quite categorically named as 'tax havens', some OECD members, such as Switzerland, Belgium, Portugal, Luxembourg, Canada and the United States, were described only as having regimes that were 'potentially harmful'. Second, the OECD carried out a unilateral evaluation of the so-called 'tax haven' jurisdictions, but its own members each performed 'a self-review' to determine whether or not they had preferential tax regimes.

The low tax or no tax regimes of these small states, coupled with literacy in English and good telecommunications gives them an advantage with which many OECD countries cannot compete. Instead of trying to vie with small states by lowering their own taxes, the OECD responded by demanding that these small jurisdictions change their tax systems and structures or face damaging sanctions.

The OECD represents the views of its member states, which have reached a high level of industrial development precisely because of tax competition in which they lured foreign investment into their countries by tax breaks. In fact, many of them continue with this practice.

In the US, for instance, figures from the Bureau of Economic Analysis, and the US Department of Commerce reveal that institutions, both banks and non-banks, held more than US$1.8trillion in deposits from foreign persons at the end of 2000. That money is there because the US exempted the holders of those accounts from taxes on their interest income!

Is OECD representative?

The OECD is only a multinational grouping of 30 countries. It is not an international organisation and 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 dictating terms on what, in short, could be described as cross-border tax matters.

The Chief Foreign Affairs Representative of Antigua and Barbuda revealed in a speech in 2001, that 80 per cent of the total offshore financial services industry is located in the OECD countries. 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 the OECD had not named as 'tax havens'. This means that approximately less than 10 per cent of

offshore business in the world is done in the targeted jurisdictions.

In *Towards a level playing field – regulating corporate vehicles in cross-border transactions*, the Canadian law firm, Stikeman Elliot has strongly suggested that progress must be premised on the basis that uniform rules, developed in an inclusive process are implemented by all states, on the same time frame, with the same consequences for those states which do not cooperate. This is a fundamental objective, and essential to achieving an equitable result.

The imposition of more onerous 'compliance requirements' exclusively on non-OECD member countries could be seen as hypocritical. For example, efforts to minimise the misuse of corporate vehicles should not be used as a guise for undermining the competitive position of those jurisdictions which have limited input into the standards' design process. To allow this misuse would be to compound the non-tariff barriers to the trade in services arising in other initiatives.

Even without the particular context of offshore business, international law has always recognised that the fiscal and penal matters of one state with respect to enforcement of foreign judgements and

other types of international assistance should be outside the realm of another. This rule has been followed rigorously by offshore finance centres. It is also consistent with the rule on the legality of tax avoidance measures which refrain from imposing a duty on the individual, to voluntarily assist tax authorities in gaining revenue.

More than a moral objection

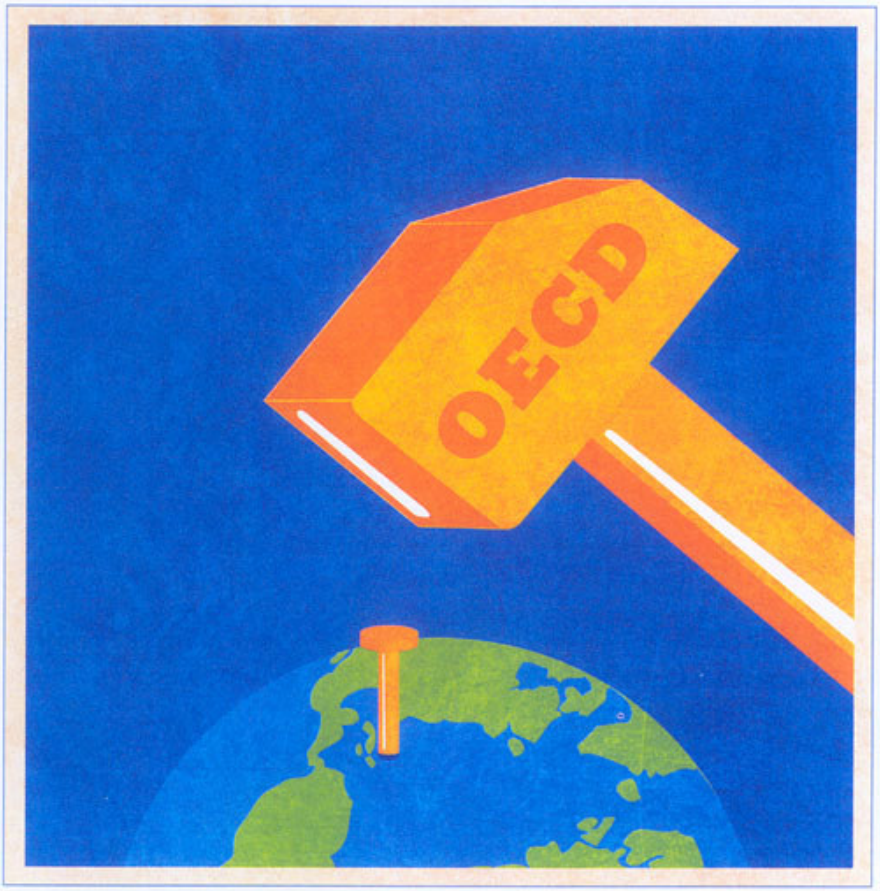
If criminal activity is not the true focus of offshore activity, and if it is demonstrable that offshore laws do not exist either to promote or conceal such activity, then why has such an offensive has been launched against the offshore sector?

The argument offered by Rose-Marie Belle Antoine in her book *Confidentiality in Offshore Financial Law* is that the real issue concerns the loss of revenue, particularly but not solely fiscal revenue flowing from onshore economies and filtering offshore. The revenue, albeit in savings which filter from onshore countries, results in the economic development of many offshore countries, several of which can be labelled as developing countries.

The fear on the part of onshore countries of the loss of revenue as a direct result of offshore activity is not one to be dismissed. Already, non-offshore jurisdictions within the European Union are beginning to experience an increase in loss of revenue as a result of offshore business, as noted in the 2003 Boston Consulting Report *Winning in a Challenging Market: Global Wealth 2003*.

European unification has improved European citizens' ability to relocate their assets to other European countries and many investors are choosing to invest in European offshore jurisdictions such as Cyprus and Ireland and in Asian countries such as Singapore and Hong Kong. The enrichment of offshore coffers at the expense of those onshore provides a powerful economic and political motive for the legal offensive aimed at the offshore sector. This factor cannot be ignored when the question of the acceptable limits of offshore activity and law are to be addressed.

The real concern for onshore countries in relation to offshore activity is often actual financial loss rather than high or moral principles. While it is clearly within the right of any country to safeguard economic and political interests, this element must be recognised for what it is and should not be



allowed to cloud the relevant legal issues, such as the validity of the offshore interests by attacking offshore law and policy. The argument thus follows that all things being equal, offshore states have a similar right to safeguard their economic and political interests by upholding them. This is an important argument in the difficult issues relating to comity, taxation and the confidentiality principle. It is central to the question of legitimacy.

The comity principle is an extension of the principle of territorial sovereignty. It sets the standard for resolving conflicting jurisdictional issues which may arise. As Rose-Marie Belle Antoine says, it is 'the degree of deference that a domestic forum must pay to the act of a foreign government not otherwise binding on the forum'.

It has been argued that offshore states are under no moral or legal obligation to assist onshore states in their law enforcement efforts in fiscal matters. The counterview that the fact that fiscal matters form the bulk of the subject matter of disclosure requests is not helpful to onshore cases.

Hence, it is one view that the confidentiality principle must sometimes be sacrificed to a greater interest in disclosure when competing interests are balanced. This is so, for example, where serious international criminal matters are an issue – an opinion shared by offshore courts. On the other hand, seeking an appropriate balance does not mean a *carte blanche* denial of the confidentiality interest in all circumstances where there are conflicts of laws, as sometimes appears to be the present judicial practice. Rather, offshore jurisdictions must be given the opportunity to define the limits of their confidentiality laws fairly.

It is therefore argued that they should not be forced into surrendering to greater political and economic powers disguised as legal interests as represented by the OECD et al. A just appreciation of the comity principle allows such an exercise by ensuring the consideration of the interests of both onshore and offshore states. It is only within such a construct that the extent to which the offshore confidentiality principle is justifiable and that inappropriate pressure on less developed nations to adopt compliant tax regimes, can it be truly appraised.

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