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Animal Farm

Carnival ends but the heat continues. I'm referring to Panama's recent Carnival and not last November's Organisation for Economic Co-operation and Development Global Forum meeting in Melbourne, Australia. The OECD heat, however, will increase more for some than for others.

Monaco, which has only 32,000 residents and, after the Vatican, is the world's smallest independent state, attended the Melbourne meeting as a non-participating partner, and is a good example. It is not a dependency, but how independent is it really? Many European countries treat it with suspicion, convinced that it is more a haven for dubious business; the view has been expressed that Monaco's sovereignty is hostage to the fundamental interests of France. (French residents living there have been subject to French taxes since 1963).

The learned British Judge, Lord Denning, stated that by international law "every sovereign state has no sovereignty beyond its own frontiers. The Courts of other countries will not allow it to go beyond the bounds. They will not enforce any of its laws to purport to exercise sovereignty beyond the limits of its authority". But sovereignty is beset with problems because there does appear to be degrees of it as this century has already shown.

Panama's sovereignty is absolute but, according to Simon Chesterman, executive director of the Institute for International Law and Justice at New York University, there are, in fact, "…different and complicated forms. The idea that sovereignty means all states are equal is the great fiction of international law". George Orwell, who wrote another piece of related fiction, Animal Farm, would have understood and Monaco, as well as another finance centre, Andorra, prove the point. Both are sovereignties with seats at the United Nations but their foreign policies are controlled by France.

The origin of sovereignty has brought about misunderstandings. History, after all, is a confused heap of facts according to Lord Chesterfield. The concept of sovereignty stems from the Treaty of Westphalia in 1648 under which a prince, or sovereign, was identified with the territory he governed. This premise formed part of the marrow of international law and led to the conviction that sovereigns are equal and always had the final word regarding their realms' affairs. This, of course, has had important consequences in the field of offshore financial services where courts in different places have claimed exclusive jurisdiction, causing a conflict over the application of laws.

As if to reinforce Mr. Chesterman's case, when Albert II, Monaco's new prince, was enthroned last November, the only head of state to attend and not give Prince Albert the cold shoulder was, ironically, the president of Iceland.

Gunsmiths and Winemakers

The OECD, when talking about taxation, speaks of harmonisation but you could just as easily substitute the word standardisation. There are countless examples (the OECD initiative, I might add, isn't one of them) where standardisation makes sense and brings with it dependability, certainty and

orderliness. Although much of the business done offshore calls for this approach (such as regulation and supervision of banks and professionals) it is also true to say that some of the business does not because, by its very nature, it falls into a special category requiring a different approach.
Bureaucrats are not the only ones who fail to appreciate the difference. Some practitioners are equally guilty or simply choose to ignore the fact. Template tactics, as I call them, can have unfortunate consequences for clients. Richard Purdey, the great-great-great grandson of James Purdey, founder of Purdey in the United Kingdom, which is said to manufacture the finest shotguns in the world, commented: "Gun-makers can do any precision engineering, but not every precision engineer can make guns". Being a professional offshore practitioner calls for precision combined with a breadth and depth of experience and knowledge of the particular services being offered. Henry Mintzberg, in his book, "Managers Not MBAs", argues that the average MBA course offers "specialised training in the functions of business, not general educating in the practice of management". He sees management as a craft and he is right and focusing one's skills will make it easy not to cross the boundary line of one's abilities. Incessantly, people travel to foreign shores where they then ask for advice about their domestic taxes which can be dangerous if the offshore practitioner, for whatever motives, does not point out that tax reservations should be addressed before flight reservations are made.
It was, of course, once so very different in a less complex world. One could be well versed in several disciplines. Take the case of the US president, Theodore Roosevelt (a name forever inextricably linked with Panama), who, before he reached 40 years of age had studied palaeontology, ornithology, mammalogy, criminology, technology, geography and history. This was all in addition to his main interest which was geopolitics. Roosevelt was a self-taught man who read about 20,000 books ranging from Aristotle to Tolstoy and managed to write 15 of his own. I agree that his thirst for knowledge was exceptional, but history is strewn with many other examples of men and women skilled in diversified disciplines.
The 21st century makes this a very difficult goal to achieve and I am convinced that the offshore arena, in particular, calls for specialisation, whether it be mutual funds, captive insurance or private banking. The complexities (ever increasing) of each service demands it if one is to be able to provide best advice. The client sitting before you needs to discern three things from you: clarity, competence and consistency, as mentioned in the book, "Do Lunch or Be Lunch", by Howard H. Stevenson (with Jeffrey L. Cruikshank) Even purveyors of wine are no exception. In Australia, the University of Adelaide has a dedicated degree in wine business and marketing and figures reveal that from a recent intake of 100 students, less than 25 are expected to graduate due to the rigours of the syllabus that covers commerce, economics, marketing, viticulture, oenology and sensory analysis. The only other similar qualification that is internationally recognised (and, even then, is restricted to only selling wine) is an MBA course offered by the University of Bordeaux in France. In the case of wine, one needs, literally, to drink deep from the pool of knowledge (with apologies to Alexander Pope).

Value for Money

Professionalism of a high degree comes, however, at a price and, to paraphrase Oscar Wilde, where a man knows the price of everything and the value of nothing, he is courting disaster in the case of offshore matters. Recognising real value is, after all, how the old, traditional private banks have not only lured but kept their clients. They have given a superlative service supported by an abundance of knowledge.
Private bankers argue that wealth management services given by big banks lean towards the impersonal. You might say that self-interest would have them say that, but having experienced working for both a monolithic and also a minuscule financial services institution, I strongly support the

contention. Friedrich von Metzler, partner in Germany's Metzler Bank, a private bank specialising in investment banking and asset management, put it this way: "We are not product-driven like a big bank and we team up with experts in certain areas when that is pragmatic. We don't force clients into a certain fund because head office has a quota to fill. Our clients pay us for the quality of what we tell them not the quantity of what we sell them". He must be on to something because Sal Oppenheim, Europe's biggest privately owned bank, reported in April, 2005, a 60 per cent rise in profits, giving it a higher return on equity for 2004 than Germany's Deutsche Bank.

"We have been content to eat a piece of the cake rather than try to have the whole cake. We do not want to be the biggest, but certainly one of the finest in our field". That philosophy has been recognised and acted upon by many successful specialists, particularly offshore, and the words were spoken in 1978 by André Heiniger, as chairman of Rolex, a privately held enterprise which sells some 750,000 watches a year and operates in 100 countries. This is an approach to business that doesn't just make Rolex tick.

Taxing Times for Sheep

Adam Smith spoke of the "frequent visits and the odious examination of the tax gatherers" and thought that taxes were "much more burdensome to the people than they are beneficial to the sovereign". I am sure, however, that the OECD (the "rich countries" club based in Paris) would share the fatalistic view of Edmund Burke: "To tax and to please, no more than to love and to be wise, is not given to men".

The OECD's Global Forum has already been mentioned and in the September, 2004, Offshore Pilot Quarterly I wrote that the forum's Berlin meeting that year still had key participants missing which meant that nobody "can predict where the process might be when the OECD Global Forum meets again in October/November next year". The forum meeting in Berlin had also set 1st January, 2006, as the date by which participants would be encouraged to have in place effective exchange of information and transparency policies, all of which are allied closely with tax harmonisation. Of course that date was too optimistic a deadline and has come and gone. New readers wishing to review the major developments of the initiative during the last ten years can do so in the back issues of the OPQ.

Last year's forum meeting had 130 representatives of 55 governments present but, as in 2004, the process remains flawed because some major finance centres continue to refuse to commit themselves and become, what has been termed, participating partners. Liechtenstein did not attend and Austria participated (not as a partner) for the first time; but two important centres, Luxembourg and Belgium, refused to be there which seems ironic when both are not only OECD members but also form part of the European Union. Singapore, Switzerland and Hong Kong attended but are not, like Austria, participating partners in the initiative.

Some countries that are already members of the forum will have to change their practices and laws to meet the standards which the OECD wants in place. The ease with which this can be achieved, not to mention (in some cases) the political considerations involved, is far from certain. Then there are two more (considerable) hurdles: the participation of all finance centres has to become a reality to achieve the much-touted level playing field, and, after that, forum participants will have to reach unanimous agreement on policies. As to unanimous agreement, I tend to quote Dean William R. Inge who reminds us that "it is useless for the sheep to pass resolutions in favour of vegetarianism while the wolf remains of a different opinion". In this case there's more than one wolf to deal with.

This is, in fact, the 10th anniversary of the OECD's tax harmonisation initiative. There's a lot at stake. The International Monetary Fund, when it made its last estimate, reckons that $5,000 billion is held offshore. Initially, the OECD decided on the stick, rather than the carrot, approach but found that this was not realistic – especially when the US government perceived an intention to clamp down on tax competition.

In Melbourne the new message was about "mutual benefits" but the crucial problem remains: the OECD is guilty of double standards. After all, non-committed Austria's Federal Chancellor, Wolfgang Schüssel, is presently President of the Council of the European Union. It is because of this background that Panama, whilst a participant in the initiative, has publicly declared that its agreement depends on universal compliance.

Viscount Sherbrooke in 1870 said of his office: "The Chancellor of the Exchequer is a man whose duties make him more or less a taxing machine. He is intrusted with a certain amount of misery which it is his duty to distribute as fairly as he can". Panama has less misery due not only to its tax system but also because, unlike the Cayman Islands and similar dependencies, it remains on the periphery of the OECD's ability to use the stick and throw away the carrot; this realisation by many has fuelled the growth in Panamanian offshore business.

Such growth offshore is frustrating for many tax-hungry OECD members who have enough difficulties collecting revenue from a captive domestic population. OECD officials, for instance, estimate that the US Internal Revenue Service has only enough auditors to check the books of each American business for one day every ten or eleven years. Clearly, a revenue service under pressure.

Another kind of pressure is atmospheric that causes hurricanes. Panama is fortunate enough not to suffer from them and it would seem to me, in a similar context, that any future pressure from the OECD is likely, figuratively speaking, to bring the isthmus perhaps light rain, but never hurricanes. Not so for those dependent finance centres in the region that have both atmospheric and OECD pressure to deal with.

Panama's 2006 Carnival and the OECD's 2005 Global Forum meeting both ended on a Wednesday. In Panama it was Ash Wednesday and even although the Melbourne meeting didn't end in ashes, I very much doubt if the organisers left fired with enthusiasm.

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