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Bridges, Bombs and Bureaucrats

The second bridge to be built over the Panama Canal at a cost of $100,000 million, and called the Centenary Bridge, is a fine sight. It promises to contribute significantly to both the residential and commercial development of the former Canal Zone, once a fiefdom of the United States of America. The problem is that the gleaming new suspension bridge is close to an old US military weapons testing range which the Panamanian government says remains unsafe because the US military has failed to meet its obligation to clear the area of any potential unexploded bombs, mortar rounds and artillery shells. The presence of access roads and plans for low income housing near the Centenary Bridge makes the situation a precarious one and talks continue between both countries.

Building bridges and unexploded bombs – admittedly, of a different kind – can also apply to offshore financial planning when a person decides to traverse the divide between onshore and offshore. The hypothetical bridge that's built between the two must be able to be crossed in safety and should be sturdy, not some flimsy foot bridge made of rope and likely to not stand the test of time. When I meet with potential clients I always remind them of how important it is to ensure that they satisfy themselves that any offshore structure put in place will not have any unintended, and unfortunate, consequences; that they don't create, as it were, a mine field in which by taking a wrong step, they see their plans blow up in their faces.

It's all about proper planning by people who know what they're doing. Speaking of which, my remarks about onshore regulators in the March issue of the newsletter (under the heading: "Blind Men") drew supportive comments from some international practitioners. It was suggested, however, that the root of the problem, namely, a lack of practical experience, extended, in some cases, to offshore regulators as well. It's fair comment and does not surprise me, particularly when often the choice of an offshore regulator does not rest in the hands of those competent to choose, but is dependent on the decision, perhaps, of a panel of bureaucrats with little understanding of the important issues. Such a situation can especially arise where the regulator's jurisdiction is a dependency of a country in Europe.

Some onshore bureaucrats, in attempting to tackle offshore regulation, realise that they don't know enough to make the right decisions but then take the illogical approach of either not seeking guidance or, if they do, failing to heed the advice given. It is, therefore, no surprise to me to read comments written by Jim Dougal who headed the European Union Commission's office in Belfast between 1997 and 2002 and then became head of its United Kingdom representation from 2002 until 2004. Most readers of this newsletter appreciate the importance which the European Union has had (and continues to have) in shaping policy towards many of the major offshore financial services centres and so Mr. Dougal's remarks are worth noting. He speaks of being "horrified and mystified" and to being exposed to the EU Commission's "outrageous lack of common sense". Coincidentally, the Commission's headquarters are in Brussels, capital of Belgium, and a city referred to by the English poet, Matthew

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Arnold, as “a cheerful, wicked little place”. The American writer, Herman Melville, described Brussels thus: “a more dull, humdrum place I never saw”. It seems to me that the EU Commission is ideally located.

Monarchs, Mandarins and Mess Ups

On King Charles Street in London, where the UK’s Foreign Office (which I used to visit on official business) is located, you will find statues of both King Charles I and Oliver Cromwell. Cromwell, a fine military leader, headed the uprising which eventually brought about the king’s downfall and his execution. Seneca said that the “foremost art of kings is the power to endure hatred”. The Stuart monarch who firmly believed in the divine right of kings, lacked endurance but was able to mismanage the royal affairs so completely that his conflict with Parliament, and therefore Cromwell, brought about three civil wars. This reserved, stammering and self-righteous king had dissolved Parliament three times and at one point chose to rule without summoning Parliament for eleven years. Oliver Cromwell, a convert to a strong puritan faith that eschewed the ceremonial ostentation of the Catholic church would change all that. He came from the middle ranks of English society and was a force in Parliament where he represented the interests of the Puritans, middle class merchants and tradesmen. The King’s supporters, on the other hand, were the peasantry and the nobility.

The statues of both men on King Charles Street are reminders of Lord Palmerston’s view that a country has no permanent friends or enemies, only permanent interests. So do bureaucrats. Expediency is a given: today’s and tomorrow’s friends may not be the same people and the mandarins (named after the nine ranks of officials of the Chinese Empire) of Whitehall are masters of the game. They are the first to understand the usefulness, at given times, of both a ruler and a rebel, be they self-righteous sovereigns or puritanical parliamentarians. How right, then, for those statues to be on King Charles Street where the civil servants readily appreciate the proverb of the fox and the hedgehog. It was used by the 7th century BC Greek poet, Archilochus, to illustrate how diverse traits can be of equal importance. Archilochus said that the fox devises many strategies; the hedgehog, however, knows one great and effective strategy. King Charles was most certainly a fox and Cromwell, (who would become Lord Protector of England, Scotland and Ireland), was a hedgehog. But, of course, Whitehall is not the exclusive territory of mandarins and, in various guises, along with their acolytes, they can be found in the ranks of the Organisation for Economic Co-operation and Development, as well as the EU Commission.

In the case of the Brussels-based bureaucracy, mandarins have found bureaucratic bliss. There are three main EU bodies: the European Council (representing governments); the European Commission (the executive arm that proposes legislation); and the European Parliament representing the peoples of the member states. So the Commission proposes laws which must be approved by the Council and Parliament. It is unlike any other form of government previously known and its uniqueness – and sometimes its obliqueness – leads to a mystique only pierced by the bureaucrats themselves. It should not be surprising, therefore, that the European Union Savings Tax Directive, which came into effect on 1st July this year, has created a stir in some offshore financial services centres. Bermuda was not affected when the directive came into force and Gibraltar was compliant except that the directive does not apply between itself and – believe it or not – the United Kingdom which has sovereignty over Gibraltar. Now, there are blunders and there are blunders. Those of the instant, spontaneous kind can perhaps be more readily forgiven, such as when, in 1998, a Salomon Brothers trader leant an elbow on a computer keyboard which activated an order to sell around US$1 billion’s worth of French government-bond futures; or, more recently, when a trader at a bank keyed in the wrong number of shares on his trading screen with the result that a sell order for a basket of shares worth around US$50 million was changed into one valued ten times that. The London stock exchange saw the FTSE 100 index plunge by 2.2% in the final moments of trading on that particular day. In the case of the European Commission, however, it

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has had five years of planning to get it right and slips by fingers or elbows cannot be blamed for the Bermuda and Gibraltar mess.
The directive, in some instances, forces offshore financial services centres to disclose details of certain types of income an EU national has earned to the tax authority in the EU country in which he resides, or deduct a retention tax. The directive does not affect persons who are resident in the offshore jurisdiction, nor those who are not resident in any one of the 25 EU countries. It was intended to also extend to dependencies of one or more of the 25 EU countries and the British government has found itself in a spot. The blunder, once realised, caused a cornucopia of contentious issues to be raised – especially by some of the other leading offshore jurisdictions already foaming at the mouth over having to comply. Bermuda is the only British dependent territory (Gibraltar is a Crown dependency enjoying more legislative freedom) that was not included in the directive. How did its name disappear from the list? Was this the work of the Bermuda triangle? It may take time, but Bermuda can be sure that the issue will be something that doesn't disappear. The same goes for Gibraltar.

That Magnificent Seven

This month the annual Catholic feast day known as the Seven Sorrows of Our Lady is celebrated. Its purpose is to reflect on the sadness endured by the Virgin Mary because of the suffering and death of her Divine Son. Not just sorrows, it seems, come in sevens. The offshore financial services industry was told by the OECD at its meeting in Switzerland in May, 1998, of its grand design to stamp out tax havens within seven years. You will have noticed that the deadline has recently expired and that most of the so-called tax havens are alive and well – and prospering. Offshore private banking – a main ingredient of offshore services – certainly seems set to grow with one research source estimating that more than 8.3 million people worldwide had over $1 million in financial assets in 2004. This is an increase of (here comes that numeral again) 7 per cent over 2003 and doubtless a number of those millionaires will be looking for investments and strategies beyond their domestic markets.
You might ask why the OECD decided to set a target of seven years. It would be a mistake to automatically assume that it followed a period of considering the logistics and practicalities of the objective. Proper planning, in other words. It was probably chosen for the same reason that many of us are drawn to that special number. What brought about this septimal obsession has its roots over 40 centuries ago in Sumeria (once part of Mesopotamia) which was conquered by Sargon I, King of Akkad, who instituted the first ever recorded seven-day week. Actually, we owe not only the week to the Sumerians but also the 60-minute hour. Subsequently, Babylonians, Greeks and Romans adopted the seven-day week; Europe and the Americas were to follow. The week reached India from Mesopotamia more than 2,000 years ago and about 1,000 years later, even China capitulated. Seven was significant for the Sumerians because they worshipped seven gods that could be seen in the sky and they decided to name the days of the week for these heavenly bodies. Today we know these gods as Sun, Moon, Mars, Mercury, Jupiter, Venus and Saturn.
The future of the OECD's grand design to stifle tax havens is in the lap of the gods, but one thing is for sure: that organisation is at sixes ***and*** sevens over how to achieve its goal.

War of the Worlds

Panama's railway, inaugurated in 1855, is celebrating its 150th anniversary. A lot has changed since Mark Twain, who travelled on the railway, wrote an article for the Chicago Republican in 1868. He described his train journey across Panama and how he spent two or three hours travelling through "a tangled wilderness of tropical vegetation". The hapless Jim Dougal, who abandoned the EU Commission, spent seven years negotiating a tangled wilderness in the byzantine, bureaucratic depths of the EU headquarters before his journey came to an end. Even he succumbed to the number seven after coming unstuck mainly because of a poor communication system, smothering rules and

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incompetence. As an ex-regulator myself I can sympathise with him.

Much like the EU Commission, the OECD has similar problems. It has often been too ambitious and has suffered from failures of grand design, two subjects that not only Oliver Cromwell and King Charles I understood, but also Adam Smith and Macbeth. One sometimes feels that the OECD's offshore tax campaign is built on the scepticism of Adam Smith. In Wealth of Nations he wrote: "Commerce sinks the courage of mankind. The minds of men are contracted, and rendered incapable of elevation". Honoré de Belzac, however, said that bureaucracy was a giant mechanism operated by pygmies: surely, then, that's where you would find an abundance of "contracted minds" and a scarcity of elevation? There is no doubt that a war of the worlds is raging. One world is onshore and the other is offshore, but it is nothing like the war that H. G. Wells wrote about. I suspect that H. G. Wells would have had some sympathy for those combatants offshore and, certainly, no mandarin would have agreed with his sentiment that in politics the best way to play your cards is to lay them face upwards on the table. Who will be triumphant and how the OECD tax and other anti-offshore initiatives will end is not known.

In 1660, eleven years after the execution of his father and with Cromwell no more, Charles II ascended the throne and The Restoration was complete. The poet, John Dryden, described the son's reign as "a very merry, dancing, drinking, laughing, quaffing and unthinking time". Another Charles is waiting in the wings today to assume the British throne. But just as things have changed for monarchs, so they have for money managers – particularly those offshore. There will be no Restoration for either and the merry times of the past have gone forever.

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Engaging an offshore representative is an important decision and we advise all persons to seek appropriate legal and tax advice from professionals licensed to render such advice before making offshore commitments.

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