

## FISCAL HAVENS IN LATIN AMERICA AND THE CARIBBEAN

JEFFREY OWENS AND ALESSANDRA SANELLI

pubblicazione internet realizzata con contributo della



società italiana di economia pubblica

---

dipartimento di economia pubblica e territoriale – università di pavia

# FISCAL HAVENS IN LATIN AMERICA AND THE CARIBBEAN

by

Jeffrey Owens

and

Alessandra Sanelli

Director OECD's Centre for  
Tax Policy & Administration

Italian Central Bank

## **Abstract**

This paper is part of a wider research on “Tax Systems and Tax Reforms in Latin America”, carried out at the Department of Public Economics of the University of Pavia, under the direction of L. Bernardi, A. Barreix, A. Marenzi and P. Profeta, and the supervision of V. Tanzi. Tax havens have played an increasingly important role in world financial markets, particularly in the Caribbean and Latin American regions. This paper examines the role of tax havens, particularly in the Caribbean, the response of the international community in the context of the OECD *Harmful Tax Practices* initiative and sets out what are the longer term prospects for these economies. After discussing the growing concerns about tax havens, particularly those of national tax administration, and reviewing the theoretical and empirical literature on tax havens and information exchange, the paper illustrates the origins and evolution of the Caribbean tax havens and their present weight in the international financial and economic landscape. Finally, the current position of these jurisdiction is examined in the light of the international initiative launched by the OECD Member countries to curb harmful tax practices.

**Reference Authors:** Jeffrey Owens [Jeffrey.Owens@oecd.org](mailto:Jeffrey.Owens@oecd.org);

Alessandra Sanelli [Alessandra.Sanelli@bancaditalia.it](mailto:Alessandra.Sanelli@bancaditalia.it)

**Keywords:** Fiscal Havens, Caribbean, Latin America

**JEL Codes:** H20, H26, H87

Department of Public and Environmental Economics  
University of Pavia - Italy- March 2007

## **1. Introduction\***

Tax havens play an increasingly important role in world financial markets, particularly in the Caribbean and Latin American regions. Tax havens thrive in a climate characterized by excessively strict bank secrecy, a lack of transparency and where countries are not prepared to cooperate to counter abuse. Over the last 30 years, we have seen many Caribbean islands move into offshore financial activities. This has had profound implications for the structure of their economies. It has also had profound implications for both developed and developing countries. This paper examines the role of Caribbean tax havens, the response of the international community and sets out what is the current position of these jurisdictions in the light of the international initiatives aimed at curbing harmful tax practices.

The paper is organized as follows. Section 2 identifies the growing concerns about tax havens, particularly those of national tax administrations, and reviews the theoretical and empirical literature on tax havens and information exchange. Section 3 tracks the origins of the Caribbean tax havens, while Section 4 examines their present weight in the international financial and economic landscape. Section 5 reviews the international initiative undertaken at the OECD level to counter fiscal abuse through tax havens and the response of Caribbean jurisdictions. Finally, Section 6 examines the possible future prospects for these economies.

## **2. Tax havens: a growing concern for the international community**

In recent years, improved communications and liberalization of financial markets have fostered an impressive growth of both cross-border financial transactions and foreign direct investment (FDI). The rising volume of international transactions has brought new risks, among which the wider potential adverse effects of financial crises and financial instability and the larger possibilities to hide abroad the proceeds of illicit activities.

A fundamental concern of national governments, both in developed and developing and transitional economies, relates to the possible erosion of national tax bases arising from

---

\* The views expressed in this article are those of the authors and do not in any way commit the OECD and its Member countries nor the Banca d'Italia.

the transfer of their residents' capital to offshore financial centers. In fact, while there may be legitimate reasons to use offshore financial centers, including tax reasons, they are often used for tax evasion and avoidance purposes. This is due to the fact that offshore financial centers are often referred to as "*tax havens*", because these are often countries or territories which attract foreign capital by promoting themselves through a combination of low or no taxation, advanced communication facilities, reliable legal systems and a high degree of confidentiality for financial data, such as those on beneficial ownership, companies, trusts and bank accounts.<sup>1</sup> Tax havens are used both by individuals and companies. In the new era of "banking without borders" wealthy individuals can easily evade capital income taxes in their country of residence by transferring capital abroad and channeling passive investments through tax havens. This type of tax evasion is facilitated by the existence of jurisdictions with strict bank secrecy rules which prevent information exchange with the residence country, and by the increased recourse to foreign institutional investors and shell companies with opaque structures based in offshore financial centers, which can make it very difficult for domestic tax authorities to track the capital income. With the growth of cross-border capital flows, the potential for abuse created by the lack of access to bank information for tax purposes and the resulting adverse consequences have increased exponentially. At the same time, tax authorities find it more and more difficult to monitor foreign portfolio investments of their residents because of the removal of traditional sources of information on these transactions (e.g. exchange controls). The decision by one country to prevent or restrict access to bank information for tax purposes now is therefore much more likely than ever before to adversely affect tax administrations of other countries.

Furthermore, the progressive elimination of withholding taxes at source on non-residents' portfolio investment income allows more and more taxpayers to escape all form of capital income taxes. Quite often, even when investing in their own countries, resident investors use foreign financial intermediaries and corporate or trust vehicles based in bank secrecy jurisdictions or offshore financial centers to disguise themselves as non-residents and evade domestic taxes. Thus, for example, a significant part of the investment into China via Hong Kong is made by Chinese residents; Cyprus plays a similar role for Russia. An increasing proportion of investment into Asia is channeled through structures established in

---

<sup>1</sup> These different factors may have a different weight for each tax haven. This also means that there may be different groupings of tax havens, depending on the combination of relevant factors chosen to identify them.

the British Virgin Island. Even more significant is the possible use of bank secrecy jurisdictions to escape domestic taxes on income and wealth of a different origin (business income, inherited wealth, etc.) that represent the “*principal*” of the foreign investment.

Companies make use of tax havens mostly for tax minimization purposes. They shift income to tax havens through their foreign affiliates in order to reduce or defer residence-country taxes. In this respect, the most attractive features of tax havens are the low level of taxation and the availability of flexible and tax-advantaged vehicles to channel international business, such as shell or holding companies. Investments in high-tax countries, for example, may be financed with loans from affiliates in tax havens; the resulting interest payments reduce taxable incomes in high-tax locations while producing taxable income in the havens. Another method is the use of transfer pricing. Even if most high-tax countries require firms to use transfer prices that would be paid by unrelated parties, following the OECD’s 1995 Transfer Pricing Guidelines, difficulties in enforcement makes it possible for firms to reduce the overall tax burden. Tax havens can be also used to avoid repatriating foreign income in the firm’s home country and thereby producing a home country tax obligation. The resulting tax savings can be substantial, contributing to the value of tax haven operations (Dharmapala and Hines, 2006). Bank and financial confidentiality may nonetheless play a role, both for closely held or passive investment companies and, more generally, because it makes it more difficult for home-country tax administration to track tax haven activity aimed at tax avoidance and evasion.

The effects of tax havens have recently been the object of a theoretical and empirical literature (see box 1).

**Box 1 - Tax havens: theoretical analysis and empirical findings**

*The nature of tax havens and the effects of tax haven activity on the economies of high-tax countries have been examined in the context of the tax competition literature.*

*A first question addressed by the theoretical studies concerns the factors that influence the desirability of becoming a tax haven (see Dharmapala and Hines, 2006, and Slemrod and Wilson, 2006, for a review). A common result is that small open economies have an incentive to undercut large countries in order to attract mobile capital: whilst they are not able to influence the interest rates prevailing on international markets through their mainstream economic policies, they can quite easily attract international capital flows by reducing their tax rates, either directly and/or by offering a “favorable” tax climate for non-resident investors. The budgetary cost of these tax reductions need not be very high, since the tax reduction is accompanied by a larger tax base due both to greater*

*investment by non residents and to greater taxable income of residents.*<sup>2</sup>

*This result seems confirmed by the patterns observed in tax havens economies. Tax havens tend to be small countries with extremely open economies and substantially smaller natural resource endowments than non-havens. Also the experience of tax haven economies over the last two decades is consistent with the predictions of the theory. The period of globalization has been very favorable for tax havens, which grew at an average annual real per capita rate of 3.3 percent between 1982 and 1999, compared to the 1.4 percent growth rate of the world as a whole (Hines, 2004). This result is consistent with the growth of FDI in the same period<sup>3</sup> and with the empirical evidence showing that both the volume and location of FDI are sensitive to tax differentials.<sup>4</sup>*

*The effects of tax haven activity on the economies of non-haven countries is a highly controversial point. A common fear of non-haven countries is that tax havens may help diverting economic activity away from them, eroding tax bases that might otherwise be used to raise government revenue. This fear is more acute in the case of nearby tax havens, which might divert activity from other countries within the same region or economic federation. In this respect, the empirical evidence seem to suggest a complementary rather than substitute relationship between investment in tax havens and investment in nearby countries: the availability of tax havens seem to stimulate, rather than divert, economic activity in nearby non-haven countries (Hines, 2004; Desai, Fritz Foley and Hines, 2004). However, as suggested by Sullivan (2006), it is possible that the complementary relationship holds for certain types of foreign investments in low-tax countries (for*

---

<sup>2</sup> The explanation lies in the classic argument of Diamond and Mirrlees (1971) that governments unnecessarily distort production when they tax intermediate production, from which it follows that in small open economies governments with a sufficient number of available tax instruments can make all domestic residents better off by not taxing internationally mobile capital. In fact, since small open economies are price-takers in world markets, they are unable to shift any of their tax burdens on foreign investors: any attempt to do so would simply distort their economies by putting additional costs on domestic factors in the form of lower wages and land prices. It follows that domestic residents would be made better off by removing any taxes on foreign investors and instead directly taxing the returns to local factors of production. In addition to the price-taker position of small economies and to the availability of a sufficient set of tax instruments for the governments of the same economies, another basic assumption on which the Diamond and Mirrlees argument relies is that foreign investors do not earn economic rents from their investments in the small economies.

<sup>3</sup> Between 1982 and 1999 total world foreign direct investment grew from around 0,5 per cent to around 3,5 per cent of world GDP. See Hines (2004), that reports data from the World Bank database *World Development Indicators*.

<sup>4</sup> Empirical studies have shown other relevant features of tax havens. For instance, better-governed countries seem more likely to become tax havens (Dharmapala and Hines, 2006). A possible interpretation of this is that only better-governed countries can credibly commit not to expropriate foreign investors. It is not clear, however, whether it is the decision to become a tax haven that affects the quality of local governance or the quality of governance itself is influenced by economic and political conditions that also determine whether or not a country becomes a tax haven. Another relevant finding (from studies referring to American multinational firms) is that the highest share of tax haven operations seem to come from large firms with high volumes of international activity, high R&D intensity and significant volumes of intrafirm trade (Desai, Fritz Foley and Hines, 2006b). For these firms tax haven affiliates appear to facilitate the relocation of taxable income from high to low tax locations and to reduce the cost of deferring home country taxation of income earned in low tax foreign locations. Of course, the issue at stake here is not the tax haven characteristics of the jurisdiction, but the existence of a low rate of tax.

*instance, those aimed at establishing “export platforms” that provide market access for goods and services from the home country), while a substitute link holds for other types of FDI (those aimed at establishing production facilities for goods and services). Thus, the overall impact of tax havens on the welfare of high-tax countries is still ambiguous. Tax haven operations may stimulate activity in nearby countries by facilitating the avoidance of taxes in that country, the avoidance of taxes elsewhere, or by reducing the cost of goods and services that are inputs to production or sales in high-tax countries. At the same time, tax haven activity could provide governments of high-tax countries with a device to move toward a less-distorting tax regime, that could not otherwise be implemented, mainly for political constraints. The use of tax havens could in fact allow high-tax countries to apply a lower effective tax rate on mobile firms compared to the one applied on immobile firms. On the other hand, tax avoidance and evasion will erode the tax base and therefore tax revenues of high-tax countries. In a recent study, Slemrod and Wilson (2006) demonstrate that the full or partial elimination of tax havens would improve welfare in non-haven countries, reduce compliance costs and lead to a more balanced tax structure.*

Even if the conclusions of the theoretical and empirical analysis are somewhat still controversial, policy makers in non-haven countries are increasingly concerned about the potential adverse effects of tax haven activity on their national tax systems and, more generally, on their economies. These concerns have prompted many governments to consider international cooperative efforts designed to preserve their economies from the negative externalities due to tax havens. Following an endorsement by the G-7 at the Lyon Summit in June 1996, the OECD launched in 1998 the *Harmful Tax Practices* initiative<sup>5</sup> to discourage OECD Member countries and certain tax havens outside the OECD from pursuing policies that were thought to harm other countries by unfairly eroding tax bases.

The OECD initiative has evolved considerably since its launch in 1998, offering a forum for constructive dialogue between on and offshore financial centres. Overtime, an increasing emphasis has been put on access to bank and financial information and on exchange of taxpayer-specific information between national tax authorities, which are increasingly viewed as necessary pre-conditions for the effective functioning of national tax systems in a context where the ever-increasing levels of foreign direct investment and of portfolio cross-border capital flows implies the risk of a growing demand for tax haven operations. In the OECD’s view, an effective information exchange should allow all countries to protect the integrity of their tax system from the effects of international tax

---

<sup>5</sup> OECD (1998), hereafter “the 1998 Report”. Luxembourg and Switzerland abstained on the approval of the Report.

evasion, while preserving the right to tailor their tax systems to their own needs.<sup>6</sup> Put it another way, effective cooperation to counter abuse is an essential requirement to get the full benefits of a more competitive environment.

Conversely, the existence of obstacles hampering the access to financial information by domestic and foreign tax authorities leads to adverse consequences. First, it distorts international capital flows, since funds can be attracted by or routed through countries whose strict secrecy provisions offer a favorable environment to tax evaders. Second, it has adverse consequences on the structure of national tax systems, since the tax burden is shifted from capital to less mobile factors (such as labor) or consumption, in an attempt to limit the erosion of the tax base. Preventing the full taxation of income arising from portfolio investments, the lack of access to bank information jeopardizes the overall equity of the tax system, both between compliant and non-compliant taxpayers and among different income sources. Strict bank secrecy rules may represent a significant constraint for governments wishing to raise a given amount of tax revenues in order to be able to deliver the desired amount of public goods. This latter effect is particularly serious for developing countries where capital flight towards bank secrecy jurisdictions may give rise to an erosion of their already potentially weak tax base, which can seriously undermine the ability of governments to make the vital investments in social services and economic infrastructure upon which sustainable economic development depends. Finally, strict bank secrecy regimes may have adverse effects in domains other than taxation, attracting money laundering and other types of criminal activities, ranging from terrorism to financial fraud.

The issues of bank secrecy and information exchange and, in more general terms, the need for an increased level of transparency - have become a priority also on the political agenda of other international organizations, particularly those dealing with the different forms of financial abuse or taking care of the stability of the international financial system: both the *Financial Stability Forum* (FSF) and the *Financial Action Task Force on Money Laundering* (FATF) have undertaken efforts to convince offshore financial centers to comply with international standards by requiring, among other things, enhanced transparency.<sup>7</sup>

---

<sup>6</sup> OECD (2004a).

<sup>7</sup> In April 2000 the *Financial Stability Forum* (FSF) launched an assessment of the compliance of supervisory and regulatory systems of the OFCs' financial sector with international standards with the prospect of enhancing financial stability and fighting financial fraud and the financing of terrorism. The assessment led to the identification of several OFCs, especially in the smaller and poorer jurisdictions, having critical deficiencies. In the

The lifting of bank secrecy and the need for information exchange have received considerable attention in the economic literature (see Box 2), which has also tried to answer the question of whether information exchange agreements can arise spontaneously.

**Box 2 - The theoretical and empirical analysis on information exchange: a survey**

*In the theoretical literature, the lifting of bank secrecy and the need for information exchange between national tax authorities have received consideration within the analysis of the impact of tax policy on mobile financial capital in a context of open economies (Giovannini 1990; Bacchetta and Espinoza 1995; Huizinga and Nielsen 2000; Makris 2003; Sørensen 2001; Keen and Ligthart 2003). Information exchange between tax authorities and the prerequisite of access to relevant information have been recognized as essential for the taxation of capital income according to the residence principle. The residence principle is recommended by several authors as a second-best measure to the full coordination of tax policies (interpreted as a system of uniform tax rates and uniform tax bases: see, for instance, Giovannini, 1990, and Sørensen, 2001), since it allows national governments to choose their own preferred tax rates without violating international production efficiency, i.e. without distorting the location of international investment (the Diamond and Mirrlees theorem, 1971).<sup>8</sup> Other reasons in favor of the residence principle are interpersonal equity, as it allows for the progressive taxation of worldwide capital income, and a fair distribution of tax revenues among countries (since each country is able to tax its own residents).*

*An effective implementation of the residence principle is only possible when national tax authorities have full information on foreign source income earned by domestic taxpayers. This condition is met when information exchange covers all types of foreign source income and when foreign tax authorities have access to all relevant information. In practice, however, information exchange is far from perfect, mainly for two reasons: transaction costs and differences in country incentives. The last factor is probably the most important: the level of information sharing with foreign*

---

same year the *Financial Action Task Force on Money Laundering* (FATF) undertook an initiative to identify non-cooperative countries and territories in the fight against money laundering. Between 2000 and 2001 the FATF identified a list of 21 non-cooperative countries and territories, among which several Caribbean OFCs. Thanks to the significant and rapid progress in addressing deficiencies, all countries have been gradually removed from the list.

<sup>8</sup> The residence principle is consistent with the Capital Export Neutrality (CEN) condition, since it implies that the taxpayer faces the same tax burden on domestic and foreign source income. In the presence of different marginal tax rates across countries, the CEN condition implies that the international allocation of investments is neutral because the cost of capital (the required pre-tax rate of return) is equated across countries. For this reason the residence principle is considered superior to the source principle of taxation, which implies taxation of capital income at different rates depending on the country of the investment. The source principle allows for neutrality in the international allocation of savings and is thus consistent with the condition of Capital Import Neutrality (CIN), since it assures that capital income is taxed in the source country (usually through withholding taxes) at the same rate for residents and non residents and that foreign source capital income is exempted from tax in the investors' home countries. However, it distorts the investment decisions because it allows the pre-tax rates of return to differ among countries.

governments is considered a strategic variable and is taken into account by national governments when designing the optimal international tax system in the same way as the tax rate on domestic and foreign source income (Bacchetta and Espinoza, 1995). Since countries face a diverse set of incentives to exchange taxpayers' information, it is far from clear that information exchange agreements can be self-enforcing.<sup>9</sup> This question has been addressed by several studies. Assuming perfect capital market integration, Eggert and Kolmar (2002) show that there exist equilibriums where information exchange arises spontaneously. However, this happens in a paradoxical context, where the high elasticity of capital makes governments unable to apply any tax that could potentially benefit from the exchange of information (typically, taxes on capital income). In other words, if capital is perfectly mobile, information exchange arises spontaneously but is useless, since all the taxes that are potential candidates for information-induced tax-base effects simply disappear. In the authors' opinion, this model can help explain why in recent years the growing integration of capital markets is being accompanied by some progress in measures of tax information exchange.

Apart from the paradoxical case of perfect capital mobility described by Eggert and Kolmar, three sets of circumstances have been identified in which countries may find in their interest to provide information (Keen and Ligthart, 2003). The first can be modeled as a two-stage game where countries first decide the level of information exchange and then set the tax rates. Assuming that the institutional features of the tax system are given from the outset to tax authorities, Bacchetta and Espinosa (1995) find that a country may choose to provide at least some information to foreign tax authorities if this enables the information-receiving country to increase its own income tax rate. These conclusions are confirmed by Sørensen (2001). On the other hand, using the same two-stage game framework, but with the different assumption that all the institutional features of the tax system (i.e. the degree of information exchange and the level of tax rates) are chosen by the tax authorities instead of being given from the outset,<sup>10</sup> Makris (2003) finds not only that the non-cooperative equilibrium is characterized by zero information transmission, but also that there is no scope for cooperation in information sharing policies, irrespective of the transactions cost function and of the double taxation schemes. In fact, he shows that a coordinated increase in information exchange not only will make no difference, but in the case where information exchange is an equilibrium outcome, it will even leave countries worse off.

---

<sup>9</sup> Some countries may choose to not release bank information to foreign jurisdictions in the attempt to enhance their attractiveness for foreign investors, thereby increasing the size of their financial industry, employment and national welfare. Other countries, particularly those which have substantial capital outflows, may be interested in obtaining information on portfolio investments made abroad by their residents, in order to limit the erosion of their tax base due to underreporting of foreign source income. In general, the discrepancy in the values placed by any two countries on each other's taxpayer information depends on a number of factors (Tanzi and Zee, 2001). The most relevant are: asymmetries in the economies' size (as GDP level, taxpayers' number, capital flows, etc.); differences in the capital account balances (taxpayer information provided by the tax authorities of a capital-importing country to a capital-exporting country is more valuable to the latter than similar information to the former provided to it by the latter); differences in the completeness and reliability of information gathered by national tax administrations.

*The second possibility, explored in a later paper by Bacchetta and Espinoza (2000) and by Huizinga and Nielsen (2002), is one where countries view the choice of tax rates and information provision as an infinitely repeated game and continuously adapt their decisions to those of other countries. In this setting, information exchange arises spontaneously if the possible advantages that each country can have by defecting from (or not entering) the agreement are balanced by some form of punishment.<sup>11</sup> The result of this balance – and hence the long-term sustainability of cooperative information exchange agreements – depends on several variables. The attractions of defection will be greater the higher are policy-makers' discount rates (information exchange is more likely to be chosen if governments have little discounting of the future, i.e. if they are long-term oriented), the more imbalanced are capital flows and the more sensitive are capital flows to their effective tax treatment. One clear implication of this approach is that small capital-importing countries are likely to have least to gain from information exchange: for these countries, the advantages arising from the choice of lower tax rates in order to attract inward investment - an increase in the size of the banking and financial industry, a resulting increase of the wage tax base and of welfare in general - largely compensate the losses of any revenue from the small domestic capital tax base.*

*The third possibility consists in introducing some kind of compensation rather than punishment in order to induce countries to exchange information, as proposed by Keen and Ligthart (2003, 2004). Countries may redistribute to the information providing jurisdictions a certain proportion of the additional revenue they are able to collect thanks to the exchange of information, in order to compensate them for the adverse economic effects of voluntarily engaging to exchange information. Keen and Ligthart (2004) show that while large countries always prefer information exchange with any level of revenue sharing (since they always gain more from taxing their residents thanks to the information they receive compared to what they lose from the transfer of a certain amount of revenues to the information providing countries) small countries only have attractions to information exchange if the difference in size with the information receiving country is not very pronounced and if the share of revenue they receive from the residence country is sufficiently large.<sup>12</sup>*

*An issue connected with the implementation of information exchange is the “third country problem”, i.e. whether a group of countries (i.e., the OECD or the EU) as a whole can gain from reaching an agreement on information exchange if the rest of the world does not join into the agreement. Unless all countries take part in the information exchange, the gains to any subset from*

---

<sup>10</sup> Unlike Bacchetta and Espinoza, Makris assumes that all distortionary tax rates can be different and endogenously determined.

<sup>11</sup> Since in this context it is likely that uncooperative behaviour by any country would lead to other countries behaving also non-cooperatively, each country must balance the long-term gains from continued cooperation with the temporary gain from failing to provide information and with the permanent cost of non-cooperative behaviour by the other countries.

<sup>12</sup> When the difference in size with the information receiving country is very pronounced, small countries may resist moving to exchange information, whatever the share of revenue sharing. If, however, the size of the two countries is sufficiently close, the small country will prefer information exchange even if all the additional revenue it generates is retained by the information receiving country (the residence country).

agreeing to exchange information are likely to be reduced to the extent that third countries continue to provide an opportunity to invest without declaring the proceeds. These latter countries could even become more aggressive in tax competition because of their enhanced monopoly power in the provision of strictly confidential saving schemes and in consideration of their potentially higher gains. Since small countries have probably more to gain from remaining outside information exchange agreements, and since the number of small jurisdictions is quite high, the difficulties of implementing a truly comprehensive information exchange agreement are obvious. However, it is also possible that the small dimension of these countries represents a factor of vulnerability on which bigger countries can rely to persuade the small ones to agree to exchange information.

To sum up, it turns out from the theoretical literature that it is unlikely that full information exchange will spontaneously emerge, particularly because offshore financial centers have little interest to agree to any international agreement that will curb their ability to attract capital, unless some form of positive incentives is given. This solution requires a coordinated effort on a multilateral basis and needs to be extended to as many tax havens and bank secrecy jurisdictions as possible in order to reduce the risk of defections.

The empirical literature on the implications of bank secrecy is more limited. A few studies (Grilli, 1989; Alworth and Andresen, 1992; Huizinga and Nicodème, 2004) have found a certain degree of sensitivity of international bank deposits to bank secrecy and other tax variables, from which it could be argued that cross-border financial flows are, at least to a certain extent, “tax-driven”, i.e. affected by tax cheating purposes.

### **3. Origins and evolution of the Caribbean tax havens**

Most tax havens are small, very open economies, and this is particularly true in the Caribbean region where the majority of islands have, over the last thirty years, moved into the offshore financial business. At least three reasons can explain this development.

- a) *The agricultural sector* in the Caribbean area was increasingly unviable as preferential trading schemes were removed and more efficient producers entered their traditional markets;
- b) *Few of the islands* have any natural resource endowments;
- c) *Tourism*, which was highly successful in certain of the islands, was volatile and, in some cases, it could not be further exploited.

Financial services have been seen as an area in which, for a modest initial investment, Caribbean islands could upgrade the skills of the population, generate employment and revenues for their governments and, more generally, boost their GDP by taking advantage of the high growth rate of the industry.

For some of these dependencies the move towards the offshore financial center and tax haven status was quite successful and led to significant rates of economic growth. Their colonial heritage gave them important competitive advantages, among which a modern-style legal system (usually based on the Anglo-Saxon model), English language (for most of them), a currency tied to that of the mother country, and in many cases the benefit of tax treaties which had been extended to them. These advantages were strengthened through the introduction of attractive rules for the incorporation of international business companies (IBCs) and for the establishment of trusts, the adoption of zero or very low taxes on incomes, profits and wealth tax (particularly for foreign-source and non-resident income), the absence of exchange controls and the introduction of strict bank secrecy and confidentiality of information rules.<sup>13</sup> Further advantages were the political stability, a pleasant physical environment and, more importantly, the proximity to or links with major on-shore financial centers (such as the US and the UK).<sup>14</sup>

In the Caribbean region these factors allowed the Bahamas first and the Cayman Islands soon later to become leading offshore financial centres, moving from poor subsidized economies in the beginning of the 1960s to net providers of resources to the Commonwealth since the 1980s. The Bahamas is nowadays ranked among the top five locations in the world for offshore mutual funds and trust funds and has also developed a significant inter-bank market. The Cayman Islands are nowadays the world's fifth largest banking centre, and the first among offshore jurisdictions, with a prominent position both in the inter-bank business and in private banking. The Cayman also host half of the world's hedge funds, hundreds of major non-financial subsidiaries of US corporations and the World's second-largest captive insurance market. The British Virgin Island has developed into one of the most successful centres for IBCs and Trust arrangements.

The Netherlands Antilles developed as a typical "treaty tax haven", being used in the 1960s through the mid-1980s to allow non-resident investors to receive portfolio income from the United States tax free.<sup>15</sup> Once the US abolished its withholding tax, there was no longer

---

<sup>13</sup> For instance, the rules for the legal protection of bank secrecy were introduced in 1966 in the Cayman Islands and in 1980 in the Bahamas.

<sup>14</sup> Sullivan (2004) reports that, according to the Cayman Islands Monetary Authority 2002 Annual Report, about 70 percent of the international assets and liabilities booked through the Cayman Islands originate from the US.

<sup>15</sup> Until 1984, interest income received by non-residents from US sources was subject to withholding tax, either at 30 percent or at a lower rate as provided in a tax treaty. Since the treaty between the US and the Netherlands

any motive for taking this route. Nowadays, the country is not anymore among the most prominent offshore jurisdictions, and is trying to develop other sectors of the offshore industry, namely incentives aimed at international business companies.

In more recent years, the demand for tax haven facilities has considerably expanded, owing to the high growth rates of cross-border investment and to the increased number of potential customers arising from the new possibilities offered by the new technological and communication infrastructures and the growing use of multiple layers of transactions to structure offshore operations through vehicles located in different countries. The gradual relaxation of reserve requirements, interest rate controls and capital controls in the main “onshore” markets and the creation of offshore banking facilities in some of the main industrial countries (the US and Japan) have reduced the regulatory advantages of offshore financial centres, making them less attractive for conventional banking. On the other hand, the tax avoidance facilities of OFCs have become more and more important, particularly for FDI and asset management.<sup>16</sup> The limited initial investments needed to enter the offshore industry have induced new countries, especially the smaller ones, to implement the “offshore package” of financial services and asset protection products in order to join in the competition for attracting internationally mobile capital:<sup>17</sup> hence, the number of tax havens has grown remarkably. This process have involved also some new entrants in the Caribbean area: Antigua and Barbuda, St. Kitts and Nevis, Grenada, Dominica, St. Lucia.

In this more competitive environment, the choice of a tax haven is increasingly determined by their ‘specialization’ and by their proximity to target investment markets, although in some cases the geographical proximity to taxpayers still acts as a driver.<sup>18</sup> Some Caribbean tax havens have been able to succeed or to retain their market share thanks to

---

Antilles reduced the withholding tax rate to zero, and the Netherlands Antilles did not charge any withholding tax, the country was used to route interest payments from the US to third-country recipients free of taxes at source.

<sup>16</sup> With reference to this latter market, it is especially the possibility to reduce inheritance and other capital taxes for individual investors that acts as a prime incentive and has led to a large expansion in offshore fund management activity, in particular by the use of investment vehicles such as trusts and private companies.

<sup>17</sup> For example, Malta launched its international financial centre facilities in 1994.

<sup>18</sup> Thus in the last few years, we have witnessed the growth of some new OFC and tax haven practices in the East-Asia region, where some jurisdictions (Labuan in Malaysia, and Samoa) are emerging thanks to their ability to intermediate in a “tax-efficient” way the growing capital flows which circulate in the area. Given the significant economic growth rates currently reached by some of the biggest countries in the region, such as China and India, the global weight of Asian OFCs - both of well established ones, such as Singapore and Hong Kong, and of those which seem to be emerging more recently - is likely to increase.

product diversification and specialization in specific market niches. For instance, Bermuda is nowadays one of the world's biggest insurance and reinsurance markets; the British Virgin Islands have become one of the world's favorite locations for international business corporations (which are used exclusively as offshore vehicles); the Bahamas have developed a significant inter-bank market. Furthermore, in order to enhance their reputation, some of the most significant Caribbean offshore centres have taken the political decision to commit to tax information exchange by entering into *Tax Information Exchange Agreements* (TIEAs).<sup>19</sup>

Some of the late arrivals in the Caribbean region and elsewhere, however, have had little success, because they have not been able to offer any advantage over the more established centers.<sup>20</sup> Overall, it is fair to say that with the exception of the Bahamas, Bermuda, British Virgin Island, the Cayman Islands and Panama, the other Caribbean offshore financial centres are struggling to make their financial activities a sustainable part of their economies.

#### **4. The position of the Caribbean tax havens in the global financial markets**

The relative importance of Caribbean tax havens can be measured through several indexes. However, a difficulty often encountered when trying this kind of estimates is the limited availability of reliable and internationally comparable data for many sectors of the OFC industry.

Suss, Williams and Mendis (2002) collect some relevant indicators with reference to 2001 or previous years. Overall, these indicators show that the size of the Caribbean tax havens and offshore financial centers varies significantly from one country or territory to another, and that there is a wide range of specialization across the region. So, for instance, while the British Virgin Islands is the largest register of international business companies (estimated to account for 48 percent of global IBC incorporations), the Cayman Islands, estimated to be the fifth largest offshore financial center in the world, has fewer registered IBCs, but significantly more banks, insurance companies and trusts. Among recent entrants into the OFC sec-

---

<sup>19</sup> The Cayman Island, for example, has a TIEA with the United States and Bermuda; Antigua has one with Australia; the Netherlands Antilles have signed a TIEA with Australia and New Zealand.

<sup>20</sup> This was the case, for instance, of Dominica, Grenada, St. Lucia and, to a lesser extent, St. Kitts and Nevis.

tor, St. Kitts and Nevis has the largest number of registered IBCs, while Antigua and Barbuda has the most diversified OFC industry, including not only IBCs, but also banks and trusts.

The study also examines the contribution of the OFC sector to specific economic indicators. So, for example, it emerges that in many Caribbean jurisdictions employment opportunities arising from the OFC industry are significant. In 2000 the estimated employment in the OFC sector represented 15 percent of the labor force in the British Virgin Islands, 8 percent in Antigua and Barbuda, 1 percent in the Bahamas and 0.5 percent in Dominica. The wide range of variation depends both on the relative size of the economy and on the type of OFC business prevailing in each jurisdiction (for instance, offshore banks and shell companies do not require physical presence and as such, do not require a significant number of people).

Another significant indicator used in the study is the amount of the fees collected by the central government from OFCs service providers. As of end-2000, Antigua and Barbuda derived over 7 percent of central government revenues from offshore sector fees, followed by Grenada at 4.5 percent and Anguilla at 3.6 percent. Among the more established OFCs, the British Virgin Islands, which is the world market leader in incorporation of international business companies, collected fees representing 55 percent of government revenues, equal to 13 percent of GDP. The Cayman Islands also rely heavily on fees collected from offshore banks, which accounted for 14.5 percent of government revenues by end-2000. In contrast, the governments of Bahamas and Barbados were less dependent on offshore sector fees (respectively: about 1 percent of government revenues and between 0.2 percent and 0.4 percent of GDP).

Further information on the weight of the financial industry and offshore business for tax havens can be obtained looking at the contribution of these sectors to GDP. According to the limited information publicly available, it can be estimated that at end 2001 the contribution of all offshore services to GDP ranged from around 25 percent in the Cayman Islands to 30 percent in the Bahamas and 45 percent in the British Virgin Islands. For other tax havens, the only available information was the GDP share of the whole area of services; quite often, the financial sector and tourism represent the main components of this share. According to available information, at end 2001 the GDP share of all services was 89 percent for Bermuda, 84 percent for the Netherlands Antilles, 81 percent for Montserrat, 77 percent for Antigua and Barbuda.

With reference to the offshore banking sector, a more detailed set of comparable sta-

tistical data can be taken from the Bank for International Settlements *Locational Statistics* as complemented, in some cases, by national sources.

Table 1 reports (at the first column) the size of foreign bank liabilities as a multiple of GDP<sup>21</sup> for a set of offshore financial centers that have historically relied heavily on bank secrecy and for other representative offshore and mainstream financial centers; the second column of the table reports each country's share of global foreign bank liabilities. Countries in each group are ranked according to the amount of their foreign liabilities *vis-à-vis* all sectors, banks and non-banks.

The Caribbean tax havens amount to just under 8.5 percent of the world foreign bank liabilities. As can be expected, the foreign liability/GDP ratio is much higher in small havens compared to other financial centers, however, even within small countries, the ratio shows a wide diversity, ranging from the highest value of 617.87 in the Cayman Islands to less than 0.11 for Aruba. Apart from the Cayman Islands and, to a lesser extent, the Bahamas, the Netherlands Antilles and Bermuda, for the remaining tax havens the banking business with non-residents seems to be far less important, confirming the specialization of the different Caribbean jurisdictions.

Table 2 reports similar indicators with reference to the amount of bank deposits of non-bank non-residents for a subset of countries for which relevant data are available. These indicators can be useful to assess more specifically the value of private banking in each tax haven. Once again, the Cayman Islands show a very high ratio (bank deposits *vis-à-vis* non-bank non-residents being equal to 230.87 times the country GDP), followed at a distance by the Bahamas (21.52). Also the share of total bank deposits of non-resident non-banks which is held by the most prominent offshore financial centers appears to be significant: as can be seen from the last column in the table, the Cayman Islands hold more than 10 percent of the global stock of these deposits, a share comparable to that of Switzerland and higher than the United States.

TABLE 1 HERE

TABLE 2 HERE

---

<sup>21</sup> Data on GDP are from the *World Development Indicator* of the World Bank.

## **5. The OECD initiative on *Harmful Tax Practices* and the position of Caribbean jurisdictions**

### **5.1 The OECD *Harmful Tax Practices* initiative**

In 1998, the OECD Ministerial Council established a forum which identified the following four key criteria for identifying harmful tax practices:

- a) No or nominal taxes, in the case of tax havens, and no or low taxation, in the case of Member country preferential tax regimes;
- b) Lack of transparency.
- c) Lack of effective exchange of information.
- d) No substantial activities, in the case of tax havens, and ring-fencing, in the case of Member country preferential regimes.

The no/nominal/low taxes criterion was intended merely as a gateway to determine those situations in which an analysis of the other criteria is necessary. The adoption of low or zero tax rates is *never* by itself sufficient to identify a jurisdiction as a tax haven. The OECD does not prescribe appropriate levels of taxation or dictate the design of any country's tax system. This work has received considerable political support.<sup>22</sup>

In 2000, the OECD identified 35 jurisdictions that were found to meet the tax haven criteria.<sup>23</sup> A process was also established whereby the identified tax havens could commit to improve transparency and establish effective exchange of information for tax purposes. Those jurisdictions that were not willing to make such commitments would be included in a list of uncooperative tax havens. Thus, the key distinction for OECD countries became whether a tax haven was cooperative or uncooperative. *The 2001 Progress Report* made certain

---

<sup>22</sup> The G7/8 Finance Ministers have consistently provided political support for the project and the G-8 Heads of Government confirmed their support at the Gleneagles Summit in July 2005. Also, at the November 2004 meeting of the G-20 Finance Ministers a strong statement in support of this work was issued and further endorsement of this work was provided in the most recent G-20 Communiqué issued in November 2006 and in a Communiqué from the Caribbean-UK Forum on 28 April 2006.

<sup>23</sup> Andorra; Anguilla; Antigua and Barbuda; Aruba; The Bahamas; Bahrain; Barbados; Belize; British Virgin Islands; Cook Islands; Dominica; Gibraltar; Grenada; Guernsey; Isle of man; Jersey; Liberia; Liechtenstein; the Maldives; Marshall Islands; Monaco; Montserrat; Nauru; Netherlands Antilles; Niue; Panama; Samoa; Seychelles; St. Lucia; St. Kitts and Nevis; St. Vincent and the Grenadines; Tonga; Turks and Caicos; US Virgin Islands; Vanuatu. Six other jurisdictions - Bermuda, Cayman Islands, Cyprus, Malta, Mauritius and San Marino - were not included in the 2000 report because they committed to eliminate their harmful tax practices prior to the release of that report.

modifications to the tax haven work. There were two principal modifications. First, a tax haven that committed to eliminating lack of transparency and lack of effective exchange of information would be considered cooperative and therefore would not be included on the OECD's list of uncooperative tax havens. A second modification was that a potential framework of coordinated defensive measures would not apply to uncooperative tax havens any earlier than it would apply to OECD countries with harmful preferential tax regimes. In April 2002, the OECD published the list of uncooperative tax havens, containing 7 jurisdictions that still were at that time unwilling to commit to transparency and exchange of information for tax purposes; two jurisdictions - Nauru and Vanuatu - made commitments in 2003 and the list now contains only 5 jurisdictions: Andorra, Liberia, Liechtenstein, the Marshall Islands and Monaco.

The 33 jurisdictions that made commitments to transparency and effective exchange of information are referred to as Participating Partners. The OECD and non-OECD Participating Partners have worked together in the *Global Forum on Taxation* to develop the international standards for transparency and effective exchange of information in tax matters. The Caribbean offshore financial centers have played a particularly active role in the Forum. They took part in the specially created working group which developed the 2002 *Model Agreement on Exchange of Information on Tax Matters*.<sup>24</sup>

In order to determine exactly where countries stand in relation to transparency and information exchange, the Global Forum decided at its June 2004 meeting in Berlin that it was important to carry out a review of countries' legal and administrative frameworks in these areas so as to assess progress towards a level playing field. In addition to Global Forum Participating Partners (Table 3a), other significant financial centers (Table 3b) were invited to participate in the review.<sup>25</sup> Overall, the factual assessment covered 82 countries.

---

<sup>24</sup> Available on the OECD website at <http://www.oecd.org/ctp>. The Model Agreement, released in March 2002, was developed by the Global Forum Working Group on Effective Exchange of Information which consisted of representatives from OECD countries and delegates from Aruba, Bermuda, Bahrain, Cayman Islands, Cyprus, Isle of Man, Malta, Mauritius, the Netherlands Antilles, the Seychelles and San Marino. The work of that group has been complemented by the work of the Global Forum's Joint Ad Hoc Group on Accounts which has developed guidance on accounting and recordkeeping requirements for corporations, partnerships, trusts and other entities or arrangements.

<sup>25</sup> All Global Forum Participating Partners except Antigua and Barbuda and Grenada responded to the questionnaire which forms the basis of the factual assessment. The information of the factual assessment about Antigua and Barbuda and Grenada is based on publicly available information or information previously provided by Antigua and Barbuda and Grenada. Among the invitees, all but two – Brunei and Liberia – responded to the ques-

### TABLE 3 HERE

The Report “*Tax Co-operation: Towards a Level Playing Field - 2006 Assessment by the Global Forum on Taxation*” issued in May 2006 reflects the outcome of the factual review carried out by the Global Forum. All the OECD and non-OECD Participating Partners in the Global Forum on Taxation have endorsed the principles of transparency and exchange of information for tax purposes that are reflected in the Report. They have also agreed to their legal and administrative frameworks being reviewed in the light of these principles. For the first time, other significant non-OECD economies such as Hong Kong, China and Singapore have participated in the work of the Global Forum in these areas. Six of these non-OECD economies have also endorsed the principles of transparency and exchange of information and agreed to work with the Global Forum towards a level playing field: Argentina; China; Hong Kong, China; Macao, China; the Russian Federation and South Africa.

## **5.2 How do the Caribbean and other financial centers measure up to these criteria?**

The results of the Global Forum assessment of legal and administrative practices concerning transparency and information exchange is a valuable mean to examine the current standpoint of the Caribbean tax havens towards the OECD *Harmful Tax Practices Initiative*. Their position regarding the different aspects of the assessment is as follows:

### ***A. Exchanging Information***

Many of the Caribbean jurisdictions have (or are in the process of negotiating) exchange of information arrangements that permit them to exchange information for both civil and criminal tax purposes in the form of double tax conventions or TIEAs (some exceptions are Anguilla, Panama and Turks and Caicos). In addition, as a practical matter, Panama is

---

tionnaire used as the basis for the factual assessment. Liberia was unable to do so due to its current political situation.

rarely, if ever, able to exchange information in criminal tax matters. None of the Caribbean jurisdictions reported having a *domestic tax interest*, i.e. being unable to respond to a request for information where they have no interest in obtaining the information for their own tax purposes. Also, none of the Caribbean jurisdictions reported applying the principle of dual incrimination to all their information exchange relationships concerning the administration or enforcement of domestic tax law. However, Saint Lucia and Saint Vincent and the Grenadines apply this principle in connection with exchange of bank information (see Section B below).

### ***B. Access to Bank Information***

While in 77 countries covered by the factual assessment governmental authorities have access to bank information and/or information from other financial institutions for at least some tax information exchange purposes, among the Caribbean jurisdictions Panama have indicated an inability to access bank information for any exchange of information purposes. In 17 countries, access to bank information is granted only for the purpose of responding to a request for exchange of information in criminal tax matters. Of these the Caribbean jurisdictions of Saint Lucia, Saint Vincent and the Grenadines (in addition to Andorra, Austria, Cook Islands, Luxembourg, Samoa, San Marino, and Switzerland) apply the principle of dual criminality in connection with access to bank information for exchange of information purposes.

### ***C. Access to Ownership, Identity and Accounting Information***

Of the 82 countries reviewed, 78 - including all the OECD countries - generally have powers to obtain information that is kept by a person subject to record keeping obligations which may be invoked to respond to a request for exchange of information in tax matters. In addition, 71 countries reported that they also generally have powers to obtain information from persons not required to keep such information which may be invoked to respond to a request for information. Anguilla, Montserrat, Panama and Turks and Caicos Islands have very limited powers to obtain this kind of information for criminal tax matters.

#### ***D. Availability of Ownership, Identity and Accounting Information***

##### *Companies*

Of the 82 countries reviewed, 77 require companies to report legal ownership information to governmental authorities or to hold such information at the company level. Three countries (Montserrat, Saint Kitts and Nevis and the U.S. Virgin Islands) each have one form of company where this is not the case<sup>26</sup>. More stringent ownership reporting requirements exist in the financial sector in certain countries. All but 5 countries (Aruba; Guatemala; Hong Kong, China; Macao, China and Singapore) indicated that applicable anti-money laundering legislation would normally require corporate service providers or other service providers to identify the beneficial owners of their client companies.

In 75 countries, all domestic companies are required to keep accounting records. No such requirements exist for international business companies in Belize, Brunei and Samoa or for limited liability companies in Anguilla, Montserrat and Saint Kitts and Nevis<sup>27</sup>. In the Bahamas, only public companies and regulated companies in the banking, securities and insurance sectors are required to keep accounting records. Mandatory accounting records retention periods of five years or more exist in 63 countries.

Bearer shares may be issued in 48 countries. Of these, 39 have adopted mechanisms to identify the legal owners of bearer shares in some or all cases. Furthermore, 10 of these 39 countries (Antigua and Barbuda, Belize, British Virgin Islands, Cayman Islands, the Cook Islands, Dominica, Grenada, Montserrat, Saint Kitts and Nevis and Saint Vincent and the Grenadines) also require bearer shares to be immobilized or held by an approved custodian. The remaining 29 rely mainly on anti-money laundering rules, investigative mechanisms or a requirement for the holders of shares to notify the company of their interest in the shares. Anguilla is one of the 9 countries that reported not having any mechanism to identify the owners of bearer shares, although it indicated to plan to adopt such mechanisms in the near future.

Bearer debt instruments may be issued in 52 countries and 40 of these have adopted mechanisms to identify the owners of such instruments. In general, these mechanisms rely on anti-money laundering rules, on investigative powers or, in the case of EU Member

---

<sup>26</sup> With respect to Grenada there was not sufficient information to reach a conclusion.

<sup>27</sup> In these cases only records that the directors of such consider necessary or desirable need to be kept

States and their associated or dependent territories, on procedures set out in the EU Savings Tax Directive and savings tax agreements.

### *Trusts*

Of the 82 countries reviewed, 54 have trust law. Of these, Macao, China and the Seychelles have no trust law applicable to residents, but have trust law applicable to non-residents. Information on the settlers and beneficiaries of domestic trusts is required to be held under the laws of 47 countries. In 36 of the countries with trust law, a domestic trustee of a foreign trust would also be required to have information on the identity of settlers and beneficiaries, in some or all cases. Of the 28 countries that do not have trust law, 18 indicated that their residents may act as trustees of a foreign trust. In all of these, except for Luxembourg, there is a requirement on resident trustees to identify settlers and beneficiaries of foreign trusts. Of the 54 countries which have trust law, 45 countries reported requiring all trusts formed under their law to keep accounting records. Dominica, Saint Lucia and Turks and Caicos are among the 7 countries that have not reported a requirement to keep records under their trust law.

## **6. The way forward for Caribbean Offshore Financial Centres**

The future for Caribbean offshore financial centres depends, to a large extent, on their willingness to meet the new international standards that have been developed by such bodies as the FATF, the FSF and the OECD. Meeting these standards will enhance their reputation and make them more attractive as financial centres in which to carry out legitimate transactions.

For the more established centers, such as the Bahamas, the Cayman Islands and the British Virgin Islands, which have already developed relatively strong and extensive legislative and regulatory frameworks, the cost of introducing the additional measures necessary to comply with international standards need not be substantial. At the same time, the international community is committed to helping these countries and territories to implement effectively these standards. The main mechanism for this implementation in the tax area is *Tax Information Exchange Agreements* (TIEAs). These agreements provide an effective mechanism that minimizes the risk that these centres are misused by residents of

other countries to evade their tax responsibilities. Over the last few years, all the major Caribbean offshore financial centres, other than Panama, have entered into one or more TIEAs. We can expect that this trend will accelerate and that these OFCs will extend their network of TIEAs, not just with OECD countries, but also with major non-OECD countries (China, India, Brazil and South Africa have already begun negotiations).

In the case of some of the smaller Caribbean OFCs, they may decide that the burden of meeting these new standards means that the cost of having an offshore sector outweighs the benefits. In these cases, the international community needs to stand ready to provide assistance so that other economic activities are open up for these islands.

## References

- Alworth, J. and Andresen, S. (1992), *The determinants of cross-border non-bank deposits and the competitiveness of financial market centers*, *Money Affairs* 5, 105-133.
- Bacchetta P. and Espinosa, M.P. (1995), *Information sharing and tax competition among governments*, *Journal of International Economic*, No. 39, 102-121.
- Bacchetta P. and Espinosa M.P. (2000), *Exchange-of-information clauses in international tax treaties*, *International Tax and Public Finance*, Vol. 7, 275-93.
- Desai, M.A., Fritz Foley, C. and Hines J., Jr. (2004), *Economic Effects of Regional Tax Havens*, October.
- Desai, M.A., Fritz Foley, C. and Hines J., Jr. (2006a), *Do tax havens divert economic activity?*, *Economic Letters* 90 (2006), 219-224.
- Desai, M.A., Fritz Foley, C. and Hines J., Jr. (2006b), *The demand for tax haven operations*, *Journal of Public Economics* 90 (2006), 513-531.
- Dharmapala, D. and Hines J., Jr. (2006), *Which countries become tax havens*, paper submitted to the conference organized by the International Tax Policy Forum, Washington D.C., December 2006.
- Diamond, P. and Mirrlees, J.A. (1971) *Optimal Taxation and Public Production II: Tax Rules*, *American Economic Review*, Vol. 61, 261-78.

- Eggert, W. and Kolmar M. (2002) *Residence-based Capital Taxation: Why Information is Voluntarily Exchanged and why it is not*, International Tax and Public Finance, Vol. 9, 465-482.
- Giovannini, A. (1990) *International Capital Mobility and Capital Income Taxation*, European Economic Review, No. 34, 480-488.
- Gordon, R., J. and Hines, J., R. Jr. (2002), *International Taxation*, NBER Working Paper, No. 8854, April.
- Grilli, V. (1989), *Europe 1992: issues and prospects for the financial markets*, Economic Policy, October.
- Hines, J, Jr. (2004), *Do Tax Havens Flourish?*, NBER Working Paper 10936, November.
- Huizinga, H. and Nicodème G. (2004), *Are international deposits tax-driven?*, Journal of Public Economics, Vol. 88.
- Huizinga, H. and Nielsen, S.B. (2000), *The taxation of interest in Europe: a minimum withholding tax?* in Cnossen, S. (ed), *Taxing Capital Income in the European Union*, Oxford University Press.
- Huizinga, H. and Nielsen, S.B. (2002), *Withholding taxes or information exchange: the taxation of international interest flows*, Journal of Public Economics, No. 87, 39-72.
- Keen, M. and Ligthart, J.E. (2003), *Information Sharing and International Taxation: A Primer*, mimeo, Washington, D.C.: IMF - Fiscal Affairs Department.
- Keen, M. and Ligthart, J.E. (2004), *Incentives and Information Exchange in International taxation*, CentER Discussion Paper 2004-54.
- Makris, M. (2003), *International tax competition: there is no need for cooperation in information sharing*, Review of International Economics, Vol. 11 (3), 555-567.
- Mc Lure C. E. Jr (2005), *Will the OECD Initiative on Harmful Tax Competition Help Developing and Transition Countries?*, Bulletin of International Bureau of Fiscal Documentation, March.
- OECD (1998), *Harmful Tax Competition – An Emerging Global Issue*, Paris.
- OECD (2000), *Improving Access to Bank Information for Tax Purposes*, Paris.
- OECD (2004a), *The OECD's Project on Harmful Tax Practices: the 2004 Progress Report*, Paris.
- OECD (2004b), *A process for Achieving a Level Playing Field*, Outcome of the OECD Global Forum on Taxation in Berlin, 3-4 June 2004.

- OECD (2006), *Tax Co-operation, Towards a level playing field*, Paris.
- Rose, A.K. and Spiegel, M. M. (2006), *Offshore Financial Centers: Parasites or Symbionts?*, paper submitted to the conference organized by the International Tax Policy Forum, Washington D.C., December 2006.
- Slemrod, J. and Wilson, J.D. (2006), *Tax Competition with Parasitic Tax Havens*, NBER Working Paper, No. 12225, May.
- Sørensen, P.B. (2001), *Tax Coordination in the European Union: What are the issues?*, Swedish Economic Policy Review, Vol. 8, 143-195.
- Sullivan, M.A. (2004), *US Citizens Hide Hundreds of Billions in Cayman Accounts*, Tax Notes International, May 24.
- Sullivan, M.A. (2006), *A Challenge to Conventional International Tax Wisdom*, Tax Notes International, December 11.
- Suss, E.C., Williams O.H. and Mendis C. (2002), *Caribbean Offshore Financial Centers: Past, Present, and Possibilities for the Future*, IMF Working Paper, WP/02/88.
- Tanzi, V. and Zee, H. H. (2001), *Can Information Exchange be Effective in Taxing Cross-border Income Flows?*, in Andersson, C., Melz, P. and Silfverberg, C. (Eds.), *Modern Issues in the Law of International Taxation*, Dordrecht: Kluwer Law International.

Table 1 Weight of foreign banking activity in selected OFCs (2001)

	<b>Bank liabilities vis-à-vis non-residents as multiple of GDP</b>	<b>Country share of total bank liabilities vis-à-vis nonresidents (%)</b>
<b>CARIBBEAN OFCs IDENTIFIED AS TAX HAVENS BY THE OECD</b>		
The Cayman Islands	617.87	6.97
The Bahamas	20.86	0.94
Netherlands Antilles	13.33	0.28
Bermuda	3.91	0.13
Panama	0.73	0.11
Aruba	0.11	0.0020
Antigua and Barbuda	0.20	0.0013
St. Kitts & Nevis	0.26	0.0012
The Commonwealth of Dominica	0.31	0.0011
St Lucia	0.13	0.0010
Grenada	0.24	0.0009
St. Vincent and the Grenadines	0.12	0.0006
Anguilla	0.65	0.0006
<b>OTHER NON-OECD OFCs</b>		
Singapore	4.36	3.63
Hong Kong SAR	1.58	2.35
<b>OECD OFCs</b>		
Switzerland	3.16	5.70
Luxembourg	16.93	3.57
Belgium	1.16	2.71
Austria	0.46	0.90
<b>OTHER SELECTED FINANCIAL CENTRES</b>		
United Kingdom	1.65	20.77
United States	0.13	11.42
Germany	0.47	8.77
France	0.49	6.76
Japan	0.15	4.64

Sources: data on foreign liabilities are taken from BIS Locational Statistics and from national sources; data on GDP are from World Bank (World Development Indicators database), from national sources or from other international organizations estimates.

Notes: data on foreign liabilities and GDP are for 2001 when available, otherwise latest available.

Table 2 Weight of foreign private banking in selected OFCs (2001)

	<b>Bank deposits of non-resident non-banks as multiple of GDP</b>	<b>Country share of total bank deposits of non-resident non-banks (%)*</b>
<b>OFCs</b>		
The Cayman Islands	230.87	10.83
The Bahamas	21.52	4.04
Bahrain	2.02	0.89
Netherlands Antilles	3.21	0.28
Singapore	1.31	4.52
Hong Kong SAR	0.44	2.71
Switzerland	1.43	10.72
Luxembourg	5.37	4.70
Belgium	0.36	3.44
Austria	0.04	0.35
<b>OTHER SELECTED FINANCIAL CENTRES</b>		
United Kingdom	0.33	17.46
United States	0.02	7.01
Germany	0.15	11.33
France	0.04	2.34
Japan	0.01	1.13

Sources: data on non-residents bank deposits are from BIS Locational Statistics; data on GDP are from World Bank (World Development Indicators database), from national sources or from other international organizations estimates.

Notes: data at end 2001 when available, otherwise latest available; \*total stock for BIS reporting countries.

*Table 3 Countries covered by factual assessment*

**a) Global Forum Participating Partners**

Anguilla	Dominica	Korea	San Marino
Antigua and Barbuda	Finland	Malta	Seychelles
Aruba	France	Mauritius	Slovak Republic
Australia	Germany	Mexico	Spain
The Bahamas	Gibraltar	Montserrat	Saint Kitts and Nevis
Bahrain, Kingdom of	Greece	Nauru	Saint Lucia
Belize	Grenada	Netherlands	Saint Vincent and the Grenadines
Bermuda	Guernsey	Netherlands Antilles	Sweden
British Virgin Islands	Hungary	New Zealand	Turkey
Canada	Iceland	Niue	Turks and Caicos Islands
Cayman Islands	Ireland	Norway	United Kingdom
Cook Islands	Isle of Man	Panama	United States
Cyprus	Italy	Poland	U. S. Virgin Islands
Czech Republic	Japan	Portugal	Vanuatu
Denmark	Jersey	Samoa	

**b) Invitees**

Andorra	Guatemala	Monaco
Argentina	Hong Kong, China	Philippines
Austria	Liberia	Russian Federation
Barbados	Liechtenstein	Singapore
Belgium	Luxembourg	South Africa
Brunei	Macao, China	Switzerland
China	Malaysia (Labuan)	United Arab Emirates
Costa Rica	Marshall Islands	Uruguay