Tax Research

Finding the Secrecy World

Rethinking the language of 'offshore'

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Abstract

This paper shows four things. The first is that the existing language of the so-called 'offshore world' is inappropriate for the purposes of rigorous analysis of the issues to which that term has been applied. It offers a new language for this purpose, renaming the 'offshore world' the 'secrecy world' in the process.

Second, it suggests that the assumption that the secrecy world is geographically located is wrong. It is instead a space that has no specific location but is intended by the legislation that creates it to be either 'elsewhere', and so apart from the jurisdiction that permits the creation of the entities that trade within that space, or to be wholly or almost entirely unregulated with the knowing consent of all parties involved, and so effectively 'nowhere' for regulatory purposes.

Thirdly, this paper shows that the illicit financial flows that are the cause of concern with the secrecy world do not flow through locations as such, but do instead flow through the secrecy space that secrecy jurisdictions create. To locate them in a place is not only impossible in many cases, it is also futile: they are not intended to be and cannot be located in that way. They float over and around the locations which are used to facilitate their existence as if in an unregulated ether. This suggests that any attempt to measure or regulate them on a national basis will always be problematic, or just impossible, a task made all the more difficult because regulation within these spaces is also heavily influenced by the professional bodies and agencies of many of the persons providing services within the secrecy space; a fact that allows them to increase the opacity of that space.

Finally, this paper suggests that the change in language that it promotes is consistent with existing understanding of the observed phenomena whilst adding new dimensions to the lexicon that will

permit regulators to extend the scope of their work whilst reducing the opportunity for sophistic avoidance of obligation by the secrecy jurisdictions and the secrecy providers who work within them to create the secrecy spaces that in combination make up the secrecy world.

Introduction – the language of offshore

"There is no single, clear, objective test which permits the identification of a country as a tax haven" (1981, 21). So said the Gordon report to the American Treasury in 1981.

Mark Hampton said in his book 'The Offshore Interface' "It is difficult to draw a clear analytical distinction between a tax haven and an OFC" (1996, 15).

Twenty five years after Gordon, Jason Sharman reached very similar conclusions: "The term "tax haven" lacks a clear definition, and its application is often controversial and contested" (2006, 21).

The UK's Financial Services Authority said in 2008 that "There is no internationally agreed definition of what constitutes an offshore financial centre (OFC), but there are common perceptions. Generally, there is a tendency to adopt the approach of "you know one when you see one"." (Treasury Committee, 2008a, 3)

"If one had to choose a single criterion, we might define an offshore centre as one that is part of a jurisdiction that has few or no Double Tax Agreements ('DTA') with other countries. … However, this is an oversimplification." (Deloittes in Treasury Committee, 2008a, 379)

"It has proven difficult to define an OFC using a widely-accepted description. A range of criteria have been used, including (i) orientation of business primarily toward nonresidents; (ii) favorable regulatory environment; (iii) low or zero tax rate; and (iv) offshore banking as an entrepôt business." (IMF, 2008, 17)

Chief Minister Lyndon Trott of Guernsey, referring to the IMF's decision to change its OFC regulation programme in July 2008 said "On a scale of one to 10, this is a 10. The IMF is probably the most respected financial agency in the world. The key message is that the

IMF has acknowledged that it is wrong to distinguish between jurisdictions because they are either onshore or offshore. The distinction should always be that some are well regulated and others are not so well regulated." (Guernsey Evening Press, 2008)

"The Isle of Man has been urged to rebrand itself as an 'independent financial centre' rather than an offshore centre, as tax havens look to clean up their act. William F. Baity, deputy director of US anti-money laundering agency FinCen, the Financial Crimes Enforcement Network, suggested the territory move away from the label 'offshore', which has negative connotations, to 'independent financial centre'. 'Perception is reality and you will struggle as long as people talk about offshore,' Bailey said." (Accountancy Age, 2008)

In July 2008 Rt. Hon John McFall MP asked a panel of expert accountants appearing before the UK parliament's Treasury Select Committee what the difference between a tax haven and an offshore financial centre might be and was told "A tax haven only distinguishes itself from an offshore financial centre if it encourages tax evasion. That would be a rough definition - which none of them would accept." (Treasury Select Committee, 2008b)

This most cursory review of the language of the offshore world makes three things clear. The first is that no one agrees what the language of the offshore world is or means. The second is that despite that disagreement the use of that language is incredibly important to those who do operate in the offshore world. The third is that this is a debate which those involved in it think has serious implication for the future of offshore regulation. This paper builds on all three perceptions.

Why the language is important

There are four main concerns about the offshore world. The majority of offshore regulators address only two of them. The two that are most commonly addressed are money laundering and the financing of terrorism. These are the primary concerns of the IMF and the Financial Action Task Force, for example.

The third area of concern relates to financial stability, but until the recent credit crunch this attracted very little attention, with the Financial Stability Forum being seen as a relatively minor player in offshore regulation.

The fourth area of concern is tax evasion. However, with almost all international regulatory authorities apart from the OECD and the European Union paying little or no attention to this issue it has had remarkably little attention paid to it. This has meant that despite the importance of the issue it has remained primarily a matter of domestic concern for the countries who believe they are losing revenue as a result of it, and they are have enjoyed remarkably little scope for action when working in isolation.

The language of the offshore world has been confused by the divided attention given to it by regulatory agencies. As Chavagneux, Murphy and Palan (forthcoming) have shown, the language that each of these agencies uses depends largely upon their own primary purpose and the political necessity of securing support for that goal. So those agencies focused upon anti-money laundering activity will not talk about tax havens. They will, in addition, ignore all issues relating to financial stability but will instead seek to flatter and cajole those locations they wish to regulate into compliance with their inspection regimes. The latest move by the IMF to drop the terms offshore and onshore when considering the quality of financial regulation with regards to most issues is a clear example of this. It is, however, counter-productive. As the reaction of Guernsey to this announcement, noted above shows, tax havens will exploit such announcements for their own political advantage and seek to secure benefit from the apparent endorsement they represent.

The result is harmful at almost every level. The widespread confusion as to what the term offshore means is deepened. No one seems to know what a tax haven is as a consequence. And, as is clear, there is little agreement on what an offshore financial centre (OFC) is, but many to whom the label is applied would rather describe themselves as international or independent financial centres (IFC) even though there appears no greater understanding of what such a centre might be.

This is important. Since the Gordon Report first drew attention to the problems that tax havens cause awareness of the issue has increased enormously, the offshore market has grown substantially but, as many argue, almost all attempts to regulate the activity have failed. This paper argues that the imprecision of the language used has been a significant contributor to that failure.

The purpose of this paper

This current confusion in the language of offshore is unsurprising. Some of the available language puts an emphasis upon tax, which can be misleading. Tax is not the sole concern of the offshore world. The language also implies a specific geographical form in which this issue is framed, and maybe an island location. This is frequently wrong. The use of the word 'centre' implies the existence of a location in which an activity takes place, but that may not be true.

When available language fails to assist proper communication, and worse, when it obscures thinking and the policy initiatives that might result from that thinking, then it needs to be reformed. The purpose of this paper is threefold. First it explores the way in which the offshore world works. Second, it suggests a new language to describe the 'offshore world'. Third it explores the policy implications that result from that revised language.

The offshore world

Any new language for use in analysing the 'offshore world' (whatever that might be) has to be based upon an understanding of what actually happens there.

At the core of the 'offshore world' are jurisdictions. They are not necessarily countries or states, although some might be. For example, Malta and Cyprus are both states in their own right but not all are. Some are dependencies, as is the Isle of Man, whilst some are effectively protectorates, as are Cayman and the British Virgin Islands. Others are sub-national states, such as Delaware in the USA. The status of others is even more esoteric; the principalities of Lichtenstein and Monaco coming immediately to mind. The difference in status does not matter; what characterises these places is their ability to create law that can have impact outside their own territories. This may require the tacit or implied consent of other parties; for example that of the Federal State of which they are a part, or their Protector state, or even of the political alliance of which they are a member (the EU in the case of Cyprus and Malta), but the issue remains the same; it is those jurisdictions that choose to create legislation or regulation with the intent that it has use and impact beyond their geographical

domain that are of concern here. That is why any description of these locations has to include the word 'jurisdiction'.

Being a jurisdiction does not, however, categorise a location as being a part of the 'offshore' world. The majority of the world's jurisdictions play no part in this activity. There have, therefore, to be identifiable characteristics that differentiate those that are in the 'offshore world' from those that are not. This paper suggests that there are two such characteristics.

The first such characteristic is that the secrecy jurisdiction creates regulation that they know is primarily of benefit and use to those not resident in their geographical domain.

The second characteristic is the creation of a deliberate, and legally backed, veil of secrecy that ensures that those from outside the jurisdiction making use of its regulation cannot be identified to be doing so.

It is, I suggest, pursuit of these two characteristics that in combination define the secrecy jurisdiction.

It is important to note two things. The first is that tax is not mentioned in reaching this definition, and nor does it need to be. There is no doubt that low taxation is one of the attractions that secrecy jurisdiction's offer, and that if they did not do so then, all other things being equal, laxity in other regulation would lose much of its appeal to potential users, but in that sense low taxation is simply a marketing mechanism for secrecy jurisdictions. It is one of the numerous regulations they provide that are open to abuse by those resident elsewhere, all of them backed by secrecy, and as such to highlight it, as has been commonplace by use of the term tax haven is a mistake. That term may have popular appeal, but it has little practical application.

The second important point is that both of the identified characteristics must exist. As a matter of fact the creation of regulation for the benefit of people living elsewhere will almost always be a fruitless exercise if the person using it cannot avoid their obligations in the place in which they really reside as a consequence. Secrecy is the only guarantee that they can do that.

There is also the important point to note that at a practical level no one would wish to use the regulation created by a secrecy jurisdiction, or take that risk that they might be found to be doing so if that regulation were more onerous than that in the place in which they normally reside. As such it is inevitable that the regulation created by secrecy jurisdictions for the benefit of those resident elsewhere will be less onerous than that found in the economies from which they seek custom and that this regulation will, inevitably, as a result undermine the effectiveness of regulation in those places. A race to the regulatory bottom is inherent in the business model of these places. This is again, however, not a defining characteristic of a secrecy jurisdiction but is instead the practical marketing necessity if it is to raise revenue from the regulation that it creates. The inevitable consequence is, however, pernicious. This why so many of the major nations and regulatory agencies of the world want to eliminate the abuse that secrecy jurisdictions promote.

The range of regulations that might be created by secrecy jurisdictions for use by those not normally resident in their domain is wide. Such regulations might include:

1. Corporate laws, including those on incorporation, company residence, the types of share in issue, the use of nominees, the filing of accounts and other information on public record and the maintenance of records themselves;
2. Trust law, including those on the registration and taxation of trusts, the use of nominees, the right of settlors to declare trusts for their own benefit, the filing of information and accounts with regulatory authorities and the need to maintain records;
3. Taxation law of all sorts;
4. Banking laws, including the right to maintain bank secrecy for taxation, civil law and criminal law purposes;
5. Regulation with regard to competition law, labour issues, shipping, environmental matters, health and safety and other issue which might either through their absence, level of obligation or compliance obligations produce a lesser burden than those commonplace in other jurisdictions;
6. Information exchange agreements relating to civil, criminal and taxation law issues;

7. Legal cooperation regulation, including the willingness of the jurisdiction to enforce obligations arising in other jurisdictions through its legal system;
8. Human rights laws and related issues, such as obligations with regard to corruption;
9. Accounting and other information disclosure requirements of a non-statutory nature.

In combination these regulations cover a large range of business activity and it is this, when combined with secrecy that provides enormous scope for abuse.

It is stressed though that secrecy by itself is not a problem. In a world made up of one state the right to secrecy would not be an issue if the state chose not to know about the activity of its citizens. Secrecy is a problem when the regulation of one state is used to deny information to another state which believes it has the legal right to know it.

It should also be noted that the undertaking of transactions outside a location is not a problem: the trade of the world is dependent upon such events occurring. It is hiding the fact that a transaction has taken place in one location by use of regulation and secrecy created in another location so that the full regulatory consequences of the transaction do not arise in the place where it was really located that gives rise to a problem. In that case the avoidance of obligation has occurred.

It is the combination of lax regulation and secrecy that hides its use that defines the problem created by secrecy jurisdictions and yet it is precisely this problem that all regulators have so far failed to address.

Offshore and the secrecy jurisdiction

Defining the secrecy jurisdiction and the problem it creates is one thing. Linking the secrecy jurisdiction to the concept of offshore necessitates a further step in understanding. That step requires appreciation of the fact that wherever 'offshore' is it is not in the secrecy jurisdiction.

The secrecy jurisdiction is a place. That means it is physically identifiable and it is, in consequence, constrained by geographic borders that limit its apparent domain. However, as the definition

used here makes clear, a secrecy jurisdiction seeks to extend its sphere of influence beyond its borders. Those places beyond its borders is where offshore is.

This has real implication within the secrecy jurisdiction. It is highly unlikely that there will be any secrecy at all within the secrecy jurisdiction. Most secrecy jurisdictions have very low tolerance for domestic non-compliance with their own regulation. After all, they have a society to run and tax to collect, and doing so in an efficient, organised and even transparent manner may well be vital to the political survival of those who run the secrecy jurisdiction. So, and for example, local companies will usually be required to report their income to domestic tax authorities, as will individuals and trusts, whilst safety and environmental laws will hopefully be in force and labour regulations may apply. This is, in fact a definition of what should be called 'onshore' because in an onshore environment the location in which the transaction takes place and the location in which it is regulated coincide. In addition there is (or at least there is expected to be) full transparency with regard to all the onshore the transactions involved.

In that case we are faced with a dichotomy: the secrecy jurisdiction is both onshore and offshore simultaneously. To understand offshore it does therefore have to be understood that the secrecy jurisdictions that create and support offshore activity are not the place where one should look to find it. This is, of course, the logical consequence of the definition of a secrecy jurisdiction used in this paper. The regulation that it creates for the benefit of those not resident within it, and the veil of secrecy that it draws over their doing so disguises the fact that except in minor part the activities so enabled do not have anything to do with the secrecy jurisdiction itself. The impact of those transactions is not within the secrecy jurisdiction itself, because if they were they would be onshore, which for these purposes we might call 'here'; they are instead offshore, which for these purposes we might more usefully call 'elsewhere'.

It is as if there is a divide between these two places that the secrecy jurisdiction enables. There is a regulated, onshore, domestic space and then that other offshore space that is 'elsewhere' that is deemed to be somewhere quite distinctly different from the onshore economy of the secrecy jurisdiction. It is commonplace for the regulation of those places to make clear that there is a clear, although physically

entirely unidentifiable and non-locatable, line between the two areas in which its regulation has impact. In the current jargon of the offshore world that line is a 'ring fence'. Onshore is one side of that fence, and can be located within the physical domain of the jurisdiction. Offshore is those places elsewhere where its regulation has impact, but as I note below, this does not necessarily mean that the resulting transactions can be physically located.

Secrecy spaces

This gives rise to the next development in the language of this phenomenon. The term 'offshore' is problematic as the introductory quotes show. It gives rise to substantial confusion: indeed I have witnessed small island administrators from locations that are without doubt secrecy jurisdictions laugh at the idea that Switzerland might be 'offshore'. Liechtenstein, as one of only two double land locked states in the world certainly pushes these people's idea of offshore to the limit. In that case, and given the change in approach that the IMF is adopting, just as it seems timely to displace the term 'tax haven' with the term 'secrecy jurisdiction' so it seems appropriate to replace the term 'offshore' with the term 'secrecy space'.

The secrecy space is created by a secrecy jurisdiction, or a combination of them. It is not, however, in those jurisdictions, at least for legal purposes. As such in many, if not most cases, the secrecy jurisdiction will argue it has no duty to regulate the transaction undertaken using the mechanisms it supplies from within the secrecy space, its logic being that these transactions are undertaken 'elsewhere'. This has most notably been seen in the recent report of the United States Government Accountability Office on the Cayman Islands (2008, 1) in which it was stated that:

> *Cayman officials said they fully cooperate with the United States. Maples [and Calder] partners said that ultimate responsibility for compliance with U.S. tax laws lies with U.S. taxpayers.*

Maples and Calder is the largest firm of lawyers in Cayman. As the same report also noted:

> *While U.S. officials said the Cayman government has been responsive to information requests, U.S. authorities must provide*

specific information on an investigation before the Cayman government can respond.

The Cayman secrecy jurisdiction does, of course, make it as hard as possible for the US authorities to secure the specific information required before cooperation can take place. In addition, Maples and Calder make it quite clear that their concern extends solely to the Cayman, or onshore, aspects of what are, by definition, offshore transactions undertaken by the more than 18,000 companies registered in their offices, almost all of which work within the secrecy space that Cayman has created for them but which it considers to be 'elsewhere' for regulatory purposes.

It is also worth noting that this concept of 'elsewhere' is not restricted to taxation. Indeed, commentators such as Ronen Palan think the 'offshore' world began in October 1957 when the Bank of England ruled that bank transactions undertaken in London in transactions other than sterling between parties not resident in the UK might be recorded by London banks as having occurred for accounting purposes within the UK but they were not otherwise to be considered subject to UK banking and foreign exchange regulation. They were deemed to have occurred 'elsewhere' for these purposes even though it was obvious they took place in London. (Palan, 2003)

The same phenomenon is also to be found in a UK company law case. In 1928 it was decided in the case of The Egyptian Delta Land and Investment Co. Ltd. v. Todd in the UK House of Lords (ATO) that a company was resident where its central management and control was, which was deemed to be determined by the place where the directors met. This meant a company incorporated in the UK could be resident and regulated somewhere else. The decision was profoundly important: it endorsed the legal concept that an entity might be located in more than one place. Put simply, the company might be incorporated in the UK and be subject to its company law but if not resident there its taxation affairs were regulated 'somewhere' else.

Somewhere, not elsewhere

A further distinction is necessary at this point. Those who sought to prove that The Egyptian Delta Land and Investment Co. Ltd., noted above, was 'elsewhere' so that it did not have to suffer UK tax could

only do so because they could demonstrate that the company was not only not in the UK, but was actually somewhere else.

This concept of 'somewhere' is important. It provides a clear indicator for assessment of conduct. If a company created in a secrecy jurisdiction operates outside its regulated area but it is known despite that to be operating somewhere else that is properly regulated, and it is known to be making full disclosure of its activity in that other location then the overall risk of regulatory abuse is limited. The regulatory environment might be weakened by being located across more than one domain but regulation is none the less intact. This can be shown diagrammatically:

	'Here'	'Somewhere'
Country providing the transaction structure	Jurisdiction A	Jurisdiction A
Country providing regulation of the transaction	Jurisdiction A	Jurisdiction B
Transaction type	Onshore	Regulated somewhere else

It is stressed: this diagram describes regulated transactions. What is happening here is entirely legal. Jurisdictions A and B might, for example, fully cooperate to ensure that the transaction is properly accounted for. But, as a matter of fact, for Jurisdiction A to consider that the transaction is 'somewhere' it must know the identity of Jurisdiction B and that that location in question has assumed responsibility for the transaction. If it does not then the claim that the transaction is regulated somewhere else is wrong.

Elsewhere

Now the concept of 'elsewhere' as created by the secrecy jurisdiction has to be added into this diagram.

	'Here'	'Somewhere'	'Elsewhere'
Country providing the transaction structure	Jurisdiction A	Jurisdiction A	Jurisdiction A
Country providing regulation of the transaction	Jurisdiction A	Jurisdiction B	Unknown
Transaction type	Onshore	Regulated somewhere else	In the secrecy space

The secrecy space has now been created and the transaction that takes place within that space is now categorized. This concept of 'elsewhere' is critical: without understanding it the ideas and motivations of those working in the secrecy space cannot be appreciated. The importance of 'elsewhere' is that it is unknown. That though does not mean it is nowhere, that is something else altogether.

Nowhere

To be 'nowhere' is the ultimate goal of those who use secrecy jurisdictions. If added to the diagram it looks like this:

	'Here'	'Somewhere'	'Elsewhere'	'Nowhere'
Country providing the transaction structure	Jurisdiction A	Jurisdiction A	Jurisdiction A	Jurisdiction A
Country providing regulation of the transaction	Jurisdiction A	Jurisdiction B	Unknown	Nowhere
Transaction type	Onshore	Regulated somewhere else	In the secrecy space	Unregulated
Space name	The regulated space		The secrecy space	

'Nowhere' in this case means that the jurisdiction which supplies the regulatory structure for the transaction cannot be identified because there is none responsible for doing so.

In the diagram it is Jurisdiction A that should have obligation to identify where the transaction undertaken by an entity created under its law is regulated. It is commonplace that it does not do so though because secrecy jurisdictions do not usually make enquiry of the use made of entities created under their law when they operate outside their domain. There is good reason for this action on their part: first, they do not ask because they know that enquiry in such cases causes offence and that is bad for their business. Secondly they know that it is frequently the case that no jurisdiction can be identified in which the transaction is located for regulatory purposes, even if enquiry is made[1]. That is because it is not reported anywhere even if there might be obligation to do so. If that obligation to report does exist, but is ignored then the transaction is elsewhere and it is clear that a law has been broken. If that obligation to report does not exist then the transaction is nowhere.

Being nowhere does not happen by chance. It happens through the interaction of 'secrecy paces' provided by 'secrecy jurisdictions'. An example might be where a person resident but not domiciled in the UK creates a trust in a secrecy jurisdiction such as the British Virgin Islands that in turn owns a company incorporated in Jersey that has a bank account in the Isle of Man and nominee directors in Cayman. The income of that company and trust are retained within the company. This sort of structure is costly, but that is a price of being 'nowhere'.

This structure might achieve the aim of being unregulated almost everywhere. This is possible because the individual creating this trust is allowed to do so without breaching UK law subject to meeting the non-domicile requirements of that country. If they can do so then they are not taxable in the UK on their income arising outside the UK even though they are resident in the UK. Nor do they have to make any declaration of that income or their involvement with the trust in question to the UK authorities, a right reconfirmed in 2008[2]. If they are not resident anywhere else then this means the regulation of this

[1] Examples of this phenomenon are to be found in the report of the US Senate Permanent Subcommittee on Investigations Hearing: Tax Haven Abuses: The Enablers, The Tools & Secrecy, 2006.

[2] For an explanation see http://www.withersworldwide.com/news-publications/274/stop-press-budget-2008-residence-domicile-offshore-trusts.aspx accessed 30-7-08

trust does, with regard to the settlor, happen nowhere, as defined here.

Trusts in most secrecy jurisdictions do not have to be registered with any authority. The trustees do not have to file tax returns if the settlor and beneficiaries are located outside that jurisdiction. There is no requirement to prove they are elsewhere. This is true of the BVI.

As noted above, the same is possible with Jersey companies, and will continue to be so when its law on company taxation changes in 2008.

If a bank account is in a different jurisdiction from the company that owns it who regulates it? Maybe the bank in the jurisdiction of location is responsible for money laundering, but there is certainly no tax oversight in that jurisdiction because the bank providing the account will know that at least notionally no tax liability will arise upon company in its place at incorporation. Since in this case that bank is located in a secrecy jurisdiction you can be sure it will not ask where the economic substance of the transactions undertaken by the company are located and as such it will accept no obligation to review compliance of the company with taxation obligations in the place in which it really trades, behaviour indicated to be normal in the Cayman Islands by Maples and Calder, as noted above.

Having the directors in a location with no tax achieves the same result. Even if the rule established in the UK in 1928 noted above is followed and the company is taxable where its directors meet, there is no corporation tax in Cayman so in this case no regulation need apply.

As a result this combination creates a structure that is nowhere for tax purposes, and almost entirely so for all other purposes and yet apparently quite legitimately so.

More than that though, none of these involved, be they the UK non-domiciled settlor of the trust, the trust or trustees, the company or its directors, would need to file a tax return in that capacity anywhere by reason of this careful choice of structure. This is the ultimate aim of the offshore operator. This structure is nowhere. Achievement of this might not be possible in the physical world, but it is in this strange regulatory and secret space.

Transparency

There is one final twist in the diagram. Regulation is one issue, but what is required as a result of much regulation is transparency. Another line is needed to explain this. This is indicated as follows:

	'Here'	'Somewhere'	'Elsewhere'	'Nowhere'
Country providing the transaction structure	Jurisdiction A	Jurisdiction A	Jurisdiction A	Jurisdiction A
Country providing regulation of the transaction	Jurisdiction A	Jurisdiction B	Unknown	Nowhere
Transaction type	Onshore	Regulated somewhere else	In the secrecy space	Unregulated
Space name	The regulated space		The secrecy space	
Transparency status	Transparent	Visible	Opaque	Impervious

It is clear that there is a gradation in transparency as structures move from here, to somewhere and on through elsewhere to nowhere. It might cost more to be 'nowhere' but for the person seeking secrecy the result is an impervious structure that suits their purpose but thwarts regulators the world over.

The secrecy providers

There is then a further matter to be addressed. Quite clearly structures of the sort described in the preceding paragraph do not come into place by chance. They are created by people seeking to exploit the secrecy spaces provided by the secrecy jurisdictions. These people may be (and often are) located in a secrecy jurisdiction. They might even seek to establish their own operations in a secrecy space. But they are not part of the structure of any one secrecy jurisdiction, nor are they part of the secrecy space, which they exploit but do not create.

These people are the secrecy providers. They are the lawyers, accountants, bankers, trust companies and others who provide the services needed to manage transactions in the secrecy space. These organisations, working together, might be called Offshore Financial Centres (OFC) except for the fact (as the opening quotations demonstrate) that the use and definition of that term has been problematic, and as such it has been discredited for all practical purposes. Despite that there is a continuing need for a collective term for those organisations that commercially exploit the opportunities created by the legislation promulgated by the secrecy jurisdictions. The term 'secrecy provider' is used here to describe those organisations.

Many of the organisations that are secrecy providers will also, of course, provide services within the regulated space. That does not negate the use of the term secrecy provider. Just as every secrecy jurisdiction will have a regulated space that is 'onshore' which does not prevent it also supplying structures deliberately designed for use in the secrecy space, so can a secrecy provider service both the regulated (onshore) and secrecy (offshore, unregulated) market places.

Consigning offshore to history

These last terms also suggest that the terms offshore and onshore should, like tax havens and OFCs be consigned to history. The onshore market is either regulated, whether that be locally ('here') or internationally ('somewhere'). What has been considered the 'offshore' market is more accurately, and simply defined as the unregulated market, whether that be either secretly unregulated ('elsewhere') or knowingly unregulated ('nowhere'), all of which terms have considerably greater value in use than those they replace.

If these terms, and the identities of the firms providing services to these markets, are built into the diagram we now have the following final form of the diagram developed in this section:

	'Here'	'Somewhere'	'Elsewhere'	'Nowhere'
Country providing the transaction structure	Jurisdiction A	Jurisdiction A	Jurisdiction A	Jurisdiction A
Country providing regulation of the transaction	Jurisdiction A	Jurisdiction B	Unknown	Nowhere
Transaction type	Locally Regulated	Internation-ally Regulated	Secretly Unregulated	Knowingly Unregulated
Space name	The regulated space		The secrecy space	
Market type	Regulated market		Unregulated market	
Transparency status	Transparent	Visible	Opaque	Impervious
Financial services providers	Local provider	International provider	Secrecy providers	

Using this language to create the secrecy world

It is stressed that when using these definitions there is no overlap between the terms secrecy jurisdiction, secrecy space and secrecy provider. They relate to different parts of the unregulated market. To see how this works a diagram of the intricate structure described above is needed, with the additional assumption added that the funds are ultimately invested in the UK and the advice upon it has come from Guernsey:

Investments located in						UK
Secrecy provider						Guernsey
Unregulated entity	Settlor	Trust	Company	Directors	Bank	
Secrecy jurisdiction	UK	BVI	Jersey	Cayman	Isle of Man	

What is stressed is that the important locations within this diagram are not the white spaces. That white space is the identifiable geographic location in which certain structures, people and commercial organisations can be located. It is even possible to locate the secrecy provider and the investment target for the whole structure within the white space, but the important part of the diagram is not the white space. The real issue about this structure is the grey area. That grey space is the secrecy space.

It is in the grey secrecy space that the entities located (and in this case almost entirely unregulated) in specific geographical locations operate. They do, of course, appear within the diagram to be located in the white space. This is the manner in which the secrecy jurisdictions would wish them to be viewed: as they rightly claim, to the very limited extent that they do actually have relationship with that white space that represents the secrecy jurisdiction they are regulated. But the impact of the entities is deliberately elsewhere, and this is the key concept that the grey space represents. The activity in that grey space is knowingly unregulated by the secrecy jurisdiction, a fact that current language enables them to ignore, and it is this vital distinction that this paper seeks to create, because it is in that grey space that the damage caused by secrecy jurisdictions occurs.

The secrecy space surrounds, but is not in any of the secrecy jurisdictions. The secrecy provider might work from within a secrecy jurisdiction (very often, indeed, they might sell services to unregulated entities working within that same jurisdiction) but they too, by selling services into the secrecy space can also work (at least in part) outside the regulated place in which their activity resides, and it is common

for secrecy jurisdictions to ensure that regulation exists to make sure that this can be achieved.

So it is in the grey secrecy space that the unregulated market exists, established by secrecy providers using unregulated entities registered in secrecy jurisdictions to move transactions from the regulated local or international sectors that are 'here' or 'somewhere' else that is identifiable into the secretly or knowingly unregulated spaces that are mythical locations 'elsewhere' or, maybe 'nowhere' at all.

It is this combination that some call the offshore world. But that is another misnomer. This is the secrecy world, the final term to be added to the list that already includes secrecy jurisdictions, secrecy spaces and secrecy providers.

Illicit financial flows

So what, one might ask? Why be concerned about this secrecy world? The answer is straightforward. It is in the secrecy world that illicit financial flows occur. The grey lines in the diagram are the conduits through which money passes for which people do not wish to be held to account. Those funds might be the proceeds of crime, payments associated with bribery and corruption, capital seeking flight from the territory in which it belongs and from which it has not secured legal departure, or they might be profits seeking to be located in a place other than that in which they really arose so that taxation liabilities might go unpaid in the place where they are rightfully due. These are the illicit fund flows of the world. Raymond Baker has estimated that these flows amount to between US$1 trillion and US$1.6 trillion a year, of which 60-65 per cent relate to commercial tax abuse (Baker, 2007).

The flow of these funds would be seriously impeded if the secrecy space did not exist. It is that fact that makes tackling the secrecy world an issue of such importance.

Facilitating opacity

The secrecy space is created by jurisdictions that promote legislation that facilitate transactions that they know will actually take place elsewhere, outside their regulatory domain, and about which they will make no enquiry. The ability to create regulation is not, however, the

sole preserve of legislatures. Others have that opportunity and exercise it. In particular the accountancy profession has through the International Accounting Standards Board (IASB) acquired power to create regulation that has the force of law in approximately 100 countries in the world, with more steadily coming within its sphere of influence. That regulation covers the form and content of accounting disclosure for many of the multinational companies of the world, including all in the European Union, and the United States now permits the use of this disclosure regime.

It so happens that the organisations sponsoring the IASB have substantial overlap with many of the better known secrecy providers selling services into the secrecy space. Perhaps it is unsurprising as a result that their regulations do appear to facilitate opacity within that space. The rules of international accounting include features that are extraordinarily beneficial to those companies that wish to use the secrecy space to reallocate the reported geographic location of earnings arising within multinational corporations. This is because all intra-group transactions are eliminated from view in the published consolidated accounts of multinational groups of companies. Many of the companies working in the secrecy space will be of this type. In addition those rules of disclosure do no require that the name or even the existence, let alone trading information of subsidiaries that parent companies do not consider significant to the user of their accounts be disclosed, and since intra-group trades are not considered of any interest for this purpose (since they are eliminated from view on consolidation) all entities used within the secrecy space for the purpose of profit reallocation do automatically fall out of view as a result.

In combination this command of accountancy regulation by secrecy providers adds considerably to the opaqueness of the secrecy space.

Reconciling this view of the secrecy world with other opinion

This paper has suggested a new language for describing what has been previously been called the offshore world. There appear to be two criteria for determining the usefulness of this language. The first is that it fits with existing understanding of the nature of the phenomenon being observed. The second is that it has value in use.

Dealing with the first of these issues, it is obvious from the quotations at the start of this paper that there is substantial difference of opinion concerning the meaning of many of the terms relating to offshore already in use. So, and for example, the precise nature of a tax haven has been disputed, although mainly by the places to which the term has been applied. However, there is a general consensus that they are geographically identifiable locations that seek to attract business to their domain by offering light regulatory regimes, usually including low levels of taxation. This is a perception that easily fits with that of the secrecy jurisdiction as defined here.

The use of that secrecy jurisdiction as the provider of unregulated services within the secrecy space fits well with many of the definitions of offshore, and in particular that advanced by a Ronen Palan (2003) who identifies offshore as being the banking Euromarket, which exists entirely within the secrecy space and is very largely unregulated, sometimes quite deliberately knowingly so.

The definition of an OFC use by Zoromé for the IMF (2007) also fits well with that used here for a secrecy jurisdiction. He defines an OFC as:

> *a country or jurisdiction that provides financial services to nonresidents on a scale that is incommensurate with the size and the financing of its domestic economy.*

The overlap is obvious.

For some the term secrecy jurisdiction is already synonymous with that of tax haven. For example, Senator Carl Levin has used the terms interchangeably when promoting the Stop Tax Haven abuse Act in the USA, and at the same time talks of the secrecy that these places sell as being their major product[3].

The term secrecy jurisdiction has another powerful advantage for those, such as Sol Picciotto who have problem with the term tax haven, simply because this is too restrictive in that the regulation they produce for those not resident in their domain is of much wider range than that relating to taxation.

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3 Statement of Senator Carl Levin on Introducing the Stop Tax Haven Act, Part I http://levin.senate.gov/newsroom/release.cfm?id=269514 accessed 30-7-08

What then of the other terms? 'Secrecy world' is a direct replacement for 'offshore world' but removes the geographic ambiguity inherent within the latter. It has the advantage of describing the essential attribute that characterises the domain.

In the same way the term 'secrecy space' replaces 'offshore', which has been problematic in use and has the same advantage that the term secrecy world has in that it describes more accurately the phenomena it defines which is not geographically located but which is precisely identifiable by its opacity.

Finally, the term secrecy provider will, without doubt, be unpopular with those firms of lawyers, accountants and banks who operate from within the secrecy jurisdictions to provide services within the secrecy space, but that is not the concern of this paper. Those firms knowingly use the secrecy that their host jurisdictions provide to disguise the activities of their clients, and there is clear evidence that they do not seek to regulate the activity of those clients beyond the jurisdiction in which they are located. As such the description of those firms as secrecy providers within unregulated market appears accurate and removes the ambiguity within the term offshore financial centre which has caused considerable confusion, and some degree of inactivity with regard to regulation to date.

In this sense it is suggested that the terminology proposed by this paper is both consistent with existing understanding and eases comprehension of that understanding by the lay user of these terms.

That, however, is dependent upon their effectiveness in assisting the process of regulation which has motivated research in this area. There is insufficient space here to explore all the possibilities that this new language offers, so a couple must suffice.

The first example relates to confusion with regard to regulation. The following claim is typical of those made by those working within secrecy jurisdictions:

> *Jersey is well known ... as a Crown Dependency with a well regulated Finance Industry on which the local economy is dependent for its economic wellbeing.*[4]

In as far as it goes this is true. Jersey regulates as much as is currently required by international regulators but that regulatory requirement does not at present extend to the secrecy space which its laws create. So, Jersey may be well regulated, but for all practical purposes a company registered within its domain does not have to disclose any information that might be of use to an enquirer, nominees being allowed to perform all functions required to be disclosed on public record. A Jersey company that does not trade within the island does not have to submit either accounts or tax returns to any Jersey authority. Trusts created within its domain do not have to be registered with any authority and do not have to submit either accounts or tax returns to the Jersey authorities. Whilst the local banks do, according to the regulations of the Jersey Financial Services Commission have to report suspicion of tax evasion undertaken outside the island there were no such suspicious activity reports submitted to the Jersey police in 2006[5] and when in 2007 the UK offered a tax amnesty to the customers of just five UK banks that maintained branches in that island tens of thousands of customers voluntarily declared sums upon which evasion had taken place but about which, apparently, no local bank had considered there to be any cause for concern (Times, 2007).

All this is clear evidence that the claim that Jersey makes to be well regulated is true, but only to the extent that regulation relates to activity undertaken within its geographic domain. When the whole basis of its financial services industry is to provide services to people outside its domain, many of whom rely on the secrecy it provides to hide that fact from their jurisdiction of residence, then this concept of regulation can be seen to be of decidedly limited extent and value.

The definitions proposed in this paper would allow this to be highlighted because the difference between the regulated and secrecy spaces is identified by the language used. No existing language does that and in consequence secrecy jurisdictions have, as Senator Walker

[4] Paragraph 1 of a statement submitted by Senator Frank Walker, Chief Minister of Jersey in Treasury Committee 2008a, 393

[5] See http://www.taxresearch.org.uk/Blog/2007/03/02/jersey-officially-a-money-laundering-free-zone/ accessed 30-7-08 based on The Jersey Police Report, 2006

does above, claimed to be well regulated whilst knowing that the vast majority of the transactions they facilitate remain entirely beyond the scope of their regulatory regime. As a consequence the claims of the secrecy jurisdictions would be exposed as having limited value, as almost all regulators know to be the case.

Secondly, there is the issue of the problem with the 'onshore / offshore' distinction. As another submission to the UK Treasury Select Committee hearing on OFCs says:

> *Generally, the view is taken that the Treasury Committee's inquiry into offshore finance centres must not be seen as centering on the longstanding debate between onshore and offshore jurisdictions. Rather, it should be focused on the pertinent issue of the standard of regulation and supervision of financial centres, whether onshore or offshore, and a demonstrated willingness to cooperate on matters of exchange and sharing of information.*[6]

By eliminating the terms onshore and offshore from discussion and substituting in their place the terms the regulated space and secrecy space, which is exactly what the new language does, this dispute could be consigned to history, and yet at the same time the deficit in regulation that the secrecy jurisdictions create could be highlighted.

As these two examples show, this new language has value in use, not just in more accurately describing the observed phenomena, but also in providing those wishing to regulate those phenomena with a lexicon that empowers their action. The different standards of regulation that secrecy jurisdictions apply to their regulated space and the secrecy spaces they enable will allow regulators to add the secrecy space to their focus of attention. At present they do not have the language to do that. This new lexicon quite literally empowers them to go to areas they have never been before, and that is what society needs them to do.

The language makes three further things clear. The first is that regulation must extend to the secrecy space, which will require radical transformation of its current opacity. The second is that regulation cannot work if it does not apply to the work of the secrecy providers in

[6] Memorandum from the British Virgin Islands Financial Services Commission (FSC) in Treasury Committee, 2008a, 541

and beyond the places in which they are located. The third is that regulatory reform is not just a local issue, reform of accounting and other international standards to expose the nature and use of the secrecy space is essential if it is to be both exposed to view and properly regulated as a result.

Conclusion

This paper shows four things. The first is that the existing language of the so-called 'offshore world' is inappropriate for the purposes of rigorous analysis of the issues to which that term has been applied. It offers a new language for this purpose, renaming the 'offshore world' the 'secrecy world' in the process.

Second, it suggests that the assumption that the secrecy world is geographically located is wrong. It is instead a space that has no specific location but is intended by the legislation that creates it to be either 'elsewhere', and so apart from the jurisdiction that permits the creation of the entities that trade within that space, or to be wholly or almost entirely unregulated with the knowing consent of all parties involved, and so effectively 'nowhere' for regulatory purposes.

Thirdly, this paper shows that the illicit financial flows that are the cause of concern with the secrecy world do not flow through locations as such, but do instead flow through the secrecy space that secrecy jurisdictions create. To locate them in a place is not only impossible in many cases, it is also futile: they are not intended to be and cannot be located in that way. They float over and around the locations which are used to facilitate their existence as if in an unregulated ether. This suggests that any attempt to measure or regulate them on a national basis will always be problematic, or just impossible, a task made all the more difficult because regulation within these spaces is also heavily influenced by the professional bodies and agencies of many of the persons providing services within the secrecy space; a fact that allows them to increase the opacity of that space.

Finally, this paper suggests that the change in language that it promotes is consistent with existing understanding of the observed phenomena whilst adding new dimensions to the lexicon that will permit regulators to extend the scope of their work whilst reducing the opportunity for sophistic avoidance of obligation by the secrecy jurisdictions and the secrecy providers who work within them to

create the secrecy spaces that in combination make up the secrecy world.

Glossary

Elsewhere	An unknown place in which it is assumed, but not proven, that a transaction undertaken by an entity registered in a secrecy jurisdiction is regulated.
Here	The geographical limit of a jurisdiction.
International financial centre (IFC)	A commercial centre for the supply of financial services for use in the regulated space that both provides and executes a full range of such supplies on behalf of clients located within the jurisdiction in which the service supplier is located and from other identified locations.
International provider	A financial services supplier making supply within the regulated market from an international financial centre to clients in more than one country, including that in which it is itself located.
Internationally regulated	A transaction regulated in more than one jurisdiction, with all jurisdictions being aware of the others involvement.
Knowingly unregulated	A transaction which is not regulated by any jurisdiction, or where the degree of regulation is so minimal that this is effectively the case, with this being known to all parties with any responsibility for the entity. This has the effect that the transaction takes place 'nowhere'.
Local provider	A financial services provider supplying services to entities resident in the jurisdiction in which they themselves operate.
Locally regulated	A transaction or entity that is solely regulated within the jurisdiction in which it is registered or takes place.
Nowhere	The part of the secrecy space where by design or chance the combination of unregulated entities used results in transactions being either legally unregulated, or being very lightly regulated.

Offshore financial centre (OFC)	See secrecy providers
Regulated entity	An entity that is located within the regulated space and is regulated both in its jurisdiction of registration and in all other jurisdictions in which it trades.
Regulated market	A market in which regulated entities trade with each other.
Regulated space	That area previously known as onshore in which all transactions are knowingly and openly regulated by one or more national agencies.
Secrecy jurisdiction	A jurisdiction that creates regulation that they know is primarily of benefit and use to those not resident in their geographical domain. And in which there is created a deliberate, and legally backed, veil of secrecy that ensures that those from outside the jurisdiction making use of its regulation cannot be identified to be doing so. Formerly known as a tax haven.
Secrecy provider	The lawyers, accountants, bankers, trust companies and others who provide the services needed to manage transactions in the secrecy space. These organisations, working together, congregate in a secrecy jurisdiction for the purpose of providing these services.
Secrecy space	The unregulated spaces that are created by a secrecy jurisdiction that are suggested to be outside their domain and so are treated by them as being 'elsewhere' or 'nowhere'. Both of these are domains without geographic existence.
Secretly unregulated	An unregulated transaction undertaken by an entity created using the law or regulation of a secrecy jurisdiction that is not reported to those authorities elsewhere that have legitimate interest in it despite there being an obligation for such report to be made.
Secrecy world	The collective term for the sum total of the operations facilitated by the secrecy jurisdictions, the secrecy space and the

	secrecy providers. What was once called 'the offshore world'. It is more than the unregulated market because that is total of the commercial consequence of operations within the secrecy space: the secrecy world encompasses the unregulated market and all those who create and promote secrecy jurisdictions and what they offer.
Somewhere	A place other than that in which a regulated entity resides in which it undertake transactions that are both reported and regulated, with transparent interaction between that place and the location in which the regulated entity is registered or resides taking place, at least on request.
Tax haven	A secrecy jurisdiction.
Unregulated entity	An entity created within a secrecy jurisdiction intended for use in the unregulated market that operates in the secrecy space. This entity will not be accountable for its transactions either because that has been engineered to be the case, in which case it is operating nowhere, or because there is deliberate omission to make that declaration in a place elsewhere to that in which it is legally located, which place elsewhere is unaware of the unregulated entity's obligation to make declaration because of the existence of the secrecy space.
Unregulated market	What was once called 'offshore'. It is the sum of the commercial operations created to exploit the secrecy spaces created by secrecy jurisdictions. Unregulated entities trade within the unregulated market, either with other unregulated entities or with regulated entities.

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Since 2000 Richard has increasingly been involved in taxation policy, both as an adviser and campaigner. He is director Tax Research LLP and advises the Tax Justice Network, the Publish What You Pay campaign, Christian Aid, the TUC in the UK and many other organisations on tax issues. He advises several prominent MPs on taxation issues. He has also advised the States of Jersey on reform of its taxations systems and has addressed meetings of the UN Committee of Experts on International Cooperation in Tax Matters and of the European Commission Directorate on taxation policy. His current research work on tax havens is largely funded by the Ford Foundation.

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