



Offshore financial centres and internal development in the Pacific islands

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This paper provides an overview of how hosting offshore financial centres affects the internal development of Pacific island countries. While offshore financial centres have been attractive development options for many regional élites, none has become fully functional and the returns have often disappointed the island politicians who sponsored them. While there is some synergy with up-market tourism, construction, and telecommunications, financial centre development has also increased island countries' contacts with criminals, increased their conflicts with metropolitan states and international organisations, and increased their dependence on unstable financial flows.

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The small size and isolation of Pacific island states—factors that usually limit their development options—can be advantages for an offshore financial centre (OFC). Their small size provides their promoters with influence over the local state for relatively modest contributions, and isolation furnishes a safe distance from inquisitive metropolitan tax and regulatory officials. Some Pacific island countries' OFCs play a significant role in the local economy and government revenues, but they are increasingly leading the countries into conflicts with international agencies, metropolitan governments, and

even some large international banks. Hosting an OFC increasingly leads to international criticism (from the OECD for abetting tax evasion, the Financial Action Task Force for facilitating money laundering, and the Financial Stability Forum for raising systemic risk in global banking) and this hurts the image of the Pacific island country. Local offshore institutions (small in number and largely run by expatriates) have been faced with a growing problem of image management and damage control in international relations and even in their personalised ties with island political leaders—who have so



far emphasised the OFC's importance to the local economy, but who may not be able to resist international moves toward harmonisation of taxation and financial practices over the longer term.

Norfolk Island

The first Pacific island offshore financial centre was created in 1966 on Norfolk Island, a unique external territory of Australia with a peculiar form of self-government. Promoters of Norfolk's tax haven have seen its potential to become a major global OFC blocked by the Australian Federal Government. There have been enormous opportunities for offshore centres around the world during this period—with bank deposits in offshore centres rising from US\$11 billion in 1968 to US\$2,000 billion in 1996 (Diamond et al. 1997; *Financial Times*, 24 November 1995, 7 June 1996; *Offshore Investment*, October 1999). Advocates of OFC development contrast Norfolk's frustrations with the success of the British-affiliated territories and dependencies such as Jersey, Guernsey, the Isle of Man, Bermuda, the Cayman Islands, and the

British Virgin Islands. The OFCs of these UK-affiliated make major contributions to their islands' local economic development.

While the British state and the City of London have encouraged the expansion of tax havens in present and past UK colonies, the Australian government has usually been antagonistic toward this sort of offshore development in its own external territories and within its sphere of influence in the Pacific islands region more generally. This has meant that Norfolk's OFC has been repeatedly thwarted by the Australian state, although there is still no income tax on the island and it still provides some offshore possibilities. The historical trajectory of Norfolk's tax haven can be analysed in terms of its dialectical tensions with the Australian state—tensions between self-determination and subordination which emerge from Norfolk's anomalous status as a self-governing external territory of Australia.

The question of Norfolk Island's exact status (and the closely related issue of the future of its tax haven) has been at the centre of local political controversy since the mid 1960s. OFC development is hindered by the constant perception that Norfolk

Table 1 Companies registered on Norfolk Island, 1962–98

1962	7	1975	998	1988	350
1963	10	1976	1,025	1989	375
1964	26	1977	1,008	1990	..
1965	36	1978	1,056	1991	..
1966	106	1979	1,107	1992	..
1967	294	1980	954	1993	..
1968	774	1981	..	1994	..
1969	972	1982	638	1995	approximately 250
1970	1,354	1983	..	1996	approximately 250
1971	1,571	1984	..	1997	approximately 260
1972	1,452	1985	..	1998	approximately 260
1973	1,328	1986	..		
1974	1,294	1987	..		

Note: Between 1962 and 1975 the year ends on 31 December; after 1975, the year ends on 31 June.

Sources: *Norfolk Island Report*, 1968–98; Treadgold, M.L., 1988. *Bounteous Bestowal: the economic history of Norfolk Island*, The Australian National University, Canberra:219.



Island's political status may change in some unwelcome way at Australia's behest and without the islanders' consent.

Nowhere in the Pacific islands region has there been such consistent and generally successful opposition to OFC development as from the Australian Federal Government in relation to Norfolk Island. Its offshore centre was effectively attacked

from the 1970s and yet at major critical junctures the Australian federal campaigns that threatened Norfolk's residential tax haven simply disintegrated in the face of concerted and determined local opposition although the danger has never entirely disappeared.

In the mid 1970s, the hostility of the Australian state was directed primarily at

Table 2 Company fees on Norfolk Island, 1969–2000 (US\$, per cent)

Year	Company fees (US\$)	Company fees/total government revenue (per cent)
1969	25,150	3.9
1970	48,609	7.2
1971	57,571	7.7
1972	100,521	11.8
1973	233,107	18.7
1974	209,653	14.0
1975	259,329	14.1
1976	217,944	12.9
1977	230,164	12.4
1978	270,802	11.7
1979	208,643	8.2
1980	155,831	5.4
1981	138,775	3.7
1982	104,426	3.0
1983	100,823	4.2
1984	84,793	2.5
1985	66,043	2.1
1986	56,663	2.0
1987	64,854	2.0
1988	84,741	2.3
1989	63,304	1.5
1990	54,295	1.2
1991	59,708	1.1
1992	45,606	0.8
1993	47,380	1.0
1994	39,698	0.8
1995	37,751	0.6
1996	36,608	0.5
1997	28,273	0.4
1998	25,000	0.4
1999	24,198	0.4
2000	26,470	0.4

Note: Between 1969 and 1975 the year ends on 31 December; after 1975, the year ends on 31 June.

Sources: Royal Commission into matters relating to Norfolk Island, 1976. *Report*, AGPO, Canberra:127, Australian Commonwealth Grants Commission 1997:67; Butland, G.J., 1974. A Long Term Population Study of Norfolk Island (unpublished):19; *Norfolk Island Government Gazette*, 9 February 1967; *Norfolk Island Report 1968–2000*; *Norfolk Islander*, 2 September 1972, 2 August 1975.



offshore entities and at the island's fledgling OFC, particularly after the number of registered companies (mostly owned by Australians) rose from 7 in 1962 to 1571 in 1971. The number of companies was approximately equal to the total number of Norfolk residents, and the island had seven resident legal and accounting firms and bank deposits of A\$262.8 million (US\$294.4 million) in 1971 (Royal Commission into Matters Relating to Norfolk Island 1976).

New Australian amendments to counter tax avoidance were applied to Norfolk's OFC from 19 July 1972 (Royal Commission into Matters Relating to Norfolk Island 1976), causing company registrations to decline to 998 in 1975 and the volume of bank transactions to fall by over two-thirds in the three years from 1972. On 30 March 1976, the High Court of Australia unanimously ruled that Australia had full sovereign (including taxation) powers over Norfolk, although it added that the Federal Government might choose not to apply these powers (*Australasian Tax Reports*, 1975–76).

By 1979, the limitations on Norfolk's ability to innovate and promote itself in the face of Australian hostility and increasing competition from other offshore centres (which offered up-to-date laws and financial secrecy) led to the disintegration of its offshore business and a decrease in company fees received by the island's government. The decline of the OFC was of little concern to many (although not all) of the local millionaires, since it principally affected outsiders who were using artificial Norfolk arrangements and attracted unwelcome attention from the Australian government to the island's privileged tax status. Most of the local wealthy people were outsiders who had made substantial investments in time and money to become Norfolk residents, since even millionaires find it difficult to become permanent residents on Norfolk (which controls its own immigration). The local

plutocracy, however, remained concerned about their narrow victory over Australian attempts to destroy their residential tax haven in the mid 1970s.

Further challenges to Norfolk's self-government came in 1990 and 1991, when some Australian federal politicians again proposed placing Norfolk in the Canberra electorate, and in 1998 and 1999, when the Australian government challenged the island's immigration controls (Human Rights and Equal Opportunity Commission 1999) and proposed changes under which only Norfolk Islanders with Australian citizenship would be allowed to be elected to the island's Legislative Assembly or enrol to vote. Taxation and representation are closely related issues and most islanders oppose moving closer to Australia, fearing (among other things) that this will bring income taxation.

By the 1990s most of the companies registered on Norfolk were local (*Norfolk Island Report*, 1994–96), even though a few exotic offshore structures were still on the register and there were possibilities for more (*Offshore Centres Report*, April 1991). In 1997, however, there was an unprecedented recommendation from an Australian governmental organisation that an OFC might be a valuable vehicle for the island's economic diversification and growth—initially through offshore gambling or a flag of convenience and later through offshore banking (Australian Commonwealth Grants Commission 1997:31, 45–46).

In 1998, Norfolk implemented offshore gambling legislation as a substantial step to revive the island's OFC, which continued to be prominent in the minds of local political leaders. The online gambling issue led Norfolk Island to more intense conflicts with Canberra in 2000 and 2001—with the Howard Federal Government promising to thwart its internet gaming ambitions. Yet, even if Norfolk's OFC never fully develops, the island's political economy and external



relations are likely to remain inextricably bound to its tax haven into the foreseeable future.

The New Hebrides–Vanuatu

Vanuatu's OFC started in 1969. In 1970 and early 1971 a full offshore regime was legislated and a significant amount of early business came from clients who were abandoning Norfolk Island. The New Hebrides quickly attracted support from

major international banks. The early rapid growth in the New Hebrides offshore centre began to slow by mid 1975, somewhat ironically, as its telecommunications (which had often been regarded as substandard and hampering the development of its OFC in the early 1970s) were reaching a more acceptable standard (Cockett and Fox 1977:153, *Tax Haven Review*, January, May and June 1975). Over time, most of Vanuatu's offshore promoters have gone somewhat down-market, and over the past decade it has been competing primarily with mass-market

Table 3 Companies registered in the Vanuatu offshore financial centre

Year	Exempt companies	International companies	Offshore banks	OFC insurance companies	Flag of convenience registrations (including dual registrations)	Trust companies
1976	469	-	..	..	-	..
1977	480	-	..	..	-	..
1978	480	-	..	..	-	..
1979	473	-	35	34	-	12
1980	505	-	41	33	-	12
1981	555	-	56	34	1	12
1982	584	-	68	34	4	12
1983	516	-	72	36	25	16
1984	600	-	85	37	46	15
1985	644	-	93	40	65	15
1986	666	-	93	43	93	10
1987	711	-	93	42	150	12
1988	736	-	97	42	198	12
1989	834	-	103	43	310	12
1990	932	-	103	43	357	12
1991	890	-	105	32	401	12
1992	1,018	..	114	35	381	12
1993	905	100 ^E	120	35	386	12
1994	461	700 ^E	122	35	398	12
1995	430	1,800	64	34	412	12
1996	175	1,004	74	32	444	12
1997	232	1,597	77	35	438	12
1998	235	1,789	66	36	457	12
1999	195	2,695	65	37	500	12
2000	184	3,831	56	40	485	13

^E Estimate.

Sources: *Offshore Investment*, 1996–2001; Reserve Bank of Vanuatu, 1988–2000, *Quarterly Economic Review*, Port Vila; *Republic of Vanuatu Official Gazette*, 20 January 1997.



offshore centres such as the British Virgin Islands in the Caribbean (*Offshore Investment*, July 1995).

In contrast to Norfolk Island, Vanuatu has a broad international clientele. Vanuatu's traditional markets of Australia and New Zealand are relatively static and its promotional efforts have targeted growing markets in Hong Kong, China, Taipei, Singapore, Japan, Canada, the United States, South Africa, Russia, and other Eastern European countries (*PITCO Vanuatu Update*, January 1993–December 1999).

The Vanuatu haven often provides more personalised services to wealthy, but not mega-rich, clients who might be served in a less considerate manner in larger, older and more expensive OFCs. Vanuatu's potential has been blunted by considerably higher political instability and lower government commitment than exist in most of its Pacific island competitors. In 1993, the Vanuatu OFC began to register more companies after parliament enacted new legislation that created the international company—from which little is expected apart from solvency and the payment of creditors (Ogley 1993). The introduction of international companies was aimed at satisfying the stated needs of Asian, particularly ethnic Chinese, clients, who find that even the minimal reporting required for the older exempted company is too onerous. The international company offers them a corporate entity that may be something of a formality covering what is basically a family enterprise (although this business may, in some cases, be quite large). The growth in registrations of international companies has been uneven but it has exceeded the decline in the number of exempt companies.

Substantial growth has occurred during three principal periods: 1988–90, when Panama faced a crisis (culminating in the US invasion); in 1995, when the Cook Islands were under particular pressure from the 'wine box' inquiry in New Zealand; and in

1999–2000, when the country intensified promotional efforts and the pressure brought by international organisations (ironically) gave it greater public recognition. The Vanuatu Letters of Guarantee fiasco and widely reported political instability (for example, the strike of the Vanuatu Mobile Defence Force, the arrest of strike leaders, and false newspaper stories that they had attempted to take over the government; *Offshore Investment*, December 1996) appear to be reasons for the decline in 1996. The 1994 report of William Penman-Brown, former Financial Services Commissioner in Gibraltar's OFC, which recommended raising the quality of banks registered in Vanuatu through more supervision and higher reporting requirements, resulted in a decrease in the number of registered offshore banks (*PITCO Vanuatu Update*, July 1994).

The rate of internal development of Vanuatu's offshore centre is indicated by statistics concerning the gross income of professional services firms, the net earnings of commercial banks, the OFC's local expenditure, employment, total foreign exchange earnings, and value added. All statistics about the OFC should be treated with caution, as they have in many cases been substantially revised and some doubts have been expressed about their mode of collection. Nevertheless, while perhaps not being conclusive, the figures in the following tables are of value in providing a rare view of the continuous internal development of a Pacific islands OFC.

Particularly notable is the exceptional growth in the gross incomes of legal firms in comparison with the less impressive growth of accountancy firms and the erratic trajectories of trustee companies. The uneven earnings of commercial banks' offshore business are also significant, but some comments should be made in relation to these banking statistics. In 1995, the worst year reported for commercial banks from their OFC operations, the overall profits of most



Table 4 **Gross income of OFC trust company, accounting, and legal firms and net earnings of banks, 1984–99 (US\$ million)**

Year	Trust companies	Accounting firms	Legal firms	Total professional	Banks net
1984	3.34	1.93	0.68	5.95	..
1985	3.14	2.10	0.51	5.75	..
1986	2.55	2.47	0.63	5.65	..
1987	2.49	2.62	0.69	5.80	3.09
1988	2.57	2.66	0.66	5.89	3.50
1989	2.95	2.40	0.68	6.03	5.65
1990	2.78	2.83	1.17	6.78	3.43
1991	6.22	3.58	1.02	10.82	14.11
1992	3.59	3.48	1.23	8.30	6.06
1993	2.67	3.20	1.25	7.12	12.73
1994	3.46	3.20	1.37	7.93	6.43
1995	3.25	3.07	1.50	7.82	2.40
1996	3.70	4.01	2.20	9.91	7.26
1997	2.99	4.32	2.23	9.54	6.78
1998	3.20	3.93	1.98	9.11	8.22
1999	6.16	6.50*	n.a.	12.66	17.61
2000	6.43	7.04*	n.a.	13.47	..

Note: *Accounting and legal firms combined.

Source: Reserve Bank of Vanuatu, *Quarterly Economic Review*, 1988–2000.

(or perhaps all) of them were still very high. While Westpac does not reveal its income from its Vanuatu activities, two other full-service banks in Vanuatu (the Bank of Hawaii and ANZ) reported operating net profits of 48 per cent and 36 per cent on shareholders' equity. The overall reported profits of banks include onshore as well as offshore income and are therefore not directly comparable to the Reserve Bank's calculations of their OFC profits. Even if the profits of the offshore centre are lagging, extraordinarily high profits can be made by being in an OFC free of corporate income tax.

While the contribution of the OFC's local expenditure (Table 5) has been as high as 12.8 per cent of GDP, a fairly high proportion of local expenditures may leak out of Vanuatu to purchase imports such as computers, financial technology, or goods and services for expatriates. Expatriates, while decreasing in number, continue to have high and

presumably tax-free annual incomes of US\$59,900 per expatriate in 2000. Indigenous ni-Vanuatu employees' yearly incomes are US\$7,400 on average, which, while being high by national standards, is less than 15 per cent of the expatriate salaries (Table 6). Although the OFC employs only a very small proportion of the country's labour force, the tax haven provides a high percentage of jobs in the private sector that are locally considered to be well-paid.

The offshore centre has had a decisive effect on the history of the New Hebrides–Vanuatu. From 1970, it greatly boosted the revenues of the pro-independence British administration and reduced the relative importance of the French, with whom the British shared rule in a condominium arrangement. The OFC brought lawyers, trustees, and bankers, particularly from Australia and New Zealand, who were more favourably disposed toward independence



and Melanesian aspirations than the French settlers, who were predominantly planters on the large proportion of the country that had been alienated from the indigenous inhabitants. Thus, the offshore centre greatly increased the powers of the British administration. By 1976, British revenues had reached twice those of the French, who were in favour of maintaining the New Hebrides as a settler bailiwick. The OFC helped to transform Port Vila from a sleepy French colonial village into an active town with a few French people in it. More importantly, it contributed to the independence movement by providing resources for the British administration and anglophone indigenous politicians (Treadwell 1989, personal communication).

After the indigenous anglophone politicians—led by the country's first Prime

Minister Father Walter Lini—won the independence battles in 1979 and 1980, they jettisoned their 'socialist' reservations about the offshore centre. All prominent Vanuatu politicians express support for the OFC and even francophone politicians now seek to gain benefits for their constituents from offshore development. Independent Vanuatu's relatively high level of sovereignty and its policy of non-alignment during the Cold War contributed to the country's image of resisting pressures placed upon it by metropolitan governments and taxation officials.

Clearly, Vanuatu has come to depend on its offshore centre. This dependence can be seen very clearly when we consider the OFC's foreign exchange earnings, which actually exceeded the total value of all the country's merchandise exports in two years (1990 and 1991) and made substantial contributions to

Table 5 Vanuatu offshore financial centre local expenditure and GDP, 1981–99

Year	Total local expenditure (US\$ million)	Total expenditure (per cent of GDP)
1981	12.69	12.8
1982	..	..
1983	..	..
1984	10.45	8.7
1985	10.31	8.4
1986	10.59	8.8
1987	12.47	10.9
1988	15.27	10.9
1989	18.66	12.8
1990	17.56	10.7
1991	19.67	11.6
1992	27.38	16.0
1993	20.25	11.7
1994	20.36	10.8
1995	17.67	8.1
1996	18.82	8.2
1997	17.42	7.4
1998	16.60	7.8
1999	17.88	7.4
2000	20.96	8.7

Sources: Asian Development Bank, various issues. *Key Indicators of Developing Countries*, Asian Development Bank, Manila; Reserve Bank of Vanuatu, various issues, *Quarterly Economic Review*, Reserve Bank of Vanuatu, Port Vila; World Bank, various issues. *World Tables*, World Bank, Washington, DC.



reducing Vanuatu's balance of payments deficits in all the other years listed. While the use of vatu (rather than the more common US dollar) as the currency unit for many of Vanuatu's offshore activities may have put off some potential clients, it has assisted Vanuatu in solidifying its national currency and foreign reserves.

New offshore gambling operations promise even greater foreign exchange earnings as they are subject to a 2.5 per cent revenue tax and reportedly draw up to A\$600 million (US\$360 million) a year out of the Australian racing industry alone (*The Australian*, 21 February 2000), but questions have been raised about whether all key offshore promoters are making their contributions to foreign exchange and paying their

local taxes. One scheme to avoid the turnover tax (and to escape converting fees into vatu) led to a split among Vanuatu's tax haven promoters in 1998 and 1999—one accounting firm resigned from the Finance Centre Association over its claims that the Association had failed to act against a rival accounting firm for using a Vanuatu offshore company to avoid paying the 4 per cent tax on its fees. It is not known how commonly tax haven promoters in Port Vila use offshore structures to avoid paying revenue to the Vanuatu government. Likewise, considerable numbers of passports of convenience have been sold illegally to ethnic Chinese, but the proceeds do not appear in government accounts. Finally, Vanuatu is struggling to refute accusations that it is a centre for money

Table 6 Vanuatu: wages and employment, 1979–99

Year	Wages and salaries (US\$ million)	Vanuatu citizens' wages and salaries (US\$ million)	Total OFC employment	Expatriate employment	ni-Vanuatu employment
1979	..	..	311	249	62
1981	..	..	322	210	112
1984	3.97	1.45	380	123	257
1985	3.90	1.48	365	104	261
1986	3.92	1.65	370	98	272
1987	5.13	1.81	366	89	277
1988	5.83	2.36	389	82	307
1989	4.80	1.90	389	76	313
1990	5.00	1.86	393	80	313
1991	5.79	2.63	397	86	311
1992	7.98	2.73	432	70	362
1993	7.35	1.96	374	59	315
1994	7.15	2.10	386	62	324
1995	5.55	2.55	386	61	325
1996	6.04	2.79	424	64	360
1997	6.66	2.99	409	61	348
1998	6.13	2.78	393	56	337
1999	6.66	2.61	409	61	348
2000	6.79	3.26	506	68	438

Sources: Asian Development Bank, *Key Indicators of Developing Countries*, Asian Development Bank, Manila, various issues; Reserve Bank of Vanuatu, various issues, *Quarterly Economic Review*, Reserve Bank of Vanuatu, Port Vila; World Bank, *World Tables*, World Bank, Washington, DC, various issues.



Table 7 Vanuatu OFC foreign exchange earnings, 1982–99

Year	OFC/foreign exchange earnings (US\$ million)	Per cent of total merchandise exports
1982	9.002	39.3
1983	9.924	33.5
1984	12.698	28.7
1985	15.109	49.3
1986	16.131	92.9
1987	13.028	73.6
1988	16.242	83.4
1989	22.182	99.8
1990	25.901	137.6
1991	20.999	114.8
1992	17.039	72.2
1993	14.106	62.2
1994	11.168	44.7
1995	13.148	46.5
1996	14.511	48.1
1997	13.524	38.3
1998	12.995	38.7
1999	12.085	48.7
2000	11.247	44.0

Sources: Asian Development Bank, *Key Indicators of Developing Countries*, Asian Development Bank, Manila, various issues; Reserve Bank of Vanuatu, *Quarterly Economic Review*, Reserve Bank of Vanuatu, Port Vila, various issues; World Bank, *World Tables*, World Bank, Washington, DC, various issues.

laundering and tax evasion and to ward off possible sanctions from the OECD and other organisations (including four large international banks that suspended US dollar transactions with Vanuatu, Nauru, and Palau in November 1999—contending that the three countries were not vigilant against money laundering). However, the Financial Action Task Force regarded Vanuatu as making substantial progress against money laundering and removed it from its blacklist in November 2000.

Nauru

Nauru began to provide offshore services in 1972. Like Vanuatu, Nauru promotes itself as one of the world's few 'pure' tax havens, with no internal or external personal or corporate income taxation. Nauru's policy

toward offshore development has been paradoxical. On one hand, the OFC was initiated to provide an industry that would compensate somewhat for the ultimate disappearance of the phosphate that had made the country one of the richest in the world on a per capita basis. On the other hand, Nauru has been extremely reluctant to issue work permits to foreigners who could promote the industry. The government has often been suspicious of attempts to open the island to tourism, which usually has synergies with the offshore sector. The airport is small, the hotel facilities are mediocre, and business travellers require a visa to visit the country. The Nauru Agency Corporation has a monopoly on all offshore trustee business but has only six employees. Furthermore, almost no legal, accounting, or banking services are available on Nauru for offshore business, which means that clients must



organise all of these by themselves. This produces very weak regulation of Nauru's offshore entities. Fraudsters have used so many Nauru offshore banks that the country's OFC has a credibility problem in many quarters. Its reputation has not been enhanced by the country's government-owned phosphate trust (a capital exporter on its own account) having been defrauded of millions of dollars in a prime bank instrument scheme oriented around Vanuatu and other OFCs.

As a result, Nauru's OFC has sometimes formed alliances with questionable operators. For many years in the 1980s and 1990s its OFC strongly resisted pressures from US and other investigators and it justified this refusal to cooperate in terms of its sovereign independence (Shockey 1992, personal communication). In 1999, according to the US Treasury, Nauru had registered at least 400 offshore banks (about half of them owned by Russians) and the Russian Central Bank contended that US\$70 billion had been transferred from Russia to Nauru's OFC as of 1998. The association of Nauru's offshore banks with crime is so strong that the OECD threatened to terminate Nauru's links with the international financial system in 1999 and further pressure came from the G-7, the US government and some international banks. The image of the country was not improved when President Bernard Dowiyogo reportedly wrote to the US Treasury Department (in what one official described as an attempt at extortion) demanding a minimum of US\$10 million from the United States before Nauru could begin reforming its OFC. Nauru has come to be regarded as a prime target for global financial regulators. The OFC contributed approximately US\$500,000 (or 2 per cent) of government revenues in 1999 (Diamond and Diamond 1997; Diamond, Diamond and Kaplan 1997; Global Information Network, IFS Newsfeed, 25 May 1999; *New York Times Magazine*, 10 December 2000; *Pacific Islands Monthly*, April 1999).

Tonga

Tonga's ventures in offshore banking and passports of convenience have a chequered history. In 1978–79, the Bank of the South Pacific, which was given a monopoly over OFC activities, rose and fell amidst allegations that its principal, John Meier, a former executive in the Howard Hughes organisation, had been involved in an assortment of felonies. New offshore banking legislation introduced in 1984 led to the licensing of a number of banks that defrauded depositors. Almost all were deregistered, but in 1999 three new offshore banks were incorporated in Tonga.

Passports of convenience have been sold to wealthy foreigners seeking freedom of movement and tax minimisation. Despite legal challenges from some commoner members of Tonga's parliament, all Tongan offshore projects have been initiated by the King, who is a nearly absolute monarch. The highly secretive registration of offshore banks and the surreptitious issuance of passports by Tonga delayed the construction of a more comprehensive and transparent OFC that could offer a broader, less lopsided range of offshore entities and better prospects for durable and continuous future development. Despite Tonga's problems, its experiment in offshore banking has apparently produced revenue of at least US\$100,000 in 1986, judging by the vague replies of the Minister of Finance to parliamentary questioning. Tens of millions of US dollars of profit have been derived from passport sales and deposited in the Tonga Trust Fund. Only small proportions of these large amounts (most of which are held in San Francisco bank accounts) have gone to the kingdom's internal development, and most of the funds that have been forthcoming are in the form of loans, not grants—so that in 1999 US\$10.7 million of advances to the Tongan government were held as assets of the Tonga Trust Fund (*Tonga Government Gazette*, 29 September 2000). There has been little

Table 8 **Tonga trust fund: assets and contributions, 1988–99** (US\$ million)

Year (as of 31 March unless otherwise noted)	Tonga trust fund's reported assets	TTF's budgeted contributions to development budget	TTF's actual contributions to development budget	Total actual development budget	Total recurrent revenue
1988–99	8.1*	-	-	8.4	29.0
1989–90	19.4	1.6	1.7	8.0	32.3
1990–91	24.7	6.2	1.6	9.6	36.6
1991–92	27.6	5.6	0.2	5.6	34.8
1992–93	26.5	10.8	1.8	7.2	37.6
1993–94	27.8	8.4	0.0	8.5	40.2
1994–95	28.1	2.5	1.6	16.2	45.6
1995–96	30.1	6.4	1.1	13.8	50.9
1996–97	32.3	6.5	0.9	12.8	49.2
1997–98	32.3	4.0	3.6	12.6	41.7
1998–99	42.0	2.3	1.1	..	..
1999–2000	43.1	..	..	..	..

Note: * 1 July 1989

Sources: Kingdom of Tonga, *Budget Statement for the Year by the Minister of Finance*, Kingdom of Tonga, Nuku'alofa, various issues (1989–96); National Reserve Bank of Tonga, *Quarterly Bulletin*, National Reserve Bank of Tonga, Nuku'alofa, various issues (1993–98); Kingdom of Tonga, 1997. *Report of the Minister of Finance 1997*, Kingdom of Tonga, Nuku'alofa; Kingdom of Tonga, 1998. *Report of the Minister of Finance 1998*, Kingdom of Tonga, Nuku'alofa; *Tonga Chronicle*, 3 June 1999; *Tonga Government Gazette*, 28 October 1992, 26 May 1993, 31 January 1996, 29 February 1996, 30 June 1997, 26 February 1998, 31 July 1998, 10 August 1999, 29 September 2000, 18 September 2001, 21 September 2001.

domestic legislative control over these ventures.

The assets and contributions to government revenue of the Tonga Trust Fund are detailed in Table 8.

Most people in Nuku'alofa political circles believe that the Tonga Trust Fund is ultimately controlled by and for the benefit of the royal family. A scandal emerged in 2001 when more than US\$20 million of the Trust's funds were alleged to have been lost in the purchase of life insurance policies that gambled on the early deaths of prominent Americans.

Guam

The US territory of Guam has remained dependent on the decisions or indecisions of Washington, DC, and the island has had

little ability to determine its own course for offshore development. Guam became an official offshore banking centre in 1979 under fairly strict US supervision, but it had been doing less formal offshore banking since about 1975. The approval of international banking facilities in the continental United States in the 1980s diminished Guam's relative attractiveness as an offshore banking site with a US connection. OFC promoters have been continually frustrated by what they felt to be lost opportunities, comparatively low returns from offshore operations for the local economy and the island's extreme dependency on the priorities and legislative predilections of the US Congress for whatever offshore development Guam might be permitted to enjoy. Its offshore deposit and lending facilities have risen and fallen and its ambitions to become a tax treaty shopping centre (Anonymous 1984) have been scuttled as a result of US legislative



changes. The uncertainty about Guam's exact relationship to the US tax system has stifled its captive insurance initiatives in the late 1990s. Guam's recent attempts to offer tax minimising offshore trusts were effectively thwarted by the US Treasury in November 2000.

Guam's most successful OFC operation—the licensing of foreign sales corporations (FSCs)—was completely dependent on the initiatives of the US Congress. The FSC regime was destroyed by the World Trade Organization, which ruled in 1999 that the FSC regime was an illegal export subsidy to US businesses and proclaimed that it would have to be eliminated by October 2000. In 1994, Guam derived only 0.2 per cent of government revenue (or approximately US\$150,000) from all offshore activities, the vast majority being from the registration of 215 active and 131 relatively inactive large and small FSCs (Government of Guam 1997). These revenues were minuscule compared to the advantages that Guam's FSCs conferred on their owners. In 1992, the most recent year for which figures are available, 7 per cent of all FSCs were in Guam, and all FSCs were providing additional net profits to US businesses of between US\$1.4–2.5 billion a year (Quest Economics Database, 21 October 1999).

The general situation has produced frustration and a sense of futility among local offshore promoters. Many indigenous Chamorro politicians see a considerably higher level of sovereignty as being necessary for the creation of a larger and more successful offshore centre, a goal that is often mentioned by indigenous nationalists, even to casual visitors (see also Malcomson 1990:57). Many local offshore promoters acknowledge that proper OFC development cannot come without Guam moving from its current status as an unincorporated territory. Becoming a commonwealth similar to the Northern Marianas or Puerto Rico might be enough to propel some offshore development, but even this would give Washington

considerable power to over-rule tax haven initiatives. Many local offshore supporters have long doubted that the US will ever permit the creation of a proper OFC in Guam (*South Sea Digest*, 8 May 1992) and it seems likely that their desire to create an offshore centre along the lines of Bermuda (*Guam Business*, September 1997) will not succeed within the foreseeable future.

Cook Islands

Cook Islands emerged as an OFC in 1981 and 1982. The advent of a modern satellite link in 1980 increased the feasibility of a project that had first been proposed some time earlier. Cook Islands (like Niue more recently) emphasised that it combined the sovereignty to write its own laws (without any higher authority needed to ratify them) and the stability provided by its relationship of free association with New Zealand.

The Cook Islands offshore centre was seen as taking advantage of the political instability in Vanuatu after it became politically independent in 1980. Vanuatu's rhetoric of 'Melanesian Socialism', its Libyan connections, and its volatile coalition governments contrasted with the conservatism and continuity of the Cook Islands polity. Vanuatu's principal rival as a Pacific islands tax haven has been the Cook Islands. The Cook Islands OFC has developed in a steadier manner. A rough idea of the comparative positions of the OFCs is provided by the ratio of their contributions to their respective governments' receipts (Table 9).

The Cook Islands' figures do not include the secret proceeds to government revenue from artificial withholding tax schemes (such as that outlined in Parliament of New Zealand 1994), that alone may have produced more revenue than is indicated here for each of the years in the late 1980s. This means that the actual government revenues may be significantly more than the reported



amounts for these years. The former Cook Islands Finance Minister Michael Fleming (who left the position in the middle of 1988), claimed that OFC deals were generating millions of dollars of secret revenues for the Cook Islands government—as much as NZ\$900,000 (US\$530,000) a month in 1987 that were not reported in public accounts (*Cook Islands Press*, 6 August 1995). The Cook Islands Trustee Companies Association estimates that these indirect benefits exceed direct payments, so that in 1995 the OFC contributed (directly and indirectly) a total of NZ\$4.5 million (US\$3 million) to the

government or well over 6 per cent of its receipts (*Cook Islands News*, 5 July 1996).

The Registrar of International and Foreign Companies of the Cook Islands is secretive (refusing to give figures even to *Offshore Investment*, a periodical oriented toward OFC promoters and clients), but a fragmentary understanding of the history of offshore registrations is available from other sources (Table 10). The early years were quite slow for the Cook Islands OFC. In early 1986, only 176 offshore companies were registered and most of them were from the United States. In New Zealand, however, a new élite of

Table 9 Vanuatu/Cook Islands offshore financial centre government receipts

Year	Vanuatu OFC taxes, levies, fees (US\$ million)	Per cent of government receipts	Cook Islands OFC taxes, levies, fees (US\$ million)	Per cent of Cook Island government receipts	Cook Islands/Vanuatu receipts (per cent)
1984	1.068	4.2	0.011	0.1	1.0
1985	1.122	4.0	0.055	0.4	4.9
1986	1.480	5.3	0.367	2.0	24.8
1987	1.508	4.6	0.671	2.6	44.5
1988	1.705	4.6	0.749	3.5	43.9
1989	2.628	7.3	0.752	2.7	28.6
1990	3.443	8.2	1.003	2.6	29.1
1991	5.758	13.7	1.067	3.1	18.5
1992	5.971	13.4	..	..	..
1993	4.688	11.3	..	..	..
1994	1.967	3.9	..	..	..
1995	2.908	5.5	..	..	..
1996	2.569	4.5	..	..	..
1997	1.942	3.5	1.256	4.5	64.7
1998	2.227	4.1	..	..	..
1999	1.666	..	..	..	..
2000	3.239	6.4	..	..	..

Source: Asian Development Bank, 1990. *National Accounts of the Cook Islands: technical assistance report*, Asian Development Bank, Manila; Asian Development Bank, 1995. *Cook Islands: economic performance, issues and strategies*, Asian Development Bank, Manila:18; Parliament of Cook Islands, *Cook Islands Parliamentary Debates*, Parliament of Cook Islands, Avarua, various years (1982–97); Asian Development Bank, *Key Indicators of Developing Countries*, Asian Development Bank, Manila, various issues; *National Business Review*, 18 March 1994; New Zealand Audit Office, 1991. *Report of the Audit Office and Financial Statements of the Government of Cook Islands*, New Zealand Audit Office, Wellington; New Zealand Audit Office, 1992. *Report of the Audit Office on the Accounts and Transactions of the Government of Niue*, New Zealand Audit Office, Wellington; Parliament of the Cook Islands, *Papers and Order Papers Presented*, Government of the Cook Islands, Avarua, various issues (1986–94); Reserve Bank of Vanuatu, *Quarterly Economic Review*, Reserve Bank of Vanuatu, Port Vila, various issues (1988–2000); World Bank, *World Tables*, World Bank, Washington, DC, various issues (1993–98).



Table 10 Registrations in the Cook Islands offshore financial centre

	Companies	Trusts	Banks	Partnerships	Total
Early 1986	176	..	..	..	..
October 1986	325	..	33	..	..
July 1987	1,600	..	..	..	..
1988	..	..	..	..	1,500
Late 1980s	855	266	24	5	..
1995	..	..	12	..	3,065
1997	..	500	..	..	..
2000	1,200	..	..	..	..

Sources: Asian Development Bank, 1995. *Cook Islands: economic performance, issues and strategies*, Asian Development Bank, Manila; *Cook Islands Government Gazette*, 8 September 1997; *Cook Islands Parliamentary Debates*, 23 July 1987; Davison, R.K., 1997. *Report of the Wine Box Inquiry: Commission of Inquiry Into Certain Matters Relating to Taxation*, vol. 1, Department of Internal Affairs, Wellington; *Los Angeles Times*, 23 June 2000.

financiers (who would become prominent clients or promoters of the Cook Islands tax haven) was at this time rising to prominence and influence in New Zealand power circles, and this group acted to encourage offshore development in the Cook Islands.

Spectacular growth occurred in 1986 and 1987 and by the end of July 1987 about 1,600 offshore companies had been registered—most of them with connections to New Zealand, Australia, Singapore, Hong Kong, the United States, and Europe. The Cook Islands became an important centre for the business of large corporations and this encouraged the creation of branches by ANZ and Westpac banks in 1988 and the purchase of its largest trust company by Standard Chartered Bank (in 1991) and then by the Bank of Bermuda (in 1994). The OFC directly accounted for about 6.4 per cent of the Cook Islands' total GDP in 1994, compared to less than 1 per cent ten years before (Asian Development Bank 1995, *Cook Islands Press*, 23 July 1995).

Despite these successes, a serious image problem arose in the 1990s. Documents from the largest trust company in the Cook Islands (outlining tax schemes for leading companies in New Zealand, Australia, and Japan) found their way (in a wine box) to Brian Henry, a

lawyer for Winston Peters, a maverick member of the New Zealand parliament. Peters attempted to table them in the parliament on 23 September 1992 and subsequently summarised their contents (not always very successfully) under the protection of parliamentary privilege. This set off the 'Wine Box Affair' that dominated headlines in New Zealand and stigmatised the Cook Islands for years (Davison 1997; Parliament of New Zealand 1994; Wishart 1995, 1999).

Yet the Cook Islands OFC still demonstrated long-term growth. In contrast to Vanuatu's legislature, the Cook Islands parliament has constantly and speedily introduced, passed and amended legislation to attract new offshore business. This is connected to the fact that some parliamentarians in Rarotonga have close connections with offshore promoters. Local indigenous Cook Islands Maoris (particularly those who have earned law degrees) are prominent in the OFC. In March 1999 the offshore centre employed about seventy people, including eighteen expatriates and over fifty Cook Islanders. Cook Islanders constituted almost half of the twenty-four professionals, with four of the qualified accountants and seven of the lawyers being indigenous. The Cook Islands OFC tends to be lawyer-driven. This



contrasts with Vanuatu and most other OFCs in the world, where accountants are more significant, and makes the Cook Islands a legal laboratory (with important and innovative offshore vehicles such as the asset protection trust having been pioneered in Rarotonga). Although the Cook Islands have been placed on international organisations' blacklists for not taking sufficient action against tax evasion and money laundering, asset protection trusts (which are not primarily oriented toward tax minimisation or money laundering) have accounted for a substantial and growing proportion of the business of Rarotonga's OFC since the early 1990s. The great importance of asset protection trusts may make the Cook Islands less vulnerable to possible sanctions by the OECD and the Financial Action Task Force compared with offshore centres that rely more on tax minimisation structures and financial secrecy. The ultimate threat to the Cook Islands OFC may come from US courts that seek to overturn the asset protection trusts, which were primarily designed for US clients seeking to escape the so-called 'litigation explosion'.

Thwarted offshore centres in 'American Micronesia'

The OFCs of the Northern Marianas, Palau, and Marshall Islands rose but then fell quickly between 1982 and 1986. This erratic trajectory was the result of concerted pressure from the US government to halt the unregulated registration of offshore banks within its sphere of influence in the US dollar zone of Micronesia. A small number of offshore banks survived and a few new ones were even registered after the campaign, but the original offshore plans of all three states were effectively thwarted until Palau became independent in 1994 and the Marshall Islands OFC reinvented itself (primarily as a flag of convenience registry) in 1990. We shall consider the reinvented Marshall Islands offshore centre later.

Even after the virtual demise of the Northern Marianas' offshore banking operations in 1982–83, the Commonwealth continued to assert some sovereignty by maintaining a registrar for a few offshore banks, conflicting with the US Federal Government over its tax regime, and serving as a place of tax exile for rich US citizens. Planners in the Northern Marianas continue to give high priority to the development of offshore financial services (Northern Marianas College 1999), despite the fact that only two offshore banks were registered there in 1998 (*Annual Report of the Director of Banking* 1998).

Palau defiantly reinstated its 1982 offshore banking laws (which had been emasculated by US *diktat*) soon after its independence in 1994, although doubts were expressed about whether Palau could develop a full OFC if it remained part of the US monetary system (Government of Palau 1994). In late 1999, four large international banks suspended US dollar transactions with Palau, contending that the country had not taken adequate precautions against money laundering. The Palau government initially protested with vehemence, and sued the Bank of New York, which was itself embroiled in a major Russian money-laundering scandal. The Bank of New York replied that there were a number of questionable banks registered in Palau and that one of them had handled over US\$1.7 billion in transactions over an eighteen month period (*Palau Horizon*, 9 June 2000). Despite the controversy and the fact that Palau registered four new banks during 2000 (*Guam Business*, April 2001), including one particularly dubious institution that was developing strong ties to local politicians, Palau was not on the money laundering blacklists of the Financial Action Task Force. The contribution of the international banking sector to the local economy is not clear in official statistics and (as in Tonga) many offshore activities seem to take place on a rather secretive and



Table 11 Registrations in Samoa's offshore financial centre

Year	International companies	Long-term companies	International trusts	Offshore banks	OFC insurance companies	Trustee companies
1989	126	-	5	4	1	3
1990	232	-	22	4	3	3
1991	404	-	65	7	4	3
1992	622	-	67	10	6	3
1993	877	14	73	13	7	4
1994	1,487	34	204	17	8	4
1995	2,127	69	215	20	12	5
1996	2,930	91	235	23	14	5
1997	3,878	113	262	25	14	5
1998	4,736	124	275	25	16	6
1999	5,876	147	303	25	16	6
2000	7,300	..	..	..	..	..

Source: *Asiamoney*, September 1995; Central Bank of Samoa, various years (1989–99). *Annual Report*, Central Bank of Samoa, Apia; *Offshore Investment*, March 2001.

informal basis. Since Palau has no corporate income taxation and weak banking regulation (with low capitalisation requirements), some de facto offshore operations have been organised according to its domestic laws.

Samoa

A very different process of OFC development continued in the New Zealand-oriented zones of Polynesia. In Samoa (formerly Western Samoa, the first independent country in the Pacific islands), there has been some growth in the number of registered entities since the offshore centre was founded in 1988. Samoa (unlike other Pacific island OFCs such as Vanuatu and the Cook Islands) lists cumulative, rather than current, registrations (Table 11).

At the end of 1999, Samoa's OFC register held 3,329 live international and long-term companies, 161 trusts, 11 offshore banks, and 6 insurance companies (Central Bank of Samoa 1999). These figures are comparable to those supplied by other Pacific island OFCs.

Table 12 presents the growth of governmental receipts from the Samoan OFC. Although the total direct and indirect contributions of the Samoan OFC to the country's economy from 1988 to 1998 were estimated to be US\$9.3 million and it employed 55 people in 1999 (*Pacific Islands Monthly*, April 1999), there is disappointment among many politicians that the economic benefits for the country have not been as great as promised or anticipated, especially as there was more state assistance for early offshore development in Samoa than in the Cook Islands.

This attitude has a history—government officials had been convinced as early as 1983 that enormous benefits would accrue if they performed one-off licensing of the International Pacific Bank, wholly owned by the Hong Kong-based Erylmore Co. Ltd. (*Islands Business*, March 1983). After great promises, it never really started operating—temporarily discouraging local officials who had previously contemplated creating an OFC in the early 1970s but had abandoned the idea because they felt the country's



Table 12 Governmental OFC receipts and total governmental receipts

Year (July–June)	Governmental OFC receipts (US\$)	OFC/total governmental current revenue (per cent)
1992	0.082 ^E	0.2
1993	0.096 ^E	0.2
1994	..	..
1995	..	..
1996	0.803	1.2
1997	0.925	1.5
1998	1.021	1.8
1999	1.297	2.1

^E Estimate

Source: Asian Development Bank, 2000. *Key Indicators of Developing Asian and Pacific Countries*, Asian Development Bank, Manila; Central Bank of Samoa, *Annual Report*, Central Bank of Samoa, Apia, various issues; Legislative Assembly of Western Samoa, 1992. *Approved Estimates of Receipts and Payments*, Legislative Assembly of Western Samoa 1992, 1997, Legislative Assembly of Western Samoa, 1997. *Approved Estimates of Receipts and Payments*, Legislative Assembly of Western Samoa, Apia.

infrastructure was not sufficiently sophisticated. Plans for the current offshore centre developed soon after the famous New Zealand ‘entrepreneur’ Ron Brierley (whose company, Brierley Investments, had a large stake in the largest trust company in the Cook Islands) joined the board of directors of the country’s largest bank, the Bank of Western Samoa, in 1987. The Western Samoan parliament passed the enabling legislation in January 1988, less than one year after Brierley’s appearance in local financial circles.

By world standards, the parliament is relatively responsive to the desires of offshore promoters, although they occasionally complain of delays in passing legislation (*Offshore Investment*, October 1999). The refusal of Malietoa Tanumafili II, the Head of State, to sign an offshore bill in 1993 (parts of which were to facilitate deals similar to those found in the ‘wine box’), after the New Zealand government put pressure on him, tends to consolidate the impression that OFC promoters have less influence than they would like to have.

Unlike the Cook Islands, which initially gained its stature as an important inter-

national OFC primarily through US, New Zealand and Australian clients, Samoa has from the start been oriented primarily toward Hong Kong, China (with which Samoa has long had strong diplomatic relations), Singapore, and (after the disintegration of the Soviet Empire) Eastern Europe (particularly Russia and the Ukraine). In some ways it is surprising that Samoa’s growth has not been greater, since much of the business of the British Virgin Islands comes from Chinese in Asia (particularly Hong Kong)—the single most important source of Samoa’s clients. However, the British Virgin Islands (like Bermuda, another Hong Kong favourite) have become institutionalised as a brand name for this clientele (which also appears to value their British colonial status). Samoa’s promotional strategy has emphasised the disadvantages of the colonial link and the weak sovereignty of the British Virgin Islands and Bermuda, as well as the uncertainties entailed by Britain’s taxation policies and its integration into the European Community (Powell 1997). Samoa proclaims its full sovereignty and sees this as the key to its offshore development, but recently it has been



under pressure from the OECD to 'harmonise' its system of taxation or risk possible sanctions if it remains on the OECD list of non-cooperative countries. Significantly, Samoa (like Vanuatu and Palau) was not on the money laundering blacklists of the Financial Action Task Force, giving it a better reputation than the Pacific islands competitors that remained on the list—Nauru, Niue, the Cook Islands, and the Marshall Islands.

The reinvented Marshall Islands

The reinvented Marshall Islands OFC was set in place in 1990 by International Registries Inc. (IRI) of Reston, Virginia. IRI was also the promoter and administrator of the Liberian offshore centre. It wanted a less politically turbulent jurisdiction in the Pacific, which would enact the innovations it had desired in offshore law in Liberia, where the legislature was immobilised by the civil war (Grundy 1993:63). It acquired the Marshall Islands flag of convenience registry that had been founded a short time before by Howard Zeder, the son of Fred Zeder, the chief confidant of former US President George Bush. The initial success of the reinvented Marshall Islands OFC was at the expense of Panama, which was beset by crisis around the time that Bush ordered the 1990 US invasion (van Fossen 1992).

The OFC has grown and quickly become the ninth largest shipping registry in the world. The Marshall Islands OFC generated US\$500,000 in annual revenues for the government there in 1996 (1.6 per cent of the Marshalls' total government revenue of US\$30.5 million for that year), but considerably less than the US\$9,977,255 (32.4 per cent of total revenue) that the government received in 1996 from offshore passport sales, which were unrelated to IRI (*Marshall Islands Journal*, 7 November 1997).

After IRI refused to accede to Liberia's demand that it end its relationship with the

Marshall Islands, IRI was stripped of its right to operate the African country's offshore register in 2000. This intensified its concentration on developing the Marshall Islands OFC—as foreshadowed in February 1999 with its completion of a new US\$1.3 million two-storey office building at Ajetak on Majuro atoll near the capital, although most of the Marshall's increasing offshore work is done in Reston, Virginia and IRI's numerous offices in other metropolitan countries.

Niue

Most impressive has been the growth of offshore company registrations in Niue, oriented particularly toward the growing Chinese markets (Table 13). In 1993, the government was cautious about creating an OFC on Niue in view of the gathering crusade that the New Zealand parliamentarian Winston Peters was leading against the Cook Islands OFC in relation to the 'wine box' documents. Niue has a very similar 'free association' relationship with New Zealand and Peters was calling for the termination of aid to the Cook Islands in retaliation against its offshore activities which, he said, deprived the New Zealand government of hundreds of millions of dollars of tax revenue.

However, Peter's threat to cut off aid to the Cook Islands seemed increasingly hollow. Raising the issue also highlighted the series of cuts in New Zealand aid that had already occurred in both the Cook Islands and Niue and the fact that Niue, one of the most aid-dependent countries in the world, needed new sources of revenue. The wealthy against whom Peters was fulminating had more influence over the New Zealand government than at any time in the previous one hundred years (Eldred-Grigg 1996) and the New Zealand state took no effective action against the creation of the OFC in Niue.



Table 13 Niue offshore company registrations

Registered Niue offshore companies	
1994	141
1995	556
1996 (30 November)	1,405
1997 (15 November)	2,396
1998	3,662
1999	5,550
2000	7,262

Source: *Offshore Investment*, 1995–2001.

Table 14 OFC contributions to government revenue in Niue

	OFC fees (US\$)	Per cent of total government revenues
1994-95	320,001	3.1
1995-96	142,155	1.6
1996-97	300,945	3.0
1997-98	381,970	4.2
1998-99	447,865	6.5

Sources: *Far Eastern Economic Review*, 4 July 2000, New Zealand Audit Office, *Report of the Audit Office on the Accounts and Transactions of the Government of Niue*, New Zealand Audit Office, Wellington, various years (1997–2001).

The success of Niue in such a short time seems to indicate the desirability of new Pacific islands offshore centres becoming a (highly promoted) part of a pre-existing global multi-OFC marketing strategy. Like the Marshall Islands, another jurisdiction without extensive local infrastructure, Niue has entered into a franchising agreement with a multinational offshore promoter headquartered in another country. The early exclusivity of the powerful Mossack Fonseca & Company's promotional contract with Niue is also connected to the great effort this legal firm spent in promoting Niue to its existing and prospective clients from its headquarters in Panama and its many offices in the OFCs and onshore financial centres around the

world. While Mossack Fonseca maintained its monopoly on Niue company registrations, some of the responsibilities for registering and administering Niue offshore banks were spun off to a complementary trustee company created in 1997 which began to promote Niue's offshore banks actively in 1999.

Despite the success of the Niue OFC, there is disappointment among legislators, who were apparently told at one point that it would be a panacea for the country's extreme dependency on foreign aid (particularly from New Zealand), which amounted to 171 per cent of GDP in 1993. Nevertheless, Niue's OFC started auspiciously (Table 14).

Niue's offshore promoters have also had some influence over the Niue government's



proposed policy of becoming a pure tax haven (like Vanuatu and Nauru) through a deliberate effort to eliminate all onshore and offshore corporate and personal income taxation (*Niue Star*, 26 June 1998). Since 1999, however, Niue, like many other Pacific Islands OFCs, has been threatened with sanctions by international organisations combating money laundering and tax evasion. In January 2001, the JP Morgan Chase Bank and the Bank of New York banned transactions with Niue, citing its vulnerability to money laundering.

A comparative view

OFCs tend to emerge in microstates, usually concentrated in the capital cities, and their actives have a tendency to dominate the host state's economic activity. Nevertheless, Pacific island OFCs' payments into government revenues are not particularly high when compared to some offshore centres in other parts of the world. For example, 60 per cent of Jersey's government revenue in 1998 was generated by its OFC (*Financial Times*, 22 February 2000). The

figures in Table 16 exclude the proceeds of episodic offshore passport sales.

While OFCs may supply a number of clerical jobs, most of the professionals working at the highest levels of Pacific Islands OFCs are expatriates (although there are significant numbers of indigenous offshore professionals in the Cook Islands and Samoa). In the Pacific islands this 'foreign domination' has not created the unrest which has characterised some other offshore centres, such as the anti-OFC protest movement on the Isle of Man, where activists fighting rent increases and evictions have gone as far as committing arson (*Offshore Adviser*, October 1989).

The strongest development links in the Pacific islands have been with up-market tourism, construction, and the channelling of local people into clerical, accounting, financial, and legal careers, as well as growth in telecommunications, air links and financial services. Up-market tourism is assisted by offshore development. Vanuatu has gone the furthest in the region in establishing this synergy—including a great deal of advertising for its OFC in local

Table 16 Contributions of major Pacific island offshore centres to government revenues

	Year	Government revenues from the OFC (US\$)	Per cent of total government revenues
Vanuatu	2000	3,239,000	6.4
Cook Islands	1997	1,256,000	4.5
Samoa	1999	1,297,000	2.1
Marshall Islands	1996	500,000	1.6
Nauru	1999	500,000	2.0
Niue	1999	447,865	6.5
Guam	1994	150,000	0.2

Source: Central Bank of Samoa, 1999. *Annual Report 1999*, Central Bank of Samoa, Apia; Government of Guam, 1997. *Guam Code Annotated*, Government of Guam, Agana; *Marshall Islands Journal*, 7 November 1997; *New York Times Magazine*, 10 December 2000; New Zealand Audit Office, 2001. *Report of the Audit Office on the Accounts and Transactions of the Government of Niue*, New Zealand Audit Office, Wellington; Parliament of the Cook Islands, 1997. *Cook Islands Parliamentary Debates*, Parliament of the Cook Islands, Avanaua; Reserve Bank of Vanuatu, 2000. *Quarterly Economic Review*, Reserve Bank of Vanuatu, Port Vila.



tourism promotional literature. The success of the Vanuatu and the Cook Islands; the current limitations of the Marshall Islands and Niue; the unattractiveness of Nauru; the unrealised potential of Samoa and Tonga; and the significant opportunities for offshore development on Guam, the Northern Marianas, and Palau are related to their appeal as destinations for the sorts of wealthy visitors who use offshore facilities.

Local élites often find the potential fees, commissions and benefits generated by OFCs an attractive prospect. Furthermore, offshore centres can be relatively cheap for a nation to create. There may also be relatively few ethical qualms about tax haven development, since some Pacific island states derive relatively little (or, in some cases, no) revenue from direct taxation. Nevertheless, offshore promoters generally 'oversell' the OFC to get it established by local politicians, who are then generally disappointed after few of the promised benefits materialise.

Only one Pacific island state, Tuvalu, has rejected concerted pressure by promoters to develop an OFC, and this rejection was based on particular factors rather than a general or abstract opposition to offshore development there. The defeat of the first Prime Minister, Toalipi Lauti, in 1981 was attributed to his investing most of the government's funds in a Californian business that was (among other things) promoting offshore development. Although this firm reportedly returned the money (with interest) in 1984, it remained highly unpopular within Tuvalu and its association with the idea of building an OFC there created substantial antagonism to the idea.

Offshore development may be seen in relation to a typology of its likely effects on the political economic development of its society. There is a continuum between the booking, paper, or brass-plate OFCs (that do little more than paperwork), on one hand, and functional offshore centres where banks, lawyers, accountants, and other financial

personnel have a physical presence and are likely to have a greater local impact on the other. On Norfolk Island, Guam, and the Northern Marianas, booking OFCs have been stifled by pressures from hostile metropolitan parent states, although the residential tax havens (and local tax exiles) on Norfolk and Saipan continue to have important influences on the political economy of these islands. The booking centres in Tonga and Palau display erratic patterns. In Nauru and the Marshall Islands, booking centres have emerged, but only the Marshall Islands show some initial signs of maturing into a more functional centre that might be able to make important contributions to shaping the local society. In Samoa and Niue, successful booking centres have developed rapidly (generating locally significant fees for the governments of these countries) along with the possibility (given these OFCs' high growth rates) of their becoming increasingly functional, although there may be some local limitations on this in Niue. The Cook Islands have successfully developed important functional aspects, which has had a considerable impact on the country's political economy. Vanuatu's functional operations are more mature and have for years exercised a significant influence on the archipelago's political economic structure (for example, in successfully lobbying against the introduction of income taxation on residents). Nevertheless, all Pacific Islands havens are primarily involved in booking regardless of how large their functional operations may have become (see also Hampton 1996).

In one of the few general considerations of the impact of offshore development on the economy of its host country, McCarthy (1979) finds that, while the benefits exceed the costs, the net benefits are not likely to be very great for new OFCs, particularly as they are entering a very crowded, competitive and perhaps stagnant global market for tax haven services. According to him, 'new paper centers are not likely to succeed [and]...even



existing centers might become less important and less profitable' (1979:48). In a similar spirit, Johnson (1976) is only slightly less pessimistic when he observes that any growth in Panama's offshore centre is unlikely to make a great contribution to the country's economy. Francis (1985) is considerably more optimistic about the possibilities for offshore development, both generally and in relation to the Bahamas. Her view is that the offshore market is continuing to grow and that there is a tendency for OFCs to move from booking to functional operations. Although Francis's work is more helpful in explaining how Pacific island offshore centres have emerged in the 1980s and 1990s, all three of these studies are narrow cost-benefit analyses.

Caulfield's (1978) interpretation of the Cayman Islands is unusual in showing how the centrality of the offshore centre in that small Caribbean country (and its synergies with up-market tourism) have led to a political, economic and social metamorphosis—the transformation from one type of life (more independent and subsistence-oriented) to another kind of life based on intense monetisation, commodification, and growing dependency on the vagaries of international financial markets and taxation regimes. Yet there are reasons to doubt that the OFC (rather than non-OFC-related tourism) has been as decisive in the Caymans as Caulfield suggests.

There are, however, some general conclusions that may be drawn from surveying Pacific islands tax haven development. The OFC may move the Pacific island host further toward a MIRAB-style rentier economy (Bertram 1999, Bertram and Watters 1985) dependent on volatile transnational financial flows and ever-changing metropolitan political-economic agendas. Offshore centres help to bring countries into the world's financial and banking systems, make them more recognisable to financiers, and make it easier for them to borrow money.

In addition to reputable banks, however, OFCs also attract criminals. The loans for the disastrous Cook Islands Sheraton hotel project (associated with Mafia interests) and the fraudulent letters of guarantee that threatened to bankrupt the Cook Islands and Vanuatu in 1996 were all deals negotiated with people attracted to or associated with these countries' offshore centres.

The creation of new offshore centres obviously increases competition. It does not necessarily follow that in the long term this diminishes the opportunities available to older OFCs. The proliferation of offshore centres creates many new opportunities for capital to escape taxation and regulation. Offshore development has dramatically increased the global pool of hot, stateless money (Wachtel 1990). Even the traditional havens are still growing, despite competition from new OFCs.

New offshore centres are not just competitors. Their entities and services are used by older havens to make their tax minimisation and other strategies more opaque and effective. The amount of money available to OFCs is not fixed. The more avenues that international finance capital is offered for exiting from costly responsibilities in metropolitan states, the more capital is likely to flow into a growing pool of offshore funds.

It is clear that the revenues to the OFCs' host countries are a small proportion of the revenues lost by the governments of metropolitan countries. It is also in the interest of metropolitan states and offshore governments to agree to trade the abolition of OFCs for higher levels of economic assistance. The proliferation of countries offering offshore centres and the intensified competition between them, however, make bilateral agreements difficult. Any OFC entering into such negotiations is extremely vulnerable (Irish 1982). The new multilateral strategies of international organisations (involving 'black lists' and threats against OFCs) may



be more effective than the older bilateral tactics and they may continue to pose a challenge to Pacific islands countries that hope to increase revenues through offshore development.

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